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FOR ECONOMIC AND SOCIAL RESEARCH

# EU Integration Issues - Visegrad Countries and the South Caucasus

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**Authors:**

Temur Tordinava  
Elguja Khokrishvili  
Giorgi Kuparadze  
Natia Daghelishvili  
Michael Dzagania  
Otar Kikvadze  
Nana Maisuradze  
Shota Getia  
Krzysztof Senger  
Vugar Bayramov  
Hovsep Khurshudyan  
Karel Janda  
Grigorij Mesežnikov  
Tausz Katalin  
Ekin Özbakkaloğlu  
Irakli Javakhishvili  
Zaal Kvinchia

**Responsible Person for the publication:**

Temur Tordinava, Executive Director of Caucasian institute for economic and social research (CIESR)

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## *Foreword*

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The present book is published by the Caucasian Institute for Economic and Social Research (CIESR) within the framework of the project: The Visegrad Countries for the South Caucasian Countries EU Integration – V4 for C3 EU Integration. The work compiles analyses of the social and economic aspects of the European integration. The analytical articles analyse on-going reforms in the South Caucasus, as well as reform experience of the Visegrad countries on the way to the European integration. The book also includes the best articles identified on the bases of the competitions for students.

The term - The Visegrad Group refers to an alliance of four Central European countries - Czech Republic, Poland, Slovakia and Hungary. The goal of the cooperation of the Visegrad countries is to deepen regional cooperation and strengthen the processes of European integration.

This form of sub-regional cooperation, originated in the Hungarian town of Visegrad on 15 February 1991 at the initiative of Vaclav Havel, President of Czechoslovakia, created a successful example of integration with the European Union.

Although the Visegrad Group does not have a distinct structure as is the case of other regional or international organizations and has no permanent secretariat and staff, since the 90's it still became a symbol of successful regional cooperation. The only organized structure is an International Visegrad Fund (IVF) established in 2000. It supports development of the cooperation among the countries of the region in the fields of culture and science, research and education, trans-border cooperation and tourism. Recipients of the IVF grants mainly include non-governmental organizations. This fact underlines an importance of a role to be played by the civil society in strengthening regional cooperation among the countries.



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This form of cooperation among the countries of the Visegrad Group does not constitute an alternative to the EU. It is indeed supported by the EU as a format of sub-regional cooperation. Cooperation among the Visegrad countries contributes to the spread of common values, strengthening security and economic development through multilateral cooperation.

Similar to the Visegrad countries, the process of the European integration is a priority for one more region bordering the Eastern Europe – the states of the South Caucasus.

The South Caucasus countries strive for the successful economic and social transformation of their societies, the convergence with EU standards and the EU membership.

As it is well-known, EU offered a new form of cooperation in the form of the Eastern Partnership to 6 countries of the Eastern Europe (Armenia, Georgia, Azerbaijan, Belorussia, Moldova and Ukraine).

Eastern Partnership is not an alternative to the future EU membership, but it promotes deeper integration of the partner countries in the European Union and offers the participant countries assistance in implementing social and economic reforms. In this regard, experience of the Visegrad countries and specific aspects of the EU integration is an important example for the South Caucasus countries.

It is important to note that representatives of the non-governmental organizations and experts from seven countries participated in designing this book.

Organizations and experts involved in the project express their readiness to take into consideration all remarks and opinions voiced in connection with the materials presented in this book.

**Temur Tordinava**

Executive Director of Caucasian Institute  
for Economic and Social Research

# I. EURO INTEGRATION AND SOCIO-ECONOMIC POLICIES IN GEORGIA

## 1. Social Policy in Georgia

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**Temur Tordinava**  
**Executive Director of Caucasian**  
**Institute for Economic and Social Research**

**Shota Getia**  
**Analyst at Caucasian Institute**  
**for Economic and Social Research**

### 1.1 Introduction

*Social policy could be defined as the complex of social economic activities of the government, enterprises, organizations and local governments, directed to provision of population with welfare and equal access to incomes, livelihoods, healthcare, education and professionalism.<sup>1</sup>*

Social policy is gaining the increased importance in modern world, especially in EU countries. For example: Germany, France, Italy, Sweden, Denmark, Norway allocate significant funds from budget, for funding the social field. Unlike them, UK, USA, Canada, Australia envisage much less for social expenses, but this does not mean that social field is less developed or living standard is worse than in other countries.

EU countries are not on the same level of development and their social systems are not identical, but they have common values, in particular care for human welfare, provision of equal conditions for

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<sup>1</sup> Source Meyers Universal lexikon. Meyers Lexikonverlag. Mannheim. 2007.

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life and work, ensuring conditions for long and healthy life, as well as development of social solidarity among different regions, which means provision of support by rich countries to the poor.

Basic principle of implementation of social policy is the following:

- Providing support to the poorest families;
- Provision of unemployment benefits;
- Social insurance policy;
- Identifying minimal salary for employees and so on.

Social policy is one of the priorities for development of a prosperous state. Development of a national welfare model, means agreement between the state and society on mutual responsibility for identifying financial and social rights and duties. The main function of social policy is to regulate the private sector and community relations for the welfare of the people and for distribution of the resources necessary the process. Consequently, the identification of proper social welfare model its adjustment to public values is essential besides .considering its political and economic conjuncture. Implementation of active social policy taking into consideration the experience of other countries and sharing modern trends is important for Georgia.

The goal of the present research paper is assessment of major trends of social policy in Georgia for 2009-2012; there are several issues which need consistent policy implementation and timely solution of urgent topics.

## **1.2 The European Neighbourhood Policy and the social sphere**

The far-reaching goals set by the European Neighbourhood Policy, which are based on shared values and a commitment to effective

implementation of political, economic and institutional reforms. EU offers to intensify cooperation in several fields of social issues.

Social sector programs are under 3<sup>rd</sup> priority of the European Neighbourhood Policy - the five-year action plan (which is in force since November 2006). Priority 3 includes specific action, which means "implementation of the reforms social and health sector, including effective legal framework and effective management systems."<sup>2</sup> In addition, the actions of the European Neighbourhood Policy defined in the Action Plan include the social sector reform within poverty eradication measures, health care reform, and provision of the system for internally displaced people and refugees which aims their integration with local communities and improvement of livelihoods.

Social Security problem echoes the European Neighbourhood Policy Action Plan Chapter 4 (general goals and objectives) section 4.4 - "The economic and social reform, poverty reduction and sustainable development." The action plan includes the necessary steps in order to reduce poverty in the future. The measures for reduction the poverty level include the following areas:

1. Implementation of effective poverty reduction-oriented measures, which aim to reduce the number of persons below the poverty line and improve social equality, as well as the education and health systems and to improve the sustainability and access to other social services;
2. Further reform of the social security system, in particular, in terms of improving effectiveness of social protection and social welfare measures taking into consideration child care.

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<sup>2</sup>Source: [http://ec.europa.eu/world/enp/pdf/action\\_plans/georgia\\_enp\\_ap\\_final\\_en.pdf](http://ec.europa.eu/world/enp/pdf/action_plans/georgia_enp_ap_final_en.pdf)

Besides, directing effort to implementation of the standards defined by “EU Social Charter”: provision of basic rights of trade unions and basic labour standards, pursuant to ILO conventions ratified by Georgia.

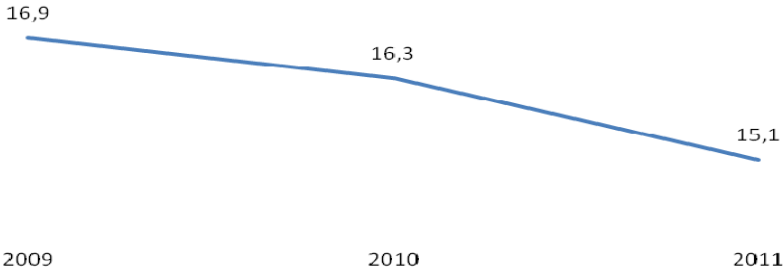
### **1.3. Tendencies of the labor market in Georgia in 2009-2011**

Unemployment is the problem of global nature. It is a condition when the workable person cannot be employed due to structural, political or social reasons. Employment means that person has allowance which is adequate to service or activity.

Employment of workable population and reduction of unemployment are key problems of economic growth and poverty reduction in Georgia. Low levels of household income conditions the low level of employment, which is associated with many negative social and economic consequences.

The problem of unemployment is much more painful than demonstrated by the official statistics. In spite active state employment policy implemented for many years, which means employment programs initiated by the government and businesses to stimulate the creation of new jobs, the unemployment problem is still urgent in our country.

Based on official data provided by Geostat, the unemployment has been decreasing since 2009 (see the chart #1)

**Chart № 1 Unemployment level 2009-2011 (%)**

*Source: National Statistics office of Georgia, [www.geostat.ge](http://www.geostat.ge)*

In 2011 number of unemployed people compiled 15,1% of workable population of Georgia. If we compare this figure to the norm determined by international organizations, this number is not disastrous. In 2009 – 2011 Georgian economy was growing rapidly, however this is not reflected on unemployment indicator and connection among them is weak. The indicator of economic growth was more than 6,5% in 2011, while unemployment was reduced only by 0,8%. In 2010 number of unemployed people in the country was more than 315 thousands and compiled 16,3% of economically active population (see the table 1).

**Table 1. distribution of the population of 15years and older by economic activities 2009-2011**

	2009	2010	2011
			Thousand persons
	<b>2009</b>	<b>2010</b>	<b>2011</b>
<b>Total active population (labour force)</b>	1991.8	1944.9	1959.3
<b>Employed</b>	1656.1	1628.1	1664.2
<b>Hired</b>	596.0	618.6	632.0
<b>Self employed</b>	1059.0	1007.1	1025.4

<b>Unclear</b>	1.2	2.4	6.8
<b>Unemployed</b>	335.6	316.9	295.1
<b>Population beyond labour force</b>	1139.3	1083.3	1045.9
<b>Unemployment level (percentage)</b>	<b>16.9</b>	<b>16.3</b>	<b>15.1</b>
<b>Active population in urban areas (labour force)</b>	857.0	847.8	839.5
<b>Unemployment level in urban areas (labour force)</b>	<b>28.8</b>	<b>27.2</b>	<b>26.5</b>
<b>Active population in rural areas (labour force)</b>	1134.8	1097.1	1119.8
<b>Unemployment in rural areas (in percentages)</b>	<b>7.8</b>	<b>7.9</b>	<b>6.5</b>

Unemployment in rural areas is 4 times less than in urban areas (28% and 7,8%). Compared to 2000 number of self-employment is increased by 45,7 thousands, i.e. by 5,6%; while in urban areas was decreased by 28,1 thousands i.e. 12,6%. Unemployment level these years increased in both urban and rural areas. After 2003 this increase in rural areas was in 1,8 and in urban areas just by 32%.<sup>3</sup>

Unemployment level in Georgia is in 1,6 more than in EU (10,0% and 16,3%). Only four EU countries have unemployment level higher than Georgia: Spain (20,2%) and Baltic countries (Estonia - 18,5%, Lithuania - 18,2%, Latvia - 19,4%). However, due to the fact that hired employment level is higher in these countries compared to Georgia (proportion 4/1) unemployment level is much severe in Georgia then in EU countries. Since 2003 the problem of hired employment was significantly solved in Georgia. To date average monthly salary is more than 600 GEL. In 2003 it was 128 GEL. Non resolution of employment problem means that in general number of jobs is not increased in the country and consequently

<sup>3</sup>Source: Geostat [www.geostat.ge](http://www.geostat.ge)

the level of unemployment is higher. The mentioned is caused by undeveloped market and lack of jobs.

Nowadays hundred thousands of active work forces have left Georgia. The latter is quite high number in comparing the whole employed people in Georgia. If not the high outflow of active workforce from Georgia official unemployment level would be much higher than official 16-17%.

#### **1.4 Social Provision System of Georgia**

Improvement of social economic condition of Georgia is impossible without implementation of the forms of relations that are popular in civilized part of the globe. Here we mean all forma of social economic relations between state and society as well as among the society members. One of them is social provision system, which is fundamental right of human; this is confirmed by articles 12 and 14 of European Social Charter, which is acknowledged as mandatory by Georgian legislation.

Pension system is serious problem of post soviet countries, since it is not able to ensure social provision of society, consequently the civilized states want to substitute state pension system with relatively perfect private pension system. In addition, the substitution process was continued over time and did not violate legal right of the community with regard to the freedom of choice.

The pension system of developed countries was established when the employees of retirement age compiled insignificant part of population and their provision with pension was not a problem. However, the situation changed radically after the completion of demographic process and existence of negligible contributions-based pension systems was impossible.



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Since becoming independent Georgia has been facing the problem of social security. Unlike 90s when the state was not able to issue even the smallest pensions, it should be noted that now it timely implements its obligations. However, the forms and volume of social security system is still symbolic.

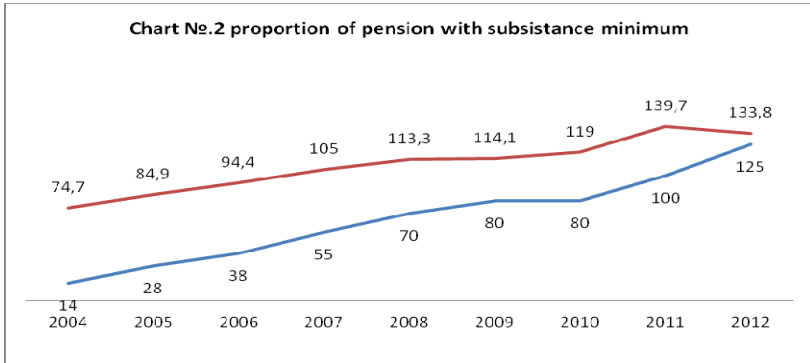
In Georgia the pension system consists of state pension system and newly established non state pension, but really just state pension system operates. The state pension system is based on the scheme of generations' solidarity, or distribution principle, which means distribution of tax payers' money to the pensioners. The state pension was monthly state payment until September 2012, received by Georgian citizens as well as by particular category without citizenship, residing on territory of Georgia legally for 10 years, due to pension age, disabilities, loosing breadwinner or any other reason.

Since September 2012, social package was defined for the other categories, received by particular category of Georgian citizens, in case of nonexistence of the grounds provided by the Law<sup>4</sup>.

It is interesting to see the proportion between state pension and subsistence minimum in dynamics of the years (see the chart)

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<sup>4</sup>Source: Social Service Agency [www.ssa.gov.ge](http://www.ssa.gov.ge)



**Source:** Geostat [www.geostat.ge](http://www.geostat.ge)

Diagram depicts the state pension and average consumer subsistence minimum dynamics in 2004-2012. We can see that the minimum wage is significantly higher than the level of the state pension, which means that the average pensioner is unable to satisfy the minimum wage requirements. In 2004, the ratio of pension to the subsistence minimum amounted to 0.18 . This means that the pensioner could satisfy only 18% of the needs. Please note that the minimum wage is necessary for satisfying the primary needs. In the last decade the ratio between the pension and the minimum wage gradually decreases.

According to the budget of 2013 , approved by the Parliament since April 1 all age pensions will become 125 GEL, while all pensioners receive 150 GEL from September 1, but this time the minimum wage is likely to grow. This is certainly a positive development, however, is far from the indicators, which sooner or later must be achieved in Georgia.

## 1.5 Progress reports of Georgia for 2009-2011 years in terms of European Neighborhood Policy

In February 2009 the government elaborated health care assistance programme for poor population. The beneficiaries are vulnerable and IDP families, registered in official database.

In February 2009 the state programme for rehabilitation of people with disabilities, elderly people and children was approved.

According to 2009 condition social benefit for unemployment was not envisaged. In March 2009 the programme was approved aiming at providing support to children that became victims of violence. In 2009 child care action plan was revised and particular activities were identified, to be implemented in 2009 – 2011.

**In 2010** economic recovery just slightly improved labour market, which was reflected only by insufficient reduction of unemployment - from 16, 9 in 2009 to 16, 3% in 2010. According to EU recommendations inconsistency between the skills and market demands should be eliminated.

In 2010 there was no general strategy of social sector. However, short term action plans were elaborated in particular fields, in particular regarding vulnerable children, people with disabilities, IDP and trafficking.

As for social assistance, in 2009 the government was implementing action plan for providing support to children, and in 2010 approved action plan for reforming child care system. In 2011-2012 the process of child welfare system was underway. In June 2010 poverty assessment mechanism was revised and new criteria for targeted

social assistance were elaborated. By means of mentioned criteria the families below poverty line should be identified.

In 2011 accurate data on poverty are not accessible. However, according to data of social service agency just one third of population is below poverty level.

In October 2011 the government published 10 point strategic plan on social economic policy of the country, which envisaged modernization and employment, including improvement of social policy.

The improvement of 2011 labour indicators was continued in 2012, which caused reduction of unemployment in 14,4% in 2012. However there are still difficulties on Georgian labour market, in particular: high level of structural unemployment, high level of unemployment in urban areas; high level of unemployment among the youth and increasing unemployment among people with high education, which develops inconsistency between supply and demand on labour market.

## **1.6 Conclusions**

Effective employment and unemployment are still pressing problems, which negatively affect the social situation of the population in Georgia. The problematic nature of the issue is complex. That is why it is important to outline the major themes that need to be resolved in a timely manner.

Over the years, the government carried out programs for employment and unemployment, but they never brought real results.

One of the main reasons of unemployment could be vocational education and training planning technologies. To date, education of

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population does not match with market requirements, due to professions that are ‘in fashion’.

Topical issues related to labour legislation, requiring further perfection are still urgent.

It is necessary for the state to employment the programs promoting creation of long-term jobs;

In order to solve the problem of unemployment it is necessary to prepare detailed analysis of the labour market, based on the real figures. Comprehensive analysis of the labour market of Georgia, based on objective data and comprehensive methodology is one of the most important issues to be solved.

It is desirable to analyse the experience of developed countries concerning the problem of unemployment and use it for solving the problem in Georgia.

It is necessary to reform the education sector. The modernization of the educational standards and improving the quality of higher education is necessary for meeting the requirements of labour market.

It is important to ensure compliance of Georgian labour legislation with ENP standards.

There's no doubt that there is the need for urgent reform of the pension system. Since existing pension system develops many problems to financial system and budget of Georgia.

Main gaps of Georgian pension system:

- Pensions are lower than subsistence minimum;

- Significant portion of the income of employees is not registered;
- Proportion of active employees with pensioners is not good.

Development and implementation of such model is real challenge, which will increase efficiency of country's pension system and facilitate to provision dignified old age of the elderly population.

In Georgia achievement of proper social provision is impossible without changes. In particular, it is essential to implement pension reform aiming at development of pension funds. The state shoals act important role in establishment and further development of private pension funds. That private funds should have dominating position in pension system of the country, since they ensure growth of national savings, investments and consequently of economy.

Social Charter of Europe, in particulate its article 12 and 14, is very urgent. Acknowledging these articles the state accepts responsibility to maintain social provision system and take measures for its further improvement.

Selection of the model of pension system is important issue in the process of reform, for this purpose international best practice should be used. In the result of analyses several possible models should be developed.

It is to be mentioned that interagency council is already developed for purpose to work on pension system issues. High officials of different agencies are members of the council. Main goal of the council is provision of recommendations for development of pension system. Deputy minister of sustainable development and deputy minister of health, vice state minister, vice president of national bank , chairperson of financial budget committee of the

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Parliament and deputy director of Geostat are the members of the council.

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## **2. Social Dialogue in Georgia and European Union (2009-2012)**

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**Temur Tordinava**  
**Executive Director of Caucasian Institute**  
**for Economic and Social Research**

**Ekin Özbakkaloğlu**  
**Research Fellow at Caucasian Institute**  
**for Economic and Social Research**

### **2.1 Introduction**

After the independence of Georgia, European Union (EU) emerged as an important partner as well as a significant model for Georgia in terms of establishing its statehood. As the first step of this new orientation, Georgia signed the Partnership and Cooperation Agreement with the European Union in April 1996 and started to make an effort to implement European treaties in different spheres to come closer to Europe. Following the Rose Revolution of 2003, the new Georgian leadership showed a renewed interest in becoming a part of wider Europe by pursuing a closer relationship with Euro-Atlantic partners. In 2004, Georgia joined the European Neighbourhood Policy initiated by the European Union to reinforce its relations with its neighbouring countries with the aim of promoting prosperity, stability, and security at its borders.<sup>5</sup> In 2009, the EU launched another initiative, the Eastern Partnership, in order to foster the necessary conditions to accelerate political association

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<sup>5</sup> European Neighbourhood Policy-Overview, European Union External Action Service, [http://eas.europa.eu/enp/index\\_en.htm](http://eas.europa.eu/enp/index_en.htm) (Accessed 13 January 2013)



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and further economic integration between itself and its Eastern neighbours including Georgia.<sup>6</sup>

As Georgia became closer to the European Union as well as wider European structures through these processes, the successive governments of Georgia assumed the responsibility to carry out extensive reforms in political, social, and economic sectors. With its goal to transform labour relations by ensuring effective communication between workers, employers, and the government; social dialogue is one of the most interesting issues that encompasses all of these sectors. In addition, post-communist context in Georgia offers a different experience and a different set of challenges concerning labour relations since it requires worker's unions, employer's associations, and the government to redefine their roles in a free market setting.

On the other hand, the practice of social dialogue is central for the European social model and industrial relations. As the "Communication from Commission: The European social dialogue, a force for innovation and change" argues; social dialogue is rooted in the history of the European continent as a distinguishing factor and it is a component of democratic government and of economic and social modernisation.<sup>7</sup> Thus, the developments regarding the progress of social dialogue in Georgia within the scope of its European commitments is an important aspect of Georgia's European integration. After defining the concept; this paper will discuss Georgia's obligations concerning social dialogue as a

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<sup>6</sup> The Eastern Partnership, EU Neighbourhood Info Center, <http://www.enpi-info.eu/eastportal/content//743/The%20Eastern%20Partnership> (Accessed 13 January 2013)

<sup>7</sup> Commission of the European Communities, Communication from the Commission: The European social dialogue, a force for innovation and change. Brussels, Belgium: 26 June 2002, p. 4 and p. 6.

condition of its European integration, summarize current developments, and analyse the problems in this field between 2009 and 2012.

## 2.2 What is Social Dialogue?

Social dialogue is a formalized set of labour relations between representatives of employers, workers, and the government that seeks to provide a platform for communication in order to protect the interests of all parties and to resolve disputes. Ideally, social dialogue will ensure effective communication among parties and help them to reach agreements based on consensus. As Gogelashvili points out, “[t]he main goal of social dialogue is to establish labour relations based upon equality and democratic values.”<sup>8</sup>

According to the International Labour Organization (ILO), social dialogue encompasses “all types of negotiation, consultation and exchange of information between, or among, representatives of governments, employers and workers on issues of common interest.”<sup>9</sup> The ILO also identifies social dialogue as the most suitable tool for promoting better living and working conditions and greater social justice as well as an instrument that enhances governance.<sup>10</sup>

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<sup>8</sup> Levan Gogelashvili. “Labour Market and Social Dialogue in Georgia” in *Moving Closer to Europe? Economic and Social Policies in Georgia, Armenia and Azerbaijan*. Tbilisi, Georgia: The Centre for Economic Problems Research and Friedrich-Ebert-Stiftung, 2010, p. 119.

<sup>9</sup> Social Dialogue, International Labour Organization. <http://www.ilo.org/global/about-the-ilo/decent-work-agenda/social-dialogue/lang--en/index.htm> (Accessed 13 January 2013)

<sup>10</sup> Social Dialogue Sector, International Labour Organization. <http://www.ilo.org/public/english/dialogue/index.htm> (Accessed 13 January 2013)

Social dialogue is an important notion for the European Union that finds its source in the very basis of European ideals. In Europe, institutionalized labour relations and social dialogue are indispensable elements of market economics as well as the European social model.<sup>11</sup> According to European Commission, “European social dialogue refers to discussions, consultations, negotiations and joint actions involving organisations representing the two sides of industry (employers and workers).”<sup>12</sup> In European Union law, the term social dialogue is mentioned in the “Treaty on the Functioning of European Union” which came into force in December 2009. According the Article 152 of the Treaty, “[t]he Union recognises and promotes the role of the social partners at its level, taking into account the diversity of national systems. It shall facilitate dialogue between the social partners, respecting their autonomy.”<sup>13</sup> In line with this provision, the European Commission asserts that social dialogue includes “both the bipartite and the tripartite processes between the European social partners themselves and between the two sides of industry and the Commission.”<sup>14</sup> European social dialogue can take two different forms. A tripartite dialogue involves public authorities while a bipartite dialogue takes place between employers or employer associations and trade union organisations.

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<sup>11</sup> Paata Beltadze. “Status of the Social Dialogue in Georgia” in *Eastern Partnership and Convergence with EU Policies in Georgia*. Tbilisi, Georgia: Georgian Foundation for Strategic and International Studies, 2012, p. 69.

<sup>12</sup> Social Dialogue, Employment, Social Affairs, and Inclusion, European Commission. <http://ec.europa.eu/social/main.jsp?catId=329&langId=en> (Accessed 13 January 2013)

<sup>13</sup> Consolidated Version of Treaty on the Functioning of the European Union, 9 May 2008. <http://eurlex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:C:2008:115:0047:0199:EN:PDF> (Accessed 24 December 2012)

<sup>14</sup> Treaty on the Functioning of the European Union, European Foundation for the Improvement of Living and Working Conditions. <http://www.eurofound.europa.eu/areas/industrialrelations/dictionary/definitions/treatyonthefunctioningoftheeuropeanunion.htm> (Accessed 26 December 2012)

In compliance with the diversity concerning the practices of social dialogue explicitly recognized by the European Commission, three different forms of social dialogue can be identified in Europe. The first model is “institutionalized tripartism” practiced mainly in Belgium, Netherlands, Ireland, Finland, and Austria. These countries have tripartite mechanisms that meet on a regular basis to reach agreements on various issues concerning labour relations. The second model is a “flexible combination of bilateral and trilateral relations” that includes bipartite relations within a sector in the form of collective negotiations between employers and workers and separate relations with state authorities that usually result in the signing of joint documents. France, Spain, Italy, and Portugal adopted social dialogue systems that can be defined as this second model. Finally, the third model practiced in the United Kingdom is “pragmatic and coincidental tripartism.” Depending on the nature of the problem, all three parties engage in negotiations without establishing a permanent mechanism of social dialogue.<sup>15</sup>

### **2.3 Social Dialogue and Georgia-EU Relations**

The importance attached to social dialogue by the European Union as a European value resulted in its inclusion in major documents that outline Georgia’s commitments to the EU in order to achieve European integration. Arguably, the European Neighbourhood Policy is the cornerstone of Georgia-EU relations because it provides a general framework for cooperation as well as a clear set of priority areas that Georgia has to address in order to fulfil its European aspirations. As the essential document that summarizes these areas, the EU/Georgia Action Plan adopted in November 2006 includes a general provision that directly relates to social dialogue.

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<sup>15</sup> The classification and information in this paragraph is cited from Beladze’s work on European models of social dialogue. Beladze, *op.cit.*, pp. 69-72.

The “Political Dialogue and Reform” section of the Action Plan includes a sub-section that enumerates actions that need to be taken by Georgia in order to ensure “respect for human rights and fundamental freedoms.” Under this sub-section, Georgia commits to continuing its efforts “to ensure implementation of the standards set in the European Social Charter and ensure trade union rights and core labour standards in accordance with relevant ILO conventions as ratified by Georgia”<sup>16</sup>

In fact, Georgia had a long history of cooperation with the International Labour Organization that precedes its involvement in the European Neighbourhood Policy. Georgia joined the ILO in 1993 and ratified 16 conventions between 1993 and 2002.<sup>17</sup> The International Labour Organization has been working with state authorities, trade unions, and employers in order to initiate necessary reforms to apply international standards to labour legislation in Georgia.<sup>18</sup> In addition, Georgia’s involvement in the Generalized System of Preferences of the European Union dictates that the country fully satisfies main principles of labour standards set out by the ILO.

Similarly, Georgia ratified the European Social Charter in August 2005 by accepting 63 of the Revised Charter’s 98 paragraphs.<sup>19</sup>

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<sup>16</sup> Ensuring Respect for Human Rights and Fundamental Freedoms, 4.1 Political Dialogue and Reform, General Objectives and Actions, EU/Georgia Action Plan. [http://ec.europa.eu/world/enp/pdf/action\\_plans/georgia\\_enp\\_ap\\_final\\_en.pdf](http://ec.europa.eu/world/enp/pdf/action_plans/georgia_enp_ap_final_en.pdf) (Accessed 25 December 2012)

<sup>17</sup> List of Ratification of International Labour Conventions-Georgia. <http://webfusion.ilo.org/public/applis/appl-byCtry.cfm?lang=EN&CTYCHOICE=0230&hdroff=1> (Accessed 14 January 2013)

<sup>18</sup> Beladze, *op.cit.*, p. 82.

<sup>19</sup> Department of the European Social Charter and the European Code of Social Security, Georgia and the European Social Charter, March 2012. [http://www.coe.int/t/dghl/monitoring/socialcharter/CountryFactsheets/Georgia\\_en.pdf](http://www.coe.int/t/dghl/monitoring/socialcharter/CountryFactsheets/Georgia_en.pdf) (Accessed 14 January 2013)

According to the report of the European Committee of Social Rights, Georgia joined the European Social Charter by ratifying only the minimum required number of provisions. However, the Committee meets with the representatives of the Georgian government to exchange information on the non-accepted provisions every five years and the next meeting will take place in 2015.<sup>20</sup>

Meanwhile, with its participation in the European Neighbourhood Policy and Eastern Partnership, Georgia renewed its commitment to European Union to accept the standards set in the European Social Charter and ILO conventions. As the Eastern Partnership Roadmap for 2012-13 identifies developing social dialogue and social partnerships as an objective, Georgia will need to intensify its efforts to foster social dialogue in order to further pursue its European integration agenda.<sup>21</sup>

## 2.4 Developments in Social Dialogue in Georgia: 2009-2012

Prior to 2008, social dialogue in the context of labour relations did not exist on an institutional level in Georgia. As Gogelashvili pointed out, “contacts between the parties to labour relations had an individual nature and lacked any systemic regulation.”<sup>22</sup> However, the developments that took place at the end of 2008 initiated the institutionalization of social dialogue in Georgia.

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<sup>20</sup> European Committee for Social Rights, First Report on the Non-Accepted Provisions of European Social Charter-Georgia, European Committee of Social Rights, 21 May 2012, pp. 3-4. [http://www.coe.int/t/dghl/monitoring/socialcharter/non-acceptedprov/Georgia2012\\_en.pdf](http://www.coe.int/t/dghl/monitoring/socialcharter/non-acceptedprov/Georgia2012_en.pdf) (Accessed 12 January 2013)

<sup>21</sup> European Commission, Eastern Partnership Roadmap 2012-13: the multilateral dimension, 15 May 2012, p. 11. [http://ec.europa.eu/world/enp/docs/2012\\_enp\\_pack/e\\_pship\\_multilateral\\_en.pdf](http://ec.europa.eu/world/enp/docs/2012_enp_pack/e_pship_multilateral_en.pdf). (Accessed 14 January 2013)

<sup>22</sup> Gogelashvili, op.cit., p. 120.

With the efforts of the International Labour Organization, a tripartite group was established in 2008 after the appointment of A. Kvitashvili as the new Minister of Health, Labour and Social Affairs.<sup>23</sup> In October 2008, the group comprised of the representatives of the government, Employers' Association, and the Confederation of Trade Unions issued an agreement outlining a work plan they elaborated. According to the Tripartite Agreement; social partners mainly agreed to meet at least biweekly to discuss the current socio-economic situation and to solve raised problems, to discuss legislative initiatives connected to social and economic issues, and to develop activities in order to make progress concerning Labour Code as well as Collective Bargaining and Freedom of Association. Also, the decisions of the group would be taken into account by the government as recommendations.<sup>24</sup>

For a while, the work of the tripartite group focused on changing the labour legislation of Georgia and the representatives of the Georgian government agreed to adopt amendments to the Labour Code at the ILO Conference held in Geneva in June 2009. Although this agreement did not materialize once the delegations returned to Georgia, the government moved to institutionalize the tripartite group as the Tripartite Commission at a round table meeting in October 2009. On November 12, 2009, a decree issued by the Prime Minister established the Tripartite Commission on Social Dialogue.<sup>25</sup> Finally, on March 2, 2010, the Prime Minister of Georgia issued the decree on the "Approval of Social Partnership Trilateral Commission

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<sup>23</sup> Marina Muskhelishvili. *Social Dialogue in Georgia*. Tbilisi, Georgia: European Union and Friedrich-Ebert-Stiftung, 2011, p. 18.

<sup>24</sup> Tripartite Agreement, 31 October 2008, <http://gtuc.ge/en/pressandpublications/88> (Accessed 14 January 2013)

<sup>25</sup> Information in this paragraph is from Marina Muskhelishvili's work. Muskhelishvili, op.cit., pp. 18-19.

Regulations and Structure” that ratified the charter of the Tripartite Commission elaborated by a team of experts.<sup>26</sup>

Accordingly, the Tripartite Commission is chaired by the Minister of Health, Labour and Social Affairs of Georgia.<sup>27</sup> The Georgian Government, Union of Employers, and Trade Unions are represented at the Tripartite Commission by several representatives. The Tripartite Commission’s functions include the promotion of social partnership in Georgia and social dialogue among the government, workers and employers; and, the development of proposals and recommendations concerning labour relations.<sup>28</sup>

The Tripartite Commission held its first meeting in May 2010 with the participation of a delegation from the International Labour Organization. However, the work of the Commission was quickly blocked by disagreements concerning the agenda of the meetings and sending appeals to the ILO and EU instead of working to reach a consensus concerning the Labour Code. After a slow start in 2010, the Tripartite Commission started to work more systematically in 2011, but the similar operational problems continued to affect its functioning.<sup>29</sup> In her report, Muskhelishvili argues that “the meetings of the Tripartite Commission soon looked like senseless repetition of already declared positions.”<sup>30</sup> Similarly, International Trade Union Confederation and European Trade Union Confederation argue that “the commission has not solved a single issue and none of the

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<sup>26</sup> Beladze, *op.cit.*, p. 66.

<sup>27</sup> Davit Narmania et al. *Eastern Partnership and Socio-Economic Policy of Georgia*. Tbilisi, Georgia: Caucasian Institute for Economic and Social Research (CIESR), Centre for Economic Problems Research (CEPR), Open Society Georgia Foundation (OSGF), 2011, p. 20.

<sup>28</sup> Gogelashvili, *op.cit.*, p. 120.

<sup>29</sup> Beladze, *op.cit.*, p. 67.

<sup>30</sup> Muskhelishvili, *op.cit.*, p. 19.



decisions and recommendations taken thereof have been acted upon” since its establishment two and a half years ago.<sup>31</sup>

Meanwhile, labour relations in Georgia continued to experience tensions. Annual Survey of Violations of Trade Union Rights published by the International Trade Union Association cites various examples of anti-union discrimination and violations of labour rights. A wave of strikes took place in 2012, influenced by the political dynamics of the election cycle. Mine workers in Chiatura went on strike demanding an increase in wages.<sup>32</sup> Similarly, workers of the Poti Port and of Georgian Railways organized strikes to improve their working conditions and salaries.<sup>33</sup> In 2011, Hercules Steel Plant in Kutaisi fired trade union activists and the strike initiated by workers after this incident was forcefully ended by the police. The LTD “Georgian Railway” pressured its employees to refrain from union activities and the railway administration disregarded recommendations of the Tripartite Commission that urged parties to engage in collective bargaining to resolve their dispute.<sup>34</sup> Similarly,

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<sup>31</sup> International Trade Union Confederation and European Trade Union Confederation, *A Roadmap for Georgia*. Brussels: October 2012, p. 10. [http://www.ituc-csi.org/IMG/pdf/ituc\\_roadmap\\_for\\_georgia\\_final.pdf](http://www.ituc-csi.org/IMG/pdf/ituc_roadmap_for_georgia_final.pdf) (Accessed 16 January 2013)

<sup>32</sup> Hundreds of Miners Went on Strike in Western Georgia, *Georgia Times*, 15 October 2012. <http://www.georgiatimes.info/en/news/81818.html> (Accessed 16 January 2013)

<sup>33</sup> Strike in Poti Port, *Georgian Trade Union Organization*, 25 October 2012. <http://www.gtuc.ge/en/component/content/article/12-front-page-items/646-2012-10-25-12-36-04> (Accessed 16 January 2013)

More Workers Join Wave of Strikes in Georgia, *Democracy and Freedom Watch*, 24 October 2013. <http://dfwatch.net/more-workers-join-wave-of-strikes-in-georgia-54264> (Accessed 16 January 2013)

<sup>34</sup> International Trade Union Confederation, *2012 Annual Survey of Violations of Trade Union Rights - Georgia*, 6 June 2012. <http://www.unhcr.org/refworld/docid/4fd8894ec.html> (Accessed 25 December 2012)

in 2010, workers were dismissed from the Geo-Steel metallurgical plant for organising a union.<sup>35</sup>

The Office of the State Minister on European and Euro-Atlantic Integration issues annual reports that assess Georgia's progress in implementing the ENP Action Plan. The Ministry's 2009 Progress Report explains the events that paved the way to the establishment of the Tripartite Commission and emphasizes the International Labour Organizations involvement in the process through provision of technical and advisory support. In addition, the Report underlines that Georgia ratified all 8 fundamental conventions and that the government carefully studies all recommendations and observations received from the ILO.<sup>36</sup> The Ministry's 2010 and 2011 Progress Reports repeat some of the detailed information from the previous year's report concerning the establishment of the Tripartite Commission and the 2010 Report asserts that the "Government of Georgia will actively work to further promote constructive social dialogue and discuss labour and social related issues with social partners."<sup>37</sup>

As opposed to progress reports from the Office of the State Minister on European and Euro-Atlantic Integration, Progress Reports issued by the European Union provide a more balanced narrative of the developments concerning the Tripartite Commission. The 2009 Progress Report states that:

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<sup>35</sup> International Trade Union Confederation, 2011 Annual Survey of violations of trade union rights – Georgia, 8 June 2011. <http://www.unhcr.org/refworld/docid/4ea6620dc.html> (Accessed 25 December 2012)

<sup>36</sup> Office of the State Minister of Georgia on European and Euro-Atlantic Integration, Georgia's Progress Report on Implementation of the ENP Action Plan in 2009, February 2010, p. 37.

<sup>37</sup> Office of the State Minister of Georgia on European and Euro-Atlantic Integration, Georgia's Progress Report on Implementation of the ENP Action Plan 2010, p. 56.

“The social dialogue of October 2009 led to the issuing in November 2009 of a Decree institutionalising the tripartite National social dialogue commission. A working group was created to review and analyse the legislation’s conformity with ILO core conventions and to draft the charter of the newly established social dialogue commission. The commission’s charter defines its role, functioning and objectives, remains to be finalised.”<sup>38</sup>

In contrast to the previous year’s report, the 2010 Progress Report voices some concerns regarding the anti-union discrimination and non-compliance with the International Labour Organization’s core labour standards. The Report explains that the Commission agreed to introduce minimum changes to the Labour Code, particularly about anti-union discrimination, but the Georgian Trade Union Conference is claiming that the government practices anti-union discrimination and interferes in social dialogue.<sup>39</sup> As to core labour standards, the 2010 Progress Report states that the ILO is concerned about the lack of compliance with core labour convention by Georgia and warns that “these concerns put at risk Georgia’s continuing inclusion in the EU’s General System of Preferences (GSP+).”<sup>40</sup>

Finally, the 2011 Progress Report briefly states that the tripartite social dialogue meeting took place regularly. However, as opposed to the progress reports from the Ministry of European and Euro-Atlantic Integration of Georgia that focus on the number of meetings that took place, the 2011 Progress Report stresses that the process fell short of delivering “in practice a functioning and mutually agreed

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<sup>38</sup> Office of the State Minister of Georgia on European and Euro-Atlantic Integration, Georgia’s Progress Report on Implementation of the ENP Action Plan in 2009, February 2010, p. 10.

<sup>39</sup> Implementation of European Neighbourhood Policy in 2010, Country Report: Georgia. Brussels, Georgia: 25 May 2011, p. 10.

<sup>40</sup> *Ibid.*, p. 3.

mediation mechanism between employers (including the government as employer) and trade unions.”<sup>41</sup>

*Problems concerning Social Dialogue in Georgia: 2009-2012*

The progress of social dialogue in Georgia, especially the establishment of the Tripartite Commission is a positive development. However, serious problems continue to hinder this process as they prevent effective social dialogue between the government, employers, and workers from taking place. This section will outline the major problems that need to be addressed in order to facilitate social dialogue in Georgia.

The first obstacle that stands in the way of social dialogue is the Labour Code of Georgia promulgated in 2006. The preparation process of the Code itself bore witness to the lack of social dialogue in Georgia as the government did not reach an agreement with the trade unions prior to ratification.<sup>42</sup> The Labour Code of 2006 radically liberalized the labour market to the detriment of worker’s rights. This approach was in contradiction with Georgia’s commitments to the International Labour Organization as well as the European Union. According to a report from 2008, the code violates several international labour standards, especially standards on freedom of association and on the right to organise and collective bargaining.<sup>43</sup>

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<sup>41</sup> Implementation of the European Neighbourhood Policy in Georgia, Progress in 2011 and recommendations for action. Brussels, Belgium: 15 May 2012, p. 9.

<sup>42</sup> Muskhelishvili, op.cit., p. 10.

<sup>43</sup> International Trade Union Confederation, Georgia: labour code tears fundamental rights to shreds. Union View, No. 9, May 2008, p. 3. <http://www.ituc-csi.org/georgia-labour-code-tears.html?lang=en> (Accessed 8 January 2013)

The most problematic provisions of the Labour Code are articles 5(8), 37(d) and 38(d). When interpreted together, they allow the employer to dismiss an employee without any grounds or prior notice after paying the equivalent of one month's salary. As a result, employers can dismiss workers for their trade union activity and practice anti-union discrimination.<sup>44</sup> According to the 2012 Annual Survey of Violations of Trade Union Rights published by the International Trade Unions Association, "Georgia has become one of the worst cases in Europe as far as the rights of workers are concerned."<sup>45</sup>

The progress reports issued by the European Union also insistently recommend that the Labour Code be amended. The 2010 Progress Report asserts that "[t]he Labour Code and the Law on Trade Unions need to be amended in order to comply with core labour standards, notably regarding the criteria for establishing trade unions, protection against anti-union discrimination, the right to strike."<sup>46</sup> Similarly, the 2011 Progress Report warns that "Georgia is still expected to address several of them, notably with regard to legislative amendments to the Law on Trade Unions and the Labour Code."<sup>47</sup> Apart from the Labour Code, the European Union is also concerned with Georgia's implementation of ILO conventions. The 2011 Progress Report warns that "[t]he issue of labour rights continues to be a serious concern, including the insufficient implementation of core ILO conventions, in particular No 87 on Freedom of association and

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<sup>44</sup> Muskhelishvili, op.cit, pp. 10-11.

<sup>45</sup> International Trade Union Confederation, 2012 Annual Survey of Violations of Trade Union Rights - Georgia, 6 June 2012.

<sup>46</sup> Implementation of European Neighbourhood Policy in 2010, Country Report: Georgia. Brussels, Georgia: 25 May 2011, p. 10.

<sup>47</sup> Implementation of the European Neighbourhood Policy in Georgia, Progress in 2011 and recommendations for action. Brussels, Belgium: 15 May 2012, pp. 9-10.

protection of the right to organise and No 98 Right to organise and collective bargaining.”<sup>48</sup>

Another problem about social dialogue and Georgia’s European commitments relates to the European Social Charter. The periodic reports issued by the European Committee of Social Rights assess the compliance of Georgia with the Charter’s provisions. The Conclusions 2010 Report that addresses labour rights found 6 cases of non-conformity with the Charter’s provisions. The most important cases of non-conformity for social dialogue are Article 5 (Right to organise) and Article 6 (Right to bargain collectively). For Article 5, the commission concluded that the situation in Georgia is not in conformity with the European Social Charter on the grounds of “the excessive number of members required to establish a trade union; the restrictions on the right to organise that may be included in employment contracts; and the insufficient protection against discrimination based on trade union membership in the context of recruitment and dismissal.”<sup>49</sup> For Article 6, the commission stated that Georgia is not in conformity with “Article 6§2 on the ground that it has not been established that an employer may not unilaterally disregard a collective contract and that the conclusion of collective agreements is promoted” and “with Article 6§3 on the ground that there is no effective conciliation, mediation or arbitration service.”<sup>50</sup>

Incompliance with international and European norms serves as a way to weaken the influence of trade unions. As Muskhelishvili explains, trade unions are subject to strong pressure because they have a broad social basis, international support, and possible influence on economic policy. Particularly, cases of terminating collective

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<sup>48</sup> Ibid., p. 9.

<sup>49</sup> European Committee of Social Rights, Conclusions 2010 (GEORGIA) Articles 2, 4, 5, 6, 26 and 29 of the Revised Charter, December 2010, p. 11.

<sup>50</sup> Ibid., p. 14 and p. 15 respectively.

contracts, employers refusing to collect membership deductions, pressuring and dismissing trade union members have become frequent strategies used against trade unions.<sup>51</sup> This situation influences social dialogue processes negatively as one of the major partners of the dialogue is subject to constant pressure. In turn, this undermines the work of the Tripartite Commission as social partners cannot cooperate with each other in good faith.

In short, the main problem regarding the development of social dialogue in Georgia is the difference between Georgia's commitments to the European Union through various mechanisms and their implementation within the country. Mainly, the compliance with core labour rights recognized by the ILO and the provisions of the European Social Charter by changing relevant legislation such as the Labour Code can unblock the Tripartite Commission's work. As Muskhelishvili argues, the establishment of the Tripartite Commission by itself does not mean that the policy of mutual ignoring and confrontation to the dialogue between social partners has changed.<sup>52</sup> The problems explained in this section need to be addressed in order to further social dialogue in the country in conformity with its commitments to the European Union.

## 2.5 Conclusions

The progress of social dialogue in Georgia between 2009 and 2012 is a positive development. Especially, the establishment of the Tripartite Commission and its regular meetings are important steps that can further encourage institutionalization of social dialogue as well as making it an essential element of industrial relations in Georgia. However, the development of social dialogue has not been a

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<sup>51</sup> Muskhelishvili, *op.cit.*, p. 14.

<sup>52</sup> *Ibid.*, p. 20.

smooth process that lacks setbacks. The Tripartite Commission continues to lack effectiveness as the parties to social dialogue are not being fully cooperative with each other. Most importantly, the Labour Code promulgated in 2006 continues to undermine the development of effective social dialogue by empowering the employer side to the detriment of employees and unions. This unbalance weakens trade unions, violates the right to association and undermines social dialogue efforts.

It is also important to stress that the engagement of international community, especially of European Union and International Labour Organization have motivated the Georgian government to take positive steps in order to ensure effective social dialogue. These organizations and their involvement in the development of tripartism in Georgia guaranteed the continued interest on the part of the government to engage in social dialogue. Although the legal provisions and practices that contradict with Georgia's international obligations are not eliminated yet, the possibility to further the process of social dialogue exists. The change in government may provide new opportunities for the parties of social dialogue to cooperate if the government demonstrates the political will to take concrete steps in this area.

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### **3. The Deep and Comprehensive Free Trade Area (DCFTA) with EU**

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**Elguja Khokrishvili**

**Economic Expert**

**Natia Daghelishvili**

**Expert-Analyst at Caucasian Institute for Economic and Social Research**

#### **3.1 Introduction**

The strategy of action of the country is based on economic integration with EU, since EU market has no alternative in qualitative and quantitative terms. EU integration became especially after the Russian embargo, as a result of which we lost access to market of the biggest trade partner.

Relations between Georgia and EU are characterized by the following chronology:

First step in economic relations between Georgia and EU were made with concluding Partnership and Cooperation Agreement (PCA), which came into force in 1999. The PCA abolishes quotas in trade and protects the rights on intellectual, industrial and commercial property.

In 2004 European Neighbourhood Policy (ENP) was developed. It aimed at removal of new dividing lines between Europe and its new neighbours<sup>53</sup> and provision of stability, safety and welfare.

In December of 2005 Georgia obtained the right to use Generalized System for Preferences (GSP+). GSP+ envisages the release of goods exported from Georgia to EU from customs taxes and unilateral reduction of tariffs. Mentioned preferences do not apply to 7200 types of products produced in Georgia.

On 7 April 2009, at the Summit of Prague initiative of “Eastern Partnership” (EaP), between EU and six partner countries (Armenia, Azerbaijan, Belarus, Georgia, Moldova and Ukraine) officially came into force, facilitating political association and further economic integration. Bilateral cooperation between EU and partner country within the frame of Eastern Partnership, will be developed in following direction: 1) agreement and adoption of DCFTA; 2) movement and safety; 3) energy security; 4) facilitating economic and social development.

Free trade means trade without customs tariffs and quotes, while DCFTA removes non tariffs barriers in the trade process, which is essential for equal conditions and common “game rules” among trade partners. Let’s pay attention to mentioned term and differentiate from bilateral and multilateral track with EU<sup>54</sup>.

Multilateral track – represents the framework within the frame of which EU and Eastern partners work together in group, on resolution of common issues. Multilateral format serves for implementation of

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<sup>53</sup> In 2004 Lithuania, Latvia, Estonia, Check Republic, Slovakia, Slovenia, Hungary, Poland, Malta and Cyprus

<sup>54</sup> *Eastern Partnership and Social Economic Policy of Georgia; Caucasus Economic and Social Research Institute (CIESR), Tbilisi, 2011.*

the goals of Eastern Neighbourhood, by means of four thematic platforms (democracy, complete system for management and stability; economic integration and convergence with EU sector economic policy, including establishment of free trade zones; energy security and development of contacts among people) and 6 flagman initiatives<sup>55</sup>.

Bilateral track – the goal of bilateral track is improvement of relations among EU and each Eastern partner. This could be achieved with the help of bilateral agreements for example: agreement on association, DCFTA, bilateral dialogue on simplifying visas; closer cooperation and technical assistance in different sectors (economy, energy, environment, transport, research and so on). Eastern partnership is being implemented together with the relations of bilateral agreements. Its implementation depends on the difference between partners and conditions developed for them<sup>56</sup>.

In difference from other agreements, Georgia has concluded with various countries, DCFTA means liberalization of trade in both goods and services. It is to be mentioned that similar trade regime operates only between EU and South Chorea, besides the negotiation process is finalized between EU and Ukraine.<sup>57</sup>

According to the decision of both parties, in the process of negotiations for giving full effect to DCFTA regime, all documents are closed and negotiations on particular chapters are non public. The document consists of main text and annexes, where the list of European legislation is provided, harmonization with which is commitment of Georgia.

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<sup>55</sup> Thanks to flagship initiatives funding is obtained from different international institutions and investments are attracted from private sector.

<sup>56</sup> ENP Glossary, [http://www.enpi-info.eu/main.php?id=403&id\\_type=2](http://www.enpi-info.eu/main.php?id=403&id_type=2)

<sup>57</sup> Negotiation process with Ukraine was continued for about 4 years

The document about DCFTA consists of the following 14 chapters:

1. Trade in goods;
2. Rules for origin of goods;
3. Customs and trade facilitation;
4. Instructions defending trade;
5. Trade in services;
6. Sanitary and phytosanitary measures;
7. Technical barriers in trade;
8. Intellectual property rights;
9. Trade and sustainable development;
10. Competition;
11. Public procurement;
12. Energy;
13. Transparency;
14. Dispute resolution.

It is to be mentioned that conclusion of DCFTA will be Georgia's next step to gradual convergence with EU legislation and standards; which will follow several agreements concluded with EU in different fields, among them:

- Partnership for mobility;
- Visa facilitation and readmission;
- Visa dialogue;
- Agreement on common aviation area

Above mentioned demonstrates great importance of EU neighbourhood policy and Eastern Partnership initiatives.



### 3.2 Assessment of Current Situation

Trade always had special place in relations of EU and Georgia. EU is the most important trade partner for Georgia. In 2012 external trade turnover of Georgia compiled 10 220 million USD, out of which turn over with EU countries was 2780 million USD; which is in 12% more compared to figures of previous year. Georgia's share of export to EU countries compiles 15% in total export and – 31% in import.<sup>58</sup>

EU made decision on starting negotiations with Georgia on DCFTA on 5 December 2011. The negotiations officially opened on 28 February 2012, during Mr. Karel De Gucht's visit to Georgia. According to him DCFTA facilitates Georgia to become more competitive and capable to use EU internal market<sup>59</sup>.

Negotiations process on DCFTA covers 6 rounds:

- 1<sup>st</sup> round of DCFTA negotiations took place on 27-29 March in Tbilisi;
- 2<sup>nd</sup> round of DCFTA negotiations took place on 26-28 June in Brussels;
- 3<sup>rd</sup> round of DCFTA negotiations took place on 25-27 September in Tbilisi;
- 4<sup>th</sup> round of DCFTA negotiations took place on 26-30 November in Brussels;
- 5<sup>th</sup> round of DCFTA negotiations took place on 29-31 January in Tbilisi;
- 6<sup>th</sup> round of DCFTA negotiations is planned on 18-22 March, 2013.

<sup>58</sup> Geostat <http://www.geostat.ge/>

<sup>59</sup> According to data of January 2011 EU population compiles 502,5 million <http://ep.eurostat.ec.europa.eu/portal/page/portal/eurostat/home>

Thematic working groups set up by Georgian and European experts work on relevant topic, on each round of negotiations. The goal of their joint work is dynamic convergence of Georgia with EU. The working group terminates its work upon solving particular issue and reaching agreement.

DCFTA negotiations are led by the Ministry of Economy and Sustainable Development. According to EU Delegation trade officer – Virginia Cosul, making the statement on finalizing negotiations on agreement is thought at Vilnius Summit. Intra state processes will get started upon signing the document, which are quite long – if the negotiation process between Georgia and EU is finished in 2013, taking into consideration all above mentioned DCFTA will come into force in 2015. Besides, the possibility of entry into force of economic articles of association before its ratification is also discussed. In particular, association's entry into force requires ratification of 30 parliamentarians, including the members of the Parliaments of 27 member states, Croatia<sup>60</sup>, EU Parliament and the Parliament of Georgia; while DCFTA requires ratification of just EU Parliament.

As we mentioned existence of DCFTA is one part of association agreement with EU. As for association agreement negotiation process, the main negotiator is David Zankaliani – first deputy minister of foreign affairs. It is important, that main part of the text is agreed with parties and work on the document will be finished within one or two rounds. The text will be initialled at Vilnius summit. Then internal procedures will be started, which will be continued for about 4-5 months.

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<sup>60</sup> Croatia finalized negotiation process and will become 28<sup>th</sup> member state in 2013

In spring Association Agreement will be delivered to Georgian party, it will substitute European Neighbourhood Action Plan. The latter will be more precise and its approval is planned on Vilnius Summit.

### 3.3 Assessment of situation concerning DCFTA in 2009 – 2012

Within the frame of European Neighbourhood Policy Georgia every year receives ENP Action Plan, in which activities (programmes), terms for completion, persons responsible as well as financing sources are defined by proprietes. According to ENP for 20012, DCFTA covers following priority areas:

- **Priority area 1** – improvement of business and investment climate by means of transparent privatization process and combating corruption;
- **Priority Area 2** – encouraging development, strengthening effort for poverty reduction and social equality, facilitating sustainable development including environment protection, further convergence of economic legislation and administrative rules.

ENP implementation reports for 2009-2012, demonstrate that following steps are made for giving full effect to DCFTA:

**Customs issues: in 2009** system for customizing and farther control was improved and “on spot check” took place. New rule for risk management came into force, which aimed at making amendments concerning risk management to the Customs Code, special department for risk analyses and risks management committee were established at Revenue Service. It is to be mentioned that new rules for issuing penalties came into force, since January 2009.

In September 2010 the Parliament adopted new Tax Code, which came into force since January 2011. Norms of mentioned Customs Code were reduced from 250 articles to 36 and merged with new Tax Code. For purpose of improving risk analyses based management system, Customs Service of Georgia established operation management division in customs control department, as central unit with trained personnel. In 2010 transit vehicles oversight system came into operation, and attaching scanned image to transit documentation became possible by means of automatic system of customs data (ASYCUDA). Besides, Customs Service of Georgia elaborated manual of standard procedures, which covers customs rules violations, explanation of sanctions and border customs procedures at Tbilisi airport, Poti Sea Port and Kutaisi free industrial zone. As for ethics and human resources, the Ministry of Finances issued two orders, regulating recruitment of staff at Customs Service, for probation term and their training.

2011 was significant basically because the authority for issuance of certificate of origin was transferred to customs service.

In 2012 Georgia continued implementation of activities focused on modern customs policy and further development of possibilities (development of conditions for transiting animals, implementing border veterinary inspections). As a result of implementation of customs results the costs for customs clearance were reduced.

**Standardization, accreditation, technical regulation and metrology:** in May 2009, within the frame of DCFTA negotiations the working group for discussing issues related to standardization, accreditation, technical regulation and metrology **was** established

In 2010 the government approved strategy for Standardization, accreditation, technical regulation and metrology together with

governmental programme for legislative reforms and adopting technical regulations in the same field. Elaboration of the draft of the Code on Product Safety and Free Movement is connected with the same period. New agency responsible for market supervision – Technical and Construction Inspection was also established. In 2011 development of the strategy for market supervision was started. 2011

In 2012 Georgian Accreditation Centre (GAC) became associated member of European Cooperation Agency (ECA). Within the frame of “Comprehensive Institution Building Programme” EU continued technical assistance in this sector, by means of two twinning projects – one on Standardization and Metrology and another in the field of accreditation; facilitation of Georgian National Agency for Standardization and Metrology and Accreditation Centre was continued. It is to be mentioned that Technical and Construction Inspection Agency was registered as LEPL within the frame of the Ministry of economy and Sustainable Development.

**Sanitary and phytosanitary measures:** in 2009 Georgia developed the draft for food safety strategy, also prepared draft laws on hygiene, registration of food enterprises and food labelling. In June 2009 Georgia and EU signed the memorandum on Georgia’s participation in the EU’s Rapid Alert System for Food and Feed. It is to be mentioned, that in this period Georgia started gradual implementation of the Law on Food Safety from 2010 to 2018.

2010 was very active in terms of elaboration/perfection legislative documentation, in particular Georgia approved Food Safety Strategy; general rules for hygiene of food and feed production enterprises were also developed, including simplified rules for small entrepreneurs. The next step was elaboration of rules for supervision, monitoring and control. Georgia also elaborated the rules for registration of food producers and food labelling. In 2010

legislative articles related to food safety, terminated since 2006 came into operation. Mandatory inspection of treatability requirements is associated with this period, but just for the enterprises exporting goods to EU. The amendment was made to the Law of Food Safety, as a result of which since 2011, state control and traceability requirements became fully effective for all producers of food and feed. In December 2010 the government approved food and feed crisis management master plan. It was very important that the laboratories were upgraded and new slaughters were opened. The preparatory programme in sanitary and phytosanitary sector was also elaborated and the process of expert's preparation was started. National Agency for Food Safety, Veterinary and Plant Protection prepared assessment of discrepancies in legislative field.

In 2011 the process of implementation of Food Safety Strategy was started, improvement of the legislation regulating sanitary and phytosanitary measures was also continued and work on Food Safety, Veterinary and Plant Protection Code was started.

In May 2012 Georgia adopted new Code on Food Safety, Veterinary and Plant Protection. It should be noted that Georgia launched the first animal registration program and the state-funded vaccination campaign against anthrax. In July the agreement was reached between EU and National Food Agency on facilitating the agency within the frame of "Comprehensive institutional building" programme. Besides, with the help of EU twinning programme Georgia made steps to development of sanitary and phytosanitary legislation and customs control capacity building of sanitary and revenue service.

**Competition policy:** in September of 2009 Georgia prepared comprehensive strategy in competition policy field, which envisaged elaboration of the Law on Competition and establishment of

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Competition Agency. The Law on Competition of 2005, which was in force up to 2009, does not regulate anti stress measures, and the Agency for Free Trade and Competition was not sufficiently free and had just consultation function.

Since 2010 effective steps were made and comprehensive competition strategy was approved. Besides, independent body – LEPL the Agency for Free Trade and Competition was established.

In 2011 the draft law of “Free Trade and Competition” was prepared, which regulates competition among business companies on local market and prevents development of monopolies.

In 2012 in compliance with competition strategy, Georgia received framework law on free trade and competition. The law describes the basic principles of anti-trust and state aid. Georgia continued strengthening of the Agency for Free Trade and Competition, which since January 2012 was consolidated with Public Procurement Agency.

**Intellectual property:** in 2009 Georgia made amendments to the Law on "Drugs and Pharmaceutical Activity", which regulates exclusivity/unreliability of data and gives right to the owner of intellectual property to implement control, at own initiative, as well as parallel import and regulate this issue with the agreement on distribution or in compliance with the article on exhaustion of right.

In 2010 new Georgian Law on Design was adopted and revised Patent Law came into force, which determined Supplementary Protection Certificate. Besides, the government issued the order for purpose of ensuring compliance of tax System with international requirements (intellectual property – trade aspects - TRIPS – agreement). According to this Order Intellectual property rights

registration charges equalized both for local and foreign entities<sup>61</sup>. The amendments were made to the Law on Trademarks, which determined expedited procedure for registration of trademark (upon applicant's request and for additional fee). Criminal Code, which entered into force in October 2010, ensures the public prosecutor's rights for ex officio action in cases involving intellectual property.

Since 2012, ad hoc registration in Patent Office (Sakpatenti) became sufficient to ensure the protection of blundering rights and the registration in revenue service is no longer required. to register. EU provided support by means of TAIEX instrument and emergency assistance, for purpose of capacity building of Georgian Copyright Association (collective management society). capacity.

**Public procurement:** the amendments to the Law on Public Procurement, in order to ensure transparency of the process, were adopted in November 2009 by the Parliament and went into force in December. The Law envisaged conducting e-tenders since March 2010, and prohibition of using paper in tender procedures by September 2010. The Law also envisaged development of Complaint handling mechanism, by March 2010, involving the representatives of Public Procurement Agency and NGOs.

In December 2010 new electronic procurement system was introduced for all types of contracts despite of their size and nature. Main criterion for revealing the winner is price, and technical assessment and identification of compliance with qualification is done only in case of winner. In order to be prepared for implementation of new legislation, public procurement agency adopted action plan for implementation of electronic procurement,

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<sup>61</sup> Requirement of WTO on non-discrimination



which envisages training of clients and bidders in new procedures and procurement of IT equipment and software for electronic platform.

In September of 2011 electronic system for public procurement became bilingual (Georgian and English). Savings of public sources as a result of E-trade by Public Procurement Agency compiled 15-20%.

In January 2012 Public Procurement Agency merged with Free Trade and Competition Agency. Framework agreement form was introduced in E-procurements system, However, the system still does not provide for the use of other mechanisms, which according to the laws of the European Union (EU *acquis*) are mandatory (for example, a limited number of participants and the negotiation procedure).

Above mentioned demonstrates that in 2012 there was significant progress in EU – Georgian negotiations including DCFTA negotiations. In December EU and Georgia started negotiations on partnership and cooperation protocol, which concerns to general principles of Georgia’s participation in EU programs.

### **3.4 Economic Benefit of Deep and Comprehensive Free Trade Area**

“It is impossible to reach EU market without considering EU norms” – stated the head of EU Eastern Partnership and Central Asia Department -Gunnar Wiegand. He also mentioned that “for being imported to EU market product should comply technical norms of general EU market... the more rules are harmonized more attractive Georgia will be for investors”.

Trade relations with EU became especially urgent after Russia's economic embargo on Georgian products in 2006. Implementation of the European Neighbourhood Policy in Georgia, followed by interest of numerous experts in economic benefits, Georgia could receive from exclusive trade regime with the EU, is related to the same period.

When we analyze possible economic benefit could be provided by DCFTA, we should differ from each other short and long term economic effects<sup>62</sup>. Long term period means 5-10 years upon DCFTA's becoming effective. Time horizons results and short term period are connected with a number of difficulties, which could be caused by introduction of new regulations for accessing market. Consequently, the effect will be more reflected on long term period and DCFTA should be considered as long term prospective.

The result of the survey demonstrate that enactment of DCFTA in short term period conditions increase of Georgia's GDP in 17% points, while in long term period – in 4,3% points. In case of EU similar indicator is insignificant and demonstrates 0, 00<sup>63</sup> % points change in EU GDP (see table 1).

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<sup>62</sup> Difference between long and short term reporting periods is determined by capital mobility. In particular, in short term period capital is considered as fixed variable, while in long term period it is mobile. This means that in conditions of free movement of capital, in long term prospective the capital will gradually move to the sectors where comparative advantage is higher and return on capital is more.

<sup>63</sup> Rounded data

Table N 1

### Macroeconomic Results of DCFTA regime enactment between EU and Georgia

Variable/country	EU	Georgia
<b>Short term period</b>		
GDP, change %	0,0	1,7
Consumer process change %	0,0	-1,0
Salaries change %	0,0	1,5
Total import change %	0,0	4,4
Total export change %	0,0	8,9
<b>Long term period</b>		
GDP, change %	0,0	4,3
Consumer process change %	0,0	-0,6
Salaries change %	0,0	3,6
Total import change %	0,0	7,5
Total export change %	0,0	12,4

**Source:** *Trade Sustainability Impact Assessment in support of negotiations of a DCFTA between the EU and Georgia and the Republic of Moldova*, CASE, ECORYS, Rotterdam, 2012

All above mentioned demonstrates that enactment of DCFTA can bring much more benefit for Georgia than for EU.

As for trade balance, negative balance will be retained in long term prospective, however export volume will be increased in 9-12% in short and long term periods respectively and import volume will get increased in 4,4% in short term period and in 7,5% - in long term period. Salaries are also characterized by increasing trend: the results of survey demonstrate that 1,5% and 3,6% increase should be documented in short and long term periods. At the same time, reduction of consumer prices in 1-06% is expected in short and long term periods. This means that consumer's buying capacity will get increased as a result of enactment of DCFTA, especially in long term prospective.

Discussing the Export - Import sector analysis (see Table N 2)

Export - Import sector analysis (**change % - long term period**)

	<b>Export</b>	<b>Import</b>
Vegetables, fruits, nuts	21.9	19.1
Other cereal crops	3.0	15.1
Products of animal origin	5.7	19.8
Livestock and meat products	169.9	17.8
Vegetable oils and fats	6.5	3.4
Sugar	-1.5	1.6
Other processed foods	14.5	13
Beverages and Tobacco	2.5	22.5
Oil products	16.5	1.8
Chemical, rubber and plastic products	64.5	-2.7

Transport means	8.3	5.9
Electronics, computers	16.3	8.8
Other devices and equipment	48.1	4.1
Other production	-13.8	14.3
Construction	7.7	6.6
Trade	8.2	14
Watercraft	2.9	2.5
Air transport	21.1	7.9
Communications	4.8	5.4
Business and Information and Communication Technologies (ICT)	12	4.2
Public and other services	1.8	20.6

**Source:** *Trade Sustainability Impact Assessment in support of negotiations of a DCFTA between the EU and Georgia and the Republic of Moldova*, CASE, ECORYS, Rotterdam, 2012

If we analyze change of export, in this case DCFTA in long term period will be the most reflected on livestock and meat products (+170%), than come chemical, rubber and plastic products (+65%) and other devices and equipment hold third position (+48). As for import, the change should be in the following sectors: beverages and tobacco (+22%), products of animal origin (+20%) and vegetables, fruit, nuts (+19%).

### 3.5 Conclusion

In conclusion it could be said, that enactment of new dimension of Georgian – EU trade relations - DCFTA is real prospective and effective steps are made to its harmonization with EU legislation and

implementation in Georgian reality. After 6 rounds of negotiations internal procedures will get started and according to expert forecasts, DCFTA will enter into force in 2015.

Deep and Comprehensive trade develops grounds for developing predictable legal and institutional environment, which increases interest toward Georgia as economic partner. It will also facilitate relations among businesses and encourage internal and foreign investments.

Despite some risks, related to the difficulties caused by enacting the European regulations, starting deep economic integration with EU is significant for Georgian companies, for diversification and attracting foreign investments. If considering DCFTA in long term prospective, it is clear that after so called transition period existence of Deep and Comprehensive Free Trade Area will develop grounds for sustainable economic development.

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## **4. Sustainable Development and Economic Competitiveness Issues in Georgia**

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**Giorgi Kuparadze**

**Expert-Analyst at Caucasian Institute  
for Economic and Social Research**

**Nana Maisuradze**

**Economic Analyst**

### **4.1 Introduction**

Sustainable development issues, which are among the most topical ones of modern global economy are reflected and highlighted in official documents regulating Georgia-EU relations. Supporting of sustainable development is included in 3<sup>rd</sup> priority of EU – Georgia ENP Action Plan. Sustainable development priority is reflected, in National Indicative Programme<sup>64</sup> drafted by EU, as priority for 2011-2013, which previously was not adequately included and implemented by policy makers. Thus, sustainable development is among urgent issues in direction of development of Georgia and deepening EU integration.

Generally, sustainable development is the framework of development which considers requirements of future generations within the frame of current consumption. In 1987 UN Organization published the report providing the most acknowledged explanation of sustainable development: “Sustainable development is development that meets

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<sup>64</sup> Initial Concept Note, Potential priority areas for ENPI National Indicative Programme (NIP) 2011-2013 Georgia, page: 10 URL:  
[http://ec.europa.eu/world/enp/mid\\_term\\_review/initial\\_concept\\_note\\_georgia\\_en.pdf](http://ec.europa.eu/world/enp/mid_term_review/initial_concept_note_georgia_en.pdf)



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the needs of the present without compromising the ability of future generations to meet their own needs “<sup>65</sup>.

According to the same report above mentioned explanation contains within it two key concepts:

- The concept of 'needs', in particular the essential needs of the world's poor, to which overriding priority should be given; and
- The idea of limitations imposed by the state of technology and social organization on the environment's ability to meet present and future needs.

According to EU Commission Sustainable Development is Comprehensive goal<sup>66</sup>: of EU; it is necessary to ensure to meet our present needs without compromising the ability of future generations to meet their own needs.

To date EU policy is based on Sustainable Development strategy (EU SDS) updated in June 2006, which includes integrated economic, environmental and social issues, and the research and development (R & D) have important and diverse role.

World Organization for Environment and Sustainable Development in its report submitted to UN Organization in 1987, announced sustainable development as normative goal. Due to mentioned importance of the topic, majority of world countries actively started

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<sup>65</sup> World Commission on Environment and Development."Our Common Future, Chapter 2: Towards Sustainable Development". URL: <http://www.un-documents.net/ocf-02.htm>

<sup>66</sup> URL: [http://ec.europa.eu/research/sd/index\\_en.cfm](http://ec.europa.eu/research/sd/index_en.cfm)

modification of economic policy in their internal policy, in compliance with the concept for sustainable development. Due to the fact that sustainable development covers interrelated issues, it is important for countries governments to have indicators of sustainable development, for assessing current condition and progress of the country. At this stage the most widely accepted indicators are provided in joint document of UNESCO, OECD and Eurostat<sup>67</sup>, according to which following indicators belong to basic indicators of sustainable development (Table 1. indicators of sustainable development):

***Table 1. Indicators of Sustainable development***

<b>Direction of indicators</b>	<b>Supply indicators</b>	<b>Changes indicator</b>
<b>Fundamental welfare</b>	Average life expectancy	Mortality and morbidity (by age) indicator change index
	Share of population with post school education	Admissions for post school educational programme
	Temperature deviation from the norm	Greenhouse gas emissions
	Ground level ozone and fine particulate concentrations	Emissions of smog forming emissions
	Availability of good quality water	Mineral fertilizer run-off to water
	Fragmentation of natural habitats	Conversion of natural habitats for other

<sup>67</sup> Measuring Sustainable Development; Report of the Joint UNECE/OECD/Eurostat Working Group on Statistics for Sustainable Development; pp. 10–11

		purposes
<b>Economic welfare</b>	Net foreign ownership of financial assets per capita	Investments in foreign financial assets per capita
	Produced capital per capita	Net investments in produced capital per capita
	Human capital per capita	Pure investments in human capital per capita
	Natural capital per capita	Net investments in natural capital per capita
	Reserves of energy resources	Reduction of energy resources
	Reserve of mineral resources	Reduction of mineral resources
	Forest – resources	Reduction of forest resources
	Marine resources	Reduction of marine resources

Given indicators describe two main directions of sustainable development which in its turn covers several sub directions.

Thus, progress of sustainable development in state policy should be assessed in a complex manner, in fundamental and economic welfare prospective. It is quite broad issue. This research aims to review state institutional mechanisms of sustainable development in Georgia, analyses of development issues in Georgian – EU relations; analyses of achieved progress and existing challenges. The documents regulating Georgian –EU relation, as well as project analyses prepared by the Ministries of Energy, Environment and Sustainable Development are used in this research. Yale University-Environmental Performance Index research<sup>68</sup> is used for assessing

<sup>68</sup> Yale University-Environmental Performance Index, URL: <http://epi.yale.edu/>

sustainable development policy and condition in Georgia with this regard; as well as data of the World Economic Forum's Global Competitiveness index research (GCI) 2012-2013<sup>69</sup>. Sustainable development policy in Georgia is discussed in first chapter of the research. Second chapter is dedicated to the issues regulating sustainable development in Georgia – EU relations; the conclusive part represents current challenges and problems of the mentioned field. The survey period covers years of 2010 – 2012.

#### **4.2 National Policy in Sustainable Development Issues**

In Georgia institutional mechanism of sustainable development issues are coordinated by: the Ministers of Economy and Sustainable Development, Environment and Energy and Natural Resources.

In Georgia the Ministry of Economy and Sustainable development acts the role of initiator and coordinator of the issues of sustainable development. With the position of the Ministry, the role of the Government of Georgia in this process is not of a regulator or donor, but of a facilitator and the leader of processes<sup>70</sup>. In July 2010 as a result of the reform implemented in the Ministry of Economic Development, the D of Sustainable Development was established; and in October 2010 the Department for Sustainable Development was created in the same Ministry.

Main functions of sustainable development mean leading and facilitating elaboration and implementation of policy and programmes in the field of sustainable development; rising awareness of private sector and distribution of information on green business opportunities; cooperation with international organizations

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<sup>69</sup> World Economic Forum, Global Competitiveness Report, URL: <http://www.weforum.org/reports/global-competitiveness-report-2012-2013>

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and development of partners network among public agencies, business associations, ministries, NGOs and other units.

Following projects were implemented within the frame of sustainable development policy:

- Identification of green business opportunities (GBOA)
- Facilitating development of investment environment in green economy sector and development/upgrade of internet portal [www.greengeorgia.ge](http://www.greengeorgia.ge)
- Framework programme for development of information and communication technologies (ESW) in green transportation sector.

Mentioned projects basically were implemented with the help of donor funding. Given projects were basically aimed for rising awareness, main target group of which was business sector and especially investors. Within the frame of this programme the Ministry of Economy and Sustainable Development implemented the policy, in following direction<sup>71</sup>:

- Renewable energy
- Agriculture
- Tourism
- Clean energy based production

Part of state policy implemented by the Ministry of Economy and Sustainable Development of Georgia is called “Green growth initiative”. Besides, main goal of this initiative is introduction of

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<sup>71</sup> The Department for Sustainable Development of the Ministry of Economy and Sustainable Development <http://greengeorgia.ge/?q=ka>

sustainable development initiatives within the frame of existing policy. The latter on declared level (until 2013) integrates economic growth and protection of global goods (example: by means of protecting biodiversity and combating climate change). Main object of mentioned policy is private sector, with corrections in existing policy framework and not by proposing new approaches.

Sustainable development approach in tourism sector meant access to cultural diversity for guest arrived from over the world, and at the same time its long term protection. This means activities for developing protected areas; establishment of the network of 50 protected areas in compliance with international standards, among them 14 reserves, 8 national parks, 14 natural monuments, 12 managed natural restricted area and 2 protected landscapes. Besides the plan envisages declaration of 13% of the country as protected areas; reduction of costs for tourism objects by means of renewable energy and agriculture.

*Renewable energy and alternative sources of energy: in Georgia at this stage wind, solar, biomass and geothermal energy is used for direct heating, fish pond heating, industrial applications and heating greenhouses. The total reserve of geothermal waters is above 160,000 cubic meters per day. 8% of these resources are in West of the country, however geothermal fields are available also in East Georgia. Geothermal waters existing in 44 mines of the country outflow by means of 26 wells and four springs, their temperature varies from 30 to 110 degrees Celsius<sup>72</sup>. Geothermal resources of the country are of high quality; contain minimal amount of dissolved salts, which in using process reduces scaling.*

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<sup>72</sup> Social Economic Geography of Georgia (etidor R. Gachechiladze/Tbilisi, University print shop 1996. P. 42

Thanks to advantageous geographical location, forests and favourable climate for agricultural development, Georgia has great potential for the creation of biomass power plants, especially for heating and hot water. Biomass is considered as the most important source of energy in rural areas, assuming that 40% of the country's total area is covered with forests. At this stage the Ministry of Energy and Natural Resources is preparing pilot project on biomass power plant in Mestia (Svaneti region) , where wood sustainable energy chain will be used. Georgia has great potential of wind energy, whereas generates about 4 billion KWh power annually. Wind speed was measured in 165 meteorological sub stations for several decades. According to the results of the survey the most appropriate places for wind power plants in Georgia are in highland areas of Caucasus, on upland of South Georgia (Javakheti region) and South part of Black Sea.

In environment sector, which is a component of sustainable development Georgia in 1994 ratified UN Convention on Climate Change, in 1996 climate protection national programme was developed, and in 1999 Georgia joined the Kyoto Protocol. Consequently there are conditions for participating in activities within the frame of clean development mechanism. In 2010 – 2012 in parallel with declaring support to these conventions on state level the focus was on maximal simplification of getting permits for using natural resources, for example the procedures for submitting applications and issuing permits in hydro energy development sector had minimal requirements. The same simplified procedures apply to the use of following natural assets:

- Land acquisition or lease
- Obtaining Water Use Permit, issued by the Ministry of the Environment
- Environmental Impact Assessment Report

- To obtain a construction permit, issued by the Ministry of Economy and Sustainable Development
- Obtaining permit for power generation, issued by the National Energy Regulatory Commission (GNERC), required only for 13 megawatts or more power projects.

Except already mentioned conventions, in the field of environment Georgia also joined Copenhagen Accord<sup>73</sup> on 1 February 2010 and consequently accepted following liabilities:

- Implementing relevant national mitigation measures (NAMAs), which should be facilitated and enacted by the technologies and development of opportunities, so that to make possible measurement, reporting and verification;
- Deviation from baseline data (below the normal level of business), the way to make possible its measurement, reporting and verification, which should be supported and enacted by technologies and development of opportunities;
- Determine baseline data or starting point, from which implemented actions will be measured, reported and verified;
- Mitigating measures implemented by Georgia will be volunteer and relevant from national point of view, which should be facilitated and enacted by technologies and development of opportunities, by means of existing mechanisms, technological mechanisms and other mechanisms developed by Copenhagen Accord;
- Developing Carbon Reduction Plan and Carbon Low Level Strategy, especially by means of investments and global cooperation in the field of renewable energy.

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<sup>73</sup> [http://unfccc.int/meetings/copenhagen\\_dec\\_2009/meeting/6295.php](http://unfccc.int/meetings/copenhagen_dec_2009/meeting/6295.php)



### 4.3 Sustainable Development Issues in Georgian EU Relations

Operational measures of sustainable development in the public sector are reflected in the "European Neighbourhood Policy, Georgia - EU Action Plans" (ENP AP).<sup>74</sup> The "European Neighbourhood Policy, Georgia - EU action plan on sustainable development issues is included in 3rd priority. In this respect, development of procedures on framework laws and regulations as well as planning in: air quality, waste management and environment protection were basically finalized by 2012.

#### Ministry of Environment

1. Work on the issues facilitating to compliance with commitments provided by UNECE conventions:

1.1 On protection and use of transboundary waters and international lakes

1.2 On assessing environmental impact in transboundary context

1.3 working on issues related to trans boundary effects of industrial accidents

2. Preparation of third national response against Climate Change Framework Convention

3. Update of Biodiversity Protection Strategy and Action Plan

4. Elaboration of Waste Management Strategy and National Action Plan

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<sup>74</sup> Documents are obtained from official website of the Ministry of European and Euro-Atlantic Integration of Georgia  
[http://eu-integration.gov.ge/index.php?que=geo/official\\_documents](http://eu-integration.gov.ge/index.php?que=geo/official_documents)

## Ministry of Energy and National Resources

1. Continuing reforms in forestry sector, adopting Forestry Code and elaboration of sub law acts, perfection of sub law acts concerning existing legislation on raw materials and hunting
2. Development of the model of agreement concerning environment impact. Implementation of new system for administering fees
3. Substituting forest using licenses with long term leasing and concluding new agreements with leasers
4. Developing geo informational system of natural resources, starting electronic issuance of licenses and permits and improving quality of existing services;
5. In order to attract investments announcing new licensing objects for using natural resources

In the report of implementation of EU- Georgia action plan for 2010, it is mentioned concerning sustainable development that <sup>75</sup> after the enactment of Eastern Partnership Programme on Prague Summit in 2009, the progress in both bilateral and multilateral cooperation is obvious in Georgia. In this regard, the Ministry of Energy took an active part. In the meetings on energy security issues arranged within the frame of Eastern Partnership Platform II on 20 May and October 27 of 2010. Participants of the meeting were focused on discussing the issues as following: closer cooperation in energy security field, energy diversification and sustainable development.

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<sup>75</sup> Report on implementation of ENP AP of 2010  
[http://eu-integration.gov.ge/uploads/ENPREPORT2010FINAL04\\_03\\_2011.doc](http://eu-integration.gov.ge/uploads/ENPREPORT2010FINAL04_03_2011.doc) p.

At this stage elaboration of following documents is underway in the Ministry of Environment: overview of the results of environment protections, national action plan for environment protection and report on condition of environment. Mentioned documents might act significant role in the process of developing sustainable development strategy.<sup>76</sup>

In 2011 in the field of sustainable development main attention was paid to economic welfare component of sustainable development (table 1), which meant continuing use of “GSP+” for encouraging good governance, within the frame of generalized preferences of EU. These additional preferences aim to facilitate diversification of structure of Georgia’s export and increase its volume. However, getting benefit from mentioned conditions depends on compliance of existing conditions with international conventions on labour rights and good governance. In 2011 negotiations between Georgian and ILO progressed and the country adopted recommendations elaborated by this organization in 2010. Georgia still has to use some of them, especially concerning legislative changes in labour code and the Law on Trade Unions.

In 2012 in sustainable development field main attention was paid to energy and environment issues, in particular Georgia continued active participation in “Baku Initiative” in INOGATE programme. Since **2010** Georgia significantly contributed to implementation of following programmes of INOGATE:

- Harmonization of gas and oil technical standards in Eastern Europe and Caucasus;
- Safety of main gas infrastructure and security in East Europe and Caucasus;

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<sup>76</sup> p. 92

- Supporting energy market integration and sustainable energy in newly independent countries (SEMISE);
- Harmonization of technical standards and practices in electricity energy sector of newly independent countries;
- Energy saving initiative in construction sector in the countries of East Europe and Central Asia;
- Agreement of mayors

As a result, with participation in mentioned cooperation Georgia achieved significant progress in developing energy provision routes and diversification of sources and stable market framework conditions, which would be attractive for investments and improve quality of energy security. The project is initiated by EU and aims to manage waste based on the agreement signed by the heads of the municipalities; participating countries are obliged to reduce emissions (CO<sub>2</sub>) in 20% by 2020. Due to the fact that 80% of the pollution comes from big cities,, within the frame of given project Tbilisi Municipality has possibility to elaborate action plan and implement significant measures for reducing pollution and retaining clean environment.

Within the frame of the project Georgia can contribute to global process of clean development. Importance of the project was especially highlighted on the meetings of platform 3 on energy security. The main goal of the project is elaboration of sustainable energy policy and utilization of renewable energy sources.

#### 4.4 Assessment of Sustainable Development of Georgia

According to experts, despite of single steps made towards sustainable development, there is no general comprehensive concept for sustainable development<sup>77</sup> and relevant target indicators.

In the event of non-availability of general strategy, measures implemented to single directions, rise significant problems in terms of combination of interrelated factors of sustainable development. Assessment of current condition of Georgia according to Yale University<sup>78</sup> index research of 2012 could be considered as competitive and fundamental of the results caused by shortcomings. Index of 2012 is based on the data of previous years and integrates condition of natural environment of the countries as well as social reality accompanying this condition.

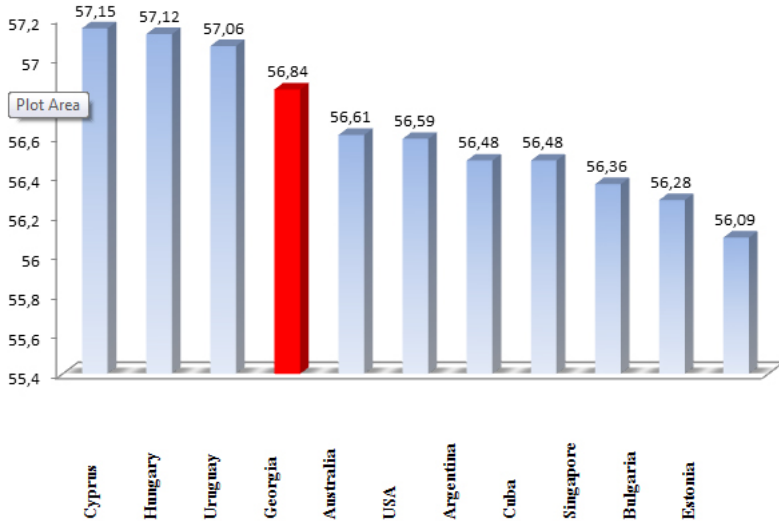
According to the survey of stability index of general condition of environment, Georgia has 47<sup>th</sup> position. The group of countries Georgia is among which, is provided on diagram 1.

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<sup>77</sup> Temur Murgulia - Sustainable development System and “Green Business” – Eastern Partnership and Social Economic Policy of Georgia p 46 Economic and Social Research Institute of Caucasus, Tbilisi 2011

<sup>78</sup> Environment condition index describes condition of environment on the background of current consumption, taking into consideration accessibility and stability of resources Yale Center for Environmental Law and Policy, Yale University. Center for International Earth Science Information Network, Columbia University <http://epi.yale.edu/>

**Diagram 1 The group of ten countries, Georgia is among which according to environment condition index (according to rating of 132 countries of the world):**



Despite relatively progressive condition of Georgia in general environment condition index (general rating describes economic development of developed countries) revision of baseline factors of welfare aspect of sustainable development index gives different picture<sup>79</sup>. Georgia has much lower figures according to baseline indicators such as access to portable water in whole country (see table 2).

<sup>79</sup> See survey methodology <http://epi.yale.edu/sites/default/files/downloads/2012-epi-full-report.pdf>

**Table 2. Georgia's position according to separate components of index (rating of 132 countries)**

Rating of indicator	53	50	22
<b>Air pollution</b>	Water quality	Accessibility of drinking water	Sulphide dioxide emissions per capita

The survey also provides interesting data in agro economy financing rating; with this indicator Georgia was included in the group of following countries (table 3):

**Table 3. Group of Georgia according to agro subsidies:**

<b>Cameroon</b>
<b>Somon Islands</b>
<b>Nepal</b>
<b>Swaziland</b>
<b>Angola</b>
<b>Georgia</b>
<b>Greece</b>
<b>Morocco</b>

With the respect of social economic component of sustainable development the assessment of current condition of Georgia according to “global competition” index 2012 -2013, can be considered as comprehensive review. Usually, international computability of the country significantly determines prospective of its sustainable development. The best means for assessing mentioned index are 11 indicators of absolute and probable meaning used in development of index, which cover great part of significant fields of sustainable development.

According to “global competitiveness” index of 2012-2013 Georgia has 77<sup>th</sup> position among 144 assessed countries<sup>80</sup>.

**Table <sup>81</sup>4. Global Competitiveness Index of 2012-2013, Georgia among 144 countries**

<i>Group of Factors</i>	<i>Position in Rating</i>
<b><i>Baseline Factors</i></b>	
Institutes	61
Infrastructure	53
Macroeconomic stability	88
Health and primary education	61

<sup>80</sup> World Economic Forum, The Global Competitiveness Report 2012–2013 გვ. 174  
<http://www.weforum.org/reports/global-competitiveness-report-2012-2013>

<sup>81</sup> According to index researching methodology starting position of the country means positive assessment



<i>Efficiency Factors</i>	
High Education and Training	93
Commodity Market Efficiency	82
Labour Market Efficiency	35
Financial Market Improvement	93
Technological Readiness	76
Market volume	99
<i>Innovation and Development Factors</i>	
Business Development	76
Innovations	99

Given data demonstrate that Georgia has relatively good position in the group of baseline indicators, while in terms of significant component of sustainable development such as business development and innovations Georgia has significantly lower assessment. According to one sub component of business development – development of production process – Georgia occupies 112<sup>th</sup> position among 144 countries; and according to sub component of innovations group – company’s expenses on research and development – Georgia occupies 125<sup>th</sup> position among 144 countries.

## 4.5 Conclusions

Analyses of current condition of Georgia revealed several important problems with the regard to sustainable development:

The role of the Ministry of Economy and Sustainable development should be expanded for better management of sustainable development issues. At this stage the department of sustainable development of the Ministry acts just role of the facilitator of the process;

There is no single strategy for sustainable development at the state level, which would, integrate the overall policy of sustainable development, including economic and environmental issues of sustainable development;

Simplified licensing system for the use of natural resources is focused on maximally simplified use of these resources, which in its turn contradicts to long-term visions of sustainable development;

Ratified international conventions in the field of environmental protection, in most cases, are less provided with internal national mechanisms of implementation;

The system of sustainable development of indicators is not developed on state level, which would enable policy makers, analytics and stakeholders to provide complex assessment of condition existing in the country in terms of sustainable development;

So called baseline factors of sustainable development are described as a problem in important international surveys, example: accessibility of portable water in whole country;

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The projects implemented in recent years, in direction of sustainable development, do not demonstrate the strategy focused on stimulation of systemic ecological system.

## **5. Public Procurement Reform in Georgia**

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**Michael Dzagania**

**Expert-Analyst at Caucasian Institute  
for Economic and Social Research**

**Otar Kikvadze**

**Expert-Analyst at Caucasian Institute for Economic and  
Social Research**

### **5.1 Introduction**

Public procurement means procurement of goods and services by the public institution. Main principles of public procurement are publicity and transparency. Public procurement system is decentralized and procurer agency is authorized for implementation of procurement, which is also responsible for lawfulness of the process.

Public procurement system operates in Georgia since 1 July 1999, which is associated with coming into force of the Law on Public Procurement. Mentioned Law was developed on the basis of UN International Trade Law.

Though in 2006 the new Law on Public Procurement was adopted, it could be said that public procurement system was not organized properly by this time, good evidence for mentioned is the World Bank report of public procurement of Georgia, prepared by 2008, where the public procurement system is evaluated as a high-risk system.

It could be said that the public procurement system was still seen as the successor to the Communist regime, by this time. There was a high level of risk and other adverse effects. Corruption was deeply rooted in the system. Facts of bribing, influencing and receiving illegal gifts were quite frequent. These deficiencies undermined confidence in public procurement institute and also damages stability of the system. Transparency was also serious problem. The suppliers did not have full information on tenders. Besides, administrative costs were very high and unjustified. The main shortcoming of the system was procedure's fully paper based procedure. For example, by the end of 2010 the number of procurement-related documents, was over 20 million sheets of paper (A4) that caused difficulties in determining and registration of required documents am=n also led to an increase in the risk of corruption.

Additional barriers were developed in the process of submitting official proposals for tenders, suppliers had to get in touch with various administrative units, in order to get requested documents. Collection of these documents required much time and money. Besides, it was necessary to pay 200 GEL for participation in tender, which was quite big amount. On one hand this hampered to companies' participation in tenders and on the other hand increases monopolistic tendencies.

According to old procedures the participants of competition should at least for four times come to purchasing organization, and the winner should come once more. With this respect geographic factor is not a barrier, mentioned shortcomings hampered to competition in public procurement system. In fact almost all international principles were violated in the procurement activities. Therefore, public procurement in Georgia was considered unsuccessful and prompt reforming of the system became necessary.

## 5.2 About new electronic system

On 1 December 2010, old public procurement system was substituted by new e-procurement system, since then all tender procedures were implemented exclusively by e-procurement system (GE-GP). At this stage all procedures (started from tender proposal including conclusive agreement) are done on-line. Using e-procurement system made significant savings of public finances, for example:

- Savings made as a result of e-tendering compiled 190 941 by the end of 2011;
- Savings made as a result of e-tendering compiled 160 423 by the end of 2012;

Efficiency of electronic system (Ge-GP) is demonstrated by its transparency as well as by reduction of corruption. The information on procurements is open and accessible via on line system, including annual procurement plans of public agencies (more than 3000 lists), tender applications, tender documentation, and decisions on tender assessments, protocols and agreements. Number of tenders was also increased considerably, for example:

- 2008 -2000 tenders;
- 2009 -2300 tenders;
- October – December 2010 - 549 tenders were announced in e- system;
- 2011 – 33 049 tenders were announced in e- system;
- 2012 𐄂 - 29 145 tenders were announced in e- system;

The progress was conditioned by simplification of procedures. According to previous law direct contracting was possible only in case if possible price of goods/services would not exceed 30 000\$, and working cost - 60 000\$. After enactment of the electronic system

all tenders, if their costs were more than 3000\$ were carried out electronically. Mentioned innovation ensured more transparency of the procurement process, this provides equal opportunities to all bidders despite their geographic location.

It is to be mentioned, that the corruption level was reduced in very short time. Just few facts of corruption were revealed after enactment of e-system, however it lost organized nature.

Black list, containing information on supplier companies which have dishonestly violated terms of contract, is determined in e-procurements system. Consequently the companies included in black list will not be able to participate in the tenders announced by public companies, during one year.

Electronic system significantly simplified procurement procedure, administrative requirements are minimal. Required documents should be short and well-grounded. Criteria and technical requirements are checked after the end of tender. Number of the applicants' visits to procurer organization concerning procurements was significantly reduced; in fact it is no longer necessary (before winning tender). Besides, cost for participation in tender is 30\$, which is four times less than before.

EU single classification system for public procurement (CPV codes) is used for enumeration of procurement premises.

Electronic system helps supplier in planning sale strategy. The suppliers are eligible to collect information about any interesting tender, besides they can immediately receive in electronic system information about the tender on topic interesting for them. Today, more than 4 000 procurer organizations and more than 11 000 suppliers are registered in entire electronic system.

At the first stage of development of electronic system, significant correction of legislation and development of new regulations, as well as changes in secondary legislation became necessary. In 2005 new Law on Public Procurements was adopted, and came into force on 01/01/2006. Main amendments to mentioned law were made in 2009 – 2010. The process was administered by State Procurement Agency (SPA), reporting to the Government of Georgia. Namely, SPA became the main institution implementing public procurement agency. At this stage Competition and Public Procurement Agency is the main actor in mentioned field. It accepts full responsibility for successful implementation of the reform.

National Agency of Public Registry (NAPR) provides technical assistance Ge-GP, since it has great experience in working electronically. Competition and Public Procurement Agency continues cooperation on programme development and innovations with NARP. Development of new server became necessary, streaming from the practice. Solving this problem would be impossible without the financial and technical assistance of the international agencies. Thus, Competition and Public Procurement Agency acquired necessary technologies and programme resources with the help of the World Bank.

Priority in reforming the procurement system was elimination of corruption. This would ensure cost effectiveness of public expenditures, healthy competition, and non discriminative approach to the bidders and transparency of procedures. Priorities also mean facilitation to publicity of public procurements and confidence building. Two models were discussed during the reform – gradual model and the model of abrupt revolutionary changes. Finally the choice was made for radical reforms. Consequently, e-tendering became necessary for all suppliers and organizations. In 2010 after four months Ge-GP pilot work and trainings and seminars, it became



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possible to move in 100% from paper to e-tendering. Strategy of radical changes worked effectively<sup>82</sup>.

In the beginning it was decided to use Chorea's experience, but it appeared to be expensive, its total cost was 10 million USD, which 20 times exceeded to annual budget of Public Procurement Agency. It required intensive involvement of foreign specialists. It would be impossible to response timely even to insignificant changes. Consequently, in house scenario was chosen. Specialists of NARP were inviting and finally less than 1 million USD was spent, which is very few for this project.

After implementation of the reform, elimination of its defects was started. The procedures were simplified. The content of website of Public Procurements Agency was translated form Georgian to English. Today, all legislative acts concerning procurement system, user's manual, all notifications and information are accessible in Georgian and English. Announcing tenders in English was good precondition for increasing number of foreign bidders; which also facilitates to improvement of procurement system of Georgia.

Procurement system of Georgia, its legal basis and practice tries to comply with international standards, share and implement technological innovations. Dialogue with public agencies and private sector is also important.

Key elements of new electronic system for public procurement are given below:

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<sup>82</sup> <http://procurement.gov.ge/>

- **Dispute resolution**

The Council for dispute resolution is established in Competition and Public Procurement Agency. The Council operates based on the order No 11 of the chairperson of Public Procurement Agency, dated 30 November 2010. It consists of six members nominated by the agency and nongovernmental sector. Chairperson of the agency chairs the Council, two members from the agency are appointed by the chairperson and the rest three (representatives of nongovernmental sector) are selected according to rotation principle, for one year. Any candidate can send electronically information concerning disputes to the Council of Disputes, by means of official web site of the agency - [www.procurement.gov.ge](http://www.procurement.gov.ge). The information will be considered as sent officially, upon being placed on the website. In case if the candidate (or any interested person) believes that the rules established by the Law on Public Procurement and relevant legislation were violated during procurement procedures s/he has the right to appeal through the electronic format.

In the event if the candidate appeals the activities of the procuring organization, the suspension of the procurement procedures shall be permitted, only in the interval between the completion of electronic trading and signing the contract. The basis for official recognition of the complaint, by the Council of Disputes is submission of the complaint on the web - page.<sup>83</sup>

Upon the recognition of complaint the Council of Disputes shall review the dispute and make decision within not less than 10 calendar days. The complainant and respondent both can make statements in the process of dispute review, after that the members of the Council ask questions in order to clarify the circumstances. The

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<sup>83</sup> [http://procurement.gov.ge/index.php?lang\\_id=GEO&sec\\_id=12](http://procurement.gov.ge/index.php?lang_id=GEO&sec_id=12)

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session can also be held by means of electronic communication tools.

The Council is authorized for full or partial non satisfaction of the complaint. If the Council believes that the complaint is fear, it has the right to point to incorrect action of the purchasing organization and request for revision or abolishment of the decision. Besides, the Council can raise with relevant body the issue of responsibility of the participants of the procurement.

E-model for submission of complaints is in operation since November 2011, which means that the candidates can submit complaints electronically. This procedure makes the process easier and supports society's involvement in public procurements process.

- **Questions and Answers Function**

In 2012 new function was added to electronic system for public procurement, which enables the candidate to ask electronically questions to purchasing agency, concerning announced tender. The name of the candidate remains confidential until the end of trade process. Procurer organization 2012 shall answer the question within 2 days.

Mentioned Mechanism supports transparency and objectiveness of public procurement process.

- **E-PLAN**

Since 2013, the purchaser organizations have a responsibility to have Purchase Plan in electronic format, which is provided by electronic public procurement system. The advantage of submission of electronic plan is that if the amount indicated in the relevant code of the plan is not sufficient, the system does not give possibility for

announcing electronic/simplified tender, which minimizes possibilities of mistakes of procurer organization.

E-PLAN is comfortable in terms of correcting the plan, since it is not necessary to upload PDF document after each change.

- **White list**

**Competition and Public Procurement Agency** is authorized to register user in white list. The supplier that satisfies following requirements can apply for registration in white list:

1. The supplier should not have been registered in black list during last 1 year, by the date of applying for registration in white list;
2. The supplier should not have been registered in the black list available on official web – site LEPL Revenue Service ([www.rs.ge](http://www.rs.ge)) during last 1 year, by the date of applying for registration in white list;
3. Proceedings due to insolvency of supplier should not be in progress by the date of applying for registration in white list;
4. The supplier has at least one positive recommendation about the fulfilment of accepted contract liabilities, during last three years. The cost of the contract should not be less than 50 000 GEL. The form of recommendation is determined by Annex 3. The recommendation should be provided on the form of the organization, otherwise the recommendation will not be reviewed;
5. Legal proceedings are not underway against the supplier (proxies or representatives);
6. The supplier has not less than 1 000 000 GEL total turnover during last 3 years, by the date of applying for registration in white list;

7. The supplier has no dept against the state budget, by the date of applying for registration in white list;
8. The supplier has updated reference form the registry of entrepreneurs and non commercial legal bodies, by the date of applying for registration in white list.

### 5.3 Assessment of Electronic System by International Organizations

Various international organizations confirmed effectiveness of the system; for example: Public Procurement Department of EBRD reviewed EBRD region in 2011 and made following assessment of procurement system in Georgia: “Eastern European countries, including Georgia and Russia are implementing public procurement policy, however just Georgia managed to share international best practice and to develop effective procurement system”.

In the region just Georgia managed to reach the best result (83%), which is due to high compliance with international standards. Three other countries got results lower than 75% (in average): Russia – 75%, Belarus - 74% and Moldova – 71%. Ukraine’s result (59%) was assessed as having low compliance. Georgia’s results according to all principles are more than of other countries, especially according to transparency, flexibility<sup>84</sup>

In some regions the barriers to international trade were identified however, using modern procurement techniques and electronic communication is possible only in Georgia.

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<sup>84</sup> <http://procurement.gov.ge/>

According to Transparency International Georgia, corruption is lower in Georgia than in some EU countries, among them: Slovakia, Italy, Greece, Romania and Bulgaria.

According to the director of Transparency International Georgia, e-procurement system implemented last year was transparent. Government's attempt to provide information to society electronically is really very positive. We call government to make more effort in this direction and make public agencies more transparent.

Georgia is ready to share its experience with the countries of Africa and Pacific region, which wish to share international experience. The World Bank and ADB plan surveys in purpose to implement our reforms in other countries.

#### 5.4 Conclusions

The reform implemented in public procurement field, which meant introduction of electronic format is quite progressive system. Due to mentioned changes, the tendering process was simplified and the threat of subjectivism of tender commission was reduced; this will of course facilitate to effective functioning of the process.

Positive results of implementation of e-procurement system can be stated as following:

- **Transparency** – access of any interested person to full information regarding announced or conducted tenders is the most important element of e-procurement system;
- **Saving public finances** - electronic format of public procurement ensures healthy competition and selection of

the best candidate as a winner; these processes significantly save public funds;

- **Confidentiality** - nobody can know the names of candidates or see technical documentation until e-trade (main time and added rounds) is not finished. The candidate's information is available after completion of the trade;
- **Supporting development of e-governance** – the implementation of electronic system assigned to public agencies in various regions of Georgia (territorial bodies of central government, self governances and so on) the responsibility for improvement of e-systems in their units; due to mentioned no agency has problem of internet, which will support development of e-tendering as well as other directions in the regions;
- **Elimination of geographic misbalance** - previously when e-procurement system was not yet implemented, the suppliers in different regions had difficulties in getting information, for example about the tender announced in capital city. Consequently, only companies which had personal contacts with procurer organizations, participated in tenders. To date mentioned condition is cardinally, now all companies in Georgia and even abroad can participate in tenders, announced in Georgia.
- **Encouraging business sector** - e-procurement system improves motivation of companies to participate in tenders, this is confirmed by increasing figure of registration of private companies on relevant web-site, which compiles 12299 suppliers by March 2013 <sup>85</sup>.
- **Marketing research tool** - the representatives of private sector as well as any other interested person can visit web site of e-procurement system ([www.spa.ge](http://www.spa.ge)) , and obtain

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<sup>85</sup> Data of entire electronic system of public procurement

information concerning supply procurement of various goods and services in accordance with EU classifications, The system provides following information: who are key players of particular segment, which companies participate often in tenders and win or not them, how much funding they have received within the frame of particular tender. Which technologies do they use, raw materials and goods of which country do they supply, what kind of experience do they have in mentioned field, how competitive are they, are they included in the black list or not; as well as information on new companies which plan to enter the market and participate in tenders and so on;

- **Saving time and funds of suppliers** – electronic format of public procurement system provides suppliers with the opportunity for preparing tender proposals locally and uploading to the relevant web-site. Consequently they do not loose time for travelling (especially in regions). Besides, the companies do not spend money for stationary (paper, envelope and so on) and its transportation.



## **6. Eastern Partnership Status Quo Assessment and Future Prospects**

**Vakhtang Charaia**

**Expert Analyst at Caucasian Institute for  
Economic and Social Research**

### **6.1 Eastern Partnership and its Precondition**

On 26 May 2008 Prime Minister of Poland, with support of the Government of Sweden introduced Eastern Partnership (EaP) at EU General Affairs and External Relations Council meeting in Brussels. Mentioned programme came into force one year later on 7 May 2009 (during the Presidency of Czech Republic), at Eastern Partnership Summit with the Declaration 27 + 6.

EaP – is new partnership programme proposed by EU to post soviet countries, located in its east, which at the moment are not considered as candidates for EU membership, but due to “real-politics” deserve attention and support of EU on both economic and social levels. These countries are: Georgia, Ukraine, Azerbaijan, Armenia, Moldova and Belarus. It is to be highlighted that Eastern Partnership is not the way for becoming the EU member for any country.

According to the experts development of Eastern Partnership programme was conditioned by following important issues:

a) Geo economic interest – access to markets of six neighbour countries would be attractive for EU, which would be quite difficult to achieve without reforms and incentives leading to EU standards;

b) Geo political interest – diversification of energy resources supply channels (avoiding Russia) or/and strengthening existing supply channels /ensuring safety

c) Neighbour countries’ interest towards EU On economic, social and political levels is different in all six countries, due to Russia’s factor.

Interests of these six countries to EU are as following:

- a) Political benefit;
- b) Economic benefit;
- c) Diversification of geo political relations and/or future prospective for EU integration (not based on this project, but cooperation in general).

It is also to be mentioned that development of EaP programmes is associated with the fact that its predecessor “Liaison” programme was already being implemented by EU and its eastern neighbours (ENP AP), and the new EU initiative was necessary for showing support to eastern neighbours and partners.

It is to be mentioned, that significant argument for starting Eastern Partnership was Russian – Georgian War of 2008, which opened new window of opportunities to the supporters of eastern expansion of EU (Poland, Sweden, Baltic countries and so on), in order to persuade their opponents (France, Spain, Germany, Italy) in the need for such programmes.

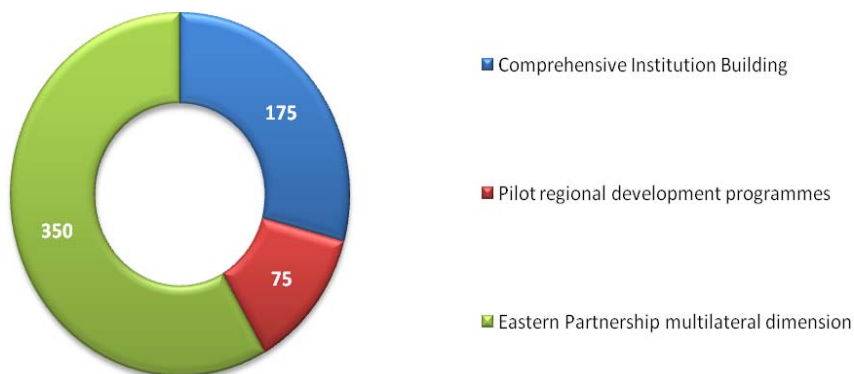
## **6.2 Funding of the Eastern Partnership Program**

Within the frame of Eastern Partnership EU provides financial support to its partners, on their way to coming closer to EU standards

in different fields, for example: democratic governance, market economy, environment, and the rule of law and so on. In order to achieve this purpose EU systematically increases the volume of funding, however it is not possible say that allocated funds are definitely enough for significant changes in particular fields.

In 2009 the budget for 2010-2013, defined by Eastern partnership programme compiled 600 million Euros (\$804million),<sup>86</sup> distribution of which to priorities by years is demonstrated in diagrams #1 and #2.

**Diagram #1 .** EaP funding by sectors 2010–2013 (million Euros)



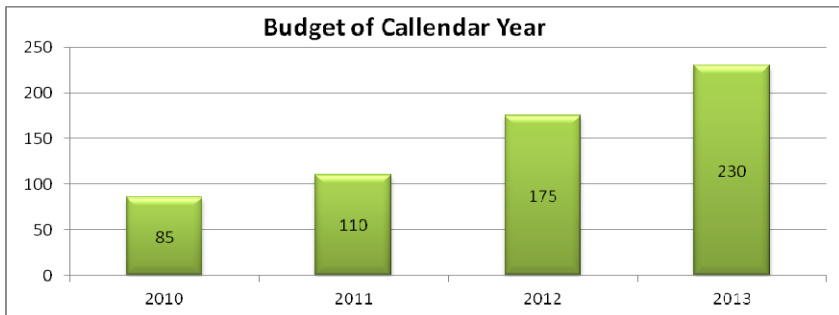
**Source** Handbook on the Eastern Partnership funding

[http://www.eas.europa.eu/eastern/docs/eap\\_vademecum\\_en.pdf](http://www.eas.europa.eu/eastern/docs/eap_vademecum_en.pdf)

<sup>86</sup> European commission, European external action service: [eastern/docs/eap\\_vademecum\\_en.pdf](http://www.eas.europa.eu/eastern/docs/eap_vademecum_en.pdf)

It is to be mentioned however, that these funds are not the maximum which the neighbour countries can receive from EU for various needs. Additional funding can be received from the following instruments: a) Macro-Financial Assistance, b) European Instrument for Democracy and Human Rights, c) Programmes for Non State Actors and Local Authorities, d) Instrument for Stability, e) Eastern Partnership Integration and Cooperation.

**Diagram #2.** EaP funding by years (million Euros)



**Source** Handbook on the Eastern Partnership funding

[http://www.eas.europa.eu/eastern/docs/eap\\_vademecum\\_en.pdf](http://www.eas.europa.eu/eastern/docs/eap_vademecum_en.pdf)

It is to be highlighted that for purpose of supporting the reforms implemented by the partner countries, EU moves to new principle of financing – “more for more”, i.e. more support from EU for success of partner countries on the way of democratic reforms. Good demonstration of this principle is possibility of getting additional funding with the help of above mentioned instruments; for example: EaPIC (Eastern Partnership Integration and Cooperation) is open for all countries of Eastern Partnership and in 2012 – 2013 its total budget compiled 130 million Euros.

As for Georgia, Stefan Fule mentioned that more for more principle acknowledges government's achievement in direction of the reforms and good governance. This is reflected in additional allocation of 22 million Euros in 2012, for ensuring fair and transparent elections.<sup>87</sup>

It is to be mentioned that EU supports to accumulation of investments in Eastern Partnership countries, with the help of EIB. Within the frame of this program EIB enables Eastern Partnership programme countries and Russia and to take loans in total amount of €3.7 billion, in 2007 – 2013; for further development of following sectors: transport, energy, media and communications. EIB supports implementation of infrastructural projects in Georgia, for example: construction of high power transmission lines, budget of which compiles 80 million Euros.

### **6.3 Eastern Partnership and Georgia Achievements and Perspectives**

On 15 May 2012 EU High Representative for European Commission and Foreign Affairs and Security Policy adopted a joint communiqué, which contained Eastern partnership road map. It is public document, which means that civil society can monitor the process of implementation of the liabilities by EU and its partner countries. In this regard civil society forum and its national platform are very active especially in Georgia.

It is to be mentioned that the survey was conducted in all six countries of Eastern Partnership, which assessed each country according to particular parameters, with relevant indexes. According to mentioned survey, Georgia with its achievements got second

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<sup>87</sup> <http://www.interpressnews.ge/ge/thvalsazrishi/207142-aghmosavlethis-partniorobasaqarthvelo-da-evrokavshiri.html>

position among six countries - in management, connection and harmonization (see table #3). Georgia is behind Moldova, which means that it was not the best “student” of EU, as it was always said by the government of Saakashvili.

**Table #3.** Comparing countries according to their achievements

<b>Index / Country</b>	<b>Georgia</b>	<b>Moldova</b>	<b>Ukraine</b>	<b>Armenia</b>	<b>Azerbaijan</b>	<b>Belarus</b>
connection	<b>0.51</b>	0.69	0.64	0.41	0.36	0.31
harmonization	<b>0.60</b>	0.65	0.57	0.59	0.44	0.31
management	<b>0.51</b>	0.53	0.45	0.31	0.31	0.22

**Source** Eastern Partnership Index <http://www.eap-index.eu/index2>

Table #4 can be used for detailed analyses of above mentioned table. Table #4 clearly demonstrates where Georgia is according to single parameters, for example the table shows that awareness regarding Euro integration is on zero level in Georgia, while participation of civil society in EaP reaches almost maximum value (0.9 out of possible 1.0).

**Table #4.** Indexes for Georgia (2011)**Source** Eastern Partnership Index

<b>Management 0.51</b>	<b>Index</b>
INSTITUTIONAL ARRANGEMENTS FOR EUROPEAN INTEGRATION  (coordination and implementation)	0.65
LEGAL APPROXIMATION MECHANISM	0.67
MANAGEMENT OF EU ASSISTANCE	0.64
TRAINING IN THE FIELD OF EUROPEAN INTEGRATION	0.21
AWARENESS RAISING ON EUROPEAN INTEGRATION	0.00
<i>PARTICIPATION OF CIVIL SOCIETY</i>	0.90

<b>Approach -0.60</b>	<b>Index.</b>	<b>Connection 0.51</b>	<b>Index</b>
<i>DEEP AND SUSTAINABLE DEMOCRACY</i>	0.59	<i>POLITICAL DIALOGUE</i>	0.56
Elections	0.40	Bilateral Institutions	0.52
Freedom of Media	0.63	Multilateral Institutions	0.91

Human Rights 0.55	CFSD/ESDP Cooperation 0.25
Independent justice 0.73	<i>TRADE AND ECONOMIC INTEGRATION 0.49</i>
Public Administration 0.47	Trade turnover: Goods 0.38
Tackle with Corruption 0.78	Trade barriers: Goods 0.89
Accountability 0.57	Services 0.20
<i>2. MARKET ECONOMY AND DCFTA 0.67</i>	Foreign direct investments 0.23
Business Environment 0.72	Trade defence instruments 0.78
Sectorial Transition 0.48	Sectorial Cooperation 0.46
DCFTA 0.81	Freedom, security and justice 0.47
<i>3. SECTORAL APPROXIMATION 0.81</i>	Energy 0.58
Freedom, Justice and Security 0.67	Transport 0.31
Energy sector: Legal approximation and policies 0.42	People to people relations 0.45
Transport: Regulation policies 0.54	Mobility 0.38
Environmental Protection and	Participation in EU programs 0.53



Sustainable Development 0.45	
Education, Culture, Information technologies use level 0.59	Assistance 0.57
	Overall EU Development Aid 0.70
	European Neighbourhood and Partnership Instrument 0.48
	Thematic instruments and programs and special technical assistance 0.46
	European financial institutions 0.62

<http://www.eap-index.eu/georgia>

Participation in Eastern Partnership in 2011 - 2013 together with other benefits will bring minimum 180.29 million Euros to Georgia. Besides EU proposes various tools for supporting Georgia:

- **Association agreement**

This programme was officially started on 15 July 2010, in Batumi, during official visit of EU Commission vice president Ms. Catherine Ashton to Georgia. Association agreement officially substituted previous project PCA and this demonstrated that EU will continue cooperation with Georgia and provide opportunity for integration.

With solid democratic background Georgia has chance for rapid move to association, which will provide long term stability and

welfare – stated Stefan Fule in 2012.<sup>88</sup> According to experts this statement meant that elections in Georgia were fair and that signing association agreement will be inevitable process in 2013. Moreover, this issue should be resolved in May 2013 to be signed and entered into force by the Vilnius summit in November.

- **Simplification of the visa regime**

After Russian Georgian war EU and its member states started active discussions on simplification (or abolishment) of visa regime with Georgia, but real steps were made in December 2010, when EU Parliament signed relevant document.

Despite of the statement made in EU Commission report of 2013, that Georgia had significant achievements in simplification of visa regime and readmission,<sup>89</sup> I think that reduction of the number of necessary documents and the fee from 60 Euros to 35 Euros could not be considered as real achievement and that much more should be done for provision of better conditions, maximum of which could be abolishment of visa regime.

In general despite of particular achievements with this regard, there were no significant changes took place during the last years, however we hope that there will be great success at the Summit in Vilnius. In this case Georgia might get maximally simplified visa regime with EU, which could mean movement without visa in EU countries up to 3 months for Georgian citizens. We have such regime with Turkey.

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<sup>88</sup> <http://www.interpressnews.ge/ge/thvalsazrиси/207142-aghmosavlethis-partniorobasaqarthvelo-da-evrokavshiri.html>

<sup>89</sup> Joint working document implementation of ENP in Georgia, achievements in 2012 and recommendations, Brussels 20 March 2013.

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It is to be mentioned however that this agreement will not allow Georgian citizen to work in EU.

- **The Deep and Comprehensive Free Trade Agreement (DCFTA)**

This is an agreement which aims implementation of quality standards and removal of tariff and non tariff barriers, for purpose of improving conditions for trade between Georgia and EU and other countries. This agreement has double importance for Georgia, since in 2011 Georgia's export and import with EU compiled 15% and 31% of total turnover respectively.

At this stage Georgia has Special System of preferences for development and good governance - GSP+, which ensures preferences for developing countries (reduced or special tariffs). The system covers 7200 types of products which could be imported to EU with special conditions in the event of proper adherence to sanitary and phytosanitary norms. However, Georgia's strategic goods – wine and mineral waters are not included in “GSP+” list and consequently are fully taxed while imported to EU market. It is to be mentioned that Georgian exporters export less than 50 types of product out of given 7200 products (e.g.: 2010 – 25 types, 2011 – 39 and 2012 – 34).

In difference form “GSP+”, DCFTA will provide Georgia with an opportunity for trading with EU in free trade regime, of course in case of compliance with relevant standards. The economists assume that ensuring compliance with EU standards in short period of time, will be expensive as for the Government of Georgia so for private organizations, however it will be really profitable in long term prospective.

According to the results of survey implemented by UNDP, enactment of free trade regime between EU and Georgia, could have the following results: <sup>90</sup>

1. Insignificant negative impact on fiscal revenues;
2. Insignificant positive influence on all sectors of local production;
3. Purchasing power of population will be increased as well as nominal GDP;
4. In parallel with increase of trade turnover between the parties, increase of direct investments to Georgia is expected.
5. Clear demonstration for international community that Georgia is on right track of stable democratic development and improvement of relations with EU.

DCFTA will facilitate improvement of trade, financial and other relations between the parties. Diversification of export is important for Georgia and namely this is offered by DCFTA. In case of reaching agreement all tariffs will be abolished fully or gradually, which is more attractive for us, since Georgian market is already open for EU.

- **Facilitating harmonization of legislation**

Harmonization of EU and Georgia legislation is one of the key requirements for Georgia's EU integration, and consequently new Government of Georgia started reforms in different fields. Georgian

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<sup>90</sup> Garepo ჯ., Fill., Assessment of the impact of possible free trade agreement between EU and Georgia , Tbilisi, UNDP 2007

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legislation is still often argued and criticized by EU, since : 1) intellectual property; 2) the law on competition; 3) technical barriers to trade; 4) sanitary and phytosanitary norms; 5) quality of freedom of media do not comply with relevant standards.

- **Civil Society Forum and National Platform**

The goal of Civil Society Forum is to encourage development of civil society and its cooperation with civil societies of EU partner countries.

Eastern Partnership Civil Society Forum, meets with one year intervals since 2009. To date, more than 100 organizations (NGOs, trade unions and so on) are consolidated in National Platform of Civil Society Forum of Georgia.<sup>91</sup>

In general, Eastern Partnership is not simple process. The specialists assume that fulfilment of all recommendations requested by Eastern Partnership would cause weakening of former Government of Georgia (National Movement), thus it just neglected the mentioned recommendations:<sup>92</sup>

a) Reforms in judiciary system, despite the fact that EU quite often highlighted the need for their implementation;

b) Improving quality of freedom of media

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<sup>91</sup> Eastern Partnership Georgia

<http://eapnationalplatform.ge/index.php?a=main&pid=146&lang=geo>

<sup>92</sup> Source:.. David Rinnert. "The Eastern Partnership in Georgia." 2011 year. P13-15.

c) Labour Code was not improved, because changing the ultra liberal norms might reduce direct foreign investments, which would not be beneficiary from political point of view.

Former government of Georgia always tried to rise the mobility issue (since it was popular among population), which meant abolishment of visa regime with EU in long term prospective; for this purpose Georgian government introduced biometric ID in 2010 – 2011.

#### 6.4 EU – Georgia Trade

According to data of Geostat, EU is the biggest partner for Georgia, by January 2013 EU share was  $\frac{1}{4}$  of total export of Georgia and  $\frac{1}{3}$  – of import.

Trade of EU – Georgia increased several times in absolute and percentage figures, since 2005 (see table #5) and in 2012 export in absolute figures compiled 353 million GEL and import – 2427 million GEL, which can be considered as positive for EU, but negative for Georgia due to worsening already negative our trade balance with EU. For example: in 2005 our export to EU was just 3.5 less than import, in 2012 the same figure nearly doubled and reached 6.8.

**Table #5.** Georgian Trade balance and EU share in it (million GEL)

	2005	2006	2007	2008	2009	2010	2011	2012
Export total	865	936	1.23 2	1.49 5	1.13 3	1.67 7	2.18 9	2.37 7
Export	216	225	268	335	237	309	424	353

t EU								
Import total	2.487	3.674	5.212	6.301	4.500	5.257	7.057	7.842
Import EU	740	1.104	1.538	1.756	1.335	1.467	2.053	2.427

**Source:** Geostat

[http://geostat.ge/?action=page&p\\_id=136&lang=geo](http://geostat.ge/?action=page&p_id=136&lang=geo)

As demonstrated by table #5 GSP+ did not give positive results to our trade balance and due to objective reasons we do not think that DCFTA can do this in short or medium prospective (if ever).

However we can conclude that improvement and simplification of economic relations with EU can be the step forward not just form economic but also from political or security point of view, which is not less important for us due to our national interests and geo political condition.

## 6.5 Conclusion

Nowadays in Georgia is transition period. There are several important reforms undergoing in important spheres of state that may determine the overall development of the country in the nearest future. First of all our main task is the following: to build stable democratic institutes, to strengthen the fundamentals of steady economy, the latter is impossible without the cooperation with the European Union besides the negative sides that this processes can be accompanied.

## II. EU INTEGRATION ISSUES IN THE SOUTH CAUCASUS

### **1. The Performance of South Caucasus Countries (Georgia, Armenia, Azerbaijan) in Terms of EU Integration: The Case of Deep and Comprehensive Free Trade Agreements (DCFTA)**

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**Krzysztof Senger**

**The Head of the European Programmes Office**

**at Adam Mickiewicz University**

#### **1.1 Introduction**

This study addresses the free trade negotiations between the European Union (EU) and the South Caucasus (C3) countries, and how they progressed during the 2009-2011 period. In this respect, the European Commission's reports on implementation of the European Neighbourhood Policy for these periods are highly important. This analysis is especially interested in the framework for the negotiations between the EU and the South Caucasus countries on the Deep and Comprehensive Free Trade Agreements (DCFTA). Furthermore, it compares the rationale behind the political process and the substance in the trade talks with International Business research. It should be noted that DCFTAs remain a central part of the association agreements of the Eastern Partnership. Negotiations on association agreements are launched with the decision to start negotiations on DCFTAs with Georgia taken in December 2011 and with Armenia in February 2012. Azerbaijan has yet not achieved one of the preconditions for launching DCFTA negotiations, namely the membership of the World Trade Organization (WTO),



The preparation process for the DCFTA aims to foster a deeper integration both politically and economically into global and, above all, EU markets. It could have a great impact on the international competitiveness of South Caucasus companies, since the rationale behind free trade is to build a comparative advantage [The Heckscher–Ohlin model (H–O model)]. However, one should remember the importance of trade costs [Krugman 1980], so the South Caucasian countries should develop specializations to overcome the drawbacks of the poor innovative structure of their economy which could hamper long-term export opportunities. The fact that the terms of trade change over time due to a shift from demand for primary products to demand for manufactured goods should not be ignored. Developing economies should diversify their export structures, thus enhancing their manufacturing industry. One of the solutions is to attract Foreign Direct Investment (FDI) in the fields of knowledge intensive industries. Henceforth, this could create a foundation for new and innovative branches of their economies, thus diversifying their trade structures.

Nowadays, competition on the global market entails all aspects of innovation. Those connected with the OLI paradigm [Dunning 1998], i.e. ownership, location, internationalization can be developed under the DCFTA framework. For example, in order to attract more foreign investment, necessary local potential must be built together with the development of clusters and joint efforts to facilitate business-to-business relations. A critical mass of local cooperation linked to Foreign FDIs could foster domestic investments as well. The DCFTA will help the South Caucasus countries to attract investors, by cutting red tape (e.g. competition policy, food safety and intellectual property rights) and building the right business climate. Another important aspect of trade liberalization is to lower costs, thus creating the advantage of economies of scale.

On the one hand, trade is better than aid. For gaining independence from the finance of international institutions and putting a country's foot firmly on the development ladder, there is nothing more helpful than international trade. On the other hand, well directed aid for export support and capacity building can intensify the pace of development. The impact of the financial crisis on developing countries had several consequences, including a decrease in export revenues and a decrease in FDIs [The AidWatch 2009]. The higher than usual risk aversion towards the South Caucasus led to a lower level of investment, while there was a lower energy demand due to the global crisis at the same time. These factors had a significant impact on exports. International trade could significantly improve the competitiveness of the South Caucasus products and better investment incentives for attracting more and more stable FDIs. This, in turn, could create a positive impact on the socio-economic development of the South Caucasus region. Some analysts of the DCFTA negotiations process claim that the agreement is only half of the modernization process and it will take a long time to achieve all the necessary milestones of a market economy [For example, see: Wijkman 2011].

The South Caucasus countries' political association and economic integration with the EU, and the efforts to improve trade relations and mobility for its citizens remains a challenging task which needs a long-term vision.

## **1.2. Cooperative Actions**

Negotiations with the EU lead to a very important consequence for the South Caucasus countries, namely closer cooperation among them. Development of regional cooperation is one of the best tools providing stability for the South Caucasus. Thus, it is worth mentioning some of the indicators. For example, Armenia,

Azerbaijan, and Georgia created a joint management for the Regional Environmental Centre for the Caucasus (REC) in 2009. The work of the REC for the Caucasus consists of environmental policy and local environmental action plans. Another example, the Southern Caucasus Integrated Border Management (SCIBM), promoted by the EU between Georgia, Armenia, and Azerbaijan, began operating in March 2010.

In terms of trade, the most visible cooperation took place between Azerbaijan and Georgia. Two countries acted together on export items such as liquefied natural gas and compressed natural gas from Azerbaijan, through a Georgian Black Sea terminal and worked towards a Euro-Asian Oil Transportation Corridor.

One of the most challenging tasks within the negotiations effort is to diversify the export structure of each country. A very important factor for achieving that is research and development expenditure. If a country is to gain from free trade, it must diversify its economic activity and specialize in new areas. The R&D sector is an important driver, strengthening the power of exporters. If the South Caucasus countries want to build a comparative advantage, a high level of expenditure on R&D, both public and private, is a necessity. Thus, it is worth noticing that Armenia, Azerbaijan, and Georgia cooperated for the first time in the areas of higher education, distance and e-learning.

### **1.3 Country-by-country negotiation progress – what is visible from the European Commission perspective**

#### *Georgia*

Everything starts with the political will, which was shown in 1996 through a Partnership and Cooperation Agreement in this case. This

agreement which entered into force in 1999 was the beginning of contractual relations between Georgia and the EU. It took seven years to arrive at the point where the EU-Georgia ENP Action Plan was approved and launched (similarly to Armenia and Azerbaijan). The Action Plan was approved in November 2006 for a five year period. Another leap forward took place in May 2010 when the negotiating directives for an Association Agreement were adopted by the EU. This created the appropriate framework for the future Association Agreement, in which negotiations on the Deep and Comprehensive Free Trade Area (DCFTA) were foreseen to start, provided that the necessary conditions have were met [European Commission, 12/05/2010].

In the European Union development model, everything needs a plan. Therefore, a draft of strategic reform plans was put in place in 2009. It was at this moment that Georgia showed readiness and strong political will to implement the EU's recommendations which would pave the way for starting DCFTA negotiations. A very important ingredient of the DCFTA process is to build administrative capacity. In 2010, the Georgian National Investment Agency (GNIA) established an Export Promotion Department, which demonstrated the commitment of the Georgian authorities. Negotiations on an EU-Georgia Association Agreement were launched in July 2010 and in the EC's opinion, they progressed at a good pace [European Commission, 25/05/2011]. In terms of red tape and Georgia's capacity for the trade negotiation process, progress was made in 2011 as Georgia introduced reforms in the field of technical barriers to trade, food safety, competition and intellectual property rights. Accordingly, the Georgian government worked on Free Trade and Competition regulations, including very important issues from the European Commission's perspective, i.e. merger control and state aid.

In 2009, EU exports to Georgia declined by 27.9%<sup>93</sup> compared to the previous year. During 2010, EU exports to Georgia increased by 31.6% compared to the previous year. In 2011, EU exports to Georgia increased by 36.9%.

In 2009, exports of Georgian products to the EU decreased by 34.8%, while in 2010, exports of Georgian products to the EU increased by 7.1%. In terms of Georgia's exports structure to the EU, mineral products formed 71.8% (in 2010). In 2011, EU imports from Georgia increased by 8.2%. Primary products such as fuels and mining products formed 69.1% of imports from Georgia.

Total bilateral trade amounted to EUR 2.2 billion in 2011, indicating a more dynamic recovery of EU exports to Georgia compared to imports from Georgia. The trade deficit, at 22.9% of GDP in 2010, increased further in 2011 to around 28.7% of GDP. This high trade deficit was partly offset by growing tourism revenues and currency transfers (remittances). Recovering FDI and official assistance also helped finance the current account deficit. In 2011, FDI was estimated to have reached EUR 650 million (around 6.3% of GDP), against EUR 440 million (5% of GDP) in 2010.

In July 2010, the EU and Georgia concluded negotiations on a bilateral agreement for the protection of their respective 'geographical indications'. The agreement, which is the first of this kind with an ENP partner, will foster trade in agricultural products and foodstuffs originating in the territories of both Georgia and the EU.

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<sup>93</sup> the database used in this article is of DG TRADE, see <http://ec.europa.eu/trade/creating-opportunities/bilateral-relations/statistics/>; and from the EC Implementation reports

During the 2009-2011 period, Georgia benefited from the special incentive arrangement for sustainable development and good governance — the GSP+ — within the EU's Generalised System of Preferences (GSP). These preferences aim to assist in diversifying Georgia's export structure and improving its export performance. However, benefitting from this is conditional on the country's compliance with international conventions on human and labour rights, environmental protection and good governance [European Commission, 15.5.2012].

During the negotiations process, both diversifying Georgia's export base and attracting foreign direct investment were at the center of talks. However, these two cannot be treated separately. Although, preferences were the means of diversifying Georgia's export structure and improving its export performance during this period, the issue of how to drive innovation was neglected.

### *Armenia*

During the period under analysis, Armenia significantly made progress in the area of customs and border management. The lack of diversified exports and the closed borders with two neighbouring countries were identified as main obstacles. At the same time, the Armenian authorities were encouraged to provide more competition to the private sector and create a hostile business climate [European Commission, 25/05/2011].

Foreign direct investment increased to 6.4% of GDP (6% in 2010) and it is expected to reach approximately USD 650 million (around EUR 500 million) for the full year (a 16% increase over 2010) [European Commission, SWD(2012) 110 final]. EU exports to Armenia in 2009 declined by 20.6% compared to the previous year, while EU exports to Armenia increased by 4.2% in 2010. Exports of

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Armenian products to the EU decreased by 49.3% in 2009 and exports of Armenian products to the EU increased by 59.9% in 2010. In terms of commodity structure in particular, base metals formed 61.9% and pearls and precious stones 19.1% of Armenia's exports to the EU.

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

In 2009, Armenia established an institutional structure for the preparatory and future negotiating process, which still needs to become operational. Some progress was made on the free movement of goods and technical regulations. A number of new draft laws and amendments to existing laws that affect technical barriers to trade were prepared. During the period between 2009 and 2011, Armenia prepared itself for the DCFTA negotiations with the EU by implementing the "key recommendations" made by the European Commission on the basis of the 2009 fact finding mission. The government presented a strategic approach to some of the most important trade-related issues, such as intellectual property, quality infrastructure reform and the food safety system. In 2010, Armenia started talks on expanding its exports to the EU to include fish and fishery products.

The institutional capacity remained an issue during the whole period of the negotiations. Particular actions were taken such as legislative

and institutional reforms (an Institutional Reform Plan) in the areas of Technical Barriers to Trade, Sanitary and Phyto-sanitary Standards and Intellectual Property Rights. Substantial EU assistance was provided on trade-related issues. The Eastern Partnership Comprehensive Institution Building programme provided EUR 32 million for Armenia in 2011-2013 in support of DCFTA negotiations, together with EUR 22 million to help reforms in public finance management and public sector transparency, related to the DCFTA [European Commission, SEC(2010) 516].

### *Azerbaijan*

In political terms, during 2009-2011 EU-Azerbaijani bilateral relations strengthened, with particular focus on cooperation in the field of energy. The EU welcomed some of the Azerbaijani efforts, such as its support for the Southern gas corridor. Nonetheless, progress of negotiations on its accession to the World Trade Organization (WTO) and the related talks were not significant in bringing Azerbaijan closer to the WTO [European Commission, SEC(2010) 519]. Azerbaijan did not become a member of the World Trade Organization (WTO), and as a result, negotiations on the Deep and Comprehensive Free Trade Area (DCFTA) could not be launched. The increase in the visibility of Azerbaijan as an EU trade partner is confirmed by the growing presence of EU states in the country. Furthermore, European companies from the energy sector have invested in Azerbaijan, thus demonstrating the strategic destination of their activities in the region for years to come [E. Nuriyev, 2008].

Within the Eastern Partnership (EaP), the EU and Azerbaijan continued to strengthen their relations. Following the adoption of negotiating directives for an Association Agreement, negotiations were launched in July 2010 in Baku. In 2011, a Joint Declaration on



the Southern Corridor was signed, demonstrating the commitment of both sides to ensuring energy supplies to the European gas market [European Commission, SEC(2011) 640]. At the same time, the EU launched negotiations with Azerbaijan and Turkmenistan on the construction of the Trans-Caspian gas pipeline system [European Commission, SWD(2012) 111 final]. Azerbaijan plays a significant role in the EU's energy security.

During the period between 2009 and 2011, energy was the main revenue basis for Azerbaijan, the oil sector accounting for around half of the country's GDP and almost all of its exports.

Both exports and investment bounced back after contracting in 2009. In 2010, exports rose by 14.5%, driven by increasing global demand and higher oil and gas prices. Investment rose by 6%, linked to a slight recovery in foreign direct investment (FDI). The trade balance ran a surplus of around 38% of GDP in 2010, compared to 34% of GDP in 2009. Higher oil prices boosted export revenues and dwarfed increases in import spending.

Azerbaijan sustained oil and gas exports, particularly through the Baku-Tbilisi-Ceyhan (BTC) and Baku-Tbilisi-Erzurum oil and gas pipelines. In 2010, oil from Turkmenistan was shipped over the Caspian Sea and exported through the BTC pipe.

No meeting of the WTO Working Party convened in 2011 as Azerbaijan did not make the required progress and did not circulate sufficient information. Negotiations advanced slowly on upgrading the trade-related provisions of the Partnership and Cooperation Agreement, including a non-preferential trade part [European Commission, SWD(2012) 111 final].

## 1.4 Conclusions and Recommendations

In terms of preparation for the DCFTA's negotiations process, Georgia and Armenia made sufficient progress for meeting the criteria. Nonetheless, Armenia still needs to strengthen its efforts to meet EU expectations. In terms of the pace of change and trade related institutional capacity, Georgia remains the leader of the South Caucasus countries. In the case of Azerbaijan, the EU's priorities make the country a strategic partner in energy related exports. However, the DCFTA negotiations are still on the long-term agenda, with WTO accession as a precondition.

Although a strong R&D sector remains central to innovation, investment in research and innovation in all C3 countries remains at a low level. Georgia participates in the 7th Framework Programme (FP7), with 26 projects, receiving just over EUR 2.54 million. Armenia has 22 FP7 projects, receiving over EUR 1.27 million of EU funding. Azerbaijan is involved in 13 FP7 projects, receiving EUR 780,000 of EU funding. More effort is needed to build an R&D sector that could attract knowledge intensive investment and trade.

South Caucasus companies should be supported in their efforts to compete on the international market. Aid programmes should be directed at trade support such as sales promotion, sponsored foreign trade shows, trade missions, support for brand promotion, information on foreign markets, or investment support. In this way, South Caucasus businesses could prepare themselves to benefit fully from Free Trade.

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## **2. sector policy CONVERGENCES IN AZERBAIJAN to support eu eastern partnership initiative**

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**Vugar Bayramov, Ph.D.**

**Centre for Economic and Social Development, Azerbaijan**

### **2.1 Introduction**

The EU single market with about 500 million consumers is the largest in the industrialised world, making it specifically attractive for neighbouring countries to harmonise their laws and regulations for better trade relations and economic integration. There is a huge economic, social and geopolitical reason and interest at government and societal levels in Azerbaijan towards effective European integration. Moreover, EU expressed its interest in sectoral convergences with EU policies and policy reforms in Azerbaijan via the Partnership and Cooperation Agreement (PCA) between EU and Azerbaijan, and European Neighbourhood Policy (ENP). The EU's recent widening towards South-East provided the EU with growing responsibility to help the neighbouring countries address the socio-economic challenges, and with closer political ties and energy security strategies with more involvement of the neighbouring countries.

The Eastern Partnership (EaP) endorsed by the European Council in March 2009 aims at development of a specific Eastern dimension of ENP. EaP emphasizes several priority areas and growing cooperation, including a border management program, the Southern corridor, integration of economies, improved mobility and contacts

among people and businesses. All these make convergence of policies of EaP countries in the field of *trade and cross-border cooperation* with respective policies of EU very important to facilitate the implementation of EaP priorities and overall EU policy and goals in Azerbaijan and the region.

## 2.2 POLICY LANDSCAPE IN PRIORITY AREAS

The analysis below indicates that the priority areas of TBT and customs in this paper have a larger importance and demonstrate bottlenecks to be addressed towards EU-Azerbaijan cooperation first, and EaP policy convergences in these areas will also have indirect impact on every EaP priority, including border management programme, the Southern corridor, integration of economies, improved mobility and contacts among people and business.

Below is the analysis of TBT and customs, including the mapping of the policy landscape and analysis of facilitation of and assistance in the accession of Azerbaijan to WTO, and promotion of overall European integration in the context of the subject areas.

### *EU Customs Policy*

For EU businesses, the starting pointing is the bilateral EU-Azerbaijan relationship and the Partnership and Cooperation Agreement (PCA), especially its trade and investment provisions. As the PCA's trade and investment provisions are largely based on WTO principles, Azerbaijan's accession will reinforce at an international level those principles and protections existing at bilateral level and establishing this added degree of legal certainty is absolutely key to ensure greater trade and investment by EU businesses to the benefit of Azerbaijan's economy beyond just the energy sector.

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The added transparency imposed by the WTO is a prerequisite for trade and investment in the majority of the areas of greatest interest to EU businesses, besides oil and gas and hydrocarbon transit:

- Financial services
- Consumer goods
- Agriculture and food
- Information technology
- Telecommunications
- State procurement

WTO accession commitments in these areas are a guarantee for EU businesses that, regardless of the levels of practical implementation, Azerbaijan is bound and potentially subject to that discipline.

The Customs Law is an essential element of the EU single market and has huge implications for its four basic freedoms (free circulation of goods, persons, services and capital). With no internal economic frontiers it is the catalyst for the economic integration of the European Union. Thus the effects of the Community's Customs Union (CU) are far reaching. To set up, develop and run a single common market, wherein goods circulate freely, can only be achieved within the framework of a CU where common rules are applied at external borders. CU is a secure basis for highly developed integration.

Without the Community's CU, the EU common commercial and development policy, its common agricultural market and an effective coordination of economic and monetary policies would not be possible.

The basic principles of CU are:

- To establish universally accepted rules and principles that have proved their efficiency;
- To abolish gradually the customs duties that applied in trade between the original six member states and to introduce a Common Customs Tariff (CCT) applicable to goods imported from third countries. On 1st July 1968 the tariff union was accomplished. Since then any new Member State joining the Community has undergone the process of abolishing duties on intra-Community trade and aligning its external tariff to the CCT;
- A growing harmonisation and further simplification of customs procedures resulting from the necessity to facilitate trade, e.g. the Single administrative document and the combined nomenclature were introduced. In parallel, the EEC-EFTA Convention on a Common transit procedure was signed on 20 May 1987; and
- The consolidation of virtually all the Community customs provisions into a single coherent text, the Community customs code and its implementing provisions which entered into force on 1 January 1994.

CU was one of the EU's earliest milestones. It abolished customs duties at internal borders and put in place a uniform system for taxing imports into the EU from third countries. As a result, internal



border controls subsequently disappeared and today customs officers are found only at the EU's external borders.

The main objectives of the Common Customs Policy of the EU are:

- to foster world trade;
  - to promote fair trade relations;
  - to increase the attractiveness of the EU as a location for industry and trade and contribute to the creation of new jobs;
  - to promote development elsewhere;
  - to assist the candidates for accession in their future role;
  - to ensure protection for the Community's citizens and business in all areas involving imports or exports in a clear, uniform, simple way as efficiently as possible;
  - to 'ring fence' the single market, securing the maximum benefit from it for everybody;
- to facilitate a practical system to collect revenues, customs duties, VAT and excise duties; and to collect essential statistics on trade.<sup>94</sup>

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<sup>94</sup> Jafar Alakbarov, Ulviya Abdullayeva, and David Parsons, *Scoreboard Report On Customs Law*, [http://pca.az/uploads/Customs\\_final.doc](http://pca.az/uploads/Customs_final.doc) (accessed November 1, 2010).

### *Azerbaijan Customs Policy*

The State Customs Committee of Azerbaijan Republic (SCC) which is the main State authority in the area of customs was established by the Presidential Decree Nr. 561 on 30 January 1992. SSC adopts in the area of customs legislation: decrees, regulations and instructions. Since 1995 these acts are regularly published in the Committee official newspaper “Gömrük xəbərləri” (Customs news). The list of normative acts is presented in Annex 1.

According to the Statute of SSC approved by the Decree of the President Nr. 7 from 27 October 1998, the Committee is the central executive authority which implements state customs policy and has the following functions:

- Realisation of single customs policy;
- Provision of unity of the customs territory;
- Organisation and improvement of customs;
- Securing economic interests and economic safety of Azerbaijan Republic;
- Use of progressive methods of customs regulation;
- Control after execution of which was obligated on it;
- Securing compliance with the customs and other legislation.

The Committee bears responsibility for:

- Fighting customs crimes and preventing illegal carriage of narcotic drugs, weapons, articles of artistic, and items of historical and archaeological importance;

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- Collecting taxes, customs duties, excise duties and other customs payments on goods transferring customs border;
  - Controlling the accuracy of defining customs value of goods;
  - Issuing licenses and keeping the records;
  - Providing efficient use of equivalent customs procedures;
  - Keeping customs statistics on foreign trade and specific customs statistics;
  - Organizing forming goods nomenclature of foreign economic activity;
  - Establishing the system of information and consultation;
  - Creating conditions for realisation of rights to appeal of physical and legal persons;
  - Representing the interests of the State in international organizations and implementing international obligations.

Many aspects of organisation of customs activity are reflected also in the Law on approval of the Statue of “The service of the Customs Authorities” from 7 December 1999.<sup>95</sup>

The Government of Azerbaijan has taken the following legislative steps to promote foreign investment :

- 1992 Law on the Protection of Foreign Investments
- 1992 Law on Foreign Investment Activity
- Bilateral Investment Treaties
- Azerbaijan Investment Company

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<sup>95</sup> Ibid.

- Law on the Special Economic Regime for Export Oil and Gas Activity (2 February 2009)
- Law on Special Economic Zones (14 April 2009)

More recently, the GoA has made improvements with its Customs policy. As part of a \$1,694,320 reform project co-financed by the European Commission and implemented by the United Nations Development Programme in 2006-2007, steps were successfully made to prepare Azerbaijan Customs draft legislation in line with EU and international standards. Improvements were also made specifically in modernizing information technologies for customs processing.<sup>96</sup> Separately, Azerbaijan introduced the Single Window system in 2009. "In a theoretical sense, a Single Window can be described as a system that allows traders to lodge information with a single body to fulfill all import- or export-related regulatory requirements."<sup>97</sup> Therefore, the Single Window environment aims to accelerate and simplify the flow of information between traders and the government. This will help increase the flow of trade by streamlining the process and decreasing the transit time of goods going across the borders.

### 2.3 EU Policy on Standardization and Technical Barriers to Trade

Before the harmonization of technical rules or standards of trade in the EU, irregularities between national standards created Technical Barriers to Trade (TBT) that negatively impacted the flow of goods

<sup>96</sup> United Nations Development Programme, "Azerbaijan: Modernization of Customs Services in Azerbaijan," Public administration reform and anti-corruption in Europe & CIS, <http://europeandcis.undp.org/governance/parac/show/80FB8FE5-F203-1EE9-B27BFEEA6C9CE783> (accessed November 1, 2010).

<sup>97</sup> United Nations. *The Single Window Concept*. Geneva, 2003. <http://unpan1.un.org/intradoc/groups/public/documents/UNECE/UNPAN019892.pdf> (accessed November 1, 2010).

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between EU countries. Currently, the three main governing standards organizations in Europe include European Committee for Standardization (CEN), the European Committee for Electrotechnical Standardization (CENELEC), and the European Telecommunications Standards Institute (ETSI). These organizations play a central role in limiting TBT in the European Union and enhancing the ability of trade to flow freely throughout the region. CEN and CENELEC both have one voting member representing the national standards body of each of the 30 member countries, which include the 27 European Union member states, and the 3 countries of the European Free Trade Association. All ratified European standards are then voluntarily adopted as national standards in each country.

Moreover, the European Council created the “New Approach” in 1985 that sets essential requirements that products must meet before they can be distributed on the European Market. As long as manufacturers provide a ‘technical file’, they can choose any technical way to meet these requirements. However, by far the easiest way is to follow the relevant ‘European Standard’, which will gain you access to the European Single Market.

A main TBT that presents problems for international trade is when a country changes technical regulations required for all products without giving manufacturers or governments of other countries time to review the changes. In addition to the 98/34 notification procedure that requires Member states to go through a three-month examination period by other Member States when adopting a new draft, the European Commission has also adopted the WTO TBT notification procedure. Both of these procedures limit barriers and enable competitive and open trade for the Internal European Market. More specifically, the TBT Agreement of the WTO requires all members “to notify their draft technical regulations and conformity assessment procedures and to respect the principles of non-

discrimination between national and imported products, proportionality and equivalence.”<sup>98</sup> This procedure gives WTO Members and producers to have the chance to review all changes to product requirements. The access to open information allows manufacturers to make the necessary changes to their products in order to compete in the international market.

### ***Azerbaijan Policy on Standardization and Technical Barriers to Trade***

The current State Agency on Standardization, Meteorology, and Patents of the Republic of Azerbaijan (AZSTAND) was established by Decree No. 623 on December 27, 2001 to become the main authority for creating and enforcing standardization policy in Azerbaijan. It is backed by the following 6 State standards of law “On Standardization”: (AZS 1.0-96, AZS 1.2-96, AZS 1.3-96, AZS 1.4-96, AZS 1.5-96, AZS 1.6-96). AZSTAND is officially a member of the International Standards Organization.

These are the following Duties of the Agency as stated on a state website<sup>99</sup>:

- To implement the state policy in the field of standardization, metrology, certification and protection of objects of the industrial property

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<sup>98</sup> European Commission. "Single market for goods Prevention of technical barriers to trade." Enterprise and Industry. [http://ec.europa.eu/enterprise/policies/single-market-goods/prevention-technical-barriers-trade/index\\_en.htm](http://ec.europa.eu/enterprise/policies/single-market-goods/prevention-technical-barriers-trade/index_en.htm) (accessed November 1, 2010).

<sup>99</sup> Heydar Aliyev Foundation. State Committee On Standardization, Meteorology, and Patents of Azerbaijan Republic. [http://www.country.az/portal/StatePower/Committee/committeeConcern\\_12\\_e.html](http://www.country.az/portal/StatePower/Committee/committeeConcern_12_e.html) (accessed November 1, 2010)

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- To form the basic directions of a state policy, prepare and provide implementation of target programs, coordinate activities of other state bodies and institutions of local governing, economic subjects in the above-mentioned fields;
  - For the purpose of observance of requirements of standardization and metrology, to take measures of the state control;
  - To provide unity of means of measurements;
  - To organize works on protection of objects of the industrial property;
  - In order to increase the competitiveness and quality of the goods (works, services) made in the territory of the Republic of Azerbaijan, to update normative documents in the field of standardization, metrology, certification and protection of objects of the industrial property, uniting in themselves modern scientific and technical potential and the advanced international practice, and take measures on providing their conformity to modern international practice;
  - In accordance with procedure provided for in the legislation, to implement the state control over the conformity of imported (put into free circulation) and exported goods (works, services) to the requirements of standards, metrological rules and norms, rules of certification and protection of industrial property objects;
  - To implement the necessary measures in the sphere of application of appropriate international standards in the Republic of Azerbaijan;
  - To implement the other duties provided for in the legislation of the Republic of Azerbaijan.

### *Azerbaijan WTO Accession Process*

Government of Azerbaijan (GoA) officially applied to the WTO Secretariat to become a WTO member in 1997, thus resulting from the establishment of Azerbaijan's Working Party in the same year. A group by GoA had been established, with a view to tackling problems before the country in the accession period. GoA submitted a Memorandum on its Foreign Trade Regime on 22 April 1999. Later on, the Permanent Mission of the Republic of Azerbaijan had provided replies to additional questions submitted by Members on the Memorandum on the Foreign Trade Regime - Australia, Japan, the European Union states, and the United States.

Azerbaijan has reached agreement with Georgia and Moldova on bilateral negotiations meanwhile negotiations with other selected countries including US, EC continues. In order to continue negotiations on fair trade principles in the wake of joining the WTO and to develop the documents to be submitted to the WTO by the coordination from related structures, as well as to provide a single economic policy in WTO negotiations, an appropriate Commission consisting of high-rank government officials according to the 22 August 2003 order by the Cabinet of Ministers had been established. To tackle these items, the Commission/Committee had designed nine Working Groups.

## **2.4 RECOMMENDATIONS AND CONCLUSION**

The Government of Azerbaijan has shown slow but promising steps towards modernizing its Customs and Trade sectors to facilitate a greater integration with the European Union. However, there are still many steps that need to be taken to fulfill economic integration goals set by the European Partnership Initiative. The process involved with Azerbaijan's accession to the WTO can simultaneously



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contribute to a more open and trade-friendly environment that follows the spirit of European integration.

In fact WTO accession must remain a priority for Azerbaijan as it:

- It is key to effective economic diversification
- It will render the domestic market more competitive
- It will help domestic companies compete abroad

Despite its strategic location, rapid economic growth and economic reforms, Azerbaijan must adhere to the principles and disciplines of the WTO to attract the greater levels of trade and investment by EU businesses that are warranted in the long run

As much as for its rich but concentrated domestic market, Azerbaijan is of interest to EU businesses from a regional perspective as a promising platform or bridge for expansion. Given Turkey's WTO membership and Russia's impending WTO accession, Azerbaijan's WTO status will necessarily become an increasingly important consideration for EU businesses. As EU businesses elaborate their regional business strategies, WTO membership could well be the decisive factor in attracting trade and investment in Azerbaijan over its neighbors.

Inconsistency and a lack of transparency in the implementation of customs rules and procedures are routinely cited by EU businesses as major hurdles to increased trade with Azerbaijan. EU businesses also highlight greater transparency and consistency in the application of other regulatory provisions and government tenders as necessary to encourage more investment. Through the discipline and coordination that may be imposed under the PCA and WTO in conjunction, EU businesses are accustomed to addressing such issues in many

emerging markets and by increasing transparency and predictability, in a rules-based trade system, the resulting gains for the local economy are likely to be very significant.

By joining WTO, the CIS countries have committed to adjusting local regulations to comply with international norms and to replacing the GOST (Soviet) system with those that meet WTO standards. As a norm, implementation of this commitment has been a **legal limbo**. Consequences are following:

- The GOST system of standards is not recognized in the major export markets (i.e. restricts the acceptability of products in non-GOST markets)
- Barrier to international trade, barrier to innovation as well as costly for businesses

In addition to standards themselves, the procedures through which products are evaluated for conformity to regulatory requirements have important implications for market efficiency and trade expansion.

Example: quality infrastructure (metrology, accreditation, standardization and certification) systems in Kazakhstan and Kyrgyzstan. In this case, negative impact will be on the output of local production, the ability of local suppliers to export products and services, and the start-up costs for new businesses.

Perhaps one of the greatest needs of the Azerbaijan Government with reform efforts has been foreign assistance is drafting modern legislation to meet the requirements of the WTO and other international trading partners. Azerbaijan has shown interest in seeking foreign assistance by participating in multiple programs. An

example is the program implemented by the United Nations Development Programme and co-financed by the PCA and TACIS programs, which was entitled “Modernization of Customs Service in Azerbaijan.” The project aimed at developing customs legislation that was in line with European legislation and international standards. Azerbaijan’s cooperation with an international team of experts led to a successful draft of a new customs code. This is a very positive step for Azerbaijan in becoming a more transparent and efficient trading partner and also follows the goals laid out in the Azerbaijan developed a "State Programme on Development of Customs System of the Republic of Azerbaijan in 2007-2011", which was developed by Presidential Decree in February of 2007. However, this code is still waiting final approval by the President and the Cabinet of Ministers and has not become official law. It is recommended that the Parliament approve this new Customs Code to replace the current outdated Customs Code that was developed in 1997. In addition, if this new Customs Code is adopted, special trainings and seminars should be held to ensure that Customs employees would be able to efficiently implement and operate the new system. Moreover, changes to Customs Code will also help with Azerbaijan’s process of accession to the WTO.

Our research found out also that Ukraine as a Useful Analogy for EU Businesses, since;

- Ukraine’s PCA with the European Union entered into force in 1998, approximately at the same time as Azerbaijan’s (1999)
- However, EU businesses’ confidence in Ukraine has increased markedly since the country’s WTO accession in 2008
- Practical implementation by Ukrainian authorities of many key trade and investment provisions remains problematic

- However, EU businesses are more reassured because recourse is now available under multiple legal regimes
- Ukraine has thus figured more prominently in regional business strategies, whether to supply Ukrainian domestic consumers or as a platform for exports to the European Union, Russia and South-Eastern Europe

The paper found that producers in the CIS countries members of the WTO face;

- diminished demand for their products,
- increased competition from foreign producers, and
- lower prices and release of their potential competitiveness.

Joining the WTO is a great step towards being more connected with the European Union trading partners and the international trading community as a whole. Accession to the WTO requires Azerbaijan to comply with the Technical Barriers to Trade Agreement that would simultaneously comply with trading requirements set by the EU. This agreement aims to create a transparent environment where no technical rules unnecessarily impede trade between countries. As part of the WTO process, Azerbaijan has begun liberalizing its trade regime and has drafted new legislation on TBT. Therefore, it is recommended that Azerbaijan continue the accession process without the delays that have existed in the 13 years since it officially began the negotiations process.

The WTO membership will also lead to increases in direct foreign investment flows and expansion of export opportunity of import-oriented industry. Practices of WTO members show that following

accession, the results are different for each member. The WTO accession attracts direct foreign investment: not only increase the investment into the membership, but also it leads to economic growth. For example, serious improvements are observed in the amount of foreign investments after Kyrgyzstan, a “pioneer” in the CIS-space, joined the WTO. Notably, the WTO is a unique international global institution regulating trade relations between nations. The WTO activity is based on agreements between it and the states. These agreements rest upon negotiations conducted between the countries and are ratified by these countries parliaments. The WTO charter indicates that its key goal is to assist producers, exporters and importers of commodities or services to manage and expand their businesses. WTO membership will promote foreign investment flow into Azerbaijan’s export sectors.

And it means assumption of commitments to protect the right of creditors and from this viewpoint, the regional governments cannot pursue discrimination policy in the foreign investment field after WTO accession. Horizontal investments (investments into the local market) will be directed to the regions where population is densely concentrated and vertical investments (export investments) will target the overseas sectors where more qualified employees are accumulated. On the other hand, regardless of Azerbaijan’s WTO membership, the improvement of the investment environment will promote long-term economic growth.

By WTO experts estimates, liberalization of foreign trade may be implemented more rapidly through regional and bilateral trade agreements. The number of Regional Trade Agreements (RTAs) has been steadily increasing over the last 20 years as has the share of preferential trade in world trade. By the beginning of 2005 more than 250 RTAs had been notified to the WTO, of which 130 were reported after 1995. Of these: 170 are currently in force. The total

amount of agreements in force could come close to 300 towards the end of next year. The regional and bilateral trade agreements may give an impetus to the processes on multilateral trade agreements. The most recognized regional trade agreements may include: the European Union, the European Free Trade Association, the North American Free Trade Agreement, the Southern Common Market, the Association of Southeast Asian Nations, Asian Free Trade Area and the Common Market of Eastern and Southern Africa, the Economic Cooperation Organization. The WTO membership will help Azerbaijan take advantage of going beyond at least the regional frontiers. Besides, the regional trade agreements within the CIS-space are not effective. For this purpose, it is not worth comparing WTO membership with the regional trade agreements. Moreover, the countries prioritising regional trade agreements are WTO members. For example, the countries of European Union are WTO members and these states are represented in this organization in the form of sole institution. And the majority of WTO members have joined one or more regional trade agreements. So, Azerbaijan's WTO accession will not have a negative impact on its position and role in the regional trade agreements. In fact, it will help make it a more attractive trading partner for the European Union.

As far as standardization systems, the current Azerbaijan laws are not fully compliant with international and European rules in the area. Convergences as close as possible to relevant EU sectoral policy rules is the best way of ensuring that Azeri policies and system comply with the WTO Agreement on Technical Barriers to Trade, while providing for the most favourable conditions in order to foster trade between Azerbaijan and the EU. By following "European Standards" for products, Azerbaijan will be setting itself up for an access to the European Single Market, which requires standardization and no product discrimination. Policy convergences are to be made in the more general context of legislative adaptations

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currently taking place in other CIS countries in respect of technical barriers to trade and standardisation. This will also assist Azerbaijan with increasing trade with other regional countries. Since joining the WTO will require Azerbaijan to not discriminate against foreign imported products, Azerbaijan must begin taking steps to revamp the local production industry and prepare factories for the import of competitive goods.

For instance, Azerbaijan could aim at fostering, in a first stage, compliance of imported products (depending on the priority set forth by Azeri government; e.g. import of compatible agricultural and food products such as nuts, fruit and vegetable juices) with international standards. On the other hand, Azerbaijan may decide to initially encourage compliance of its domestic production with international standards. Such a policy convergence might for instance be carried out with a view to enhance exports of its domestic productions to geographical areas other than the CIS (Commonwealth of Independent States) countries.

Another reason might be to develop local production in connection with future import of cheap and compatible products following accession to the WTO. Emphasis on the national production might thus be targeted at the economic areas where harmonization is the most lagging behind. Another option could also be to select as a priority the industrial or service sectors that hold the largest share of the economy, should they present the best prospects for exports. Such an analysis in the early stage of the project will let mapping the relevant policy landscape in Azerbaijan, conducting the policy gap analysis and regulatory need assessment for sector policy convergences in TBT and custom fields, all necessary for developing recommendations, and conducting effective policy convergence and advocacy.

No matter which path Azerbaijan chooses to take in regards to standardization, it is very important that the government follows the lead of other standardization bodies, such as the European Committee for Standardization that brings “together all interested parties such as manufacturers, consumers, and regulators of a particular material, product, process or service” when setting regulations.<sup>100</sup> It is very important that a dialogue is created and that manufacturers are given the correct information, time, and resources needed to change standards needed for more effective regional trade.

All of these measures of Trade and Customs modernizing can be huge in making Azerbaijan more integrated with the EU. However, while the EU’s presence is large in Azerbaijan with its EaP, ENP and PCA, as well as multiple development projects and programs implemented with involvement of state and civil society actors. EU awareness however is very low in Azerbaijan; it is lower than the awareness in the neighboring countries, and lower than one would expect given the range and scale of EU involvement in Azerbaijan and the region. This ignorance applies now not only to the society in general, but also to civil society organizations and state officials/public servants, including even many of those involved with EU projects and programs. This is why the promotion of EaP as an urgent task in the context of raising the awareness of EU and its policies, programs and priorities in the national and regional levels.

For that reason, advocacy and communication have to be planned within this context towards effectively identifying and reaching the target groups and promoting the outputs of sector policy convergences discussed in this paper. Such an advocacy and communications strategy will have side effects on raising the

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<sup>100</sup> European Committee for Standardization. FAQs.  
<http://www.cen.eu/cen/Pages/FAQ.aspx> (accessed November 1, 2010)



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awareness and interest in other EU activities in Azerbaijan and the region, including ENP, PCA and also WTO related reforms.

In conclusion, in order for Azerbaijan to further integrate with European Union, the government must (1) draft customs and trade legislation that moves to meet EU standards while still being conscientious of local needs, (2) effectively include the input and cooperation of local entrepreneurs and producers (3) create an action plan that will allow for effective implementation of the new legislation and (4) ensure that these new implementations are monitored and prepared for any shocks from the new legislation. Azerbaijan has the ability to be a stronger EU trading partner. This integration will help facilitate the movement of services, information and people, in the region. It will also help strengthen the non-oil and gas sectors that need to be developed as oil revenues decrease over the next decade. The WTO accession is a good step towards being a more global and open trading partner. It can have great advantages in increasing investment, trade, transparency, and encourage large-scale technology transfers. It will also bring legislation against TBT, give Azerbaijan an incentive to conform to international standards, and open the country to increased foreign products that help to increase competition in domestic firms and aid in increasing transparency, while decreasing corruption. To meet these goals, Azerbaijan must show strong leadership and commitment to meet the many international requirements. However, the tough short-term disadvantages during this transitional period will lead to a more diverse, transparent, and stable, long-term economy for Azerbaijan.

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### **3. European Union-Armenia Activities Carried Out within the Framework of EaP between 2010 and 2012**

**Hovsep Khurshudyan**

**The National citizens Initiative, Armenia**

#### **3.1. Introduction**

Armenia and the EU first established contractual relations in 1996 through a Partnership and Cooperation Agreement which entered into force in 1999. On that basis, the EU-Armenia Action Plan (AP) was approved in November 2006 for a period of five years.

The Eastern Partnership (hereinafter EaP) was launched by 27 European Union (hereinafter EU) Member States and their Eastern European Partners (hereinafter the partner countries) at a summit in Prague on May 7 2009. The EaP—as stated in the adopted Joint Declaration—is aimed at closer cooperation between the EU and six former Soviet Union countries—Armenia, Georgia, Ukraine, Belarus, Moldova and Azerbaijan—and at implementation of new initiatives through the efforts of the EU and mentioned states. As it is mentioned in the Declaration, the main goal of the Eastern Partnership is to create the necessary conditions to accelerate political association and further economic integration between the European Union and interested partner countries<sup>101</sup>.

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<sup>101</sup> Joint Declaration of the Prague Eastern Partnership Summit, Prague, 7 May 2009 [http://ec.europa.eu/europeaid/where/neighbourhood/eastern\\_partnership/documents/prague\\_summit\\_declaration\\_en.pdf](http://ec.europa.eu/europeaid/where/neighbourhood/eastern_partnership/documents/prague_summit_declaration_en.pdf), p. 6.

The Eastern Partnership is being developed in bilateral and multilateral dimensions: The EaP agenda is mainly being developed within the bilateral dimension—EU—the partner country. The participants of the Prague Summit agreed that bilateral cooperation under the EaP umbrella should provide foundation for Association Agreements between the EU and the partner countries, with respect to the specific aims and goals of the partnership envisaged by each partner country. Association Agreements are aimed at regulatory approximation leading to convergence with EU laws and standards.

The multilateral cooperation is being implemented through four platforms: 1) democracy, good governance and stability; 2) economic integration and convergence with EU policies; 3) energy security; and 4) people to people contacts<sup>102</sup>.

According to the Joint Declaration of the Prague EaP Summit, high level official meetings are held within the EaP framework. In particular, meetings of Heads of States or Governments take place every two years, while Ministers of Foreign Affairs meet every year. The meetings of the four thematic platforms are held twice a year at the level of senior officials engaged in the reform activities carried out in relevant policy areas<sup>103</sup>. To note, the first ministerial meeting took place in Brussels on December 8 2009<sup>104</sup>.

In 2010 EU-Armenia meetings took place at the level of the Cooperation Council, Cooperation Committee, the Subcommittee on

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<sup>102</sup> Joint Declaration of the Prague Eastern Partnership Summit, Prague, 7 May 2009 [http://ec.europa.eu/europeaid/where/neighbourhood/eastern\\_partnership/documents/prague\\_summit\\_declaration\\_en.pdf](http://ec.europa.eu/europeaid/where/neighbourhood/eastern_partnership/documents/prague_summit_declaration_en.pdf), p. 9.

<sup>103</sup> Joint Declaration of the Prague Eastern Partnership Summit, Prague, 7 May 2009, p. 8-9.

<sup>104</sup> Eastern Partnership implementation well on track - 1 st Eastern Partnership Foreign Ministers meeting [http://europa.eu/rapid/press-release\\_IP-09-1891\\_en.htm](http://europa.eu/rapid/press-release_IP-09-1891_en.htm)

Trade, Economic and Related Legal Issues, and the newly established subcommittees on Justice, Freedom and Security and on Transport, Environment and Energy and Nuclear Safety. The second meeting of the EU-Armenia dialogue on human rights took place in December 2010. In November 2010, the EU and Armenia agreed a EUR 100 million financial assistance package to alleviate the effects of the global financial crisis on the country.

Within the Eastern Partnership, the negotiations for an EU-Armenia Association Agreement (AA) were launched in July 2010. They progressed at a good pace. This Agreement is conceived by both Parties as illustrating the most advanced and ambitious approach to the Eastern Partnership vision of association, including a Deep and Comprehensive Free Trade Area and a comprehensive programme of approximation to EU *acquis*. The negotiations on a Deep and Comprehensive Free Trade Area (DCFTA) started in the same framework at the 2012 after the necessary conditions have been met.

From September 29 to 30 2011, the second EaP Summit was held in Warsaw.

At the end of the summit, a Joint declaration was adopted by the heads of states or governments of EU member states and 5 Eastern Partnership countries<sup>105</sup>. The declaration gives a further impetus to the eastern Partnership with a focus on the following areas of cooperation:

- Deeper bilateral cooperation: political association, socio-economic integration and mobility;

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<sup>105</sup> Joint Declaration of the Eastern Partnership Summit Warsaw, 29-30 September 2011  
[http://ec.europa.eu/europeaid/where/neighbourhood/eastern\\_partnership/documents/warsaw\\_summit\\_declaration\\_en.pdf](http://ec.europa.eu/europeaid/where/neighbourhood/eastern_partnership/documents/warsaw_summit_declaration_en.pdf)

- Enhanced sectoral cooperation;
- Participation in EU programmes and agencies,
- Strengthening of multilateral cooperation

In accordance with the Eastern Partnership 2011 Warsaw summit decision, Eastern Partnership Roadmap was adopted at a ministerial meeting in July 2012.

The EaP Initiative— jointly undertaken by Sweden and Poland and supported by the EU high level officials—was launched in 2010. It is built up in the frame of the European Neighborhood Policy and is aimed to enlarge it for purposes to deepen integration of the partner countries—Armenia, Georgia, Ukraine, Belarus, Moldova and Azerbaijan—into the EU and to support in sustaining democratic institutions within these countries.

This new framework was welcomed by the mentioned six countries and was officially approved by their governments. However, the processes within this frame do not run that much smoothly and encounter many obstacles both available within the partner countries and posed by other regional actors. The aim of this article is to reveal the economic, social and political environment within which Armenia's—as one of the mentioned six countries—integration process with the EU is evolving.

### 3.2 Negotiations on EU-Armenia Association Agreement

On July 19 2010, the EU and Armenia started negotiations on an Association Agreement to succeed the Partnership and Cooperation Agreement (hereinafter PCA) that currently governs the EU relations with Armenia. On July 10 1999, the PCA with Armenia entered into force. It was concluded for an initial period of 10 years. As of 2009, the PCA has automatically being renewed year by year. Besides PCA, on January 1 2007, a joint EU-Armenia European Neighborhood Policy Action Plan came into force. Through this document Armenia assumed the commitments to cooperate with the EU and to achieve progress in such priority domains as reform of judiciary; strengthening of respect for human rights; improvement of investment climate; convergence of economic legislation and administrative practices; development of an energy strategy; contribution to a peaceful settlement of the Karabagh conflict; and enhancement of efforts in the field of regional cooperation. In April 2012, the List of Activities for 2012-2013 Ensuring the Implementation of the EU-Armenia European Neighborhood Policy Action Plan was approved.

The Association Agreement is set to reflect the guidelines of cooperation in the spheres of economic integration, free movement and energy issues. It aims to deepen political association and economic integration with the EU through regulatory approximation leading to convergence with the EU laws and standards, and via increased access to markets of the countries involved. The prospective Agreement will include provisions on the establishment of DCFTA. In June 2012, the EU announced the launch of DCFTA talks with Armenia within the framework of the currently negotiated EU-Armenia Association Agreement. From 2010 to 2012, a significant progress has been recorded over the negotiations on EU-Armenia Association Agreement. Particularly, over the course of the

mentioned period, 11 plenary sessions and 6 dozen videoconferences were held in the framework of the talks. So far, 28 Chapters on economic and sectoral cooperation out of 29 of future Agreement have been negotiated and temporarily closed. The talks over the creation of DCFTA—as part of the Association Agreement—are successfully evolving, the third stage of which took place in early December 2012. In view of the significant progress achieved in the negotiations, the Armenian side considers it realistic to conclude works on the Association Agreement—including DCFTA—by the EaP Summit in Vilnius in 2013<sup>106</sup>. On December 1 2012, the President of the Republic of Armenia (hereinafter RA) Serzh Sargsyan made a statement on this matter following the meeting with José Manuel Barroso, President of the European Commission<sup>107</sup>. On December 19 2012, the eleventh plenary session of negotiations between Armenia and the EU over Association Agreement took place in Brussels<sup>108</sup>. During the event the sides agreed to commence works on outlining the Association agenda early in 2013. The Association agenda will be a political document targeted at the implementation of the Association Agreement’s provisions. The Armenian side considers it feasible to implement the Association agenda as of early 2014. That is to say, the Association agenda may replace the PCA scheme.

From 2010 to 2012, the multilateral dimension of the EaP achieved considerable progress as well. Meetings within the framework of four multilateral thematic platforms, formal and informal ministerial conferences, and a number of working group gatherings were held.

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<sup>106</sup> [http://www.mfa.am/en/press-releases/item/2012/12/17/bru\\_visas/](http://www.mfa.am/en/press-releases/item/2012/12/17/bru_visas/)

<sup>107</sup> <http://www.president.am/en/press-release/item/2012/12/01/President-Serzh-Sargsyan-meeting-European-Commission-Jose-Manuel-Barroso/>

<sup>108</sup> [http://www.mfa.am/hy/press-releases/item/2012/12/19/eu\\_arm\\_assoc/](http://www.mfa.am/hy/press-releases/item/2012/12/19/eu_arm_assoc/)



### 3.3 EU-Armenia Visa Facilitation

Facilitation of the EU visa regime for Armenian citizens is an important part of EU-Armenia relations. In February 2012, negotiations on EU-Armenia visa facilitation and readmission agreements were launched. Following a number of effective negotiation cycles, on December 17, the texts of the finalized two agreements were signed by Edward Nalbandian, Minister of Foreign Affairs of Armenia, Erato Kozakou-Marcoullis, Minister for Foreign Affairs of the Republic of Cyprus in his capacity as President of the Council of the EU, and Cecilia Malmström, EU Commissioner for Home Affairs<sup>109</sup>. The Agreement would further simplify the procedures of acquiring Schengen visa for Armenian citizens which is an important step towards the liberalization of the visa regime<sup>110</sup>. The Agreement will now be sent to the European Parliament and National Assembly of the RA with a view to be ratified before it can enter into force. The parties will set up a Joint Committee, which will be tasked to monitor the implementation of this Agreement and to suggest amendments or additions to it. The Committee will meet at least once a year.

According to the Agreement between the EU and the RA on the Facilitation of the Issuance of Visas—signed on December 17 2012—the fee for processing visa applications will be reduced, and will amount to 35 EUR instead of previous 60 EUR. The Agreement also provides that the visa handling fee will not be collected for certain categories of applicants, including pensioners; children below the age of twelve; members of national and regional governments and of Constitutional and Supreme courts, in case they are not

<sup>109</sup> [http://www.mfa.am/en/press-releases/item/2012/12/17/bru\\_visas/](http://www.mfa.am/en/press-releases/item/2012/12/17/bru_visas/)

<sup>110</sup> Եվրոպական միության և Հայաստանի Հանրապետության միջև վիզաների տրամադրումը դյուրացնելու մասին Համաձայնագիր, [http://www.mfa.am/u\\_files/file/EU\\_AM\\_VFA\\_am.pdf](http://www.mfa.am/u_files/file/EU_AM_VFA_am.pdf)

exempted from the visa requirement by this Agreement; journalists and technical crew accompanying them in a professional capacity; and persons participating in scientific, academic, cultural or artistic activities, including university and other exchange programs<sup>111</sup>. The citizens of Armenia who are holders of valid diplomatic passports may enter, leave and transit through the territories of the EU member states without visas. The Agreement also provides for simplified supporting document requirements and wider issuance of multiple-entry visas for certain categories<sup>112</sup>. On 4 October 2012, the Government of the Republic of Armenia issued a decree on the exemption of visa requirements for the citizens of the EU and non-EU states applying EU Schengen acquis, starting from January 10, 2013.

A Joint Declaration on Mobility Partnership between Armenia, EU and its 10 Member States was signed by Minister of Foreign Affairs Edward Nalbandian, EU Commissioner of Home Affairs Cecilia Malmstrom and Ministers of Home Affairs of respective EU member states on October 27, 2011 in Luxemburg with the overall aim of promoting contacts between people and societies focusing on better managing legal and labour migration, enhancing cooperation on mobility, promoting exchange programmes and joint initiatives in the area of vocational and higher education.

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<sup>111</sup> Եվրոպական միության և Հայաստանի Հանրապետության միջև վիզաների տրամադրումը դյուրացնելու մասին համաձայնագիր, [http://www.mfa.am/u\\_files/file/EU\\_AM\\_VFA\\_am.pdf](http://www.mfa.am/u_files/file/EU_AM_VFA_am.pdf), էջ 9-10

<sup>112</sup> Agreement between the EU and the RA on the Facilitation of the Issuance of Visas <http://register.consilium.europa.eu/pdf/en/12/st16/st16913.en12.pdf> (pp.15-17)

### 3.4 Parliamentary Cooperation

The parliamentary cooperation with EU is implemented through the EU-Armenia Parliamentary Cooperation Committee. In May 2011, the Euronest Parliamentary Assembly was established that is a parliamentary forum to promote cooperation between the EU and the Eastern European Partners. The Euronest Parliamentary Assembly will be composed of equal number of Members of European Parliament and equal number of MPs from Eastern Partner countries. Armenia has welcomed the idea of EURONEST as a structure of parliamentary dialogue between the EU and its Eastern Partners. EURONEST comprises 60 members of the European Parliament and 10 members of parliament from each of the Eastern Partnership country. The Euronest Parliamentary Assembly includes the plenary, chaired by two Co-Presidents, the Bureau, four standing committees and two working groups. Euronest meets once a year, alternately in an Eastern European Partner country and on the premises of the European Parliament in one of its places of work (Brussels, Luxembourg or Strasbourg)<sup>113</sup>. Standing committees are

- Committee on Political Affairs, Human Rights and Democracy;
- Committee on Economic Integration, Legal Approximation and Convergence with EU Policies;
- Committee on Energy Security;
- Committee on Social Affairs, Education, Culture and Civil Society. Working groups are
- Working group on Belarus;
- Working group on the Rules of Procedure.

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<sup>113</sup> <http://www.euronest.europarl.europa.eu/euronest/cms/home>

### 3.5 EU Advisory Group

A new development in Armenia's relations with the European Union was the establishment of the EU Advisory Group in Armenia. The decision to send EU advisers to Armenia was made in November 2008 during the visit of President Serzh Sargsyan to the European institutions in Brussels. In accordance with the memorandum signed by Minister of Foreign Affairs Edward Nalbandyan and Commissioner Benita Ferrero-Waldner, the EU advisors provide consultancy assistance to institutions of public administration /government agencies, the office of Prime Minister, the National Assembly, ministries of economy, finances and transport, as well as the State Revenues Committee and the Ombudsman's office.

Originally planned for six months, the project has proved to be a success and has been prolonged to September 2010, with a prospect of further extension. The EU Advisory Group is to assist the Armenian authorities in the preparation of a process to negotiate, conclude and implement an Association Agreement with the European Union, including setting up a Deep and Comprehensive Free Trade Area (DCFTA). The EU advisors cooperate with government agencies in spheres of anticorruption strategy, governance reform, human rights, government debt management, raising the efficiency of customs administration, establishment of the Diplomatic Academy of the MFA of Armenia. Armenia was the first to initiate such a model and it is being introduced in other Eastern partner countries as well. The EU Advisory Group is a project funded by the European Union and implemented by the United Nations Development Programme (UNDP) in Armenia<sup>114</sup>. An Advisory Board, jointly chaired by the EU Delegation, the

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<sup>114</sup> [http://www.euadvisorygroup.eu/mission\\_vision](http://www.euadvisorygroup.eu/mission_vision)

Presidential Administration and the RA National Security Council staff acts as the supervisory body for the project.

The EU Advisory Group will ensure that the Armenian authorities have direct access to best practices and reform experiences from within the European Union. This will serve to strengthen the policy-making process, including consultation processes with civil society, policy formulations and its subsequent implementation. The Group will also assist to make effective use of the Comprehensive Institution Building (CIB) programme and other instruments of technical assistance such as Twinning, TAIEX and SIGMA.

The EU Advisory Group will assist in advancing the implementation of the European Neighbourhood Policy Action Plan (ENP AP), also through an increased dialogue between the national authorities and the European Commission's services. Core areas for policy advice are the following:

- Strengthening respect for human rights, fundamental freedoms and enhancing democratic structures;
- Supporting reforms in the field of Justice, Liberty and Security;
- Enhancing economic integration of Armenia into the European Union's internal market.

### **3.6 The Role of Civil Society in the Integration with the EaP**

EaP CSF Armenian National Platform

On December 2009, an Initiative Group (IG) involving the delegates of the first edition of the Civil Society Forum (CSF) was formed.

The IG was engaged with the launch of the CSF Armenian National Platform (ANP), setting out a working plan, as well as expanding the ANP founding documents (the regulations, the selection procedure, the concept, etc).

On September 2-3 in Tbilisi at the working meeting, “***Democracy Promotion through EaP***”, the representatives of Armenian, Georgian and Azerbaijani NGOs discussed the methodology of a possible monitoring on the implementation of the EaP priorities. The meeting was also attended by experts from Belarus and Poland.

The announcement to join the EaP CSF Armenian National Platform was disseminated in April, 2010. This was followed by the submission and classification of the applications. The founding meeting were took place on June 7, 2010 in Yerevan. The meeting was attended by 138 of the 145 NGOs, registered as ANP members.

The Founding Meeting endorsed the Regulations of the National Platform, formed four CSF ANP working groups and chose the ANP Coordination Council. 20 out of 50 candidates were elected as members of the CSF ANP Coordination Council. Voting was by majority rule.

The ANP Founding Meeting was attended and greeted by the Head of the European Commission Delegation to Armenia and many ambassadors of EU countries to Armenia, representatives from the European and International organizations, RA Ministries of Foreign Affairs and Economy, journalists and others.

It has been almost three years since the Eastern Partnership Civil Society Forum (EaP CSF) Armenian National Platform (ANP) was launched in Armenia. However, there are many problems within it, the main of which is the lack of focus on the European liberal and

democratic values. In contrast to that, the processes regarding the formation of non-value-based and non-standard-based groups—that are aimed to achieve predominance within EaP CSF ANP—prevail within the latter. The involvement of the representatives of organizations—that are targeted at introduction and protection of democratic values and principles of competitiveness in Armenia—in the mentioned processes seems particularly strange. It is obvious that one of the paths to solve the problem refers to the implementation of a global change of generations in the domain representing civil society organizations—and thus to the elimination of dominance of the Soviet way of thinking.

### ***Armenian Parties' Membership in the European People's Party***

In the 2012 Armenia has registered essential progress in European integration. In February 10, 2012 at EPP congress in Brussels, Republican Party of Armenia, Rule of Law and Heritage parties became members of the European People's Party. As a result of discussion three parties received status of observers which is the only available status for non-members of the EU. This status means full participation in the political life of the EPP and is of great significance for Armenia. It will register new good opportunities in the political life of the country and in the Armenia-EU integration process. After important actors in Armenia's political arena joined the European family, it should be considered a most important factor both in Armenia's domestic political life and in foreign policy. The fact that both pro-government and opposition forces may join the EPP is most interesting in the context of political culture. The EPP's great potential and experience will introduce essential elements of political culture and would be good impetus to Europeanization of Armenian domestic political culture.

It is important to mention that only four political parties from around the South Caucasus region were accepted into the European People's Party as observer-members. The fourth party—Georgian United National Movement—was joined the EPP earlier - in September 2007.

It is also noticeable that the European People's Party (hereinafter EPP) rejected the application of “Prosperous Armenia” Party—as the fourth applicant from Armenia—on the EPP membership. According to experts, it is due to not only the Party as being formed to serve the interests of one oligarch and his businesses, but also because “Prosperous Armenia” and Russia's “Yedinaya Rossia” are sister parties. In this regard, the Republican Party of Armenia acted with circumspection, and avoided such affiliation.

### ***High Level Official Visits between 2010 and 2012***

The cooperation with the EU is one of the key priorities of Armenia's foreign policy. There is an enhanced political dialogue between Armenia and the EU which is marked by regular high level official visits.

On March 5 2012, Minister of Foreign Affairs of the RA Edward Nalbandian participated in an extended ministerial meeting of the Visegrad Group in Prague attended by the representatives of the partner countries as well as Denmark, Lithuania, Latvia and Estonia. The meeting was also attended by Catherine Ashton, EU High Representative for Foreign Affairs and Security Policy, and Štefan Füle, Commissioner for Enlargement and European Neighborhood Policy<sup>115</sup>.

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<sup>115</sup> <http://www.mfa.am/en/country-by-country/eu/>



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On June 5 2012, the first informal ministerial meeting of the EaP took place in Chisinau. The Armenian delegation was headed by Zohrab Mnatsakanian, Deputy Minister of Foreign Affairs of the RA.

On July 23 2012, Edward Nalbandian, Minister of Foreign Affairs of the RA, participated in the ministerial meeting of the EU and the partner countries in Brussels, which was also attended by Catherine Ashton, EU High Representative for Foreign Affairs and Security Policy, and Štefan Füle, Commissioner for Enlargement and European Neighborhood Policy.

The President of the RA Serzh Sargsyan visited EU institutions in Brussels from November 5 to 6 2008; from November 25 to 27 2010; from March 6 to 7, 2012; and on June 27 2012. President Sargsyan participated in the EaP summits in Prague, on May 7 2009, and in Warsaw, on September 30 2011.

In Dec. 7, 2011, in Marseilles, France, President Serzh Sagsyan participated in the first plenary session of the 20th Congress of the European People's Party (EPP) as a special guest<sup>116</sup>. Speaking at the Congress, EPP President Wilfried Martens invited the Armenian leader to participate in the Dec. 8 summit of the Heads of European state and government. “As of today you can consider yourself as part of the party’s large family,” Mr. Martens said. In October 18, 2012 Serzh Sagsyan participated in the European People’s Party (EPP) 21st Congress, which took place in the Romanian capital Bucharest.

The RA National Assembly President Hovik Abrahamyan visited the European Parliament in Brussels from July 12 to 13 2010, and from May 2 to 3 2011. The RA Prime Minister Tigran Sargsyan visited the

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<sup>116</sup> <http://en.hayernaysor.am/1323330547>

EU institutions on November 12 2010; from March 16 to 17, on September 19, and from November 7 to 8 2011; and from June 3 to 4 2012.

Edward Nalbandian, Minister of Foreign Affairs of Armenia, co-chairs the annual sessions of the EU-Armenia Cooperation Council in Brussels. Minister Nalbandian regularly participates in the EaP ministerial meetings.

In 2011 and 2012, Arthur Baghdasaryan, leader of EPP member “Rule of Law” Party and Secretary of the RA National Security Council, and Raffi Hovannisian, leader of EPP member opposition “Heritage” Party, participated in EPP Congresses and working meetings within the framework of this pan-European Party in different European cities.

From November 30 to December 1 2012, President of the European Commission José Manuel Barroso visited Yerevan. Over the course of his visit, President Barroso participated in the EaP Leaders' Summit of the EPP, had separate meetings with Armenia's President, Speaker of the National Assembly, and Prime-Minister, and addressed the civil society. EPP President Wilfried Martens, who arrived in Yerevan along with Barroso, met with the leaders of the parties that were conferred upon observer-member status within the EPP. In particular, he had meetings with Serzh Sargsyan, President of the RA and leader of the Republican Party of Armenia, Arthur Baghdasaryan, leader of “Rule of Law” Party and Secretary of the RA National Security Council, and Raffi K. Hovannisian, leader of opposition “Heritage” Party. The video addresses by Martens were published during the Congresses of the Republican Party of Armenia and “Heritage” Party held in December 2012.

On September 27 2012, April 29 2011, and April 6 2010 EU Commissioner for Enlargement and European Neighborhood Policy Štefan Füle visited Armenia.

From July 3 to 4 2012, Herman Van Rompuy, President of the European Council, visited Armenia. From November 16 to 17 2011, EU High Representative for Foreign Affairs and Security Policy Catherine Ashton visited Yerevan. From June 9 to 10 2011, Miroslav Lajcak, Managing Director for Europe and Central Asia of the EU European External Action Service, visited Armenia. From May 17 to 18 2011, President of the European Parliament Jerzy Buzek visited Yerevan.

On January 19 2009, and on February 5 2008, Benita Ferrero-Waldner, EU Commissioner for External Relations and European Neighborhood Policy, visited Armenia.

On March 2 2010, Miguel Angel Moratinos, Minister of Foreign Affairs and Cooperation of Spain, visited Armenia in the framework of Spain's EU Presidency.

On December 14 2012, Foreign Ministers of Poland, Sweden and Bulgaria Radosław Sikorski, Carl Bildt and Nickolay Mladenov paid a visit to Yerevan<sup>117</sup>, and had meetings both with the high-level governmental officials and leaders of parliamentary opposition of Armenia.

The EU Special Representative for the South Caucasus visits Yerevan on a regular basis.

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<sup>117</sup> <http://www.mfa.am/hy/videos/item/102/>

### 3.7 Identified Problems

#### *Economic Framework*

The main challenge concerning economic cooperation that Armenia and the EU face within the EaP framework can be formulated as follows: Armenia's institutions and processes considerably do not meet the European standards, and substantial financial investments are required to eliminate or significantly reduce these discrepancies through the application of the European standards both in the fields of infrastructure and production. However, the economy of Armenia is not able to attract much investments, especially if to take into account the trends pertinent to Armenia's economy over the course of recent years—recorded growth of poverty, reduction of foreign direct investment (hereinafter FDI), and other relevant trends.

According to the Global Competitiveness Report 2012-2013—released by the World Economic Forum—Armenia's institutes of market economy and justice system in general do not comply with the EU standards. Though Armenia is ranked 82nd among 144 countries—leaving behind EU member Greece (96th)<sup>118</sup>—its competitiveness index (4.02) is significantly lower than that of the EU initial eleven states out of fifteen—excluding Greece, Italy, Portugal, and Spain, whose index totals at nearly 5.31<sup>119</sup>. The Global Competitiveness Report's competitiveness ranking is based on the Global Competitiveness Index (hereinafter GCI). The GCI comprises 12 categories—the pillars of competitiveness—which together provide a comprehensive picture of a country's competitiveness landscape. The pillars include institutions, infrastructure, macroeconomic environment, market size, business sophistication

<sup>118</sup> The Global Competitiveness Report 2012–2013, [http://www3.weforum.org/docs/WEF\\_GlobalCompetitivenessReport\\_2012-13.pdf](http://www3.weforum.org/docs/WEF_GlobalCompetitivenessReport_2012-13.pdf), p 13.

<sup>119</sup> The Global Competitiveness Report 2012–2013, p 25.

and innovation, and others. As Table 1 suggests, Armenia's best ranking refers to the pillar of labor market efficiency.

Table 1. Armenia: Changes in Competitiveness Pillar Ranking <sup>120</sup>

Pillars	2011-2012 Rank among 142 countries	2012-2013 Rank among 144 countries	Change
Institutions	83	71	+12
Infrastructure	77	80	-3
Macroeconomic stability	114	83	+31
Health and primary education	94	80	+14
Higher education and training	76	70	+6
Goods market efficiency	108	72	+36
Labor market efficiency	34	30	+4
Financial market development	95	78	+17
Technological readiness	88	92	-4
Market size	115	115	0
Business sophistication	107	92	+15
Innovation	112	105	+7

In general, the competitiveness performance of Armenia steadily decreased since 2005, but during recent two years the pillar-based GCI reversed to the positive. To note, Armenia was ranked through GCI for the first time in 1995. According to Table 2, Armenia's competitive advantages are related to business impact of HIV/AIDS

<sup>120</sup> <http://www.ev.am/media/documents/GCR/2012-13/GCRPressRelease2012-1305SEP2012final.pdf>, p 2.

and malaria incidents, business costs of terrorism and crime, and labor market efficiency.

**Table 2. Some Competitive Advantages and Disadvantages of Armenia<sup>121</sup>**

<b>Notable Advantages</b>	<b>Rank</b>	<b>Notable Disadvantages</b>	<b>Rank</b>
Business impact of malaria	1	Intensity of local competition	130
Malaria incidence	1	Quality of management schools	127
Number of procedures to start a business	8	Burden of customs procedures	127
Business costs of terrorism	8	Index of international markets	123
Hiring and firing practices	10	University-industry collaboration in R&D	122
HIV prevalence	12	Effectiveness of anti-monopoly policy	116
Business costs of crime and violence	13	Financing through local equity market	115
Transparency of government policymaking	16	Quality of scientific research institutions	111
Flexibility of wage determination	21	Company spending on R&D	111

<sup>121</sup>

<http://www.ev.am/media/documents/GCR/2012-13/GCRPressRelease2012-1305SEP2012final.pdf>, p 3.

Government services for improved business performance	31	Judicial independence	110
Pay and productivity	31	Efficacy of corporate boards	110

Meanwhile, the disadvantages exceed the number of advantages, and are related to lack of independence in judicial system, weakness of local competition, inefficiency of anti-monopolistic and customs policies, and several others. In these directions Armenia should carry out reforms within the framework of the EaP.

Harmonization of Armenian institutions (laws, procedures) with the EU standards, and implementation of the DCFTA Agreement, of course, will help to ensure high economic growth that will also be based on foreign trade and increased FDI. On the other hand, the macro-economic situation and high level poverty recorded in Armenia during recent years can impede the effectiveness of the reform process. In Armenia Gross National Income (hereinafter GNI) per capita was reported at 3360 USD in 2011<sup>122</sup>, which is 10 time less than GNI per capita in the EU member states—34.000 USD<sup>123</sup>. According to the World Bank classification, Armenia is a

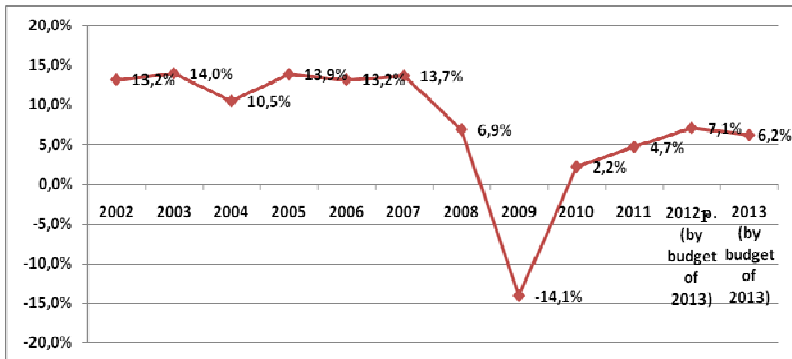
<sup>122</sup> <http://data.worldbank.org/indicator/NY.GNP.PCAP.CD>

<sup>123</sup> [http://databank.worldbank.org/ddp/html-jsp/QuickViewReport.jsp?RowAxis=WDI\\_Ctry~&ColAxis=WDI\\_Time~&PageAxis=WDI\\_Series~&PageAxisCaption=Series~&RowAxisCaption=Country~&ColAxisCaption=Time~&NEW\\_REPORT\\_SCALE=1&NEW\\_REPORT\\_PRECISION=0&newReport=yes&ROW\\_COUNT=1&COLUMN\\_COUNT=1&PAGE\\_COUNT=1&COMMA\\_SEP=true](http://databank.worldbank.org/ddp/html-jsp/QuickViewReport.jsp?RowAxis=WDI_Ctry~&ColAxis=WDI_Time~&PageAxis=WDI_Series~&PageAxisCaption=Series~&RowAxisCaption=Country~&ColAxisCaption=Time~&NEW_REPORT_SCALE=1&NEW_REPORT_PRECISION=0&newReport=yes&ROW_COUNT=1&COLUMN_COUNT=1&PAGE_COUNT=1&COMMA_SEP=true)

lower middle income country<sup>124</sup>. It is noticeable that Armenia's economy recorded significant growth from 2002 to 2007 (Figure 1).

However, in 2009 Armenia faced a 14.1 percent deep recession of the economy that was one of the sharpest ones in the world. The depression was followed by a slow recovery of the economy in 2010-2012. In 2012, however, the Gross Domestic Product (hereinafter GDP) has not yet reached the pre-crisis 2008. Figure 2 shows the percentage of 2009-2011 real GDP and GDP projected for 2012/2013 compared to 2008 GDP<sup>125</sup>.

**Figure 1. GDP Real Growth Rate 2002-2013<sup>126</sup>**



<sup>124</sup> <http://data.worldbank.org/about/country-classifications>

<sup>125</sup> In figure 2 the calculations of indicators for 2009-2013 are as follows: for 2009  $100\% - 14.1\% = 85.9\%$ ; for 2010  $85.9\% * 1.022 = 87.8\%$ ; for 2011  $87.7\% * 1.047 = 91.9\%$ ; for 2012  $91.9\% * 1.071 = 98.4\%$ ; and for 2013  $98.4\% * 1.062 = 104.5\%$ .

<sup>126</sup> Statistical Yearbook of Armenia-2006: International Comparisons

<http://armstat.am/file/doc/492.pdf> (p.526)

Statistical Yearbook of Armenia-2008: International Comparisons

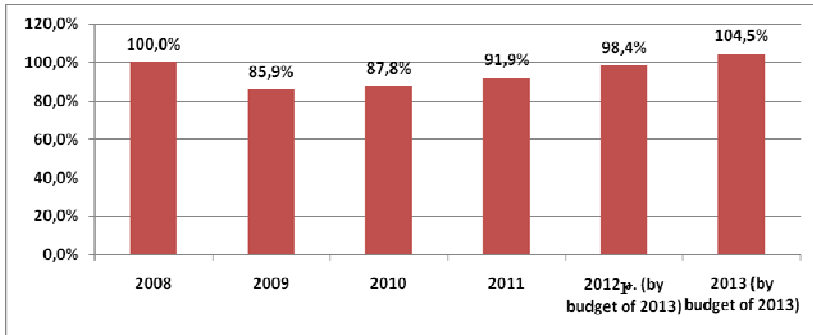
<http://www.armstat.am/file/doc/99471528.pdf> (p.553)

Statistical Yearbook of Armenia-2012: International Comparisons

<http://www.armstat.am/file/doc/99471528.pdf> (p.551)

ՀՀ Կառավարության 2013թ. բյուջետային ուղերձ, էջ 50



**Figure 2. 2009-2013 GDP Compared to 2008 GDP**

In 2009, the recession resulted in an increased poverty that started to grow for the first time since 1998. While active phase of the crisis occurred in 2009, Armenia continued to suffer from enhanced poverty in 2010 as well. Compared to 2009, however, Armenian economy observed modest recovery in 2010 with growth totaling at 2.2 percent, while in 2011 the progress remained on the same level as it was in 2010—4.7%. Thus, in 2011—as compared to 2008—the level of poverty with its depth and severity (very poor and extremely poor share of the total poor structure) significantly increased. According to the National Statistical Service of Armenia, Armenia's poor population in 2008 was 27.6%; in 2009 34.1%; in 2010 35.8 %; and in 2011 35%<sup>127</sup>. In 2008 very poor in Armenia amounted to 12.6% of total population, and in 2011 approximately to 20%. In 2008 the share of extremely poor amounted to 1.6% of total population, while in 2011 their number increased up to 3.7%.

From 2009 to 2012, Armenia's government exerted efforts aimed to amend the legislation that will ensure improved business

<sup>127</sup> Armenia: Poverty Profile and Labor Market Development in 2008-2011 [http://www.armstat.am/file/article/poverty\\_2012a\\_2.pdf](http://www.armstat.am/file/article/poverty_2012a_2.pdf), (p. 36-39)

environment in Armenia and the country's competitiveness. Nowadays, in Armenia a new business can be registered in 15 minutes via the Internet<sup>128</sup>. The amount of profit tax advance payment and minimum profit tax was reduced by 8, property tax and land tax payments were cut down by 2, and the reports on the compulsory social security payments by 8. The barrier of inspection visits to companies with turnover less than 70 million AMD was extended. The introduction of electronic tax filing system is also of paramount importance since this tool decreases one to one communication of tax payers with tax officials. As of 2013, the system will be used by all tax payers. The mentioned and other shifts were reflected in the Doing Business led by the World Bank, and indexes of competitiveness and economic liberalization. To note, Armenia advanced from 41<sup>st</sup> position among 181 countries in Doing Business-2008<sup>129</sup> to 32<sup>nd</sup> position among 185 countries in Doing Business-2013<sup>130</sup>.

The changes concerning business environment, however, did not increase FDI. Moreover, Armenia faced sharp decline in FDI flows. If the decline recoded from 2009 to 2010 could be justified on the grounds of the world economic crisis, the unprecedented low level of FDI particularly in 2012 will be problematic to explain on the same basis.

According to Doing Business-2013, Armenia made its biggest jump in the category of Protecting Investors<sup>131</sup>. However, in 2012 FDI

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<sup>128</sup> RA Prime Minister Tigran Sargsyan's statement at National Assembly on 2011 State budget performance results <http://www.gov.am/am/speeches/1/item/3237/>

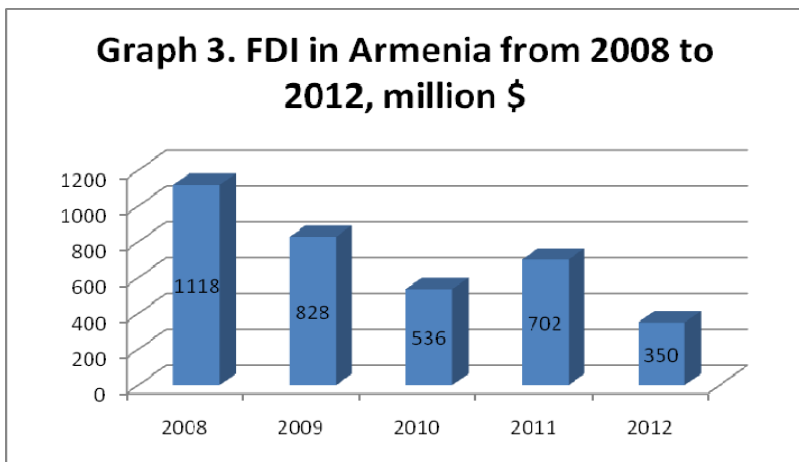
<sup>129</sup> Doing business 2009' <http://www.doingbusiness.org/~media/fpdkm/doing%20-business/documents/annual-reports/english/db09-fullreport.pdf>, page 6.

<sup>130</sup> <http://www.doingbusiness.org/rankings>

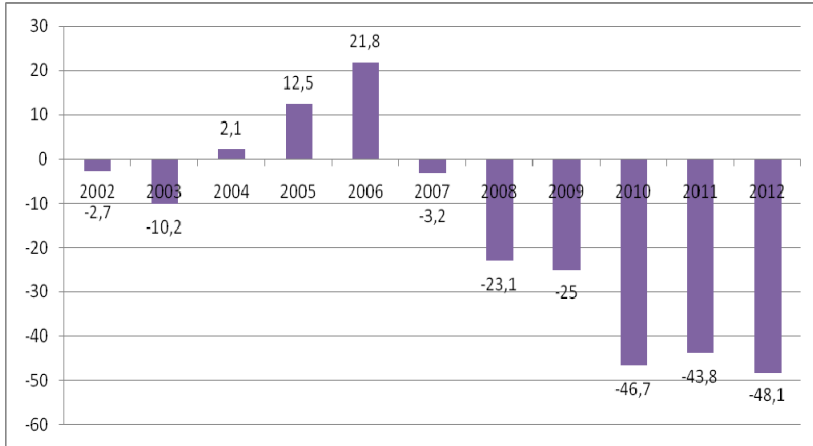
<sup>131</sup> <http://www.doingbusiness.org/data/exploreeconomies/armenia/>

decreased 2 times compared to 2011 and 2007, more than 3 times compared to 2008, and 2.5 times compared to 2009 crisis (Figure 4).

From 2008 to 2012, migration from Armenia increased significantly. From 2002 to 2007—during years of the economy's two digits rise—the migration balance was positive and amounted to 20.000 people, while from 2008 to 2012, the number of migrants from Armenia totals at nearly 190.000 (Figure 3).



**Figure 4. Net Migration Rate in Armenia from 2002 to 2012 (+, -) (1000 persons)<sup>132</sup>**



This number exceeds that of the population of Armenia's second largest city Gyumri. To note, according to 2011 population census, there are 2.870.000 people who actually live in Armenia<sup>133</sup>. Such high rates of immigration are not only due to lack of jobs and low wages, but also to general public hopelessness, people's decreasing faith in the prospects of their own country, lack of accountable public administration bodies, and growing volumes of monopolies.

### ***Political Framework***

The political factors affecting Armenia's European integration are of no less importance. It seems that except Iran, Armenia's other immediate and recognized neighbors—Georgia, Azerbaijan and Turkey—are seeking maximum integration with the EU. Moreover,

<sup>132</sup> [http://www.smsmta.am/?menu\\_id=18](http://www.smsmta.am/?menu_id=18), [http://www.smsmta.am/?menu\\_id=17](http://www.smsmta.am/?menu_id=17)

<sup>133</sup> [http://www.armstat.am/file/article/sv\\_09\\_12a\\_520.pdf](http://www.armstat.am/file/article/sv_09_12a_520.pdf), p. 121

EU membership is one of the foreign policy priorities set by two of them—Turkey and Georgia. However, at one hand, being involved in one of the frozen and yet unresolved Karabagh conflict, and subject to illegal blockade imposed by Turkey on the other hand, Armenia actually found itself in a much more intricate political tangle than it may seem at first glance. The situation is becoming more complicated in view of the agreement signed in 1995 on the deployment of Russian military base in Armenia—that was extended in 2010<sup>134</sup>—against the backdrop of Turkish military threat and Armenia's need for protection, and increased the dependence of Armenia on the northern "strategic ally," with which Armenia does not even have common borders. In the process of the South Caucasus States' European integration considering its decreasing influence, the Kremlin initiated the formation of a new organization—Eurasian Union<sup>135</sup>—the first step of this which will be the establishment of the Customs Union with involvement of the Commonwealth of Independent States. In this regard, European senior officials have repeatedly and publicly warned EaP countries that the joining of the latter to the Kremlin-backed Eurasian Union is incompatible with the prospect of Association Agreement and accession of the these countries to DCFTA. They also stressed that EaP countries do need to make an unambiguous choice between the two. To note, in December 2012 the spokesperson for EU High Representative for Foreign Affairs and Security Policy Maja Kocijancic stated: "If Armenia were to join any customs union, this would not be compatible with concluding a bilateral Deep and Comprehensive Free Trade Agreement between the European Union and Armenia," she said, "because a customs union has a common external-trade

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<sup>134</sup> [http://www.armenianow.com/news/28963/russian\\_military\\_base\\_gyumri](http://www.armenianow.com/news/28963/russian_military_base_gyumri)

<sup>135</sup> <http://izvestia.ru/news/502761>

policy and an individual member country no longer has sovereign control over its external-trade policies." <sup>136</sup>.

Armenia is obviously interested in joining DCFTA, and being fully aware of that Russia—which itself seeks increased level of integration with the EU—either economically or technologically cannot be prospective from the viewpoint of Armenia’s development. Moreover, the sale of two S-300 missile systems by Russia to Azerbaijan<sup>137</sup>—which together with Armenia are locked in an unresolved conflict—demonstrated that Russia is Armenia’s unreliable ally, and is ready to violate its obligations taken in the framework of Collective Security Treaty Organization by betraying its ally. In case of Armenia’s accession to Eurasian Union—according to our sources close to Kremlin—Russia will grant 1,5 billion USD credit to Armenia, and that is discussed between official Moscow and Yerevan. However, it cannot play a significant role in persuading the Armenian authorities. They give evasive answers to the Kremlin’s proposal, and justify them on the grounds of lack of common borders. In response to that, the Eurasian Economic Commission Board Chairman Victor Khristenko compared Armenia to the Russian exclave of Kaliningrad, arguing that having no border with Russia or other members of the Customs Union would not be a problem for integration. This statement drew strong reaction from some political circles in Armenia, including pro-Russian “Prosperous Armenia” Party that is the second largest one represented in the National Assembly of Armenia. In particular, the representative of the Party assessed this statement as “far from diplomacy.”<sup>138</sup>.

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<sup>136</sup> <http://168.am/2012/12/22/156690.html>

<sup>137</sup> [http://en.rian.ru/military\\_news/20100729/159989155.html](http://en.rian.ru/military_news/20100729/159989155.html),  
<http://www.news.az/articles/politics/38777>

<sup>138</sup> <http://pda.regnum.ru/news/1607126.html>

In its turn, in 2011 the EU states its intention to convene a conference of donors that will be aimed at supporting the reforms in Armenia. In late December, in an exclusive interview with Radio Free Europe/Radio Liberty's Armenian Service, Peter Stano, a spokesperson for EU Enlargement Commissioner, stated that the EU is ready to call an international meeting after Armenia's parliamentary elections 2012, aiming to support Armenia in its reforms, and meanwhile stressed that the elections must be free and fair.<sup>139</sup>

"To sum up 2011, I can say that there is a mutual commitment to further strengthen the ties between the EU and Armenia. Armenia is certainly a very important partner for the European family in the 'Eastern Partnership,' and we are glad that the country is active and provides all new initiatives," maintained Stano.

Earlier, the office of EU High Representative for Foreign Affairs and Security Policy stressed the need for holding free and transparent elections in Armenia in 2012 underlining that they would closely be monitoring the process.

In an exclusive interview with Radio Free Europe/Radio Liberty's Armenian Service, Maja Kocijancic, spokesperson for EU High Representative for Foreign Affairs and Security Policy Catherine Ashton, stated: "We are very happy to hear from the authorities of Armenia that the elections scheduled for 2012 will be free and fair, and will be the best in the history of Armenia." "The EU has a clear position on this issue—we want the elections to be held in accordance with international standards, and we will closely monitor them, also because this issue is one of the most important elements

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<sup>139</sup> <http://www.azatutyun.am/content/article/24437529.html>

of democratic development that is the priority for the European Union," concluded Kocijancic<sup>140</sup>.

But the European Union (EU) is postponing a conference on financial aid to Armenia, alluding to the fact that the May 6 parliamentary elections in Armenia did not quite meet the EU's expectations. So Brussels is now waiting for the 2013 presidential election in Armenia, Peter Stano, Spokesperson for Štefan Füle, Commissioner for Enlargement and European Neighborhood Policy, told [azatutyun.am](http://azatutyun.am).<sup>141</sup>

The May parliamentary elections in Armenia were largely positive. However, some issues require settling. Armenia's holding free and fair presidential election in 2013 will make it clear when the conference will be held and what else the EU will be able to do assist Armenia in implementing all the programs on the agenda, Stano added.

At a similar conference in Paris, in 2001, international institutions allocated a total of US \$620m to Armenia for poverty reduction.

The approaches of Armenia's political forces suggest that there is a wide consensus among the country's political elite towards the need for deepening the European integration, and to conclude the Agreement on DCFTA. It gives hope that there is a deep understanding of the importance of Armenia's European integration, and there is an acknowledgment in Armenia that this process is irreversible.

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<sup>140</sup> <http://www.azatutyun.am/content/article/24437529.html>

<sup>141</sup> <http://www.tert.am/en/news/2012/06/28/brussels/>



### 3.8. Conclusions

According to the High Representative's of the European Union for Foreign Affairs and Security Policy JOINT STAFF WORKING PAPER "Implementation of the European Neighbourhood Policy in 2010: Country report: Armenia", overall, Armenia made some progress in the area of political dialogue and reform. Positive steps were taken to overcome the political crisis, with the gradual release of a number of persons detained for charges related to the March 2008 events. There was good progress on decriminalisation of defamation. Some progress was made on enhancing transparency in the court system but no progress was made on enhancing the independence of the Judiciary Progress on enhancing media pluralism was limited. Some progress was made on enhancing the freedom of expression. Armenia also made good progress in improving the National Preventive Mechanism under the Optional Protocol to the UN Convention against Torture, and in the area of enhancing document security by making preparations for the introduction of biometric passports.

Armenia made some progress in the area of customs and border management, while overall more progress would have been desirable in trade-related areas. The situation of the Medzamor Nuclear Power Plant remains a topic of major concern and its early decommissioning is a key priority for both sides.

Armenia maintained prudent macroeconomic policies and introduced several structural measures to mitigate the impact of the economic crisis. Armenia also made good progress in the area of vocational education and training.

No developments took place after Armenia's suspension of the ratification process of the two protocols on the establishment and

development of bilateral relations with Turkey in April. The EU continues to support the normalisation of relations between Armenia and Turkey without preconditions. Negotiations on a peaceful solution of the Nagorno-Karabakh conflict continued at the highest level with some progress notably regarding exchange of prisoners of war, as a necessary confidence-building step to further advancing the process. An increased number of incidents of exchanges of fire and casualties on the line of contact continued to be reported and are cause for serious concern.

The main challenges facing the Armenia-EU association and its deepening still also remain the issues in Armenia concerning democracy, human rights, and protection of diverse groups, including minorities. However, the standpoints adopted by the political forces advise that there is a consensus on the deepening of the European integration and on conclusion of DCFTA Agreement among the political elite of Armenia.

### III. VISEGRAD COUNTRIES AND EU INTEGRATION

#### **1. Social reforms in Slovakia: experience and contexts**

**Grigorij Mesežnikov**

**President of the Institute for Public Affairs (IVO),  
Bratislava, Slovakia**

#### **1.1 SYSTEMIC AND SECTORIAL REFORMS**

Socio-economic reforms constituted an integral part of the process of social transformation in Slovakia after the fall of the communist regime in 1989. There were major (systemic) economic and social reforms, which took place simultaneously with the reform of the political system, the establishment of an independent state after the breakup of the Czechoslovak federation in 1993 and building of its institutional basis, integration into Euro-Atlantic political, economic and defense and security structures. In political area these changes included:

- elimination of the legacy inherited from the communist regime (process of political and judicial rehabilitations, property restitutions, screening procedures/lustrations),
- formation of political system based on pluralism and democracy, efficient mechanism of checks and balances, rule of law, free and fair elections,
- creation of a functional system of protection of human and minority rights,

- formation of a modern civil society,
- development of self-government and local democracy.

Profound systemic reforms in different areas were carried out over a relatively short period of time, often in an interconnected manner. Their constituent elements were partial (sectorial) reforms, affected by variety of internal and external factors. These reforms included reform of ownership relations, reform of entrepreneurial environment, tax reform, reform of system of public finances, constitutional reform, public administration reform, pension system reform, welfare system and labor market reform, health care system reform, education system reform, judicial reform, and military reform.

The efforts of reform did not lead to identically positive results in all of these areas. In some areas considerable progress was made, while in others results were more modest compared to initial expectations and reform processes have not been fully completed.

## **1.2. Factors of reforms' success**

The effectiveness of reform measures depended mainly on the impact of three determining factors:

- 1) the ability, readiness and commitment of the dominant political forces to pursue reforms;
- 2) Slovakia's participation in European integration process, the attempts to join the European Union (EU) and the actual membership of the EU;
- 3) Activities of pro-reform segments of civil society.

### *Political elites*

Reforms, especially in socio-economic area, have been enforced in Slovakia in a more intensive manner when the country was governed by coalitions of the center-right political formations (parties of liberal and conservative orientation). In 1990, 1998, 2002 and 2010, these parties gained a support in parliamentary elections, which allowed them to create a coalition government with majority of seats in the parliament. In 1992, 1994, 2006 and 2012, parties of other orientations (national-populist, nationalist, leftist) came to power. After forming their coalition governments, they usually re-evaluated the results of some of the reform measures taken by the center-right parties and introduced policies that corresponded better with their own programs. These “revisionist” parties preserved mainly the results of sectorial reforms carried out by their predecessors, which did not endanger their efforts to maintain political power. At the same time, the mentioned parties that could be described as parties with weaker potential for conducting the reforms accepted the existing framework of fundamental systemic changes that was formed in the early stages of transformation process (introduction of parliamentary democracy and market economy, orientation to achieve membership in the EU and NATO) and did not question them. It can be concluded that with few exceptions, there has been a consensus about systemic (major) reforms among the main political actors in Slovakia. Differences and disputes between the parties in their approaches to partial (sectorial) reforms did not undermine this basic consensus.

### *Factor of European integration*

Process of implementation of socio-economic reforms in Slovakia was intensified and deepened after 1999, when the country opened the negotiations on accession to the EU. Participation in the process of

European integration served as a catalyst for the process of internal reforms. Without integration pressure, Slovakia would not be able to implement a large number of reform steps in a very short period of time. Before, during the 1994–1998 period, Slovakia was ruled by semi-authoritarian national-populist parties which impeded country's participation in the European integration process. In this period, Slovakia was the only associated EU member state that did not fulfill political criteria for accession to the union due to internal problems (authoritarian methods of governance, power-institutional confrontation, violation of rule of law, worsening situation in the area of human and minority rights etc.). Only the retaking of power by pro-democratic forces (broad coalition formed by the center-right and center-left parties and party representing interests of Hungarian minority) after the 1998 elections has led to positive changes and restoration of country's integration chances. In March 1999, Slovakia launched the EU accession process and completed the process at the end of 2002.

### *Civil society*

An important role in the overall process of social transformation and promotion of reforms has been played by civil society actors: NGOs, civic initiatives, think tanks, professional associations, business unions, trade unions, independent media, and public intellectuals. They participated in the elaboration of reform strategies in some areas, advocated the specific reform measures, sought to influence the approach of government officials, and tried to shape the public opinion. Civil society actors belonged to the most pro-reform and pro-European oriented forces in the country.

The next section will take a closer look at the basic principles of society's transformation in Slovakia in economic and social areas.

### 1.3. Economic transformation

The socialist system of economy that existed in Czechoslovakia between 1949 and 1989 was based on the dominance of state ownership, command governance and management, over-centralization, regulation, and planning. Collateral effect of the system was the shortage of goods and services for ordinary people. In addition, this system did not create a motivating environment for technological innovations, particularly in those areas of production that critically affected the quality of citizens' life. The structure of industrial production in Slovakia was largely determined by external factors such as decisions of Council for Mutual Economic Assistance and the Warsaw pact. In the 1950s and 1960s, big defense-industry factories were built in Slovakia. They produced tanks, armored vehicles and other military equipment that was exported to the Soviet Union, Warsaw Pact states and other states, which cooperated with the Soviet bloc (for instance, in the Middle East). At the end of the 1980s, Czechoslovakia's economy showed signs of apparent stagnation and increasingly lagged behind the economy of the developed Western countries.

#### *Basic principles of economic transformation as a fundament of social reforms*

The basic principles of economic transformation in the former Czechoslovakia, of which Slovakia was a constituent part until 1993, were formulated in 1990. The reform strategy introduced the process of marketization of the economy. The sequences of the process included liberalization of conducting business, prices and foreign trade, the introduction of real interest rates and the exchange rate of the Czechoslovak currency, achievement and maintenance of fiscal and monetary balance, privatization and creation of new ownership relations, and restructuring of industry and economy as a whole. Neo-

classical and monetarist school of economy served as the theoretical basis for economic transformation. In 1991, Czechoslovakia (including Slovakia) succeeded to liberalize up to 95% of all prices.

### ***Privatization***

Privatization became the core of the marketization process. The basic legal and institutional conditions for privatization had been created in 1990–1991 during the so-called “federal” transition phase (i.e. in the period of the united Czechoslovak state). During this period, the laws on property restitutions, “small” and “big” privatization, were approved. The privatization ministries and the national property funds were established in the Czech and Slovak republics.

The process of privatization started with the launching of the so-called “small” privatization that included the sale of retail shops, services, restaurant, caterings, etc. These facilities were sold out at public auctions. The “small” privatization began in February 1991 and it was completed in July 1993.

In 1991, the process of “big” privatization was launched. It entailed the change of ownership of the vast majority of state-owned enterprises in all sectors of industry, agriculture, trade and services after four decades of dominance of state-owned property. Each state company was required to elaborate its own privatization project proposal, containing the scope and conditions of sale. Companies had a choice to apply different privatization methods such as direct sales to particular domestic or foreign investors, tender, public auction, transfer of property to the municipality, sale of shares for vouchers to the population. Ministry of Privatization or the government decided on each project.



After 1993, the privatization process was heavily influenced by the influence of political forces in the country. The law on “big” privatization was amended dozens of times. Other laws related to privatization have been often amended too. Between 1993 and 1995, these laws were amended on average every 51 days which indicates a lack of stability concerning the legal framework of the privatization process. The most significant change in privatization process was the abolition of the second wave of the so-called voucher privatization by the government led by Vladimír Mečiar, leader of the semi-authoritarian national-populist “Movement for a Democratic Slovakia (HZDS)” in 1995.

In 1991–1993, the first wave of voucher privatization that was prepared by the Czechoslovak Federal Government and the first Slovak post-communist pro-reform government, involved 2.59 million of citizens, i.e. two thirds of the country’s adult population. The first wave included privatization of 751 state companies. In the summer of 1994, up to 3.4 million of citizens registered themselves for the second wave, which was prepared by the government led by Jozef Moravčík. It included 648 companies. After the 1994 parliamentary elections, however, the new government led by Mečiar decided to abolish the second wave of voucher privatization. Cancellation of the voucher method of privatization and its replacement by direct sales reflected the intent of HZDS to create the conditions necessary for concentrating economic and political power by generating a system of patronage and protectionism in favor of its own members and political supporters. Between 1995 and 1998, Mečiar’s government carried out non-transparent privatizations favoring its clients and this policy had negative consequences for the economic development. This privatization was evidently disadvantageous for the state: the privatized enterprises were sold at prices much lower than the market prices (sometimes even 80% lower). In return for property acquired at cheap prices, new owners were politically loyal to HZDS, its

government and leaders. At the beginning of 1998, up to 62% of the previously state-owned property was privatized by various methods. 82.6% of the total GDP was created in the private sector.

In order to understand better the broader context of socio-economic reforms in Slovakia in 1990s, it should be noted that HZDS, the winner of parliamentary elections in 1992 and 1994, mobilized its voters during the election campaign particularly by criticizing the “federal” model of economic reforms for being “disadvantageous” for Slovakia. This criticism used as a pretext focused on the negative collateral phenomena which accompanied economic reforms in Slovakia in more excessive manner than in the Czech Republic (deeper economic downturn, higher rate of unemployment, lower level of foreign direct investments). HZDS argued that these negative phenomena were caused by the economic reform itself and not by the peculiarities of Slovakia’s economy that was deformed during the communist regime (large share of defense industry, dependence on Soviet bloc markets, technological backwardness). Despite this criticism, in 1993 and 1994, HZDS continued to implement an economic policy that perpetuated the key trends of the reform strategy applied in 1991 and 1992, particularly in fiscal and monetary areas. In 1995, Mečiar’s government approved the economic program based on the principle of continuity with the inherited transformation path. In practice, however, the government began to make efforts to establish a patronage system with significant elements of state interventionism. Non-transparent privatization process between 1995 and 1998 was accompanied by a policy of economic growth that did not reflect the real possibilities. GDP growth was maintained mainly at the cost of rapid rise of debt and deficit of public finances.

After the elections in 1998, the center-right democratically oriented parties came to power and the privatization process began to focus more on public tenders with participation of international investors. Thanks to this development, the part of state property in the so-called natural monopolies (utilities such as energy complex and telecommunications) was sold through more transparent processes and the restructuring of the banking sector was carried out. In 2006, the share of GDP produced by the private sector amounted to 91.3%.

#### **1.4 Transformation of the welfare system**

Some of the most important aspects of social transformation in Slovakia after 1989 were the changes related to social status of citizens, their access to work, social security, education and health care.

##### *Necessity of reforms*

Social system that existed in Czechoslovakia until 1989 was based on the assumption of social equality among citizens and it emphasized that the aim of public policy was to create conditions for the satisfaction of the wider population by improving life conditions. Public policies emphasized social achievements, full employment and the state welfare system that embraced different sectors of the population. However, gradual economic stagnation led to the deterioration of social “achievements” that the communist state presented as its biggest advantage. The quality of social services and health care system steadily declined. The full employment policy of the centralized and one-sided oriented (de facto deformed) economy further exacerbated the negative trends of economic development – many factories, especially the defense-industry ones, produced their products to store, not to sale. Nevertheless, state had to pay workers full salaries while ensuring the functioning of the welfare system (age

and disability pensions, social allowances to various categories of citizens). State maintained artificial employment, but it became evident that this socio-economic model was simply not sustainable in the long-term term.

Fundamental changes in political and economic system inevitably initiated changes in the welfare system. The reform scenario in this area, presented in October 1990 by the federal government of Czechoslovakia, included privatization in the social sector and encouraged individuals to take over a large share of responsibility for their own living standard. However, due to the short electoral term, the Federal Assembly (parliament) of Czechoslovakia failed to approve all draft proposals of social (welfare) legislation, in particular the draft law on social assistance, before the crucial elections in 1992. After the split of Czechoslovakia and the creation of an independent state, Slovakia started to carry out its own national scenario of social reforms that were implemented in a chaotic manner without a clear conceptual base according to some analysts. This was evident especially in the area of legislation. Some important social laws were approved only after discussions lasting several days and they were often revised and amended later on.

In late 1992, shortly before the division of Czechoslovakia, the National Insurance Office was established in Slovakia that provided the combined social and health insurance. In 1994, the system of social (welfare) and health insurance were separated. The Social Insurance Company was established and the pluralist system of health insurance was introduced. In 1995, the *Concept of Transformation of Social Sphere in the Slovak Republic* was publicized. Its aim was to create conditions that enable citizens to fulfill their social needs through three main sources: labor income, social security and individual insurance.

During the period 2002–2006, radical reforms were launched in the area of social policy, including the pension system. The purpose of the reforms was to evenly distribute the responsibility for creating satisfactory social conditions between the state, private sector and citizens themselves. The elements of pluralism were introduced into the pension system as private pension funds were created. The idea behind the social policy reform was to combine the merit principle and the principle of solidarity, so that every citizen could create the conditions for a dignified life. Reform of health care system was aimed at improving the quality of health care.

Reforms in social sector included changes in pension, welfare, health care and education systems.

### ***Pension system reforms***

The aim of the pension system reform was to achieve the long-term sustainability of public finances that were endangered by long-term unfavorable demographic trends; to strengthen the elements of merit in pension system so that the expected pension would reflect the level of contributions paid into the system; and to increase the incentive for making savings in long term. In 2005, the three-pillar pension system was established. The first pillar includes the continuous pay-as-you-go system, the second (private) pillar is based on pension savings and the third pillar consists of various forms of voluntary pension savings or insurance. The retirement age was increased and the new valorization mechanism of the already appointed pensions was introduced.

### ***Reform of welfare system and labor market***

Another important sectorial reform was the reform of the welfare system and labor market. As unemployment was one of the most pressing problems in Slovakia since the beginning of 1990s, the

urgency of these reforms were clear. At the initial stage of transformation, trade liberalization, privatization of state assets and restructuring of the economy were accompanied by massive redundancies, especially the employment of workers in unprofitable state enterprises. At the end of 1990s, the rate of unemployment in Slovakia rose to 20% of labor force. In mid-2000s, it decreased to 7%, but in 2012, it increased again to 14%, mainly due to the global economic crisis. The state had to cope with this new social problem by creating a separate system of social assistance and professional retraining (re-qualification) of workers. The aim was to provide citizens who have lost their jobs with the opportunity to start their professional career again.

Slovakia's experience showed that the unemployment rate had a direct correlation with the type of socio-economic policy pursued by the government. After 1993, the lowest unemployment rate in Slovakia was recorded when the country was ruled by political forces that introduced liberal economic reforms which improved the overall business environment, created favorable conditions for the inflow of foreign capital and the introduction of new technologies. On the other hand, when the country was ruled by parties that emphasized state regulation and refused to further liberalize the market environment, unemployment rate increased.

The aim of welfare system and labor market reform was to support the working class families, to strengthen employment growth, to create a flexible labor market and to increase the level of targeted assistance to people in need and disabled people. Flexible Labor Code was approved and tax burden was reduced. Penal Code increased the flexibility of labor relations. It introduced a simplified procedure of dismissal in case of economic difficulties or dissatisfaction with the work of individuals. Simplified process of employment for fixed-term and part-time removed relatively strict limits for working pensioners.

Before this change, they could not work longer than a year. The reform that envisaged an active policy for the labor market focused on the creation of an effective “helping hand” for long-term unemployed persons seeking to return to work. However, the Labor Code was amended by every new government since the positions of center-right and left-wing parties were significantly different in the area of labor market.

### ***Reform of the health care system***

The health care system reform is an example of an unfinished reform. It was launched in 2002, but the left-oriented government led by Smer-Social Democracy Party that came to power in 2006 refused to continue implementing it. The aim of the reform was to create a model that included flexible tools for implementing the health policy; to modify the role of the state in health care system; to ensure balanced and financially sustainable management; to prevent the abuse of the health care system, to improve the quality of health services; and to form a competitive environment. Key measures in the health care reform included the removal of free of charge health care services; the introduction of symbolic fees for basic health services such as visits to physicians, drug prescriptions, hospitalization, and use of ambulance transport; the transformation of health insurance companies and hospitals into the joint stock companies; and cancellation of redundant capacities. The measures that introduced symbolic fees for basic health services and the transformed hospitals to joint stock companies were cancelled by the left-oriented government in 2006.

### ***Reform of the education system***

Another example of an uncompleted reform in social sector was the education system reform. Although some measures have been taken such as the transformation of the state administration of education at

the regional level, the introduction of a multi-source model for financing that included the payment of tuition at universities and the creation of a student loans model failed mainly due to political reasons. The model of equal funding of public and private universities was not established yet and the education market was not open for foreign high schools and universities. The process of changing the content of education was also impeded.

### **1.5. Social partnership and social dialogue**

After the change of the political regime, a mechanism of so-called tripartite negotiations (government – trade unions – entrepreneurs) was established. Trade unions and business associations gained the opportunity to influence the content of the upcoming legislative proposals through the tools of social dialogue (social partnership). Social partnership in the form of tripartite negotiations exists in Slovakia since 1990. Currently, it is regulated by a special law on tripartite consultations at the national level. Social partners (trade unions and business associations) negotiate with the government about draft laws concerning the interests of employees and employers, particularly on economic, social, labor and wage conditions. In addition, social partners negotiate about the positions and recommendations on economic and social development and on provisions of the state budget. Every major government decision has to be discussed by social partners. Important government proposals are considered and discussed at the plenary sessions of the Economic and Social Council of the Slovak Republic, which is the consultative and negotiation body of the government and social partners at national level. The aim of tripartite negotiations is to reach mutually acceptable agreements. Partners conclude the so-called general agreement for each calendar year that defines the responsibilities of the government, trade unions, and employers.



In addition to the tripartite mechanism, other institutionalized and non-institutionalized forms of social dialogue exist in Slovakia. There are advisory bodies of the government such as government councils and committees for different areas including public administration, informatization, human rights, ethnic minorities and gender equality, NGOs, elderly people, sustainable development, people with disabilities, culture, crime prevention, science and technology, vocational education and training, etc. Their members include members of organizations representing various segments of the society, experts, and representatives of municipal self-governing bodies. Individual ministries create commissions dealing with specific issues with the participation of civil sector representatives.

## **1.6. European integration**

Slovakia's participation in the process of European integration played a key role in carrying out the transformation process. After the collapse of communist regimes in 1989, the most popular slogan in Slovakia, similar to other Central European (CE) countries, became the slogan of "Return to Europe". This slogan quickly became synonymous with joining a community of states which embodied the idea of a united Europe. Transformation of the society and the endeavor to join the EU became two sides of the same coin.

### ***Tools for EU enlargement***

Immediately after CE countries embarked on the road to democratization and transformation, the EU began to form a new type of partnership with them. First steps were the programs of assistance and economic cooperation. Later the association agreements were signed. Finally the negotiations on full membership for these countries took place. In the post-communist countries,

achieving EU membership was defined as number one priority, which had a society-wide support.

During 1990s, the European Union created a set of instruments to regulate the process of enlargement that had three phases. The character of these instruments reflected the main trends of the transformation process in candidate countries. In the first phase, the European Community/European Union reacted to revolutionary societal and geopolitical changes in CE. In the second phase, EC/EU took into consideration the transformed status of the post-communist states by applying the associated membership. In the third phase, the EC/EU elaborated a pre-accession strategy before the membership negotiations with the applicant countries. It became apparent that EC/EU and the post-communist countries needed to create new forms of relations which would make broader and more intense cooperation possible while encouraging CE countries to deepen their transformation process. The newly defined status of these countries as associated members precisely provided the basis for this new form of relations. It was the introduction of a privileged relationship, which was a de facto symbol of the involvement of CE countries in the process of European integration. The so-called European Association Agreements created an asymmetrical relationship between the EC/EU and associated countries by granting CE countries the opportunity to participate in the processes for reaching some goals of the EC/EU without achieving full membership. Gaining the status of associated members had a practical and symbolic significance because all of the agreements on association referred to commonly shared values. The main goals of the agreements were to establish a platform for dialogue for deepening mutual political relations; to create a free trade zone; to provide support for trade and harmonization of economic relations; to shape the conditions for cooperation in economic, financial, cultural and social areas; and to fight against crime. The provisions on the

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EC/EU's obligation to support CE countries in their efforts to develop functional market economies through the transformation process; to create a framework for gradual integration into the EC/EU; and to create and ensure the efficient work of association institutions were of extraordinary importance. All the signed agreements emphasized the necessity to respect human rights and principles of market economy and they also determined the frameworks for political dialogue. Association agreements directly connected the issue of relationship between the Community and the associated states with the issue of internal societal changes in these states. Emerging institutions in charge of oversight of the agreements were also very important. Thanks to them, the process of association took a systemic character and was highly effective.

The asymmetrical character of relations, which were formed on the basis of the association process, was mostly in favor of the associated members because the responsibilities of EC/EU toward the associated countries were greater than of the associated members toward the EC/EU. Further, the fulfillment of some provisions in certain areas (for instance in customs area) were less beneficial for EC/EU countries. Although the association agreements did not touch directly on EC/EU enlargement, they contributed to strengthening the relationship between the Community and post-communist states and they motivated the associate members to carry out internal reforms.

However, these agreements had their limitations because they did not go beyond the framework of bilateral political dialogue and they contained significant elements of protectionism in the area of mutual trade. Both in the associated countries and in the EC/EU, the voices demanding further steps for deepening the relationship between EC/EU and CE countries started to be heard. The view became dominant in EC/EU that the community would offer the associated

countries a clear idea about the effect that their efforts can have on internal reforms if they were interested in joining the EC/EU at the same time.

### *Copenhagen criteria*

In June 1993, the European Council in Copenhagen formulated a clear position on the prospect of EU enlargement stating that if any European country shows interest in becoming a member state of the Union, it may do so. However, the accession process and EU enlargement can take place at a time when the candidate country is able to accept membership obligations by fulfilling the required economic and political criteria. These conditions included the following:

- stability of democratic institutions, rule of law, respect for human and minority rights,
- functioning market economy,
- ability to meet the pressure from the market of EC,
- ability to accept membership obligations, which include commitment to the goals of political, economic and currency union.

In fact, the first two conditions represented the core of internal transformation processes in the political area (transition to democratic system) and in the economic area (transition to a market economy – carrying out reforms for privatization, price liberalization, economic competition etc). The third condition was about the effectiveness of the implemented reforms. The fourth referred to the strength of a country's conviction to become an integral part of the community and to its commitment to accept the common legislation of community/union (the *acquis*). At the Copenhagen summit in 1993, the European representatives decided

to directly involve the associated countries in the framework of multilateral discussions. The historical decision to start the negotiations with the so-called first group of the candidate countries was made at the EU summit in Luxembourg. The negotiations began in March 1998. Then the European conference –a multilateral forum for discussion about the common positions in various areas– was created and it involved the representatives of the member and candidate states. The candidate countries were offered the opportunity to present their positions on issues of common policies of the organization despite the fact that they were not yet full members. In December 1999, a decision was taken at the EU summit in Helsinki to open negotiations with all candidate countries. The negotiation process and its core procedure – the closing of the particular accession chapters – was putting pressure on the candidate countries to take the necessary legislative and administrative measures aimed at intensifying their reform efforts.

### ***EU conditionality***

Evaluating the impact of the integration process on the development of Central Europe, we can conclude that the process of European integration provided an irreplaceable catalyst for transition in the post-communist countries throughout the 1990s. In fact, in the final stage of the accession process, strong integration conditionality aimed at achieving transformation in the societies of the accession countries was established. This conditionality led to two outcomes – the policy of encouragement for those countries which met the criteria for membership or the policy of refusal for those countries which did not meet the criteria. In the second case, this approach was designed to generate pressure and motivation for carrying out internal reforms in these countries and it activated political forces with alternative pro-integration programs.

Slovakia can serve as an excellent example because the process of EU enlargement fundamentally affected the country's domestic development. Slovakia signed the Association Agreement with the EU in October 1993 and it officially applied for membership in June 1995. However, the Slovak Republic was the only Central European country that had to struggle for democracy and the principal character of its political regime after the communist regime's collapse in 1989. Due to troubled domestic political developments between 1994 and 1998, it failed to comply with the political criteria for EU membership. Slovakia was left outside of the so-called Luxembourg group of EU candidate countries in 1997.

Country's chances to be part of the European integration were renewed after the 1998 parliamentary elections that resulted in the landslide victory of the coalition of democratic forces. In 1999, Slovakia was included to the Helsinki group of applicant countries. At the end of 2002, it successfully completed the negotiations with the EU about membership at the same time with other nine applicant countries, including its neighbors – Czech Republic, Poland, and Hungary. In May 2004, Slovakia became a full member of the EU. In 2007, it entered the Schengen zone and it joined the Eurozone in 2009.

High popular support for idea of EU membership played a very important role in the successful transformation of the country during the accession period. In Slovakia, the European idea enjoyed an exceptionally strong support. The support for Slovakia's EU accession became the main determinant of public opinion concerning foreign policy orientation and it consistently reached very high values. As an institution, the EU has always enjoyed a great confidence among Slovakia's citizens. Public opinion polls have repeatedly shown that trust in the EU clearly prevails over distrust. The public support of Slovakia's EU accession oscillated between two thirds and three quarters of the population.

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## **2. Reforming International Trade in Visegrad Countries**

**Karel Janda**

**Professor at Institute of Economics Studies, Faculty of  
Social Sciences, Charles University in Prague,**

### **2.1 Introduction**

Knowledge of international trade development and its analysis is a necessary condition to understand the incentives of governments when dealing with important issues of European integration. The development of international trade, especially implementation of free trade areas, is a very important part of the overall scene of social and economic policies and of social dialogue among interest groups like exporters, importers and domestic consumers. The trade liberalization development in Visegrad countries provides important lessons for other countries interested in developing closer ties with the European Union or interested in establishing regional free trade areas.

In this paper, we are first going to talk about development of foreign trade in all four Visegrad countries in general. Later, we are going to analyse trade development in four Visegrad countries individually since 1990 in the light of their preparation for accession to EU. Concluding section will offer some remarks concerning foreign trade and a comparison of development in Visegrad countries during last two decades.

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## **2.2 Common Trade Development in Visegrad Countries**

At the end of 1980s, according to Winiiecki (2002), the members of COMECON traded among each other from 40-50% of their overall domestic production to as much as 75% (Romania). Nevertheless, foreign trade was sub-optimal, caused by a lack of market mechanism for the determination of a structure of specialisation at the level of standard economic agents. A market mechanism was substituted by extensive bureaucratic decision-making at the macro level. Hence some problems with external balance and growth had to necessarily occur in long run.

At the aftermath of the demise of the Soviet Union block, all former COMECON countries started to shift from control and command regimes to economies based on market institutions determined by supply and demand forces rather than by bureaucratic central planning. Eastern European countries did not operate under convertible currency system or competitive prices at this stage of their development. State planners could indeed lower prices of exports to stimulate sales; however, it would not automatically affect imports. They could also easily control consumption because they had direct control over wages, employment, and prices (Poznanski, 1996).

Central European Free Trade Area (CEFTA) was established in 1994 originally with four members that are the Visegrad countries. They were joined by Moldova, Romania, and Bulgaria, but founding members left to join the enlarging European Union in 2004.



### **2.3 Individual Trade Development in Visegrad Four**

This section describes trade development since the beginning of the movement toward integration with the EU as envisaged since the early 1990s. Each Visegrad country is analyzed separately.

#### *Czech Republic*

The Czech Republic is the most Western-oriented among the four Visegrad countries, having a favourable geographical position located in the heart of the European Union and being surrounded exclusively by other European Union members. The proximity of developed economies has also been an important factor of its relatively above average economic development. Nowadays, it is often characterized as one of the most successful cases of transition economies. Despite a cost related to the breakup of Czechoslovakia in 1992-1993, the Czech government was able to implement rapidly some market-oriented reforms during the early post-communist period after the Velvet Revolution in November 1989. Extensive economic reforms, such as mass privatization and liberalization of international trade, were top priority for the Czech government in early 1990s, even at the cost of a short run performance.

In their research paper, Svejnar and Uvalic (2009) draw our attention to the economic performance of the Visegrad economies in 1989. They characterized Czechoslovakia as one of the less reformed Central and Eastern European (CEE) countries and much less of a market economy in comparison to Poland and Hungary. It had the highest share of public sector (97% of net national product). The economy was concentrated within monopolistic firms and it was the most dependent economy on

trade with other Soviet countries. A complicated system of bilateral trade agreements based on the non-convertible currency was introduced within the COMECON. Contrary to other Central and Eastern European countries which faced hyperinflation already in 1980s, Czechoslovakia had to face a rather moderate inflation during early years of its transition process and Czechoslovak budget deficit and unemployment were also relatively low.

The Czech Republic increased its export to the EU between 1993 and 1999 from US \$8 billion to US \$18.4 billion. That implies an annual average growth rate of 16.3%, while Czech exports to the rest of the world continued to grow at a normal rate of 4% annually. Trade liberalisation created enormous opportunities for Czech exporters. Authors considered this surprisingly fast development of external trade in 1990s to be a crucial moment of Czech economic transition. Czech import and export both increased by almost 500% in total during the last two decades (CzechTrade, 2008).

Balance of payments surplus was reported in 1991; however, there was already a balance deficit one year later. It was caused by expected instability linked to a political situation and a tax reform introducing VAT taxation. A share of imports increased as a form of pre-supplying. The first year of the Czech Republic was considered to be quite successful with export surplus. The sharply increased demand of Czech consumers could not be satisfied exclusively by Czech manufacturers in the following years, thus it needed to be covered by import. Czech export and import achieved growing year-on-year performance each time with an exception in 2002 and with the highest annual difference in 2004 for export and in 1995 for import (CzechTrade, 2008). However, Czech balance deficit was reported each year during last 2 decades.

Territorially, Czech export shifted from former COMECON countries to mostly 15 European Union countries. European Union export formed at least 80% of Czech export and minimally 70% of Czech import (CzechTrade, 2008) since 1993. Thus, developed countries, especially Germany, created the widest group for both Czech export and import, followed by European transition and developing countries. China has been an important import partner with gradually increasing performance. Overall, the most important trading partners for the Czech Republic after 2004 were Germany, Slovakia, Poland, and France. European Union countries accounted for more than 85% and other developed states outside of the European Union for more than 9% of export.

Czech export has been historically composed of goods for processing in general. Export of machinery and means of transportation increased throughout the last two decades and they formed 43% of overall export in 1999. Their quantity increased by 1000% during this period (CzechTrade, 2008). Other important group of export goods is chemicals and consumer goods such as textile and furniture, scientific devices and other industrial goods. Mesaros (2001) also pointed out an effect of free import of subsidized agricultural goods from other European Union countries that ruined Czech agriculture. In the first decade of the 21st century, machines and other transport equipment formed the biggest group of exporting products (50%), followed by manufacturing products (around 20%). Those two groups also formed the biggest share of import goods.

### *Slovakia*

Jakoby (2000, 2002) published an extensive study of the Slovak foreign trade in the transition period. Similar to other transition economies, the international trade of the Slovak Republic is

characterized by a sharp increase of exports and imports shortly a year after 1989. It was caused by the removal of a state monopoly and massive liberalization. The typical feature was a balance deficit in early years of transition. A surplus was reported in 1994 and it was replaced by a substantial deficit caused by the absence of restructuring and the inability to preserve a fixed exchange rate of koruna. Slovakia experienced a relative slowdown of exports in 1996. Thus, raising export performance together with decreasing the balance deficit became the top priority for the new Slovak government in 1998. New stabilization measures were put into practice in 1999 and 2000. More concretely, these measures included an increase of adjusted prices, an increase of indirect taxes and a VAT basis, and the reintroduction of import fees. Their mutual objective was to decrease domestic demand, hence to decrease import. A short-term stabilization of the balance in 1998 and an increased deficit in late 1990s caused by growing import and fairly stable export is also highlighted by Jakoby (2002). According to Jakoby (2000), the current account deficit exceeded 10% critical value of the Slovak GDP. Moreover, the Slovak foreign debt grew significantly throughout 1990s. Dynamics of Slovak export tended to slow down around 2005, with turbulent changes of balance surpluses and deficits. In 2006, there was a significant growth of both export and import value (adequately of about 24% for export and of about 22% for import). The deficit increased steadily in the period between 2004 and 2007 (Wach et al., 2008). Balance deficit sharply increased in 2008. After this year, balance deficit moderately decreased and its surplus is reported in the period between 2009 and 2011.

Machinery and electronic devices formed a stable and considerable part of Slovak export in the beginning of the new century. The major part was created by intermediate products that were highly dependent on price factors. Jakoby (2000) also states that the

historically important share of iron and steel decreased in 1990s and the modern sector with audio-visual equipment and motor vehicles became more important for exporters at the same time. This growth was mainly accomplished by Volkswagen Bratislava that became the biggest exporter in Slovakia. Agricultural products formed only around 4% of overall export. Automobile industry keeps its leading position in export nowadays. On the other hand, components for the automobile industry account for the biggest share in Slovak import in the new century.

Slovak exporters quickly reoriented towards Western markets. Two main blocks of the Slovak export (90%) were the European Union and the Central European Free Trade Area (hereinafter: CEFTA). Export to the European Union doubled during the 1990s and export to CEFTA countries remained roughly stable. The biggest decrease in export was recorded with the Czech Republic (caused by its recession in 1997-1999) and with Russia (Slovak dependence on raw material imports implied long-time passive balance of payments). Primary export partners became Germany (around 30%, but decreasing throughout time and 23% in 2011) and the Czech Republic (around 10% with an increasing trend and 20% in 2011) in the 21<sup>st</sup> century. Other major partners in 2011 were neighbouring countries: Poland, Hungary, and Austria. Slovak export to these countries increased in comparison with the previous year.

### *Hungary*

A considerable market-oriented reform and decentralization had already taken place in 1968, in comparison with Poland (early 1980s) and with Czechoslovakia where archetypal characteristics of central planning and a state ownership prevailed until the process of decentralization started in 1989. Although the reform process was gradual with many setbacks in Hungary, it was better

prepared for the dramatic political liberalization in 1989.

Hungarian external debt reached 75% of its GDP, which put Hungary in the group of very highly indebted countries in the initial years of transition. Hungary was very close to a liquidity trap. A rapid export growth to Western countries improved the balance deficit quickly. Some factors that contributed to the massive growth of exports in Hungary are considered to be the transformation to world prices in 1991 and convertible currency. Overall, export increased each year during the last two decades with the exception of 2009. Nevertheless, Hungary experienced a negative balance since the beginning of 1990s until the year 2009.

A typical feature of European transition countries, the shift of export towards Western markets, was also reported in Hungary. The share of export to the European Community increased by 35% in 1990 and by 42% in 1991. There was also a 27% decline of export to COMECON countries reported in 1991. The share of export to European Union increased from 40% shortly after opening of Western markets to 75% in 2011.

The liberalization of private activities caused an expansion of export-oriented small businesses. They increased by 69% in 1991, especially in machinery, chemical and light industry, and food processing export categories. Hungary now focuses on exporting machinery and transport equipment that accounts for more than half of the total export, followed by manufactured goods and food.

### *Poland*

The composition of export goods moved towards natural-resource and unskilled labour-intensive products during the 1980s. Only exporters of coal and farm products were able to succeed in

increasing their shares in OECD markets. Export improved in all product categories in 1990 and 1991, most importantly in manufacturing with an average annual rate of growth equal to 40% (Kaminski, 1991).

Since 1994, the overall volume of export increased each year in comparison with the previous year. The sharpest growth was achieved in 2000. The amount of export grew by more than 600% throughout the last two decades. To describe changes in foreign trade in Poland, it is necessary to point out the transformation of the deficit in trade from EU 15 from EUR 6.6 billion in 2001 to a surplus of EUR 1 billion in 2006. The largest influence on the deficit was created by foreign trade turnovers from Russia and China. The growth of deficit only with these two countries in the period between 2005 and 2007 leveled the surplus from EU24 countries (Wach et al., 2008). The growth of exports started to slow down relatively in 2007 and a slightly negative growth was reported already in 2009.

After the Second World War, the Soviet Union became the most important partner for Polish manufacturers together with Czechoslovakia and Germany for four decades. After the demise of the Soviet Union, Polish manufacturers quickly reoriented towards Western markets. Germany became a major partner for export and especially for import.

Nowadays, the European Union accounts for almost 80% of exports and 60% of imports while Central and Eastern European countries account for only around 10% of the trade turnover.

Export product goods moved significantly from minerals and food in the beginning of 1990s. The share of high-processed products in export value increased around 2005. The main group of export products was electro-machine industry items. Increasing

competitiveness of Polish goods is visible. The share of high-processed products in export value increased from 56.8% in 2000 to 63.7% in 2006(Wach, 2008). Nowadays, the Polish manufacturers mainly focus on exporting machinery and electrical equipment as well as transport equipment. It is important to note that transport equipment has been historically an important category of the Polish export. Other consequential export product groups are metals and chemicals.

## 2.4 Conclusions

A common feature of international trade of the Visegrad countries was a strong orientation towards the Eastern bloc and COMECON countries. They traded extensively among each other. However, this trade has been considered to be sub-optimal due to state planning and the absence of free markets. A dominant part of trade of the Visegrad countries shifted from the East to the West after the end of the Soviet pressure for keeping goods in the Soviet bloc. Winiecki (2002) investigated a structural change of export partners (as well as import partners, however with a delay) of CEE countries. The trade moved where the markets were, towards the high-income Western countries. On the basis of Heckscher-Ohlin theory, an increase in exports of traditional labour-intense production goods was expected. Being in the heart of Europe and relatively close to some large production centers in Europe, CEE countries also possessed a location advantage. Table 1 contains empirical evidence in support of this theory. We can observe that the West-oriented trade expanded more rapidly than expected.

Another typical feature of early transition trade is that all CEE



Table 1: Geographical change of exports: in % shares of aggregate exports

Country	1928	1988	1994	1996
Czech Republic Westbound	55.2	33.5	58.9	62.8
Eastbound	19.8	55.2	31.8	30.6
Hungary Westbound	40.9	37.2	71.5	69.0
Eastbound	37.3	45.5	25.2	28.8
Poland Westbound	62.7	44.7	75.0	71.6
Eastbound	14.2	40.8	15.0	21.4

Note that Westbound stands for 1988-1996 OECD countries except Turkey and Eastbound for ex-COMECON countries including Turkey; data for 1928 and 1988 are for Czechoslovakia  
Source: Winiecki (2002)

Countries imported more sophisticated and high-quality products from the West than the ones they exported. Nowadays, a vast majority of overall export is headed towards the European Union, especially to Germany (the major partner of Czech and Polish exporters). Slovak exports are headed mainly towards the Czech Republic and Germany.

After the EU accession of the Visegrad countries in 2004, one of the most remarkable developments was the sudden increase in mutual trade. In 2007, the value of aggregate intra-Visegrad trade was 2.5 times higher than in 2003. The growth rate of the trade of these countries with the “old” EU member states was only half as much. Although they similarly witnessed a rapid expansion, individual intra-Visegrad bilateral relations had diverging character concerning the composition of trade. Hungary’s excessive specialization in transport equipment and components in exports

to the other three Visegrad Group countries was considered to be extreme. Another extreme was Slovakia because the initial proportions across main commodity groups hardly changed in the period of rapid expansion of trade volumes.(Hunya, 2011) Automobile and transport industry accounts for the major part of exports in Slovakia, Poland, and Hungary. Hungary also exports food while Poland and Slovakia are both famous for their electrical device plants that are widely spread.

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### 3. EU Integration and Social Policy in Hungary

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**Katalin Tausz, Independent Expert**

#### 3.1 The notion of social policy in the EU vocabulary

Social policy has several different definitions in the academic discourse. Some apply a functional approach, others, identify it with the different institutions providing social services, while some, more complex definitions are deeply embedded in the social structure. To quote a classic, T. H. Marshall: *““Social Policy” is not a technical term with an exact meaning ... it is taken to refer to the policy of governments with regard to action having a direct impact on the welfare of the citizens, by providing them with services or income. The central core consists, therefore, of social insurance, public (or national) assistance, the health and welfare services, housing policy.”*<sup>142</sup> In this approach social policy is a response to human needs and this way affects the well-being of members of the society through redistributing the resources.

There is no clear cut definition or concept of social policy in the EU, rather different activities and political declarations reflect the actual understanding or interpretation of it. These interpretations, similarly to the nation states, tightly correlate to the economic situation and the dominant ideological considerations of the community.

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<sup>142</sup> Marshall, T. H., *Social Policy*, Hutchinson, London, 1965, p. 7

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Historically analysing the evolution of social policy in the EU at the beginning a rather descriptive, administrative type of approach was applied related to issues of labour market policy. Then the scope of the incorporated areas broadened covering gender related issues and later institutions like the pension and the health care systems.

The Treaty of Amsterdam reflected a significant change in this descriptive approach when speaking of social rights and extending the competencies of the community to handling certain social problems, first of all the problem of poverty and social exclusion.

The Treaty of Lisbon at the millennium resulted in a conceptual breakthrough when integrating social cohesion to the strategic objectives of the Union and liberating it from the subordinated situation to the economic policy. At EU-Summit Nizza the first strategic document of social policy emphasizing the productive nature of the discipline, the Social Policy Agenda was adopted. The Social Policy Agenda introduced new initiatives like the modernisation of social protection, the promotion of social inclusion and support to anti-discrimination programmes.

The next, most recent, development is the Europe 2020 strategy. As José Manuel Barroso, President of the European Commission framed: *“Europe 2020 is the EU's growth strategy for the coming decade. In a changing world, we want the EU to become a smart, sustainable and inclusive economy. These three mutually reinforcing priorities should help the EU and the Member States deliver high levels of employment, productivity and social cohesion. Concretely, the Union has set five ambitious objectives - on employment, innovation, education, social inclusion and climate/energy - to be reached by 2020. Each Member State has*

*adopted its own national targets in each of these areas. Concrete actions at EU and national levels underpin the strategy.*"<sup>143</sup>

When analysing these sentences one has to perceive a controversy: in one of the sentences an inclusive *economy* is mentioned which does not automatically imply an inclusive society. However in another sentence social inclusion is one of the five equally important objectives.

Summarising: in spite of the gradual enrichment of the interpretation of social policy and ever so ambitious are the above mentioned objectives subsidiarity still remained the central principle concerning the social protection system. "*Charter of Fundamental Rights of the European Union does not declare, independently from the legal system of the member states, directly enforceable social rights, but delivers a message which may contribute to a stronger protection of social rights. First of all a structural innovation is worth to mention: grouping the fundamental rights along the values protected by them abolishes the situation when the social (and economic) rights are quarantined and as traditionally, are subordinated to civil and political rights.*"<sup>144</sup>

### 3.2 Procedural and institutional changes

Hungary joined the European Union at 1st of May 2004 as the country fulfilled the Copenhagen criteria: „*Membership requires that candidate country has achieved stability of institutions*

<sup>143</sup> [http://ec.europa.eu/europe2020/index\\_en.htm](http://ec.europa.eu/europe2020/index_en.htm)

<sup>144</sup> Juhász Gábor (2012 ) Szociális jogok az EU Alapjogi Kartájában. in: Az Európai Unió szociális politikái. p. 55. <http://tatk.elte.hu/intezetek/szocialis-tanulmanyok-intezete/szocialpolitika-tanszek/e-tananyagok>

*guaranteeing democracy, the rule of law, human rights, respect for and protection of minorities, the existence of a functioning market economy as well as the capacity to cope with competitive pressure and market forces within the Union. Membership presupposes the candidate's ability to take on the obligations of membership including adherence to the aims of political, economic and monetary union.*"<sup>145</sup> Hungary expressed readiness to adjust the administrative structures as well as legislation to the requirements of the EU.

However Copenhagen criteria do not refer to the so called European social model and to the obligation of the accession countries to adjust their social protection systems to the welfare regimes of the 'old', West-European member states. "*... The Commission, when evaluating the progress reports hardly paid any attention to the measures and legal arrangements targeting social policy. Comments made reflected: synergies concerning the social protection systems are rather the formal than the substantive preconditions.*"<sup>146</sup>

EU founders believed the full harmonisation of social policies is not a necessary component of integration. Harmonisation in this case would mean common standards, uniformity, identical regulations in different fields of the social protection system. Coordination does not affect the sovereignty of the member states to shape their own national social policy systems. In other words: harmonisation would approximate the different welfare state regimes, while coordination (in terms as it is used in 'OMC') sets targets, priority areas, social

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<sup>145</sup> Presidency Conclusions, Copenhagen European Council - 21-22 June 1993, 7  
[http://www.europarl.europa.eu/enlargement/ec/pdf/cop\\_en.pdf](http://www.europarl.europa.eu/enlargement/ec/pdf/cop_en.pdf)

<sup>146</sup> Juhász Gábor (2012) A bővítési folyamat szociális vetülete. in: Az Európai Unió szociális politikái. p. 255. <http://tatk.elte.hu/intezetek/szocialis-tanulmanyok-intezete/szocialpolitika-tanszek/e-tananyagok>

and institutional problems to be solved, but procedures of implementation are tailor-made.

Thus social policy, based on the principle of subsidiarity is the responsibility of the nation states: no regulations, concerning the provisions and financing the social protection system, are incorporated into the legislative system of the European Union. *“The EU started relatively late to inject social considerations into the enlargement process. A vision connected to the European Social Model could have been instrumental in handling the social problems emerging after the transition but did not play a basic role in shaping Hungarian social policy. (...) the European impact in the social sphere has strengthened over recent years, and its main payoff is the growing interest and commitment of politics towards poverty and inclusion, and the widening practice of civil and social dialogue.”*<sup>147</sup>

Ferge and Juhász based the analyses on the impact of the EU membership on social policy in Hungary on three dimensions: *procedural changes, institutional and administrative changes and substantive changes.*

As far as the *procedural changes* are concerned – in line with the EU requirements – the main organisations of social dialogue were institutionalised in Hungary and even financial resources were provided by the EU to diminish the democratic deficit, but the quality of the social dialogue (the role and activities of the trade unions, the strengths and the relevant involvement of the civil organisations in the decision making processes etc.) was not monitored.

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<sup>147</sup> Zsuzsa Ferge-Gábor Juhász (2004) Accession and social policy: the case of Hungary. *Journal of European Social Policy*; Vol 14(3) p.1.



According to János Kornai “*The communist system led to a “premature welfare state,” with universal entitlements out of all proportion to the country’s resources and the fiscal capacity of the state.*”<sup>148</sup> Some social policy experts and sociologists –among them Zsuzsa Ferge contend this approach which subordinates social policy to economics, leaves out of consideration the societal impact of it and applies a one dimensional evaluation, namely the costs of social policy. „... *despite all its inhuman features and tragic failures, state socialism was not unqualified evil. Unlike its political or economic system, its social (societal) policy was not an artificial construct, forced in an inorganic way on the country. By development, and assuring access on a mass scale to the health care system, to education and to stable incomes, it contributed to the eradication of practically feudal social distance, the very significant reduction of utmost poverty, and the development of human capital.*”<sup>149</sup>

By the accession in 2004 the bases of the social protection system were laid in Hungary: the main components of the regulatory and the institutional framework were settled (branches of social insurance, family benefit system, child protection, social assistance, social services). However characteristics of the social protection

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<sup>148</sup> János Kornai (1997) Editorial: Reforming the Welfare State in Postsocialist Societies. World Development, Vol. 25, No. 8, Elsevier Science Ltd. p. 83.

<http://www.kornaijanos.hu/Kornai1997%20Reforming%20the%20welfare%20state%20in%20postsoc%20societies%20-%20World%20Development.pdf>

<sup>149</sup> Zsuzsa Ferge (1997) “Is the world falling apart? A view from the east of Europe”, in Berend, I. (ed.) *Long-Term Structural Changes in Transforming Central & Eastern Europe (The 1990s)*, München: Südosteuropa-Gesellschaft in cooperation with the Center for European and Russian Studies, University of California. p.108.

system were more strongly influenced by path dependencies, ideologies and political orientation of the ruling elite as well as by the pressure of some international organisations (World Bank, IMF) than by the so called European social model.

New social risks, first of all increasing unemployment and inactivity rate, poverty and social exclusion were recognised, institutions and services dealing with these problems were set up before the beginning of the accession process.

Equality had a crucial role in the dominant ideology of the state-socialist regimes. None the less due to compulsory employment there were relatively low income inequalities and efforts – sometimes leading to extreme solutions – were made to guarantee gender equality, some problems like the situation of the Roma population, the disadvantages of people with disabilities and other minority groups were not handled adequately. However, these minority groups carried heavier burden from the costs of transition than the majority population as they had and have to cope not only with the increasing existential insecurity but with the growing intolerance and several forms of prejudice. Attitudes of people cannot be easily altered especially when a large proportion of the population has to face economic difficulties when looking for scapegoats is an almost natural psychological reaction to this situation, but the institutionalisation of discrimination can be prevented. In this field directives of the EU strongly influenced the institutional development in Hungary.

*„Chapter III  
Bodies for the Promotion of Equal Treatment  
Article 13*

*1. Member States shall designate a body or bodies for the promotion of equal treatment of all persons without discrimination on the grounds of racial or ethnic origin. These bodies may form part of agencies charged at national level with the defence of human rights or the safeguard of individuals' rights.*

*2. Member States shall ensure that the competences of these bodies include:*

- without prejudice to the right of victims and of associations, organisations or other legal entities referred to in Article 7(2), providing independent assistance to victims of discrimination in pursuing their complaints about discrimination,*
- conducting independent surveys concerning discrimination,*
- publishing independent reports and making recommendations on any issue relating to such discrimination.”<sup>150</sup>*

The regulation came into force in 2003 and antidiscrimination legislation was enacted this year in Hungary and The Equal Treatment Authority was set up to conduct “*proceedings if the principle of equal treatment might have been violated either at the request of the injured party or upon its own motion (ex officio) in*

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<sup>150</sup> Council Directive 2000/43/EC of 29 June 2000 implementing the principle of equal treatment between persons irrespective of racial or ethnic origin

*cases set forth by law in order establish whether any discrimination occurred.”<sup>151</sup>*

Based on the fundamental principles of the EU and recognising the large regional economic differences on the continent various programmes were launched to level off these inequalities having the potential to result in serious social tensions and hampering permanent and sustainable economic development. Financial resources for these activities were provided through the Structural Funds, for Hungary since 1989. Hungary, as every accession country, had to create a system of brand new institutions to make them able to receive financial resources, to carry out the tender procedures, to implement a large amount of programmes and to monitor them. A huge, new administrative capacity was generated and a new culture, the culture of tendering operation was established. As a precondition of access to these resources developmental objectives, adjusted to the overall objectives of the EU, had and has to be elaborated and implemented.

Besides the unquestionable gains of the enormous financial resources and the new institutional framework the shades also became visible. The practice of tendering and project based operation broadened and social services formerly provided with normative financing became grant based to make budgetary cuts, have to participate in a tendering procedure which makes their functioning more unstable (e.g. services providing panic button for the elderly citizens, support service for disabled people). Another serious problem is due to the timing of disbursements and the overcomplicated bureaucracy. Smaller non-profit organisations, typically initiating innovative solutions for different social problems and covering so far neglected areas of social protection,

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<sup>151</sup> <http://www.egyenlobanasmod.hu/index.php?lang=en>

have no sufficient funds to bridge the financing gaps and face tremendous problems in their functioning. The government in power is responsible for the third type of difficulties: EU funds favour the creation of new services, new solutions and new procedures however resources to uphold the services are frequently missing after the completion of the projects.

### **3.1 Open method of coordination – and the fight against poverty and social exclusion**

The fight against poverty and social exclusion was integrated into the community policies by The Treaty of Amsterdam and the Treaty of Nizze disposed of the application of the Open Method of Coordination to facilitate the success of this objective.

The open method of coordination (OMC) is an alternative form of governance in the EU based on 'soft law' (guidelines, declarations and opinions instead of directives and regulations) aiming at to spread best practices in areas where the member states are unable to agree. OMC is applied to employment, research and development, immigration, enterprise policy and social protection. The OMC is targeting complex problems like the sustainability and quality of the pension and health care systems or the reduction of poverty and social exclusion in Europe. The failure in the implementation of the jointly outlined policies is not punishable due to lack of lack of 'hard' measures.<sup>152</sup>

*„The substance of the open method is that the member states – following minimal 'editorial' guidelines – thematise the social issues, determine the political procedures and the measures to be applied. (...)*

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<sup>152</sup> Juhász Gábor- Taller Ágnes(2005) A társadalmi kirekesztődés elleni küzdelem az EU új tagállamaiban Esély 2005/6

*Coordination means the national social policies has to be summarised in a National Action Plan against Poverty and Social Exclusion; social conditions and results have to be supported by indicators, indices and statistical data provided by the EU.”<sup>153</sup>*

Thus OMC has an indirect impact on the social policies of the member states only. Although social policy in Hungary is dominantly determined by the values and ideologies of the government in power even if the consecutive always refer to the situation of the national economy, OMC resulted in some positive changes in running Hungarian social policy.

Hungary joined the OMC before becoming a member state. Hungary also elaborated a social inclusion strategy and followed the logic as well as the structure of the OMC: translated the European level policy goals into a national policy, created specific benchmarks and indicators to measure the output and exercised monitoring and evaluation. Although OMC and the national social inclusion strategies have not resulted in substantive changes in the level and nature of poverty and social exclusion in Hungary, but promoted the evolution of a more result-oriented approach in the preparation phase of the governmental measures (e.g. setting up the institutional background of new statistical data collections due to the requirement of using the Laeken indicators, execution of regular data collections, inform the public about the results of these data collections etc.). Voluntary undertaking these requirements of the OMC uncovered so far neglected dysfunctions of the social protection system, however that's another pair of shoes that what kind of actions followed these 'discoveries'.

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<sup>153</sup> Krémer Balázs (2002a): Az EU „bujkáló reformjai” – avagy: mihez is kellene csatlakoznunk? Kézirat, Budapest

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This Janus-faced character of the commitment to fight against poverty and social exclusion was clearly reflected in the different national action plans.

As Juhász and Taller expressed<sup>154</sup> new member states were inclined to ‘recycle’ previously developed templates in their national action plans instead of focusing on targeted measures to handle poverty and social exclusion. According to the above mentioned authors another characteristic feature of the action plans is the lack or the very weak correlation between the statistically described objectives and resources assigned to the measures indicating that “*public policy commitments were not associated with budgetary ones that is social inclusion strategy hardly hit the redistributive relations of the member state.*”

Paradoxically in most of the national action plans statistical data are provided to describe the situation, however, for instance in the Hungarian one, the objectives are not specified or expressed in indicators.

However due to the specificities of the OMC genuine commitment to the fight against poverty and social exclusion cannot be enforced and no sanctions can be made if the objectives are not realised.

Nevertheless extended and deep poverty as well as social exclusion can be combated if a strong and sincere political will exists, but this is what is and was missing in Hungary.

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<sup>154</sup> Juhász Gábor-Taller Ágnes ( 2005 ) A társadalmi kirekesztődés elleni küzdelem az EU új tagállamaiban Esély 2005/6 p.50.

### 3.2 Words, meanings and objectives

Social policy was not an independent sector in the state socialist countries; due to the lack of the market economy and the political democracy social protection systems were functioning, to some extent, but welfare states did not exist there. The transitions occurred in many respect belatedly, in the period of deepening crises of the traditional welfare states. During the golden ages of the welfare state these countries lived in another type of regime, they had no modern traditions to go back to, the welfare state is not embedded in their civilization heritage. When developing their new welfare systems, by and large they could not rely on anything else but the very controversial solutions in the so called Western European countries. *“When Western European societies approached the concept of an integrated Europe it had become clear as day to the nation-states that the universal programs institutionalized after World War II had not been able to establish equality in social rights. They knew that unless they continued reforming their national welfare policies it would be impossible to design welfare policy principles and practices that were operable throughout the community. Eastern Europe, however, is sidestepping a major phase in the process as it approaches the European Union. Though it has never even designed national welfare policies, it is already thinking in terms of superseding them. However, sidestepping an indigestible problem is quite dangerous and may lead to a backlash that far surpasses the original difficulty. An overemphasized belief in sameness (“even in our problems, we are just like the West”) lends itself to social falsehoods, and the political response to a falsehood can only be harmful.”*<sup>155</sup>

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<sup>155</sup> Júlia Szalai (2002) Social Outcasts in 21st Century Hungary *Review of Sociology Vol. 8 (2002) 2, 36–37pp*



This is why it would be so much important to have a ‘European level vision’ on the future of the European societies, on the characteristics of a good society and worded in a language understandable and acceptable for the politicians and the ruling elites. However because of the above recited reasons this is recently lacking.

We have a two level social policy in the Union: one on the national levels and another on the community level. Regulatory systems, approaches, objectives are differing, sometimes diverse. In this sense it was not an unfounded apprehension to raise doubts regarding the accession of the post-communist countries saying they may undermine and erode the traditional European social model. Social policy of the European Union cannot be interpreted with the notions and logic used on the national level. The EU ‘parallel’ of social policy is so much differs from the national social policies that efforts were made to use a different language. An umbrella expression - social dimension of the EU - was applied to label the very different national policies. Due to the fundamental economic, demographic and social changes in Europe and the new challenges to the employment and social policy of the Union the label changed and recently rather the European Social Model is the point of reference. Even though no detailed and analytical interpretation of these two phrases was and is provided, it is evident the denotation of these expressions is not identical. The social dimension refers to certain policies (employment, social protection); the European Social Model comprises values, principles and traditions.<sup>156</sup> The same haziness characterises the objectives of social policy. In some periods social policy was reduced to problems of employment and the increase of the efficiency of the labour market was the main objective. Later other

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<sup>156</sup> Gyulavári Tamás-Krémer Balázs (2004) Európai Szociális Modell?Útközben a jogharmonizációtól a jóléti politikák konvergenciája felé Esély 2004/3

areas of social policy sneaked into the EU level discourse (poverty, social exclusion, migration etc.) however even well defined target indicators are inappropriate to outline in a systematic and complex way the desired future. Regulations, guidelines, political declarations, the Open Method of Coordination may have the potential to contribute to the convergence of the national social policies, but cannot substitute a well defined concept based on the theory, traditions and practices of the welfare state and social rights of the European citizens.

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#### IV. EU INTEGRATION ISSUES IN VISEGRAD COUNTRIES, STUDENTS VIEWS

### **1. State policy of Hungary in the field of relations with civil sector and the role of civil sector in the process of Euro integration of Hungary**

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**Zaal Kvinchia**

**Fourth course student of Tbilisi State University, Faculty of Social  
and Political Studies**

Hungary is one of successful countries among the Visegrad countries, where positive interactions between civil sector and government were intensified as a result of rational and reasonable policy.

Cooperation between the government and civil sector covers wide range of mechanisms and instruments, and the main thing is relevant legal basis which facilitates to stable functioning of civil sector, its development and creation of other nongovernmental subjects. Phenomenon oh Hungary is very interesting, since government funding for development of civil sector is reality here. National Civil Fund of Hungary facilitating to civil society was established namely for these purposes. The activities, functions and goals of this fund will be discussed later. Following issues will be discussed in this document:

1. Legal norms regulating operation on nongovernmental organizations, legal bases and state approach of Hungary to this sector;
2. Analyses of innovative methods public funding for development of the sector;

3. Forms of institutional cooperation between government and NGOs;
4. Programme documents used for sector development;
5. Participation of NGOs in decision making and policy making of Hungary;
6. Role of civil sector subjects in the process of EU integration of Hungary.

### **The Laws which regulate the rules for establishment and operation of NGOs**

The Laws on NGOs develop grounds for their functioning, which regulate operation of the organization from registration until its liquidation, standards of political participation, also determine status of charity organizations and so on.

During last decade Hungary is considered as a leader in development of legislation regulating operation of NGOs, among Visegrad countries. First Laws on associations and funds were adopted in 1987, which regulated the rules for operation and management of such organizations. In 1997 the Law was adopted in Hungary, which determined separately the status of charity organizations and established special lightened tax norms.

Hungary acknowledges two main forms of nongovernmental subject: association and fund.

In Hungary the fund could be established only for benefit of the interests of society, consequently the fund should issue grants; with this regard serious amendments to Civil Code were planned in Hungary, the goal of which is legalization of the funds focused on satisfaction of private interests.

In Hungary in parallel with associations and funds third form of NGO – non commercial union - was introduced. Consequently any commercial agency can have status of non commercial union and request for the same tax benefits as associations and funds.

There is a separate Law on charity organizations in Hungary. This Law determines status of charity organization and differentiated from one another the agencies such as for example gambling club (individual benefit) and organization focused on provision of wider benefit. This law has great importance of stability of NGOs, since in other Visegrad states and in the most of Eastern European countries the status of charity organization provides conceptual precondition for getting benefits, similarly to real charity organization, which is of course bad practice in legal field.

In this regard the legislation of Hungary is much more preventive, rational and precise. Hungarian Law on charity organizations is interesting because it identifies two levels of charity activities: basic and exemplary. The organization which implements tasks assigned by local governance and cooperates with political institutes, can have status of charity organization. Despite of the fact that just 6-7% of Hungarian NGOs have this status this still demonstrates good example of cooperation between civil sector and the government, which is focused on implementation of joint projects. Other organizations which do not have above mentioned status are considered as basic charity organizations.

### **Support of the NGO to Government in getting private income and philanthropy**

Normally the NGOs have three sources for income generation and financial resources: economic activity (rent, passive investments), direct public investments and philanthropy (sacrificing time and

money). As a result of lightening tax policy the NGOs in Hungary became more stable with more private incomes.

### **1. Economic activity and tax benefits**

In all countries the NGOs have right to be involved in economic activities, which could be defined as regular trade or business for selling goods or services. Financial sources obtained from donations, gifts, m=passive investments and irregular activity as well as fundraising are not considered as economic activity, since all above mentioned does not represent activity inspired by market principles.

In Hungary NGOs can be involved in activity focused on commercial profit. This Law determined several types of operation of organization, which is not considered as focused on commercial profit: (1) charity activity; (2) income for selling particular items, property and inventory, which is targeted to charity; (3) part of finances received from the institutions issuing securities and state bonds, in which funds necessary charity and other project needs are balanced.

Tax regulation reform of Hungary was successful, which brought significant financial stability and organizational development to the subjects of civil sector. In 90s several useful decisions were made in Hungary and all charity organizations were released from income tax for economic activity if it was not more than 10% of total income.

In Hungary, tax benefits apply only to the donations targeted to charity organizations.

### **2. Legal regulation of the volunteers' work**

Participation of volunteers in civil life processes is essential for successful functioning of civil society worldwide. The volunteers

participate in various useful projects, humanitarian actions, provide services to the poor and protect the interests of those who cannot actively participate in public life and other activities. The government and NGOs of Hungary understood the importance of volunteers in civil activities and started to elaborate joint projects for purpose of supporting the volunteers.

In 2005 the Law on volunteerism and community services was adopted in Hungary. The Law clearly defines specific nature of voluntarism, such as work in charity organization, public agencies and some private companies, which basically are focused on services in following fields: social affairs, healthcare, education, culture and protection of rights of minorities. Since in Hungary the majority of NGOs do not have the status of charity organization, this low has low coverage.

### **Direct state donation (funding)**

In cooperation between the government and NGOs, direct state funding is very important and often disputable. For this purpose the programme document was elaborated in Hungary, which provided the grounds for implementation of detailed and precise regulatory acts of the cooperation between the government and civil sector subjects. For example in 2002 the government of Hungary promised to increase financing of civil sector and establish national civil fund. During last decade direct funding of civil sector by Hungarian government compiles 42% of total income of this sector (while in 1993 the share of state donation in total income was just 16%).

State donation mechanism has three types of financing: support (subsidies and grants); order (concluding contracts for provision of services) and payment by third person (per capita financing). These resources can be allocated from the central budget (through



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parliament, ministries, lotteries, and privatization and public funds) or from local governments' budgets.

National civil fund of Hungary gives possibility to NGOs to cover their expenses and use fund resources for other basic organizational needs.

Procedural aspects of receiving public funding are subject of separate discussion and deserve important attention. In majority of the countries of Central and Eastern Europe public funding mechanism often is not transparent and public. In order to solve this problem, amendments to legislation were made in some countries, including Hungary.

### **Percentage mechanism**

At first the percentage mechanism was implemented in Hungary, where in 1996 the law on one percent was adopted. This is new mechanism for redistribution of payments, by means of which any payer can allocate certain amount from own resources in order to pay fees of any other particular organization. The original idea of the law on one percent, became the subject of sharp debates, but the law was adopted and this was expression of strong political will of coalition government of Hungary. The decision aimed at solution of two basic problems: (1) in Hungary NGOs got much less financial support from abroad, than in the countries of Central and Eastern Europe and (2) the process of reallocation of state funding between the NGOs was extremely politicized. The percentage mechanism operating in Hungary allows individual payers – natural persons – to allocate 1% out of sum designated for payment of income tax for benefit of NGO and 1% for supporting the church. In Hungary this law operates successfully until now, due to which experience of this country will be successful for many countries.

Despite of the mentioned, some experts say that this mechanism might not achieve stated goals and even if it does the level of achievement is unclear. First of all, the group of potential donors comprises just individual payers i.e. natural persons and only they can allocate 1% from income tax; and with the second mechanism it is possible to allocate just limited resources for donation (1% in Hungary), which is not big amount for NGOs and could not be more than volume of financial sources. However here is the impression that the organizations which have good relations with marketing companies will get much more financial support by means of this mechanism than other organizations. Despite of the fact that all individual payers can use this mechanism and help NGO, such action is not frequent and just 35% of individual payers use it. According to the last survey it was identified that who allocates 1% from own resources for NGO, that makes much more financial donation for benefit of the same organization.

Despite of above mentioned potentially negative trends, percentage mechanism is very useful, successful phenomenon that provides support to development of civil sector. Given mechanism ensures competition between NGOs, for purpose receiving more financial support and organizational strengthening these organizations try to improve their image and establish good relations with other economic or social subjects and so on. The mechanisms available in Hungary made interactions of NGOs with the members of society more active and wide scale.

### **National civil fund – Hungary**

This fund was established in 2003 by the government of Hungary, for purpose of providing institutional support to NGOs. The idea of the fund was development of the institute that would help NGOs in covering expanses in parallel with percentage mechanism.

Consequently, national civil fund together with functioning of percentage mechanism supports to the satisfaction of the needs of the subjects of civil sector. 60% of financial volume of this fund is used for operative expenses. Besides, part of the fund resources is used for development programmes (researches, education and international representation).

Administrative office of the fund – advisory committee consists of 17 members: (2 members form parliamentary committee for public relation, 3 representatives of the ministries and 12 representatives of civil society, among them 5 are elected from national organizations operating in different sectors and 7 are represented according to regional specifics).

In first years upon putting the fund into operation, various problems were developed; financial applications were complicated and unclear, due to which 70 – 90% of such applications were not satisfied. The government decided to establish strict monitoring on management of finances, for which adequate decisions were taken. The decisions made for monitoring of reasonable spending of finance assigned responsibility to the organizations that would receive certain finances form the fund, to spend these funds not later than one month in complacence with the goals agreed in advance.

In 2006 public audit stated that national fund of Hungary faced serious challenges, since the process of allocation, management and spending of finances had the problem of publicity. Besides, the advisory committee and the ministry did not elaborate joint strategy for development of civil sector, did not determine indicators of effectiveness and criteria for getting financial donation.

Despite the benefit got from the functioning of the fund, it had serious disadvantages. The advisory committee paid maximal attention to certain issues, while some issues were not regulated, in particular did not determine the criteria and types of the projects which would be priorities from point of view of financial support.

### **Cooperation between Hungarian government, the parliament and NGOs**

#### ***Organizational structure of provision of support to NGO and dialogue with them***

In recent years cooperation between NGOs and the government became strictly regulated on horizontal as well as on vertical of the governance. In some ministries special commissions were established for this purpose (for example in the ministry of labour and social development) which was set up by the representatives of NGOs and they work intensively on the strategies necessary for strengthening the relations.

In 1998 the department of civil relations was established under the supervision of the office of prime minister, which later was transferred to the competence of the ministry of the labour and social development. The first chairperson of this department became one of competent representatives of civil sector, after which operation of this department became more productive. The department responses to all draft laws and initiatives related to third sector, it also publishes information regarding the resources allocated by EU and observes the civil funds policy for management of these finances.

Later, special subdivision was established in the ministry of self governance and regional development, with the name – national agency for development (monitors the process of implementation of EU recommendation and plans in the country). The department of social dialogue is also functioning in Hungary, which coordinates

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and monitors participation of NGOs in realization of EU initiated draft laws.

The parliamentary committee for supporting civil organizations was functioning in 1990 – 2006. The committee used to allocate subsidies from the budget for national associations and when this function was transferred to newly established national civil fund, the committee started lawmaking in this sector. In 2006 this committee was consolidated with the committee for human rights and religious minorities.

### **The strategy of Hungarian government on civil society**

In 2002 civil relations department developed the strategy on civil society. This was the priority of new government – to establish close relations with civil society organizations. The process of elaboration of programme document was rapid, however in conditions of active participation of the society. The comments of NGOs were taken into consideration and incorporated as amendments to the final version of the document.

In 2006 the government of Hungary elaborated new strategy on partnership in this sector. However this strategy was not clear and the idea envisaged adoption of pluralistic compromising and constructive document. Consequently, each ministry was entrusted to develop own strategy. In 2007 general strategy of the government was developed in parallel with the strategies of the ministries.

### **Participation of NGOs in policy making and decision making process**

Participation of NGOs in policy and decision making process means that these organizations should have possibility to participate in the

process of discussing intellectual issues, act as consultants concerning particular issues, provide recommendations and with that support the government in adopting rational laws or political decisions.

In order to make participation of civil society more active, following mechanisms should put into operation: informing regarding the terms for starting the process and fulfilment of tasks; provision of draft laws to NGOs, for further analyses and provision of commendations concerning changes; intensification of consulting processes.

In Hungary cooperation of the government and NGOs in policy making is a bit complicated issue, because the government is not always open for such activities. It is to be mentioned that no legislative act determines participation of NGO in the process of political decision making. Such regulations are given only in sub law acts of local level.

Part 36 of the constitution of Hungary determines that the government by all means should cooperate with civil society organizations in the process of solving urgent and important issues, but nothing is said in the act about the form or standards of participation of the organizations. In 2005 Hungary made step forward towards strengthening civil participation, when adopted the law on freedom of electronic information. This law provides the NGOs with the best access on information on draft laws. Besides the law imposes the responsibility to national and local governments to publish on their web sites the information on their activities that are important and interesting for the society. This information means draft laws as well as the decisions made and future plans and concepts.

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Civil office of the parliament facilitate to participation of NGOs in political activities on parliamentary level. This office prepares “Lobbying list” of NGOs and the organizations included in the list will get information on current issues and attend their discussions in the parliament.

NGO-government partnership in Hungary is diverse, however in this case their partnership in EU integration of Hungary is important. Their partner relations are very close in the field of organization and distribution of public services, as a result of constructive dialogue they send delegated representatives to appropriate institutes of EU.

It seems that government – NGO partnership, dialogue, constructive attitude, consultations and of course real political will are important for development of civil sector. Despite of the fact that Hungary was under influence of communist nomenclature for many years, it managed to develop civil sector by means of initiatives based on rational and national goals. Democracy is unimaginable without civil society, consequently today post communist and EU integrated Hungary is really good example for any country, especially for South Caucasian states.

As mentioned above, several negative trends were seen in the process of implementation of this law or first years of operation of any department or fund, but everything was brought to optimal level. It is time for Georgian politicians, civil society and people to start action for achieving such success. In the beginning the reforms, decisions and laws might not be successful, but the progress is still possible and this is confirmed by the example of Hungary -“Who does not do anything, it does not make mistake”

Development of civil society brought positive results to Hungary and probably acted decisive role on the way to EU integration. Consequently, it will do no harm if the government of Georgia facilitates similar processes.

Georgian democracy cannot be developed just by parties and ruling political elite, third sector makes it diverse, strong, competitive and healthy.



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## **2. Economic and social reforms in Visegrad countries**

**Irakli Javakhishvili**

**Technical University of Georgia**

**4th year student, BA in International Relations**

In the last decade after the demolishment of social coalition countries of Central and Eastern Europe restored their independence and started reforms. Their main goal was integration in European Union, which should become the grounds for their stability and development. Besides it is to be mentioned that mentioned countries had to implement painful and decisive reforms in transition period, before entry in EU and after that. Check Republic, Poland, Slovakia and Hungary also went through the same way, cooperation of which is known as Visegrad Group. Besides it could be mentioned based on the experience of these countries, particular context could be developed for these countries, which move to EU integration. Caucasian states also belong to this group. Contextual review of the reforms of Visegrad group will give possibility to see similarities and identify circumstances.

Visegrad Group was established on 15 February 1991 at the meeting attended by the president of Check Republic Vaclav Havel, the president of Poland Lech Valensa and Prime Minister of Hungary Joseph Antali. The main idea of the meeting was intensification of cooperation and friendship between the countries of Central Europe. Besides, establishment of Visegrad Group was motivated by four factors:

1. Wish for eradication of remains of communist block;
2. Defeating historical contradiction between the countries of Central Europe;

3. Belief, that joint effort will facilitate to achievement of stated goals: successful completion of social transformation and European integration; and
4. Bringing together the views of political elites.

It could be said that Central European group was successful. It was very important that the minister of foreign affairs of Slovakia attended the meeting held on 16 December 1991, when three countries – Hungary, Poland and Check republic signed European agreements in Brussels.

Visegrad Four are now active in joint struggling against crises and difficult problems. It is to be mentioned that 22 years ago with establishment of Visegrad group small Central European family started its existence. Of course it is not separated from Europe, but is its essential part.

Visegrad Four established coalition of countries which are coordinated in decision making. All four states went through crisis periods of reforms. Social economic transformations were especially difficult.

Mentioned process was started in last decade of last century. For example in 1990 Poland started its transition with market economy, which was characterized by complicated macroeconomic conditions; hyper inflation, high unemployment level, great foreign debt, high intensity of black market and outdated public production sector.

System transaction process required fundamental changes in economy; main focus was on transition from planned to market economy. The changes covered the following fields:

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Business unions property structure by means of privatization;

- Abolishment of public control on foreign trade;
- Implementation of legal regulation for stimulating production development;
- Liberalization of international financial flows;
- Liberalization of prices;
- Convertibility of Polish Zloty, entire rate of exchange (2).

In the beginning of reforms the main focus was on macroeconomic sector and the decisions were made on this level. Less attention was paid to development of the institutions necessary for functioning of market economy. In fact mentioned reforms introduced extremely liberal measures (shock therapy).

Last period of 1994-1997 was characterized was characterized by a significant acceleration of economic growth and falling unemployment. The major factor of the growth was high dynamics of domestic demand,. However, in 1998-2001 GDP of Poland dropped down that was caused by the decline of investments and consumer demand.

In 2002–2004 the goal of economic policy was to turn mentioned trends and speed up economic growth. In May 2004 EU integration became significant factor that triggered economic development of Poland.

Several factors facilitated to development of Poland: in particular, private property already existed, especially in agricultural sector; for functioning of market economy basic legislation was necessary;

besides Poland already had independent judiciary system and finally existence of entrepreneurial culture was significant factor in economic transition of Poland. Polish society was rather open to outside world, then any other country in transition. As a result of mentioned reforms, Polish economy revived. By the end of 1999 GDP per capita reached 39% of average indicator of 15 EU countries.

In 1990 Czechoslovakia started its reforms. In 1990 – 1991 liberalization of prices was started, besides fiscal and monetary restrictions were implemented, which meant reduction of public spending, especially for companies on transfer fees and administrative restriction on bank loans. In the same year first stage of privatization was finished. In January 1990 Czechoslovakia started reforms of banking sector, as well as partial changes in taxing system.

In 1993 economic growth of Czechoslovakia was started. Transformation of this country as well as recession was moderate compared to other countries of region. In the beginning of 1997 economic growth slowed down and the need for stabilization measures became obvious.

Based on the experience of Czechoslovakia early rejection of third way between socialism and market economy became very important factor for the success of transformation process. Economic transiting of Check republic also demonstrates that just liberalization and stabilization are not enough form successful transformation: there is a need for implementing respective legislation and market institutions.

1992–1998 were the years of independence and transition for Slovakia. In 1993 the grounds for independent Republic of Slovakia were developed. In 1994 Czechoslovakia was divided and Check Republic and Slovakia were established. Slovakia introduced new currency and monetary connection was demolished; the expansive fiscal policy, was established as well as fixed exchange rate, foreign trade and price liberalization and high interest rate were introduced.

Besides in 1998–2002 Slovakia implemented the following reforms:

- Restoration of macroeconomic stability;
- Structuring and privatization of banking sector;
- Implementation of restricting fiscal policy measures.

2002 can be considered as the final stage of transition of Slovakia, when it fulfilled structural reforms for purpose of entry EU: social insurance, labour market, public financing; these reforms speeded up economic growth (10,4% in 2000).

In 1989–1990 political change took place in Hungary, by that time its economy was relatively liberalized. In the beginning of transition Hungary faced serious challenges: dissolution of ownership (privatization), liberalization of prices and foreign trade, control of inflation and unemployment (economic stability) and internal misbalance. In March 1995, the government instituted a decisive stabilization program, which accelerated structural reforms. This program consisted of 9% devaluation, strict wage policy, as well as a significant reduction in fiscal expenditures. These measures caused inflation fall 10-11% - up to 1999 years.

In 1995-1998, Hungary implemented a comprehensive program of corporate and banking reforms, which meant the main benefits of privatization and restructuring and privatization of all major banks.

In 1997 export led economic recovery, which has become the engine of growth in Hungary.

Since 1990s - the Hungarian experience proves that openness to foreign capital is a prerequisite for success. Hungary's successful reintegration into the international markets demonstrates the speed up the modernization of foreign investment.

Visegrad region has successfully joined the EU in 2004.

Visegrad Group upon its establishment existed in Central Europe, the stability of the new system is constructed idea, which is reflected in the "Declaration on Cooperation between Czech and Slovak Federal Republic, the Polish Republic and the Republic of Hungary for the rapid integration to European Union", known as the Visegrad Declaration, signed in 1991, February 15 (4).

Visegrad Group countries also focus on social reforms. In this regard, it is important to reform the pension system, health care, social security and family policy. For example, unlike other countries, the Czech Republic has not received any pension reform, as the consensus among politicians. The pension system is the so-called classical pay-as-you-go system. Pensioners have the opportunity to collect a certain amount of private pension funds.

Currently, in Czech Republic, 10 million people get the state pension costs and 28% of state costs are used for the national pension plan. The economists consider that pension system in this country is unsustainable and that there is a need for reform

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becomes. Since 2010, the first steps have been made towards the implementation of the pension reform - for people born after 1968, retirement age increased to 65 years (5).

In recent years Czech Republic introduced new measures related to social security. Since this country joined European Union, it adopted many laws on responsibility of the persons. For example, the Czech Republic adopted a new social security law and the lack of material resources, as well as some measures on pension insurance and employment policies.

By the year 2004, the Polish population was more than 38 million, which shows that the country is on the 8th place in Europe in terms of population. However, after the 2010 estimates, the number of people in the productive age decreases. By 2020 it will be 25.1 million people (6). Main characteristics of Polish labour market are high level of employment in the agricultural sector (which will be discussed later).

Aging of population is on going in Slovakia. Due to negative demographic trend of population aging as well as for sustainability of the social system, second government of the prime minister Dzurindas (2003-2004 yy), added second private sector to the social insurance system. This is individual savings project that fills a pay-as-you-go-system, it was compulsory for young people. - One of the arguments for its introduction was that this system will better reflect the level of merits and savings of individuals. However, the next government (Fiko, 2006-2010), was against this system, and said that it was a threat for savers' money. In fact, the government was calling for the return to the public system. As for private companies, which were managed by individual savings funds, they argued that government intervention was destabilizing the system.

Generally, the political parties in Slovakia have no desire to return to the old system. Discussions continue about social insurance, which is linked to individual accounts.

The differences between the Visegrad Four and the "old" members were important. These countries got financial assistance from the EU funds before becoming its members. These funds should be spent for 2004 – 2006 programme period; later in 2007 – 2013 Visegrad countries received great part of cohesion funds. Four countries got the grant in amount of 140 billions: Poland – 67 billions, Hungary 34,5 billions, Check Republic 26,7 billion and Slovakia 11,4 billion. This “gift” made significant impact on development of these countries.

Check Republic together with accession of new policy objectives, actively addresses the cohesion policies in order to cope with the many new challenges, such as climate change, global competition, migration, demographic changes, but also connecting the whole policy with Europe 2020 strategy, the Czech government underlines, that this policy is able to support these goals, but the main goal should remain the same: to improve the economic and social cohesion.

As for the Hungarian example, regional development policy of this country demonstrates discrepancy with regional cohesion. In Hungary in parallel with market economy serious differences emerged among the regions. The differences by regions are of five levels:

- Between Budapest and regions



- On regional level between developed North – West and developing South – East;
- On small zones level where differences are defined by the combination of industry, agriculture, services and geographic capacities
- On society level between the city and agglomerations
- Between the border and internal regions

For instance, - the over development of the capital city is one of the main problems of Hungarian regional development policy -,as well as of other Visegrad countries. Budapest is the only part of Hungary where GDP is above the EU average level of 75%.

Similarly, in Poland's regional policy the major problem is inequality between the rich and the poor in rural areas – basic wealth is concentrated in the cities, such as Warsaw, Katowice, Wroclaw and Poznan, with large human and economic potential.

In 2007-2013 program period, Slovakia received large amount of money. The government decided to distribute the 11.4 billion dollar financial package for 11 programs - including the employment and social inclusion, regional action program for transport, health, science and research, education and information society.

With respect to the EU funds - the main problem is corruption and bureaucracy. Some politicians and entrepreneurs were doing business with these funds and they used them for own benefit and for their friends, which ignored the main goal – regional inequality balance and improvement of regional economic conditions. Improve.

In social policy Visegrad Group the forefront is the health issue. It should be noted that health care costs are lower in these countries

than in the EU. Health care reforms are targeted to limit the search of healthcare by introducing taxes (Slovakia and Czech Republic), the privatization of health care on increased efficiency of health care providers and health insurance and the growth of new control on enhancement of security.

Czech health care services are based on the state insurance system. According to the constitution of this country, basic health services must be "free and universally available". However, certain elements of the health care system have been introduced, which changes in patients' behaviour and limit their wasting action. In January 2008, the right-wing - centrist government introduced a symbolic "regulation." For example, visiting a doctor could cost 1.15 Euros, and 3.46 - the emergency services. When this constraint is violated, insurer companies are obliged to return the overpaid money to clients. In addition, there is now the Czech Republic there is an independent agency that is responsible for all pricing regulations.

Hungary also showed progress in some areas. For example, Hungary is one of the first European state, which developed a vaccine against the H1N1 virus. The government and the political opposition were declaring that the new pandemic vaccine is in line with the objective of deterrence of pandemic.

As for Poland, where the health policy has four major goals: to increase of the public health security, improvement of the health systems performance, adjusting health care to long-term demographic trends and reduction of shortcomings between Poland and the European Union. However, there are problems, such as the Polish patients wait longer to go to a specialist, lack of access to new medicines, low wages of the health sector physicians, and so on.

In 2002 – 2006 in Slovakia the government implemented market elements in healthcare system, among them privatization of healthcare insurer companies and introduction of 0,66 Euros fee for the ambulance service. However, Fiko government (since 2006), abolished the unpopular tax.

In Slovakia health care system compiles 6% of the total GDP, which is lower than European average (8%) (10). The private health insurance is less common in the country.

In addition, the Slovak government has implemented different measures:

However, in Slovakia there are similar problems in other Visegrad countries, for example, low wages of health care professionals, high turnover of newly educated physicians to the West, etc. The overall situation shows that these countries are still in the stage of reform, and are behind Western European countries.

Like in other fields, after 40 years of communism, the educational systems of the Visegrad Group countries lag far behind the West. Currently, the state education ministers decided to learn more about each other and took new steps towards the reform.

In November of the last year, the Education Ministers of the Visegrad countries formed a working group consisting of representatives of the ministries and academies. Its main objective is to increase public confidence in the entire region, as well as establishing trust to individual universities. This group takes certain

measures based on national goals, education laws, as well as the EU and the Bologna Process directives.

Reforms in the educational system in this group of countries, mainly mean identification of the quality of standards and professionalization of accreditation agencies, transparent access to information and the introduction of working groups for implementation of the reforms.

One of the main objectives of EU is the plan of Europe for 2020. The goal of which is 40 percent increase of the number of young people who have some type of secondary education by 2020 (11). Poland and Hungary have recently made major changes in higher education systems.

For example, Poland has introduced a new system of institutional accreditation, and Hungary was focused on research universities. The Czech Republic and Slovakia are working on new legislation on higher education, which should be the opportunity to improve their education systems.

The agriculture is the constituent element of reforms structure. In this regard, common agricultural policy (CAP ) is particularly important, which is an integrated part of EU policy. It is based on the agricultural subsidies and programs.

According to the Statistical Service of the Czech Republic, Czech Republic is one of the countries which has largest share of agriculture of GDP the largest share of the economy. In this regard, the share of Czech Republic is 2-3%.

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After entering the European Union, the Czech Republic, together with the other countries of Central and Eastern Europe, received a simplified version of the CAP-aid project (Single Area Payment Project). According to this project, in 2009 the Ministry of Agriculture took into account the requirements and introduced "good" agricultural and environmental conditions that are suitable for the farmers and the supervisory authorities.

Rural development policy was implemented in 2007–2013 in Check Republic, by means of rural development programme. Its goals are in line with national and EU policy documents. Main lines of this policy are: improving competitiveness of agricultural and forestry sectors and the food industry, improving the environment and rural areas, raising living standards and encouraging diversification of the rural economy and cooperation of village actors in leaders' initiative.

Hungary is strong supporter of classic direct taxes, dairy quotes and intervention mechanisms, since without these practical measures its agriculture would be much smaller or even absorbed in global competition. At the national level, Hungary farming protection is the mostly supported sector.

Besides Hungary has active role in struggling against reduction of rural subsidies. While France and Germany were against, final decision was 10% reduction instead of the planned 13%.

Besides, while only 3% of Hungarians are working in the agricultural sector, the new Conservative government wants to turn the strategic sectors of agriculture. This plan includes the creation of a new million jobs.

Agriculture is one of the largest sectors of Poland, in which about 15% of the country's labour force is employed, although its share in GDP is only 3%.

Poland is implementing the 2007-2013 rural development program with total budget in amount 17 billion Euros. This program is based on the multi-functionality of agriculture and rural areas. Its main objectives are: strengthening economic competitiveness agricultural holdings and agro - food sector, promotion of land management and environmental protection, improving living standards and diversification of agricultural economy.

As for Slovakia, the country's agricultural sector faced a number of challenges since 1989. Production was decreased by 30% due to lower demand and higher imports between 1990 and 1997. One of the major changes was that the former agricultural cooperatives and state-owned companies were transferred into private business companies and co - partner cooperatives.

According to the Slovak Ministry of Agriculture, main strategic objectives of the 2004-2013 is protection of agricultural production, production of competitive products, and more efficient use protection, and constant reproduction of natural resources. As for the rural development program, it is mainly focused on the modernization of farming, forestry increase the economic value of the non - agricultural activities, diversify, invest in spare time and hospital facilities, the promotion of rural tourism and rural revitalization and development of social infrastructure and services.

It is evident that agricultural sector in the Visegrad countries is immature compared to Western European countries, however, the

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reform and programming process is underway and brings the desired results. This is a very good precedent for those countries who still have to go through this way. It can be said that the former communist states, which are members of the European Union, are now helping the former Soviet republics to come closer to the European Union.

Last year, at a meeting in Prague Visegrad Four representatives approved the new rules, which will help the "Visegrad Four Eastern Partnership" program to start running. This new initiative is based on the decision made in Bratislava in June by Visegrad countries and means provision of support to political and economic reforms of the countries involved in EU Eastern partnership program. Armenia, Azerbaijan, Belarus, Moldova and Ukraine participate in the programme.

The new initiative provides grants to projects to encourage the reforms, as well as students scholarships. The goal of Eastern Partnership initiative is the promotion to the strengthening of political and economic links between the countries participating in Eastern Partnership. The initiative was welcomed by EU Commissioner Stefan Fule, saying that experience of the collapse of communism in the Visegrad Four countries, could significantly help the former Soviet republics in development of their own laws and in conformity with the objectives of the European Union in the process.

Thus, the Visegrad Group's experience in economic and social reforms develops the useful practice of creating positive and useful practice, considering of which could be advantageous for the South Caucasus states. Poland, Czech Republic, Hungary and Slovakia went through a very difficult way from the period of independence, it could be said that their effort was successful. EU integration of

the member states could be identified as key indicator of socio economic success of Visegrad Group.

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CAUCASIAN INSTITUTE  
FOR ECONOMIC AND SOCIAL RESEARCH

**Caucasian Institute for Economic and Social Research (CIESR)**

Address: 0179, Tbilisi, Georgia, Abashidze Str. 43/15

Tel/Fax: (+995 32) 272 90 21;

E-mail: [info@ciesr.org](mailto:info@ciesr.org) Web: <http://www.ciesr.org>

Contact Person: Temur Tordinava, Executive Director