

Contains Procurement Related Confidential Information

Minutes No. 36

**MCA-Armenia Governing Council Session
16:00, December 10, 2008
GoA Conference Room**

The session was chaired by H.E. Tigran Sargsyan, The Prime Minister of the Republic of Armenia and the Chairman of the MCA-Armenia Governing Council.

In attendance of:

Members of Governing Council:

Armen Gevorgyan	Deputy Prime Minister, Minister of Territorial Administration
Aramayis Grigoryan	RA Minister of Agriculture
Tigran Davtyan	RA Minister of Finance
Ara Petrosyan	Deputy Minister of Economy
Hrant Beglaryan	Deputy Minister of Transport and Communication
Karen Zadoyan	Chairman of "Armenian Young Lawyers Association" NGO
Norayr Danielyan	Authorized representative of Victor Yengibaryan, Chairman of "European Movement of Armenia" NGO
Arman Voskanyan	Representative of "Development of Tavush" NGO
Shirak Mikayelyan	Authorized representative of "Work and Motherland" NGO
Poghos Shahinyan	Chairman of National Road Safety Council" NGO

GC observers:

Alex Russin	GC Observer, MCC Resident Country Director
Karine Danielyan	Environmental observer of Millennium Challenge Account-Armenia SNCO, President of "Association for Sustainable Human Development" NGO

In absence of:

Vahram Nercissyantz	Deputy Chairman of the MCA-Armenia Governing Council, Chief Economic Advisor to President of Armenia
Nerces Yeritsyan	RA Minister of Economy
Gurgen Sargsyan	RA Minister of Transport and Communication
Victor Yengibaryan	Chairman of "European Movement of Armenia" NGO

Invitees:

Andranik Andreasyan	Chairman of the State Water Committee of the Ministry of Territorial Administration
David Sargsyan	Chief of RA Government Staff

Participants:

Ara Hovsepyan	CEO, MCA-Armenia SNCO
Nora Martirosyan	Legal Counsel/GC Secretary, MCA-Armenia SNCO
Tigran Kalantaryan	Irrigated Agriculture Project Officer, MCA-Armenia SNCO
Aram Gharibyan	Advisor to RA Prime Minister
Mery Harutyunyan	Head of Public Relations Department of the Staff of RA Government
Simon Ghonaghchyan	Head of Economic Department, Government Staff
Hovhannes Sahakyan	Deputy Head of Economic Department, Government Staff
Tigranuhi Baghdasaryan	Interpreter

The meeting was opened by Mr. Tigran Sargsyan, the Prime Minister of the Republic of Armenia and the Chairman of the MCA-Armenia Governing Council.

The Agenda was approved as follows:

1. Discussion and approval of the Disbursement Request – X, to be submitted to the MCC, and the below mentioned documents:
 - a/ The Disbursement Request (DR) and the Quarterly Financial Report (QFR)
 - b/ The Conditions Precedent (CP) report
 - c/ The Multi-year workplan
 - d/ The Narrative Report and Indicators Tracking Table

e/ The Procurement Performance Report and Procurement Plan
f/ Annual Supplemental Report.

2. Discussion and approval of the Draft Contract for Rehabilitation of 6 Main Canals (Package 1) under Infrastructure Activity of the Irrigated Agriculture Project of the Millennium Challenge Account – Armenia Program.
3. Presentation of information on the main objectives of the second phase of the Credit Component and discussion and approval of Administration and Procedures Guidelines under Water-to-Market Activity of the Irrigated Agriculture Project of the Millennium Challenge Account –Armenia Program.
4. Other issues:
 - a) Discussion of an issue on tax privileges on social security payments to “VISTAA PLUS” Ltd. as an Employer within the frames of the MCA-Armenia Program.
 - b) Discussion of information on approaches for applying tertiary and main canals construction technologies;
 - c) Submission of information on audit and other inspections of programmatic and financial activities of the MCA-Armenia SNCO.

Attached to the Agenda, the members of the MCA-Armenia Governing Council were presented with corresponding references for each Agenda item.

The Agenda was approved unanimously.

Agenda item 1 was presented by Ara Hovsepyan, Chief Executive Officer of the MCA-Armenia SNCO.

Ara Hovsepyan informed that according to Disbursement Request it is planned to receive USD 6,811,305 for time period from January to March. As of the last day of current quarter, total amount of actual and forecasted expenses (December) is USD 28,081,321.

Ara Hovsepyan also informed that during the time period since the previous Disbursement Request two more conditions precedent have been satisfied:

- “The Government developed and adopted legislation and/or regulations, or amended existing legislation and regulations, to facilitate the establishment of agricultural cooperatives” and
- “The Government developed and adopted legislation and/or regulations to improve statistics on agriculture, including an accounting of the sector and data collection”.

At the same time it was mentioned that the following condition precedent under the Water-to-Market Activity was not satisfied: “M&E indicator ‘Recovery of WUA operations and maintenance costs by water user charges’ achieves targets”. It is proposed to ask deferral from MCC for fulfillment the condition precedent.

Ara Hovsepyan mentioned that according to Compact, recovery rate of WUAs for year 2008 is 55% and in accordance with GoA Decree on the Approval of Main Principles of WUA State Financial Support Reforms and Norms of Supplied Irrigation Water Losses, recovery rate is equal to 52.5%.

Based on unofficial data available at MCA-Armenia SNCO (there is still no reply to the official letter from the State Water Committee of RA Ministry of Territorial Administration) 2007 actual recovery rate is 36.6%, which doubts fulfillment of the indicator, set for year 2008.

RA Prime Minister Tigran Sargsyan asked Andranik Andreasyan to clarify whether the indicator is satisfied or no and if the indicator is not satisfied, which are the reasons of that.

Andranik Andreasyan clarified that the indicator is not satisfied, however it has been already agreed with MCC to review and set most realistic indicators. There are objective reasons why the given condition precedent is not satisfied. The revision will be carried out within coming three months and a new more realistic approach will be presented.

RA Prime Minister Tigran Sargsyan asked to explain what was wrong in previous forecasts.

Andranik Andreasyan informed that it was forecasted that the costs will decrease and the income will increase. Presently collection rate has increased, however the costs have not reduced. Even more there is an issue in reducing the costs, since the part of the activities foreseen has not been carried out, i.e. the scope of civil works of the MCA-Armenia Program has significantly reduced. Besides, there are also other objective reasons: income and collection rate have increased, but rate of actually used water reduced and besides, lower tariffs were applied instead of the forecasted ones.

RA Prime Minister agreed to the mentioned three reasons.

Aram Gharibyan asked to clarify the reason why in 2006-2007 cost of water in at least 10 WUAs was 9-11 drams, whereas in 2008 there is only one WUA, where the cost of water has not increased.

Andranik Andreasyan informed that there are different reasons, i.e. inflation.

RA Prime Minister Tigran Sargsyan stated that the given condition precedent was not met and it is necessary to conduct internal discussions to solve the issue.

Armen Gevorgyan mentioned that it is necessary to be impartial. During the recent discussion about 7 villages it was cleared out that the villagers pay only 10% of the water used. They justify it by the soil erosion, which causes piping effect and major part of water to be used is lost. However it is evident that there is no culture in the Republic of Armenia to pay for the irrigation water used. Up to present the policy of the Government on that issue was quite, but starting from next year it will be stricter.

Karine Danielyan mentioned that when there were disputes on Sevan outlet, RA Government explained it with drought and stated that there is a demand of irrigation water and as a result of providing irrigation water, corresponding funds will be transferred to RA state budget.

Armen Gevorgyan assured that, as against the previous year, additional amount equal to USD 2 mln was transferred to the state budget.

Ara Hovsepyan informed that the following two approaches are being discussed with MCC regarding the mentioned condition precedent: either to review the condition precedent to reflect the real situation or to change the indicator and set the collection rate as an indicator.

Armen Gevorgyan mentioned that presently the issue of changing subsidizing policy and transition to addressed subsidizing is in the process of discussion. Terms of Reference is in the stage of preparation, however there are concerns, since this issue is directly related with MCA-Armenia Program and can have impact on the latter. In particular, MCA-Armenia specialists consider this concept untimely. At the same time Armen Gevorgyan added that he considers necessary that MCA-Armenia consultant should study and submit his view point on the concept.

Ara Hovsepyan mentioned that MCA-Armenia SNCO specialists and consultants discussed the draft concept at the meeting with Aram Gharibyan, Advisor to RA Prime Minister and Samvel Avetisyan, First Deputy Minister of Agriculture. It was mentioned during discussions that in the result of implementation of provisions, presented in the concept, change of policy will have a direct impact on financial stability of WUA's and correspondingly on recovery level.

Taking into account that MCA-Armenia considers reasonable to start changing subsidizing system after implementation of a number of activities, i.e. carry out comprehensive, independent expertise analysis of budgets of all subsidized WUAs, specify land areas, irrigated by WUAs, the volume of water supplied and strengthen the role of water users in management and supervision functions of WUA's.

Armen Gevorgyan asked whether the Consultant proposed development program of WUAs or no.

Andranik Andreasyan mentioned that it was within the Terms of Reference of the Consultant. Presently the Consultant proposes to provide in-depth support to improve management of 2 water supply agencies and 8 WUAs within the frames of selected main canals, as well as to apply to the remaining 44 WUAs the approach, stated in management improvement plans.

Armen Gevorgyan was interested to know when the results will be available.

Ara Hovsepyan clarified that management improvement plan for pilot project will be prepared by May, 2009 and if the results are positive, the plan will be applied to other WUAs as well.

Aram Gharibyan informed that addressed subsidizing does not mean weakening of WUAs. In this case participatory management and institutional strengthening of WUAs will still remain a continuous process. Besides, the World Bank expressed an opinion that state subsidies do not support WUAs and addressed subsidizing creates serious prerequisites for establishment and development of WUAs.

After discussions **it was unanimously decided** to approve Disbursement Request – X and documents, attached to it.

Agenda item 2 was presented by Ara Hovsepyan, Chief Executive Officer of the MCA-Armenia SNCO.

Andranik Andreasyan mentioned that it is the first high volume civil works contract in irrigation sphere of the MCA-Armenia Program and it is necessary to start the works as early as possible.

Ara Hovsepyan informed that the contract will be signed and the works will commence within the coming week.

After clarifications **it was unanimously decided** to take as a basis the draft Contract and approve signing of Contract with SADE (France) jointly with ShMSh-23 OJSC.

Agenda item 3 was presented by Ara Hovsepyan, Chief Executive Officer of the MCA-Armenia SNCO.

RA Prime Minister Tigran Sargsyan informed that 50 mln. USD has been already provided by commercial banks, additional 50 mln. USD is planned to be allocated to credit sphere and the World Bank is also planning to provide additional 250 mln. USD for the same purpose, therefore the amount, equal to 7 mln. USD within the frames of the MCA-Armenia Program is not a significant amount for the sphere and it is more reasonable to use the funds for development of other spheres.

Ara Hovsepyan informed that MCA-Armenia conducted a study and presented brief information about credit component and the role of the latter in credit sphere. According to that study, as of November 2008 only 7% of credits, provided by 22 commercial banks and only 15%, provided by 23 universal credit organizations are directed to agriculture sphere.

Arman Voskanyan informed that this issue has been discussed at MCA-Armenia SC recent session and although SC has not carried out serious studies, anyway they approved further implementation of credit component, since the given credits have low interest rates and they are logical order of Water-to-Market Activity. And moreover, in the second stage it is proposed to focus on a quality of services provided rather than on interest rates. Arman Voskanyan repeated again his suggestion on providing the funds in grant form hence excluding participation of banks and credit organizations.

RA Prime Minister proposed to provide money to Development National Center for Small and Medium Enterprises (SME DNC) if it is possible to provide credits this way within the frames of the MCA-Armenia Program.

Tigran Davtyan mentioned that he considers necessary to use money for increase of capital rather than on capacity building.

Ara Hovsepyan informed that MCA-Armenia SNCO has not studied this way of providing credits.

RA Prime Minister proposed to assign MCA-Armenia SNCO to clarify whether it is possible to allocate the amount to SME DNC.

Ara Hovsepyan informed that in general MCC is impartial regarding credits, since this money is considered to be RA grant resources. However, MCC position is that in case of any decision, even alternative, the objectives of Water-to-Market Activity should be followed and the program should try to avoid negative impact. At the same time MCA-Armenia is proposing increase of

scope of works of tertiary canals rehabilitation project, as an alternative. A separate Reference is presented to GC members.

Karen Zadoyan mentioned that as SC members they are assigned either to vote pro to the continuation of credit component or postpone the approval to the next GC session. He proposed to continue the discussion after having received the results of corresponding study.

RA Prime Minister Tigran Sargsyan suggested voting pro for the continuation of credit component through SME DNC.

Ara Hovsepyan proposed MCA-Armenia SNCO to review and submit a reference at the next session on whether it is possible and if yes, so how it will be possible to provide credits through SME DNC.

RA Prime Minister recommended discussing the issue with Nerces Yeritsyan, RA Minister of Economy and proposing joint solution.

After discussions **it was unanimously decided** to study the possibility of implementing second stage of credit component through SME DNC and assign MCA-Armenia SNCO jointly with RA Ministry of Economy to discuss and submit to RA Prime Minister within 1 week period possible mechanisms of implementation of the latter.

Agenda item 4 a) was presented by Ara Hovsepyan, Chief Executive Officer of the MCA-Armenia SNCO.

It was unanimously decided to assign MCA-Armenia SNCO jointly with RA Ministry of Finance to study the issue of applying tax privileges on social security payments and give positive solution to the issue, if possible.

Agenda item 4 b) was presented by Ara Hovsepyan, Chief Executive Officer of the MCA-Armenia SNCO.

Ara Hovsepyan informed that in the stage of discussing the preliminary designs, technical solutions, proposed by design company aroused disagreement of expert of “Jacobs” (Great Britain), MCC Technical Consultant. The issue is described in the Reference attached.

RA Prime Minister Tigran Sargsyan mentioned that local specialists insist that it is necessary to carry out fundamental repair, whereas American colleagues state that it is extremely expensive and is not financially justified.

Aramais Grigoryan mentioned that local experts are right, because the result will be long term, whereas in opposite case the whole irrigation system will be destroyed again in a couple of years.

Ara Hovsepyan added that 15% co-financing is expected from communities for the rehabilitation of tertiary canals. Each of the communities knows exactly which section they want to repair and concrete. As a rule, it is the intake structure, but MCC specialists insist that it will not solve irrigation problem in lower part of the canal and the technologies that they propose are more affordable and they will allow repairing more canals and assuring entire irrigation. Presently MCA-Armenia SNCO will start the implementation of first pilot project on six main canals and will apply the proposed new technologies.

RA Prime Minister was interested to know when the results of pilot project will be available.

Tigran Kalantaryan informed that actually the canal should be operated for one season in order to see the results, however in this case the main objective of MCC is to figure out whether these technologies area applicable in local conditions or no.

RA Prime Minister Tigran Sargsyan proposed that local and American specialists to participate at the next GC session and present their view points and justifications.

After discussions **it was unanimously decided** to assign MCA-Armenia SNCO to present to Governing Council on periodic basis information on process and results of civil works.

Agenda item 4 c) was presented by Ara Hovsepyan, Chief Executive Officer of the MCA-Armenia SNCO.

RA Prime Minister recommended that SC members get familiar with the Reference presented and discuss it with MCA-Armenia SNCO in case of necessity.

After discussions **it was unanimously decided** to take into account the information presented.

After expiring the agenda items, the meeting was adjourned.

MCA-ARMANIA GOVERNING COUNCIL CHAIRMAN,

RA PRIME MINISTER

T. SARGSYAN

The minutes were taken by:

Nora Martirosyan

Legal Counsel/GC Secretary,

MCA-Armenia SNCO