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Asian Development Bank

LIST OF ABBREVIATIONS

ACC	Anti-Corruption Council
ADB	Asian Development Bank
ADS	Armenia Development Strategy
ARF	Armenian Revolutionary Federation
ARMEPS	Armenian e-procurement system
ATDF	Armenian Territorial Development Fund
CoE	Council of Europe
CPI	Corruption Perceptions Index
CPS	Country Partnership Strategy
CSC	Civil Service Council
CSO	Civil Society Organization
DFID	Department of International Development
DLI	Disbursement-linked indicator
EA	Executing Agency
EBRD	European Bank for Reconstruction and Development
EDB	Eurasian Development Bank
EEU	Eurasian Economic Union
EIB	European Investment Bank
EITI	Extractive Industries Transparency Initiative
EU	European Union
FIDIC	Fédération Internationale Des Ingénieurs-Conseils [International Federation of Consulting Engineers]
GACAP II	Second Governance and Anticorruption Action Plan
GDP	Gross Domestic Product
GFMIS	Government financial management information system
GIZ	Gesellschaft für Internationale Zusammenarbeit
GoA	Government of Armenia
GRA	Governance risk assessment
GRECO	Group of States against Corruption
IA	Implementing Agency
ICB	International competitive bidding
IMF	International Monetary Fund
IT	Information Technology
LMIC	Lower middle income country
MFF	Multitranches financing facility
MoESCS	Ministry of Education, Science, Culture and Sport
MoF	Ministry of Finance
MoTAD	Ministry of Territorial Administration and Development

MoTCI	Ministry of Transport, Communication and Information Technologies
MTEF	Medium-term expenditure framework
NCB	National competitive bidding
NGO	Non-Governmental Organization
NSRC	North-South Road Corridor
OBS	Open Budget Survey
ODA	Official development assistance
OECD	Organisation for Economic Co-operation and Development
OGP	Open Government Partnership
OSCE	Organization for Security and Cooperation in Europe
PAR	Public administration reform
PEFA	Public Expenditure and Financial Accountability
PFM	Public Financial Management
PIM	Public investment management
PIU	Project Implementation Unit
PPL	Public Procurement Law
PRA	Procurement risk assessment
RBL	Results-based lending
RPA	Republican Party of Armenia
SAI	Supreme audit institution
SDG	Sustainable development goal
SNCO	State non-commercial organization
SSIP	Seismic Safety Improvement Program
SUDIP	Sustainable Urban Development Investment Program
TA	Technical Assistance
ToR	Terms of Reference
TPIO	Transport Project Implementation Organization
UNCAC	United Nations Convention Against Corruption
UNDP	United Nations Development Program
USAID	United States Agency for International Development

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I. EXECUTIVE SUMMARY

The Asian Development Bank (ADB) has prepared this Governance Risk Assessment (GRA) to establish the status of country systems and governance reforms in Armenia. It follows ADB's Second Governance and Anticorruption Plan (GACAP II) framework and informs ADB's 2019-2023 Country Partnership Strategy (CPS) for Armenia.

The report provides an overview of the historical and political context, economic context, governance and institutional arrangements, and the country development strategy (Chapter III), which is followed by an assessment of country systems for public financial management (PFM), procurement and anticorruption (Chapter IV). It outlines ADB's use of country systems (Chapter V), and provides an overview of governance risks (Chapter VI) and presents a risk management plan (Chapter VII). Four brief assessments of ADB's priority sectors for Armenia are also included (Chapter VIII).

Country Institutional Overview

Armenia is a unitary and multi-party nation-state with a history that dates back longer than most other countries. The modern Republic of Armenia became independent from the Soviet Union in September 1991 and, as a sovereign state, has since then experienced remarkable developments, but also faced some key challenges.

Armenia's government was from 1991 to 2017 based on a semi-presidential system. Elections in the 1990s were considered relatively fair and free, but later elections saw allegations of perceived widespread electoral fraud that several times led to large demonstrations, which in some cases were violently dispersed by security forces.

The presidential elections in 2008 and 2013 as well as the parliamentary elections in 2007, 2012 and 2017 were won by the Republican Party of Armenia (RPA), which was led by Serzh Sargsyan. The RPA in 2015 took the lead in a constitutional referendum that changed the government system to a parliamentary system which, opponents argued, was Sargsyan's intended way to stay in power after his second term as President would end in April 2018. Despite earlier declarations to the contrary, the RPA majority in the National Assembly on 17 April 2018 elected Sargsyan as Prime Minister. This resulted in huge protests, which were led by Nikol Pashinyan from the Way Out Alliance and whose criticism of the government resonated with many people. On 23 April 2018 Sargsyan announced his resignation. The 'Velvet Revolution' thus became the biggest political upheaval in Armenia in more than a decade.

Pashinyan was elected Prime Minister on 8 May 2018 following which a new Cabinet was formed and approved by the President. Snap parliamentary elections on 9 December 2018, that were deemed to respect fundamental freedoms and enjoyed broad public trust, resulted in a landslide victory for the new Pashinyan-led My Step Alliance, which received 70% of the vote and won 88 out of the 132 seats in the National Assembly. A new government was formed in January 2019.

The political changes since April 2018 has challenged the established pattern of governance, wherein decision-making bypassed state institutions and ensured 'favorable' election outcomes, and thus unchallenged power despite the public's demands for change. However, Armenia has for many years had an energetic and engaged civil society with relatively strong organizations, and the status of the press, while somewhat mixed, is relatively free, especially when compared to most other ex-Soviet Union countries.

In its foreign policy, the Armenian Government attempts to balance and reconcile different policy options, which are mainly between the European Union (EU) and the

Russian Federation. This was seen when, having since 2010 negotiated an Association Agreement with the EU, the Government in 2013 decided instead to join the Eurasian Economic Union (EEU). Apart from historical ties and Russia's dominant trade position, this may also have been as there are many Armenian migrant workers in Russia as well as Russia's strong security involvement in the region.

Economic context. From independence in 1991 until the global financial crisis in 2008, Armenia was considered a transition economy success story due to its sustained macro-economic achievements and socio-economic developments, which was supported by liberal economic reforms and a favorable external environment. In contrast to this, the decade after 2008 was less benign with the economy characterized by low growth, low investment and relatively high debt as well as socio-economic conditions that showed limited resilience to deteriorated external circumstances (e.g. poverty was almost 26% in 2017 and unemployment was 16% by end-2018).

However, the macro-economic situation improved during 2017-2018. Economic growth was 7.5% in 2017 and 5.2% in 2018, average annual inflation was 1.0% in 2017 and 2.5% in 2018 (in 2016 there was deflation), and remittances decreased only slightly from 2017 to 2018. The 2017 budget deficit of the Government of Armenia (GoA) was 4.8% of GDP and fell to 1.8% in 2018, which thus continued a fiscal consolidation that is needed to lower the government debt-to-GDP ratio (51.3% by end-2018). The Government aims to reduce the ratio to below 50% in the medium term based on a Public Debt Management Strategy was designed and approved as part of 2019-2021 medium-term expenditure framework (MTEF). The fiscal deficit is financed by official development assistance (ODA), which amounted to 9.8% of GoA spending in 2017.

The government has over the past decade implemented a number of reforms to facilitate private sector development. However, Armenia needs to further improve the conditions for economic growth, which will require additional business climate reforms to increase competition and deepen financial development, strengthening export performance as well as better trade and transport facilitation, and addressing labor market challenges (including in relation to the existing skills mismatch). Also, the GoA needs to increase public capital investment into productive infrastructure.

Country development strategy. The *Armenia Development Strategy (ADS) 2014-2025* was approved by the previous government, but it is understood to remain the strategic framework for development of state policies until a new country-level strategy has been prepared (expected to be ready by early 2020). The ADS sets out four main priorities: (i) employment growth; (ii) human capital development; (iii) improving the social protection system; and (iv) institutional modernization of the public administration and governance. For the latter, the ADS calls for strengthening PFM, reforming the state inspection system, enhancing local self-governance, developing e-government, improving the civil service and judicial systems, and reducing corruption. The government has in place strategies for civil service reform, e-governance and anticorruption, but there is no overall approach for public administration reform (PAR).

As the Constitution requires, the new Government in June 2018 prepared a policy program that was approved by the National Assembly. The program focused on preparing for early elections, ensuring external and internal security, and fighting corruption. The Cabinet in February 2019 presented a five-year plan focusing on economic reform, which was adopted by the National Assembly. The plan includes a number of ambitious macro-economic and social development goals, but is somewhat less specific about how these goals would be achieved. It would thus seem that a more concrete action plan will need to be developed to guide the necessary reforms.

The change in government in April/May 2018 is generally acknowledged to having brought about a more transparent and “cleaner” administration, but also slower decision-making processes due to reduced capacity at senior management levels. The GoA’s strategic planning is complicated by a lack of a hierarchy of national and sectoral strategic plans and a synchronization of planning horizons, which results in a lack of consistency across planning documents.

Armenia has no formal forum for government-development partner coordination, which instead takes place on an ad-hoc and bilateral basis. Development partners exchange information through thematic groups, e.g. the PFM Donor Coordination Group, which meets bi-annually, sometimes with Government representation.

Assessment of Country Systems

Public financial management. The PFM system has undergone a number of positive developments in recent few years, including legislative and regulatory initiatives (strategic planning, budgeting, accounting, taxation, treasury system, and external audit), institutional changes (establishing a Budget Office as secretariat for the National Assembly’s Standing Committee on Financial-Credit and Budgetary Affairs), and improvements in methodologies and guidelines (economic analysis, program-based budgeting, internal control, internal audit, and fiscal risk management).

However, a number of PFM challenges remain, which relate to sector strategies (not fully costed and recurrent cost implications of investments not estimated), annual and medium-term budgeting (implementing new procedures), budgetary resources for development partner-financed projects (prioritizing allocations in the context of fiscal consolidation), fiscal risk management (no summary reporting, limited quantification, and mitigation measures not formulated), public investment management (clear rules for selection and prioritization of investment projects yet to be established), payroll controls (weaknesses in reconciliation of payroll and personnel records), internal audit (capacity to be developed), annual financial statement (not auditable due to quality and consolidation issues), and the external audit function (the Audit Chamber is not fully independent (finances and staffing), and the audit capacity needs to be improved).

Public-private partnerships (PPPs) could be of particular importance for infrastructure investments in Armenia, but strengthened processes and capacity for identifying, developing and managing PPP transactions are needed to ensure they are effective and do not lead to unsustainable fiscal obligations. The new PPP Law, approved by the National Assembly in June 2019 and coming into force in January 2020, will codify the PPP policy framework as well as facilitate the establishment of proper appraisal methodologies, fiscal risk management and reporting related to PPPs. Currently, secondary legislation is being developed. It will also be important that the PPP pipeline is sourced from line agencies’ own medium-term infrastructure development plans, which will require reform of the GoA’s public investment management (PIM).

Recent financial management assessments undertaken by ADB for new investments have found PFM weaknesses as regards program-based budgeting (weak capacity and poor information flows) as well as budget execution reporting and external audit (not consistent with international standards). As a fiduciary safeguard, the implementation of ADB-financed projects is managed by project implementation units (PIUs), and applying international accounting, reporting and auditing standards.

It is understood that the Government intends to ‘mainstream’ PIUs into ministries, although the exact approach remains to be formulated. Considering the existing technical and human resources capacities of ministries, including their limited experience with development partner requirements and procedures, it would seem that

such reorganization will require the continued use of dedicated units for managing implementation of external-funded projects.

The Ministry of Finance (MoF) has since 2011 implemented a PFM Reform Strategy accompanied by a detailed action plan. The MoF undertakes quarterly follow-up on implementation progress and prepares an annual report. The reports are not published, but the MoF does periodically provide information on reform implementation to development partners and other stakeholders. The MoF aims to prepare a new/updated PFM reform strategy and action plan in the near future.

A number of development partners provide support to the MoF for PFM reform, but institutional coordination on PFM reform is somewhat limited as there is no formal forum to coordinate activities with the GoA. This has led to some level of fragmentation as well as overlap of efforts and resources as well as contrasting policy advice. Development partners exchange information in the PFM Donor Coordination Group.

ADB's support for PFM reform has previously included a policy-based loan (PBL) with actions on recurrent cost financing strategies and internal audit capacity development in the roads, energy and water sectors. More recent PBLs have aimed at promoting policy actions to strengthen public debt and fiscal risk management policies (including related to PPPs), improve cash/treasury management, and further develop the financial market infrastructure and related legislation.

Procurement. Armenia's public procurement system is overall fairly well-functioning. The legislative framework was significantly improved with the new Public Procurement Law (PPL), which is based on international best practices and was prepared with development partner support. The PPL, which came into effect in April 2017, has narrowed the scope for exemptions from the default method (open tender), although the extent of 'urgent' (single source) procurement has already decreased since 2015.

Some challenges remain as regards to the institutional framework and management capacity of procuring entities as well as procurement operations and market practices. This is, among other reasons, because procurement is fully decentralized, i.e. there is no centralized procurement agency and all 1,000 procuring entities (ministries and agencies as well as municipalities and state non-commercial organizations (SNCOs)) undertake their own procurement. The MoF continues to focus on further developing and improving the Armenian e-procurement system (ARMEPS).

The integrity and transparency of the procurement system has been improved following the establishment of the Complaint Review Board as an independent administrative procurement complaints system. The number of complaints grew from 46 in 2014 to 170 in 2017. According to current regulations, it is mandatory for bidders to provide a 'statement on beneficial ownership' and a 'statement on absence of conflict of interests', both of which are publicly available, although it is not clear that the information provided in the statements is being verified by the procuring entities.

ADB has during program/project implementation in recent years, mainly in the road transport sector, noted some delays in procurement processes as well as examples of poor contractor performance and payment issues.

The World Bank in 2014 reviewed the ARMEPS vis-à-vis requirements for electronic tendering of multilateral development banks. It concluded that most requirements were fulfilled for shopping and simple goods/works/non-consulting national competitive bidding (NCB) procedures. Following the development of new procurement modules for

the ARMEPS and training of PIU staff, the World Bank in 2017 started using ARMEPS for project-related shopping and NCB. ADB should consider the same.

The GoA does not have a separate procurement reform strategy, which is instead part of the PFM Reform Strategy, but this has not adversely affected procurement reform.

Vulnerability to corruption. Corruption in Armenia is deemed to affect some sectors of the economy as well as government. Important parts of the economy are controlled by well-connected businesspeople who, until the political changes in May 2018, had government-protected market dominance, which led to concerns about the relationships between businesses, politicians and bureaucrats. However, this nexus appears to be changing under the new Government.

Policy documents prepared under previous governments outlined various planned anticorruption activities, which resulted mainly in changes to the legal framework to enable a more effective fight against corruption, but this did not affect the level of perceived corruption in Armenia. However, while corruption earlier topped the list of problematic factors for doing business, this has in recent years been overtaken by other concerns (e.g. access to financing, inefficient bureaucracy and tax administration). Also, international organizations have found that since 2017 there has been progress in implementing preventive measures to fight corruption (including related to ethics, conflict of interests, whistle-blowing and procurement). Furthermore, information from the Prosecutor General's Office (PGO) indicate that the number of persons prosecuted in corruption-related criminal cases has increased significantly during 2018 and include a large number of public officials.

The institutional framework for fighting corruption is somewhat fragmented and involves several different entities with overlapping jurisdiction, which weakens accountability. The high-level Anti-Corruption Council (ACC) was established in 2015 and has met frequently, including with participation of NGOs and development partners, but it was mainly a discussion forum rather than for decisive reform actions. A new Commission for Prevention of Corruption is presently being established as an independent collegial body with broad preventive powers, but it remains to be seen how it will function.

The Government in December 2018 presented a draft 'Anti-Corruption Strategy and Action Plan 2019-2022' for commenting to civil society organizations (CSO) and non-governmental organizations (NGOs). It focuses on corruption prevention, identification, and education. A second draft that takes into account many of the comments from CSOs/NGOs was published in June 2019. It is expected that the Anti-Corruption Strategy and Action Plan will be finalized and published during 2019.

Many governance activities supported by development partners include anticorruption aspects, but a few initiatives also focus specifically at anticorruption initiatives. As there is no formal forum for development partners and the GoA to discuss anticorruption issues, these aspects are covered bilaterally and through other thematic groups.

Use of Country Systems

ADB's 2019 assistance program for Armenia consists of 21 separate operations – with road transport, energy and urban transport being the main sectors – and with a total of 15 loans (99.4% of financing), some of which are equity investments, and 14 technical assistance projects (0.6%).¹ ADB's use of country systems for loans is 'partial' as it is used for budgeting and partly for treasury functions, but not for accounting and

¹ Hence a total of 29 activities as some operations include both loan and TA.

reporting, procurement and external audit. ADB could, given recent improvements in PFM and procurement systems, consider expanding the use of country systems.

Summary of Governance Risks and Risk Management Plan

Based on the assessments of PFM, procurement and vulnerabilities to corruption, an overview of the main governance risks in these three areas is presented in Chapter VI. A total of 25 risks were identified of which 11 are considered 'high risk'. Mitigation actions and related indicators for the high risks are proposed in Chapter VII. ADB will consider these risks when developing the CPS 2019–2023 and during dialogue with the GoA about future program and reform priorities as well as the related ADB support.

The following could be considered as ADB focus areas for operational assistance going forward:

- **PFM** – Ensuring that GoA funding is being provided for loan operations in line with agreements, encouraging operational counterparts to strengthen their internal audit functions and payroll controls, and developing the external audit methodology and staff capacity to be included in an updated PFM reform plan. On-going activities related to PPP development, as supported by a new PBL, are also highly relevant, and aim to ensure an improved decision-making framework and process.
- **Procurement** – Supplementing the e-procurement system with a new 'unit price data base' module to help procuring entities prepare more accurate cost estimates, strengthening procurement training for GoA entities and stakeholders, and encouraging the GoA to establish an independent review mechanism.
- **Anticorruption** – Supporting the GoA in preparing a diagnostic to assess the activities and capacities of relevant entities as well as making recommendations for a proactive anticorruption approach.

ADB should continue supporting policy reforms and institutional strengthening in the areas of PFM, public procurement and anticorruption. Particular attention may be directed at supporting the GoA's efforts in carrying out programs to promote supporting private sector growth. To raise accountability, ADB should together with other development partners also hold policy dialogues with the GoA to identify possibilities for de-monopolizing the economy and enabling separation of business and politics.

Brief Sector Assessments

Assessments have been prepared for ADB's four priority sectors – road transport, urban transport, urban infrastructure, and education – so as to provide preliminary overviews of governance issues in these sectors. The assessments describe the main challenges in the sectors, relevant GoA's strategies, external assistance provided by ADB and other development partners, and selected results from ADB's CPS 2014–2018 final review. Sector-specific PFM, procurement and corruption risks are also presented and discussed where such information has been available.

II. INTRODUCTION

1. This GRA report has been prepared to examine the status of governance in Armenia as of 2018 and informs the preparation of ADB's CPS for 2019–2023.
2. The assessment is based on ADB's GACAP II framework and follows ADB's guidelines for preparing country-level GRAs.² ADB's guidance on political economy analysis was also applied.³ The assignment was carried out intermittently during May 2018 and March 2019, including with two in-country consultation missions.
3. In accordance with the terms of reference (ToR) for the assignment, the GRA focuses on the national government level, including the institutional set-up and governance arrangements that shape and constrain the functioning and performance of systems in the areas of PFM, procurement, and anticorruption. The GRA includes two brief sector assessments, focusing on road transport and urban transport, which have been prepared using the value-chain methodology.⁴
4. The assessment draws on a desk review of available reports and diagnostic studies for governance, PFM, procurement⁵ and corruption in Armenia as well as consultations with Government of Armenia (GoA) officials, non-governmental organization (NGO) representatives, development partners, and ADB staff members.
5. The GRA report provides a country overview of the historical and political context, economic context, governance and institutional arrangements, and the country development strategy (Chapter III). An assessment of the performance of country systems covering PFM, procurement and vulnerability to corruption is made (Chapter IV) and a description of ADB's use of country systems is provided (Chapter V). The governance risk matrix is included (Chapter VI) together with a risk management plan (Chapter VII). Four brief sector descriptions are also provided (Chapter VIII).
6. The annexes include the bibliography (Annex A), persons consulted (Annex B), ADB's 2019 assistance program (Annex C), a summary of international governance surveys for Armenia (Annex D), and the road transport and urban transport sector assessments based on the value-chain approach (Annex E and Annex F, respectively).
7. A draft of the GRA report was shared with ADB, and the feedback received taken into account in preparing the final version of the report. The draft GRA report was likewise shared with the Government in May 2019 and September 2019, and the feedback received taken into account in preparing the final version of the report.
8. Logistical support provided by ADB's Armenia Resident Mission (ARRM) during the in-country consultation missions is gratefully acknowledged as is the technical guidance extended by ADB's Climate Change and Sustainable Development Department. The valuable inputs provided by representatives of the GoA, NGOs, development partners and ADB staff members are greatly appreciated.

² ADB. 2014. *Staff Guidance for Implementing the Second Governance and Anticorruption Action Plan (GACAP II)*.

³ ADB. 2013a. *Guidance Note – Use of Political Economy Analysis for ADB Operations*.

⁴ The value chain concept was developed in the 1980s for business management and focused on activities that firms undertake in order to deliver products or services for a market in order to identify inefficiencies in supply chains. Development organizations in the 2000s adapted the value chain concept to analyze process flows in projects in order to explain how resources are transformed into development outcomes. This in particular focused on mapping where critical decisions are made that affect the delivery of services in sectors, which would help to identify the political and economic factors that influence projects and, thereby, locate key vulnerabilities and risks so as to develop strategies for improving governance and fighting corruption.

⁵ Including ADB's 2018 Procurement Risk Assessment report, which was prepared in parallel with the GRA.

III. COUNTRY INSTITUTIONAL OVERVIEW

9. This chapter describes Armenia's historical and political context (Section A), economic context (Section B), governance and institutional arrangements (Section C), and country development strategy (Section D).

A. Historical and Political Context

10. Armenia declared independence from the Soviet Union on 21 September 1991. The presidential election in October 1991 was won with significant popular support by Levon Ter-Petrosyan who had led the Karabakh Committee since May 1988 and, following arrest from December 1988 to May 1989, had been elected as deputy of the Supreme Soviet of the Armenian Soviet Socialist Republic (SSR).

11. Levon Ter-Petrosyan was re-elected in 1996, but stepped down in early 1998. This was due to allegations of electoral fraud, Armenia's economic challenges in the post-Soviet period, but mainly after having advocated for a settlement of the Nagorno-Karabakh conflict, which many Armenians viewed as undermining their security.⁶

12. In 1998, Robert Kocharyan, previously President of Nagorno-Karabakh and Prime Minister of Armenia, became President after an election marred by irregularities. During his presidency, the Prime Minister and several members of the National Assembly were killed in 1999 by gunmen claiming to be carrying out a *coup d'état*. Kocharyan was re-elected in 2003, but alleged electoral fraud resulted in large protests. During 2004-2006 talks were held between Armenia and Azerbaijan to resolve the status of Nagorno-Karabakh, but no agreement was reached.

13. Presidential elections in 2008 saw Serzh Sargsyan, then Prime Minister and chairman of the Republican Party of Armenia (RPA), winning against Ter-Petrosyan. The latter accused the government of rigging the election and large protests ensued, which were violently dispersed. Sargsyan was re-elected President in 2013.

14. In December 2015, a constitutional referendum which aimed at changing the government system from a semi-presidential to a parliamentary system was held. Opponents argued that it was President Sargsyan's intended way to stay in power after his second and last term in office would end in April 2018. The referendum passed with 66% voting in favor, although with a low voter turnout (51%) and following allegations of irregularities, interference and intimidation in the voting and counting processes.⁷

15. Parliamentary elections in April 2017 resulted in the RPA winning 58 out of 105 seats in the National Assembly. President Sargsyan's term ended in April 2018 and, despite having earlier declared that he would not seek to become Prime Minister, the RPA on 14 April nominated Sargsyan as their candidate following which he was elected Prime Minister by the National Assembly on 17 April. This resulted in huge protests, first in Yerevan and later across the country, led by Nikol Pashinyan, a parliamentarian from the Way Out Alliance. Pashinyan's criticism resonated with many parts of society,⁸ including members of the armed forces who joined the protests, and on 23 April Sargsyan resigned. By 28 April all opposition parties had announced their support for Pashinyan's candidacy as Prime Minister. On 1 May, the National Assembly held elections with Pashinyan as the only nominee, but the RPA blocked his nomination. However, a renewed vote on 8 May, following country-wide protests, saw

⁷ OSCE. 2016. *Republic of Armenia – Constitutional Referendum 6 December 2015*. Final Report, 5 February, p. 3.

⁸ Olesya Vartanyan. 2018. "Velvet Revolution" Takes Armenia into the Unknown. International Crisis Group (ICG) Commentary, 26 April 2018.

Pashinyan elected Prime Minister and a new Cabinet approved by the President. The new government's program was approved by the National Assembly on 6 June 2018.

16. The government was initially a three-party coalition, but became a minority government of the My Step Alliance⁹ on 3 October 2018 when ministers from the two other coalition parties left the government following their support for a bill that made it harder for the Prime Minister to call snap elections. To trigger the snap parliamentary elections,¹⁰ Pashinyan subsequently resigned as Prime Minister on 16 October 2018 and parliamentary elections were held on 9 December 2018.¹¹ The election result was a landslide victory for the Pashinyan-led My Step Alliance which received 70% of the vote and won 88 out of the 132 seats in the National Assembly. The elections were held with 'respect for fundamental freedoms and enjoyed broad public trust' and were well-administered despite a short timeframe.¹² However, voter turnout (49%) was notably lower than during the previous elections.

17. A new government was formed in January 2019 with a Cabinet consisting of the Prime Minister, two Deputy Prime Ministers and 12 Ministers (down from previously 17 Ministers).¹³ Six Cabinet members are from the Civil Contract party and nine are independent.¹⁴

18. The governance process in Armenia has, for most of the time since independence, been based on consensus among elite groups which, during a decade from 2008 to 2018, centered on the RPA and a patronage network that included business people and senior bureaucrats.¹⁵ This bypassed state institutions, thereby making them ineffective, and explains the absence of free and fair elections as well as why previous administrations held more or less unchallenged power despite the general public's demands for change. However, at the same time the overall governance situation during the RPA period was also characterized by relative stability. The change in government in April/May 2018 is generally acknowledged to have brought about a more transparent and "cleaner" administration, but also slower decision-making processes due to challenges associated with the transition.

19. Armenia is noted for an energetic civil society with relatively strong organizations.¹⁶ The status of the press is somewhat mixed with investigative journalism flourishing online, a diverse but polarized print media, and a broadcast media that lags pluralism.¹⁷ Attacks on journalists covering elections and local developments by security forces have occurred in earlier years.¹⁸ However, compared to most other ex-Soviet Union countries, the Armenian press is relatively free.

⁹ The 'Way Out Alliance' was dissolved in September 2018 when its constituent parties – Hanrapetutyun Party, Bright Armenia and Civil Contract – agreed to participate in the 2018 parliamentary elections separately. The 'Civil Contract party (led by Nikol Pashinyan) together with the Mission Party formed the 'My Step Alliance'.

¹⁰ Under Armenia's Constitution, the Prime Minister would have to step down and the National Assembly then fail to elect a new Prime Minister after two votes in two consecutive sessions during two weeks.

¹¹ The elections took place based on the existing Election Code since the National Assembly twice in October rejected changes to the Code proposed by the Government. The proposed changes would have revised the mechanism for distributing seats in the National Assembly.

¹² OSCE. 2018. *Republic of Armenia – Early Parliamentary Elections, 9 December 2018 – Statement of Preliminary Findings and Conclusions*. International Election Observation Mission.

¹³ The necessary changes to the relevant law were approved by the National Assembly and the new structure became effective on 1 June 2019.

¹⁴ Previously one Cabinet member was from a party outside Parliament (Hanrapetutyun Party).

¹⁵ Bertelsmann Stiftung. 2018. *BTI 2018 Country Report Armenia*, p. 9.

¹⁶ *Ibid.*, p. 10 and p. 29.

¹⁷ <https://rsf.org/en/armenia>.

¹⁸ United States Department of State. 2018. *Armenia, Country Report on Human Rights Practices for 2017*, Bureau of Democracy, Human Rights and Labor, pp. 16-18.

20. In its foreign policy, the Armenian Government attempts to balance and reconcile different policy options, which – given its geopolitical position – are mainly between the European Union (EU) and the Russian Federation. This was seen when, having since 2010 negotiated an Association Agreement with the EU to replace an earlier agreement, the Government in 2013 instead decided to join the Eurasian Economic Union (EEU).¹⁹

21. However, in November 2017, Armenia and the EU signed the Comprehensive and Enhanced Partnership Agreement (CEPA), which provided for close cooperation in a number of areas, including energy, transport, environmental protection, trade and investment. Also, the agreement seeks to strengthen comprehensive political and economic cooperation and partnership, and stipulates the level of Armenia's involvement in the policies, programs and activity of the EU.²⁰ An Interagency Commission was established by the Government in 2017 and a Roadmap developed to ensure the implementation of the CEPA.

22. The Armenian Apostolic Church, as the national church and one of the most ancient Christian communities, has played an important role in the historical and cultural orientation of the Armenian people and impacted the country's cultural and political conduct.²¹ Although Armenia is a secular state and has freedom of religion, the Constitution clearly reflects the importance of the church.²² The church today holds a strong position within society as about 95% of the population are members as well as based on an informal but influential relationship with the state. The church has not traditionally been involved in politics, but has in recent years started engaging in public debates, e.g. on family issues and urban development.²³

B. Economic Context

23. Armenia was from independence in 1991 until the global financial crisis in 2008 considered a transition economy success story due to its sustained macro-economic achievements (high growth, economic stability, low inflation, low deficits and modest debt level) as well as improved socio-economic developments.²⁴ This was supported by first-generation reforms that liberalized the economy and a favorable external environment. However, the decade after 2008 was much less benign for the economy which until 2016/2017 struggled with low growth and investment, rising debt, and socio-economic conditions that showed limited resilience to deteriorated external circumstances. From 2008 to 2018, the population in Armenia shrank by 266,000, or 8.2%.²⁵

24. Macro-economic fundamentals: Armenia's macro-economic situation in 2016 was challenging, but has improved since then. *Economic growth* increased from 0.2% in 2016 to 7.5% in 2017, and moderated to 5.2% in 2018 mainly driven by services and industry.²⁶ Average annual *inflation* was negative in 2016, but 1.0% in 2017 and 2.5%

¹⁹ The decision to join the EEU was announced in September 2013 and the accession agreement signed in October 2014 and came into effect in January 2015.

²⁰ https://eeas.europa.eu/delegations/armenia/896/armenia-and-eu_en.

²¹ Hranush Kharatyan. 2011. *Religion and the Secular State in Armenia*. International Center for Law and Religion Studies, Brigham Young University, p. 1.

²² The Constitution's Article 18 states: "1) The Republic of Armenia shall recognize the exclusive mission of the Armenian Apostolic Holy Church, as a national church, in the spiritual life of the Armenian people, in the development of their national culture and preservation of their national identity; 2) The relations between the Republic of Armenia and the Armenian Apostolic Holy Church may be regulated by law."

²³ Bertelsmann Stiftung. 2018. op.cit., p. 7.

²⁴ World Bank. 2017. *Future Armenia: Connect, Compete, Prosper – A Systematic Country Diagnostic*, Report No. 124816-AM, November, p. ix.

²⁵ Statistical Committee of the Republic of Armenia – 'Number of De Jure Population of the Republic of Armenia' as of 1 October 2008 and 1 October 2018.

²⁶ ADB. 2019b. *Asian Development Outlook – Strengthening Disaster Resilience*. April, p. 143.

in 2018 due to higher excise taxes on fuel, liquefied gas, beverages, and cigarettes as well as increased customs duties. *Government debt*,²⁷ which had reached 53.7% of GDP by end-2017, declined in 2018 (to 51.3% of GDP) due to a strong tax administration effort and under-execution of planned expenditures. About 4/5 is external debt and 1/5 domestic debt.²⁸ The *current account* deficit widened from 2.4% of GDP in 2017 to 9.1% of GDP in 2018 as the balance of goods and services worsened and investment income and employee earnings from abroad declined. Exports and imports of goods grew at 9.3% and 16.3%, respectively, widening the trade deficit to 14.2% of GDP in 2018 from 11.9% a year earlier. The services account, virtually balanced at end-2017, recorded a negative balance of 1.2% at end-2018. *Remittances* fell by 2.8% to \$1.45 billion in 2018.²⁹

25. The government's *fiscal policy* in 2017 resulted in a budget deficit of 4.8% of GDP (compared with 5.5% in 2016) and thus the beginning of a fiscal consolidation process that is necessary to lower the public debt-to-GDP ratio. The 2018 budget envisaged a fiscal deficit of 2.7% of GDP, based on modest rises in revenues and expenditures as well as constraints on wage and pension outlays, but it in fact reached just 1.8%.³⁰ The projection for 2019 is 2.2%. The GoA's fiscal deficit is financed by official development assistance (ODA), which accounted for 9.8% of GoA spending in 2017,³¹ and public borrowing from external and domestic sources.³²

26. Poverty and employment: Poverty in Armenia declined significantly between 2004 (53.5%) and 2008 (27.6%) supported by high growth, but then increased somewhat following the global economic crisis (25.7% in 2017).³³ Unemployment reached 18% by end-2016 due to sluggish economic growth and structural weaknesses in the labor market (this despite the labor force shrinking due to substantial emigration),³⁴ but unemployment declined slightly to about 16% in 2018. There are significant regional disparities in poverty, while unemployment is mainly concentrated in urban areas, and among youth and women.

27. Armenia has a high level of short-term labor migration, especially to the Russian Federation,³⁵ with migration coming mainly from households outside Yerevan. Remittances in 2018 amounted to about 11.7% of GDP which as such is high, but well below 2013 when it made up 19.4% of GDP.³⁶ Remittances have fueled domestic consumption and construction, and thereby been a driver of poverty reduction, especially for rural households. The concentration of economic ties with the Russian Federation in terms of remittances as well as trade³⁷ and investment is a further characteristic of Armenia's economy.

28. Socio-economic development: The human development index (HDI) for Armenia in 2018 was 0.755 (83rd out of 189 countries), which makes it a "high" human

²⁷ Government debt differs from public debt which, as a share of GDP, was 58.9% in 2017 and 55.8% in 2018.

²⁸ The share of foreign currency debt in Armenia is high (about 85%) and a source of vulnerability.

²⁹ <https://www.cba.am/en/sitepages/statexternalsector.aspx>.

³⁰ ADB. 2019b. op.cit., p. 127.

³¹ <http://databank.worldbank.org/data/reports.aspx?source=world-development-indicators>.

³² The significance of borrowing is particularly clear when considering that public debt in 2008 amounted to just 16.4% of GDP, but increased to 40.6% of GDP in 2009 and reached 58.8% in 2017 of GDP.

³³ <https://www.armstat.am/en/?nid=82&id=2095>.

³⁴ IMF. 2017. *Republic of Armenia, 2017 Article IV Consultation and Fifth and Final Review Under the Extended Arrangement* ... Country Report No. 12/111, 30 April, p. 20.

³⁵ Exact figures on the number of migrants are not available and estimates vary from 191,000 (World Bank's 'World Development Indicators' databank [<http://databank.worldbank.org/data/reports.aspx?source=world-development-indicators>]) to 937,000 (2017 OECD/CRRC study quoted in World Bank. 2017. op.cit.) in 2015, i.e. migration would affect between 6.3% and 31% of the total population.

³⁶ <http://www.worldbank.org/en/topic/migrationremittancesdiasporaissues/brief/migration-remittances-data>.

³⁷ While the EU is Armenia's largest export market (accounting for 28.4% in 2018, which compares to Russia's 27.6%), Russia accounts for the largest share of Armenia's imports (28.1% compared with the EU's 24.8%).

development country.³⁸ This is an improvement in absolute terms compared to 2010 (when the HDI score was 0.695) and also in relative terms (in 2010 Armenia was 76th out of 169 countries), i.e. the socio-economic development in Armenia has been positive during 2010-2018. Income inequality in Armenia, as measured with the Gini index,³⁹ is comparatively low but increasing: it was 30.0 in 2010 and 32.5 in 2016.⁴⁰ Progress in meeting the Millennium Development Goals (MDGs) was poor: only 34% of the indicators were met and 15% were “well-advanced”, while 46% were not achieved and for 5% progress was not clear.⁴¹

29. GoA revenue performance and expenditure management: As noted above, Armenia has run significant budget deficits in recent years but, even so, the International Monetary Fund (IMF) in 2017 deemed the fiscal situation to be “broadly well managed”.⁴² The GoA’s *revenue performance* is good: tax revenue mobilization, measured as tax-to-GDP, was 17.1% in 2010 and increased to 20.8% in 2017 (which is well above the average of upper-middle income countries (UMICs)⁴³ and compares positively with most countries in the region).⁴⁴ However, taking into account expenditure levels, revenue mobilization is inadequate as the gap has been financed by increasing public debt. The GoA works to improve tax administration and strengthen revenue mobilization based on the 2016 tax code, which entered into force from January 2018. Further amendments, approved in June 2019, will come into force in January 2020. The limited ability to raise public revenues results in *public expenditures* that are relatively low compared to the size of the economy (general government spending was 29.3% of GDP in 2016). The share of public investment in total investment declined from 22% in 2009 (7% of GDP) to 12% in 2016 (3% of GDP) due to limited resources and prioritization of current over capital spending (due to social spending obligations).⁴⁵ In order to improve public expenditure management for capital spending, the GoA in 2016 developed a mechanism for monitoring and prioritizing projects, set up a new project database, and extended the strict controls over domestically-financed expenditure to future externally-financed capital projects.⁴⁶ The latter implies that future commitments are subject to registration to ensure consistency with the medium-term expenditure framework (MTEF) and the annual budget. Also, upgraded fiscal rules were operationalized in 2018.⁴⁷

30. Business environment: The government has over the past decade implemented a number of reforms to facilitate private sector development. However, in terms of

³⁸ UNDP. 2018. *Human Development Indices and Indicators – 2018 Statistical Update*, Table 1.

³⁹ The Gini coefficient measures inequality among values of a frequency distribution. “0” represents perfect equality (everyone has the same income) and “100” perfect inequality (only one person has all the income).

⁴⁰ To compare, the 2015 Gini index for Georgia was 35.4, Kazakhstan 26.9, and the Russian Federation 37.3.

⁴¹ The percentage achieved and “well-advanced” was as follows: Goal 1 (eradicate extreme poverty and hunger) 43%, Goal 2 (achieve universal primary education) 20%, Goal 3 (promote gender equality and empower women) 33%, Goal 4 (reduce child mortality) 33%, Goal 5 (improve maternal health) 67%, Goal 6 (combat HIV/AIDS, malaria, and other diseases) 67%, Goal 7 (ensure environmental sustainability) 56%, and Goal 8 (develop a global partnership for development) 33% [United Nations (UN). 2015. *Millennium Development Goals: National Progress Report Armenia 2015*. October, Chapter 1].

⁴² IMF. 2017. op.cit., p. 1.

⁴³ Armenia has been an upper-middle income country (LMIC) since 2017.

⁴⁴ <http://databank.worldbank.org/data/reports.aspx?source=world-development-indicators>.

⁴⁵ World Bank. 2017. op.cit., p. 6.

⁴⁶ The actions were structural benchmarks under the 2014-2017 IMF supported program with Armenia.

⁴⁷ The amended framework has three thresholds: If debt exceeds 40% of GDP, capital spending should not be below the level of the state budget deficit. If debt exceeds 50%, the previous rule continues to apply and restrictions are imposed on current spending (excluding debt service costs). If debt exceeds 60%, the previous rules continue to apply and current spending (including debt service costs) cannot exceed the total amount of tax revenue and stamp duties specified in the draft state budget for the upcoming year. Within the range of 50-60%, the Government must design a program of measures in the MTEF to gradually reduce debt to below 50% within a five-year period. Also, if the debt exceeds 60%, the Government must submit a program of measures to the National Assembly to gradually reduce debt to below 60% within a five-year period. Furthermore, the framework includes escape clauses related to natural disasters, war and economic shocks.

international survey rankings – such as by the World Bank’s Ease of Doing Business⁴⁸ and in the World Economic Forum’s Global Competitiveness Report⁴⁹ – Armenia’s relatively position has remained fairly constant from 2011 till 2018. The credit ratings for Armenia, as undertaken by two major credit rating agencies, were downgraded in 2015 (Fitch) and 2016 (Moody’s) from non-investment grade ‘speculative’ to ‘highly speculative’, but the ratings have since then been stable (June 2018, Fitch)⁵⁰ and upgraded to “positive” (August 2019, Moody’s).⁵¹

31. Economic reform challenges: Armenia’s pre-global financial crisis economic growth was largely driven by external financial flows and the domestic construction sector, but it appears that these have become less effective. Hence the country will need to improve the conditions for economic growth, which will require strengthening export performance as well as better trade and transport facilitation, undertaking further investment climate reforms to increase competition and deepening financial development, and addressing labor market challenges (including the mismatch between learning outcomes and the demand for skills sought by the market).⁵²

C. Governance and Institutional Arrangements

32. The Constitution of Armenia outlines the role and responsibilities of the National Assembly, Government (including the Prime Minister) and the President. It also provides for the state administration system, which consists of ministries and other bodies subordinate to the Government, and states that the administrative-territorial units shall be regions (marzes) and municipalities (communities). There are currently 10 regions and 503 municipalities (46 urban and 457 rural), including Yerevan which is a separate municipality. Regions are led by a governor appointed by the Government, while municipalities are led by elected councils and the mayor.

33. The National Assembly is a unicameral parliament with currently 132 members⁵³ elected for a five-year term based on a two-tier party list proportional representation method (50% of votes distributed via party lists and 50% among territorial lists submitted in electoral districts). There is a 5% threshold for parties and 7% for blocs to be included in mandate distribution. The parliamentary elections in December 2018 saw just three parties elected.⁵⁴ There are 11 standing committees,⁵⁵ which discuss draft laws and other issues as well as exercise parliamentary supervision. Seats within standing committees are allocated in proportion to the number of parliamentarians in each faction. It is only the National Assembly which, with a vote of no confidence, can remove the Prime Minister and Cabinet from office.

⁴⁸ <http://www.doingbusiness.org/data/exploreeconomies/armenia>.

⁴⁹ <https://www.weforum.org/reports/the-global-competitiveness-report-2018>.

⁵⁰ <https://banks.am/en/news/newsfeed/15678>; <https://tradingeconomics.com/armenia/rating>.

⁵¹ https://www.moody.com/research/Moodys-upgrades-Armenias-rating-to-Ba3-changes-outlook-to-stable--PR_404870.

⁵² World Bank. 2017. op.cit., pp. x-xi.

⁵³ The National Assembly must have at least 101 seats but can, with additional seats allocated, have more seats. This can happen if, in a first election round, no party wins over 50% of mandates and no coalition is established within six days of the election results announcement, following which a second round of elections will be held (all mandates received in the first round will be preserved). Also, if a party or bloc wins more than 2/3 of mandates in the first round, additional mandates will be distributed among other parties to ensure that at least 1/3 of all seats are held by parties other than the winning one.

⁵⁴ The ‘My Step Alliance’ gained 70.4% of the votes and 88 seats, Prosperous Armenia 8.3% and 26 seats, and Bright Armenia 6.4% and 15 seats. The former ruling party, the Republican Party of Armenia (RPA), 4.7% and thus is not represented in the National Assembly.

⁵⁵ Defense and Security; Economic Affairs; European Integration; Financial-Credit and Budgetary Affairs; Foreign Relations; Health Care and Social Affairs; Protection of Human Rights and Public Affairs; Regional and Eurasian Integration; Science, Education, Culture, Diaspora, Youth and Sport; State and Legal Affairs; and, Territorial Administration, Local Self-Government, Agriculture and Environment.

34. The new Government comprises the Prime Minister, 2 Deputy Prime Ministers and 12 Ministers.⁵⁶ There are furthermore 11 committees and inspectorates as well as 3 entities directly referring to the Prime Minister (National Security Service, Police, and State Control Service). The Prime Minister is nominated by the parliamentary majority (roll-call voting) and appointed by the President. The Government is then formed by the Prime Minister proposing deputy prime minister and minister candidates to the President who appoints them.⁵⁷ The (new) Government must then within three weeks prepare and submit a program to the National Assembly, which approves it by a simple majority.⁵⁸ The Prime Minister determines the main directions of the Government's policy, manages the related activities, and coordinates the work of the Government members. The Prime Minister also chairs the National Security Council. Deputy Prime Ministers coordinate specific activities upon assignment of the Prime Minister, while Ministers independently manage their ministerial activities. From September 1991 to December 2018, Armenia had 16 prime ministers, i.e. an average term of about 1½ year, but – as Armenia until early 2018 had a semi-presidential system – this high turnover had limited impact on policy development and implementation.

35. The President is the head of the State and is elected by the National Assembly for a term of seven years. The duties and functions include appointing the Prime Minister and the Cabinet; concluding international treaties upon recommendation of the Government; appointing and recalling diplomatic representatives upon recommendation of the Prime Minister; appointing and dismissing the supreme command of the armed forces and of other troops upon recommendation of the Prime Minister; granting and terminating citizenship; granting pardon to convicts; decorating with orders and medals, and conferring honorary titles; and making temporary appointment of officials in cases where the National Assembly fails to do so. Hence the role and responsibilities of the President is now largely ceremonial.

36. The judicial system has a three-tier structure comprising courts of the first instance of general jurisdiction (civil and criminal cases) and the Administrative Court (cases involving public entities), courts of appeal, and the Cassation Court and Constitutional Court. The Supreme Judicial Council, a state body, is set up to guarantee the independence of courts and judges as regards appointment and promotion, disciplinary liability and criminal prosecution, and other matters. Judges of the Constitutional and Cassation Courts are elected by the National Assembly by a three-fifth majority, which is the same procedure applied to the election of the Prosecutor General, but the President has retained an unlimited discretion to reject nominated judges. The judiciary has often been considered compliant to the demands of the Executive, and there has been a general problem of prosecutorial bias and dominance of the prosecutor within the system.⁵⁹ Also, judicial accountability mechanisms are weak and bribery are common at all levels, which results in the courts being mistrusted institutions.⁶⁰ Reforms have been based on a strategic program for 2012-2017, which was carried out with the 2015 constitutional amendments and other measures. However, some challenges remain, including that the workload of judges adversely affects the quality of judicial decisions, and that judges lack training on how to write qualified judicial decisions.⁶¹ The Minister of Justice in October 2018

⁵⁶ According to Article 147 of the Constitution, the number of deputy prime ministers may not exceed three, and the number of ministries may not exceed 18.

⁵⁷ The President must within three days either appoint the candidates, or apply to the Constitutional Court which will then examine the application and take a decision within five days.

⁵⁸ Failure to approve the program, which would then also require the election of a new Prime Minister, would result in the National Assembly being dissolved.

⁵⁹ Bertelsmann Stiftung. 2018. op.cit., p. 12.

⁶⁰ Freedom House. 2018. *Nations in Transit – Armenia*. April, p. 6.

⁶¹ EU Delegation. 2018. *Development Partners' Joint Analysis of the Situation in Armenia*. May, pp. 142-143.

established a working group, with an equal ministerial and CSO representation, to prepare a Legal and Judicial Strategy and Action Plan for 2019-2024.

37. The GoA has in recent years reviewed and amended many core legislative acts to align with international standards and to eliminate inconsistencies,⁶² but consistent application remains a challenge. There has also been progress in implementing structural reforms – e.g. the 2016 tax code, 2017 energy sector reform, and 2018 pension reform – but sustainability of these achievements will depend on carrying out further reforms, including in strategic economic areas and with regard to anticorruption.

38. Decentralization is a relatively new concept in Armenia as the two-tier government system was introduced only with the 1995 Constitution, which assigned the responsibility for a number of tasks to the municipalities,⁶³ while the Law on Local Self-Government was enacted in 2002. Constitutional amendments in 2005 assigned further functions to municipalities.⁶⁴ The decentralization process generally improved the delivery of public services, but has also seen some challenges due to the large number of small municipalities and many having limited financial resources.⁶⁵

39. Armenia in the 1990s had an unstable public administration with a high staff turnover. This was changed with the adoption of the Civil Service Law in 2001, which outlined new employment principles (professionalism, merit-based hiring, guarantees of stability and independence, etc.) and created the Civil Service Council (CSC).⁶⁶ However, some issues remained that had an adverse effect on public sector performance, including that ministries and agencies had limited discretion in hiring, firing, promoting and disciplining civil servants, which has constrained their capacity to undertake effective and timely human resource management.⁶⁷ This issue extends to the Audit Chamber as it lacks full independence from the Executive, which is inconsistent with international best practice for supreme audit institutions (SAIs). Another issue is that civil servant salaries are relatively low compared to the private sector, which makes it difficult to recruit and retain qualified staff, but also increases the risk of corruption. Further issues are:⁶⁸ Inadequate tools and capacities for HR management, legal framework not consistent with international best practice, and insufficient training and capacity building.

40. The Government in December 2015 approved the CSC's Civil Service Reforms Strategy and related action plan, which is being implemented during 2016-2020 and aims to establish a professional and merit-based civil service system in line with modern public administration principles, standards and international best practices.

41. The NGO sector in Armenia is considered fairly well-developed and institutionalized, but also detached from the broader public, donor-driven and with low public trust.⁶⁹ The impact of civil society is constrained by the state not engaging it sufficiently in constructive dialog or granting it a role in public debate and in formulating policy.⁷⁰ Civic activism has in recent years developed more through social media-based

⁶² Bertelsmann Stiftung. 2018. op.cit., p. 31.

⁶³ The decentralized tasks included water supply and sanitation; solid waste management; local roads construction, rehabilitation and maintenance; and, regulation of local public transport.

⁶⁴ Including municipal development, construction and operation of public utilities, and land management.

⁶⁵ ADB. 2014c. *Overview of Armenia's Public Sector Management*. Country Partnership Strategy: Armenia, 2014-2018, p. 3.

⁶⁶ The CSC was, according to the new Law on Civil Service approved by the National Assembly in March 2018, dissolved as of July 2018 and its functions transferred to the Prime Minister's Office.

⁶⁷ ADB. 2014c. op.cit., pp. 2-3.

⁶⁸ Civil Service Council (CSC). 2015. *Civil Service Reform Strategy of the Republic of Armenia*. Annex No. 1, Government Session of 29 December 2015, Protocol Decision No. 57, pp. 6-7.

⁶⁹ Bertelsmann Stiftung. 2018. op.cit., p. 15 and p. 29.

⁷⁰ Ibid.

practices ranging from environmental to social campaigns. This is partly a generational change as new activists were born after Armenia gained independence that have expectations and means that differ from their predecessors.

42. Armenia started preparations to join the Extractive Industries Transparency Initiative (EITI) in 2015 and became a candidate country in March 2017. The EITI process is led by the Deputy Prime Minister and supported by a secretariat. The 2017 EITI Annual Progress Report was published in June 2018, and Armenia's first EITI National Report (on the metal mining sector) was published at a conference in January 2019. A new official website (www.eiti.am) has also recently been introduced. The validation process vis-à-vis EITI's 2016 Standard is scheduled for September 2019.

D. Country Development Strategy

43. The *Armenia Development Strategy (ADS) 2014-2025* was approved in March 2014.⁷¹ While the second Pashinyan government has initiated the preparation of a new country-level strategy, which is expected to be ready by early 2020, it is understood that the ADS remains the strategic framework for development of state policies.

44. The ADS has four main priorities: (i) Employment growth (creating well-paid jobs); (ii) human capital development (enhancing scope, quality and accessibility of primary services as well as professional growth, civic education and better cultural activities); (iii) Improving the social protection system (ensuring the effectiveness of existing systems, provision of social guarantees, reducing social risks and poverty, and gradual transiting from monetary social aid to needs-based social assistance); and, (iv) institutional modernization of the public administration and governance (adopting policies focusing at improved public service efficiency, targeted use of public resources, improved service quality and accessibility, reduced corruption, transparent decision-making, and increased civil society participation in these processes).

45. To modernize public administration and improve governance (priority no. 4), the ADS calls for strengthening PFM,⁷² reforming the state inspection system, enhancing local self-governance, developing e-government, improving the civil service and judicial systems, and reducing corruption.⁷³ There is no overall public administration reform (PAR) approach in place,⁷⁴ but rather the government has prepared separate strategies for civil service reform, e-governance, digital transformation and anticorruption.

46. The previous RPA-led Government prepared a 2017-2022 program with medium-term goals in various reform areas as well as annual programs with detailed action plans.⁷⁵ It is understood that progress reviews of the annual action plans were undertaken, but the monitoring reports were not made public. The previous Government also in February 2018 prepared a draft document 'Armenia Development Strategy 2030', but it was not approved before the change in government.

47. The new Government in June 2018 presented a policy program to the National Assembly, which was approved by 61% of the parliamentarians. It focused mainly on preparing for early elections, ensuring external and internal security, and fighting

⁷¹ GoA. 2014. *Armenia Development Strategy for 2014-2025*. Annex to Government Decree # 442-N, 27 March.

⁷² Enhance the quality of macro-economic analysis and the linkage to medium-term and annual budgeting, improve fiscal risk management, transition to program-based budgeting, introduce internal public finance supervision/internal audit, implement accrual accounting, initiate rigorous public investment assessments, establish fixed asset registers, and increase the salaries of civil servants by at least 10% annually.

⁷³ ADB. 2014c. op.cit., p. 3.

⁷⁴ The institutional set-up for PAR is also not clear, but it appears that the 'Commission on Public Administration System Reforms' established in 1999 by the Prime Minister (Decree No. 544-A) and the Government (Decision No. 624), is still active and hence would be the focal point for PAR.

⁷⁵ For example, the 2018 'Action Plan and Priority Issues' covered 169 actions presented by state entities.

corruption, but it also covered planned reforms in regard to judicial and social issues, economic development, and the diaspora. To provide direction, the GoA is now preparing strategic roadmaps for infrastructure, human capital, financial and economic sectors, public administration, and justice.

48. The Cabinet in February 2019 presented a five-year plan focusing mainly on economic reform, but also covering other areas and sectors. The plan was adopted by the National Assembly on 12 February 2019. It includes a number of ambitious goals – e.g. reducing poverty and eliminating extreme poverty by 2023, increasing exports to 43-45% of GDP by 2024, and average 5% annual economic growth – but is somewhat less specific about how these goals would be achieved. The plan thus seems to be a vision document that will require a concrete action plan to be developed.

49. Strategic planning is complicated by the lack of a hierarchy of national and sectoral strategic plans and a synchronization of planning horizons. While the Constitution (Article 154) requires the Government to make a ‘unified economic and financial state policy, no legislation is in place that specifies a structure of planning documents or facilitates consistency between these.⁷⁶ A decree was passed in 2017 to streamline strategic plans into three levels (comprehensive, medium-level budget program),⁷⁷ but further regulations required to make it fully effective is outstanding.

50. The GoA in 2015 initiated preparations for adopting the *Sustainable Development Goals (SDGs)* of the United Nations (UN), but this only gained traction when the Prime Minister established an Inter-Agency Committee under the National Council for Sustainable Development in February 2017.⁷⁸ The process of nationalizing SDG targets started in 2016, but is yet to be finalized. The GoA in November 2017, with support from UNDP, set up a National SDG Innovation Lab, which aims to help accelerating the achievement of SDGs by drawing upon innovative methodologies and expertise. Also, a National SDG Statistical Platform has been developed by the Statistical Committee of Armenia with UN support.⁷⁹ Armenia has so far had mixed results in implementing SDGs:⁸⁰ While there is good progress in many areas (e.g. child and maternal health; water supply; urban sanitation; reliable and renewable energy; and, environmental protection), there are several areas with slow or mixed progress (e.g. poverty; education; gender equality; water usage; land degradation; rural sanitation; governance; and, sustainable consumption and production practices).

51. Armenia has been a member of the *Open Government Partnership (OGP)* since 2011, and is presently implementing its fourth action plan (2018-2020).⁸¹ It covers 11 actions related to ‘ensuring transparency and accountability’ (open data in official declarations, accountability for grants, and open and public beneficial ownerships’ register), ‘promoting access to information’ (modernizing community websites, unified

⁷⁶ IMF. 2019b. *Republic of Armenia – Public Investment Management Report*. Technical Assistance Report, Country Report No. 19/33, January, Table 6, p. 45.

⁷⁷ Protocol Decision No. 42 of 5 October 2017 (‘On approving the instruction for developing, presenting of and performing control over strategic documents having implications on public expenditures and revenues’).

⁷⁸ The National Council was set up already in 2002 to support the design of sustainable development-oriented programs as well as to foster and stimulate public participation in decision-making processes in the area of sustainable development. It is headed by the Prime Minister and comprises a number of ministers, the heads of three National Assembly standing committees, and representatives from business associations and CSOs.

⁷⁹ The database can be found at <http://www.armstat.am/en/?nid=699&thid=1&submit=Search>.

⁸⁰ UNDP. 2018. *SDG Implementation, Voluntary National Review (VNR), Armenia*, p. 3.

⁸¹ An annual progress report is yet to be prepared the fourth action plan. The latest review, from early 2018, was of third action plan and found the commitments as being too limited in scope to lead to significant changes and thus recommended that the government should work with CSOs and the National Assembly to develop more ambitious commitments that could lead to sustainable reforms in budgeting, contracting and company ownership. The level of completion was assessed as substantial for two commitments, limited for five commitments, while one action had not yet started [Open Government Partnership (OGP). 2018. *Independent Reporting Mechanism (IRM): Armenia Progress Report 2016-2018*. Version for public comment].

information system for water resources, public accessibility of the Land Cadastre, and access to integrated social services), and 'promotion of public participation (unified information for education management, on-line listing of state guaranteed free-of-charge medical assistance and services, unified electronic platform for submitting petitions, and dashboard for citizen feedback on public services). The actions thus focus on e-government and public participation. The GoA's current working group to coordinate the work stipulated under the OGP action plan comprises 25 members.⁸²

52. Armenia has no formal forum for government-development partner collaboration. Coordination and information exchange instead takes place on an ad-hoc basis. Development partners are occasionally invited as observers to government meetings and vice versa. The latter include meetings of *development coordination thematic groups*, such as the PFM Donor Coordination Group, which are informal gatherings to exchange information and discuss current issues.

53. A number of development partners are providing support in the broader governance area. Some of the major initiatives are **ADB's Social Sectors Reform Program** (2018-2019), which is helping the GoA developing comprehensive policy reforms in the education and health sectors that aim to improve resource utilization and service quality. The **Gesellschaft für Internationale Zusammenarbeit (GIZ)** is implementing the *Legal Approximation towards European Standards in the South Caucasus Project* (2015-2020), which provides support for reform of the legal and judicial systems in line with EU standards and uses regional dialogue on the rule of law. The **EU Delegation** is implementing a *PAR budget support program* (2017-2019)⁸³ that covers policy and legislative capacity building, CSO professionalization, anticorruption as well as openness and integrity, and e-governance. The EU Delegation is also implementing several other projects in the areas of IT, governance and human rights, and civil society.⁸⁴ The **United Kingdom's** Good Governance Fund (2015-2021), implemented across the region, supports reforms on anticorruption, business environment, responsive and accountable governance, and media and civil society freedom. **USAID** is implementing several initiatives, including the *Local Governance Reform Activity* (2014-2019), which assists the Ministry of Territorial Administration and Development (MoTAD) to implement its decentralization policy and provide grants for community development, *Civic Engagement in Local Governance* (2014-2019), which supports CSOs to increase civic engagement and oversight of local governance and decentralization reform, *CSO Development Program* (2014-2019), which works to develop CSOs to become more business-oriented and sustainable service providers, *Media for Informed Civic Engagement Project* (2016-2022), which focuses on public media literacy and access to independent and reliable information on government policies and reforms, and *Enhanced Transparency in the Mining Sector project*, which supports Armenia's EITI engagement. The **World Bank** is implementing the *Armenia Social Investment and Local Development Project* (2015-2020), which aims to improve the quality and use of and access to community and inter-community infrastructure through capacity building and institutional strengthening, *Implementation of the National Strategy Program for Strengthening of the National Statistical System* (2017-2021), which will help to develop the statistical system and the technical capacity of National Statistical Service staff, *Armenia Mineral Sector Policy* (2017-2020), which is supporting relevant ministries to develop a Mineral Sector Policy, and *Armenia EITI*

⁸² 14 are from the Government, 10 from civil society, and 1 from the private sector (<https://www.ogp.am/en/>).

⁸³ A related TA component is yet to be launched.

⁸⁴ *EU4Digital in Armenia* (2017-2020), *Protection of Human Rights in Armenia Budget Support Program and TA project derived from it*(2017-2019), *EU4HumanRights: Pursuing Positive Change through Empowering Civil Society* (2017-2019), *Access to Information and Investigative Journalism for Better Informed Citizens* (2017-2019), and *A Public Glimpse into a Closed World: Increasing Awareness on the Human Rights Situation in Closed Institutions* (2017-2019).

Support (2017-2020), which is assisting the GoA to increase transparency and accountability in the mining sector by implementing the EITI standard. **GIZ, USAID and the Swiss Agency for Development and Cooperation (SDC)** are furthermore co-financing the *Good Local Governance in South Caucasus Project* (2017-2019), which supports the MoTAD and municipalities to carry out administrative and development tasks in line with good governance principles.

IV. ASSESSMENT OF COUNTRY SYSTEMS

54. This chapter provides an overview over and descriptions of the functioning and performance of the government's PFM, procurement and anticorruption systems.

A. Public Financial Management

55. The description and analysis of the performance of the government's PFM system is based on the following information sources: The 2014 country-level PFM Performance Assessments,⁸⁵ documentation from the MoF and development partners, discussions with ADB staff engaged in PFM reform activities, and consultations with various stakeholders on recent developments and current status.

PEFA Assessment

56. A comparison of the 2008 and 2014 PEFA assessments in terms of the average scores for the six high-level PFM dimensions provide a first indication of the trajectory of change regarding PFM reform in Armenia.⁸⁶ The results of the 2013 PEFA assessment of Yerevan City⁸⁷ are shown as a comparison to the national-level.

Table 1 – Comparison of 2008 and 2014 PEFA Assessments, and Yerevan City

Dimension		GoA 2008	GoA 2014	Trajectory of Change	Yerevan City 2013
A	Credibility of the budget	A	A	↔	C+
B	Comprehensiveness and transparency	A	A	↔	B
C	Policy-based budgeting	A	A	↔	C
D	Predictability and control in budget execution	B	B	↔	C
E	Accounting, recording and reporting	C+	B+	↑	C
F	External scrutiny and audit	C	C	↔	C
Overall Average Score (all indicators)		B	B	↔	C

Note: The dimension-level scores are calculated by quantifying the 28 PEFA performance indicator-level scores (using the following conversion: A = 4, B+ = 3.5, B = 3, C+ = 2.5, C = 2, D+ = 1.5, D = 1) and the average score per dimension then calculated and converted into PEFA scores (1.00-1.75 = D, 1.75-2.50 = C, 2.50-3.25 = B, 3.25-4.00 = A).

57. The average dimension-level PEFA scores were high both in 2008 and 2014, meaning that the GoA's PFM system overall is considered well-functioning (in terms of the elements covered by the two assessments). The average score for the 'accounting, recording and reporting' dimension improved from C+ in 2008 to B+ in 2014. The risk associated with the overall score at the national level was 'moderate' in both years.

58. The scores for Yerevan City are lower than the GoA's for all dimensions except 'external scrutiny and audit' (which reflects that the work of the Audit Chamber is similar between the GoA and Yerevan City). The risk associated with the overall score in 2013 for Yerevan City was 'substantial'.

59. The performance status of the six high-level PFM dimensions as of 2014 for the GoA is briefly described below:

⁸⁵ Government of Armenia. *Public Expenditure and Financial Accountability (PEFA) Assessment 2013 – Republic of Armenia (Central Government)*, 11 May. The assessment was supported by the EU Delegation, the World Bank and GIZ.

⁸⁶ The conversion is not part of the PEFA framework, but has been done here to facilitate asserting general changes in performance from 2009 to 2015.

⁸⁷ World Bank. 2013. *Yerevan City: Public Expenditure and Financial Accountability (PEFA) Performance Review*. October.

- **Credibility of the budget** – Actual expenditures and revenues were relatively close to the approved budgets at both aggregated and disaggregated levels. Expenditure arrears were almost non-existent due to strong expenditure commitment controls.
- **Comprehensiveness and transparency** – The budget classification was based on international standards, and information included in budget documentation was comprehensive. The level of unreported extra-budgetary expenditure was estimated at 4.5% of total state expenditures as the spending of state non-commercial organizations (SNCOs) and other government-owned entities was not covered by the annual State Budget Law and the entities did not use the treasury system. Transparency of inter-governmental fiscal relations was high and the public had access to most key fiscal information. However, fiscal risk oversight of SNCOs and closed joint stock companies (CJSCs) was limited and external audits were not mandatory. Also, financial monitoring of communities was incomplete, except for Yerevan Municipality.
- **Policy-based budgeting** – The annual budget preparation process was well-functioning and included program-based budgets submitted to the National Assembly in parallel with the official budgets. The budget process had a multi-year focus through the MTEF,⁸⁸ but sector strategies were not costed and the recurrent cost implications of major investments were not always estimated and included in the budgets.
- **Predictability and control in budget execution** – Progress had been made to strengthen revenue administration, but tax arrears remained high. The predictability of resources for budget execution was high and the management of cash and debt was strong. However, payroll controls were adversely affected by reconciliation between the payroll and personnel records not being undertaken. Internal control of non-salary expenditure had improved with the introduction of the client-treasury system and payments being processed with the treasury software, but shortcomings remained in the understanding of and compliance with internal control rules and procedures. The internal audit function was new and performance was hence being developed.
- **Accounting, recording, and reporting** – Account reconciliation of treasury-managed accounts was frequent and timely, and information on resources received by service delivery units was available. Also, the quality and timeliness of in-year budget reports was relatively good. However, the absence of modern accounting standards hindered the preparation of meaningful and auditable annual financial statements.
- **External scrutiny and audit** – The performance of the external audit function had improved, but it did not yet meet international standards for SAI independence.⁸⁹ The National Assembly and its Standing Committee on Financial and Budgetary Affairs closely examined audit reports, but recommendations had no mandatory force. The legislative scrutiny of the annual State Budget Law had adequate scope and time, but the Executive had significant discretion to adjust the budget during the year without seeking prior approval from the National Assembly.

60. A number of initiatives have been implemented since 2014 to improve the functioning of the PFM system, including:

- Adoption of the Law 'On Accounting of Public Sector Organizations' (2014), which provides for a new accounting system and new public sector accounting standards based on International Public Sector Accounting Standards (IPSAS).

⁸⁸ The MTEF in Armenia includes a macro-fiscal framework that defines medium term fiscal priorities, macro and budgetary forecast overall, and sector resource envelopes.

⁸⁹ Independence is covered in the 1977 Lima Declaration of Guidelines on Auditing Precepts (International Standards of Supreme Audit Institutions (ISSAI) 1) and the 2007 Mexico Declaration on SAI Independence (ISSAI 10) of the International Organisation of Supreme Audit Institutions (INTOSAI).

- Enhancement of the MoF's macro-economic and revenue forecast modeling tools.
- Improvement of strategic planning with linkages to the annual budget process and the MTEF, and establishment of a Strategic Planning Unit in some ministries.
- An incremental rolling baseline process that focuses on new initiatives and discretionary expenditures that could be re-allocated as well as ensuring that mandatory expenditures are correctly defined.
- Preparation of a program budgeting manual outlining methodological aspects and defining program activities and indicators, and common guidelines for costing of individual programs and activities.
- Development of a public internal financial control (PIFC) methodology and piloting in two sectors.
- Preparing guidelines for economic analysis of public investment programs and establishing program database.
- Amendment of public investment execution procedures to reduce under- and over-execution.
- Expansion of annual fiscal risk statements (in the MTEF and the state budget documentation) to include non-financial corporation fiscal risks in the energy, water and transport sectors.
- Amendment of the internal audit methodology (2016) to clarify and improve internal audit performance, development of an Internal Audit Manual, and preparation of an External Quality Assessment Manual.⁹⁰
- Development of fiscal risk management guidance for the energy, water and transport sectors, and for budgetary lending.
- Adoption and implementation of a new Tax Code (2016), which integrates tax legislation and aims to simplify tax administration procedures.⁹¹
- Amendment of the Budget System Law (2017), which introduces concepts required for the full implementation of program budgeting, including for appropriation by the National Assembly,⁹² and upgrade of the fiscal rule system.
- Amendment of the Treasury System Law and the Law on SNCOs (2017) extending the coverage of the treasury system to the extra-budgetary entities.
- Adoption of the Law On the Audit Chamber (2018) making it an independent state body and providing for some independence in its operations and for undertaking financial audits according to international standards.
- The Government approved a public-private partnership (PPP) policy statement (2017) and the National Assembly approved a new PPP law (June 2019), which will codify the PPP policy framework. Secondary legislation is currently being prepared.
- Elaboration of a new concept of MTEF-annual State Budget development based on which the budget preparation process will be revised (applicable for the 2020 budget preparation process once the decree is signed by the Prime Minister).

⁹⁰ The Manual was tested at the MoF and the Ministry of Education and Science (MoESCS).

⁹¹ The GoA plans further changes to the tax system from 1 January 2020, including to simplify the tax system for small entrepreneurs, eliminate patent tax, transition to a single income tax rate, reduce the profit tax rate from 20% to 18% and the dividend tax rate from 10% to 5%, and increase excise tax rates (to compensate for revenue loss resulting from reducing profit tax and income tax). The overall impact on the state budget is expected to be neutral [http://www.minfin.am/en/content/the_key_directions_of_the_proposed_amendments_to_the_tax_system_were_presented/#sthash.gyjKtFrk.dpbs].

⁹² The 2019 State Budget was submitted in program budgeting format, as the main budget classification format, to the National Assembly and adopted on 22 November 2018. Furthermore, budget programs of the draft budget were, prior to the official submission to the National Assembly, discussed by the sector standing committees jointly with the MF and line ministries.

- Training of staff in various areas, including MTEF development, public investment management (PIM), asset management, internal audit and external audit.
- Establishment of the Budget Office as a secretariat for the National Assembly's Standing Committee on Financial-Credit and Budgetary Affairs.

61. The many significant developments that have taken place in recent years provide the GoA's PFM reform with a positive trajectory.

62. The present PFM reform challenges and outstanding activities include the following:

- The annual as well as the medium-term budgeting processes have recently been amended (for 2020 annual budget and the 2020-2022 MTEF, respectively) and are now to be implemented, including with a separation of mandatory and discretionary commitments so as to consider and make decisions on expenditure policy taking into account discretionary and flexibility in the budgetary process.
- A methodology for costing sector strategies is yet to be developed and approved, and the recurrent cost implications of major investments are not estimated and included in the budgets on a regular basis.
- Due to the fiscal rule debt and deficit ceilings (and the lack of a mechanism to protect funding for on-going projects), the Government has had challenges in ensuring adequate funding for some development partner-financed projects.
- Several existing public expenditure items classified as subsidies are actually grants or transfers, and regular monitoring of their performance does not take place.⁹³
- While the MoF discloses specific fiscal risks, mitigation measures are not formulated, and there is no summary reporting and limited quantification.
- Fiscal risk management functions are weak (e.g. SOEs). Legal aspects, appraisal methodologies and fiscal risk management related to PPPs are particularly weak or yet to be fully established. Information about total rights, obligations and other exposures under PPP contracts are not published or tracked.⁹⁴
- The internal audit function in line ministries requires further capacity development.
- Payroll controls remain weak as the reconciliation process between the payroll and personnel records has not yet been improved.
- The preparation of an auditable annual consolidated financial statement is work-in-progress (currently planned for 2019),⁹⁵ including as regards to developing the necessary software.
- The basic approach for the government financial management information system (GFMIS) is yet to be decided (integrated versus interfacing) based on which a design can be developed.⁹⁶
- The status of the Audit Chamber remains inconsistent with INTOSAI standards on independence as regards financial autonomy, appointment and termination of staff.

⁹³ World Bank. 2016. *Republic of Armenia – Programmatic Fiscal Work, Supporting Effective Fiscal Management*. Report No: ACS18362, 20 June, p. 46 and p. 49.

⁹⁴ Considering that the PPP capital stock presently amounts to about 10% of GDP, and with several new PPPs planned, this is a critical issue.

⁹⁵ The MoF does prepare an annual budget execution report, but it does not include accounting information on financial assets and liabilities, and the Audit Chamber is therefore not able to provide an opinion about the fair presentation of the financial position and the result of operations.

⁹⁶ A 2011 review of the existing PFM IT system highlighted the following weaknesses: Poor system integration and automation; poor articulation of modules with the general ledger; and absence of a double-entry accounting system to facilitate timely and accurate annual financial reporting [World Bank. 2015. *Project Appraisal Document on a Proposed Loan ... for a Third Public Sector Modernization Project*. Report No: PAD1252, 2 September, p. 14].

- The external audit activities as carried out by the Audit Chamber are not yet fully based on international standards and staff capacity needs to be further developed.

63. Furthermore, the Law on Audit Activity (2002), which regulates private auditors, does not provide for independent public oversight or quality assurance review. A new law drafted in 2014 would have addressed both issues,⁹⁷ but it remains under review by the MoF.⁹⁸ However, in auditing externally-funded projects implemented by the public sector, private auditors carry out a key PFM function, and addressing the issues of oversight and quality assurance is therefore important.

64. Armenia faces particular challenges with regard to public investments:⁹⁹ 1) The public capital stock has declined from 160% of GDP in 2000 to 62% of GDP in 2017 due to a faster growth of recurrent spending relative to capital spending; 2) There are significant gaps in the efficiency of public investments in the health, energy and roads sectors in terms of physical outputs and quality; and, 3) There is an increasing reliance on external financing for major public investment projects with the share having risen from 21% to 63% of total capital expenditure in the past ten years. Furthermore, there are several weaknesses in the PIM framework,¹⁰⁰ including that planning documents do not guide investment decisions as planning horizons and project costs are inconsistent across documents and with the MTEF envelop, there is no standardized requirements or methodologies for project appraisal, there are no criteria for selecting major projects and no project pipeline exists, and the MoF does not have the mandate to reprioritize projects with implementation problems.

65. Financial management assessments undertaken by ADB in recent years for new project investments have found PFM weaknesses as regards implementation of program-based budgeting (weak capacity and poor information flows), budget execution reports (not consistent with international standards) and external audit (not consistent with international standards). The fiduciary safeguards applied by ADB have generally been based on establishing a PIU to manage project implementation, including by using accounting, financial reporting and external auditing standards acceptable to ADB. Some risk management plans also include the risk of counterpart funding being released with a delay, or being less than budgeted/required, but no actual safeguards have been formulated in this regard.

PFM Reforms

66. Based on the results of the 2008 PEFA assessment, the MoF in 2010 developed a PFM Reform Strategy for 2010-2020 which, after approval by the GoA, was implemented from 2010 onwards. It was based on strengthening the control framework and decentralizing management responsibility for budgeting and planning, budget execution and procurement. It also covered the introduction of program-based budgeting, capacity building for managers and PFM specialists across the GoA, and the development of a GFMS. The activities implemented during 2011-2014 were evaluated with technical assistance provided by the European Union in 2014. The PFM Reform Strategy was revised in 2016 for the period 2016-2020,¹⁰¹ which included a

⁹⁷ The Law on Regulation and Oversight of Audit would transform the Armenian Association of Accountants and Auditors (AAAA) into the Chamber of Accountants and Auditors of Armenia (CAAA) with a mandate to certify auditors, conduct quality assurance reviews, perform auditor training/qualification functions, and adopt and translate professional standards. A new Public Oversight Board (POB) would oversee the CAAA's activities.

⁹⁸ <https://www.ifac.org/about-ifac/membership/country/armenia>.

⁹⁹ IMF. 2019b. op.cit., p. 7.

¹⁰⁰ Ibid, Table 1, p. 9.

¹⁰¹ MoF. 2016. *Revised Strategy of the Public Finance Management System Reform*. Annex 1 of the Protocol Decision N6 of the Government Session 18 February 2016.

detailed Action Plan covering 11 specific areas/components.¹⁰² The MoF undertakes quarterly follow-up on implementation progress and prepares an annual report that is submitted to the Prime Minister's Office. However, the reports are not publically available, hence implementation progress cannot be established externally, although the MoF does periodically provide information regarding reform implementation to the development partners and other stakeholders. The MoF aims to prepare a new/updated PFM reform strategy and action plan in the near future.

67. The MoF in 2015, with support from GIZ, prepared a strategy for the full implementation of program-based budgeting,¹⁰³ which included a detailed action plan for 2015-2017 covering the MoF, National Assembly's Standing Committee on Financial-Credit and Budgetary Affairs, Audit Chamber and state institutions. It appears that the action plan has been more or less fully implemented, although with some delay. While this as such an achievement, considering that program-based budgeting was first introduced in 2004, the overall progress has been very slow.

68. Development partner support: Development partners have been engaged in PFM reform activities for a number of years. The main development partners are:

- **GIZ** – Support to develop and improve program-based budgeting, internal audit, external audit, parliamentary control, and tax administration through the Public Financial Management in the South Caucasus project (2017-2020).
- **IMF** – TA in the areas of fiscal rule, tax policy and fiscal risk management. The IMF is also in the process of preparing a fiscal transparency assessment.
- **World Bank** – Support to develop and implement a GFMIS through the Third Public Sector Modernization Project (2016-2020) and for tax administration reform through the Tax Administration Modernization Project (2012-2019).¹⁰⁴
- **EU Delegation** – A 2016-2020 budget support program covers the areas of program-based budgeting, procurement, citizen engagement in budgeting, external audit and parliamentary oversight. Related TA is not yet launched.

69. Other development partners providing support for PFM reform include USAID (revenue mobilization as well as IT support for the Audit Chamber), UK Embassy (parliamentary oversight), Russian Federation (grant to support the GFMIS development process) as well as UNICEF and WHO (budget-related aspects in their sector engagements).

70. ADB's support for PFM reform includes the Infrastructure Sustainability Support Program (2015), a policy-based loan (PBL) with actions on developing recurrent cost financing strategies and carrying out capacity development of internal auditors in the roads and water sectors. Other ADB operations have focused more broadly on developing public sector management as well as improving the business environment and investment promotion. This includes the Support to Public Efficiency and Financial Markets Program (2017-2019) with two PBLs with actions on strengthening public debt and fiscal risk management policies, improving the GoA's securities market and money market infrastructure, and broadening the base of instruments and investors as well as enhancing corporate transparency. Also, TA support has been provided for fiscal risk

¹⁰² 1) Fiscal strategy and budget credibility – forecasting macro-economic and budget indicators; 2) Fiscal strategy – strategic planning, preparation of MTEF and the budget; 3) State procurement; 4) Public internal financial control (PIFC) – financial management and control as well as internal audit; 5) Budget execution reporting; 6) SNOCs; 7) Public sector accounting; 8) Corporate accounting and auditing; 9) State revenue policy; 10) External oversight and legislative control; and, 11) GFMIS.

¹⁰³ MoF. 2015. *Strategy for Full-fledged Introduction of Programme Budgeting*. Annex to the Government Protocol Decree N38 13 August 2015.

¹⁰⁴ The Tax Administration Modernization Project closed on 31 January 2019.

management to improve the GoA's capacity for PPPs and ensuring that a proposed new legal and institutional framework promotes development-relevant and fiscally responsible PPPs. ADB is currently preparing a third PBL within this program. In December 2018, the GoA requested ADB to provide technical assistance in order to support (i) diagnostic work and analysis on performance-based budgeting, PIM and revenue management, (ii) preparation of a prioritized and sequenced PFM Reform Implementation Roadmap that would provide a cohesive framework for coordination, and (iii) capacity building and training programs needed to implement the Roadmap.

71. Institutional coordination as regards PFM reform is somewhat limited. While development partners exchange information in the PFM Donor Coordination Group, which meets a few times per year, this only includes GoA representatives on an ad hoc basis. This has led to some level of fragmentation as well as overlap of efforts and resources as well as contrasting policy advice. It is understood that the Government aims to set up a new coordination mechanism.

B. Procurement

72. This section provides an overview regarding the functioning and performance of the government's procurement system based on available diagnostics supplemented by consultations with stakeholders.

73. The MoF is in charge of public procurement policy and all operational aspects, including developing and operating the Armenian e-procurement system (ARMEPS). Procurement is fully decentralized, i.e. there is no centralized procurement agency and all public entities undertake their own procurement.¹⁰⁵ There are currently about 1,000 procuring entities, including state entities, local governments and SNCOs.

74. Procurement legislation and regulations, procurement plans, procurement advertisements, contract awards, complaints and decisions, reports and training programs are available on an official website (www.procurement.am). ARMEPS has a separate website (www.armeps.am). The website www.gnumner.am is also used.

75. Total spending on public procurement in 2015 amounted to 11% of the state budget. The aggregate value of procurement was 3.2% of GDP in 2017. According to the MoF, 17% of procurement-related expenditure in 2015 related to 'urgent' (single source) procurement, which in 2017 had decreased to 5.2%. The total number of contracts in 2017 was approximately 25,000 of which 13,000 were managed through ARMEPS, while the remaining 12,000 were paper-based.

76. A new Public Procurement Law (PPL) was adopted by the National Assembly in December 2016 and amended in March 2018. It is based on the United Nations Commission on International Trade Law (UNCITRAL) model and was drafted with support from the EU's Support for Improvement in Governance and Management (SIGMA) program and the European Bank for Reconstruction and Development (EBRD). NGOs were consulted during the drafting process. The PPL distinguishes between four principle procurement procedures – electronic auction, tender, price quotations and single source – and the default method is open tender, unless the goods to be procured are included in an approved list for which electronic auction must be applied. The scope for exemptions has been narrowed in the new PPL.¹⁰⁶

¹⁰⁵ The State Procurement Agency (SPA), in place from 2002 to 2011, was responsible for conducting procurement in coordination with procuring entities. The SPA was in 2011 replaced by the Procurement Support Center (PSC), which provided procedural support for procurement and carried out staff training for procuring entities. The PSC ceased to exist when the new PPL came into force in April 2017.

¹⁰⁶ OECD. 2018. *Anti-Corruption Reforms in Armenia – Fourth Round of Monitoring of the Istanbul Anti-Corruption Action Plan*. September, p. 100.

77. Complaints resolution is undertaken by a three-member Procurement Appeals Board appointed by the President upon nomination of the Prime Minister. The number of complaints grew from 46 in 2014 to 170 in 2017. While there is a high level of transparency as regards the review sessions, the independence of the body can be questioned.¹⁰⁷ Related issues that follow from the amendment to the PPL in March 2018 include:¹⁰⁸ the status of the Board is unclear;¹⁰⁹ the financing of the Board is unclear; the Board members are no longer considered public servants, which means that rules about ethical behavior no longer apply; it is now the MoF that assigns cases to the Board members, which would appear to undermine the independence of the appeals process; and, the previous provision in the PPL on appointment and dismissal of Board members has been deleted.

78. Armenia in 2011 became the first of the former Soviet Union countries to become party to the General Procurement Agreement (GPA) of the World Trade Organization (WTO),¹¹⁰ which regulates government procurement of goods and services by public authorities based on the principles of openness, transparency and non-discrimination.

Procurement Assessments

79. ADB's 2018 Procurement Risk Assessment (PRA) is the most recent and comprehensive diagnostic available for Armenia.¹¹¹ The methodology applied¹¹² is similar to that of a 2009 World Bank study, and the scores of both diagnostics can therefore be compared to show the development over time as seen below.¹¹³

Table 2 – Procurement Assessment Scores and Trajectory of Change

<i>Highest Score: 3.0; Lowest Score: 0.0.</i>		World Bank 2009	ADB 2018	Trajectory of Change
I	Legislative and regulatory framework	2.00	2.40	↑
II	Institutional framework and management capacity	1.50	1.70	↑
III	Procurement operations and market practices	1.70	2.00	↑
IV	The integrity of the public procurement system	1.50	1.80	↑
Overall Assessment Score		1.68	1.98	↑

Source: ADB. 2018b. *Republic of Armenia – TA9033 REG: Procurement Risk Assessment for Improved Procurement Outcomes*, 21 October.

80. There have over the past decade been improvements in the scores across all four pillars, especially as regards legislative and regulatory framework (pillar I) and the integrity of the public procurement system (pillar IV). The overall procurement score for Armenia would indicate a 'moderate' risk rating at the country level.

¹⁰⁷ IDFI. 2017. *Comparative Analysis of Public Procurement Legislations and Practice in Eastern Partnership Countries*, p. 12.

¹⁰⁸ ADB. 2018b. *Republic of Armenia – TA9033 REG: Procurement Risk Assessment for Improved Procurement Outcomes*, 21 October, pp. 29-30.

¹⁰⁹ The PPL amendment in March 2018 changed the term 'Board' to 'Person', but the meaning of this is unclear.

¹¹⁰ The revised GPA of the WTO was approved by the President's Decree N NH-217-N, dated 23 February 2015.

¹¹¹ ADB. 2018b. *op.cit.*

¹¹² ADB. 2015. *Guide on Assessing Procurement Risks and Determining Project Procurement Classification*. Manila. This is based on the 'Methodology for Assessing Procurement Systems (MAPS)'.

¹¹³ World Bank. 2009. *Republic of Armenia, Country Procurement Assessment Report*. Report No. 49975-AM, 29 June, p. 21.

81. **Pillar I – Legislative and regulatory framework:** The legislative and regulatory framework for public procurement is comprehensive and applies to all procurement of goods, works and services. The MoF is in charge of all procurement related policies and operations. The PPL does not include a provision on sanctions for the violation of its provisions by public officials responsible for conducting and managing public procurement. Open competitive bidding is the default method of procurement, and the requirements for undertaking single source procurement are clearly defined. There is no registration requirement for participation in tenders. The legal and regulatory framework does not require the use of e-procurement for all procurement, and part of public procurement therefore remains paper based.

82. **Pillar II – Institutional framework and management capacity:** The procurement cycle begins after the approval of the annual budget, but procuring entities can in some cases launch tenders without securing funding. Estimates of goods, works and services are not accurate and result in procurement that does not necessarily ensure value-for-money. The MoF registers all signed contracts and reviews them for compliance with the PPL, and can return contracts for corrections or recommend annulment. Capacity building programs are inadequate to meet the needs of all stakeholders, including oversight bodies, the private sector and civil society.

83. **Pillar III – Procurement operations and market practices:** The domestic private sector cannot fulfill all public sector requirements for goods, works and services in a manner that enables value-for-money in public procurement. Applied cost estimation methods are inadequate and result in inaccurate estimates. There is a practice of selecting the lowest priced bidder who, after bids are opened, is allowed to modify the bid for major and minor deficiencies. This often results in provision of substandard goods, works and services, and occasionally to contract performance failure. The PPL originally provided for a more or less independent appeals board, but a change to the PPL in 2018 has in effect made the MoF responsible for the process. Armenia is a signatory to the Convention on the Recognition and Enforcement of Foreign Arbitral Awards, but arbitration is not used for contract dispute resolution.

84. **Pillar IV – Integrity and transparency of the public procurement system:** Relevant and comprehensive procurement information, including laws and regulations as well as procurement data, is available on the web portal. However, as most of procurement information, including tender documents, is only published in Armenian and Russian, international firms do not participate in GoA tenders. Anticorruption measures are governed by relevant laws, but there is no specific code of ethics or conduct for public procurement officials. The PPL includes provisions on conflicts of interest, but there are no sanctions for the violation of provisions.

85. According to current regulations, it is mandatory for bidders to provide a 'statement on beneficial ownership' and 'statement on absence of conflict of interests'. Submitted statements are available on the procurement website. However, it is not clear that a mechanism to objectively and diligently review the statements is in place.

Other diagnostics

86. The 2014 PEFA assessment found that the new PPL, establishment of a Procurement Complaint Review Board, and the introduction of e-procurement pointed to increased transparency in the procurement system. It was specifically noted that the legislative framework as well as the procurement appeal system met all listed requirements. However, there was insufficient data to assess the extent to which the use of non-competitive methods was justified, which was a concern due to the high incidence of non-competitive procurement on the basis of special or exclusive rights.

87. The results of the World Bank’s Benchmarking Public Procurement 2017 for Armenia are shown below together with the results of neighboring countries.

Table 3 – World Bank’s 2017 Benchmarking Public Procurement

Indicator	Score (out of 100)				
	Armenia	Georgia	Azerbaijan	Iran	Turkey
Needs assessment, call for tender, bid preparation	60	70	64	60	68
Bid submission	39	59	65	78	67
Bid opening, evaluation, and award	64	71	43	57	79
Content and management of procurement contracts	59	77	64	73	73
Performance guarantee	50	54	42	62	74
Payment of suppliers	33	67	30	37	37
Average	51	66	51	61	66

Source: World Bank. 2016. *Benchmarking Public Procurement 2017 – Assessing Public Procurement Regulatory Systems in 180 Economies*, Economy Datasheets.

88. The scores for Armenia indicate that the procurement system is overall assessed as moderately well-functioning. However, there are significant differences between the different areas with two receiving low scores: ‘bid submission’ (because bidders are not required to register on a government registry of suppliers, bidders cannot choose on the form of bid security instruments, and there is no stated timeframe for return of bid security instrument) and ‘payment of suppliers’ (as supplier cannot request payment online and since there is no legal timeframe for the purchasing entity to process payment). Also, the functioning of Armenia’s procurement system is, in a regional comparison, at a relatively low level.

89. The *World Bank* in 2014 carried out an assessment of ARMEPS, which reviewed the system and procedures vis-à-vis the requirements for e-tendering of multilateral development banks.¹¹⁴ It concluded that most requirements were fulfilled for shopping and simple goods/works/non-consulting national competitive bidding (NCB) procedures. Following the development of new procurement modules for the ARMEPS (for procurement planning, monitoring and reporting, and contract administration) and training of PIU staff, the World Bank in 2017 started using ARMEPS for project-related shopping and NCB.¹¹⁵

Procurement in ADB-financed projects

90. ADB’s Final Review of the Armenia CPS 2014-2018 has overall assessed the ADB program implemented as relevant and effective, but ‘less than efficient’ (due to implementation delays, including start-up delays, slow civil works construction, delays in procurement as well as lower-than-expected disbursements and contract awards) and ‘likely sustainable’ (although the Government’s fiscal consolidation program is adversely affecting some projects).¹¹⁶

¹¹⁴ World Bank. 2014. *Assessment of Armenia e-procurement system (ARMEPS)*.

¹¹⁵ http://arka.am/en/news/business/world_bank_to_use_armeps_system_of_public_procurement/.

¹¹⁶ ADB. 2018a. *Armenia CPS 2014-2018 – Country Partnership Strategy Final Review*. First Draft, May, Chapter III.

Procurement Reforms

91. The GoA does not have a separate reform strategy or action plan for public procurement, which is instead part of the PFM Reform Strategy 2016-2020. This covers the following components: 1) Procurement appeals system; 2) Application of non-competitive procurement methods; 3) Computerization of the procurement process; and, 4) Approximation of the procurement legislation to international commitments. Most planned activities appear to have been carried out as planned during 2016-2017, and the current on-going initiatives include technical improvements to the procurement planning system as well as training on procurement sector. With the PPP Law now approved, it may be necessary to revise some aspects of the PPL.¹¹⁷

92. Development partner support: The key development partners supporting procurement reform are the World Bank (procurement planning and e-procurement), EU (e-procurement modules) and EBRD (contract management and e-auction).¹¹⁸

93. Development partners exchange information on procurement reform and discuss related issues in the PFM Donor Coordination Group, which sometimes includes GoA representatives from the First Deputy Prime Minister's Office or the MoF.

C. Vulnerability to Corruption

94. This section provides an overview regarding the GoA's policy, legislative and institutional frameworks for anticorruption, international commitment, corruption-related surveys, reform activities and development partner support. The information is based on review reports, perception surveys and consultations with stakeholders.

95. Policy documents: The *Armenia Development Strategy (ADS) 2014-2025* includes a separate chapter on anticorruption policy. It provides a general background, lists past achievements in the areas of corruption prevention and criminalization, and outlines planned future steps in general terms. The new Government's Program notes that effectively fighting corruption requires proper implementation of checks and balances, applying the existing legislative and institutional frameworks, and introducing new initiatives. The latter includes establishing a specialized and independent anticorruption body with operative, intelligence, investigative and preliminary investigation functions. Other initiatives include enhanced vetting of high-ranking officials and broader asset declaration procedures, eliminating extra-budgetary funds, penalizing ineffective procurement and wasteful budgetary spending, and introducing more openness as regards the beneficial owners of state-registered legal entities.

96. The Government in April 2014 prepared a concept paper on fighting corruption in the public administration system (Protocol Decision N 14) and in September 2015 adopted the *Anti-Corruption Strategy and Action Plan for 2015-2018* (Decision 1141-N). The strategy outlines the main means of fighting corruption (including related to civil servants, the public administration system, and cooperation with civil society), priority sectors (education, revenue collection, police and health care), and the monitoring and evaluation approach. The GoA prepared regular implementation reports, but these did not include overall assessments of progress and challenges.

97. The Government in December 2018 presented a draft Anti-Corruption Strategy and Action Plan for 2019-2022, which had three main strategic directions are corruption prevention, corruption identification, and anticorruption education. The process of

¹¹⁷ In this it will be important to ensure that preparing PPPs do not risk circumventing public procurement rules.

¹¹⁸ The MoF has recently presented a business intelligence tool, developed with support from the EBRD. It complies with the Open Contracting Data Standard (OCDS) and enables disclosure of data and documents at all stages of the contracting process, and thus helps to ensure transparency and allows for data analysis.

preparing the initial draft was criticized by CSOs/NGOs,¹¹⁹ which led the Ministry of Justice to extend the deadline for submission of comments on the draft. A new and significantly changed draft, that took into account many of the submitted comments, was published in June 2019 and, following discussions with stakeholders, sent to the Prime Minister's Office. It is expected that the Anti-Corruption Strategy and Action Plan will be finalized and published before end-2019.

98. The GoA's official website with documents on anticorruption and information about on-going activities is <https://anti-corruption.gov.am/am/> (only in Armenian).

99. **Legislative framework:** The *Criminal Code* (2003, as amended)¹²⁰ criminalizes the major forms of corrupt activity, including active and passive bribery, attempted corruption, extortion, trading in influence, bribing a foreign official, money laundering, abuse of office in the public sector, and illicit enrichment.¹²¹ The *Criminal Procedure Code* (1998, as amended) outlines the principles of criminal proceedings, including related to immunity. The *Law on Whistle-blowing System* (2017) regulates the protection of whistle-blowers' rights, procedure of whistle-blowing related to corruption cases, conflict of interest and breach of ethics rules, and financial disclosure.¹²² The *Law on Civil Service* (2018) prohibits public employees accepting gifts, money or services for performing a service. The *Law on Public Service* (2018) establishes the Ethics Commission for High-Ranking Officials and requires high-ranking public officials and their families to undertake financial disclosure. The *Law on Commission for Prevention of Corruption* (2017), which is to establish an independent corruption prevention body, is yet to come into force.

100. **International commitments:** Armenia signed the United Nations Convention Against Corruption (UNCAC) in 2005 and ratified it in 2007. OECD carries out regular monitoring¹²³ that uses UNCAC as a benchmark together with other instruments, and covers a number of aspects related to anticorruption policy, criminalization of corruption and law enforcement, and prevention of corruption. The results of the progress assessments undertaken in recent years are shown below:¹²⁴

Table 4 – Progress / Compliance Assessments of UNCAC Implementation

Recommendations	3 rd Round				4 th Round
	Mar. 2015	Oct. 2015	Sept. 2016	Sept. 2017	Sept. 2018
Pillar 1: Anticorruption Policy					
1) Anti-corruption policy	Progress	Progress	Progress	Progress	Partially
2) Surveys	Progress	Progress	Progress	Significant progress	Largely
3) NGO participation and awareness raising	Progress	Progress	Progress	Significant progress	Largely
4) Anti-corruption institutions	Progress	Progress	Progress	Progress	Partially

¹¹⁹ <https://transparency.am/en/news/view/2596>.

¹²⁰ The Government expects to adopt a new Criminal Code and a new Criminal Procedure Code in 2020.

¹²¹ Illicit enrichment was criminalized only with the 2017 amendment to the Criminal Code.

¹²² Following the adoption of the law, an externally-financed project in 2017 developed a business sector whistle-blowing website (<https://bizprotect.am/en>), but it is not yet widely used by the public.

¹²³ OECD in 1998 established the Anti-Corruption Network (ACN) as an outreach program for Eastern European and Central Asian countries. The Istanbul Anti-Corruption Action Plan was launched in 2003 as a peer-review program to support anticorruption reforms in Armenia, Azerbaijan, Georgia, Kazakhstan, Kyrgyzstan, Mongolia, Tajikistan, Ukraine and Uzbekistan through country reviews and follow-up on recommendations to assist UNCAC implementation as well as other international standards and best practices.

¹²⁴ Indications of progress do not mean that all aspects of each recommendation have necessarily been fully complied with.

Recommendations		3 rd Round				4 th Round
		Mar. 2015	Oct. 2015	Sept. 2016	Sept. 2017	Sept. 2018
Pillar 2: Criminalization of Corruption						
5) Criminalization of Corruption		Progress	Progress	Progress	Progress	Partially
6) Immunities		Progress	Progress	Progress	Progress	Fully
7) Bank secrecy and complex financial cases		Progress	Lack of progress	Progress	Progress	Partially
8) Investigation and prosecution of corruption		Lack of progress	Lack of progress	Lack of progress	Lack of progress	Partially
9) Statistics		Lack of progress	Progress	Progress	Progress	Largely
Pillar 3: Prevention of Corruption						
10) Ethics Commission		Progress	Progress	Progress	Significant progress	Fully
11) Ethics commissions in public institutions		Lack of progress	Lack of progress	Progress	Progress	Partially
12) Code of ethics		Progress	Progress	Progress	Progress	Partially
13) Merit-based recruitment		Progress	Progress	Lack of progress	Progress	Largely
14) Conflict of interests		Lack of progress	Lack of progress	Lack of progress	Progress	Fully
15) Whistle-blowing		Lack of progress	Lack of progress	Lack of progress	Significant progress	Largely
16) Ethics training		Progress	Progress	Progress	Progress	Partially
17) Transparency and discretion in public administration		Progress	Progress	Significant progress	Significant progress	Largely
18) Public financial control and audit		Lack of progress	Progress	Progress	Progress	-
19) Public procurement		Progress	Progress	Progress	Progress	Largely
20) Access to information		Progress	Progress	Significant progress	Lack of progress	Partially
21) Political corruption		Lack of progress	Lack of progress	Progress	Progress	-
22) Judiciary		Progress	Progress	Progress	Progress	Largely
23) Business integrity		Lack of progress	Progress	Progress	Progress	Partially
<i>Significant Progress</i>	<i>Fully compliant</i>	0 (-)	0 (-)	2 (9%)	5 (22%)	3 (14%)
<i>Progress</i>	<i>Largely compliant</i>	15 (65%)	17 (74%)	17 (74%)	16 (70%)	8 (38%)
	<i>Partially compliant</i>					10 (48%)
<i>Lack of Progress</i>	<i>Not compliant</i>	8 (35%)	6 (26%)	4 (17%)	2 (8%)	0 (-)
Sum		23 (100%)	23 (100%)	23 (100%)	23 (100%)	21 (100%)

Note: 'Public Financial Control and Audit' and 'Political corruption' are not covered under the 4th monitoring round.

Sources: OECD. 2017. *Istanbul Anti-Corruption Action Plan – Third Round of Monitoring, Armenia – Progress Update*, 13 September, p. 6-7; OECD. 2018. *op.cit.*, p.16.

101. Overall progress in implementing peer review recommendations has improved notably over time. There has in all five years been progress as regards Anticorruption Policy, while for Criminalization of Corruption progress has been somewhat mixed, while for Prevention of Corruption progress mainly took place during 2017-2018. The latter is explicitly seen in the areas of 'conflict of interests' and 'whistle-blowing' where there was no progress during the first three years, and in the area of 'investigation and prosecution of corruption' where there was no progress until mid-2017.

102. In May 2019, the GoA introduced a unified electronic platform for whistle blowing (<https://www.azdararir.am/en>), which allows users to submit reports and data, including by doing so anonymously.

103. Armenia has been a member of the Group of States against Corruption (GRECO), the anticorruption monitoring body of the Council of Europe (CoE), since 2004. Evaluation reports with recommendations are adopted by GRECO and the implementation measures subsequently assessed under a compliance procedure. The fourth evaluation round was launched in 2012 and deals with the prevention of corruption in respect to parliamentarians, judges and prosecutors. The 2017 compliance report on Armenia found that 5 out of 18 recommendations had been implemented satisfactorily, 12 had been partly implemented, and 1 had not been implemented.¹²⁵ Progress was relatively best in the implementation related to prosecutors followed by judges and then members of parliament.¹²⁶

104. Armenia is also a member of the CoE's *Committee of Experts on the Evaluation of Anti-Money Laundering Measures and the Financing of Terrorism (MONEYVAL)*. It carries out monitoring to ensure that countries take steps to meet international standards and follow MONEYVAL recommendations within an appropriate time frame. According to the fifth round evaluation report,¹²⁷ Armenia has a broadly sound legal and institutional framework to combat money laundering. The level of technical compliance is generally high with respect to most recommendations. The biggest threats are considered to be fraud, tax evasion,¹²⁸ theft and embezzlement. However, findings also indicate that corruption and smuggling constitute a threat, and that the real estate sector, the shadow economy and the use of cash constitute significant vulnerabilities.

105. Institutional framework: The Government in February 2015 (Decision N165) established the *Anti-Corruption Council (ACC)*,¹²⁹ which for some years led the process of coordinating anticorruption activities. A *Monitoring Division* was set up as a secretariat¹³⁰ and tasked with monitoring and evaluating implementation of the Anti-Corruption Strategy and Action Plan, which was supported by a three-person *Expert*

¹²⁵ Council of Europe. 2017. *Fourth Evaluation Round, Compliance Report, Armenia*. GRECO, 21 December.

¹²⁶ Regarding prosecutors, the Law on Prosecutor's Office was adopted, steps were taken to enhance recruitment procedures and strengthen the ethics committee of prosecutors, but more measures were needed to introduce dedicated mandatory training and confidential counseling. Regarding judges, constitutional amendments were made that reformed the judicial self-governance with the establishment of the Supreme Judicial Council, the immunities of judges were limited to "functional immunities", and some progress was achieved in terms of procedures for recruitment, promotion, dismissal and transfer of judges with the Supreme Judicial Council given a key role. However, more effort was required in relation to dedicated training and counselling of judges, establish safeguards against the use of disciplinary proceedings to influence or retaliate against judges, and ensure effective rules against undue interference. Regarding members of parliament, there was progress in terms of transparency of the legislative process in Parliament and measures to implement standards on incompatibilities, but more efforts was required to establish a code of conduct and to strengthen the mechanism for monitoring compliance with ethical norms and standards.

¹²⁷ Council of Europe. 2015. *Armenia – Fifth Round Mutual Evaluation Report*. MONEYVAL(2015)34, December.

¹²⁸ As an example, a private firm involved as a borrower in an ADB non-sovereign operation (Spayka LLC) was in July 2018 subject to an investigation by the State Revenue Committee's Investigation Department for non-payment of taxes. The case was based on exports of agricultural products from Armenia to the EEU for which product prices were allegedly under-declared (eventually resulting in under-payment of profit tax amounting to AMD 2.0 billion). The firm in September 2018 filed corrected calculations based on which it ruled not to prosecute the firm. However, the firm's Chief Executive Officer (CEO) was arrested in April 2019 due to new allegations about non-payment of tax. (<http://www.petekamutner.am/mdNews.aspx?sid=ts&nid=5792> and <http://www.petekamutner.am/mdNews.aspx?sid=src&nid=5794>).

¹²⁹ The Anti-Corruption Council is chaired by the Prime Minister and comprises the Deputy Prime Minister; Ministers of Justice, Finance, and Economic Development and Investment; Chief of Staff of the Government; Deputy Prosecutor General; Human Rights Defender; Head of Ethics Commission for High-Ranking Officials; Head of the Presidential Oversight Service; President of the Public Council; and, representatives of the Union of Communities and CSOs as well as of the parliamentary opposition. The seven ACC meetings held during 2015-2017 also included representatives from line ministries, NGOs and development partners. The Anti-Corruption Council was in June 2019 replaced by the Anti-Corruption Policy Council.

¹³⁰ The Monitoring Division is lead by the Deputy Chief of Staff of the Government and has five staff.

Task Force (funded by a USAID grant). However, it is the *Ministry of Justice* that acts as the focal point for international commitments and the related frameworks. The *Commission on Ethics of High-Ranking Officials* maintains a declaration register which it analyses to guard against conflict of interests and violations of ethics rules. The Commission is being replaced by the *Commission for Prevention of Corruption*, which is envisaged as an independent collegial body comprising five members appointed for six-year terms by the National Assembly¹³¹ (as well as a 55-member staff contingent) and has broad preventive powers. The *Special Investigation Service* is an independent state body that conducts preliminary investigation of criminal cases related to officials. The *Investigative Committee*, also, an independent state body, is authorized to undertake preliminary investigations of criminal offenses. The *Prosecutor General's Office (PGO)* presents case in a criminal trial against individuals accused of corruption. The *Financial Monitoring Center* is a separate unit within the Central Bank of Armenia, which acts as an intermediary between reporting entities and law enforcement authorities in combating money laundering. The *Audit Chamber* can, if it finds evidence of illegal activities, forward this to the PGO. A new *State Oversight Service* was set up in May 2018 under the Office of the Prime Minister to oversee implementation of anticorruption programs and measures.

106. The institutional framework for anticorruption is thus somewhat fragmented, which weakens accountability as several entities have overlapping jurisdiction.¹³² The OECD's latest peer-review report notes that the weaknesses of the ACC include political will to tackle corruption through decisive and fundamental reforms.¹³³ Also, the ACC has largely failed to be proactive and meaningfully engage with relevant state bodies to move the anticorruption reform implementation process forward. The OECD notes that the introduction of an independent corruption prevention body would bring Armenia closer to international anticorruption standards. The Government's draft Anticorruption Strategy envisages establishing a new Anticorruption Committee that will concentrate on detection and investigation of all corruption-related crimes.

107. Corruption perception: Corruption in Armenia has traditionally been considered extensive and affecting all sectors of the economy as well as government, including the judiciary, tax and customs operations, and law enforcement. A close relationship between oligarchs, politicians and high-level officials has raised concerns about cronyism and influence.¹³⁴ Also, while gifts and facilitation payments are illegal, the practice of giving and accepting these is widespread. Important parts of the economy are controlled by well-connected businesspeople who, under the previous RPA-led governments, had government-protected market dominance.¹³⁵

108. Transparency International's Corruption Perceptions Index (CPI) ranks countries in terms of the degree to which there is perceived to be corruption among public officials and politicians. The results for recent years are shown below.

Table 5 – Transparency International's CPI Data

Year	No. of Countries	Ranking of Armenia	CPI Score*	Confidence Range	Surveys Used
2012	176	105	34	29-38	6

¹³¹ The appointment of Commissioners was criticized by Transparency International's Anti-Corruption Centre in Armenia, which in January 2019 proposed an "immediate revision of the election of members" stating that it should be done by the newly elected National Assembly [<https://armenpress.am/eng/news/962022.html>].

¹³² European Union Delegation. 2018. op.cit., p. 107.

¹³³ OECD. 2018. op.cit., p. 35.

¹³⁴ GAN Business Portal. 2016. *Armenia Corruption Report*, July.

¹³⁵ United States Department of State. 2017. *Armenia, Investment Climate Statements for 2017*.

Year	No. of Countries	Ranking of Armenia	CPI Score*	Confidence Range	Surveys Used
2013	177	94	36	30-42	6
2014	175	94	37	31-43	6
2015	168	95	35	30-40	5
2016	176	113	33	26-40	6
2017	180	107	35	29-41	6
2018	180	105	35	28-42	6

* The CPI score is: 100: highly clean, 0: highly corrupt.

Source: <http://www.transparency.org/>.

109. The CPI indicates that corruption among public officials and politicians has been perceived as very high and virtually unchanged from 2012 to 2018.

110. Some other international governance surveys, e.g. the World Bank Institute's Worldwide Governance Indicators, likewise find that control of corruption has been unchanged in recent years (see Annex D). However, the World Economic Forum's Global Competitive Reports, which up to 2014/15 found corruption to be the most problematic factor for doing business in Armenia, has since 2015/16 noted other factors to be more problematic (such as access to financing, inefficient government bureaucracy, tax rates and tax regulations). Also, according to a recent national survey, the biggest success of the present government is decreased corruption, 63% of respondents view the fight against corruption as having progressed in the past six months, and 59% see the government as making enough effort to fight corruption.¹³⁶

111. High-level corruption and the names of alleged perpetrators are being discussed openly in the Armenian media, and several senior politicians and bureaucrats have been arrested on corruption charges. However, there were over the years under the previous RPA-led governments few convictions (and many senior figures were not prosecuted in the first place), which often led the general public to view anticorruption activities as token gestures. The PGO in March 2019 reported that a total of 960 persons were prosecuted during 2018 on corruption-related criminal cases of which 470 were public officials.¹³⁷

112. Development partner support: Many development partner activities in the broader governance area include anticorruption aspects. The development partners providing support for specific anticorruption initiatives are the EU (capacity building of civil society, media and youth as well as public sector institutions) and USAID (implementation of the Anti-Corruption Strategy in priority sectors and establishing a civil society consortium to mobilize citizens in public oversight).

113. The Anti-Corruption Policy Council is charge with donor coordination on anticorruption issues, although the GoA and development partners also discuss and coordinate anticorruption issues through thematic groups as well as bilaterally on an ad hoc-basis.

¹³⁶ Center for Insights in Survey Research. 2019. *Public Opinion Survey: Residents of Armenia*. 6-31 May.

¹³⁷ <http://www.prosecutor.am/en/mn/7385/>.

V. USE OF COUNTRY SYSTEMS

114. The use of country PFM and procurement systems by development partners can decrease transaction costs, improve alignment with country priorities, strengthen government ownership, and help to strengthen national capacities. In planning and implementing operations, ADB should therefore consider the widest possible use of country systems, taking into account practical aspects as well as fiduciary risks.

115. ADB's current project portfolio in Armenia is provided in Annex C for the 2019 assistance program. It shows that ADB is implementing a total of 21 programs and projects with total ADB financing of \$854 million (over the full lifetime of the programs and projects). The portfolio covers several sectors – with road transport, energy and urban transport being the main sectors (together amounting to 79% of total financing) – and consists of 15 loans (some of which are equity investments) and 14 TA projects.¹³⁸ 99.4% of the ADB financing is for loans and 0.6% for TA.¹³⁹

116. TA projects are managed using ADB procedures for financial management and procurement, and hence do not use partner country systems. ADB's loan projects in Armenia generally apply country systems as follows:

- **Budgeting** – The GoA includes loan and grant information for each development partner-financed program/project in the annual State Budget¹⁴⁰ and in the MTEF document on a three-year rolling basis.¹⁴¹ *ADB funding is thus 'on budget'.*
- **Treasury functions** – Loan proceeds are disbursed in accordance with ADB's Loan Disbursement Handbook and as agreed between ADB and the Government. Larger payments to contractors and suppliers (usually above \$50,000 or \$100,000) are made directly by ADB, which ADB considers to be use of the country system.¹⁴² The commitment procedure is used for some operations. The advance fund procedure is used for smaller payments. The advance account is established at a commercial bank by the MoF and managed by a Project Implementation Unit (PIU). ADB's statement of expenditure (SOE) method is used for reimbursement of eligible expenditures and liquidation of advances to the advance account. *ADB funding is thus partially 'on treasury'.*
- **Accounting and reporting** – ADB requires that separate program/project accounts and records are maintained by funding source for all expenditures incurred, and that accounting is based on international principles and practices. Financial statements must be prepared in accordance with international financial reporting standards. *ADB funding is thus not 'on accounting' and not 'on reporting'.*
- **Procurement** – For ADB operations, ADB requires that all procurement types (including for works, goods and services) and methods (ICB, NCB, shopping and

¹³⁸ This sums to a total of 29 activities since some operations include both loan and TA.

¹³⁹ Armenia has since January 2017 been classified as a Group C country. This means it has access to borrow from ordinary capital resources (OCR) at near-market terms, but not at concessional OCR loan terms, or to receive grants from the Asian Development Fund (ADF).

¹⁴⁰ In the 2018 State Budget document, Annex 1, Table 15 'On 2018 indicators of grant programs implemented with the support of foreign states and international organizations', and Annex 4, Table 2, 'Funds allocated to provide loans within the framework of loan programs implemented with the support of foreign states and international organizations'. Both are presented by economic classification of expenditure. The annual GoA state budget documents are available on: <http://www.gov.am/am/budget/> (in Armenian only).

¹⁴¹ In the 2017-2019 MTEF document, Annex 2, Table 2 'Funds allocated to provide loans within the framework of loan programs implemented with the support of foreign states and international organizations ...' and Annex 2, Table 3 'Funds allocated to provide loans within the framework of grant programs implemented with the support of foreign states and international organizations ...'. The GoA's MTEF documents are available on: <http://www.gov.am/am/medium-term/> (in Armenian only).

¹⁴² ADB views direct payments to contractors and consultants as consistent with commercial banking practices and hence not a departure from country systems [ADB. 2014. op.cit., p. 15].

direct contracting) to be undertaken in accordance with ADB's procurement guidelines. *ADB funding is thus not 'on procurement'*.

- **External audit** – ADB requires that the EA must ensure that program/project financial statements are audited in accordance with International Standards on Auditing by an independent auditor acceptable to ADB. The audited financial statements, together with a management letter and the auditor's opinion, must be submitted to ADB within six months from year-end. ADB generally also requires audit assurances on financial covenant compliance and that funds have been used for the purposes intended, which ADB considers to be within the use of the country system.¹⁴³ The financial statements are audited by private firms engaged under the programs/projects and funded from loan proceeds. The Audit Chamber is currently not involved in the external audit process. *ADB funding is thus not 'on audit'*.

117. ADB's use of country systems for loan operations in Armenia is thus overall 'partial'.¹⁴⁴ ADB could, in principle, expand the use of country systems in four areas: 1) treasury functions (by channeling funds through the GoA's treasury systems); 2) accounting and reporting (by applying GoA systems and procedures); 3) procurement (by allowing GoA entities to undertake procurement based on the PPL and/or using the government's e-procurement systems for (selected) procurement types and methods); and, 4) external audit (by having the Audit Chamber carry out project audits). However, in practice – i.e. taking into account existing weaknesses and related fiduciary risks – ADB is using the GoA's PFM and procurement systems to the fullest extent possible.

118. Given recent improvements of the government accounting standards, it could be relevant in future to consider expanding the use of country systems for program/project implementation as well as for financial reporting. Similarly, for the procurement area where the new legislative and regulatory frameworks as well as changes to the e-procurement system may warrant in new ADB operations using the country procurement system for shopping and NCB (although a decision as regards procurement, of course, should be based on the findings and recommendations of the forthcoming Procurement Risk Assessment).

119. There have recently been discussions within Government about *mainstreaming PIUs into government entities*, although the exact approach remains to be formulated. Considering the existing (low) capacity of ministries and agencies, their (lack of) experience with development partner requirements and procedures, and the vulnerabilities and risks related to using GoA systems and procedures, it would not appear feasible that the implementation of development partner-financed projects can be managed by "ordinary" GoA entities in the near future. Hence even if a structural reorganization is undertaken, the GoA would likely need to maintain dedicated units for managing implementation of external-funded projects.

¹⁴³ ADB considers the request for audit assurances on financial covenant compliance and that funds usage to be consistent with commercial banking practices, i.e. it is not considered a departure from the use of country audit systems [ADB. 2014. op.cit., p. 14.].

¹⁴⁴ This is similar to the findings of the Global Partnership for Effective Development Co-operation, which tracks country-level progress in implementing internationally-agreed development co-operation principles. For 2016, it assessed the use of Armenian country systems as follows: Budget 79%, financial reporting 54%, auditing 50% and procurement 40% [Global Partnership for Effective Development Co-operation. 2016. *Monitoring Profile – October 2016, Armenia*, p. 3].

VI. SUMMARY OF GOVERNANCE RISKS

120. The main governance risks for PFM, public procurement and corruption are summarized below.

Table 6 – Summary Governance Risk Matrix

Weakness	Risk	Likely	Relatively Serious	Not Mitigated Over CPS Period	High Risk
Public Financial Management (PFM)					
Sector strategies are not fully costed, and the recurrent cost implications of major capital projects are not estimated and included in the budgets.	There may be insufficient budgetary resources to implement capital projects, and adequate maintenance during operation may not be provided for.	✓	✓		
Due to PIM weaknesses, the GoA has had challenges in ensuring adequate funding and implementation of some development partner-financed projects.	Programs and projects that do not receive sufficient funding cannot be properly implemented in line with agreed investment and procurement plans.	✓	✓	✓	✓
Fiscal risk management functions are generally still weak in capacity and with limited role in vetting and mitigation functions.	Fiscal shocks affect risk premiums and fiscal credibility in general, and budget implementation efforts in particular.		✓		
The codification of the PPP policy framework is still incomplete as secondary legislation (on appraisal methodologies, fiscal risk management and reporting regulations) remains to be developed. Also, capacity to manage a full operational framework is still emerging.	PPPs pose significant fiscal risks to the GoA. The current PPP capital stock of 10% of GDP is weakly understood and managed, and there is pressure for new PPPs to be planned.		✓		
The GoA's annual consolidated financial statements are incomplete and thus not auditable.	Funds may not be properly accounted for and may not be used for the intended purposes.	✓	✓		
The internal audit functions in line ministries lack capacity.	Lack of management oversight in the functioning and effectiveness of entity-level PFM systems and processes.	✓	✓	✓	✓
There are weaknesses in payroll controls as the linkages between staff lists, other personnel records and payroll are manual and reconciliations are not carried out.	Funds may not be used for their intended purpose or not properly accounted for, due to leakages caused by ineffective payroll controls.	✓	✓	✓	✓
The existing PFM IT system has a number of weaknesses, and the design for a new system is yet to be decided and prepared.	Financial reporting may not be timely and sufficiently accurate, and accounting and internal controls may not be fully adequate, which creates fiduciary risks.	✓			

Weakness	Risk	Likely	Relatively Serious	Not Mitigated Over CPS Period	High Risk
The Audit Chamber's financial autonomy as well as its ability to appoint and terminate staff is not consistent with international standards on the independence of SAIs.	The lack of independence may impact adversely on the organizationally functioning of the Audit Chamber.	✓		✓	
The external audit functions are not yet fully based on international standards, and the capacity of staff is characterized by some shortcomings.	Funds may not be used effectively and efficiently due to limited staff accountability and lack of proper assessment caused by weak external audit function.	✓	✓	✓	✓
Procurement					
The legal and regulatory framework does not require all procuring entities to use the e-procurement system.	Some procurement processes remain manual and paper-based which is less efficient.	✓		✓	
The PPL in some cases allows for procuring entities to launch tenders without prior securing of funds.	Uncertainty about funding availability and payments may result in some firms refraining from bidding, which may adversely affect competition.		✓	✓	
The PPL states that MoF may not be directly involved in the procurement process, but at the same time requires MoF to register all signed contracts (and it can recommend contracts to be amended or cancelled).	The role of the MoF in relation to line ministry contracts is unclear.	✓		✓	
Procurement plans are frequently prepared using an outdated cost methodology for goods, works and services.	Inaccurate cost estimates reduce the usefulness of procurement plans and can result in inefficient procurement processes (e.g. necessitating contract variations) as well as implementation delays.	✓	✓	✓	✓
The procurement capacity building program, which is formulated and coordinated by the MoF, is inadequate to meet the training needs of all stakeholders, including the private sector and civil society.	Stakeholders may not receive the support and develop their technical skills as required given their roles and responsibilities in the procurement process.	✓	✓	✓	✓
There is no structured approach to capacity building for e-procurement, so some procuring entities may not be able to use the e-procurement system.	Lack of access to the e-procurement system may result in poor value-for-money.	✓	✓		
The Armenian private sector is not fully able to meet all GoA requirements	Without a well-organized and -functioning private sector, government cannot	✓	✓	✓	✓

Weakness	Risk	Likely	Relatively Serious	Not Mitigated Over CPS Period	High Risk
for goods, works and services.	achieve value-for-money in its procurement.				
The amended PPL does not provide for an independent review mechanism.	Higher project costs due to few bid submissions caused by the lack of trust in the functioning of the public procurement system.	✓	✓	✓	✓
Some procurement information is not available in English language, which may reduce the number of international bidders.	Fewer bidders reduce competition and may ultimately result in poor value-for-money.	✓		✓	
Many civil works projects supported by development partners are characterized by slow implementation progress, long land acquisition processes, and low contractor performance.	Implementation of civil works projects may be subject to quality issues as well as cost and time overruns.	✓	✓		
Corruption					
The draft 'Anti-Corruption Strategy and Action Plan 2019-2022' is yet to be finalized and formally approved by Government.	The lack of an updated and implementable strategic plan means that appropriate actions may take time to identify and execute.	✓	✓		
The institutional framework for fighting corruption is somewhat fragmented, and one of two new entities is yet to become operational.	The lack of institutional clarity combined with overlapping jurisdiction weakens the accountability of the involved entities.	✓	✓		
Law enforcement and prosecutorial entities have insufficient specialization in anticorruption, and lack a proactive and targeted approach aimed at high-level officials and the main risk areas of the economy and public administration.	A lack of specialist capacity hinders the detection, investigation and prosecution of complex corruption cases.	✓	✓	✓	✓
Significant parts of the economy are controlled by well-connected businesspeople who, until recently, have had government-protected market dominance.	Misuse of funds due to cronyism, influence peddling, and other corrupt practices.	✓	✓	✓	✓
While a significant part of the population view corruption as one of the biggest problems facing the country, and despite gifts and facilitation payments being illegal, the practice of giving and accepting gifts remains widespread.	Passive acceptance of corruption and participation in (low-level) bribery further erodes trust in public institutions and undermines attempts to carry out awareness raising initiatives.	✓	✓	✓	✓

GDP = gross domestic product, GoA = Government of Armenia, IT = information technology, MoF = Ministry of Finance, PFM = public financial management, PIM = Public investment management, PPL = Public Procurement Law, PPP = Public-private partnership, SAI = Supreme Audit Institution.

VII. RISK MANAGEMENT PLAN

121. As mentioned in Chapter V, ADB is only to some extent using the country systems for PFM and procurement. Expanding the use would potentially expose ADB funds to additional fiduciary risks related to the weaknesses identified in Chapter VI as regards the PFM and procurement systems as well as related to corruption vulnerabilities. Mitigation measures will therefore be necessary to address risks. The table below provides proposals for mitigation measures and indicators for high risks.

Table 7 – Risk Management Plan

Weakness	High Risk	Mitigation Action	Indicators
Public Financial Management (PFM)			
Due to PIM weaknesses, the GoA has had challenges in ensuring adequate funding and implementation of some development partner-financed projects.	Programs and projects that do not receive sufficient funding cannot be properly implemented in line with agreed investment and procurement plans.	ADB will discuss with the GoA possibilities for ensuring that funding is being provided for loan operations in line with agreements.	Adequate funding is being allocated in the annual state budget.
The internal audit functions in line ministries lack capacity.	Lack of management oversight in the functioning and effectiveness of entity-level PFM systems and processes.	ADB will encourage government entities which are operational counterparts (EAs and IAs) to strengthen their internal audit unit.	Proposal to strengthen internal audit units included in relevant program/project documentation.
There are weaknesses in payroll controls as the linkages between staff lists, other personnel records and payroll are manual and reconciliations are not carried out.	Funds may not be used for their intended purpose or not properly accounted for, due to leakages caused by ineffective payroll controls.	ADB will encourage government entities that are operational program/project counterparts to strengthen their payroll controls.	Proposals to strengthen payroll controls are included in relevant program/project documentation.
The external audit functions are not yet fully based on international standards, and the capacity of staff is characterized by some shortcomings.	Funds may not be used effectively and efficiently due to limited staff accountability and lack of proper assessment caused by weak external audit function.	ADB will encourage the Audit Chamber and the MoF to ensure that developing the external audit methodology and staff capacity is included in an updated PFM reform plan.	Updated PFM Strategy and Action Plan.
Procurement			
Procurement plans are frequently prepared using an outdated cost methodology for goods, works and services.	Inaccurate cost estimates reduce the usefulness of procurement plans and can result in inefficient procurement processes (e.g. necessitating contract variations) as well as implementation delays.	ADB will encourage the GoA to supplement the e-procurement system with a new 'unit price data base' module that will help procuring entities to prepare more accurate cost estimates.	New 'unit price data base' module implemented for the e-procurement system.
The procurement capacity building program, which is formulated and coordinated by the MoF, is inadequate to meet the	Stakeholders may not receive the support and develop their technical skills as required given their roles and responsibilities in the	ADB will discuss with the GoA how support may be provided for developing procurement training, including by assigning	Procurement capacity building activities strengthened.

Weakness	High Risk	Mitigation Action	Indicators
training needs of all stakeholders, including the private sector and civil society.	procurement process.	training functions to the Public Administration Academy.	
The Armenian private sector is not fully able to meet all GoA requirements for goods, works and services.	Without a well-organized and -functioning private sector, government cannot achieve value-for-money in its procurement.	ADB will support the GoA's efforts in carrying out programs for supporting domestic private sector growth.	The number of domestic firms bidding for GoA contracts increased.
The amended PPL does not provide for an independent review mechanism.	Higher project costs due to few bid submissions caused by the lack of trust in the functioning of the public procurement system.	ADB will encourage the GoA to establish an independent review mechanism with an appropriate legal status.	Independent review mechanism set up.
Corruption			
Law enforcement and prosecutorial entities have insufficient specialization in anticorruption, and lack a proactive and targeted approach aimed at high-level officials and the main risk areas of the economy and public administration.	A lack of specialist capacity hinders the detection, investigation and prosecution of complex corruption cases.	ADB will support the GoA in preparing a diagnostic to assess the activities and capacity of relevant entities, and make recommendations for a proactive anticorruption approach.	Updated Anticorruption Strategy and Action Plan.
Significant parts of the economy are controlled by well-connected businesspeople who, until recently, have had government-protected market dominance.	Misuse of funds due to cronyism, influence peddling, and other corrupt practices.	ADB will together with other development partners hold policy dialogues with the GoA to identify possibilities for de-monopolizing the economy and enabling separation of business and politics.	Policy note prepared by the GoA for discussion with internal and external stakeholders.
While a significant part of the population view corruption as one of the biggest problems facing the country, and despite gifts and facilitation payments being illegal, the practice of giving and accepting gifts remains widespread.	Passive acceptance of corruption and participation in (low-level) bribery further erodes trust in public institutions and undermines attempts to carry out awareness raising initiatives.	ADB will encourage the GoA together with civil society and private sector representatives to devise and implement public awareness campaigns aimed at shifting public behavior away from accepting corruption.	Joint proposal prepared and agreed among stakeholders.

ADB = Asian Development Bank, EA = executing agency, GDP = gross domestic product, GoA = Government of Armenia, IA = implementing agency, MoF = Ministry of Finance, PFM = public financial management, PIM = Public investment management.

VIII. BRIEF SECTOR ASSESSMENTS

122. This chapter provides very preliminary overviews of governance issues in three ADB priority sectors – road transport, urban transport, urban infrastructure, and education – prepared based on existing assessments and information obtained during the in-country mission.¹⁴⁵ Due to differences in focus as well as regarding the availability of information, the length and content of the four sections differ somewhat.

Road Transport Sector

123. Armenia's road transport sector plays an important role in the national economy. The road network is 7,575 km long and comprises 1,803 km interstate roads, 1,966 km republican roads, and 3,806 km local roads.¹⁴⁶ About three-quarters of interstate roads were in 2010 estimated to be in good to fair condition, while about 60% of local roads were deemed in need of rehabilitation.¹⁴⁷ However, in 2018 only about 15% of interstate and republic roads are deemed to be in good condition,¹⁴⁸ which is due to lack of quality control during construction and inadequate maintenance. Other issues include insufficient financing for maintenance; outdated road design, maintenance standards, and technical specifications; and lack of qualified workers, contractors, and consulting firms. The overall network capacity is considered adequate to accommodate the estimated traffic volumes up to 2020.

124. Armenia overall faces three main transport constraints:¹⁴⁹ (i) the legacy of a transport network that was designed to serve a centrally planned economy; (ii) being landlocked and disadvantaged by a difficult topography and a severe continental climate; and, (iii) prevailing geopolitical problems, which remain a source of instability and have severed important transportation routes (closed borders with Turkey and Azerbaijan). These constraints cause high transport cost as well as costly implementation, maintenance, and operation of transport infrastructure, which impede Armenia's external trade and competitiveness.

125. The major challenges for the road transport sector are:¹⁵⁰ (i) to maintain the capacity and efficiency of the international road corridors; and, (ii) to ensure reasonable service levels of the republican and local roads. This requires modernizing road design and maintenance standards as well as technical specifications, improving collection of road and traffic data, and developing cost-effective technical solutions for low-volume roads. Also, road safety needs to be enhanced through improvements in institutional coordination, traffic safety audits, road designs, and other measures.

126. The *Ministry of Transport, Communication and Information Technologies (MoTCI)*¹⁵¹ is the principal government entity in charge of the transport sector. It administers interstate roads and about half of republican roads. Road administration functions, including road maintenance and data collection, are delegated to the *Armenian Road Directorate (ARD)*,¹⁵² is a SNCO, through annual contracts. *Regional administrations and local communities* manage the remainder of republican roads and

¹⁴⁵ As per ADB's GACAP II Staff Guidance, there is no requirement to undertake sector assessments in preparing the country-level GRA, but such assessments can provide useful inputs.

¹⁴⁶ Statistical Committee of the Republic of Armenia. 2018. *Statistical Yearbook of Armenia 2018* [Transport and Communication – <https://www.armstat.am/file/doc/99510808.pdf>].

¹⁴⁷ ADB. 2014d. *Sector Assessment (Summary): Transport*. Country Partnership Strategy: Armenia, 2014-2018, p. 1.

¹⁴⁸ ADB. 2018a. op.cit., p. 10.

¹⁴⁹ Ibid.

¹⁵⁰ ADB. 2014d. op.cit., p. 1.

¹⁵¹ According to the proposed changes to the 'Law on Government Structure', the transport function will be transferred to the new Ministry of Territorial Development and Infrastructure.

¹⁵² Based on Government decision dated 29 March 2019, the functions of the ARD are to be transferred to a new structural unit of the Ministry of Territorial Development and Infrastructure.

all local roads. Private companies provide road maintenance services under five-year contracts with the ARD, regional administrations and local communities. The *Transport Project Implementation Organization (TPIO)*,¹⁵³ a SNCO, implements transport initiatives, including the 'North-South Road Corridor Investment Program' and the 'Armenia-Georgia Border Regional Road (M6 Vanadzor-Bagratashen) Improvement Project'.¹⁵⁴ While this institutional set-up as such is rational, it is likely a contributing factor to the disconnect between road construction (TPIO) and road maintenance (ARD), which is reflected in imbalanced budgetary allocations between the two areas.

127. There has over time been considerable turnover among the TPIO's staff, especially at the senior management-level. A reported nine individuals have held the position of General Director/Acting General Director from 2010 to 2019, and there has likewise been high turnover among heads of department and other staff. The director-level changes have generally followed the appointment of a new Minister of Transport (of which there have been five between 2010 and 2019). The high staff turnover has adversely affected the functioning and performance of the TPIO, and has often delayed in decision-making, as new managers inadvertently have required time to familiarize themselves with the tasks and challenges of the road construction projects. It does not appear that ADB has raised the issue of the TPIO's staff turnover with the MoTCI.

128. The *Armenia Development Strategy (ADS) 2014-2025* includes a section on the transport sector, which outlines the need to increase the allocation and effectiveness of public resources for maintenance of roads as well as to strengthen program budgeting in the sector and implement modern management systems.¹⁵⁵ Specific program targets for 2017 include that public investments in the road system should reach 1.1% of GDP (up from 0.49% in 2014) and that 50% of roads should be in satisfactory condition. It is not clear to which extent the fulfillment of these targets has been monitored. Armenia also has in place a *National Road Safety Strategy*.

129. ADB is a lead development partner in the road transport sector. A multitranche financing facility (MFF) was approved in 2009 for the *North-South Road Corridor (NSRC) Investment Program* amounting to \$500 million. Tranche 1 (\$60 million) covers the Yerevan-Ashtarak and Yerevan-Artashat road sections, which opened in 2016. Tranche 2 (\$170 million) covers reconstruction and widening of the Ashtarak-Talin road, which is on-going. Tranche 3 (\$100 million) covers reconstruction of the Ashtarak-Gyumri road, which is also on-going.¹⁵⁶ It furthermore includes preparation and implementation of a road sub-sector plan, road asset management and road maintenance administration system, preparation of feasibility study for the Artashat-Qajaran section, and preparation of a subsequent tranche, including preparation of the feasibility study and detailed engineering design. The *M6 Vanadzor-Bagratashen Improvement Project* was approved in 2016 for \$50 million and is on-going.¹⁵⁷ The project also includes activities to strengthen the institutional capacity of the MoTCI. Other development partners in the sector include the European Investment Bank (EIB), EDB and the World Bank.

¹⁵³ The TPIO was established in March 2017 with the merger of the 'Transport Projects Implementation Unit' and the 'North-South Road Corridor Investment Program' SNCOs.

¹⁵⁴ The TPIO also manages the World Bank-funded 'Lifeline Road Network Improvement Project' and the EBRD-funded 'Bagratashen Border Supervision Crossing Point New Bridge Construction Project'.

¹⁵⁵ This includes to 1) develop systems for unified planning of operating and capital expenses in road building programs; 2) develop and implement a methodology for determining priorities in road building programs as a basis for medium-term expenditure planning and budget decision-making; 3) improve the system for outcome planning and performance indicators; 4) develop mechanisms for evaluation of road maintenance services; and, 5) develop alternative approaches to financing of sector and investment programs.

¹⁵⁶ Tranche 3 is co-financed by the EIB for the Lanjik to Gyumri section.

¹⁵⁷ The project is co-financed by the EIB.

130. The implementation of the NSRC *Tranche 1* started in February 2010 and experienced significant delays as well as technical issues, including related to the Government's decision to use cement concrete rather than asphalt concrete,¹⁵⁸ which led to the original loan closing date being extended from June 2014 to June 2017 (the work was completed in June 2016). However, the contractor is still in the process of finishing outstanding works, and the TPIO has therefore extended the defects notification period to enable this. There is furthermore disagreement between the contractor and the employer (MoTCI) as regards additional defects of concrete pavement that have occurred since handover (in December 2015) as well as related payment issues, which remain to be resolved. For *Tranche 2*, which started in July 2011, the loan closing date was extended from June 2015 to September 2019. This was initially due to the government's land acquisition and resettlement (LAR) processes taking considerably longer than initially expected,¹⁵⁹ but also as the international contractor in July 2016 came under bankruptcy protection which led to cash flow problems that were only resolved in August 2017 (when an escrow account was set up for the program). Furthermore, technical and quality issues arose during implementation that the supervision engineer did not respond to in a timely manner, which resulted in parts of the roads having to be rectified.¹⁶⁰ Given continued slow civil works progress, it appears likely that the loan closing date will need to be extended beyond September 2019 (which would then also necessitate extension of the MFF). *Tranche 3* started in July 2014 and originally had a planned loan closing date of June 2017, which has so far been extended till September 2019. Due to severe shortcomings during the first years of implementation, including very slow work progress and major concerns with quality controls, the MoTCI considered suspending works or terminating the contract with the contractor (as well as the supervising engineer). However, following a long period of consultations with stakeholders, a number of mitigation measures were agreed and the implementation process has since then improved somewhat. The *M6 project* started in April 2017 and has a planned closing date of May 2021. There have been some issues with regard to the quality of tender-related documentation, but all contracts were eventually awarded and civil works commenced in May 2018.

131. The Armenian local media has for the past several years seen numerous news reports discussing the implementation delays and quality issues of the NSRC, and alleging corruption being a major cause. It would seem that this to some extent has been the result of misunderstandings and lack of information. It thus appears to be commonly believed that the whole NSRC was originally planned to be built based on the MFF budget of \$500 million and that that amount was provided as a loan directly to the government in 2009 (when ADB approved the MFF). The fact is that the NSRC feasibility study estimated the costs at about \$1 billion,¹⁶¹ MFF funds are only available for implementation once loan agreements for individual tranches are signed (the MFF being a financing framework rather than a loan), and most payments from the loans are made by ADB directly to the contractors (i.e. the GoA and the TPIO do not manage the

¹⁵⁸ Following a construction boom that ended in 2008, Armenia had surplus cement capacity from two local plants and, using cement, would furthermore reduce dependence on imported bitumen and prefabricated concrete elements. However, local firms involved as subcontractors did not have experience using cement concrete for road construction, given that roads in Armenia had traditionally been built with asphalt concrete, and – also – paving with cement concrete costs far more than with asphalt concrete. The switch to cement concrete was a Government decision made without a technical assessment [ADB. 2019. *Armenia: Validation of the Country Partnership Strategy Final Review, 2014-2018*, Draft, March, p. 25].

¹⁵⁹ This was because it was the first time the government applied ADB procedures for LAR, the national legislation changed during the period, cadastre data was weak, and land acquisition did not include the relocation of utilities. In contrast, *Tranche 1* had in part been selected due to the absence of LAR issues.

¹⁶⁰ During the implementation of the NSRC, there are understood to have been examples of the Employer (i.e. government) on occasions having circumvented the Supervision Engineer in directing the Contractor, which thus removed a layer of checks and balances, which made the government vulnerable to contractual liabilities.

¹⁶¹ The present estimate is \$3.5 billion..

funds). However, considering that constructing the NSRC is Armenia's largest infrastructure project and given the many significant problems that have occurred (including time delays and quality issues), it is – taking into account the governance context of Armenia – not difficult to understand why corruption has been perceived as causing the implementation problems.

132. Given the press coverage, it is clear that corruption allegations carry significant reputational risk for ADB. ADB has therefore earlier reached out to NGOs to inform about the NSRC program as well as about ADB procurement requirements and financial management procedures, and there have also been news articles based on interviews with ADB staff. However, these initiatives do not appear to have had much impact on public perception as regards the NSRC program. This is likely due to the audience and communication form rather than the actual information provided. What thus seems required to provide the Armenian public with a fact-based understanding of the program, the responsibilities of the government and ADB's role, is a public relations campaign that can deliver key messages to a defined target audience through appropriate means. ADB could thus consider engaging a consulting agency to help prepare and implement a public relations strategy and measure its effectiveness.

133. The implementation problems of the NSRC program raise questions about the applied tender procedures, which follow ADB procurement guidelines, and contract management as carried out by the TPIO. One issue is that the bid evaluation process does not take into account previous contractor performance, which can potentially lead to firms (that meet the general requirements and have secured the minimum qualifying technical score) being awarded a contract (if proposing the lowest price)¹⁶² despite lacking a good performance record.¹⁶³ Given ADB's procurement guidelines, there are limited possibilities for managing such situations. Another issue is that ADB's procurement guidelines do not impose any limit for subcontracting from the contractor (which, in large civil work projects, often is an international firm) to subcontractors (typically local firms)¹⁶⁴ and, also, subcontracting is not subject to approval or oversight by the borrower.¹⁶⁵ In a local market where many firms are controlled by well-connected businesspeople, some of whom also hold political office, this could potentially lead to main contractors having limited choice when seeking a local partner and/or the tender process being sought influenced to ensure a particular outcome.¹⁶⁶ In

¹⁶² While, under ADB's 2017 Procurement Regulations, a bid that is considered abnormally low (and thus raises concerns about the capability of the bidder to perform the contract for the offered bid price) under specific circumstances can be rejected, this does not apply to ADB-financed projects discussed here since they were approved before 1 July 2017.

¹⁶³ Poor contractor performance can presently only be considered during contract negotiation or project management (although ADB does also carry out a check of past performance as part of due diligence checks).

¹⁶⁴ The following subcontracting restrictions and requirements exist for procurement using ADB guidelines: Works – If domestic preference is provided for, then domestic contractor may not subcontract more than 50% of the total value of their work to foreign subcontractors. Small works – If domestic preference is provided for, then domestic contractor may not subcontract more than 50% of the total value of their work to foreign subcontractors. Also, a contractor may subcontract only with the approval of the Project Manager. Plants – Bids must include a list of proposed subcontractors. A 'List of Approved Subcontractors' is included in the contract agreement. If no subcontractors are listed, then the contractor must prepare such a list (if relevant). Goods – A supplier must notify the Purchaser in writing of all subcontracts awarded under the contract if not already specified in the bid. IT Products and Services – The Supplier must notify the Purchaser in writing of all subcontracts awarded under the Contract, if not already specified in the Bid.

However, limits on subcontracting can nevertheless be established, including for works, when stated in the 'Particular Conditions of Contract' of bidding documents. For the NSRC tranches 1-3, the limit was set as "no more than 50% of the works in terms of value, including the work subcontracted to nominated subcontractors".

¹⁶⁵ This refers to subcontractors that are not included as a 'nominated subcontractor' in the bid. While a contractor would typically already at the bid preparation stage agree collaboration with one or more potential subcontractors, this would be formalized only after contract award and would then be covered by the conditions of the contract between the borrower and the contractor.

¹⁶⁶ Anecdotal evidence indicates that, in Armenia, some subcontractors were connected with implementing entities and staff in decision-making positions, and that bidders sometimes were "directed" towards certain

order to avoid this, strict adherence to bid evaluation requirements is required and is, in a wider perspective, best mitigated where there is transparency in the beneficial ownership of firms (which the new Government has stated as a priority to address).

134. In September 2018, the PGO initiated a criminal case of suspected financial misconduct in relation to the North-South Road Program.¹⁶⁷ The charges include that officials during 2009-2018 have regularly accepted design and cost estimate documentation despite obvious shortcomings, that contracts have been unnecessarily modified by incorporating ineffective and unjustified activities, that extended deadlines of construction and advisory services have been unreasonably agreed without charging for damages, and that advisory services contract prices have been increased by defining service fees exceeding twice the maximum legal thresholds. As a result – according to the Investigative Committee’s press release – firms were paid more than the contractual amounts initially agreed, measures to maintain quality standards and norms for materials (particularly cement composition) and regarding work implementation were not taken, and the NSRC Investment Program Tranche 1 segments were thus accepted and put into operation despite obvious shortcomings. A press release from December 2018¹⁶⁸ stated that charges have been “pressed against” the Team Leader of the Supervision Consultant (Engineer) of Tranche 1¹⁶⁹ for “swindling” for more than \$1.8 million related to supervising compliance with qualitative and volume aspects of the construction work (it is alleged that agreement had been reached with employees of the contractor and the MoTCl to issue false payment certificates).¹⁷⁰ According to news report from August 2019, the allegation has been extended to the contractor’s program director.¹⁷¹ Further information regarding the outcome of the investigation is not yet available.

Urban Transport Sector

135. Armenia has a relatively small population (2.97 million), but is the most urbanized country in the Caucasus. 1.9 million (64%) live in urban areas, and Yerevan alone accounts for 1.1 million (36%).¹⁷² While the total population over the past five years has declined by 1.5%, the number of people living in Yerevan has increased by 0.9%.¹⁷³ Unbalanced economic growth between different parts of the country poses development challenges to urban planners and policy makers. Shifts in the location of commercial and residential centers have led to changes in the demand for transport services, which has increased motorization. Vehicle ownership has grown significantly in recent years, with the number of insured cars increasing from 407,444 in 2013 to 497,881 in 2017 (i.e. 22%),¹⁷⁴ while the number of accidents grew from 2,824 in 2013 to 3,535 in 2017 (i.e. 25%),¹⁷⁵ which has increased the focus on road safety.

subcontractors. Another challenge under the previous government was that some subcontractors seemed able to exercise political leverage over international contractors.

¹⁶⁷ <http://www.investigative.am/en/news/view/charashahimner-hyusis-harav-chanaparh.html> (accessed on 22 August 2019).

¹⁶⁸ <http://www.investigative.am/en/news/view/hyusis-harav-chanaparh-mexadranq.html> (accessed on 22 August 2019).

¹⁶⁹ The same two-firm joint venture is the Supervision Consultant (Engineer) under Tranche 2.

¹⁷⁰ It appears that the focus of the Investigative Committee has included contractual aspects, including the application of FIDIC contracts vs. national rules and regulations (FIDIC contracts are used worldwide for construction activities, and consist of general conditions (e.g. rights and obligations of each party, procedure for payment, variation, certification and dispute resolution) and project-specific conditions (e.g. language of the contract, choice of law, and appointment of staff).

¹⁷¹ <https://www.aravot.am/2019/08/13/1059966/> (accessed on 22 August 2019).

¹⁷² Statistical Committee of the Republic of Armenia. 2018. *Statistical Yearbook of Armenia 2018* [General Description – <https://www.armstat.am/file/doc/99512088.pdf>].

¹⁷³ Ibid [Population – <https://www.armstat.am/file/doc/99511628.pdf>].

¹⁷⁴ Car Insurance Bureau (<http://www.paap.am/>).

¹⁷⁵ Statistical Committee of the Republic of Armenia. 2018. *Statistical Yearbook of Armenia 2018* [Transport and Communication – <https://www.armstat.am/file/doc/99510808.pdf>].

136. While there have been improvements in Yerevan's road network in recent years, congestion during peak hours continues to be a problem. Other concerns include increasing air pollution, inadequate public transport services, and an inefficient traffic management system. In order to address these challenges, a strategic framework for urban renewal was developed in 2010 based on a roadmap, policy framework and investment plan with short (immediate), medium-term (2011-2016) and long-term (2017-2025) interventions. The overall cost estimate amounted to \$960 million and thus an average capital and recurrent expenditure outlay of about \$70 million per year.¹⁷⁶

137. ADB in 2011 approved a MFF for the Sustainable Urban Development Investment Program (SUDIP) with a financing ceiling of \$400 million. It aims to support the national priority of upgrading city transport infrastructure to improve living standards and make cities more competitive platforms for economic growth. The program was originally based on five tranches, covering Yerevan as well as other cities, and in addition to urban infrastructure outputs also includes activities to improve institutional effectiveness as well as project management support. *Tranche 1* (\$48.64 million) started in July 2011 and was originally planned to close in June 2016 but was, due to implementation delays and an increased scope of work, extended to June 2020.¹⁷⁷ It covers 4 km of the Yerevan bypass road, multiple level intersections, and capacity strengthening of Yerevan Municipality and transport operations. *Tranche 2* (\$112.97 million) started in March 2016 and is scheduled to close in March 2020. It covers the Davitashen-Ashtarak section (contract signed in December 2016 and works were completed by end-December 2018), the Ashtarak-Babajanyan section (contract signed in December 2017 and works expected to be completed in January 2020), the Argavand-Shirak section (a tender in late 2017 failed and the bid submission deadline for the retender was mid-March 2019, i.e. the bids are now undergoing evaluation), and institutional capacity strengthening of Yerevan Municipality. The contract for the Argavand-Shirak section was signed in July 2019 and construction commenced in September 2019.

138. The EA is formally the Ministry of Economy, but the responsibilities have in practice been delegated to Yerevan Municipality in its role as the IA. Program implementation is undertaken by a dedicated PIU set up by Yerevan Municipality, which later also started managing other externally-financed projects. Oversight is provided by a Supervisory Board chaired by the Prime Minister.

139. The CPS 2014-2018 Final Review indicates that SUDIP will be rated 'effective' since physical activities have been carried out as planned, albeit in some cases with delays. However, SUDIP is rated 'less than efficient' as there was a delay in completing a construction design due to late recruitment of the detailed engineering and construction supervision consultant (2012-2013),¹⁷⁸ delays in the reorganization and staffing of the PIU (2012-2013), delayed submission of an updated community and gender action plan (2013), and weak performance by the program management and institutional strengthening consultant in one out of two components (2012-2015). With regard to the latter, Yerevan Municipality considered terminating the contract, but instead eventually decided not to extend the contract with the consultant (firm) beyond its original completion date and instead use the savings from non-implemented tasks (transport sector organization, setting up a Transport Authority, and bus network and integrated tariff and ticketing system) to tender these separately, which was originally planned for 2016, but was delayed to 2017 and 2018, respectively. A civil works

¹⁷⁶ ADB. 2011. *Proposed Multitranchise Financing Facility – Armenia: Sustainable Urban Development Investment Program*. Report and Recommendation of the President to the Board of Directors, March, p. 2.

¹⁷⁷ *Tranche 1* can, if the Government requests so, be extended till April 2021.

¹⁷⁸ This was one reason that ADB had the PIU restructured, and it has since then performed well.

contract (\$19.9 million) was terminated in October 2017 due to poor performance of the contractor, and Yerevan Municipality was compensated through an arbitration by the International Federation of Consulting Engineers (FIDIC).

140. A separate issue affecting the implementation performance has been financial constraints in the budget allocations (as the government had limited disbursement so as to keep public debt-to-GDP ratio below the 60% threshold), which led to delayed start of implementation of several road sections.¹⁷⁹ It is also the reason why the recruitment of consultancy services for transport sector organization and a bus network and integrated tariff and ticketing system was significantly delayed (although noted that a Transport Committee has in the meantime been created by Yerevan Municipality). While the loan completion dates have already been extended, further implementation delays are not unlikely if budget allocations in future years continue to be below the actual requirements.

141. The PIU has been fully operational since mid-2013 and appears to be well-functioning and efficient, including with regard to ensuring effective collaboration between Yerevan Municipality and ADB. This appears to be the result of a very competent and capable senior management, which also has handled well the political transition in Yerevan Municipality in October 2018.¹⁸⁰ However, it is also clear that organizational coordination and collaboration is relatively straightforward for Yerevan Municipality to ensure given that all entities refer to the Mayor/Deputy Mayors (as compared to construction of interstate and republican roads, which involves many entities that are not under the direct control of the MoTCI/GoA. All particular and operational loan covenants related to SUDIP have been complied with by Yerevan Municipality. No concrete integrity issues have been observed during implementation, and the PIU (as well as ADB) monitors the participation of firms during tenders to assess any potential risk of collusion and other integrity issues (e.g. conflict of interest).

142. While ADB is the major development partner in Armenia's urban transport sector, other agencies providing support for urban development include the EBRD (metro rehabilitation, solid waste management, urban roads, street lighting, and water supply), EIB (energy efficiency and solid waste management), KfW (water and sanitation), and the EU's Neighborhood Investment Facility (solid waste management).

143. The authorities in 2018 launched criminal cases related to suspected corruption against two Yerevan Municipality contractors but, as of March 2019, it does not appear that these so far have led to any trials. However, there is no suggestion that the entities involved have benefitted from any contracts under ADB-financed operations.

Urban Infrastructure Sector

144. Armenia has 49 urban settlements, consisting of Yerevan and 48 secondary towns, which are home to 64% of the population. While access to basic services in urban areas is better than in rural areas, it is generally still inadequate, especially as regards housing, water and sanitation, and waste management. Also, many public buildings are of substandard quality and require strengthening or reconstruction. The core problem is unbalanced urban development with Yerevan, already larger and more developed, continuing to develop faster than secondary towns.¹⁸¹

¹⁷⁹ While for 2018 the GoA's budget allocation for Tranche 1 is well above ADB's estimated disbursement, it is significantly below the estimated requirement for Tranche 2.

¹⁸⁰ Yerevan Municipality had the same mayor and deputy mayor (responsible for the PIU) from 2011/2012 till 2018, hence the changes in officials that followed the Yerevan City Council elections in October 2018 were the first to occur since the PIU was established.

¹⁸¹ ADB. 2014e. *Sector Assessment (Summary): Water and Other Urban Infrastructure and Services*. Country Partnership Strategy: Armenia, 2014-2018, p. 1.

145. In line with the 2014-2018 CPS, ADB supports urban development – in terms of planning and investing in infrastructure and services for sustainable urban systems and promoting an improved environment and resilience – through the *Seismic Safety Improvement Program (SSIP)*. The background for the program is Armenia's vulnerability to earthquakes and the need to improve its resilience to disasters and contribute to sustainable development. This is outlined in the Government's 2012 *National Strategy for Disaster Risk Reduction*, which defines the development of an efficient disaster risk reduction system as one of the most important factors for sustainable development. In strengthening or reconstructing public buildings to meet seismic safety standards, the government has prioritized school buildings.

146. The SSIP consists of an \$88.5 million loan and capacity development TA (\$0.8 million), which will increase the seismic resilience of school buildings, strengthen seismic disaster preparedness and response capacity, and improve supportive policies and systems for risk management. The EA is the MoTAD and the IA is the Armenian Territorial Development Fund (ATDF). The ATDF Board functions as the Program Steering Committee and thus sets the strategic direction and provides policy guidance.

147. The program started in December 2015 and is scheduled to close in November 2020 (unless extended, which may be necessary due to implementation delays). ATDF initially, with support from UNICEF and the MoTAD, undertook a vulnerability assessment which identified 412 out of the total 1,379 public schools as requiring structural strengthening or reconstruction. The SSIP covers 46 schools divided into three batches, which cover 8 schools selected in June 2016, 12 schools selected in July 2017, and 26 schools selected in mid-2018. The lengthy process of identifying schools delayed implementation, which in October 2017 (loan mid-term review) was estimated to be two years behind schedule.¹⁸² At present, civil works contracts for 7 schools have been signed and construction is on-going for 6 schools. As of November 2017, all loan covenants are being complied with.¹⁸³ Four out of seven 2016 disbursement-linked indicators (DLIs) were achieved in that year. The two DLIs for 2017 were not achieved during the year. While disbursements were made in 2016, no disbursements are expected for 2017 and 2018.

148. The CPS 2014-2018 Final Review indicates that the SSIP will be rated 'effective' and 'less than efficient'. There were initially substantial implementation issues due to government internal processes (including delays in the approval of the list of schools, requirements connected with the increased design standards, and design validation requirements), but the government remained engaged and committed. There were also challenges in some years due to restrictions in the budget allocations for the program (as the government attempted to keep the public debt-to-GDP ratio below the 60% threshold), but a substantial budget allocation was made for 2019. Following a three-year extension, the program is now rated "on track", from previously "actual problem". However, risks to project implementation are:¹⁸⁴ (i) delays in the approval of program schools, (ii) reduced budgetary allocations; and, (iii) lack of coordination among the GoA entities involved. The latter aspect relates to the need for the MoTAD, given its role as inter-governmental coordination focal point, to engage actively in providing strategic and political support to SSIP and the ATDF.

¹⁸² ADB. 2017. *Memorandum of Understanding. Loan 3284-ARM: Seismic Safety Improvement Program*. Loan Mid-Term Review, 16 October-17 November 2017, p. 2.

¹⁸³ The exception was the covenant on the use of materials from non-eligible countries, but this issue has since been resolved as the Government has stated that it will no longer do so.

¹⁸⁴ ADB. 2018a. *op.cit.*, p. 25.

149. In preparing the program, the results-based lending (RBL) was deemed a suitable modality. However, the financial management assessment prepared in June 2015 found that while the government system showed strong performance in policy-based budgeting and budget execution, there were weaknesses in internal control, financial reporting, internal audit and external audit. It was therefore concluded that there would be significant risks in using the country's PFM system in the short and medium term. To mitigate risks, the unusual step (considering that RBLs are otherwise based on the full use of country systems) to create a separate account for the program. Hence the SSIP may, in terms of the financial management procedures, be considered a hybrid as compared to other ADB operations based on the RBL modality. In order to ensure ATDF's implementation capacity, the SSIP included a DLI with a prior result target to engage 11 new staff, including for financial management and procurement, which were largely in place within six months of program start. The GoA now views the RBL as an effective modality that helps to increase ownership and focus on relevant outcome measures. The audited financial statements for the period December 2015 to December 2016, prepared by a private audit firm, have an unqualified opinion.

150. The procurement capacity assessment undertaken in 2015 found that to properly implement the SSIP, the ATDF would need to develop standard bidding documents, strengthen its capacity for technical bid evaluation, update its operations manual, submit an annual procurement monitoring report to the Board, and would require additional staff. Most of these actions were included in the program as DLIs. Given the estimated contract value, it was recommended to apply NCB procedures, adjusted in accordance with ADB's NCB annex for Armenia, for the majority of the procurement.¹⁸⁵ It appears that the SSIP procurement processes as undertaken by the ATDF are well-functioning.

151. No corruption-related issues have been observed by the ATDF or ADB in the implementation of the SSIP. While acknowledging the potential for such risks, the ATDF specifically notes that strict adherence to the procurement requirements, which have been strengthened as part of the program (cf. above), minimizes risks. This is further ensured through the monitoring initiative being piloted in the construction process (see below). Also, a key risk mitigation measure of the RBL modality applied for the SSIP is the validation procedure of the quality of completed school buildings, which is being carried out by an internationally accredited third-party. This means that ADB would not finance results failing to meet the targeted seismic safety standards.

152. ADB is implementing the 'Strengthening Government and Civil Society Cooperation in Open Government Partnership to Improve Public Services' project from December 2016 to May 2019. It includes support for the SSIP to reduce potential integrity and safeguards risks through a community-based pilot initiative, which aims to (i) reduce the risks of resource leakage in the construction process, (ii) ensure that contractual specifications are adhered to, and (iii) confirm that adequate quality in material inputs are met. The initiative is implemented by an international NGO through collaboration with local NGOs. It should initially have covered 20 schools, but was reduced to 8 schools due to the SSIP implementation delays (i.e. it now covers only the first batch). The pilot initiative was started in September 2017 with training of NGO participants (on community engagement, monitoring, and use of DevelopmentCheck¹⁸⁶) following which citizens monitors were selected and trained in January 2018 for each

¹⁸⁵ It was noted that the ATDF was already familiar with implementing World Bank-financed projects following NCB procedures adjusted for World Bank guidelines.

¹⁸⁶ DevelopmentCheck (<https://www.developmentcheck.org/>) is an app for real-time citizen feedback on the transparency, participation and effectiveness of development projects.

school.¹⁸⁷ The main monitoring findings relate to the quality of inputs (especially cement), workmanship performance, environmental aspects (cleaning of construction sites and establishing water system), and storage of materials. The pilot initiative has been successful in ensuring community engagement and developing a culture where monitoring is accepted and valued by both government and contractors, and resulted in improved adherence to contractual specifications and the quality of material inputs (the monitoring focus was less on reducing possible risks of resource leakage in the construction process). The ATDF has actively supported the monitoring process and has coordinated closely with the NGOs. It appears that, going forward, the government may discontinue the involvement of NGOs in the process, although a final decision in this regard is yet to be taken.

Education Sector

153. The education system in Armenia comprises pre-primary, primary, and secondary, vocational, and higher education. There are a total of 1,409 schools and 381,343 students.¹⁸⁸ Pre-primary education covers nursery (age 2-3 years) and kindergarten (age 3-6 years). Secondary education has three levels: primary (age 6-9 years), lower secondary (age 10-14 years) and upper secondary (age 15-17 years). Vocational education is conducted at colleges, while higher education is provided by universities and other institutions. Most state educational institutions are organized as SNCOs and governed by management boards. The role of the Ministry of Education, Science, Culture and Sport (MoESCS) is to develop and implement the government's education policy, and it directly oversees high schools. It operates the Education Management Information System (EMIS), which is used to collect and report education data. The National Center for Educational Technologies prepares and publishes school ratings. The regional administrations (*marzpetarans*) are the authorized bodies for most schools. Education management reforms implemented in recent years have led to increased autonomy of educational institutions and expanded the involvement of civic society.¹⁸⁹

154. ADB does not presently have operations in the education sector,¹⁹⁰ although efforts are on-going in future to provide support, including based on the Social Sectors Reform Program.¹⁹¹ Given the currently limited engagement, the following provides an overview of specific governance-related aspects of the education sector (including school governance, education sector financing, PFM and corruption) based on available studies. This can be considered and applied as and when ADB is developing its future operations in the education sector.

155. School governance: The main participants in school governance and management are the boards and the principals. The board is a collegial governing body comprising the MoESCS, regional administration, community (local government), teachers and parents. It approves the school budget and selects the principal who in turn is in charge of the school operational management. The school administration and the quality of education are subject to reviews by the MoESCS.

¹⁸⁷ An initial 30 participants were pre-selected for each school of which 15 were trained by the NGOs, and from these 5-7 participants per school were then chosen as 'citizens monitors' for the school joint working groups (originally only 3 participants per school were planned, but the group size was increased due to the interest).

¹⁸⁸ Statistical Committee of the Republic of Armenia. 2018. *Statistical Yearbook of Armenia 2018* [Education and Culture – <https://www.armstat.am/file/doc/99510758.pdf>].

¹⁸⁹ Jens Claussen and Artak Kyurumyan. 2018. *Education Financing & Public Financial Management Assessment in Armenia*. 10 April, p. 2.

¹⁹⁰ The Ministry of Education and Science (MoESCS) is involved in the SSIP, which is reconstructing school buildings to increase their seismic resilience, but so the operation does not have an education technical focus.

¹⁹¹ The Social Sectors Reform Program, is providing transaction TA to help the government and ADB develop a policy-based loan (PBL) to facilitate comprehensive policy reforms in the education and health sectors, including to improve the efficient utilization of resources and quality of services in these sectors.

156. While the legislative framework and institutional coverage in the education sector is comprehensive, there are some gaps and, more critically, malpractices in actual implementation¹⁹² that adversely affects management and governance practices.¹⁹³ The main gaps are national and sub-national policy issues, insufficient involvement of communities, leadership competence, and poor institutional support that hinders future progress of schools. These issues are augmented by deficient functioning of school boards. Although the reform agenda for some years has aimed at improving school management and governance, there has so far been limited progress.¹⁹⁴

157. According to a press release in August 2018,¹⁹⁵ the Investigative Committee has initiated 59 criminal cases related to suspected misuse and embezzlement of funds in schools, pre-schools and higher education institutions.

158. Education sector spending: The education system is funded by the state from its annual budget with ceilings projected from the MTEF. Funding for pre-primary, primary and secondary education is channeled through the budgets of the territorial administrative units. The MoESCS is currently developing a new Education Development Strategy. Armenia's education sector expenditures as a share of GDP is lower than other countries at the same income level.¹⁹⁶ Also, the education sector budget is spread among many entities, which makes it challenging in terms of coordination to link spending allocations and to sector-relevant targets. Furthermore, the school allocation formulation is wholly needs-based and does not take into account performance.

159. PFM: The annual *planning and budgeting* process focuses on updating the three-year rolling MTEF and preparing the annual budget. The latter is based on the program-based budgeting approach, which has been gradually introduced over a number of years and is fully applied in the education sector for the first time for 2019. However, the annual budget is presented as a detailed costed operational plan rather than with aggregate sub-sector targets and related resource requirements based on costing of these targets.¹⁹⁷ Hence to prepare a meaningful program-based budget for the education sector, the MoESCS should specify sub-sector targets related to net enrollment, learning achievements and other key performance indicators, which would then provide a justification for the allocations to different sub-sectors, and thus present a proper basis for decision-making.

160. The *budget execution* procedures for the education sector are similar to those of other sectors. The MoESCS transfers funds monthly from its treasury account to the bank accounts of schools and other education institutions (SNCOs) based on approved allocation lists. Following legislative changes in December 2017, however, SNCOs will in 2018 start using the treasury system and hence close their accounts in commercial banks. The spending of funds is decentralized, and each school manages its own funds based on its budget as approved by the school council (and subsequently by the MoESCS). All schools pay salaries directly to their staff. Supervision of schools is done

¹⁹² These include undue control exercised by the regional administration, .redistributing financial resources between schools (current legislation in fact allows for this), and capture of school management by local clans (which, among other reasons, happens as schools in rural areas are among the few entities with stable wages), which can lead to nepotism, corruption and sub-quality staffing.

¹⁹³ Alison Price-Rom and Hovhannes Atabekyan. 2017. *Education and Skills for Employment in Central and West Asia – National School Management and Governance in Armenia*. ADB Technical Assistance Consultant Report, August, p. 4.

¹⁹⁴ Ibid.

¹⁹⁵ <http://www.investigative.am/en/news/view/hayk-grigoryan-meknabanutyun-charashahumner.html>.

¹⁹⁶ Jens Claussen and Artak Kyurumyan. 2018. op.cit., p. 5.

¹⁹⁷ Ibid, pp. 12-13.

by the MoESCS, Yerevan Municipality or territorial administrations, depending on the location.

161. *Accounting and internal control* is based on the Armenian Public-Sector Accounting Standards (APSAS).. It appears that all schools in recent years have acquired accounting software.¹⁹⁸ As SNCOs, schools prepare and submit quarterly and annual financial reports to their authorized bodies as well as to the MoF.

162. The MoESCS has an *internal audit* function that works using a risk-based annual program approved by the Minister. Reports are presented to an Internal Audit Committee. Yerevan Municipality and the regional administrations have their own Internal Audit Units, which are responsible for audit of schools, but they have limited capacity and staff. Schools are also supervised by MoF's Financial Inspectorate.

163. Schools and other education institutions are subject to *external audit* by the Audit Chamber. Its Seventh Department covers the MoESCS, but it is not clear to which extent it also undertakes audits of individual entities, on a sample basis or otherwise.

164. A local NGO in 2017 carried out an assessment of the state funding of the education sector.¹⁹⁹ Findings included that there is a need to clarify the process of redistribution resources within the sector during budget execution; that while the GoA claims that the quality of education is improving, there is no actual data to prove this; that budget documents do not include qualitative indicators and measures; that impact assessments related to education policies are not being undertaken; that there is a mismatch between activities funded as 'subsidies' and their actual purpose, which gives rise to procurement issues; that funding mechanism for higher education needs to be clarified and should be made formula-based; and, that budget documents do not include data on actual expenditures or unit costs.

165. Corruption in schools: The GoA's 2015-2018 anticorruption action plan includes education as one of four focus areas (the others are the health sector, police and state revenue). The sector-specific plan²⁰⁰ identified 28 corruption risks for pre-school (including admission, staff hiring, and administration), general education (including governing boards, political influence, textbook publication, staff hiring and promotion, tutoring, and fundraising practices), and higher education (including political influence, hiring and promoting, academic dishonesty, examinations, and process of granting diplomas). The sector action plans also include timelines, responsible agencies, funding sources and indicators, but no target values and, also, no progress updates. Hence the planned end-results and the actual implementation outcomes are not clear.

166. Two local NGOs in 2016 carried out a corruption risk assessment of the secondary education sub-sector.²⁰¹ The study found that, despite on-going reforms of the secondary education system and improvement of the relevant legislative framework, many systemic issues that contribute to corruption remained unresolved. These included widespread practice of *tuition payment*, which is not prohibited, but also not regulated. While paid tuition by teachers is not in itself a negative phenomenon, it can become problematic if there is a conflict of interests (e.g. if teachers do not have time to fully perform their ordinary duties, or do not complete the curriculum in order to

¹⁹⁸ Armenian Software (ARMSOFT): www.armsoft.am/.

¹⁹⁹ Transparency International Anticorruption Center. 2018. *State Funding Issues of the Education System of Armenia*. USAID.

²⁰⁰ <https://anti-corruption.gov.am/am/spheres?s=35>.

²⁰¹ Transparency International Anticorruption Center and Institute of Public Policy. 2017. *Corruption Risk Assessment in the General Education Sector in Armenia*. The study was funded by USAID.

encourage students to take paid tuition). The study recommends that ethical rules are developed for school directors and teachers to regulate potential conflicts of interest, that it be prohibited for teachers to provide paid tuition in the same subject that they teach, and that sanctions are defined and applied against school staff attempting to influence parents or students to avail of paid tuition. A related issue is the *low quality of education*, which increases the demand for paid education for different reasons: (i) It is difficult to pass university admission exams without having received (paid) tuition; (ii) High schools do not perform their functions effectively with limited focus on motivation and education outcomes; (iii) Low textbook quality which are considered complex and difficult to access, including as some are inadequately translated from other languages; (iv) Low professional level of teachers. Another problem is *insufficient state control and supervision* in that while the State Education Inspectorate under the Office of Government has a broad range of responsibilities, they do not specifically include paid tuition. Also, inspections generally focus on procedures and documentation rather than on quality control issues. Addressing these issues would require more control in the enforcement of existing requirements and procedures as well as changes in the legislative framework.²⁰²

167. Corruption risks have also been noted in relation to special needs/inclusive education where the state provides additional funding support, which can be financially beneficial for schools, but where the needs assessment process may not always be fully transparent. Corruption risks have furthermore been identified in relation to textbook tenders where the competition committees and the selection procedure are deemed most vulnerable. Also, general education standard-setters and curriculum developers can, because of a legal loophole, participate in textbook competitions, which they have comparatively good chances of winning due to their inside information about the required content of textbooks.

²⁰² Relevant focus areas include defining clear criteria for the hiring and dismissal of education professionals (teachers, pedagogical-psychological support specialists, and assessors), raising professional awareness and readiness of those entities and staff that should conduct supervision and oversight, developing clear mechanisms for supervision on the quality of education, as well as on the effectiveness of allocated budgetary and extra-budgetary resources, and developing public supervision mechanisms so as to enhance the transparency and the accountability of the sector.

IX. ANNEXES

- Annex A – Documents Reviewed
- Annex B – Persons Consulted
- Annex C – ADB’s 2019 Assistance Program
- Annex D – Country Governance Surveys

A. Documents Reviewed

ADB Documents

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B. Persons Consulted

Asian Development Bank (ADB)

- **Mr Shane Rosenthal** – Country Director, Armenia Resident Mission
- **Mr Cesar Llorens** – Deputy Country Director, Armenia Resident Mission
- **Ms Gohar Mousaelyan** – Senior Project Officer, Armenia Resident Mission
- **Mr Grigor Gyurjyan** – Economics Officer, Armenia Resident Mission
- **Mr Huiping Huang** – Project Administration Unit Head, Armenia Resident Mission
- **Ms Nina Avetisyan** – Associate Project Analyst, Armenia Resident Mission
- **Mr Vardan Karapetyan** – Senior Project Officer, Armenia Resident Mission [*former Finance Manager (2016) and Acting General Director (2017-2018), TPIO SNCO*]
- **Ms Maria Pia Ancora** – Climate Change Specialist, Armenia Resident Mission
- **Mr Shavkat Vosiev** – Associate Project Analyst, Armenia Resident Mission
- **Ms Zaruhi Hayrapetyan** – International Resettlement Specialist (Consultant), Armenia Resident Mission
- **Ms Claudia Buentjen** – Principal Public Sector Management Specialist, Sustainable Development and Climate Change Department
- **Mr Thomas Herz** – Transport Specialist, Central West Asia Regional Department
- **Mr João Pedro Farinha Fernandes** – Senior Financial Sector Economist, Central West Asia Regional Department
- **Ms Sona Poghosyan** – Social Development Specialist (Safeguards), Central West Asia Regional Department [*former Head of Social Safeguard Unit, TPIO SNCO*]
- **Mr Thomas Robinson** – Procurement Specialist, Transport and Communications Division, Central West Asia Regional Department
- **Mr Eduard Avetisyan** – Integrity Specialist, Review and Outreach Unit, Office of Anticorruption and Integrity

Ministry of Transport, Communication and Information Technologies (MoTCIT)

- **Mr Bagrat Badalyan** – Deputy Minister

Ministry of Economic Development and Investment (MoEDI)

- **Mr Avag Avanesyan** – Deputy Minister

Ministry of Education, Science, Culture and Sport (MoESCS)

- **Ms Arevik Anapiosyan** – Deputy Minister
- **Mr Arkadi Papoyan** – Head, Foreign Relations and Diaspora Department
- **Mr Robert Stepanyan** – Head, Development Program and Monitoring Department

Ministry of Territorial Administration and Development (MoTAD)

- **Mr Armen Manukyan** – Head, Financial-Economic, Accounting and Local Budgeting Department
- **Ms Narine Avetyan** – Head, Territorial Investment Policy and Infrastructure Development Department
- **Mr Artur Soghomonian** – Head, Territorial Administration Department

Ministry of Finance (MoF)

- **Mr Sergey Shahnazaryan** – Head, Internal Financial Control and Public Procurement Methodology Department and Internal Audit Department

First Deputy Prime Minister's Office

- **Mr Vahan Kostanyan** – Advisor

- **Ms Anna Grigoryan** – Assistant

Armenian Road Directorate (ARD)

- **Mr Gor Avetisyan** – Director General
- **Mr Avag Petrosyan** – Deputy Director

Armenian Territorial Development Fund (ATDF)

- **Mr Ashot Kirakosyan** – Executive Director
- **Mr Arthur Soghomonyan** – Head, Procurement Department

Yerevan Municipality

- **Mr Vahe Nikoyan** – Deputy Mayor [until October 2018]

Audit Chamber

- **Mr Karen Arustamyan** – Head, Methodology & International Affairs Department
- **Mr Argishti Sargsyan** – Adviser, Methodology & International Affairs Department

Project Implementation Units (PIUs)

- **Ms Nora Martirosyan** – Project Director, Yerevan Development Project Implementation Unit (YDPIU), Yerevan Municipality
- **Ms Christine Ghalechyan** – Acting Director, Transport Project Implementation Organization (TPIO) SNCO

Development partners

- **Mr John Zohrab** – Regional Advisor, IMF
- **Ms Armine Aydinyan** – Procurement Specialist, World Bank
- **Ms Nora Mirzoyan** – Infrastructure Consultant, World Bank
- **Mr Davit Melikyan** – Senior Public Sector Specialist, World Bank
- **Mr Armen Poghosyan** – Deputy Director, EDB
- **Mr Rudik Tadevosyan** – Municipal and Environmental Infrastructure Project Monitor, EBRD
- **Mr Jens Petersen-Thumser** – Team Leader, ‘Public Financial Management in the South Caucasus’ Project, GIZ
- **Ms Varsenik Mnatsakanyan** – Advisor, ‘Public Financial Management in the South Caucasus’ Project, GIZ
- **Mr Vardan Poghosyan** – Team Leader, ‘Legal Approximation towards European Standards in the South Caucasus’ Project, GIZ
- **Mr Paulius Strelciunas** – International Aid/Cooperation Officer, EU Delegation

Civil society organizations (CSOs)/Non-governmental Organizations (NGOs)

- **Ms Naira Arakelyan** – Executive Director, Armavir Development Center
- **Ms Silva Adamyan** – President, ‘Center of Bird Lovers’ NGO
- **Mr Varuzhan Hochtanyan** – Project Director, Transparency International Anticorruption Center

Others

- **Mr Alexander Astvatsatryan** – National Procurement Consultant, ADB
- **Mr Naushad Khan** – International Procurement Consultant, ADB
- **Mr Ghukas Grigoryan** – Owner, "Vahagn ev Samvel" LLC
- **Mr Ruben Baghdasaryan** – Owner, "Khachar" LLC

C. ADB's 2019 Assistance Program

Table 8 – Approved operations implemented during 2019

Name	Implementation Period	Type	Amount (US\$ m)*	Executing Agency
Energy				
1. Power Transmission Rehabilitation Project	2016-2020	Loan	37.000	Ministry of Energy and Natural Resources
2. Sevan-Hrazdan Cascade Hydropower System Rehabilitation Project	2013-onwards	Loan	25.000	International Energy Corporation (IEC) [Borrower]
3. Electric Networks of Armenia Closed Joint-Stock Company (Distribution Network Rehabilitation, Efficiency Improvement, and Augmentation)	2017-onwards	Loan	80.000	Electric Networks of Armenia CJSC [Borrower]
4. Yerevan Gas-Fired Combined-Cycle Power Project	2018-onwards	Loan	44.000	ArmPower CJSC [Borrower]
5. High Voltage Electrical Networks, CJSC	2018-2019	TA	0.100	HVEN, CJSC
Finance				
6. SME Finance Program	2011-onwards	Loan	15.000	Ardshinbank CJSC [Borrower]
	2016-onwards	Loan	20.000	ACBA Credit Agricole Bank [Borrower]
	2017-onwards	Loan	20.000	Ameriabank CJSC [Borrower]
7. Rural Financial Inclusion Project	2016-onwards	Loan	6.000	Finca Armenia UCO CJSC [Borrower]
Finance and Public sector management				
8. Support to Public Efficiency and Financial Markets Program	2017-2019	TA	0.500	Ministry of Finance
		TA	0.100	
		TA	0.100	
Transport [road transport]				
9. North-South Road Corridor Investment Program - Tranche 2	2011-2019	Loan	170.000	Ministry of Transport, Communication and Information Technologies
10. North-South Road Corridor Investment Program – Tranche 3	2014-2019	Loan	100.000	Ministry of Transport, Communication and Information Technologies
11. Armenia-Georgia Border Regional Road (M6 Vanadzor-Bagratashen) Improvement Project	2017-2021	Loan	50.000	Ministry of Transport, Communication and Information Technologies
12. Project Management Support to the Ministry of Transport and Communication	2015-2019	TA	0.200	Ministry of Transport, Communication and Information Technologies
		TA	0.225	

Name	Implementation Period	Type	Amount (US\$ m)*	Executing Agency
Transport [urban transport]				
13. Sustainable Urban Development Investment Program – Tranche 1	2011-2020	Loan	48.640	Ministry of Economy
14. Sustainable Urban Development Investment Program – Tranche 2	2016-2020	Loan	112.97	Ministry of Economy
Education and health				
15. Social Sectors Reform Program	2018-2020	TA	0.800	Ministry of Education, Science, Culture and Sport
		TA	0.650	Ministry of Finance Ministry of Healthcare
Education and Water and other urban infrastructure and services				
16. Seismic Safety Improvement Program	2015-2024	Loan	88.500	Ministry of Territorial Administration and Development
	2015-2019	TA	0.800	
Water and other urban infrastructure and services				
17. Vertical Mobility and Safety Improvement Project	2017-2019	TA	0.225	Ministry of Economy Yerevan Municipality
18. Support and Validation of Seismic Safety Improvement Program Indicators	2018-2023	TA	0.500	Ministry of Territorial Administration and Development
Agriculture, Natural Resources and Rural Development				
19. High-Efficiency Horticulture and Integrated Supply Chain Project)	2018-onwards	Loan	32.000	Spayka Limited Liability Company [Borrower]
Finance and Industry and trade				
20. Export- and Innovation-Led Industrial Development	2016-2019	TA	0.500	Ministry of Economic Development and Investments
		TA	0.250	
Industry and trade				
21. Analysis of Economic Opportunities Associated with Armenia's New Trade Regime	2018-2020	TA	0.200	ADB

Abbreviations: TA = technical assistance.

Note *: Loan amounts include financing from ADB's Ordinary Capital Resources (OCR) only. Co-financing amounts for some loans are not indicated. TA amounts include internal as well as external sources.

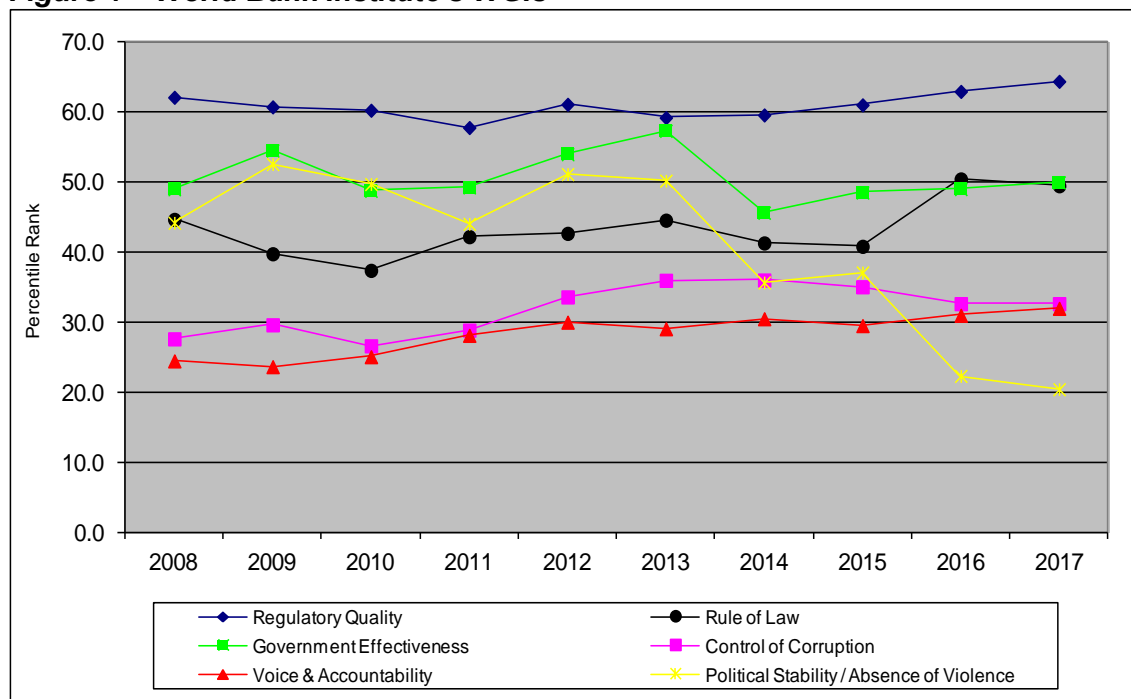
D. Country Governance Surveys

This annex presents the main findings from a number of international governance surveys. The information is presented with 2008 as the starting point to cover the full period of the presidency of Serzh Sargsyan (2008-2018) and the subsequent period.

World Bank Institute – Worldwide Governance Indicators (WGIs)

The WGIs capture six key dimensions of governance and measure the quality of governance in over 200 countries.²⁰³ They compile perceptions from a diverse group of respondents collected in surveys and other cross-country assessments.

Figure 1 – World Bank Institute’s WGIs²⁰⁴



Over the period as a whole, the ranking for ‘Political Stability’ decreased significantly, especially in 2013 and 2016. The latter may be due to the Nagorno-Karabakh clashes in April 2016 and the constitutional amendments which came into effect in June 2016. The rankings of ‘Voice & Accountability’, ‘Rule of Law’ and ‘Control of Corruption’ all increased slightly over the period but, apart from 2011, the changes took place at different times. The rankings of ‘Regulatory Quality’ and ‘Government Effectiveness’ have overall been stable.

Economist Intelligence Unit (EIU) – Index of Democracy

The Index of Democracy examines the state of democracy in 167 countries based on five general categories, and places countries into one of four groups (full democracies,

²⁰³ The governance dimensions are defined as follows: Regulatory Quality – The ability of the government to formulate and implement sound policies and regulations that permit and promote private sector development. Rule of Law – The extent to which agents have confidence in and abide by the rules of society, and in particular the quality of contract enforcement, property rights, the police, and the courts, as well as the likelihood of crime and violence. Government Effectiveness – The quality of public services, quality of the civil service and degree of its independence from political pressures, quality of policy formulation and implementation, and credibility of the government’s commitment to such policies. Control of Corruption – The extent to which public power is exercised for private gain, including petty and grand forms of corruption as well as ‘capture’ of the state by elites and private interests. Voice and Accountability – The extent to which citizens are able to participate in selecting the government, as well as freedom of expression, freedom of association, and a free media. Political Stability – The likelihood that the government will be destabilized or overthrown by unconstitutional or violent means, including politically-motivated violence and terrorism.

²⁰⁴ The WGIs show the percentile ranks where, on the continuum from 0% to 100%, a particular country is placed (i.e. it is a relative ranking). 0% represents the worst performance among the countries, 100% the best performing country.

flawed democracies, hybrid regimes and authoritarian regimes). The survey consists of 60 questions answered by country experts and also draws on public opinion surveys where available.

Table 9 – EIU’s Index of Democracy

(10: Highest, 0: Lowest)	Overall score	Electoral Process and Pluralism	Functioning of Government	Political Participation	Political Culture	Civil Liberties	Rank (167 countries)
2008	4.09	4.33	3.21	3.89	3.13	5.88	113
2010	4.09	4.33	3.21	3.89	5.63	5.59	109
2011	4.09	4.33	3.21	3.89	3.13	5.88	111
2012	4.09	4.33	3.21	3.89	3.13	5.88	114
2013	4.02	4.33	2.86	3.89	3.13	5.88	116
2014	4.13	4.33	2.86	4.44	3.13	5.88	113
2015	4.00	4.33	2.86	4.44	2.50	5.88	116
2016	3.88	4.33	2.86	4.44	1.88	5.88	120
2017	4.11	5.25	2.86	5.00	1.88	5.59	111
2018	4.79	5.67	4.64	5.56	2.50	5.59	103

The overall score was more or less stable at a moderately low level from 2008 to 2014 after which it decreased in 2015-2016 followed by notable increases in 2017 (following the constitutional changes that shifted power from the presidency to parliament) and, especially, 2018 (the “Velvet Revolution”). Armenia has been considered a ‘hybrid regime’ for the full period except in 2016 when it, according to the overall score, was deemed an ‘authoritarian regime’.²⁰⁵

Transparency International (TI) – Corruption Perception Index (CPI)

The CPI ranks countries in terms of the degree to which corruption is perceived to exist among public officials and politicians. It is a composite index that draws on corruption-related data from expert and business surveys.

Table 10 – TI’s CPI Data

Year	No. of Countries	Ranking of Armenia	CPI Score*	Confidence Range	Surveys Used
2008	180	109	2.9	2.6-3.1	7
2009	180	120	2.7	2.6-2.8	7
2010	178	123	2.6	2.5-2.8	7
2011	183	129	2.6	2.4-2.9	8
2012	176	105	34	29-38	6
2013	177	94	36	30-42	6
2014	175	94	37	31-43	6
2015	168	95	35	30-40	5

²⁰⁵ **Hybrid regimes** (score between 4.0 and 5.9) are defined with the following characteristics: “Elections have substantial irregularities that often prevent them from being both free and fair. Government pressure on opposition parties and candidates may be common. Serious weaknesses are more prevalent than in flawed democracies—in political culture, functioning of government and political participation. Corruption tends to be widespread and the rule of law is weak. Civil society is weak. Typically, there is harassment of and pressure on journalists, and the judiciary is not independent.” **Authoritarian regimes** (score below 4.0) are defined with the following characteristics: “In these states, state political pluralism is absent or heavily circumscribed. Many countries in this category are outright dictatorships. Some formal institutions of democracy may exist, but these have little substance. Elections, if they do occur, are not free and fair. There is disregard for abuses and infringements of civil liberties. Media are typically state-owned or controlled by groups connected to the ruling regime. There is repression of criticism of the government and pervasive censorship. There is no independent judiciary.”

Year	No. of Countries	Ranking of Armenia	CPI Score*	Confidence Range	Surveys Used
2016	176	113	33	26-40	6
2017	180	107	35	29-41	6
2018	180	105	35	28-42	6

* The CPI score was during 2008-2011 based on the following: 10: highly clean, 0: highly corrupt. From 2012 onwards it is: 100: highly clean, 0: highly corrupt.

The CPI score deteriorated from 2008 to 2011, but has been more or less unchanged from 2012 to 2018. Corruption among public officials and politicians is hence perceived to be very high. The relative ranking likewise deteriorated from 2008 to 2011 and remained overall unchanged from 2012 to 2018.

Fund for Peace and Foreign Policy– Failed States Index

The Failed States Index reviews state vulnerability and the risk of violence. It is based on indicators related to social, economic and political aspects that are part of a Conflict Assessment System Tool methodology, which uses open-source articles and reports.

Table 11 – Fund for Peace and Foreign Policy’s Failed States Index

<i>Rating scale: 0 is the lowest intensity (most stable) and 10 the highest intensity (least stable).</i>	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Conflict Indicators											
Security Apparatus	4.5	5.3	5.1	5.2	5.2	5.3	5.6	5.3	5.0	5.5	5.2
Factionalized Elites	6.0	6.9	7.0	7.0	7.0	7.0	7.4	7.0	7.0	7.4	7.4
Group Grievance	5.0	6.0	6.0	6.0	5.7	5.7	5.7	5.4	5.6	6.1	5.8
Economic Indicators											
Economy	5.6	5.3	5.8	5.3	5.6	5.9	5.8	6.0	6.5	6.3	6.6
Economic Inequality	6.0	6.5	6.5	6.2	5.9	5.6	5.3	5.0	4.7	4.5	4.2
Human Flight and Brain Drain	6.7	6.7	7.0	6.6	6.3	6.0	5.7	6.0	5.9	6.2	6.1
Political Indicators											
Legitimacy of the State	6.5	7.1	6.6	6.6	6.8	6.6	6.7	7.0	7.2	7.6	8.1
Public Services	6.0	5.4	5.3	5.0	4.7	4.4	4.4	4.1	3.8	3.6	3.4
Rule of Law and Human Rights	5.5	6.1	6.4	6.5	6.8	6.8	6.8	6.5	7.0	7.0	6.9
Social Indicators											
Demographic Pressures	5.8	5.9	5.7	5.5	5.2	4.9	4.7	3.6	3.3	3.1	2.8
Refugees and Internal Displaced People	7.5	7.2	6.9	6.6	6.8	7.0	6.7	7.0	6.7	7.0	6.7
External Intervention	5.6	5.9	5.8	5.8	6.1	6.2	6.5	6.8	6.9	6.7	6.4
Total (max. 120 = least stability)	70.7	74.3	74.1	72.3	72.2	71.3	71.3	69.7	69.6	71.0	69.5
<i>Relative Ranking (177/178 countries)</i>	109	101	101	102	102	105	104	108	109	102	102

Armenia has remained moderately stable during the period from 2008 to 2018, which is seen from the absolute scores (which for the whole period places Armenia in the ‘warning’ group of countries²⁰⁶) as well as the relative scores. However, while the conflict indicators and the social indicators show an improvement over time, the picture is mixed for the economic indicators and the political indicators. The least “stable” indicator is ‘Legitimacy of the State’ (relating to the representativeness and openness of government and its relationship with its citizenry), which has significantly deteriorated since 2013, while the most “stable” indicator is ‘Demographic Pressures’

²⁰⁶ The categorizations used in the Failed State Index are ‘alert’ (total score between 90-120), ‘warning’ (60-89.9), ‘monitoring’ (30-59.9) and ‘sustainable’ (0-29.9).

(referring to pressures upon the state deriving from the population itself or the environment around it), which has improved steadily every year since 2009.

Cato Institute et al – Human Freedom Index

The Human Freedom Index – prepared by the Cato Institute, Fraser Institute and Friedrich Naumann Foundation – measures the degree of personal freedom, including legal protection and civil liberties, and economic freedom. The index covers 159 countries using a large number of distinct variables.

Table 12 – Human Freedom Index

(10: Most Free, 0: Least Free)	2008	2009	2010	2011	2012	2013	2014	2015	2016
1a. Rule of Law	4.9	4.9	4.9	4.9	4.6	4.6	4.6	4.7	5.0
1b. Security and Safety	9.4	9.4	9.6	9.3	9.3	9.0	9.0	8.9	8.8
2a. Movement	6.7	6.7	6.7	6.7	6.7	6.7	6.7	6.7	6.7
2b. Religion	7.4	7.4	7.0	6.0	5.9	5.9	6.1	8.0	6.2
2c. Association, Assembly and Civil Society	-	-	-	7.5	7.5	7.5	7.5	7.5	6.5
2d. Expression and Information	5.7	6.7	6.8	8.1	8.3	8.3	8.3	7.2	7.2
2e. Identity and Relationships	10.0	10.0	10.0	10.0	10.0	8.3	8.3	8.0	8.0
Personal Freedom	7.34	7.41	7.43	7.36	7.33	7.09	7.09	7.11	6.91
<i>Ranking</i>	68/159	66/159	69/153	76/153	70/152	84/157	81/159	76/159	84/159
1. Size of Government	8.8	8.1	7.4	7.7	7.7	7.8	7.6	7.1	7.0
2. Legal System and Property Rights	5.6	5.6	4.3	4.4	4.5	4.2	4.2	5.8	5.8
3. Sound Money	8.9	9.4	8.2	7.9	8.4	8.3	8.7	9.5	9.5
4. Freedom to Trade Internationally	7.7	7.6	6.4	6.4	6.5	6.7	7.5	8.2	8.1
5. Regulation	7.1	7.1	6.8	6.7	6.3	6.6	6.9	7.4	7.4
Economic Freedom	7.59	7.55	7.56	7.71	7.75	7.69	7.70	7.60	7.57
<i>Ranking</i>	22/159	21/159	24/153	19/153	17/152	18/157	23/159	29/159	29/159
Human Freedom	7.46	7.48	7.50	7.54	7.54	7.39	7.39	7.36	7.24
<i>Ranking</i>	50/159	50/159	50/153	50/153	50/152	52/157	54/159	54/159	57/159

The level of *personal freedom* has over the period deteriorated somewhat, specifically from 2012 to 2013. At the indicator-level, it is seen that the scores for ‘Religion’ as well as ‘Identity and Relationships’ decreased over time (as did the indicator for ‘Association, Assembly and Civil Society’ in 2016), while the score for ‘Expression and Information’ increased. The level of *economic freedom* of citizens and businesses was overall unchanged. However, that is a result of the score for ‘Size of Government’ decreasing and the other four scores increasing.

The Heritage Foundation – Index of Economic Freedom

The Index of Economic Freedom measures the degree of economic freedom based on 10 quantitative and qualitative factors,²⁰⁷ which are grouped into four broad categories. The index uses statistics from the World Bank, IMF and the EIU.

²⁰⁷ **Property Rights:** The ability of individuals to accumulate private property, secured by clear laws that are fully enforced by the state. **Freedom from Corruption:** Security and certainty in economic relationships. **Government Integrity:** Fair and equal treatment of all actors in the economic system. **Judicial Effectiveness:** Efficient and fair judicial systems to ensure that laws are fully respected, with appropriate legal actions taken against violations. **Government Spending:** The level of government expenditures as a percentage of GDP. **Fiscal Freedom:** Tax burden imposed by government. **Tax burden:** Overall tax burden from all forms of taxation as a percentage of GDP. **Fiscal Health:** Fiscal balance and debt following from the government’s budget. **Business Freedom:** Overall burden of regulation and the efficiency of government in the regulatory process. **Labor Freedom:** Aspects of the legal and regulatory framework of the labor market. **Monetary Freedom:** Price stability and price controls. **Trade Freedom:** The

Table 13 – The Heritage Foundation's Index of Economic Freedom

<i>Rating scale: 0 (lowest) to 100 (highest)</i>		2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Rule of law	Property rights	35.0	30.0	30.0	30.0	30.0	30.0	30.0	20.0	20.0	55.5	55.3
	Freedom from corruption	29.0	30.0	29.0	27.0	26.0	26.0	26.7	36.0	37.0	-	
	Government integrity						-	-	-	-	43.4	40.5
	Judicial effectiveness						-	-	-	-	42.5	47.4
Government size	Government size / spending	86.4	89.7	90.9	85.7	74.9	82.1	81.3	82.8	80.7	81.7	80.0
	Fiscal freedom	89.0	90.0	89.3	89.2	89.3	88.0	86.5	84.4	83.8	-	
	Tax burden						-	-	-	-	83.7	84.7
	Fiscal health						-	-	-	-	82.9	67.2
Regulatory efficiency	Business freedom	81.3	83.7	83.4	82.4	87.8	87.6	83.1	82.7	77.5	78.5	78.7
	Labor freedom	73.1	66.3	70.6	75.9	76.6	77.1	78.5	64.3	62.2	72.4	69.9
	Monetary freedom	84.6	77.8	72.9	76.0	73.1	73.0	77.0	70.6	72.8	72.8	75.8
Open markets	Trade freedom	85.0	86.4	80.5	85.5	85.4	85.4	85.5	85.4	85.6	80.2	80.0
	Investment freedom	70.0	70.0	75.0	75.0	75.0	75.0	70.0	75.0	80.0	80.0	75.0
	Financial freedom	70.0	70.0	70.0	70.0	70.0	70.0	70.0	70.0	70.0	55.5	70.0
Overall Score		70.3	69.9	69.2	69.7	68.8	69.4	68.9	67.1	67.0	70.3	68.7
<i>Relative Ranking</i>		# 28 / 157	# 31 / 179	# 38 / 179	# 36 / 179	# 39 / 179	# 38 / 179	# 41 / 179	# 52 / 183	# 54 / 178	# 33 / 178	# 44 / 178

Economic freedom in Armenia has overall slightly deteriorated between 2008 and 2018, and has in most years been considered “Moderately Free”, but in some years “Most Unfree” (2008 and 2017).²⁰⁸ The lowest rated indicators are ‘Judicial effectiveness’ and ‘Government integrity’, while the highest ratings are for ‘Tax burden’, ‘Trade Freedom’ and ‘Government Spending’.

Bertelsmann Foundation – Bertelsmann Transformation Index (BTI)

The BTI assesses how countries manage social change towards democracy and a market economy. It synthesizes findings of a study of transformation processes and political management into the Status Index, which assesses countries in terms of their path towards constitutional democracy and market economy flanked by socio-political safeguards, and the Governance Index which assesses the quality of political management.

Table 14 – BTI 2012-2018²⁰⁹

<i>(10: Highest, 1: Lowest)</i>	BTI 2012 (2011)	BTI 2014 (2013)	BTI 2016 (2015)	BTI 2018 (2017)	Overall Trend
Status Index	5.59	5.71	5.56	5.58	↔
Democracy Status	5.25	5.35	5.23	5.12	↓

absence of tariff and non-tariff barriers that affect imports and exports of goods and services. Investment Freedom: Constraints on the flow of investment capital. Financial Freedom: Banking efficiency as well as independence from government interference in the financial sector.

²⁰⁸ The index ranks countries with scores 100-80 as “Free”, 79.9-70 as “Most Free”, 69.9-60 as “Moderately Free”, 59.9-50 as “Mostly Unfree”, and 49.9-0 as “Repressed”.

²⁰⁹ BTI scores reflect the status in the previous year, i.e. the BTI 2012 assesses the status as of early 2011, and so on.

(10: Highest, 1: Lowest)	BTI 2012 (2011)	BTI 2014 (2013)	BTI 2016 (2015)	BTI 2018 (2017)	Overall Trend
Stateness	8.5	8.5	8.8	8.5	↔
Political Participation	4.0	4.5	4.5	4.3	↑
Rule of Law	4.8	4.8	4.3	4.5	↓
Stability of Democratic Institutions	3.0	3.0	3.0	3.0	↔
Political and Social Integration	6.0	6.0	5.7	5.3	↓
Market Economy Status	5.93	6.07	5.89	6.04	↑
Socioeconomic Level	4.0	4.0	4.0	4.0	↔
Market Organization	6.5	6.5	6.3	6.3	(↓)
Currency and Price Stability	7.0	7.0	7.0	7.5	↑
Private Property	8.0	8.0	8.0	7.5	↓
Welfare Regime	5.5	5.5	6.0	6.0	↑
Economic Performance	5.0	6.0	5.0	6.0	↑
Sustainability	5.5	5.5	5.0	5.0	↓
Status Index Ranking	# 66 of 128	# 62 of 129	# 64 of 129	# 61 of 129	↑
Governance Index	4.70	4.84	4.29	4.25	↓
Level of Difficulty	4.6	4.2	4.3	4.4	↓
Governance Performance	5.35	5.55	4.92	4.85	↓
Steering Capability	4.7	4.7	4.3	4.7	↔
Resource Efficiency	5.3	5.3	4.3	4.3	↓
Consensus-Building	4.4	5.2	5.0	4.4	↔
International Cooperation	7.0	7.0	6.0	6.0	↓
Governance Index Ranking	# 74 of 128	# 69 of 129	# 84 of 129	# 85 of 129	↓

The overall trend for Armenia in the development towards *democracy* is slightly negative (although it is noted that ‘Stateness’ indicator has remained at a high level). The *Market Economy Status* has improved slightly over the period with increases in three indicator values (‘Currency and Price Stability’, ‘Welfare Regime’ and ‘Economic Performance’). However, the *governance index* has deteriorated both in absolute and relative terms, and three of five indicator values have decreased (‘Level of Difficulty’, ‘Resource Efficiency’ and ‘International Cooperation’).

Freedom House – Freedom of the World Reports

The Freedom in the World report measures the degree of democracy and political freedom in 195 countries. The scores represent the levels of political rights and civil liberties with a corresponding classification as ‘Free’, ‘Partly Free’ or ‘Not Free’. The 2010-2017 results for Armenia are shown below.²¹⁰

Table 15 – Freedom House’s Freedom of the World

(1: Most free, 7: Least free)	Political Rights	Civil Liberties	Freedom Rating	Trend
2009 (2008)	6	4	Partly Free	↓
2010 (2009)	6	4	Partly Free	-
2011 (2010)	6	4	Partly Free	-
2012 (2011)	6	4	Partly Free	-

²¹⁰ The rankings reflect events in the previous year, i.e. 2012 refers to the status in 2011 and so on.

(1: Most free, 7: Least free)	Political Rights	Civil Liberties	Freedom Rating	Trend
2013 (2012)	5	4	Partly Free	↑
2014 (2013)	5	4	Partly Free	-
2015 (2014)	5	4	Partly Free	-
2016 (2015)	5	4	Partly Free	-
2017 (2016)	5	4	Partly Free	-
2018 (2017)	5	4	Partly Free	-
2019 (2018)	5	4	Partly Free	-

The freedom rating for Armenia has been ‘Partly Free’ throughout the period. The rating of ‘Political Rights’ improved from 2012 to 2013, but that of ‘Civil Liberties’ has remained unchanged throughout the period. However, Freedom House noted in its latest report that Armenia in 2018 “... *made a breakthrough with the victory of reform-minded leader Nikol Pashinyan in snap elections that were called after unpopular incumbent Serzh Sargsyan attempted to evade term limits and extend his rule*”.²¹¹

Freedom House’s press freedom ranking of Armenia for 2017 (latest report available) was no. 137 out of 198 countries, which means ‘Not Free’ and is unchanged compared to 2016.²¹² The Internet Freedom Status for Armenia was in 2018 deemed ‘Free’, which was “*after citizens successfully used social media platforms, communication apps, and live-streaming services to bring about political change in the country’s Velvet Revolution ...*”.²¹³ This is an improvement compared to the ‘Partly Free’ rating in 2017.

Freedom House – Nations in Transit

‘Nations in Transit’ is a research project on democracy in the 29 formerly communist countries from Central Europe to Central Asia. It includes an annual survey of democratic reform based on a checklist with questions covering seven categories.²¹⁴

Table 16 – Freedom House’s Nations in Transit

(1: Most democratic, 7: Least democratic)	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
National democratic governance	5.75	5.75	5.75	5.75	5.75	5.75	5.75	5.75	6.00	6.00
Electoral process	5.75	5.75	5.75	5.75	5.75	5.75	5.75	5.75	6.00	6.00
Civil society	3.75	3.75	3.75	3.75	3.75	3.75	3.75	3.75	3.75	3.75
Independent Media	6.00	6.00	6.00	6.00	5.75	5.75	5.75	5.75	5.50	5.50
Local democratic governance	5.50	5.50	5.75	5.75	5.75	5.75	5.75	5.75	5.75	5.75
Judicial framework and independence	5.50	5.50	5.50	5.50	5.50	5.50	5.50	5.50	5.50	5.50
Corruption	5.50	5.50	5.50	5.25	5.25	5.25	5.25	5.25	5.25	5.50
Democracy score	5.39	5.39	5.43	5.39	5.36	5.36	5.36	5.36	5.39	5.43

The democracy score has throughout the period characterized Armenia as a Semi-Consolidated Authoritarian Regime.²¹⁵ The most “democratic” indicator is ‘civil society’, the least are ‘national democratic governance’ and ‘electoral process’.

²¹¹ Freedom House. 2019. *Freedom in the World – Democracy in Retreat*. October, p. 15.

²¹² Freedom House. 2017. *Freedom of the Press 2017 – Press Freedom’s Dark Horizon*, April, p. 26.

²¹³ Freedom House. 2019. *Freedom on the Internet – The Rise of Digital Authoritarianism*. October, p. 5.

²¹⁴ The rankings reflect events in the previous year, i.e. 2011 refers to the status in 2010 and so on.

Reporters Without Borders' World Press Freedom Index

The World Press Freedom Index ranks press freedom based on questionnaires sent to partner organizations as well as journalists, researchers, lawyers and human rights activists.²¹⁶ The survey covers direct attacks on journalists and the media as well as other indirect sources of pressure against free press.

Table 17 – Reporters Without Borders' World Press Freedom Index

<i>A low grade means greater press freedom.</i>	No. of Countries	Ranking of Armenia	Grade	Trajectory
2008	173	102	22.75	↑
2009	175	111	31.13	↓
2010	178	101	27.50	↑
2011/12*	179	77	27.00	↓
2013	180	74	28.04	↓
2014	180	78	29.07	↓
2015	180	78	28.43	↑
2016	180	74	28.79	↓
2017	180	79	30.38	↓
2018	180	80	29.99	↑
2019	180	61	28.98	↑

Note: The 2011/12 index was based on a different methodology than that earlier applied, and allowed for negative grades and had a wider overall spread of scores (-10 to 142 compared to 115.5 in earlier years).

Press freedom in Armenia is assessed as having improved significantly from 2008 to 2013, and then again from 2018 to 2019 in both absolute and relative terms. This latest significant improvement was because the “*new media served as an echo chamber for the “velvet revolution” in the spring of 2018 that brought a former journalist to power*”.²¹⁷ However, Reporters Without Borders also noted that while the media landscape is diverse, it remains “*polarized and the editorial policies of the main TV channels coincide with the interests of their owners. In other words, journalistic independence and transparent media ownership continue to be major challenges.*”

Sources:

- Bertelsmann Stiftung – Bertelsmann Transformation Index: <http://www.bti-project.org/en/home/>.
- Cato Institute, Fraser Institute and Friedrich Naumann Foundation – Human Freedom Index: <https://www.cato.org/human-freedom-index>.
- Economist Intelligence Unit – Democracy Index: <http://www.eiu.com>.
- Freedom House – Freedom in the World: <http://www.freedomhouse.org/reports>.
- Freedom House – Nations in Transit: <https://freedomhouse.org/report-types/nations-transit>.
- Reporters Without Borders – World Press Freedom Index: <http://www.rsf.org/en>.
- The Fund for Peace – Failed States Index: <http://ffp.statesindex.org/>.
- The Heritage Foundation – Index of Economic Freedom: <http://www.heritage.org/index/download>.
- Transparency International – Corruption Perception Index (CPI): <http://www.transparency.org/>.
- World Bank Institute – Aggregate Governance Indicators: <http://info.worldbank.org/governance/wgi/index.aspx#home>.

²¹⁵ The Democracy Score defines five regime types – 1.00-2.99: Consolidated Democracy, 3.00-3.99: Semi-Consolidated Democracy, 4.00-4.99: Transitional Government/Hybrid Regime, 5.00-5.99: Semi-Consolidated Authoritarian Regime, and 6.00-7.00: Consolidated Authoritarian Regime.

²¹⁶ The nature of the survey's methodology (based on individual perceptions) can result in wide contrasts in a country's ranking from year to year.

²¹⁷ <https://rsf.org/en/armenia>.