

**UNITED NATIONS CONFERENCE ON  
TRADE AND DEVELOPMENT**

**VOLUNTARY PEER REVIEW OF COMPETITION POLICY:  
ARMENIA**

**Full Text**



**UNITED NATIONS**

## NOTE

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## **Acknowledgement**

UNCTAD's voluntary peer reviews of competition law and policies are conducted at the annual meetings of the Intergovernmental Group of Experts on Competition Law and Policy or at the five-yearly United Nations Conferences to Review the UN Set of Principles and Rules on Competition. The substantive preparation is carried out by UNCTAD's Competition and Consumer Policies Branch (CCPB) under the direction of Hassan Qaqaya, Head of CCPB.

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## PREFACE

1. This report examines Armenia's competition policy system (ACPS). The report is based upon a review of the legal texts that supply the framework for the ACPS (statutes, implementing regulations, and guidelines)<sup>1</sup> and of decisions issued by the State Commission for Protection of Economic Competition (SCPEC);<sup>2</sup> study of other reports dealing with the ACPS;<sup>3</sup> interviews with SCPEC leadership and staff, donor organizations, officials from other government authorities, academics, and representatives of nongovernment organizations such as business associations and consumer groups).

2. The report first describes key elements of the foundations and history of competition policy in Armenia. It highlights features of the larger political economy that shape the competitive environment and require careful attention in the reform and future development of Armenia's competition policy system. Part 2 provides recommendations concerning possible reforms to the competition law. This section shows amendments to the existing law could facilitate improvements in SCPEC's enforcement program and in the application of the agency's other policymaking tools. Part 3 reviews adjustments to the institutional framework through which competition policy is formed and implemented in Armenia.

3. For the most part, the report's recommendations do not require changes to the competition law itself. Many proposed measures lend themselves to implementation by SCPEC or other government and non-government institutions. Some proposals, such as enhancements to salaries and other SCPEC resources, as well as strengthened investigatory powers require legislative action.

4. In assisting with the preparation of the report, SCPEC demonstrated an admirable willingness to invite critical inquiry concerning the ACPS. SCPEC viewed the examination process as an opportunity to strengthen the ACPS and mobilize support for needed reforms. In its openness to evaluation and suggestions for improvement, SCPEC has embraced high standards of public administration.

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<sup>1</sup> See, e.g., The Law of the Republic of Armenia on Protection of Economic Competition (enacted by the National Assembly of Armenia on November 6, 2000 and signed into law by the President of Armenia on December 5, 2000; last amended in 2008).

<sup>2</sup> See, e.g., State Commission for the Protection of Economic Competition of the Republic of Armenia, "On Imposing Sanction Against 'Armentel,' Closed Joint Stock Company" (Decision No. 79-A; July 30, 2008); State Commission for the Protection of Economic Competition of the Republic of Armenia, "On Results of Study of Prices Set by a Number of Economic Entities Operating on 'Hen Shelled Egg' Product Market and Imposing Sanctions Upon these Economic Entities" (Decision No. 05-A; April 11, 2007); see also State Commission for Protection of Economic Competition of the Republic of Armenia, Report on 2006 Annual Activity Program of the SCPEC (2007) (reviewing SCPEC activities, including decisions taken on individual cases).

<sup>3</sup> See, e.g., S.J. Reynolds, "Competition Law and Policy in Armenia: Priorities for Improvement" (2009); Eberhard Feess & Martin Mittermeier, "Consulting of the State Commission for Protection of Economic Competition (SCPEC), Armenia" (July 2009).

## 1. FOUNDATIONS AND HISTORY OF COMPETITION POLICY

### 1.1 Introduction: Armenia's Competition System in Context

5. Armenia's experience with competition law is one element of a remarkable modern global development in regulatory policy. Armenia adopted a competition law regime in 2000. Thus, it belongs to the group of approximately 110 jurisdictions that have enacted competition laws and is one of roughly 80 nations that have created their competition systems since 1980. Placed in historical context, the ACPS came into being at an important period of competition policy reform. It is one of several systems that were created anew (e.g., Indonesia's competition system) or were substantially reconfigured (e.g., South Africa's competition system) at the very end of the 1990s and the very beginning of the first decade of this century. Members of this chronological cohort might be considered to be second generation transition economy competition systems following the experience of systems established in the late 1980s and early 1990s (e.g., Mexico and Poland). As such, the design of the ACPS reflects two formative influences. Most important, it borrows heavily from the framework of the competition regime of the European Union (EU). The influence of EU institutional arrangements and doctrinal approaches likely will persist, as the Partnership and Cooperation Agreement between the EU and the Republic of Armenia will, among other forces, tend to press the ACPS toward convergence with the EU. Secondly, important elements of the ACPS are drawn from the competition systems of the former Soviet Republics, some of whose antitrust regimes were established in the early to mid-1990s (e.g., Russia and Ukraine). The most notable element adopted from the CIS experience is the register for dominant companies.

6. By what criteria should one assess Armenia's progress toward the establishment of an effective competition policy regime?

7. As a matter of principle, UNCTAD's voluntary peer reviews of competition law and policy are grounded in and bound by the United Nations Set of Principles and Rules on Competition. Within the boundaries of the set, one way to answer the above-mentioned question is to define the characteristics of an effective, successful competition regime – especially for a system that, like Armenia's, is barely a decade old. This approach has three basic dimensions. The first is the demonstrated capacity of the competition system to achieve the substantive policy results whose attainment animated the enactment of the competition law. In virtually all competition systems, old and new, the original legislation attempts to realize multiple, diverse objectives. These include improvements in economic performance (i.e., greater efficiency, productivity, innovation, and cost reduction), the prevention of inequitable wealth transfers from consumers to producers, the preservation of opportunities to compete among small and medium sized enterprises, and enhancements in the condition of groups suffering from longstanding economic disadvantage.

8. In some applications of competition law, a specific initiative may promote the attainment of all these goals. In other areas, tensions may arise among the goals. Each jurisdiction determines what balance among multiple aims is suitable. In many nations with older systems, significant adjustments take place over time in the emphasis given to each goal. Whatever the precise balance struck in any single jurisdiction at any point in the life cycle of a competition system, a paramount measure of a competition system's proficiency is its capacity to improve, in some observable sense, the quality of economic performance. One can put the point in terms of several basic questions: How has the operation of the competition system affected key measures of economic performance? Has competition policy spurred innovation? Increased the pressure upon producers to reduce costs or otherwise improve productivity and efficiency? Inspired suppliers to reduce the prices offered to consumers or to provide a variety of products that better satisfies consumer tastes?

9. It is not easy for any competition agency to provide confident answers to these questions. The impact of a competition policy program upon economic performance can be difficult – indeed, sometimes impossible -- to measure. Some valuable benefits of a competition policy program are likely to defy convincing measurement, but their imperviousness to quantification does not deny their importance. For example, there may be no convincing qualitative or quantitative metric to measure the contributions of a competition policy system to the larger social acceptance of the value of market-based processes and to the gains in perceived social legitimacy for market processes that the establishment of an effective competition system can yield by providing assurance that business enterprises will strive to serve consumer interests. The presence of an effective competition policy mechanism may be essential to a jurisdiction's decision in the first place to switch from central planning and public ownership toward reliance on markets to organize the economy and to sustain this commitment amid periodic economic upheavals that occur in every jurisdiction.

10. At the same time, in most jurisdictions a crucial test – maybe the most salient practical measure -- of a competition system's value is its contribution to superior economic performance. At a basic level, individual citizens (and the public officials they elect to represent them) are likely to ask: has this system improved the lot of consumers? One important way to judge the quality of a competition regime is the intensity of its efforts to ask, on a recurring basis, how its actions improve economic performance and how adjustments in the mix of current programs can yield a still better return to the resources society has entrusted to it. Given difficulties in directly measuring consequences, the best that an agency can do in most circumstances is to ask, based on existing theory and past experience, which allocation of resources is most likely to improve economic performance.

11. A second way to assess the quality of a competition system is to examine its success in establishing an administrative infrastructure and operational techniques that tend over time to improve the system's ability to deliver good substantive results. The notion here is that in competition law, as in many other areas of human endeavour, good technique begets good results. In the specific case of Armenia, one can ask whether the competition system is progressing in the sense of building a sound organizational structure for the competition agency, creating procedures that ensure fair, honest, and accountable decisions, assigning it the powers (e.g., to obtain information and to punish offenders) required to perform its substantive mandate, acquiring and preserving a strong base of human capital and institutional knowledge, engaging effectively with collateral public institutions (e.g., sector regulators, legislators, and the courts) whose decisions also influence the level of competition in a jurisdiction, and enlisting contributions from non-government institutions (e.g., consumer groups and business associations) whose activities can enhance the implementation of a competition policy program.

12. A third measure is to ask how well Armenia is doing within a peer group that consists of competition systems that are ten years old or less. A comparative perspective recognizes that the establishment of a successful competition system, especially in a jurisdiction that is moving from reliance on central planning and public ownership toward market-based processes, is likely to be a relatively slow, cumulative growth. Many the jurisdictions with older competition systems that are considered to be the successful – including Canada, the European Union, and the United States – struggled in their first decades to gain a basic level of effectiveness.<sup>4</sup> It is unrealistic to expect

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<sup>4</sup> See, e.g., Marc Winerman & William E. Kovacic, *Outpost Years for a Start-Up Agency: The FTC from 1921-25*, *Antitrust Law Journal* (Forthcoming 2010) (discussing difficulties encountered by U.S. Federal Trade Commission in its first decade of operations).

that a new system created in an environment featuring unfavourable initial conditions will attain a faster rate of successful implementation than jurisdictions that created their competition systems in environments that featured, among other enabling conditions, a sound judiciary and a longstanding commitment to reliance on markets to organize economic activity. New competition policy systems can benefit from a “last mover advantage” by examining the history of other jurisdictions and adopting approaches that seem, in light of experience, to yield the best results.<sup>5</sup> Even with this possibility for accelerated implementation and progress, new systems inevitably must confront and surmount serious obstacles to effective implementation that encumber all systems.

13. External observers who make normative judgments about the quality of a new competition system must take this circumstance into account. To some degree, the grading of a competition system that takes place in the context of a peer review has both relative and absolute elements. In relative terms, the question is whether Armenia’s system is progressing in comparison to other jurisdictions within its chronological peer group – systems created within the last ten years and, more specifically, systems created with economies previously predominated by central planning and public ownership. In absolute terms, what must Armenia do to realize the state of the art in administration, organization, program selection, and project delivery. This report applies both standards. It draws upon experience with other systems that fall within what roughly might be called Armenia’s peer group, and it assesses Armenia’s experience in light of standards to which all competition systems should aspire. In addition, due attention is paid to the first of the above-mentioned principles, i.e. to the assessment in how far the ACPS’ own goals and objectives are achieved in practice.

14. Recent decades have provided an extraordinary base of experience with the formation of new competition policy regimes. Each jurisdiction’s creation and implementation of a competition law has distinctive features, yet modern experience – including the introduction of 80 new systems in the past thirty years – indicates that a number of phenomena that appear to be universal, or nearly so. Among other techniques, this report focuses on challenges that competition agencies typically must confront in their first decade. The tenth anniversary of the ACPS is approaching, and this measure of performance takes account of the often daunting circumstances that accompany the development of a new body of law in a transition environment. To focus on the first ten years is not to suggest that all (or most) challenges facing a competition agency are likely to be surmounted in any single period of an agency’s existence. Rather, such challenges confront an agency throughout its lifetime.

15. In 2006, two researchers offered an assessment of the early functioning of the ACPS :

“The competition agency in Armenia, the SCPEC ... has quickly achieved a number of standards of international best practice in its three years of existence. With strong institutional development and the materialisation of a comprehensive competition culture, amongst the business community and the populace, competition policy could emerge as a dynamic force. The future prospect of competition policy in the Republic of Armenia, therefore, looks positive.”<sup>6</sup>

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<sup>5</sup> This concept originated with Khalid Mirza, Chair of Pakistan’s competition authority, who has emphasized the “last mover advantage” that new competition systems can realize by studying the experiences of other jurisdictions.

<sup>6</sup> Michael W. Nicholson & Lilit V. Melikyan, “Armenia” 3, 7 (Feb. 2006), available at <http://siteresources.worldbank.org/INTCOMPLEGALDB/Resources/1-Armenia.pdf>.



16. This view continues to serve as a fair assessment of the state of progress in Armenia. In the discussion below, this report considers measures that can assist in promoting the forms of institutional development and the establishment of a competition culture that can make the ACPS the dynamic force that the Law on the Protection of Economic Competition sought to create ten years ago.

## 1.2 The Economic, Historical, and Political Environment

17. There are several critical background facts and circumstances that impact on every aspect of Armenian life and each impacts significantly on the character and practice of competition law and policy and the challenges that it is obliged to confront. The two fundamental facts of Armenia's economic and political life are, firstly, its status for approximately 70 years as a republic of the former Soviet Union and therefore the centrally planned character, until relatively recently, of its economy, an economy planned in relation to the constellation of regions and semi-autonomous republics that made up the Soviet Union.

18. The second fundamental feature underpinning Armenia's political and economic life is the geo-political situation in the South Caucasus region, specifically the conflict-ridden relationship between Armenia and its eastern neighbour, Azerbaijan, and between Armenia and its western neighbour, Turkey.

19. These two incontrovertible facts, one in the recent past, the second very much a feature of the present, powerfully underpin and influence every aspect of Armenian public life, and this includes its competition law and policy. The spectacular decline, rise and fall of the Armenian economy in the period since 1991 to the present<sup>7</sup>; the structure of its economy; its ability to trade with the rest of the world and the severe distortions that characterise its trading patterns; the constant reference to the interpenetration and interdependency of private economic property relations, on the one hand, and public life and institutions, on the other; the size of Armenia's 'shadow economy', a term which connotes the under-reporting, for tax and import duty purposes, of a very significant proportion of economic activity; the size, indeed the very existence, of a relatively massive Diaspora of Armenians; and the structure of Armenia's public finances, on both the expenditure and income sides of its national accounts. These are but the most powerful manifestations of these two fundamental characteristics. All impact on Armenia's competition law and policy, as indeed they do on most other aspects of life in the small country.

20. Many nations have had to deal with one or another of these phenomena – troubled relations with neighbouring countries and the consequences of a lengthy history of central planning. Few have had to deal with both simultaneously. Armenia, a small, fiercely independent and ancient nation of 3 238 000 people (excluding, of course, Armenians in the Diaspora) must deal with both of these contextual realities and for advisers and reviewers of any aspect of Armenia's public and private life to understate the significance of these factors, would be an exercise in fiction.

### 1.2.1 Political Context

21. As previously mentioned, two aspects of Armenia's political context are particularly significant. Firstly, its progression from that of a Soviet republic to that of a constitutional, multi-

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<sup>7</sup> In fact, Armenia recovered quickly from the economic turbulences following the break-down of the Soviet Union and registered strong economic growth from 1994 to 2008. The average annual growth rate during this period was 9.7%. However, in 2008, Armenia was hit by the consequences of the global economic crisis, which impacted significantly on its growth rates.

party democracy. Secondly, its troubled relations with two significant neighbours, namely, Turkey and Azerbaijan.

22. While an evaluation of the character and quality of the Armenian democracy, much less an attempted prognosis of the future of geo-political relations in the South Caucasus, is beyond the remit of this report, both factors assume prominence when attempting to understand and evaluate Armenia's competition law and policy. This was consistently confirmed by Armenians from a variety of institutions and backgrounds who were interviewed for the purpose of preparing this review.

23. For example, a first principle and approximation of an evaluation of the competitive environment in any economy and society is that the level of competition is significantly compromised by a high level of concentration. In Armenia high levels of concentration are, in turn, significantly influenced by the limited points of entry and exit for the import and export of goods in what is an extremely open economy (that is, an economy where trade represents a significant proportion of GDP). These physical limitations on trade routes make it relatively easy to capture and, hence, monopolise trade in important products. If this is accompanied by a weak and compromised customs service, the upshot is a significant underreporting of trade, which, given its relative importance in economic life, results in a significant under-reporting of overall economic activity.

24. Where economic activity is frequently under-reported, the inevitable outcome – indeed the very purpose of underreporting - is that the dominant incumbents who have successfully monopolised key markets pay lower taxes and customs duties by taking advantage of loopholes afforded to them through imperfections in the law. This not only impacts on the public finances – and hence on the ability of government to build effective institutions such as competition agencies, regulators and, indeed, customs and revenue authorities themselves – but it also gives the dominant incumbents a strong competitive advantage vis a vis actual or potential rivals, thus further entrenching high levels of concentration and single firm dominance.

25. It is widely acknowledged that high levels of economic concentration, of monopolisation, do not, as a general rule, support vibrant democratic institutions. This view was emphasised by many of those consulted in the preparation of this review. Accordingly, a powerful reason frequently advanced for strengthening Armenia's competition law and its enforcement agency, is the contribution that vibrant competition enforcement would make to Armenia's democratic life, both by affording consumers greater choice and by easing the entry and the economic opportunities of would-be producers. Armenia's political system is one of the important aspects for understanding the current practice and future of competition law and policy.

26. These weaknesses notwithstanding, there nevertheless appear to be a number of vibrant Armenian-based NGOs and multilateral agencies active in the areas of trade and competition. These institutions derived considerable advantage from engaging with key public institutions in Armenia. One interviewee, who represented an impressive NGO concerned with the protection of consumer and other economic rights, derived considerable leverage from working with legislators, both of the ruling coalition and the opposition, and whose efforts and value appear to have been recognised by the government itself. His organisation was also well inserted into the international NGO community in the field of competition and trade.

27. The existence of key pockets of vibrant civil society were reinforced by an interview conducted with representatives of small and medium sized enterprises in Armenia. This body attached considerable significance to a robust competitive environment, an environment conducive to new

entry into the economy and a thriving small and medium enterprise sector. In their view a robust, independent competition authority was central to their objective of easing entry to the economy.

28. On the basis of these interviews it appears that there is considerable mileage to be gained for the future of competition law and policy in Armenia, from actively supporting the development of civil society. SCPEC should adopt a determined strategy of working with the NGO community as a source of critical, constructive support for its work. Moreover, although media representatives were not interviewed, it appears that the media is actively following competition law enforcement and is a potentially important source of effective communication between the competition authority and the public. The SCPEC has a number of registered journalists, which participate in regular press conferences by the authority.

29. It should however be underlined – and this was confirmed by many of the interviews conducted – that for the purposes of this review the key pertinent environmental factor related to the favourable treatment that selected firms were said to be accorded by certain public agencies, notably the tax and customs authorities.<sup>8</sup> The general perception conveyed was that these public agencies had effectively been compromised by those dominant companies who had wrested control of key markets, particularly the mechanisms for the distribution of imported products, and that they enjoyed significant political influence.

30. It was not, in any way, claimed that the above-mentioned practices and characteristic features had infected the entire political and business establishment. On the contrary, those interviewed were at pains to clarify that the President and Prime Minister's offices are widely regarded as genuinely supportive of political and economic reform, including robust competition enforcement. Moreover, there are clearly important institutions of government whose work placed them at the centre of the interplay between business and public institutions but who were not only aware of the potential for these relationships to undermine competition and public life in general, but who were precisely introducing measures designed to eliminate the potentially corrosive impact of these relationships in their sphere of influence. A particularly striking example is the office within the Ministry of Finance responsible for designing and implementing an honest and competitive system of public procurement, which clearly recognised the importance of co-operation with SCPEC in achieving his objectives.

31. However, where entire markets – the sugar market was the most frequently, though certainly not the only, example cited - have been captured by ambitious business people, taking advantage of weak and compromised key public institutions, market entry by legitimate businesses is rendered significantly more difficult, even impossible. As one astute interviewee observed, the early oligarchs – largely, it appears, those who captured lucrative markets for imported commodities – have accumulated considerable fortunes and can now become 'legitimate' business people whose financial clout has bolstered their commercial strength and, with it, their political connectedness thus enhancing their ability to enter and quickly dominate unrelated markets.

32. This has important implications for competition law and policy.

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<sup>8</sup> According to the order of the President of the Republic of Armenia of August 20, 2008 the State Customs Committee under the Government of RA and the State Tax Service under the Government of RA were reorganized as the State Revenue Committee under the Government of RA.

33. Firstly, it underlines and reinforces the strength of the opposition that robust competition enforcement will have to confront. And this in turn emphasises the importance of a strong and clearly drafted statute replete with the full panoply of investigative powers. It also emphasises the necessity of building a powerful coalition of public institutions and civil society in support of robust competition law and policy.

34. Secondly, it necessitates – as was called for by the Minister for the Economy himself – going beyond the realm of competition law enforcement and considering the development and implementation of a complementary, comprehensive competition policy. Competition law, which is principally concerned with private restraints of trade is a subset of a broader competition policy, which is, in turn, additionally concerned with publicly created restraints of trade. It is clear that the existence of highly concentrated markets cannot be solved by enforcement action alone. New entry will not easily be forged only by taking enforcement action against the anti-competitive practices of the business belonging to established oligarchs, but will also necessitate the development of a competition policy designed to facilitate new entry that includes the reform of what are said to have effectively become key instruments in the acquisition of market power such as the tax authority and the customs authority.

35. The competition authority, SCPEC, has a legitimate interest in the workings of these authorities because they have been clearly identified as active impediments to the promotion of competition in the Armenian economy. Certainly in exercising its advocacy function SCPEC is duty bound to point out the role played by these practices in undermining competition. However, in so doing SCPEC will clearly require the support of not only civil society but also of government itself. It is clear that the resolution of these problems should become a vital plank in the competition policy that the Minister has proposed be considered alongside the issue of strengthened competition enforcement.

36. Thirdly, the phenomena described above ironically point to some potentially positive outcomes for competition policy were its predominant source to be tackled and eliminated. As shall be elaborated below, certain dominant companies have rooted themselves in tax evasion achieved through the simple expedient of under-declaring revenues and imports. By many estimates this practice understates the size of the Armenian economy by as much as 40%-50%.<sup>9</sup> According to the personal view of an interviewed senior official of the Central Bank, 70% of economic activity is undeclared. Were the actual size of the Armenian economy to be known, new entry, including in the form of foreign direct investment particularly given the privileged access that Armenia has to the markets of the CIS states, would clearly become a more attractive option, thus potentially reducing the market power commanded by the incumbent companies. In addition, reducing tax and customs evasion as a result of underreporting would raise fiscal revenues and hence enhance the possibility of significantly improving civil service salaries, an essential requirement for effective competition law enforcement.<sup>10</sup>

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<sup>9</sup> See for example the Report on 2007 Annual Activity Program of the SCPEC which estimated the level of underreporting as equivalent to 50% of economic activity in Armenia  
[http://www.competition.am/uploads/resources/Eng\\_Program\\_2007.pdf](http://www.competition.am/uploads/resources/Eng_Program_2007.pdf)

<sup>10</sup> In this context is worth mentioning, that with the objective to fight tax evasion, a recent reform of the Law of the Republic of Armenia on Accounting introduced the legal obligation for companies with an annual turnover of DRAM 1 billion or more to undergo an independent audit before publishing their annual results, see Article 24.1.1 of the respective law.

37. A final, and extremely important, observation of Armenia's political context concerns its international relations. As may be expected, a country confronted by Armenia's unfortunate geopolitical circumstances would, quite rationally, attach considerable significance to its international relations. Of particular potential importance from the perspective of competition policy are relations between Armenia and the European Union.

38. EU relations with Armenia are governed by the EU -Armenia Partnership- and Cooperation Agreement signed in 1996 and entered into force in 1999. Following the enlargement of the European Union, the EU launched the European Neighbourhood Policy (ENP) and Armenia became part of this policy in 2004. On the basis of a Country Report (published in March 2005), an ENP Action Plan was discussed by the European Commission and the Armenian government and finally adopted on 14 November 2006. Furthermore, the EU established the EU Advisory group to the Republic of Armenia. In addition, according to the Minister of Economy, Armenia and the EU are about to start formal negotiations on a free trade agreement. It is intended that the free trade agreement will include provisions on competition. Indeed, it appears that Armenia aims at harmonising its legal framework with EU laws and regulations without any current ambition to apply for EU membership. To this end the Armenian Ministry of Justice has established a translation centre responsible for translating important European legislation into Armenian and important Armenian legislation into English.

39. The German Federal Ministry of Economics and Technology in cooperation with the Competition Council of the Republic of Lithuania have been selected to implement the EU Twinning project "Strengthening the Enforcement of Competition and State Aid Legislation in Armenia" in Armenia. This project aims at strengthening the enforcement of state aid and competition law and policy in Armenia and gaining further proximity to the "Acquis Communautaire." The proposed project activities cover the adoption of implementing regulations and enforcement guidelines in line with those of the EU, as well as capacity building for the SCPEC.

40. Under these circumstances, it is to be expected that the EU's relationship with Armenia will translate into both political support for robust competition law enforcement, but also into support for the building of capacity that the Armenian competition authority so urgently requires.

### 1.2.2 Economic Context

41. In Armenia, the relationship between public institutions and commercial power, key elements of the political context, are also relevant to the economic context. Hence much that is interesting and important about the economic context from the perspective of competition policy has already been dealt with in the above discussion of the political context and a degree of repetition is accordingly inevitable.

42. However it is important to emphasise that until a mere twenty years ago Armenia was a centrally planned economy. It was planned, as has already been observed, in relation to the requirements of the constellation of regions and semi-autonomous republics that made up the Soviet Union. In this context Armenia was an important supplier of manufactured inputs – notably machine tools – to the rest of the Soviet bloc economy and particularly to Russia itself. This market disappeared overnight both because the absence of competition had left those key parts of what was essentially a highly protected manufacturing economy chronically unable to compete in suddenly liberalised markets and because the precipitous decline of the Russian economy had significantly reduced the demand side of the market.

43. While it appears that this manufacturing capacity has never been successfully revived, certainly on the scale that it existed in Soviet times, the data indicate that the Armenian economy did recover rapidly from this shock, recording, through much of the 1990s, and then especially in the first decade of this century, growth rates, that despite the systematic underreporting of economic activity already alluded to, can only be described as stratospheric. In the period 1995-2008 an average annual growth rate of 9% per annum is recorded. Between 2001 and 2007 the economy grew at an average annual rate of 13%, while GDP per capita grew from approximately USD670 in 2001 to USD3689 in 2008. Growth dipped significantly from 2008 as a result of the onset of the global economic crisis, manifested in Armenia in particular as a significant decline in foreign remittances, a critical source of finance.<sup>11</sup> Indeed, it appears that these impressive growth rates were largely fuelled by a construction boom financed, in significant part, by remittances from the very large and loyal Armenian Diaspora.<sup>12</sup> Both the remittances and the construction activity that they financed were significantly reduced by the onset of the economic crisis.<sup>13</sup>

44. In summary then, following the shock of the collapse of the Soviet economy and society, the Armenian economy rapidly transformed itself. However, it does not appear to have re-established the manufacturing base and capacity that characterised its economy in the Soviet period. Moreover any potential that there may have been for this, was powerfully undermined by the closure of the borders with Turkey and Azerbaijan – in fact by the effective severing of economic relations with these countries who would otherwise been important markets for Armenian products and an important source of competitive inputs.

45. While it is not the remit of this report to identify a new basis for a competitive Armenian economy, several of those interviewed insisted that the underlying capacity could be revived, indeed was still in place (for example, the rates of literacy are extremely impressive) given progress in resolving the geo-political situation and a strengthening of the competitive dynamic of the economy, or expressed conversely, a weakening of the market power of the incumbent companies.

46. The purpose of this report is to examine the extent of competition in the Armenian economy and to make proposals aimed at strengthening it. This is at one with the clear objectives of successive post-Soviet Armenian governments. Since the demise of the Soviet Union, Armenia has opted for a market based economy. Nor is this mere rhetoric. If evidence of official support for a liberal, market based economy is required one need refer no further than the rapid privatisation that immediately followed the demise of the Soviet Union, the unusually liberal (in formal terms at least) trade regime and, not least, the active official support for competition enforcement. Most of those interviewed clearly viewed a strengthened competition regime as a critical element in confronting the problem of the highly concentrated nature of many important product markets.

47. This serves to underline the scale and particular nature of the problem facing an agency charged with promoting greater competition. The route to control of these markets lay, as has already been elaborated, not in competition on the merits but rather through the capture of key

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<sup>11</sup> Ministry of Economy of the Republic of Armenia, Armenia Economic Report 2009, From Crisis toward New Development.

<sup>12</sup> Ibid. The report records that between 2004 and 2008 remittances received through the bank system totalled USD5,3 billion, at annual rate of some USD1,5 billion.

<sup>13</sup> Ibid. Note that between 2001 and 2008 the construction sector recorded an average annual growth rate of 19,6%, with the share of construction in GDP increasing over that period from 10% to 27%.

markets for imported commodities, significantly abetted by compromised public institutions. Accordingly, while there may be much that competition law and enforcement can achieve, it will rely upon a supportive government and public to support the competition authority if it is not to be disempowered by the very forces that gave rise to market power in the first place.

48. It is, at this stage, apposite to emphasise some particularly important elements of the economic context that have already surfaced in the above discussion of the political context. In particular, the phenomenon of the 'shadow' economy should be re-visited and emphasised.

49. This review has been specifically charged with examining the impact of the 'informal economy' in Armenia. Informal economic activity is prevalent in most developing economies and generally takes the form of relatively small scale traders and even manufacturers, trading and producing without the overheads (for example, high property rents) of their formal counterparts and whose informal status additionally enables them to escape many of the social and economic obligations – from labour and health and safety laws to tax and business registration requirements – imposed upon formal enterprise.

50. In developing countries, this raises obvious competition issues – how does a formal clothing retailer compete with a street trader located in a stall on the pavement outside of his store, selling genuine or, as frequently, counterfeit versions of the same product sold in the formal store for a fraction of the price? How does a formal auto repair shop paying the minimum wage and meeting its various social obligations, compete with the informal shop set up in the backyard of a residential area offering a similar service again at a fraction of the price of its formal counterpart?

51. One approach emphasises the necessity to reduce the level of informal activity in order to solve the competition problems that it generates for formal traders and producers. It emphasises the need to relax regulation in an attempt to induce greater formalisation arguing that this will improve working conditions, product safety and competitiveness and broaden the tax base. An alternative approach emphasises that informal activity will always be present, that it provides much needed jobs and income and that in developing countries it should be viewed as entry level economic activity which, given the appropriate conditions and framework, including a reasonably liberal regulatory framework, will 'graduate' to the formal sector. Ultimately, there is not necessarily a great divergence between the policy implications of these alternative perspectives, even though the starting point of the former emphasises the negative impact of informal sector growth on the formal economy, while the latter emphasises the job-creation and entrepreneurial learning and opportunity associated with informal sector activity and the prospect of it constituting the basis for the growth of a vibrant formal economy.

52. However this type of informal activity is very different from that which characterises the Armenian economy. As already noted the Armenians themselves aptly refer not to the 'informal sector' but rather to the 'shadow economy'. Indeed, Armenia's centrally planned history was not conducive to the prototypically unplanned, entrepreneurial nature of what is usually understood by the term 'informal sector'.

53. The shadow economy of Armenia is effectively formal sector activity that is not reported to the authorities principally in order to enable the trader or the producer to evade the payment of taxes and import duties. As noted, the most common estimates reckon that 40%-50% of formal sector activity is undeclared. Hence, by any measure a significant slice of Armenia's economic activity is subject to neither corporate tax, nor import duties nor social taxes. This is the 'competitive advantage' – or, rather, the source of economic rent – that enabled dominant

Armenian business enterprises, or, as they are most commonly referred to, 'oligarchs', to capture entire markets.

54. Compromised customs collection appears to play a particularly important part in the capture of Armenian markets. The markets most frequently identified as highly concentrated were those such as sugar, grain, fuel and rice, all markets in which imports predominate. Nor is this surprising.

55. Firstly, Armenia, presumably because of the regional specialisation that was a feature of Soviet planning, is an extremely open economy with trade comprising some 46% of GDP in 2008.<sup>14</sup>

56. Secondly, as already noted, geo-political conflicts have closed two of landlocked Armenia's most likely routes to the ocean, namely, the borders with Turkey and Azerbaijan. The upshot is that Armenia has effectively one reliable, economically viable route to the sea, namely through its border with Georgia. This effective bottle neck clearly eases the ability to capture the import trade and the public institutions that supervise it.

57. Although privatisation has, in other countries, often been identified as a source of market power, whereby publicly licensed monopolies were converted into privately owned monopolies and put in the hands of individuals closely linked to the political rulers, this does not appear to have been the case in Armenia. A former member of the political elite who had been directly involved in the privatisation process in the immediate post-Soviet period, affirmed that public enterprises were broken up, horizontally where possible, and vertically where appropriate. However, his view was that lax post-privatisation regulation had permitted re-consolidation of critical utilities in gas, telecommunications, electricity and water. While in his view technological factors have ensured a competitive telecommunications service (a view that was not shared by well informed and experienced users of the fixed line monopoly's network), Armenia's most damaging monopolies were, in the opinion of this interviewee, now to be found in the regulated gas, water and electricity markets. This, of course, renders the building of an effective, co-operative relationship between the competition authority and the regulator of public utilities particularly important. This again serves to underline the role that a range of public institutions – we have identified customs and revenue, public procurement and public utility regulators – underpinned by a supportive government and legislature, must play in promoting and maintaining dynamic competition.

58. There are, however, grounds for optimism. Those interviewed, all well informed and from diverse backgrounds and perspectives, emphasised the need for a robust, independent competition authority. While, as suggested above, one interviewee argued that the priority task lay in revitalising the utilities regulator, this will not be possible, as will be elaborated below, without resolving the jurisdictional differences between competition authority and the utilities regulator and in the process extending a greater role in the regulated markets to the competition authority. Interviewees representative of civil society and multilateral agencies were eager to lend their active support to the competition authority. Public servants in areas critical to competition who were actively involved in promoting robust competition, were appreciative of the importance of active co-operation with SCPEC in promoting their goals. No less a personage than the Chairman of the Administrative Court expressed his willingness for the members of his court to receive training in the area of competition law. Those interviewed were confident that the offices of both the President and the Prime Minister supported the reformist path manifest in support for robust competition law and policy.

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<sup>14</sup> Armenia Economic Report from crisis toward new development (2009) page 34.



59. The Minister of the Economy's support for a competition policy framework is also encouraging. However, while there will rightly be many elements of this framework that extend beyond law enforcement, encouraging new entry will not be sufficient given the power of the incumbent companies. What will be required to achieve new entry and, thus, competitive markets, is active law enforcement by a competition authority whose independence and resource base will depend, in significant part, on the active support of the political leadership and whose public reputation and standing will be strongly influenced by its perceived vigour as an enforcer of competition law.

60. In summary then while there is much about the broader political and economic context, that is antithetical to the development of robust competition enforcement, there are equally solid grounds for believing that these obstacles can be overcome. While an adequately resourced, technically competent and publically supported competition authority will be at the centre of this effort, co-operation with a range of collateral public institutions and civil society will be critical determinants of the ability of the competition authority to confront the scourge of unrestrained market power.

## 2. THE LEGAL FRAMEWORK – THE LAW ON THE PROTECTION OF ECONOMIC COMPETITION

61. Armenian competition law is rooted in the country's constitution. Article 8 of the Constitution of the Republic of Armenia provides: 'Freedom of economic activity and free economic competition is guaranteed by the Republic of Armenia.' Most Armenian competition law provisions are provided for by Law of the Republic of Armenia on Protection of Economic Competition ('the Act').<sup>15</sup> The Act was passed on November 6, 2000 and on January 13, 2001 the SCPEC was established. There have been several amendments to the Act since then, the major of which took place on February 22, 2007. A few changes related to procedural issues were made in 2008. In addition, Article 12 of the Civil Code of the Republic of Armenia addresses the protection of civil rights in connection with prohibitions on unfair competition and the abuse of dominance. Articles 195 and 196 of the Criminal Code of the Republic of Armenia criminalise certain forms of anti-competitive conduct.<sup>16</sup> However, it appears that the latter have never been applied in practice.

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<sup>15</sup> If not indicated otherwise, all Articles referred to in this report are Articles of the Act.

<sup>16</sup> Article 195. Illegal anti-competition activity:

1. Establishment and maintaining of illegal artificially high or low monopolistic prices, as well as, restriction of competition by prior agreement or by coordinated actions, in order to divide the market by territorial principle, to restrict the penetration into the market, to force other economic subjects out of the market, to establish and maintain discriminative prices, is punished with a fine in the amount of 300 to 500 minimal salaries, or with arrest for the term of 2 to 3 months, or with imprisonment for the term of up to 2 years.
2. The same action committed: 1) by violence or threat of violence; 2) by damaging or destruction of somebody's property, or by threat of damaging; 3) by abuse of official position, 4) by an organized group, is punished with a fine in the amount of 400 to 600 minimal salaries, or with imprisonment for the term of 3 to 8 years, with or without property confiscation.

Article 196. Willful breach of procedure for public procurement.

Willful breach of the procedure for public sales and auctions which caused large damage to the owner of property, to the organizer of the sale or auction, to the buyer or other economic subject, is punished with a fine in the amount of 300 to 500 minimal salaries, or with arrest for the term of 1 to 2 months, or with

62. The Act covers what is, for the most part, the standard set of issues contained in most competition statutes. Hence Chapter 2 deals with anti-competitive practices; Chapter 3 with dominance/monopolistic practices and its abuse; Chapter 4 is concerned with concentration, that is to say, with mergers. Chapter 5 is a relatively lengthy chapter dealing with 'unfair competition' while Chapter 5-1 contains a single article dealing with state aid. Chapter 6 deals with the SCPEC including, inter alia, its objectives and functions, its powers, its composition, its responsibilities to report to the legislature and the duties of 'economic entities, state administration and local government bodies' to provide data to the SCPEC as well as the issue of confidentiality. Chapter 7 deals with sanctions and remedies.

63. However, the prevailing view of most commentaries on the Act, and supported by many of the informed Armenians whom we interviewed, including staff member of SCPEC itself, was that the legal framework remained markedly defective in key aspects.

64. Another round of amendments to the Act is in the pipeline. However, although there are undoubtedly 'losses' in translation from Armenian to English, it is fair to say that the current Act is not clearly drafted and, it would be prudent to pay careful attention to existing examples of best or recommended practices – as, for example, those contained in the UN Set ('Set of Multilaterally Agreed Equitable Principles and Rules for the Control of Restrictive Business Practices') administered by UNCTAD or the recommended practices of the International Competition Network (ICN) and to seek expert assistance in the drafting of the intended amendments.

65. The following sub-sections describe the chapters of the Act and identify their defining principles and major shortcomings. While this section contains certain recommendations for amendment, key aspects of the Act and associated recommendations – for example, the serious shortcomings in the SCPEC's investigatory powers – are dealt with in the discussion of the institutional aspects of the Armenian competition enforcement regime.

## 2.1 Anti-competitive practices

66. Anti-competitive practices – that is anti-competitive horizontal and vertical agreements and abuse of dominance – are dealt with in Chapters 2 and 3 of the current Act. Chapter 3 – comprising Articles 5.1-5.7 - is principally concerned with anti-competitive agreements, both horizontal and vertical, while Article 6 of Chapter 3 defines dominance and Article 7 of the same chapter prohibits abuse of dominance

## 2.2 Anti-competitive agreements

67. Article 5 of Chapter 2 of the Act is principally concerned with anti-competitive horizontal agreements – that is, agreements between competitors. This is verified by practices listed in Article 5.2. Although this is an uncharacteristically lengthy list - most statutes would confine themselves to simply identifying horizontal agreements that fixed prices and other trading conditions, that allocated markets and that rigged bids – the practices listed in the Armenian Act do indeed cover each of these traditional 'hard-core' cartel offences. However, certain sub-clauses in this list – for example Articles 5.2(d) and (e) also incorporate what would usually be construed as exclusionary conduct. This is possibly because, as Article 5.3(b) makes clear, Article 5 purports to cover not only horizontal agreements but also vertical agreements.

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imprisonment for the term of up to 3 years and with or without a fine in the amount of up to 50 minimal salaries.

68. It is conventionally accepted in competition law practice that agreements between competitors belong in a category of their own, not least because the harm arising from them is so universally accepted that there is generally no necessity to prove economic harm but simply to establish the conduct, that is to establish the existence of an agreement between competitors to fix prices, allocate markets or rig bids.

69. On the other hand, vertical agreements, particularly those that do not involve a party that is dominant, are rarely harmful to competition. Undeniably, these agreements do sometimes harm competition – for example minimum resale price maintenance is widely, although not unanimously, agreed to be anti-competitive. However, for the most part, it would not be common practice to condemn vertical agreements without requiring proof of anti-competitive harm.

70. For this reason it is recommended that Article 5 be broken up into 2 separate Articles, the first dealing with horizontal agreements, the second dealing with vertical agreements. It is also recommended that the list of prohibited horizontal agreements be shortened and simplified, identifying those core offences – price fixing, market allocation and bid rigging – that are widely accepted to cause anti-competitive harm. These should be defined as per se illegal, whereas other forms of horizontal agreements, as well as vertical agreements should be subject to the rule of reason.

71. Furthermore, it appears that the concept at the heart of each of the prohibited horizontal offences is that of an ‘unjustified’ price movement. This is effectively a movement in prices that cannot be explained by any underlying change in the cost structure. Article 5.2 and 5.4 are understood by the SCPEC to provide the legislative basis for this approach. Article 5.2 reads as follows:

‘Anti-competitive agreements shall refer to:

(a) Establishment of discriminatory and/or differentiated sale and/or acquisition prices

(b) Unjustified increase, decrease or maintenance of a product price;

Within the context of this sub-clause, unjustified increase of price shall be deemed the increase of a product’s and/or its substitutable products’ price by two or more economic entities during a certain period of time.

Within the context of this Sub-Clause, unjustified decrease of price shall be deemed the decrease of a product’s and/or its substitutable products’ price by two or more economic entities during a certain period of time.

Within the context of this sub-clause, unjustified maintenance of a product price shall be deemed the maintenance of the price (including up to 5% change in the price) of a product and/or its substitutable products by two or more economic entities during a certain period of time, in case when the occurrence of certain conditions (factors) could lead or would have led to establishment of lower or higher price’

72. Article 5.4 provides:

‘Anticompetitive agreements shall be deemed proven when:

a) any factual details (including any written document or other written evidence, video or record), or any other evidence not prohibited by the Law, are available;

b) the actions or conduct of economic entities as specified in Part 2 of this Article testify it’.

73. It appears that the rather unusual approach of the Armenian legislation has two origins, one explained by many years of price regulation, the other by a marked and much remarked upon absence of investigative powers. The former underlies a rather mechanistic approach to price movements – an approach that holds that price changes are only determined by underlying cost movements rather than by market demand and supply conditions. Note, however, that in conventional approaches to horizontal agreements the offence of price fixing relates precisely to an agreement to manipulate output or supply in order to increase or maintain prices above the competitive level, that is above the level which would prevail if competitors took output decisions individually. Accordingly, in prosecuting horizontal agreements to fix prices (or allocate markets or rig bids) there is never any question of a ‘justified’ increase and so never any need to gather and analyse the underlying cost data. The upshot is that the SCPEC may be imposing upon itself an unnecessary and costly burden in attempting to prove the absence of a justification.

74. However, this apparently superfluous and burdensome activity is also explained by the second of the factors identified above, namely, the extreme weakness of SCPEC’s investigatory powers. Essentially, the SCPEC gathers price data in order to identify problem areas. Where a problem is identified – and a parallel movement in prices would constitute a prima facie problem - SCPEC then delves into the underlying cost data in order to ascertain whether or not there is a ‘justification’ for the price movement. If no justification is found, a conspiracy to fix prices is then inferred. This approach led to several decisions where the SCPEC imposed a fine based on the finding of a parallel increase in prices without ‘economic justification.’ However, it should be noted that on appeal, the Administrative Court required that the SCPEC provide direct evidence for any price fixing agreement and cancelled the respective fines decisions that were purely based on economic evidence.<sup>17</sup>

75. In fact, many competition authorities do track unusual price movements. And they would accept that an unusual parallel movement in prices would indicate a prima facie problem. They may even consider and examine whether a sudden increase in the price of a key input – say steel or oil – could have accounted for a series of unilateral decisions by downstream producers to increase the price of their products. But principally what a competition authority confronted by a suspicious price movement would then proceed to do is to utilise its investigatory powers in order to ascertain whether the price movement resulted from an agreement between competitors. However, it appears that because SCPEC’s investigatory powers are unusually weak and constrained, it is obliged to turn to economic evidence, that is to the underlying cost data, in order to demonstrate that the price movement is ‘unjustified’ and, from there, to infer a price fixing conspiracy.

76. SCPEC is strongly persuaded that it can secure a conviction on the basis of economic evidence alone. In fact leading officials in SCPEC went further and insisted that where it is able to show simultaneous and identical price movements on the part of firms in the same market, the onus to ‘justify’ the price increase would rest with the firms suspected of collusion.

77. While certain of the language of the Act does suggest the possibility of securing a price fixing conviction on the basis of economic evidence alone, the Administrative Court requires some evidence of an agreement, of a "meeting of minds." According to this view, price data alone is insufficient to secure a price fixing conviction. As already noted, while conventional approaches to

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<sup>17</sup> E.g. Administrative case VD/0297/05/08 request “Qetrin Group” LLC’s v SCPEC on annulment of SCPEC Decision N 90-A related to “Qetrin Group” LLC.

horizontal agreements do examine economic evidence which is then frequently used as a prima facie indicator of a potential underlying horizontal agreement, it is neither common practice nor desirable to rely upon economic evidence alone, that is, economic evidence in the absence of any direct evidence of an agreement.

78. However, those interviewed concur with the consultant reports referred to that the current weak investigatory powers of SCPEC render it near impossible for the authority to procure evidence of an agreement beyond the 'tacit collusion' revealed by price movements which cannot be justified.

79. Increased investigatory powers require a legislative amendment. Differing views were expressed on the prospect for such an amendment. This issue is examined when the question of SCPEC's powers is discussed.

### 2.3 Abuse of Dominance

80. Articles 6.1-6.4 define dominance. It is defined by market share and incorporates both single firm dominance (a market share of one-third or greater) as well as dominance on the part of the two or three largest firms, depending again on their collective market shares (each of two economic entities will be dominant if between them they command a 50% or greater market share, while each of three firms will be dominant if they capture two-thirds or more of the market in question).

81. In practice, the SCPEC faces certain difficulties related to the interpretation of this definition of dominance.<sup>18</sup> A situation where one company holds a market share of one-third or more is considered as a case of single firm dominance, even if there are indications for collective dominance, e.g. where one company holds a market share of 35% and its two main competitors hold a market share of 30% each. If the combined market share of two companies reaches 50% or more, only these two companies are considered as collectively dominant, even if a third competitor holds a significant market share as well and there are indications that all three firms collectively exercise market power. In summary, the current interpretation of the market share thresholds does not allow the SCPEC to base its finding of dominance on the economic reality in a given market, which bears the risk of under- and over-enforcement. Against this background, it appears useful to analyse how other jurisdictions handle the question of dominance in order to find possible solutions to this problem.

82. A number of competition laws do not provide for a concrete definition of dominance, but rely on the competition authority's economic judgment. On a case-by-case basis, the competition

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<sup>18</sup> The SCPEC described the current interpretation of the market share thresholds in Article 6 as follows: Article 6(2) only applies if the conditions for Article 6 (1) are not met. Article 6(3) only applies if the conditions of Article 6(2) are not met and Article 6.4 only applies if the conditions of Article 6(3) are not met. In practice, there might be cases where the share of the first economic entity is 35%; the second one's is 32% and the third one's is 8%. Thus, the first two economic entities may enjoy similar market power, whereas the third economic entity's situation is very different. However, according to the Act, the first economic entity is deemed as having a dominant position, whereas the second one is not considered as dominant. The same approach applies for assessing collective dominance. For example, in a market with five firms in total, which hold market shares of 30%, 19%, 17.5%, 16.5% and 17% respectively, the two firms holding market shares of 30% and 19% would not qualify as dominant, whereas the three strongest firms would qualify as dominant on the basis of their collective market share.

authority will have to assess several factors that influence the determination of dominance.<sup>19</sup> High market share is one indicator in favour of a finding that an enterprise is dominant in a relevant market. Nonetheless, the sole possession of high market share is insufficient for a finding of dominance, given that some markets are characterized by a high level of competition despite relatively few players. Other market indicators such as barriers to entry and actual and potential competitors, durability of high market share, buyer power, economies of scale and scope, access to upstream markets and vertical integration, market maturity/vitality, access to important inputs, and financial resources of the firm and its competitors, among others, should be taken into consideration.

83. Other jurisdictions provide short-cuts to proof dominance by using safe harbours based on market share thresholds as a starting point in the determination of dominance. If an enterprise does not possess a minimum level of market share, it will not be considered dominant. If it does, the competition authority will analyze other factors – as mentioned above - to determine if the enterprise is dominant.

84. Further jurisdictions presume that an enterprise is dominant past a given market share threshold. They put the burden of proving the lack of market power on the defendant once it has been shown that the firm has the requisite market share. If the defendant does not overcome this burden, it will be considered dominant.

85. The use of market share thresholds to either establish a prima facie case and thus shift the burden of proof or to rule out dominance enhances the efficiency of the enforcement of the competition authority and gives entrepreneurs legal certainty. Nonetheless, market share thresholds pose the risk of underemphasizing or overemphasizing market share in certain cases, leading to over enforcement or under enforcement. Therefore, as a rule, competition laws do not stipulate irrefutably that a company is dominant when it reaches certain market share thresholds.

86. This approach would also help to overcome the above-mentioned difficulties that the SCPEC faces when applying the market share thresholds for dominance, i.e. that it cannot assess the competitive situation in the respective relevant market. It is recommended that the market share thresholds provided by Article 6 are interpreted to constitute refutable presumptions for dominance - allowing for a different finding if evidence suggests that the companies under scrutiny face significant competition despite holding a market share that reaches the legal thresholds for the presumption of dominance. In particular, it is wholly conceivable that two firms that make up 50% of the market are vigorous competitors and there would thus be no basis for considering them to be collectively dominant. If the Armenian wording of the law does not allow for the recommended interpretation, it is advisable to proceed to a respective amendment of the Act.

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<sup>19</sup> This is for instance the case in EU competition law. Article 102 of the Treaty on the Functioning of the European Union (TFEU) prohibits the abuse of a dominant position without providing for a definition of a dominant position. In their decisional practice, the European institutions have defined dominance as a position of economic strength enjoyed by an undertaking, which enables it to prevent effective competition being maintained on a relevant market, by affording it the power to behave to an appreciable extent independently of its competitors, its customers and ultimately of consumers, see ECJ Case 27/76 United Brands Company and United Brands Continental v Commission [1978] ECR 207, paragraph 65; ECJ Case 85/76 Hoffmann-La Roche & Co. v Commission [1979] ECR 461, paragraph 38.

87. Once companies are found to hold a dominant position, the SCPEC registers them in a centralised register for dominant companies and they have to provide specific information on a regular basis. The centralised register of dominant firms is central to the treatment of dominance. This involved the gathering and analysis by the resource-constrained SCPEC of large quantities of data in order to determine whether or not a firm should be placed on or removed from the register. It also imposes a heavy burden on registered firms to file information. Article 28 requires that these firms shall provide to the SCPEC ‘at 6-month intervals, information regarding the volumes of product sold (acquired) by them on the given product market, cost structure and price flows (in the case of price changes – with appropriate justification)’. It is, under these circumstances, not surprising that by far the greater part of the fines levied by SCPEC arise from the failure on the part of firms to comply with the requirement to provide information.

88. Although the Act does not require the SCPEC to register a company as dominant before prosecuting possible abuses of this dominant position, contrary to the views of the SCPEC, the Administrative Court has held that inclusion on the register is a jurisdictional prerequisite for prosecution of allegedly abusive conduct.<sup>20</sup> In practice, this view poses significant enforcement challenges to the SCPEC, since certain companies transfer their activities to a different legal shell once they are registered as dominant. That is to say, the SCPEC needs to register the new legal entity to which activities have been transferred as dominant before starting its investigation - a cumbersome process that renders the SCPEC's work much more difficult.

89. Although the phenomenon of a dominant firm register is not uncommon in transition economies, this is not a warranted use of SCPEC's constrained resources. The experience and skills of the small department that has been employed for many years in gathering this data could be far better deployed in undertaking strategically selected market studies.

90. Indeed, the use of the register and the related emphasis on justifying price increases may be positively counter-productive. For example, when interviewed the departmental head responsible for the maintenance of the register revealed that firms registered as dominant in the cement market as well as the markets for milk, cream and yoghurt had, in the wake of input price increases, informed the SCPEC about their intention to increase prices. Approving proposed price increases by dominant undertakings clearly falls outside the jurisdiction and functions of a competition authority, which is not a price regulator. The register and the perceived obligation of registered firms to inform about their price increases could become an obvious platform for collusion. Furthermore, abolishing the register for dominant companies would also render the question whether the inclusion of a dominant firm in the register is a jurisdictional prerequisite for prosecution of allegedly abusive conduct redundant.

91. Sarah Reynolds<sup>21</sup> accurately sums up the major problems associated with the maintenance of a register of dominant firms:

‘Consideration should also be given to the role and benefits of the register of dominant enterprises that is currently maintained. This mechanism appears to be causing some of the same difficulties encountered by other countries in the CIS that have used it, including undue

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<sup>20</sup> This was the position taken by the Economic Court (now Administrative Court) in its review of SCPEC Decision 111-A, “Boundaries of Gasified (Carbonated), Sweetened Drinks involving CocaCola Hellenic Bottling Company Armenia” (Sept. 14, 2005)

<sup>21</sup> S.J. Reynolds, Competition Law and Policy in Armenia: Priorities for Improvement (SJ Reynolds Associates, 2009).

**expenditure of resources on questions of inclusion in and removal from the register, and confusion about the evidentiary value of a firm's entry in the register and whether such entry is a condition precedent to enforcement against abuse of dominance.'**

## **2.4 Mergers**

**92. The Act governing mergers or, as it is termed, 'concentration', is particularly vague and terse. For example, it appears that only mergers which give rise to a 'dominant position' are prohibited but it is silent on mergers that occur when one of the merging parties is already dominant.**

**93. It appears that the Act requires pre-merger notification, if the asset-based notification thresholds of Article 9.1 are met.<sup>22</sup> However, it is certain is that mergers are only rarely notified.**

**94. The flagrant disregard for the merger notification requirement must inevitably generate damaging questions regarding the credibility of the SCPEC – in effect a major provision of the Act is simply not being honoured. To continue allowing this flagrant disregard for the law is clearly highly undesirable. To put the point clearly, it is not possible to operate an effective merger control regime if firms feel free to ignore these rules. Because merger reporting obligations tend to be clearly stated (although, as noted, the English translation of the Act is not clear on the precise nature of these obligations) and in most cases do not involve difficult issues of interpretation, a firm's deliberate disregard of such requirements casts wider doubt on the commitment of the competition authority to insist upon fulfilment of its other commands. While no satisfactory explanation has been provided for the failure of firms to register, this may result from thresholds that are not appropriately crafted to catch those mergers that possibly produce anti-competitive effects on the Armenian market.**

**95. Against this background, Reynolds suggests that:<sup>23</sup>**

**'Prior to the completion of the amendment process, SCPEC should undertake a focused inquiry, together with the Central Bank, the registrar, and other relevant bodies to determine why these provisions have been ineffective and define appropriate amendments. Thresholds based on turnover rather than on asset value may be a means to address the problem, although questions about the source and reliability of turnover figures would need to be addressed.'**

**96. International experience with merger control underscores the importance of imposing severe sanctions for the failure of firms to comply with notification procedures. Indeed the fines for**

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<sup>22</sup> Article 9.1 stipulates: "Concentration of economic entities, before its practicing or participation therein, shall be subject to declaration if: a) The joint value of assets of the participants was at least 3 billion AMD in the financial year preceding its establishment; b) Participants operate on the same product market, and the joint value of their assets was at least 1 billion AMD in the financial year preceding its establishment; c) The value of assets of one of the participants was at least 3 billion AMD in the financial year preceding its establishment; d) Participants operate on the same product market, and the value of assets of one of them was at least 1 billion AMD in the financial year preceding its establishment.."

Article 9.1 is complemented by a statutory waiting period provided for by Article 9.3: " It shall be prohibited to practice or participate in concentration subject to declaration or leading to a dominant position prior to the adoption of Commission's decision."

<sup>23</sup> S.J. Reynolds, Competition Law and Policy in Armenia: Priorities for Improvement (SJ Reynolds Associates, 2009).



failure to notify a merger provided for in Article 36(4) of the Act are higher than those for any other offence. However, while Article 10(4), dealing with 'state regulation of concentration' provides that 'enacted prohibited concentration shall be subject to liquidation (annulment, ceasing), it is not clear whether this remedy is also available for failure to notify a transaction. In the absence of more legal clarity, the fine specified in Article 36(4) appears the only sanction available in case of a failure to notify.

97. Hence, the remedies for failure to notify do not appear to include the ability to order divestiture of an illegally consummated merger. In many other jurisdictions, a common remedy for noncompliance with the notification requirements is rescission of the transaction in case that the consummated merger significantly impedes competition. By this measure the merging parties are obliged to restore, as much as feasible, the status quo ante by divesting assets and recreating the acquired entity in the form in which it operated before the acquisition. Fines are also commonly administered in conjunction with rescission. One way to calculate the fine is to apply a penalty for each day for which the firm acquired assets in violation of the notification procedures as opposed to the flat fine provided for in the Armenian Act. A third sanction is to force the violator to disgorge all profits earned from the acquired entity during the period of noncompliance. Collectively, these measures seek to deter violations by depriving the violator of all gains from its wrongdoing (via rescission and disgorgement) and by inflicting additional punishment (a fine for each day of noncompliance) to account for the possibility that the agency might not detect all violations.

98. One way for SCPEC to set the foundation for a renewed compliance program would be to issue guidelines and to have top management give speeches that announce the agency's enforcement intentions. If there is ambiguity surrounding existing notification requirements, these steps can provide useful clarification. It is common for competition agencies to designate an official, within the office that administers the notification program, to be the point of contact with the public to address questions regarding the program's requirements. Through this official, agencies often give advice in writing and place written guidance on their web sites. The official also often has a mandate to give spoken advice concerning the notification rules. Spoken comments usually are not deemed sufficient to carry the weight of written guidance, but they can supply a helpful means to address easily resolved questions of interpretation.

## 2.5 Unfair Competition

99. Chapter 5 is a relatively lengthy chapter dealing with the issue of unfair competition. Unfair competition, which is prohibited, incorporates an extremely wide-ranging and vaguely defined array of practices. These include 'breaking the principles of fairness i.e. honestly, equity, verity and impartiality among competitors or between the latter and consumers'. It includes 'creating confusion with respect to economic entity or its activity.'<sup>24</sup> It includes 'discrediting an economic entity or its activity', 'public misleading', 'damage to the reputation or goodwill or economic entity and 'unfair competition with respect to undisclosed competition'.

100. Certain of these offences incorporate what are conventionally understood as 'consumer protection' issues. There is an active debate in both competition and consumer protection circles regarding the appropriate institutional form for enforcement of consumer protection and competition rules – should the same body be responsible for enforcement of both sets of rules or

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<sup>24</sup> This seems to be the most widely used provision in this Chapter including as it does the 'unfair' use of trademarks or trade names.

should they be entrusted to separate institutions. However, the prior issue in the Armenian Act is undoubtedly the extremely wide ranging and vaguely defined nature of the practices listed.

## 2.6 State Aid

101. Article 16.1 prohibits state aid ‘which directly or indirectly leads or may lead to the restriction, prevention or prohibition of competition in any product market’. State aid is defined as ‘any aid (including financial means, such as assistance, credit, borrowing, property, privileges or other conditions) provided by the government, state or local government body, state organisations or organisation with state participation to a concrete economic entity or a certain group of economic entities’.

102. It appears that this provision has never been used. The danger inherent in including provisions in a statute that are effectively disregarded has already been noted in the discussion of merger notification. The extension of jurisdiction over state aid to a competition authority is largely a European Union phenomenon where it is a vital instrument in protecting the single market. Few national authorities possess such wide ranging powers over what are effectively industrial policy measures and instruments, although, given that these measures may impact powerfully on competition, it is not uncommon to require prior consultation between those ministries responsible for industrial policy and the competition authority. However, Article 16.1 extends some way beyond mere consultation to outright prohibition and would potentially eliminate all but the most generally applied industrial policy support mechanisms and programmes. It is thus little wonder that this clause has never been applied and is unlikely to be applied in its present form. Consideration should be given to the repeal of this clause and its possible replacement with a requirement to consult the SCPEC before the implementation of state aid measures.

## 3. INSTITUTIONAL ASPECTS: POSSIBLE ADJUSTMENTS TO COMPETITION POLICY ENFORCEMENT STRUCTURES AND PRACTICES

103. To begin the discussions of possible enhancements to Armenia’s competition policy system, general approaches are laid out that Armenia and other jurisdictions can consider in formulating a competition policy program.

104. The first dimension focuses on the enforcement of legal commands that prohibit specific forms of anticompetitive behaviour. The willingness of firms to comply with a specific competition law command depends on the answers to be given to five basic questions. First, what is the content of the legal command? Second, how likely are infringements to be detected? Third, when detected, will infringements be prosecuted? Fourth, when infringements are prosecuted, will tribunals entrusted with finding guilt or innocence exercise their decision making powers to find a violation? Fifth, what sanctions will be imposed for violations of the law?

105. A jurisdiction can increase compliance with the law by adjusting any of these factors. It can strengthen the power of the substantive legal command – for example, by subjecting certain practices (such as the setting of prices by rival firms ) to categorical, “per se” prohibition. It can increase the likelihood that infringements will be detected – for example, by enhancing the ability of the competition authority to gather information that reveals a violation. It can expand the likelihood that detected infringements will be prosecuted – for example, by augmenting the resources of the competition agency. It can boost the likelihood that cases filed will result in convictions – for example, by increasing the understanding of the courts about the rationale for competition law and by improving the quality of evidence that the competition agency presents to

the court. Fifth, it can deter violations by boosting sanctions – for example, by raising the level of monetary damages imposed on violators.

106. The second dimension addresses the mechanisms that a competition authority can employ to achieve precompetitive policy goals. Many successful agencies avail themselves of a variety of policy instruments that rely, respectively, on compulsion and persuasion. These include law enforcement; the adoption of secondary legislation that sets out standards of conduct; industry studies and other research projects that illuminate obstacles to competition and identify possible cures; advocacy that seeks to persuade other government entities to adopt precompetitive policies; policy statements, speeches, and other forms of guidance that inform business managers about the agency’s enforcement intentions, and publicity and public education programs that raise awareness about the agency’s activities and mobilize public support for competition policy.

107. Of these policy instruments, law enforcement generally is the most significant foundation for a successful competition policy program. Law enforcement is important for both the specific results to be achieved in individual cases and for the consciousness-building and deterrence effects that come from the agency’s demonstrated willingness to use compulsory measures to gain compliance with the law. In some instances, law enforcement may not be a competition agency’s most effective policy tool. This is most apparent when the source of a competitive problem resides in decisions by other government bodies – e.g., a legislature or a separate government agency – whose behaviour stands beyond the reach of statutory prohibitions designed to address the conduct of private firms and not public entities. Even a substantial enforcement program may not attain its ends if it is not accompanied by outreach and publicity programs that inform the business community and the larger public about the significance of individual cases.

108. A competition authority might best envision its program in terms of a portfolio of policy initiatives: cases, rules, studies, advocacy, and publicity. The portfolio ought to be assembled with attention to the risks and rewards promised by each initiative. A summary of factors would include the likely impact upon economic performance and legal doctrine from a successful initiative, the doctrinal difficulty of a contemplated matter, the resource cost to the agency, and the political consequences of an initiative. As a whole, the portfolio should be diversified and contain a mix of projects that promise high risks and high returns, medium risks and medium returns, and lower risks and lower returns. There is no rule of thumb for deciding how much effort the agency should invest in each of these categories, but the agency should be attentive to the aggregate distribution of its efforts as it begins new initiatives.

109. In very general terms, a new competition system in its first decade must establish itself as a credible, significant institution. It can create a credible presence in a number of ways. For example, the system of competition law revitalized in South Africa in the late 1990s achieved a reputation for effectiveness and legitimacy in its first decade through its merger control program. In Egypt, the Netherlands, and Pakistan, the competition agencies developed significant credibility within their first five years through the prosecution of major cases involving the cartelization of important economic sectors.<sup>25</sup> The Jamaican Office of Fair Trading attained great prominence in

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<sup>25</sup> Pakistan adopted its first competition system in the early 1970s and retooled its system in 2007. The anti-cartel program referred to here was initiated by the new Competition Commission of Pakistan pursuant to the transformation of Pakistan’s competition regime in 2007. For all practical purposes, the new law was the equivalent of a restart. See Khalid Mirza, Chairman, Competition Commission of Pakistan, “Putting the Consumer First” (February 2010) (paper presented before the Office of International Affairs, U.S. Federal Trade Commission, Washington).

its first decade through a competition advocacy initiative that led the Jamaican telecommunications regulator to issue multiple licenses – rather than giving the incumbent monopolist telephone company an exclusive license – for mobile telephony and thereby spurred a dramatic improvement in telecommunications services in that country. By these or other types of initiatives, a competition agency must “put itself on the map.”

110. Armenia has taken important steps toward this goal. For example, the SCPEC has developed cases that focus on products contained in what might be called the basic “market basket” of goods that Armenian consumers collect in a typical visit to the grocery store. The competition authority has pursued important initiatives dealing with key infrastructure services such as local bus transportation, telecommunications, and the distribution of jet fuel. From the interviews carried out for this report, it is apparent that SCPEC is regarded as an important public institution and a foundation for future programs to improve economic performance in the country.<sup>26</sup> At the same time, many observers indicated that SCPEC has a distance to travel to play a role in solving competitive problems whose resolution will determine the future course of economic development in the country. The adoption of specific reforms discussed below in this report will be instrumental in realizing this possibility.

### 3.1 Institutional Framework and Operations of SCPEC

#### 3.1.1 Institutional Set-up of the SCPEC

111. The Act establishes SCPEC as an independent commission, which is a crucial element for any successful competition law enforcer. A central task of new competition authorities is to resist political intervention that undermines the legitimacy of its decisions. As a core concept, the agency must achieve autonomy in the sense that it makes decisions about the exercise of its powers to investigate, initiate cases, dispose of cases, and impose sanctions free from the influence of elected officials (e.g., heads of state or legislators) or of appointees subject to their control. This autonomy increases the quality of agency decision making by deflecting demands that it serve special interests at the expense of the larger public welfare. The Act provides important structural protections against the types of influence that would undermine SCPEC’s effectiveness.

112. The SCPEC’s board is composed of seven members (the chair, the chair’s deputy, and five other commissioners) appointed by the President of the Republic of Armenia to renewable five-year terms.<sup>27</sup> Commissioners may be removed from office only for good cause.<sup>28</sup> The political branches of the government lack authority to overrule the decisions taken by the agency. SCPEC’s decisions in cases are subject to judicial review by the Administrative Court of the Republic of

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<sup>26</sup> This assessment was offered by a major Armenian consumer organization, a large association of business operators, individual businesses, and several international organizations with programs in Armenia.

<sup>27</sup> Article 20. The President of the Republic of Armenia shall appoint the Commissioners. The Commissioners, except the first composition, shall be appointed for a 5-year period. At the same time Article 21.3 states that Commissioners may be reappointed to serve additional terms.

<sup>28</sup> Article 21. As defined in Article 20, acceptable grounds for removal include judicial findings that the board member has committed a crime or lacks capacity,

Armenia.<sup>29</sup> Appeals from rulings of the Administrative Court in turn may be filed directly with the Supreme Court.

113. The Chair of the SCPEC serves, in effect, as the chief executive officer of the authority.<sup>30</sup> The Chair represents SCPEC before other government agencies in Armenia, before government bodies in other countries, and before international organizations. The Chair manages and coordinates SCPEC's the regular activities and serves as the agency's representative in interagency meetings in which SCPEC participates as an advisor on issues of competition policy.

114. The work of SCPEC is carried out through several operating units.<sup>31</sup> Three bodies are responsible specifically for the execution of the agency's substantive programs: a methodology and registrar maintenance department, a research and enforcement department, and an analysis department. The legal and administrative proceedings department provides agency-wide guidance on legal matters and represents the agency before Armenia's courts. A foreign relations department is responsible for all international liaison activities and plays a central role in policy planning and outreach, including the preparation and maintenance of SCPEC's website ([www.competition.am](http://www.competition.am)). Two units -- an administrative management department and an accounting division -- constitute the core of the agency's administrative infrastructure. Based on legal reforms in 2007, the SCPEC was authorized to establish a new department: the supervision department was set-up in 2008 but in practice, it has limited investigation powers.<sup>32</sup> Altogether the professional and support staff of the SCPEC amounts to 76 employees.

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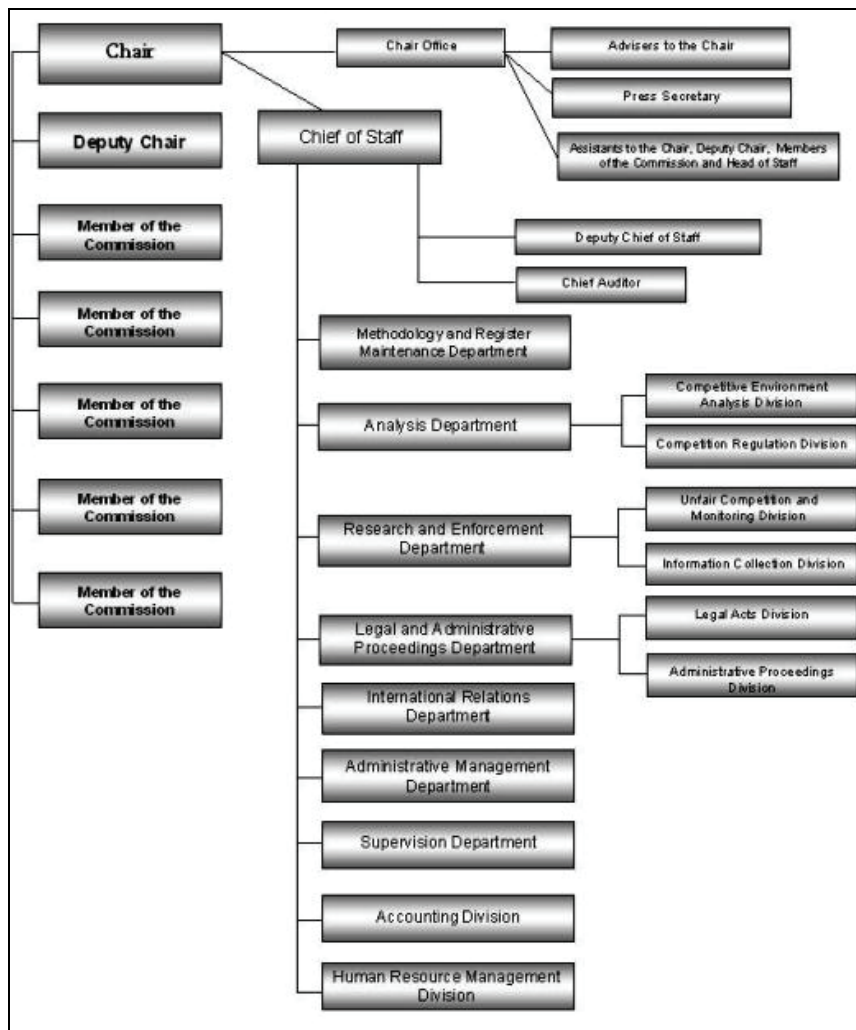
<sup>29</sup> The Administrative Court was established in 2008. Prior to this date, so-called economic courts were responsible for the judicial review in competition cases.

<sup>30</sup> Article 21.

<sup>31</sup> SCPEC, 'On Approval of the Statute of the Staff of the State Commission for Protection of Economic Competition of the Republic of Armenia,' Decision 54-1 (July 18, 2007)

<sup>32</sup> It should be noted that currently, the SCPEC is in the process of adjusting its institutional arrangements and procedures in order to increase the efficiency and effectiveness of its operations.

### Structure of the SCPEC



#### 3.1.2 Functions of the SCPEC

115. The Act assigns SCPEC responsibility “to protect and encourage free economic competition, ensure appropriate environment for fair competition, promote development of entrepreneurship and protection of consumer rights.”<sup>33</sup> To carry out its policy duties, SCPEC is authorized to:

- Exercise control over the compliance of Armenia’s competition statutes;
- Examine possible infringements of the competition statutes and issue decisions concerning such infringements;
- Maintain a centralized register of economic entities holding a dominant position;
- Bring cases in Armenia’s courts concerning infringements of the competition statutes;
- Participate in the drafting of statutes affecting competition policy in Armenia;
- Enter agreements with other jurisdictions concerning competition policy issues within its remit;

<sup>33</sup> Article 1.

- Cooperate with other government authorities in Armenia and with international organizations;
- Develop and implement measures to prevent infringements of Armenia’s competition laws;
- Examine and report upon experience with the implementation of the Act and propose improvements to the existing statutes;
- Publicize the competition authority’s activities, including through the publication of a regular bulletin;
- Perform a public outreach program to explain the competition statutes and the obligations of affected parties under the law; and
- Carry out other activities that serve to fulfil the objectives of the competition statutes.<sup>34</sup>

116. In broad terms, this set of commands provides the portfolio of policy making instruments that characterize superior practice in modern competition policy.<sup>35</sup> SCPEC has power to investigate infringements, to issue decisions and file cases to enforce the law, to use advocacy (including participation in the drafting of new legislation) to encourage the adoption of government policies that promote competition, to perform public education and other forms of outreach to publicize the law, to report periodically on the development of competition policy in Armenia, to cooperate with other public institutions at home and abroad, and to propose legislative enhancements to the existing framework of competition laws. Taken as a whole, this portfolio of duties provides a sound platform for the implementation of Armenia’s existing competition laws, the building of government wide policies that promote competition, coordination with other public bodies, and participation in international networks and other arrangements.

117. In particular and most pertinent for this report, Article 18 of the Act appears to contemplate that SCPEC will engage in periodic efforts to examine the effectiveness of existing institutional arrangements and propose adjustments to improve the performance of the ACPS. The ACPS framework is deliberately adaptable and evolutionary. This mandate for continuing assessment and improvement is consistent with internationally accepted standards that encourage competition agencies to engage in a regular process of evaluation as a way to test the quality of existing programs and to identify needed areas for improvement in legislation, organization, and operations.<sup>36</sup> Given the evolutionary nature of competition policy, by which a competition system tests various approaches for defining and implementing substantive policy commands, the starting point for a competition system – with an initial endowment of powers and institutional attributes – is perhaps less important than the commitment of a system to improve over time and its success in making modifications that reflect its own experience and that of other jurisdictions. SCPEC’s participation in this review fits well within the process of evaluation and renewal anticipated by Article 18. The recommendations presented in this report seek to contribute to that end.

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<sup>34</sup> Article 18.

<sup>35</sup> See William E. Kovacic, *Institutional Foundations for Economic Legal Reform in Transition Economies: The Case of Competition Policy and Antitrust Enforcement*, 77 Chicago-Kent Law Review 265, 281-86 (2001) (describing desirable elements of a competition agency’s charter).

<sup>36</sup> See William E. Kovacic, *Achieving Better Practices in the Design of Competition Policy Institutions*, 50 Antitrust Bulletin 511, 512-13 (Fall 2005) (emphasizing importance of periodic , regular reviews of a competition system to achieve better performance).

118. Furthermore, the Act imposes two important reporting requirements upon SCPEC.<sup>37</sup> By October 1 of each year SCPEC must present the National Assembly with a report that analyzes the state of competition in Armenia's economy, identifies important competition policy issues, spells out measures that SCPEC intends to take to implement the competition law, and discusses the performance of other regulatory mechanisms that affect competition in Armenia. By May 1 of each year, SCPEC must publish a report on the agency's activities in the previous year, including a discussion of developments in specific product markets in which SCPEC has undertaken programs. Among other uses, these reports provide SCPEC to focus government and public attention on important competition policy issues and to set out proposals for addressing specific problems.

### 3.1.3 The SCPEC's Investigatory Powers

119. According to Article 19.1 (c), the SCPEC is entitled to "Conducting research, inspection, study and (or) monitoring according to the procedure defined by the law in order to disclose the reliability of information presented by economic entities, the actual activity of economic entities, or to exercise control over fulfilment of the Commission decisions."

120. The procedure to be respected when carrying out the above-mentioned inspections is spelled out in the Law on Organising and Conducting Control in the Republic of Armenia of 17 June 2008, which lists the SCPEC as a part of the executive branch of the state empowered to carry out inspections.<sup>38</sup> Most importantly, according to Article 3 of this law, "Prior to commencing the control, the head (his/her alternate) of the relevant public authority shall issue an order or instruction on conducting a control, indicating the name of the authority carrying out control, the full name of the economic operator subject to control, the position, name and surname of the official (officials) carrying out control, issues of control, the period subject to control, the purpose, period of control, and the legal grounds for control." Furthermore, the provision stipulates: "Two copies of the order or instruction shall be given to the head of the economic operator or his/her alternate, three working days prior to the commencement of control."

121. In practice, this means that the investigation powers of the SCPEC are limited to verifying whether already submitted information is accurate after having announced such inspection three working days in advance.

122. Compared to state-of-the-art approaches that prevail in many other competition systems, these investigation powers are decidedly weak. In particular, SCPEC lacks the capacity to compel the production of records by means of dawn raids or other unannounced inspections that deny the affected parties the opportunity to destroy, sequester, or selectively present relevant evidence.

123. As discussed above, SCPEC has devoted substantial resources to two significant enforcement measures that seek, directly or indirectly, to deal with unilateral or concerted output restrictions in highly concentrated sectors. SCPEC relies upon the registry for dominant firms to track behaviour of certain large enterprises, and it is attempting to use economic evidence involving apparent coordination by oligopolists to address price increases in other sectors.

124. In an important sense, these programs may be explained as stemming from inadequacies in SCPEC's powers to gather information from business enterprises. Many competition authorities have realized that inferences drawn from parallel movements in prices can be competitively

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<sup>37</sup> Article 27.

<sup>38</sup> See Article 2.1 of Law on Organising and Conducting Control in the Republic of Armenia of 17 June 2008.



ambiguous. To identify price movements that are likely to be harmful because they result from concerted action, competition agencies increasingly have turned to investigatory techniques that permit them to collect direct evidence – in the form of business records and testimony of company insiders – of collusion.

125. Two techniques provide important means to this end. One is authority for the agency (usually subject to judicial supervision) to conduct unannounced “dawn raids” of business enterprises to obtain corporate records in paper or electronic form. Interviews underscored a concern that exists in a number of jurisdictions about giving authority to the competition agency to use powerful information gathering techniques. For example, in some countries, proposals to allow measures such as dawn raids or wiretapping summon memories of methods used by totalitarian political regimes to monitor political opponents. In many of these countries, such concerns have abated with the adoption of political and legal reforms that serve to ensure that the application of these methods is subject to proper judicial oversight. The Chairman of Armenia’s Administrative Court observed that dawn raids would be compatible with constitutional principles dealing with privacy and due process in Armenia. He doubted that Armenia’s existing administrative code provided an adequate basis for SCPEC to assert the right to conduct dawn raids. However, it should be noted that the public prosecutor is entitled to carry out unannounced inspections in criminal cases. From this perspective, it appears possible that the legislature adopts an adequate legal basis for the SCPEC to carry out unannounced searches of the premises of potential competition law violators as well.

126. To resolve uncertainties about SCPEC’s ability to use dawn raids and related forms of information gathering, legislation is appropriate to make explicit the agency’s power to use these tools. Such reforms would place Armenia with the mainstream of international experience. This mainstream includes a growing number of countries that approached these measures with scepticism and became convinced that, with proper procedural controls and judicial oversight, the instruments can facilitate the attainment of valid competition policy goals without transgressing widely accepted norms about due process and individual rights. It goes without saying that the SCPEC’s staff would need special training to carry out dawn raids and to analyse electronic and documental evidence, once its investigation powers are expanded.

127. The second is the implementation of a leniency program that rewards self-reporting of violations with a substantial or complete dispensation from sanctions. These tools have proven to be important to the ability of competition agencies to gain access to business records that assist in preparing a well-informed diagnosis of business conduct and, in the case of cartel arrangements, permit the agency to obtain reliable direct evidence (i.e., documents and testimony) of illegal collusion and reduce the need to rely upon more problematic, indirect, circumstantial proof of misconduct. However, it is important to note that the success of a leniency program depends crucially upon the severity of sanctions for infringements and the likelihood of detection and successful prosecution. The willingness of a cartel insider to report its misconduct increases as the magnitude and likelihood of the punishment to be imposed on the cartel increases.

128. Legal recognition of more powerful information gathering tools in Armenia would significantly improve SCPEC’s prospects for building an effective enforcement program. This is most evident in the case of leniency, where reliance upon informants could provide fuller information about the existence of cartels and the magnitude of harm they have caused. The adoption of legislative measures that expressly authorized SCPEC to establish a leniency program would be a valuable step. It is not clear that the relatively cryptic mention of leniency contained in current drafts of the amendments to the competition law will serve as an adequately robust grant of power. The drafters of the competition law amendments consider including a fuller

statement of the agency's authority in this respect. Furthermore, in designing the leniency programme, attention needs to be paid to the fact that certain forms of anti-competitive behaviour are not only prohibited by the Act, but also be Armenia's criminal code. If there are any chances, that the criminal provisions will be enforced in the near future, the public prosecutor/criminal courts should be involved in the design of the leniency programme in order to ensure that company's applying for leniency are granted an exemption not only from administrative, but also from criminal fines.

#### 3.1.4 Procedural aspects

129. The SCPEC also is responsible for setting the agency's administrative procedures. It may start an investigation based on a complaint or ex officio. For each case, the Chairman nominates one of the Commissioners as case coordinator and decides which division shall handle the case. When opening the case, the case team together with the coordinator identifies all interested parties in order to gather relevant information. In addition to organising meetings with these persons and with the complainant, the case team may ask the research and enforcement department for assistance in carrying out required research, e.g. for collecting information outside of the SCPEC's premises, carrying out interviews etc. This division of labour between the case team and the research and enforcement department shall allow the case team to concentrate on the economic and legal assessment of the facts and not to waste resources on the time-consuming information gathering. When the case team comes to the preliminary conclusion that a violation of the Act took place, it involves the legal department for assistance with the legal reasoning of the decision. Five working days before the discussion of the draft decision takes place within the SCPEC, it is circulated to all Commissioners and responsible departments. In parallel, it is also sent to all interested parties who are invited to comment on it and express their views during the SCPEC meetings. SCPEC carries out its key decision making tasks in sessions in which all members of the board participate.<sup>39</sup> These sessions are open to the public, except for matters in which the SCPEC discusses confidential business records or addresses other information whose revelation may cause undue prejudice to the interest of affected parties. The SCPEC issues a written decision in each matter and places these in the public domain. The SCPEC also has authority to issue public reports that present the results of its research projects.<sup>40</sup>

130. One aspect of SCPEC's administrative practice deserves particular attention. SCPEC's procedures call for investigations to be completed within 90 days.<sup>41</sup> Only in exceptional circumstances, this delay can be extended twice for ten days. Measured by the practice in other competition systems, this is an extremely short period of time to examine complex matters, which abuse of dominance cases frequently turn out to be. A more realistic period for an initial inquiry would be six months, subject to further extension by decision of the SCPEC board.

#### 3.1.5 Overview of SCPEC activities

131. Since its establishment in 2001, the SCPEC has adopted 22 decisions in competition cases (10 decisions dealing with the abuse of dominance, 7 decisions dealing with anti-competitive agreements and 5 decisions in merger cases). In contrast, in the same period, it has adopted over

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<sup>39</sup> Article 30 sets the basic foundation for SCPEC's deliberative procedures.

<sup>40</sup> Article 34.

<sup>41</sup> Article 30.10; Ioannis Kokkoris, "Anticompetitive Agreements: rules on the Monitoring and Methods of Evaluation" 19 (presenting results of study mission performed April 6-10, 2008 for project funded by OSCE).

100 decisions dealing with unfair competition and approximately 170 decisions imposing fines for the failure to submit information or the submission of false information.

**Overview of Decisions adopted by the SCPEC**

Type of decision	2001	2002	2003	2004	2005	2006	2007	2008	2009
<b>Final decisions in competition cases and procedures relating to unfair competition</b>									
Abuse of dominance	-	1	2 (1)*	1	2	1	-	2	-
Anticompetitive agreements	-	-	-	-	1	-	3	(2)	1
Mergers	-	-	-	-	1	-	-	3	1
Unfair Competition	-	(10)	(3)	40	9	10	13	1 (7)	5 (3)
Failure to submit information	(1)	3	7	19	37	54***	15	9	15****
Submission of false information	-	-	1	2	-	-	3	2	(1)
<b>Total</b>	(1)	4 (10)	10 (4)	62	50	65	34	17 (9)	15 (3)
<b>Other types of decisions*****</b>									
	70	87	96	95	93	81	77	101	79
<b>Overall TOTAL</b>	<b>72</b>	<b>101</b>	<b>110</b>	<b>157</b>	<b>143</b>	<b>146</b>	<b>111</b>	<b>127</b>	<b>97</b>

\* Decisions in brackets include warnings and cease and desist orders without imposition of fines.

\*\* 1 decision related to the egg market, by which the SCPEC fined 3 economic entities; another decision related to the butter market by which 19 economic entities were fined and the last decision related to the vegetable oil market by which 23 economic entities were fined.

\*\*\* 4 decisions from 54 were annulled by the SCPEC.

\*\*\*\* 8 decisions from 15 were annulled by the SCPEC.

\*\*\*\*\* In addition to final decisions in competition cases, the SCPEC adopts a great number of procedural decisions, such as decisions to start an investigation, to hear certain parties, to carry out market studies, etc. Also, decisions related to the expenditure of the SCPEC's budget and other administrative issues are contained in this category of decisions.

**132. The above-mentioned figures suggest that a significant part of the SCPEC's enforcement activity is dedicated to the maintenance and update of the central register of dominant companies. Taken into account the relatively low figure of decisions where the SCPEC actually found an abuse of a dominant position (10 cases since 2001), it appears that the SCPEC could make better use of its resources, which would however require some legal reforms, as explained in part of this report dealing with the registry for dominant companies.**

**133. It is recommended that the SCPEC focuses its enforcement activity stronger in the areas of anti-competitive agreements, merger control and selected cases of the abuse of dominance.**

### 3.1.6 Sanctions and Remedies

134. Article 36 of Chapter 7 specifies the remedies available to the SCPEC in the event of a contravention of the Act. Remedies are confined to fines. The article provides for a fine of 2% of proceeds for the year preceding the entry into an anti-competitive agreement to a maximum of 300 million AMD (approximately 820,000 USD<sup>42</sup>); 2 % of proceeds of the previous year in respect of an abuse of a dominant position to a maximum of 300 million AMD; and 4% for failure to notify a merger of the year proceeds up to a maximum of 500 million AMD (approximately 1.37 million USD). Acts of unfair competition carry a fine of 500 thousand AMD and repetition of the offence within a one year period carries a fine of the one million AMD. Receipt of prohibited state aid carries a fine of 2% of proceeds of the year preceding the infringement up to a maximum of 300 million AMD. Note that it appears this fine is imposed on the recipient of state aid and not on the provider of the state aid, that is the state is not penalised for breaking the law. Failure to submit required information or documentation is subject to a fine of 500 thousand AMD (approximately 1,370 USD), with a repetition of this offence within a one year period carrying a fine of two million AMD. Obstructing the SCPEC in the performance of its statutory duties carries a fine of 500 thousand AMD.

135. During the interviews for this report, it was mentioned that the rationale for the Act setting fines at fixed percentages of the violator's turnover without any margin of discretion was to limit incentives for corruption. Despite this understandable objective, this rigidity raises certain concerns with respect to the principle of proportionality. Reynolds, in calling for greater discretion in the application of fines, notes:

'Fines are defined as a single measure based on firm-wide turnover, with no ranges or discretion. A fine based on a multi-million DRAM firm-wide turnover that is applied as a sanction for a violation that relates only to a product accounting for a few tens of thousands may raise concerns about proportionality principles for legal sanctions. The lack of discretion concerning sanctions is also of concern in relation to cases in which a violator may in good faith not have been able to anticipate that the conduct would violate the law, as may happen in respect to some kinds of abuse of dominance. Higher fines may be appropriate for participation in hard core cartel agreements, but these should only be introduced together with clear provisions defining such cartels and separating them from other kinds of agreements.'

136. Note that the highest fine is reserved for failure to notify a merger. As mentioned previously, taken into account the low number of merger notifications received by the SCPEC to date, this fine apparently does fulfil its purpose.

### 3.2 The Judiciary and the Resolution of SCPEC Competition Cases

137. The courts of a country with a new competition policy system ordinarily will be unfamiliar with the economic or legal concepts that underpin the enforcement of competition policy commands. In the first decade of implementation in most jurisdictions, the competition agency has encountered considerable difficulty in pursuing successful litigation programs. One class of cases founder because the court is not persuaded by the agency's interpretation of the competition statute or is unconvinced by the evidence presented. In a separate class of cases, the

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<sup>42</sup> Converted at the exchange rate of 13 July 2010 (1AMD=0.00273USD).

courts dismiss or delay cases owing to the agency's failure to comply with the jurisdiction's requirements governing administrative practice and procedure.

138. In Armenia, the judicial system is bipartite. Ordinary courts have jurisdiction over civil and criminal matters, whereas administrative disputes fall within the jurisdiction of the Administrative Court. The ordinary jurisdiction entails three levels: first instance courts; so-called professional courts that function as appeal courts, and the Court of Cassation. The administrative jurisdiction only comprises two levels: the Administrative Court exercises judicial review over administrative decisions; and decisions of the Administrative Court can be appealed directly to the Court of Cassation. Furthermore, a Constitutional Court was established in 2005 that controls the constitutionality of legal acts and allows citizens to seek redress in case of a violation of their fundamental rights.

139. In line with the general repartition of competences between the ordinary jurisdiction and administrative jurisdiction as described above, the Administrative Court is responsible for hearing appeals against decisions of the SCPEC; see Article 30 of the Act. Chapter 26 of the Armenian Civil Procedure Code defines the grounds of an appeal. The Administrative Court is a very young institution that was established in the year 2008. Prior to this date, so-called economic courts were responsible for the judicial review in competition cases.

140. Overall 20 judges work at the Administrative Court, out of which 15 judges are based in Yerevan and 5 are based in other regions of Armenia. Due to the SCPEC's location, all competition cases are heard in Yerevan. Appeals against decisions of the SCPEC are initially handled by a single judge who is appointed by the Chairman of the Administrative Court on a case-by-case basis. The Supreme Court hears appeals against decisions of the Administrative Court. In case the Supreme Court remands a case back to the Administrative Court, three judges are responsible for handling the case.

141. The Administrative Court reviews procedural and substantial aspects of the SCPEC decisions under appeal. Generally, it does not accept new evidence in the appeal procedure. An exception to this rule may be granted if the appellant shows that particular evidence had already been submitted to the SCPEC during the administrative procedure, but the SCPEC unreasonably had not accepted this evidence. Since the year 2006, all court sessions in Armenia are being recorded. Under the new procedural law, the courts' case files are accessible to the public and court decisions are published on the internet. In addition, a new electronic programme, called data-lex, has been put in place which allows the parties to easily access all information in specific court cases.

142. In the period from 2001 to present, approximately 70 decisions of the SCPEC have been appealed against. In the same period, in 27 cases, the Administrative Court has upheld the decision of the SCPEC (which led to subsequent appeals against the decision of the Administrative Court in 7 cases), in one case the appellant against the decision of the SCPEC was partially successful and in 7 cases the appellants were fully successful, i.e. the SCPEC's decisions were cancelled. In 22 cases, the appeal process was terminated following settlement outside the judicial procedure. All these settlements relate to two investigations, where the SCPEC fined 29 companies for participating in two price fixing cartels. The Administrative Court cancelled the respective decisions for insufficient direct evidence for the alleged price fixing agreements. Since the fines imposed upon other alleged cartelists were based on the same economic findings, the SCPEC entered into settlement negotiations with 22 further addressees in order to find an alternative solution for the parallel appeal procedures outside the Administrative Court. To date, 11 cases dating from 2007 to 2009 are still pending.

## Overview of judicial review of the SCPEC's decisions

Year	Appeals	Rejected appeals	Partially successful appeals	Fully successful appeals	Pending Cases	Settlements
2001	1	1	-	-	-	-
2002	1	1	-	-	-	-
2003	1	1	-	-	-	-
2004	9	9	-	-	-	-
2005	4	3(2)*	1	-	-	-
2006	9	4 (3)*	-	4	-	1
2007	28	4	-	1	1	22**
2008	4	1	-	2	1	-
2009	11	2 (2)*	-	-	9	-
2010	1	1	-	-	-	-

\* The number in brackets indicates the number of decisions of the Administrative Court, which were appealed against to the Supreme Court.

\*\* All these settlements relate to two investigations, where the SCPEC fined 29 companies for participating in two price fixing cartels.

143. The SCPEC is one of a large number of agencies that occasionally have encountered difficulties with the courts, as reflected by the number of decisions of the SCPEC that were cancelled upon appeal. However, the SCPEC's record before the Administrative Court appears to fall within the mainstream of experience of most competition authorities operating in their first decade. There are a number of additional steps that SCPEC can take to improve the conversation between SCPEC and the Administrative Court, to increase judicial understanding of competition law, and to improve the evidentiary basis on which SCPEC builds its cases. Among the most important is to provide a fuller explanation of the evidence and legal reasoning that supports its decisions. Interviews conducted for this study indicated that improvements in this respect would improve the judiciary's view of SCPEC's work. At the same time, it also is apparent that judges would benefit from projects – e.g., workshops --that would give them more exposure to the essential economic and legal concepts underpinning competition law.

144. SCPEC's is engaged in a number of cases that will have a major impact on its effectiveness. One prominent matter involves the use of economic evidence to prove that rival firms have engaged in illegal concerted action. Another significant pending case deals with a vital question of jurisdiction and focuses on the allocation of responsibilities between SCPEC and the PSRC, respectively, for redressing apparent instances of anticompetitive conduct in the telecommunications sector. In these and other matters, an important consideration for the future development of the ACPS is the perspective and knowledge that the Administrative Court brings to bear in resolving appeals against the SCPEC's decision and in the interpretation of the SCPEC's authority.

145. All competition authorities are engaged in what can be called a continuing conversation with their courts. This conversation takes place not only inside the courtroom but also in other venues in which judges are made aware of the aims of the competition policy system and the agency learns about the expectations of the courts.

146. The true measure of the quality of the conversation between the competition agency and the courts is not whether the competition agency prevails in all of its cases. An agency that achieves complete litigation success is likely to have undertaken a program that is inadequately ambitious in its failure to wrestle with important doctrinal issues or in its tendency to dwell on matters of lesser economic significance. Two criteria supply useful benchmarks of progress in the early, formative period of a competition agency. The first is the agency's success in gaining acceptance for core areas of its authority. This concept encompasses judicial endorsement for the intended scope of its jurisdiction, for its information gathering powers, for its power to impose meaningful sanctions. The second benchmark relates to outcomes on the merits of litigated disputes. The aim is not to attain a 100 percent success rate, but to prevail in a sufficient number of litigation initiatives to achieve credibility in the eyes of the business community and in the larger society. It is not possible to identify with precision what the critical mass of substantive victories would be. But some favourable litigated outcomes are necessary to build the agency's stature and to gain compliance with the law.

147. Interviews identified several approaches that could improve SCPEC's relationship with the courts. The Chairman of Armenia's Administrative Court indicated that the judges of the Administrative Court have relatively little familiarity and experience with competition law and expressed his willingness to have his court participate in exercises – such as seminars and workshops – to increase the judiciary's knowledge in this field. He commented favourably on the study tour that enabled him and other Armenian officials to visit Germany and see how the German courts in competition cases dealt with jurisdictional issues, third party rights, evidence gathering powers, and the setting of fines. His remarks point to the benefits to be gained from future efforts to involve Armenia's judges in training activities that provide additional exposure to concepts of substantive competition law, investigational practice, remedies, and the interaction between competition law and public utility oversight.

148. Another approach to building acceptance for SCPEC's cases is to strengthen the quality of evidence presented to the courts. This relates back to the discussion above concerning SCPEC's information gathering powers. The application of stronger means for collecting evidence is likely to yield a larger volume of direct evidence – for example, in the form of business records – that make clear the fact of infringements and supply a more confident basis for the courts to find that violations have taken place. In fact, a number of adverse decisions issued by the Administrative Court and the previously competent Economic Courts have pointed to weaknesses in the stated evidentiary basis for the Commission's decisions. Strengthened investigatory powers would allow the authority to gather evidence that is more convincing and thus to provide the court with a more confident basis for upholding the SCPEC's decisions. Improved skills training also could improve advocacy and improved analytical skills could strengthen ability of staff to gather evidence and analyze it properly.

### 3.3 Budget and Resources of the SCPEC

149. The quality of a competition agency – or any other public or private institution – depends crucially on the adequacy of its resources.

150. SCPEC's annual budget is approximately USD \$500,000.<sup>43</sup> With this amount, SCPEC pays its 76 employees and supports its operations. SCPEC augments its legislative appropriation with

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<sup>43</sup> This represents a modest increase from funding levels that prevailed earlier in the decade. In 2007, the SCPEC's budget was approximately \$471,000.

occasional grants and other forms of support from donor organizations, which allows e.g. to receive advice from international experts.

151. In one sense, it is heartening to see what SCPEC has achieved with so few resources.<sup>44</sup> This is a testament to the commitment and effort of its staff. Nonetheless, it is evident that SCPEC cannot fulfil its intended role without a significant increase in the means at its disposal. The modern experience of literally scores of jurisdictions demonstrates a direct and powerful correlation between the human and physical resources the competition agency possesses and the breadth and quality of its programs. There may be instances in which agencies that enjoy comparatively substantial resources have performed in a lacklustre manner. Experience with competition policy implementation reveals no examples of jurisdictions in which a badly underfunded agency was able to devise and sustain a significant program.

152. External reviews of competition agencies often emphasize resource deficiencies and exhort national policymakers to augment existing competition agency budgets. Those with responsibility for setting national budgets may be so accustomed to hearing government departments and other public institutions ask for more funds that they react with the weariness of a parent who has just heard the latest in a long series of requests from a child who is attending university and is seeking a replenishment of funds. During interviews conducted in Yerevan for this project, a senior government official suggested that it was incumbent upon SCPEC to produce impressive results to demonstrate its worthiness for funding above existing levels,

153. This view seems seriously misplaced, for it misapprehends the nature of the tasks assigned to SCPEC and the need for the authority to recruit and retain individuals with high technical proficiency. The chief asset of a competition authority is its people. To ask what a competition agency should do is to beg the question of who will do it. As the quality of the agency's personnel grows, so too will expand its capacity to undertake more ambitious tasks and to achieve stronger results.

154. From interviews with SCPEC personnel and with other observers, it is evident that SCPEC has succeeded in recruiting and retaining a number of talented managers and professional staff. Yet, to stay abreast of current developments in competition law and to fulfil the more ambitious role that Armenia appears to contemplate for SCPEC, the agency must continue to enhance the quality of its team.

155. There are measures, outlined below, that SCPEC can take to build capacity if one assumes no improvement in its budget. One means is to enhance existing internal programs as a way to provide extensive, systematic training to all staff. A high priority of future training efforts should be information gathering and analysis techniques. The aim here would be to equip case handlers with greater capacity to develop the evidentiary basis for potential cases. It would be developed in anticipation of an expansion of SCPEC's information powers to gather information, including by dawn raids. If such reforms are not forthcoming, it would still be productive to provide training in state-of-the-art techniques for collecting data from other sources and improving the use of information available to SCPEC under existing law. These training efforts would best be conducted by experienced case handlers from other competition authorities, and the use of practical, hands-

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<sup>44</sup> By way of comparison, data presented in the Global Competition Review's 2009 Handbook of Competition Enforcement Agencies indicates the more generous budgets for competition agencies that are roughly comparable to Armenia in terms of population and age of the competition system: Barbados (USD 2 million); Bosnia/Herzegovina (712,165 Euros); Cyprus (USD 1.7 million); Jamaica (USD 820,510); Jersey (1.3 million British Pounds); Latvia (USD 2 million); Lithuania (1.18 million Euros); Serbia (800,000 Euros).



on simulation exercises would provide useful means of instruction. Instruction in these practical case development skills could be complemented by courses that focus on the conceptual framework of the ACPS and review widely accepted analytical approaches employed by other competition agencies to perform basic tasks such as defining relevant markets, measuring market power, and determining the existence of agreement in cases involving concerted action.

156. These measures are worth pursuing, but they may not suffice to achieve major improvements in performance. SCPEC's budget is a major obstacle to realizing truly substantial gains in talent. Interviews with officials at the Central Bank and the Public Services Regulator Commission (PSRC) underscored important disparities in public service talent within Armenia. The Bank and the PSRC receive substantially greater resources per capita, pay their employees far more generously than SCPEC can pay its staff (a multiple of two or four times more), and can provide additional benefits (such as opportunities to travel to attend continuing education seminars and to network with counterparts in other countries) that greatly improve prospects for recruiting and retaining first rate staff

157. Comparisons with the Central Bank and the public utility regulator are informative. Competition law is a field no less complex and technically demanding than public utility regulation or banking and financial services oversight. Competition policy has the potential to make comparably significant contributions to improvements in Armenia's economic welfare. In the execution of their duties, competition agency officials have equally frequent contact with private sector organizations who are in a position to identify and poach good talent.

158. Consider one example of the technical skills required for SCPEC to prosper. All competition agencies depend heavily on legal analysis and advocacy to formulate cases that will withstand review in the national courts. This need is especially acute in relatively new competition agencies, such as Armenia, which face basic, recurring challenges to their jurisdiction, their information gathering powers, and their remedial authority. There are enough similarities in the experience of new competition authorities to envision these agencies as having a life cycle whose first phase involves crucial litigation battles whose outcome determines future success. The nature and timing of these battles has become fairly predictable, and the arguments raised by private firms against the competition agencies have a striking measure of uniformity across jurisdictions.

159. SCPEC is mainly an agency of economists. It has a capable head of legal services, but it has a comparatively small number of lawyers as a percentage of its professional staff. To meet the litigation challenges it faces and to succeed in defining and defending the perimeter that protects its core areas of authority, SCPEC must draw upon outstanding legal talent proficient in administrative law, civil procedure, forensic advocacy, and competition law. Creating a good legal team does not come on the cheap. SCPEC either must hire more of these individuals to join its own staff or take the still more expensive step of retaining outside counsel to represent it in court. A decision to skimp on this necessary investment in human talent exposes SCPEC to legal setbacks that can severely restrict its effectiveness for years to come. It is not necessary for SCPEC to win all of its cases, but it must prevail often enough to protect core areas of authority and, more generally, to establish its credibility as an enforcement body.

160. This is simply one respect in which SCPEC must build a talent pool that is equivalent in sophistication and technical acumen as that assembled by the Central Bank and the public utility regulator. Despite similarities in the analytical challenges faced by SCPEC, the Central Bank, and the public utility regulator, the latter two institutions stand on much better footing when it comes to resources. The Central Bank and the public utility regulator pay decidedly higher salaries,

sustain training programs that enable staff to attend high quality seminars and other instructional programs outside of Armenia, and take other steps to support career development and make their organizations attractive to new candidates and existing employees. Interviews with several experts indicated that the World Bank had been instrumental in ensuring that the public utility regulator received premium salaries.

161. The disparities in treatment also extend to resources needed to build and sustain a first-rate infrastructure of communications and information management technology. International experience shows that even comparatively small agencies can improve productivity greatly with wise investments in state-of-the-art communications systems, computer networks, and electronic data bases. Among other benefits, a first-rate information technology system enables agency employees to have access to an impressive and growing body of materials on competition law that is now accessible electronically across the world. These materials include professional journals, academic papers (e.g., through the Social Science Research Network), competition policy blogs,<sup>45</sup> reports and proceedings of international organizations and networks (e.g., the work product of UNCTAD, the Organization for Economic Cooperation and Development (OECD), and the International Competition Network (ICN), and cases, guidelines, and reports by other competition agencies. The materials recited here are only a subset of what is available. To a striking degree, access to web-based information sources has obviated the need for a competition agency to develop and maintain a traditional collection of hard copy journals, reports, and books. Some of these materials are useful and necessary, but much of what occupies the shelves of traditional library collections now can be had at a computer terminal.

162. Some online resources are free of charge and some (such as access to the LEXIS-NEXIS data base) are not. At no cost SCPEC can access the vast body of literature and practical information provided by public institutions and not-for-profit organizations. For proprietary systems, there is an evident solution. Donor organizations can provide extremely valuable contributions in the form of subsidies to enable SCPEC to purchase subscriptions to these sources. This is in addition to the useful boost in capacity that donors can supply by equipping SCPEC with a state-of-the-art computer network that provides a computer terminal to all or most of the agency's employees.

163. These tools multiply the effectiveness of individual employees, enable the agency to achieve better control over the flow of information needed for law enforcement and related tasks, and to create an institutional memory that preserves knowledge and captures experience that otherwise might evanesce with the departure of top officials and staff. SCPEC functions today with a suite of personal computers that is a full generation behind what is available to the Central Bank and to the public utility regulator. It is difficult to overstate the benefits that would flow from correcting this disparity and putting SCPEC on a par with many other transition economy authorities within the same age range (i.e., ten years old or less) which have enjoyed major productivity gains from investments in information services technology.

164. Additional financial support could come from several possible sources. The Central Bank and the public utility regulator both fund operations from user fees collected from institutions subject to their oversight. One way for SCPEC to augment its salaries would be from modest registration fees imposed on firms subject to merger notification requirements. Another means would be for SCPEC to receive funds generated by a charge that would accompany other routine filings made with public authorities, such as filings made with the securities regulator or to levy annually a small fee from registered companies. An appropriate exemption for small and medium-

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<sup>45</sup> An especially useful source of this type is the Competition Policy Blog managed by Professor Danny Sokol of the University of Florida Law School.

sized enterprises would allow to take their specific economic status into account. Another more direct approach is for the legislature to directly increase SCPEC's appropriation. Donor institutions also continue and extend past practice by covering discrete infrastructure needs (such as US AID's funding of computers and of English language translations of SCPEC documents for placement on SCPEC's website) or training and factfinding exercises (such as GTZ's support for a recent study tour that brought officials from SCPEC and the public utility regulator and judges from Armenia's courts to meet with counterpart institutions in Germany).<sup>46</sup>

### 3.4 Relations with the legislature and the executive

165. New competition authorities quickly discover that the actions of various other government departments affect their ability to implement competition policy. For example, sector regulators often have concurrent authority for some competition policy issues and may have exclusive power to apply competition policy to certain types of behaviour. Other government institutions routinely make decisions that influence competition by determining which enterprises can enter specific markets. To operate effectively, a competition agency must build relationships with these public instrumentalities to determine the application of concurrent authority and to advocate the adoption of precompetitive policies.

166. SCPEC has launched a number of efforts to establish relationships with government agencies whose actions affect competition. It has signed memoranda of understanding to coordinate operations with the Central Bank, the procurement office of the Ministry of Finance, and the public utilities regulator. These measures are a useful first step toward developing the deeper cooperation that will be required to give competition policy concerns a stronger footing in the programs of other public institutions. Compared to the status quo in the middle of the previous decade, SCPEC has made considerable progress in building links with other regulatory authorities whose decisions significantly affect competition. It is also apparent that SCPEC has achieved notable success in raising the awareness of other regulators concerning competition policy questions.<sup>47</sup>

167. Earlier sections of this report have described how SCPEC's success in achieving broader competition policy objectives will be a function of its success in working with other public institutions whose policy choices shape the competitive environment. Five relationships warrant continued and, in some instances, expanded attention.

#### 3.4.1 Legislature

168. Some steps proposed above will require legislative action in the form of amendments to Armenia's competition law (e.g. as regards the need for strengthened investigation powers), increases in SCPEC's budgetary appropriations, and expressed support for SCPEC's participation in policy making by other government institutions, such as the public utility regulator. Legislative assistance of this type ordinarily does not emerge spontaneously. SCPEC can play a major –

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<sup>46</sup> Further projects to the benefit of the SCPEC are carried out with support from AECPLAC, the World Bank, and the OSCE.

<sup>47</sup> During interviews conducted in 2004, for example, SCPEC leadership identified as a major goal the creation of mechanisms to promote collaboration with other regulators and with ministry offices that deal with matters such as public procurement. Those types of relationships were largely lacking at that time, and the existing state of affairs shows that SCPEC has made noteworthy progress on this front, notwithstanding challenges that remain.

indeed, necessary – role in setting a foundation for these steps by explaining to legislators why specific reforms and other forms of support serve to increase economic progress in Armenia.

### 3.4.2 Ministry of the Economy

169. In interviews, Ministry officials articulated a vision of competition policy that emphasized the promotion of new entry as a means to increase rivalry and economic performance. Rather than SCPEC initiatives that focused heavily on conduct by existing firms, the Minister proposed an entry-oriented approach would rely on new investment – especially new outlays from abroad – to increase competition.

170. There is a useful role for SCPEC in participating with the Ministry in general discussions about this framework and about specific initiatives that might be taken to realize it. The promotion of pro-entry policies fits neatly into SCPEC’s advocacy role, and SCPEC can contribute substantially to the analysis of existing barriers to new investment and the development of ways to reduce these obstacles.

171. SCPEC’s participation in the Ministry’s pursuit of a pro-entry competition policy would serve another useful purpose. SCPEC could use regular interaction with the Ministry to drive home an important point. SCPEC’s concern with anticompetitive behaviour by incumbent firms – especially well-entrenched dominant enterprises or oligopolies – is best seen as a complement to, and not a substitute for, measures that would accomplish the Ministry’s pro-entry strategy. Foreign investors are likely to be reluctant to invest in sectors in which incumbents exercise absolute or nearly-complete control and face no effective constraints in using improper means to assert their pre-eminence. The prospect of active and effective enforcement of Armenia’s competition law is likely to provide an important assurance to potential investors that incumbents cannot swiftly stifle new enterprises by improper exclusionary tactics.

### 3.4.3 Public Services Regulatory Commission (PSRC)

172. In most other countries, the nature of the relationship between competition law and sector regulation is an important determinant of the quality of competition in energy, telecommunications, and other sectors that feature substantial public utility oversight. It the relatively rare jurisdiction in which jurisdictional boundaries are well defined and in which relations between the competition agency and the sector regulators are harmonious.

173. Armenia fits within the mainstream of nations in which difficult jurisdictional issues abound and tensions between the competition authority and sector regulators are significant. Within the past year, SCPEC and the PSRC have signed a memorandum of understanding (MOU) that provides a general framework of cooperation between the two agencies. On its face, this instrument might appear to be a useful platform for building a better relationship. Interviews indicated that SCPEC and the PSRC must surmount a number of hurdles before the promise of the MOU will be realized.

174. One difficulty is that the PSRC regards the MOU as a formality that had to be completed and not as a foundation for future progress. This view reflects the underlying tensions between the PSRC and the SCPEC and the challenges for a participation of the SCPEC in formulating competition policy for telecommunication service providers and for other firms subject to PSRC’s oversight. The PSRC Commissioner said the conduct of “natural monopolies” was or should be the exclusive preserve of his agency. He defined the zone of exclusivity to encompass all conduct on the part of energy, gas, railroad, and water companies. He acknowledged that the

telecommunications sector features important elements of competition. At the same time, he said the PSRC was capable of taking account of all competition issues, including matters such as mergers involving providers of mobile telephony services. A key foundation for this interpretation of the PSRC's jurisdiction (and its pre-eminence in competition policy for sectors it oversees) is its role in issuing licenses that the regulated firms must obtain to operate.

175. The PSRC Commissioner's comments display a perspective observable in many other jurisdictions in among sector regulators – namely, a tendency to equate the success of the sector with the prosperity of the traditional incumbent service provider. In a separate interview an Armenian internet service provider, a competitor of the traditional incumbent telecommunications company, said the PSRC was more concerned with taking steps that ensured the well-being of the incumbent than with adopting policies that promoted superior performance in the sector – for example, to allow new entry or expansion by fringe firms which might grow to displace the incumbent. The respective executive also noted the PSRC's dismissive attitude toward SCPEC.

176. The PSRC unmistakably enjoys substantially greater resources than SCPEC, and it has been able by all accounts to recruit a qualified staff. The PRSC's specialization has enabled it to develop relatively greater expertise in the technical features of the sectors subject to its authority. The PSRC appears to believe that its resources, expertise, and responsibility for licensing market participants ought to divest SCPEC of any role in applying competition policy for Armenia's regulated utilities.

177. This assessment seems unwise. SCPEC has a valuable part to play in ensuring that the competition policy considerations receive careful attention in the formulation of policy in these sectors. This applies to the treatment of specific forms of conduct – e.g., abuse of dominance, horizontal agreements, mergers, and vertical restraints – and to the question of how PSRC's authority for network management can be exercised in a way that gives Armenia the benefits of rivalry with respect to price and nonprice features of performance. Taken into account that the Act does not exclude regulated industries from its application, SCPEC's exercise of parallel jurisdiction with respect to some matters and its advice as an advocacy for competition policy can serve as a useful antidote to perspectives that regard the health of traditional incumbent suppliers to be the central aim of policy making and downplay the value of new entry as a stimulant for progress.

178. In this light, the existing MOU between the PSRC and SCPEC should not be seen as a regrettable formality that lacks practical significance. Rather, it should provide a platform for active, routine consultation between the two institutions. Shared jurisdiction should be treated as an opportunity to ensure that competition policy considerations are core elements of policy making for the affected sectors. This recommendation reflects a large body of international experience that underscores the benefits of engaging the competition authority in (1) policing anticompetitive practices, (2) seeing that routine public utility regulatory tasks are performed in a manner that imposes the fewest possible limits on competition, and (3) promotes periodic reassessment of whether areas designated by law as reserved exclusively for the incumbent provider ought, in light of technological change or other factors, be opened for entry.

179. The type of engagement envisioned here does not come automatically. Experience in many jurisdictions shows that tensions often besets the relationship between competition authorities and sector regulators. Armenia would be genuinely unusual if the PSRC and SCPEC regarded each other with nothing more than mutual admiration and approached collaboration on

shared tasks with enthusiasm. Interagency tension in this domain of policymaking is the norm. The question is how to diminish it to enable fruitful cooperation to take place.

180. Several measures promise to foster progress in this respect. The first is to use the MOU to increase contacts between the PSRC and SCPEC at three levels: by top leadership, by senior managers, and by case handlers. Many devices can serve this purpose. One necessary step is the formation of a working group or similar arrangement that supplies a clear means for regular communication and discussion between the two institutions. Another approach, tested successfully in many countries, is to use staff secondments across agencies to build understanding and improve working relationships. Still a further step is to have the PSRC and SCPEC case handlers can participate in joint workshops that explore matters of common concern, such as the definition of relevant markets and the measurement of market power in the telecommunications sector. Top leadership or senior management can participate together in exercises such as the recent GTZ-sponsored study tour to Germany, where PRSC and SCPEC officials together learned of German experience in addressing the interface between competition law and public utility regulation. Measures taken between the two institutions usefully can be supplemented by enlisting the participation of bodies outside the government, including academics, consumer groups, and business organizations.

181. Efforts to take account of comparative experience are likely to enrich all of these exercises. Perspectives drawn from foreign experience will help the two agencies anticipate points of friction and devise steps to reduce tensions. The approaches suggested above take account of international experience and, to a large degree, have been “road tested.”

182. A further ingredient of improvements in the PSRC and SCPEC relationship involves resources. A competition agency cannot do good work in the regulated industries field without having a sound understanding of the affected sectors. This base of knowledge not only enables the competition agency to develop sensible policy in the regulated sectors but also gives the agency needed credibility in its dealings with the sector regulator. There is an observable tendency internationally for sector regulators to view competition agencies with suspicion on the ground that the competition authority approaches problems with a badly imperfect understanding of the regulated sectors and therefore is prone to misdiagnose observed phenomena and prescribe mistaken policy solutions. By increasing its own expertise, the competition agency can alleviate this concern.

183. The competition agency need not match the sector regulator person for person in all relevant areas of expertise. It does, however, require a critical mass of technical skill regarding the history of the sector, the services it provides, and the business considerations that guide firms in the field. Building the requisite levels of skill within the competition agency cannot be done on the cheap. This is a further reason to take measures, discussed above, to augment the means available to SCPEC to recruit, train, and retain capable staff. Put another way, SCPEC’s engagement with the PSRC will be effective only if SCPEC can bring the right human capital and institutional knowledge to bear in the collaboration.

#### 3.4.4 Central Bank

184. The Central Bank and SCPEC have shared interests in the fields of competition law and consumer protection. The two institutions have established an MOU to promote regular discussions. This framework appears to have established effective cooperation between the organizations.

### **3.4.5 Procurement Office of the Treasury**

185. SCPEC has developed a cooperative relationship with the Treasury's public procurement office,<sup>48</sup> which has developed over time to include the formation of a joint SCPEC/Treasury working group on procurement policy. This cooperation can still be strengthened in various ways. A valuable element of this partnership would be the formation of training programs to enable procurement officers to spot bid-rigging and corruption. The implementation of training projects can employ materials produced in recent years by UNCTAD, the ICN and the OECD, which have prepared highly practical checklists and related guidance on competition law for procurement officials. A further ingredient of the partnership is to assist in the establishment of protest procedures by which potential or actual bidders can contest the creation of unduly restrictive bidding specifications or challenge irregularities in the contract award process.

186. Combined with SCPEC's own law enforcement efforts, an expanded program of cooperation with the Treasury's Procurement Office can have significant economic benefits for Armenia. The state plays a significant role as a purchaser of goods and services, and even small improvements in performance can have a major impact on the quality of life for Armenians.

### **3.4.6 Toward a Domestic Competition Network**

187. As discussed above, there are a significant number of government institutions with a major hand in shaping the competitive process in Armenia. Many of these are regulatory bodies or ministries with direct responsibility for competition policy within their own spheres of activity. There are a number of common issues that link many of these institutions together – for example, the design of a suitable methodology for defining relevant markets. This presents a reason for SCPEC to convene meetings of regulatory officials with common interests, perhaps under the auspices of what might emerge to become a domestic competition network. By regular interaction and through routine contacts among agency leaders and case handlers, it may be possible to achieve greater understanding among these government bodies about the tasks and initiatives each is pursuing, greater coordination of activity, and progress toward coherent competition policy programs.

### **3.5 Cooperation with Non-Government Organizations**

188. Successful competition policy systems depend heavily on the contributions of non-government institutions such as business organizations, consumer groups, professional societies, and universities. These organizations can play a valuable role in educating various constituencies about the requirements of competition law, in creating networks that collect and transmit complaints concerning alleged infringements of the competition law, in training competition policy experts, in performing research relevant to competition policy, and in building public support for the work of the competition agency. Non-government organizations assume particularly great significance amid conditions of budgetary austerity, where the competition agency may be able to extend its presence only through collaborative efforts with outside groups.

189. In its first decade, SCPEC has taken important steps to build effective relationships with non-government organizations. As discussed in more detail below, additional efforts along these lines could increase the agency's effectiveness.

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<sup>48</sup> Department of Procurement Process Regulation and Budget Execution Methodology within the Ministry of Finance.

190. Many observers interviewed for this study emphasized that SCPEC cannot accomplish its aims by acting alone. It must engage the resources and contributions of institutions outside its own walls. Three focal points of cooperation stand out. Each involves nongovernment institutions indigenous to Armenia: business organizations, consumer groups, professional associations, and universities.<sup>49</sup>

### 3.5.1 Business Organizations

191. An interview with the President of the Union of Manufacturers and Businessmen of Armenia revealed possibilities for collaboration that would increase SCPEC's effectiveness in expanding awareness of competition policy and mobilizing support for the application of Armenia's competition law. The official emphasized the potential value of the ACPS in promoting entry and expansion by smaller and medium sized firms.

192. The suggestion there is not that the interests of SCPEC and the business community are congruent. Nor should one regard Armenia's business community to be a single-minded, homogeneous entity. Nonetheless, there is an evident realization among a number of business operators that the application of the competition law serves valuable ends in promoting competition on the merits, setting clear and transparent rules for commerce, curtailing the incidence and influence of destructive alliances between private interests and public decision makers, and discouraging harmful government interference that reinforces the position of large incumbent suppliers to the disadvantage of new entrants or fringe firms seeking to expand.

193. Business organizations can be useful vehicles for educating firms about the aims of competition policy, for spelling out the obligations of business operators under the law, for making known mechanisms by which commercial entities can gain guidance about the requirements of the law, and for establishing lines of communication through which aggrieved enterprises can submit complaints about apparent violations. Seen this way, business associations function as part of a two way information network through which the competition agency makes known its own expectations and intentions and the business community provides feedback about the operation of the law and about possible infringements.

### 3.5.2 Consumer Groups

194. The president of one major consumer NGO had a very positive assessment of SCPEC and praised its willingness to work with SCPEC. This view indicates an important area of improvement in SCPEC's relationships with external groups over the past five to six years.<sup>50</sup> He noted a number of instances in which SCPEC and his NGO, in effect, had coordinated activities to improve the detection of infringements of the competition policy and consumer protection commands of the competition laws and to increase public awareness of SCPEC's work. He suggested that SCPEC could increase its effectiveness by working more extensively with NGO's to facilitate the identification of possible violations and to engage in public education. He also described how a more concerted, proactive media strategy would enable SCPEC to expand its base of support among consumers.

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<sup>49</sup> We treat Armenia's academic institutions as "nongovernment" bodies even though many of these are publicly funded bodies.

<sup>50</sup> A major theme of the competition policy conference conducted in Yerevan in August 2004 was the lack of SCPEC interaction with the public generally and with NGOs that deal with consumer issues.



### 3.5.3 Professional Societies

195. Armenia has a small number of legal practitioners who specialize in competition law. Experience in other jurisdictions has shown how the legal profession and the organized bar can serve as useful conduits to the business community to channel information about competition law and can play a valuable role in promoting compliance among business operators. Even at this still very early stage of the development of a legal community of competition law practitioners, it could be helpful to SCPEC to treat the bar as an element of its outreach programs and to see it as a sounding board for views concerning the implementation of competition policy.

### 3.5.4 Universities

196. An interview with the Rector of the Armenian-Russian Slavonic University pointed to a number of ways in which stronger links between SCPEC and the academic community could improve the operation of the ACPS. In many jurisdictions, universities provide key elements of the intellectual infrastructure that supports the operation of an effective competition policy system. They train individuals who will practice in the field of competition law; a number of these individuals become employees of the competition authority. They provide interns who work in the competition agency – a measure that can augment SCPEC’s resources without any cost to the agency’s budget and assist SCPEC in recruiting new talent. They conduct research that can improve an agency’s understanding of the economy, strengthen the development of doctrine, and identify possible areas for enforcement and advocacy programs.

197. This relates to a phenomenon observable in the larger community of jurisdictions with new competition policy systems. To achieve and sustain success, a competition policy system must draw upon the support of a strong indigenous academic capacity. Among other critical functions, the academic infrastructure provides instruction in economics and law and to perform research. The durability and quality of the competition system are, in important ways, functions of the strength of the local intellectual infrastructure. The contributions of outside experts and policy analysts can be informative supplements to the indigenous capacity, but efforts to build a truly effective system will fail if the outsiders serve as the principal source of ideas and training.

198. SCPEC should view the university community as a potential partner in its operations. Through informal and formal contacts, SCPEC can build relationships that encourage the teaching of courses in competition economics and law and, consistent with international practice, can make its staff available to assist in the formulation and teaching of such courses. SCPEC can encourage faculties of economics and law to undertake research that informs the development of competition law. These relationships also supply a basis for SCPEC to recruit the best students.

199. The longer term goal should be to establish a three-way partnership involving SCPEC, Armenia’s universities, and the donor community. A major focus of this partnership should be the creation of a research council or similar device to share information about research projects and to identify promising areas of research activity. The research council should focus on encouraging the development of Armenian researchers and promoting their participation in donor-sponsored research projects. From this and related activities could emerge the development of a research agenda that focuses on identifying root causes of competition problems in the Armenian economy and uses the findings to formulate programs – including competition law enforcement, advocacy, or other adjustments – to correct the problems.

#### **4. INTERNATIONAL COOPERATION AND CAPACITY BUILDING**

**200.** A further important way for SCPEC to increase its effectiveness is to draw upon learning and resources available outside Armenia's borders. SCPEC fully understands the necessity of building these relationships. The agency is actively involved in international organisations and networks such as UNCTAD, the CIS, ICN, and the OECD regional centre. It is also engaged in projects with the Organization for Security and Co-operation in Europe, the EU (in particular EU Twinning project), the World Bank and the GTZ. These commitments are well-chosen, and the continuation of efforts to work within these networks is a worthy endeavour.

**201.** The crucial factor in realizing the benefits of integration into the international community of competition agencies, donors, advisory panels, academic institutions, and think tanks is not the intensity of SCPEC's commitment. The main determinant of success on this frontier will be the international institutions and individual jurisdictions with whom SCPEC works. SCPEC is doing its part, and it is the responsibility of the external community to increase the level of assistance and improve the skill with which specific initiatives are carried out.

**202.** Major contributions from the international community could come in various ways: training for professional staff that emphasizes practical techniques for conducting investigations and developing cases; assisting in the drafting of amendments to the competition law and the preparation of secondary legislation and guidelines; providing guidance in the establishment of effective procedures for management and operations. Assistance on all of these fronts can be applied in a variety of ways: through programs conducted in Armenia, through study tours, through stipends for graduate study at foreign universities, through funding for secondments with foreign competition authorities.

**203.** Donors also can make major contributions through projects that, in effect, supplement the operating and capital budgets of SCPEC. There could be supplements for salaries or grants that fund specific personnel slots. Donors could make grants that enable SCPEC to retool its information technology system (including the acquisition of new computers and software). Assistance in translating documents into English would be valuable to improve external understanding of SCPEC's work and facilitate its cooperation overseas. Donors also can provide resources to conduct economic research that diagnoses competitive problems in individual sectors and suggests projects for SCPEC law enforcement or advocacy.<sup>51</sup> These studies not only can make useful contributions to SCPEC's base of industry specific knowledge, but the exercise of performing them can increase the agency's technical capacity to do additional work in the future.

**204.** The positive contributions of external entities to the future success of SCPEC and the ACPS generally will increase if the entities formulate programs that are long-term in nature and result from extensive coordination and consultation among external groups and with SCPEC. This seems to be the philosophy that animates GTZ's projects concerning competition policy in Armenia. GTZ managers observed that the efforts of GTZ and other donors will have the greatest impact if they are not one-offs and instead involve continuous engagement that extends for many years. GTZ also underscored how it is seeking to engage SCPEC in more actively specifying its needs and directing donors to serve them – in effect, devolving coordination tasks to the recipient rather than counting on donors to do it themselves. This is a helpful development, yet we also see a need for donors to better cooperate in the formulation of programs.

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<sup>51</sup> One example of this type of research is a project funded by Canada's International Development Research Centre in 2007 to examine Armenia's distribution sector. See SCPEC, 'Competition Issues in the Distribution Sector in Armenia' (2007).

## 5. FINDINGS AND POLICY RECOMMENDATIONS

205. The main finding of this report is that in Armenia 'political and economic context' provides more than mere framework; it is central to understanding the current practice and future of competition law and policy. The full benefit of competition policy will not be attained unless fundamental reforms to the relationship between executive government and business are undertaken.

### *Political and economic context*

206. The two fundamental facts of Armenia's economic and political system, which influence every aspect of the country's public life including its competition law and policy, are, firstly, its past as a centrally planned economy within the Soviet Union, and secondly, its geo-political situation in the South Caucasus region, specifically the conflict-ridden relationship between Armenia and its neighbours Azerbaijan and Turkey.

207. High levels of concentration, which are significantly influenced by the limited points of entry and exit for the import and export of goods strongly characterize Armenia's economy. The physical limitations on trade routes make it relatively easy to capture and, hence, monopolise trade in important products. This appears to be accompanied by a weak and compromised customs service, which leads to a significant underreporting of trade, which, given its relative importance in economic life, results in a significant under-reporting of overall economic activity. In addition, Armenia struggles with what is called the shadow economy. That is effectively formal sector activity that is not reported to the authorities principally in order to enable the trader or the producer to evade the payment of taxes and import duties. Most common estimates reckon that 40%-50% of formal sector activity is undeclared. Hence, by any measure a significant slice of Armenia's economic activity is subject to neither corporate tax, nor import duties nor social taxes.

208. Where economic activity is frequently under-reported, the inevitable outcome – indeed the very purpose of underreporting - is that the dominant incumbents who have successfully monopolised key markets pay lower taxes and customs duties by taking advantage of loopholes afforded to them by imperfections in the law. This not only impacts on the public finances – and hence on the ability of government to build effective institutions such as competition agencies, regulators and, indeed, customs and revenue authorities themselves – but it also gives the incumbent monopolist a strong competitive advantage vis-à-vis actual or potential rivals, thus further entrenching high levels of concentration and single firm dominance.

209. In order to increase the level of competition in Armenia's economy, it is indispensable to alter the structure of its highly concentrated markets and to stop the large-scale underreporting by certain firms, which results in competitive advantages for those who are non-compliant with tax and customs regulations. However, frankly spoken, mere competition law enforcement will not be sufficient to remedy these two issues. As detailed below, a common endeavour of key governmental stakeholders is needed to design and implement a competition policy aimed at facilitating new entry and improving the overall competitive situation in Armenia.

### *Legislative framework*

210. Despite several reforms, the legal framework of the ACPS has remained markedly defective in key aspects. Substantive provisions dealing with anti-competitive agreements, the abuse of a dominant positions and merger control require significant revision. Most importantly,

however, the investigatory powers accorded to the SCPEC are insufficient and do not allow the SCPEC to effectively fulfil its mandate to fight anti-competitive conduct.

#### *The SCPEC's resources*

211. In addition, to the deficiencies of the Act, the budget and overall resources of the SCPEC do not suffice to carry out satisfactorily the authority's operations and activities. The SCPEC does not dispose of the financial means to attract and maintain the highly qualified personnel that it needs to handle complex competition law cases. Neither is the SCPEC in a position to invest in staff development and training and equipment.

212. While the overall situation under which the SCPEC operates appears more than challenging, there are also reasons to believe that Armenia may overcome the various hurdles restricting the development of more competitive markets. Key government stakeholders, including the Prime Minister and the Minister for Economy are willing to lend their support to the SCPEC and there appears to be a growing conviction that strong competition law and policy are indispensable for the country's economic development.

213. This political support needs to translate into a common endeavour of all key governmental stakeholders to design and implement a competition policy aimed at facilitating new entry and improving the overall competitive situation in Armenia. While an adequately resourced, technically competent and publically supported competition authority will be at the centre of this effort, co-operation with a range of collateral public institutions and civil society, promoted by high level governmental support, will be critical determinants of the ability of the competition authority to confront unrestrained market power.

214. This common endeavour constitutes the core recommendation of the present report. In order to give guidance as to the most important steps that shall result from this common endeavour, the report recommends a number of specific measures. The respective recommendations are intertwined in the sense that they will only result in the desired success if implemented as a package. For instance, the success of increased investigation powers will depend on the availability of technically well-trained and well-equipped personnel to use these powers. Thus, the strengthening of the SCPEC's investigatory powers needs to go hand in hand with an increase of its resources.

215. Below the report's specific recommendations are set out according to whether they are addressed to the legislature, to the government or to the SCPEC.

#### 5.1 Recommendations addressed to the legislature

The recommendations addressed to the legislature fall into two main categories: firstly, proposed amendments to substantive provisions of the Act, some of which will render the Act clearer and thus easier to enforce, and others which will help to adjust the SCPEC's functions to the core aspects of competition law enforcement; secondly, proposed amendments that aim at strengthening the SCPEC's investigatory powers and improving the legal conditions under which it carries out investigations.

### 5.1.1. Proposed amendments to substantive provisions of the Act

#### **R 1: Abolish the register for dominant companies**

- *It is recommended to abolish the register for dominant companies and to carry out targeted market studies in sectors where an abuse of dominance is suspected based on complaints or general market intelligence.*
- *As an interim measure, it is further recommended to clarify that Articles 6 and 7 do not stipulate that the registration of a company as dominant is a prerequisite for the prosecution of an abuse of a dominant position.*

While the abolishment of the register for dominant companies will lead to the loss of one of the main sources of the SCPEC's market intelligence today, this recommendation needs to be read together with the recommendation to strengthen the investigatory powers of the SCPEC and thereby to allow for alternative tools of information gathering.

#### **R 2: Revise the definition of dominant companies**

- *It is recommended to carefully check whether the Armenian wording of Article 6 allows to interpret the market share thresholds as triggering a refutable presumption of dominance. If this is not the case, it is recommended to amend Article 6 in a way that allows companies to prove that they are not dominant despite reaching the market share thresholds stipulated by Article 6.*

#### **R 3: Revise the prohibition of anti-competitive agreements**

- *It is recommended that Article 5 be broken up into two separate articles, the first dealing with horizontal agreements, the second dealing with vertical agreements.*
- *It is also recommended that the list of prohibited horizontal agreements be shortened and simplified, identifying those core offences – price fixing, market allocation and bid rigging – that are widely accepted to cause anti-competitive harm.*
- *These should be defined as per se illegal, whereas other forms of horizontal agreements, as well as vertical agreements should be subject to the rule of reason.*

#### **R 4: Revise the provisions governing Armenia's merger control regime**

- *It is recommended to firstly assess whether the Act's notification thresholds for merger control are appropriately crafted to catch those transactions that potentially lessen competition in Armenia. Most probably, the notification thresholds will need to be adjusted, in which case it is recommended to introduce turnover-based thresholds rather than asset-based thresholds.*
- *Secondly, the substantive test for the assessment of mergers should be amended to include the strengthening of a dominant position in addition to the creation of a dominant position.*
- *Thirdly, it should be clarified that the fines for a failure to notify a concentration also include the possibility that the SCPEC order the rescission of a consummated merger that creates or strengthens a dominant position.*
- *Fourthly, the notification and assessment procedure should be spelled out in more detail - either in the Act or in secondary legislation.*

#### **R 5: Limit SCPEC's role with respect to state aid to an advisory function**

- *It is recommended to limit the SCPEC's role to an advisory function in the field of state aid. In order to allow the SCPEC to exercise this advisory function, appropriate consultation mechanisms need to be established.*

#### **R 6: Introduce margin of discretion for setting fines and increase maximum level of fines for hard-core cartels**

- *It is recommended that the SCPEC is being accorded a certain margin of discretion when setting fines for violations of the Act.*
- *It is also recommended that the Act or secondary legislation specify guiding principles for the use of this discretion, e.g. by stipulating that the amount of the fine shall relate to the turnover affected by the anti-competitive behaviour and by determining aggravating or mitigating factors.*
- *Furthermore, it is recommended to increase the maximum level of fines for hard-core cartels.*

#### **R 7: Revise provisions on unfair competition**

- *It is recommended to revise the provisions on unfair competition to render them more concise and thus easier to implement.*
- *Furthermore, it is recommended to revise the level of fines for acts of unfair competition.*

#### **5.1.2 Proposed amendments relating to the SCPEC investigatory powers and the investigation procedure**

As mentioned earlier, it is crucial to improve the legislative framework under which the SCPEC prosecutes anti-competitive behaviour. To date, the weak enforcement powers of the SCPEC do not only negatively affect the prosecution of anti-competitive conduct, but also result in an overuse of the SCPEC's resources for collecting market information via the register of dominant companies.

#### **R 8: Strengthening the SCPEC's investigatory powers**

- **It is recommended to empower the SCPEC's to carry out unannounced inspections (so-called down raids), when there is a justified suspicion that evidence for anti-competitive conduct may be found in a company's premises.**
- **Accordingly, also the current limitation of the objectives for an inspection of the SCPEC contained in Article 19 (1) c needs to be abolished and several provisions of Law on Organising and Conducting Control in the Republic of Armenia of 17 June 2008 need to be amended.**

Concerns that such power implies the risk of abuse can be addressed through appropriate judicial oversight and special training of the SCPEC's personnel.

#### **R 9: Allow for a longer investigation period**

- *It is recommended to set an initial investigation period of at least six months, which shall be extendable upon decision by the board of Commissioners.*

#### **R 10: Create legal basis for leniency programme**

- *It is recommended to complement the strengthened investigatory powers of the SCPEC by the introduction of a leniency programme to facilitate discovery of cartels.*

#### **5.2 Recommendations addressed to the government**

#### **R 11: Adopt and implement a comprehensive competition policy**

- *It is recommended that under the leadership of the Minister for Economy and with support from the Prime Minister and Cabinet, the SCPEC and other key government bodies, such as the tax and customs authorities and the PRSC embark on a common endeavour to design and implement a comprehensive competition policy for Armenia.*
- *A comprehensive competition policy for Armenia needs to address barriers to entry, high concentration levels in a large number of important markets, performance of key government institutions and other factors that restrict competition in Armenia today.*

#### **R 12: Increase the SCPEC's resources**

- *It is recommended to increase the SCPEC's resources to a level that allows the SCPEC to effectively fulfil its mandate.*

Possible ways to finance a budgetary increase are set out under point 3.3 of this report.

#### **R 13: Facilitate and promote cooperation on the enforcement level between various governmental stakeholders in the ACPS**

- *It is recommended that the government encourages and supports cooperation and exchange of experience on the enforcement level between the SCPEC, the Administrative Court and the PSRC, as well as between the SCPEC and the tax and customs authorities.*

While the SCPEC has started initiatives for such cooperation, it will need ministerial back-up for these initiatives to be fruitful.

#### **5.3 Recommendations addressed to the SCPEC**

#### **R 14: Readjusting priorities and strategies for law enforcement**

- It is recommended that the SCPEC continue prosecuting anti-competitive behaviour that relates to products of the basic "market basket" that Armenian consumers purchase in their regular shopping.
- In addition, it is recommended that in building a portfolio of litigation programs, the SCPEC consider giving greater emphasis to the following types of enforcement matters:
  - Bid-rigging and other collusion cases involving distortions of the public procurement process.<sup>52</sup>

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<sup>52</sup> This form of initiative would build on SCPEC experience that goes back to the middle of the previous decade, when SCPEC used information gained from the finance and transport ministries to identify suspicious patterns of tendering on public contracts for road construction and maintenance.

- Abuse of dominance or other cases involving infrastructure sectors such as energy and transport, where even small improvements in performance would have broad economic and social benefits.
- It is recommended that the SCPEC spend less resources on analysing data submitted by companies registered as dominant when there are no hints for a potential abuse of their dominant position.
- Furthermore, it is recommended that enforcing the Act's merger control provisions paired with related advocacy measures become one of the SCPEC's enforcement priorities once the legislative basis for merger control has been improved.

**R 15: Enhance staff development and training**

- *It is recommended that the SCPEC increase staff development and training activities. Ongoing training for the SCPEC's personnel and Commissioners complemented by the participation in workshops and conferences outside Armenia are crucial in order to ensure that the SCPEC's professional staff and its Commissioners benefit from the knowledge and skills required to carry out their tasks.*

**R 16: Undertake competition advocacy aimed at other government bodies**

- *It is recommended that the SCPEC engage more expansively in encouraging other government bodies to adopt pro-competitive policies.*
- *The SCPEC's advocacy efforts should mainly target other government institutions whose decisions directly affect the competitive process – e.g. public procurement offices and the PRSC.*
- *In addition, it is strongly recommended that the SCPEC continue engaging in a dialogue on competition law enforcement with the Administrative Court.*

**R 17: Strengthen public disclosure and outreach**

- *It is recommended that the SCPEC build a solid network of partnerships and relationships with bodies outside the government to increase its effectiveness. Focal points for these efforts include relations with the media, links to universities and academic research bodies, and ties to civil society organizations (such as consumer groups).*
- *It is recommended to use the opportunity presented by the tenth anniversary of the founding of SCPEC to organize a series of events – a conference, seminars, workshops – that not only would celebrate the work of the ACPS to date but would engage experts in Armenia and from other countries to suggest paths for future policy development.*
- *Furthermore, it is recommended that the SCPEC diversify its advocacy tools by using all media for its awareness- raising activities such as publications and discussions broadcasted on TV.*



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