

Azerbaijan

RISK & COMPLIANCE REPORT

DATE: March 2018

Executive Summary - Azerbaijan

Sanctions:	OSCE - Weapons
FAFT list of AML Deficient Countries	No
Higher Risk Areas:	US Dept of State Money Laundering assessment Not on EU White list equivalent jurisdictions Corruption Index (Transparency International & W.G.I.) World Governance Indicators (Average Score) Failed States Index (Political Issues)(Average Score)
Medium Risk Areas:	Non - Compliance with FATF 40 + 9 Recommendations
Major Investment Areas: Agriculture - products: cotton, grain, rice, grapes, fruit, vegetables, tea, tobacco; cattle, pigs, sheep, goats Industries: petroleum and natural gas, petroleum products, oilfield equipment; steel, iron ore; cement; chemicals and petrochemicals; textile Exports - commodities: oil and gas 90%, machinery, cotton, foodstuffs Exports - partners: Italy 25.9%, France 7.7%, India 6.7%, Indonesia 6.6%, Germany 5.6%, Israel 5.1% (2012) Imports - commodities: machinery and equipment, oil products, foodstuffs, metals, chemicals Imports - partners: Turkey 18.6%, Russia 14.3%, China 7.8%, Germany 7.2%, UK 7.1%, US 5.1%, Ukraine 5% (2012)	

Investment Restrictions:

The Law on Protection of Foreign Investments permits foreign direct investment in any activity in which a national investor may also invest, unless otherwise prohibited by law. Prohibited areas include those relating to national security and defense. The Government of Azerbaijan also exerts some measure of control over other key sectors, such as energy and communications.

In sectors of interest to certain senior government and political figures, competition is actively impeded through administrative barriers.

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Section 1 - Background

Azerbaijan - a nation with a majority-Turkic and majority-Shia Muslim population - was briefly independent (from 1918 to 1920) following the collapse of the Russian Empire; it was subsequently incorporated into the Soviet Union for seven decades. Azerbaijan has yet to resolve its conflict with Armenia over Nagorno-Karabakh, a primarily Armenian-populated region that Moscow recognized in 1923 as an autonomous region within Soviet Azerbaijan after Armenia and Azerbaijan disputed the status of the territory. Armenia and Azerbaijan began fighting over the area in 1988; the struggle escalated after both countries attained independence from the Soviet Union in 1991. By May 1994, when a cease-fire took hold, ethnic Armenian forces held not only Nagorno-Karabakh but also seven surrounding provinces in the territory of Azerbaijan. The OSCE Minsk Group, co-chaired by the United States, France, and Russia, is the framework established to mediate a peaceful resolution of the conflict. Corruption in the country is widespread, and the government, which eliminated presidential term limits in a 2009 referendum, has been accused of authoritarianism. Although the poverty rate has been reduced and infrastructure investment has increased substantially in recent years due to revenue from oil and gas production, reforms have not adequately addressed weaknesses in most government institutions, particularly in the education and health sectors. In January 2012, Azerbaijan assumed a nonpermanent seat on the UN Security Council for the 2012-13 term.



Section 2 - Anti - Money Laundering / Terrorist Financing

FATF status

Azerbaijan is not on the FATF List of Countries that have been identified as having strategic AML deficiencies

Compliance with FATF Recommendations

The last Mutual Evaluation Report relating to the implementation of anti-money laundering and counter-terrorist financing standards in Azerbaijan was undertaken by the Financial Action Task Force (FATF) in 2015. According to that Evaluation, Azerbaijan was deemed Compliant for 4 and Largely Compliant for 25 of the FATF 40 + 9 Recommendations. It was Partially Compliant or Non-Compliant for 2 of the 6 Core Recommendations.

Key findings

Azerbaijan's strategic position is attractive for criminals and organised crime groups, this being strengthened by the existing transportation infrastructure. The main risks presented by the location of the country are connected above all with drug trafficking (mostly originating from Afghanistan with the destination in Europe or Russia) and human smuggling (where Azerbaijan figures both as a transit country and the country of origin). The most common predicate offences for money laundering are theft, fraud, tax evasion, embezzlement, drug and weapons production and trafficking, smuggling and corruption. The most common predicate offences, based on the structure of the disclosures received by law enforcement agencies from the Financial Monitoring Service (FMS), are tax evasion, counting for more than 75%, followed by corruption (almost 10%), embezzlement, fraud, drug crimes and cybercrime.

Although Azerbaijan has taken steps to address the recommendations made in the 3rd round report related to the criminalisation of money laundering and the financing of terrorism, deficiencies remain. Acquisition, possession or use of property is criminalised only with respect to "significant amounts", provided that the purposive element of "concealing or disguising the illicit origin of the funds or other property" is satisfied. The law does not provide explicitly that the criminal intent, knowledge or purpose can be inferred from objective factual circumstances. With regard to the financing of terrorism, the Criminal Code does not provide a definition of individual terrorist or terrorist organisation, nor does it refer to the Terrorist Financing Law for such definitions.

Criminal liability for money laundering and the financing of terrorism has not been extended to legal persons. This has an impact in limiting prosecutions for money laundering and the financing of terrorism and also in the provision of mutual legal assistance.

The criminalisation of money laundering has not been effectively applied. There a low number of convictions for money laundering and no cases of stand-alone and autonomous money laundering.

Confiscation of proceeds and instrumentalities is now mandatory when a conviction has been secured for a proceeds-generating crime and confiscation is available for all predicate offences to money laundering. However, property can only be taken from third parties when they knew or ought to have known that it had been obtained by criminal means, regardless of whether they obtained it for value or not. There is a lack of clarity on whether confiscation of indirect proceeds and corresponding value are routinely made. Also, the effectiveness of confiscation in predicate offences to ML was not demonstrated to the evaluators

The Financial Monitoring Service (FMS) has been established as the national centre to gather, analyse and submit financial information to relevant law enforcement agencies. The FMS appears to be well resourced and operating effectively. However, the authority of the FMS to disseminate reports is limited to the General Prosecutor's Office (GPO) and the Ministry of National Security. There is a lack of safeguards for removing the FMS's management from office and this could generate vulnerabilities for the system towards risks of undue influence or interference.

The AML/CFT Law prescribes obligations for reporting entities to apply preventive measures, including customer due diligence and identification of politically exposed persons. Although financial institutions appeared to have a good understanding of the requirements, they still establish business relationships in circumstances where a foreign legal person who is a beneficial owner is not identified.

Reporting requirements have been introduced and reports are being received by the FMS. However no suspicious transaction reports have been submitted by DNFBPs and only one by a non-banking financial institution. This brings the effectiveness of the regime in the non-banking sectors into question.

Sanctions available for infringements of the AML/CFT preventive regime are not effective, proportionate or dissuasive. Very few sanctions had been applied in practice, with no sanctions at all being applied to senior management.

There is inadequate AML/CFT supervisory over the operations of post offices. Other supervisors are in the process of adopting risk-based supervision.

The AML/CFT Law contains an exemption for small businesses from implementing an internal control system. This provides an exemption from a number of controls for smaller businesses. This exemption could increase the vulnerability of small businesses to the risk of being used for the purposes of money laundering and the financing of terrorism.

There is no requirement for information on beneficial ownership to be collected or made available by state authorities. The registration system does not provide adequate access to up-to-date information on beneficial ownership in a timely manner. Barriers are in place which makes it difficult for financial institutions to request ownership information from state registers of legal persons.

Azerbaijan is categorised by the US State Department as a Country/Jurisdictions of Primary Concern in respect of Money Laundering and Financial Crimes.

OVERVIEW

Azerbaijan is both a transit point between the East and West, given its geographic location, and a conduit for illicit funding, given its economic difficulties. The majority of foreign investment and international trade in Azerbaijan continues to be in the energy sector. To diversify Azerbaijan's economy, President Aliyev signed a series of decrees in 2016 that outline strategic roadmaps for the development of the national economy through 2024 in order to diminish the country's overdependence on income from energy resources. The roadmaps focus on 11 specific sectors of the economy, including agricultural product processing, heavy industry, tourism, logistics and trade, financial services, and telecommunications and information technologies. Implementation of the roadmaps is ongoing, but the government has released two biannual status reports that indicated progress in most sectors has been limited. The economic realities of the currency's continued devaluation and a financial sector suffering from exponentially growing rates of non-performing loans, coupled with Azerbaijan's physical location between Iran and Russia, create an environment conducive to the transit of illicit funds.

VULNERABILITIES AND EXPECTED TYPOLOGIES

The major source of criminal proceeds in Azerbaijan continues to be public corruption across all sectors and agencies within the government. In addition, the Afghan drug trade generates significant illicit funds, some of which transit Azerbaijan. Although the passage of the Joint Comprehensive Plan of Action has opened Iran for transit of funds, it is unlikely that Azerbaijan will experience a demonstrable decrease in funds from Iran. Robbery, tax evasion, smuggling, trafficking, and organized crime also continue to generate illicit funds in Azerbaijan. Additional money laundering likely occurs in the financial sector, including in non-bank financial entities and alternative remittance systems. Azerbaijan also possesses a significant black market for smuggled goods for sale in-country and is a transit point for smuggled cargo.

KEY AML LAWS AND REGULATIONS

As part of its active and ongoing measures, Azerbaijan established the Financial Markets Supervision Authority (FMSA) by Presidential Decree in February 2016, with the goals of improving licensing, regulation, and supervision of the securities market, investment funds, insurance, credit organizations, and payment systems operations; improving supervision over the AML/CFT preventive systems; and maintaining transparency and flexibility in supervising these areas. The FMSA implements its functions of preventing money laundering and terrorist financing through the Financial Monitoring Service (FMS), Azerbaijan's FIU.

The key Azerbaijani AML law is the 2009 Law of the Republic of Azerbaijan on the Prevention of Legalization of Criminally Obtained Funds or Other Property and the Financing of Terrorism (AML/CFT Law). In July 2009, in order to bring existing legislation into compliance with this law, the "Law of the Republic of Azerbaijan on Changes and Amendments to Some Legislative Acts of the Republic of Azerbaijan in Connection with Implementation of the AML/CFT Law" was adopted. In March 2010, the "Law of the Republic of Azerbaijan on Amendments to Individual Legislative Acts

of the Republic of Azerbaijan to Enhance the Prevention of the Legalization of Criminally Obtained Funds or Other Property and the Financing of Terrorism” was adopted, amending the Criminal Code and the AML/CFT Law.

The FMS and the FIUs of Moldova, Belarus, Turkey, Macedonia, Russia, and Iran have signed AML/CFT information sharing agreements. Azerbaijan is currently developing MOUs on AML cooperation between the FMSA and the FIUs of the United Arab Emirates, Ukraine, San Marino, Estonia, Moldova, Turkey, Slovenia, and Georgia.

Azerbaijan is a member of MONEYVAL, a FATF-style regional body.

AML DEFICIENCIES

While the FMSA is taking significant legislative action to address the recognized deficiencies, until such legislation is approved: criminal liability for money laundering has not been extended to legal persons in Azerbaijan; criminalization of the acquisition, possession, and use of property obtained with illicit funds is limited to “significant amounts” only; banks are not legislatively required to share customers’ CDD information with correspondent banks; sanctions are not effective, proportionate, or dissuasive to financial institutions; and loopholes exist inhibiting proper identification of PEPs.

The AML law excludes dealers of arts, antiques, and other high-value consumer goods; entities dealing with jewelry and precious metals; travel agencies; and auto dealers from the list of covered entities. These entities are not required to maintain customer information or report suspicious activity.

ENFORCEMENT/IMPLEMENTATION ISSUES AND COMMENTS

In November 2016, the President signed a decree approving the Action Plan for 2017–2019 on the Fight against Legalization of Criminally Obtained Funds and Other Properties and Financing of Terrorism. Following the signing of this decree, the FMSA placed an affirmative obligation on financial institutions to report money laundering activities, including designation and placement of the offending party on the FMSA website as a “designated person.” As a result of this designation, the FMSA, through the relevant government ministries, is able to freeze the assets of the named individual/entity. Though implementing ministries are required to submit annual reports and action plans to the Cabinet of Ministers and the Commission on Combatting Corruption, these reports are not currently publically available.

Current Weaknesses in Government Legislation (2013 INCRS Comparative Tables):

According to the US State Department, Azerbaijan conforms with regard to all government legislation required to combat money laundering

EU White list of Equivalent Jurisdictions

Azerbaijan is not currently on the EU White list of Equivalent Jurisdictions

World Governance indicators

[To view historic Governance Indicators Ctrl + Click here and then select country](#)

Failed States Index

[To view Failed States Index Ctrl + Click here](#)

Offshore Financial Centre

Azerbaijan is not considered to be an Offshore Financial Centre

US State Dept Narcotics Report 2017:

Azerbaijan remains a significant transit country for illegal drugs due to its location along major Southern Caucasus trafficking routes from Southwest Asian source countries to European markets. Substances commonly trafficked through the country include opiates originating from Afghanistan (particularly heroin), synthetic drugs, and drug precursor chemicals, which enter into Azerbaijan by sea (primarily from Turkmenistan) and by land (from Iran). Azerbaijan has also expressed concerns related to its inability to secure international borders in the occupied territories that surround Nagorno-Karabakh.

Azerbaijan's Ministry of Internal Affairs provided drug seizure and arrest statistics covering the first six months of 2016. Over this period, the Ministry of Internal Affairs reported investigations of 1,675 drug related criminal acts, including 429 separate drug sales. These investigations resulted in over 1,332 drug related convictions. Of these convictions, 1,023 defendants (90.4 percent) were unemployed and not enrolled in any educational institution.

Recidivists accounted for 430 (38 percent) convictions, and only 13 convictions (1.1 percent) involved women. During this same six-month period, Azerbaijani security services reportedly detected and destroyed approximately 102 metric tons of hemp and opium poppy. During the first 10 months of the year, security services reportedly seized 1,172 kilograms (kg) of heroin and 186 kg of opium.

In April, the United States sponsored two State Customs Committee agents to attend the International Drug Enforcement Conference in Lima, Peru. Other Azerbaijani state agencies cooperate and implement joint activities with the U.N. Office of Drugs and Crime, Central Asia Regional Information and Coordination Centre, and World Customs Organization, among other international organizations.

US State Dept Trafficking in Persons Report 2016 (introduction):

Azerbaijan is classified a Tier 2 country - a country whose government does not fully comply with the Trafficking Victims Protection Act's minimum standards, but is making significant efforts to bring themselves into compliance with those standards.

Azerbaijan is a source, transit, and destination country for men, women, and children subjected to forced labor and sex trafficking. Azerbaijani men and boys are subjected to forced labor in Turkey, Russia, United Arab Emirates (UAE), and Azerbaijan. Women and children from Azerbaijan are subjected to sex trafficking within the country and in Turkey, Russia, and UAE. Azerbaijan is a destination country for sex and labor trafficking victims from Turkey, Uzbekistan, Turkmenistan, Ukraine, and, in previous years, China and Russia. Some migrant workers from Turkey and other countries in Europe and South and Central Asia are subjected to forced labor in Azerbaijan. Azerbaijan was used as a transit country for victims of sex and labor trafficking from Central Asia to UAE, Turkey, and Iran in previous years. Within the country, some children, particularly those of Romani descent, are subjected to forced begging and forced labor as roadside vendors and at tea houses and wedding facilities. Filipina victims are subjected to domestic servitude in Azerbaijan.

The Government of Azerbaijan does not fully meet the minimum standards for the elimination of trafficking; however, it is making significant efforts to do so. During the reporting period, the government increased the number of trafficking investigations, maintained strong prosecution and conviction rates, and handed down severe sentences for labor and sex traffickers. The government increased victim identification efforts through the identification of seven Azerbaijani victims of forced labor; however, the government did not provide adequate and consistent financial support to NGO partners that provide rehabilitation and reintegration services to victims for the third year in a row. The government did not have formal standard operating procedures for implementation of the referral mechanism, and communication amongst participating agencies and organizations remained weak. Sources reported the government continued to pressure victims to assist in the investigation and prosecution of alleged traffickers, and victims who refused to participate did not receive the same quality of care as those who did participate.

US State Dept Terrorism Report 2016

Overview: Azerbaijan maintained its strong counterterrorism cooperation with the United States and actively opposed terrorist organizations seeking to move people, money, and materiel through the Caucasus region. The country remained focused on counterterrorism efforts that included prosecuting individuals under statutes related to terrorism, arresting foreign terrorist fighters returning to Azerbaijan from conflicts abroad, and conducting special operations against those the government said were planning terrorist attacks.

Azerbaijan indicated its continued strong willingness to counter ISIS by sharing information, working to disrupt the flow of foreign terrorist fighters to Iraq and Syria, and countering illicit funding of terrorist groups in those countries. Senior government leaders, including the heads of the Caucasus Muslim Board and the State Committee for Work with Religious Associations,

took public steps to counter ISIS and al-Qa'ida ideology. They and other senior government representatives repeatedly condemned international terrorist attacks that occurred during 2016.

On September 17, Azerbaijani President Ilham Aliyev, and other leaders attending the Commonwealth of Independent States Heads of State Council meeting in Bishkek, Kyrgyz Republic, jointly approved a program on cooperation in the fight against terrorism and other forms of violent extremism for 2017-2019. President Aliyev also participated in discussions at the NATO Warsaw Summit on July 8-9 on measures to counter violent extremism.

Legislation, Law Enforcement, and Border Security: Azerbaijan continued to use counterterrorism legislation, first adopted in 1999, that governs the investigation and prosecution of individuals who have committed or plan to commit terrorist acts.

As the country's primary law enforcement agency, the Ministry of Internal Affairs has responsibilities for fighting terrorism. Specific counterterrorism actions are taken through the Ministry's Organized Crime Unit. The Prosecutor General's Office maintains responsibility for prosecuting individuals for terrorism, conspiracy to commit terrorism, conspiracy to aid terrorism, and other terrorism-related crimes.

Azerbaijan's State Security Service (SSS) cooperates closely with the Ministry of Internal Affairs and the Prosecutor General's Office on counterterrorism. Following a 2015 presidential decree, the Azerbaijani government in 2016 abolished the Ministry of National Security and split it into two new organizations, the SSS and the Foreign Intelligence Service. Among other duties, the SSS is charged with identifying and preventing criminal activities by terrorist groups, and countering international terrorism and transnational crimes.

The Azerbaijani government has demonstrated the ability to detect and deter terrorist activities, as well as prosecute foreign terrorist fighters returning to Azerbaijan. Authorities effectively use terrorist and criminal watch lists and biographic/biometric information to screen travelers at ports of entry. Azerbaijani security services effectively share information within the government and with other countries. Collection of Advance Passenger Information and Passenger Name Records on commercial flights occurred on some flights.

Azerbaijani law enforcement agencies continued to investigate, prosecute, and sentence those the government accused of fighting with terrorist groups in Syria and Iraq, and conducted counterterrorism operations against suspected terrorists within Azerbaijan.

In 2016, the government terminated the citizenship of 58 individuals accused of involvement in terrorist activities outside the country.

The government has continued to prosecute 17 suspects arrested during a November 2015 law enforcement operation in the village of Nardaran, about 15 miles north of the capital, Baku. The government has charged former political prisoner and religious activist Taleh Bagirzade (also referred to in media reports as Taleh Bagirov) and others with plotting to overthrow the government. The government alleged that Bagirzade and his associates were storing ammunition and explosives in Nardaran, which officers seized during the raid. During the operation, five village residents were killed, along with two police officers. Government officials alleged that radical individuals and groups within Nardaran have long been advocating establishment of a fundamentalist Islamic state and claim these groups have received support from governments and fundamentalist-backed entities outside the country.

Many democracy and human rights advocates believe the arrests were arbitrary due to lack of evidence. Observers of the trial have noted frequent violations of due process, as well as numerous inconsistencies in the prosecution's case. The trial was ongoing at the end of 2016.

Throughout the year, there were reports of terrorist acts being prevented in Azerbaijan; however, it is unclear whether some of these preventative actions were taken against bona fide terrorist threats or were designed to curb the activities of heretofore non-violent independent religious activists.

On February 12, the SSS arrested eight suspects in a counterterrorism operation. Several of those were convicted and sentenced to prison on terrorism-related charges.

On October 27, the SSS announced that its officers had conducted raids in which two men suspected of planning terrorist attacks in Azerbaijan were killed and a third was wounded. The SSS said in a statement that the men had created an armed group in Azerbaijan and pledged allegiance to terrorist groups involved in armed conflicts outside Azerbaijan.

On November 16, a court in Baku convicted seven Azerbaijani citizens on charges they fought in Iraq and Syria alongside militants from ISIS and other terrorist groups. The court sentenced the defendants to prison sentences ranging from two to 14 years.

On November 25, one terrorist suspect, Ramiq Rahimov, was killed during an SSS operation in Azerbaijan's Khachmaz District. Rahimov was suspected of leading a terrorist organization involved in armed conflicts outside Azerbaijan and of recruiting Azerbaijani citizens to fight abroad. An SSS statement said Rahimov had illegally acquired firearms and explosives and planned to carry out terrorist attacks and kidnappings.

On December 3, SSS officers killed a man the government said was carrying an explosive device and planned to commit acts of terrorism on Azerbaijan's territory. The SSS said in a statement that officers tried to arrest Emin Jami near a shopping center in Baku, and killed him when he presented a threat to the SSS officers. Jami had, according to the government, sworn "allegiance to representatives of international terrorist organizations and illegal militias involved in conflicts abroad." Jami had previously served nine years in prison for membership in a terrorist group and, according to an SSS statement, had resumed contact with other Azerbaijani violent extremists fighting in conflict zones and preparing terrorist activities in Azerbaijan.

Countering the Financing of Terrorism: Azerbaijan is a member of the Council of Europe's Committee of Experts on the Evaluation of Anti-Money Laundering Measures and the Financing of Terrorism (MONEYVAL), a Financial Action Task Force (FATF)-style regional body. The government's Financial Monitoring Service (FMS) is a member of the Egmont Group of Financial Intelligence Units.

Azerbaijan has continued its efforts to increase its capability in anti-money laundering/countering the financing of terrorism (AML/CFT) since it was last assessed by MONEYVAL in 2014. Azerbaijan has established a framework for asset freezing and requires financial institutions to conduct customer due diligence and report suspicious transactions to the FMS. Its legal framework to criminalize terrorist financing does not cover all aspects of the offense, however, and not all non-financial institutions are required to report suspicious transactions, presenting a further vulnerability in its AML/CFT framework.

International Sanctions

In February 1992, the Organisation for Security and Co-operation in Europe (OSCE) requested that all OSCE participating states should introduce an embargo on 'all deliveries of weapons and munitions to forces engaged in combat in the Nagorno-Karabakh area'. This embargo is still in force.

Index	Rating (100-Good / 0-Bad)
Transparency International Corruption Index	31
World Governance Indicator – Control of Corruption	18

Corruption poses significant compliance risks to businesses operating or planning to invest in Azerbaijan. Political corruption increases business costs and represents the main challenge for foreign companies; patronage is particularly prevalent in the oil industry, which yields the state's largest revenue. A weak judiciary and insufficient regulatory enforcement allows government officials to act with impunity. The government has a comprehensive anti-corruption legal framework in place: Passive and active bribery, extortion and abuse of office are illegal under the Criminal Code. Nevertheless, the government does not implement anti-corruption provisions effectively. Azerbaijani law puts restrictions on gifts, but companies are likely to encounter demands for facilitation payments or other informal payments. **Information provided by GAN Integrity.**

US State Department

Pervasive corruption – including bribery of public officials – continues to be a major challenge for U.S. and other international firms operating in Azerbaijan. Although anti-corruption legislation is in place, corrupt practices permeate all spheres of public life. Officials from the lowest ranks of the civil service to the top echelons of government are believed to benefit from systemic corruption in the country.

The Government of Azerbaijan recognizes that corruption is a problem but, to date, laws and regulations to combat corruption have not been effectively or consistently enforced. Azerbaijan has made modest progress in implementing a 2005 Anticorruption Law, which created a commission with the authority to require full financial disclosure from government officials.

On September 5, 2012, President Aliyev issued a decree for a National Action Plan on Open Government and a National Action Plan on Combating Corruption. ASAN service centers created by the State Agency for Public Service and Social Innovations, under the President of the Republic of Azerbaijan, were established in July 2012 by Presidential decree and became operational in February 2013. These centers provide 23 government services from nine state entities, including the registration of commercial legal entities and tax payers, notary services, state registration of civil status acts, and the renewal of identity cards/passports of citizens. ASAN centers are intended to provide more transparent and accountable services through a “one window” model that reduces opportunities for rent-seeking and petty government corruption.

In 2013, Azerbaijan's modest improvements in combating petty corruption were reflected in the global anticorruption watchdog Transparency International, which ranked Azerbaijan 128 out of 177 countries on its Corruption Perceptions Index, up from 139 a year before. Popular opinion identifies the State Customs Committee as the institution of greatest concern to businesses in Azerbaijan, followed by the Ministry of Taxes – though the reputation of the tax authorities has enjoyed some improvement in the past year as corruption-reducing reforms have been implemented. Transparency's 2013 Global Corruption Barometer – which examined bribery involved in people's contact with customs, education, the judiciary, land related services, medical services, the police, registry and permit services, tax authorities and utilities – found that roughly 50% of Azerbaijani respondents had paid a bribe to one of the nine service providers in the twelve preceding months. Azerbaijan is a party to the United Nations Convention against Corruption (UN Convention) and a signatory to the Council of Europe Criminal and Civil Law Conventions. Azerbaijan is not currently a party to the Organization for Economic Cooperation and Development Anti-Bribery Convention.

Azerbaijan has also been a participant in the Extractive Industries Transparency Initiative (EITI). In 2009, Azerbaijan became the first participating country to become fully compliant with EITI requirements. Azerbaijan's EITI reports do not currently provide data on a company-by-company basis – which is optional – but citizen groups in Azerbaijan are encouraging companies to do so.

Corruption and Government Transparency - Report by Global Security

The Political Climate

Azerbaijan is a transitional economy with important oil reserves and significant agricultural potential. In the years preceding the global financial crisis, Azerbaijan performed impressively, with double digit real GDP figures, backed by growth in the oil and energy sector. Although the government of Azerbaijan consists of three branches, the institutional setup ensures a strong role for the president and the executive branch. The strong presidential influence has resulted in the lack of independency of the Parliament (Milli Majlis) and the judiciary and has further contributed to an environment riddled with corruption and impunity. In Azerbaijan, the high-level government officials are almost never prosecuted for corruption, according to Freedom House 2013. Azerbaijan voted to lift the country's two-term presidential limit, enabling President Ilham Aliyev to be re-elected indefinitely. In the November 2010 parliamentary elections, the ruling party of Ilham Aliyev won with a majority of seats. Some foreign observers had reported flaws in the elections, while others described it as more democratic than previously, according to a 2010 article by PressTv. In 2013, President Aliyev became the "Corruption's Person of the Year", according to the Organised Crime and Corruption Reporting Project (OCCRP). The evaluation has been justified by documented evidence showing the family of the President has been involved in taking over the private sector of Azerbaijan for a long period of time, as reports by a 2013 article by Radio Free Europe. Members of Aliyev's family reportedly own a large share of the country's gold mining, banking, construction and telecom industries, according to Freedom House 2013.

It is widely recognised that corruption is deeply institutionalised throughout Azerbaijani society and poses an obstacle to both social and economic development, as illustrated by both the US Department of State 2013 and Global Integrity 2011. The political system is

paternalistic and patronage-based, consisting of networks of central persons in the administration distributing revenues - especially from the massive exploitation of oil and gas - among themselves and other strategically important figures at the expense of the generally impoverished population. Public officials at all levels are rarely held accountable for engaging in corrupt practices, according to the Bertelsmann Foundation 2012. The same report notes that in 2011, the Azerbaijani government launched an anti-corruption campaign to try to gain back the trust of the public and avoid the fate of countries which have witnessed the Arab Spring. As a consequence of the campaign, many high-level officials were dismissed. The most prominent corruption case involved a high-profile member of Azerbaijan's ruling party, Gulyar Ahmadova. In February 2013, Ahmadova was charged with abuse of functions, embezzlement and active bribery in exchange for keeping her seat in Parliament, according to a 2013 article by Radio Free Europe. The investigation is still ongoing; however, if found guilty on all corruption charges, Ahmadova could face 12 years' imprisonment.

Since his inauguration in 2003, the President has decreed several anti-corruption initiatives, most notably the adoption of the Law on Combating Corruption in 2004 and the establishment of the Commission on Combating Corruption (CCC) in 2005. In September 2012, the Government of Azerbaijan has approved a new National Anti-Corruption Plan 2012-2015 aimed at improving institutional collaboration in investigating and prosecuting corruption cases and establishing a better whistleblower protection, according to a 2013 report by the European Commission. Independent observers report, however, that the anti-corruption measures and policies lack enforcement and have not improved the level of accountability of Azerbaijan's politicians. According to Transparency International's Global Corruption Barometer 2013, 28% of surveyed Azerbaijani households perceive that the level of corruption has increased a lot over the past two years. Furthermore, 15% believe that the government's actions to fight corruption are ineffective. In addition, 37% of the surveyed households have reported that corruption constitutes a very serious problem in the public sector in Azerbaijan. Similarly, business executives surveyed in the World Economic Forum's Global Competitiveness Report 2013-2014 reveal that the level of public trust in political remains relatively low.

Business and Corruption

Azerbaijan's economy continues to undergo transformation and restructuring. In addition to its openness towards global trade, relatively moderate taxation and government spending have been essential to the transition towards greater economic freedom. Nonetheless, Azerbaijan remains a challenging market for doing business, not least due to the systemic level of corruption, which has deterred many potential investors from entering the market. Similarly, non-transparent and arbitrary regulations, corrupt government bureaucracy, weak legal institutions and a private sector regulated according to politically connected monopolistic interests have severely hampered foreign direct investment in the country, according to the US Department of State 2013. This is supported by the World Economic Forum's Global Competitiveness Report 2013-2014, which outlines that the favoritism of government officials when deciding upon policies and contracts is an obstacle to doing business in the country and that public funds are commonly diverted to well-connected individuals, companies or groups due to corruption. Despite property rights regulation being adequately defined in Azerbaijan, the efficiency of regulations and property rights registration procedures are significantly undermined by interference of high-level officials

with the aim of soliciting bribes, according to the Bertelsmann Foundation 2012. Several cases are known where the Azerbaijani state has seized private companies and given them away to new owners for the political reasons, reports the same source.

In Azerbaijan, government and business elites are strongly interlinked as top officials regularly invest in strategic industries. The Global Competitiveness Report 2013-2014 reports that Azerbaijan performs poorly in relation to the ethical behaviour of companies in interactions with public officials, politicians and other companies. Moreover, government members control companies and influential elites treat state companies as private property. This is further reinforced by Freedom House 2013, which notes that a large part of the economy is controlled by corrupt high-level officials, which significantly limits the equality of investment opportunity among companies. The intermingling of political and business interests is exemplified in the US Department of State 2013 report, which describes how the Azerbaijan State Caspian Shipping Company (CASPAR) and the national airline (AZAL) have effectively blocked foreign companies from entering their respective markets by using their mirror regulatory authorities to set up barriers for foreign investment in the sectors.

The country has few institutional checks on graft and the rapid growth in the energy sector has offered considerable opportunities for the institutionalisation of corruption. According to Transparency International's Global Corruption Barometer 2013, corruption within the business and private sectors is perceived to be relatively widespread, with more than one-third of all respondents evaluating the sector to be "extremely corrupt". Business executives surveyed in the Global Competitiveness Report 2013-2014 identify corruption as the most problematic factor for establishing business in Azerbaijan. The US Department of State 2013 reports that foreign companies operating in Azerbaijan experience limited access to market and discrimination upon entering certain sectors. The procedures connected with obtaining business licences and credits are used as administrative barriers to impede the competition in strategic sectors and elicit bribes. Given these reasons, companies are recommended to use a specialised public procurement due diligence tool in order to help mitigate the costs and risks of corruption when doing business in Azerbaijan. In addition, companies are recommended to develop and implement integrity systems, and to carry out extensive due diligence before committing funds or when already operating in the country.

Regulatory Environment

Corruption is institutionalised in the Azerbaijani bureaucracy. Companies are frequently faced with highly bureaucratic regulatory environment, offering endless opportunities to demand bribes in exchange for undue advantages. The US Department of State 2013 reports that the country has worked to improve its regulatory system over the past several years, yet allegations of corruption, lack of transparency and politically connected economic monopolies remain among the greatest obstacles for companies operating in Azerbaijan. Furthermore, according to the US Department of State 2013, the publication and the implementation of the adopted anti-corruption legislation and regulations in Azerbaijan are either majorly delayed or not executed at all.

As a result of a non-transparent regulatory environment, companies operating in Azerbaijan may face serious problems when obtaining the required licences for doing business, including continual demands for bribes from public officials. Companies surveyed in the World Economic Forum's Global Competitiveness Report 2013-2014 identify inefficient

government bureaucracy and tax regulations to be among the most problematic factors for doing business in the country. On a more positive note, the US Department of State 2013 reports that the government has created a new business registration mechanism based on the principle of a one-stop shop under the Ministry of Taxes, allowing companies to register within three days. However, Doing Business 2013 notes that it takes 11 days for companies to register property, which is longer than initially intended by the government. The tax administration does also present obstacles for businesses in Azerbaijan as tax authorities have a reputation as being notoriously corrupt. The Law on Protection of Foreign Investments permits foreign direct investment in most sectors. Prohibited areas include those relating to national security and defence, and the government carefully controls other key sectors, such as energy and communications.

Azerbaijan has passed several pieces of anti-corruption legislation, including laws regulating gifts to civil servants and ministerial relations with private companies. However, laws and regulations that exist to combat corruption are not effectively enforced, with corruption in the regulatory, tax and dispute settlement systems being most pervasive, according to the US Department of State 2013. Problems in the quality, reliability and transparency of governance, as well as abuse of the regulatory system and poor contract enforcement, significantly impede the ability of many companies to do business in Azerbaijan. Business executives surveyed in the Global Competitiveness Report 2013-2014 report that the judiciary is not independent from political influences of members of government, citizens or companies, which could negatively influence the amount of time required for appeals process and dispute settlement. The Law on International Arbitration of 2000 allows international arbitration of commercial disputes to be conducted both in Azerbaijan and in any foreign jurisdiction mutually agreed upon by the parties. Azerbaijan is a signatory to several international conventions regulating the mutual acceptance and enforcement of foreign arbitration, including the New York Convention 1958, and is a member of the International Centre for the Settlement of Investment Disputes (ICSID). Access the Lexadin World Law Guide for a collection of arbitration and other laws in Azerbaijan.

Oil and Gas Sector

Corruption and Progress in Azerbaijan's Oil and Gas Sector

The remarkable growth in Azerbaijan's market economy can be explained by the rapidly increasing production and export of oil and gas. The oil and gas sector accounts for more than 70% of Azerbaijan's exports and for 60% of its GDP. The state holds huge interests in the sector, and there are close links between the oil and gas industry and governmental institutions. Despite measures taken by the government to address issues of corruption and transparency, accusations of corruption and irregular practices in the oil sector continue. For instance, according to the US Department of State 2011, the oil and gas sector is considered by many to be one of the greatest sources of corruption within the country, despite the fact that Azerbaijan was named the first participating country to be fully compliant with the Extractive Industries Transparency Initiative (EITI) principles and criteria in 2009.

Azerbaijan created the State Oil Fund (SOFAZ) in 1999 to collect and manage oil revenues. SOFAZ contributes to the state budget to support investments in infrastructure, education, poverty reduction and other social projects. International and local NGOs claim that SOFAZ is under the control of the Presidential Bureau and that massive fraud and misappropriation of

the fund's money by top politicians and officials has taken place. For example, the government spent a large sum of money from SOFAZ to pay pensions and raise civil service salaries in a presidential election year. Furthermore, local NGOs have accused SOFAZ of funding development in the oil sector instead of strengthening other sectors in the country.

Section 3 - Economy

Azerbaijan's high economic growth has been attributable to large and growing oil and gas exports, but some non-export sectors also featured double-digit growth, including construction, banking, and real estate. Oil exports through the Baku-Tbilisi-Ceyhan Pipeline, the Baku-Novorossiysk, and the Baku-Supsa pipelines remain the main economic driver, but efforts to boost Azerbaijan's gas production are underway. The eventual completion of the geopolitically important Southern Gas Corridor between Azerbaijan and Europe will open up another, albeit, smaller source of revenue from gas exports.

Azerbaijan has made only limited progress on instituting market-based economic reforms. Pervasive public and private sector corruption and structural economic inefficiencies remain a drag on long-term growth, particularly in non-energy sectors. Several other obstacles impede Azerbaijan's economic progress, including the need for stepped up foreign investment in the non-energy sector and the continuing conflict with Armenia over the Nagorno-Karabakh region. Trade with Russia and the other former Soviet republics is declining in importance, while trade is building with Turkey and the nations of Europe.

Long-term prospects depend on world oil prices, Azerbaijan's ability to negotiate export routes for its growing gas production, and its ability to use its energy wealth to promote growth and spur employment in non-energy sectors of the economy.

Agriculture - products:

fruit, vegetables, grain, rice, grapes, tea, cotton, tobacco; cattle, pigs, sheep, goats

Industries:

petroleum and petroleum products, natural gas, oilfield equipment; steel, iron ore; cement; chemicals and petrochemicals; textiles

Exports - commodities:

oil and gas 90%, machinery, foodstuffs, cotton

Exports - partners:

Italy 26.3%, Germany 13.3%, Indonesia 7%, France 6.9%, Czech Republic 6% (2015)

Imports - commodities:

machinery and equipment, foodstuffs, metals, chemicals

Imports - partners:

Russia 19.9%, Turkey 16.5%, UK 8.6%, Germany 6.6%, Italy 6.3%, US 4.1% (2015)

Banking

Key performance indicators for the Azeri banking system have improved significantly since 2000, mainly due to strong growth in the economy and financial sector reform. However, it is still considered one of the weakest banking systems among the sovereigns rated by Fitch Ratings. Despite recent progress, the financial system remains small and highly concentrated.

Stock Exchange

The Baku Stock Exchange (BSE), founded in 2001, is the main stock exchange in Azerbaijan. A member of the Federation of Euro-Asian Stock Exchanges (FEAS). BSE trades short-term treasury bonds, common stocks (primarily from former state-owned enterprises that have been privatized, including food and beverage, construction and banking companies), and foreign currency futures.

Executive Summary

The overall investment climate in Azerbaijan continues to improve incrementally, although significant challenges remain. Over the past few years, the Government of Azerbaijan has worked to integrate the country more fully into the global marketplace, attract foreign investment, diversify its economy and maintain growth. However, as a country dependent on oil and gas products for roughly 90 percent its export revenue, continued low world oil prices have hit Azerbaijan's economy hard. Economic growth slowed to 1.1 percent in 2015 from 2.8 percent in 2014, and the European Bank for Reconstruction and Development forecasts GDP growth of 2.5 percent in 2016 as a result of the drop in world oil prices.

While the oil and gas sector have historically attracted the majority of foreign investment, the Azerbaijani government has targeted four non-oil sectors as key to diversifying the country's economy and ensuring future prosperity: agriculture, transportation, tourism, and information/communication technology. Economic diversification and greater foreign investment continue to be the stated goals of President Aliyev and the government.

Although significant challenges remain for U.S. companies and investment in the non-oil sector, such as red tape and weak legal institutions, the Azerbaijani government has begun taking necessary steps to improve the business climate and reform the overall economy. Steps planned or underway include suspending certain inspections of businesses, doing away with certain redundant business license categories, empowering the popular "ASAN" government service centers with licensing authority and active steps to improve transparency, simplifying certain customs procedures, and creating tax incentives for investors. In March 2016, President Aliyev signed a decree on a strategic roadmap of the national economy and assigned a working group, led by the newly appointed Assistant to the President for Economic Reforms Natig Amirov, to draft an economic development strategy and action plan for 2016-2020. President Aliyev signed another decree in March 2016 establishing a free trade zone area next to the Alat seaport, located 65 km south of Baku, and has assigned the Ministry of Economy the task of drafting the necessary legislation and development concepts within six months. Newly adopted amendments to the Customs Tariff law provide exemptions of up to seven years to entrepreneurs importing capital equipment for priority sectors. Additionally, up to 50 percent of their revenues can be exempted from income, property, and land taxes for up to seven years. Furthermore, Azerbaijan's business community reports seeing real improvements in customs, including more transparency, and improved and systematized customs fee collection procedures.

Azerbaijan has worked to improve its regulatory system over the past several years, but opaque procedures in a number of areas and continued allegations of corruption remain problems. In early 2016, several roundtable discussions brought government and business community representatives together, including an April-session that the President held with the board of the American Chamber of Commerce in Azerbaijan, with both sides welcoming and applauding this increase in communication and engagement.

Under Azerbaijani law, foreign investors may engage in investment activities not prohibited by law. Private entities may freely establish, acquire and dispose of interests in business enterprises. Foreign citizens, organizations, and enterprises may lease, but not own land. Azerbaijan's Law on the Protection of Foreign Investments protects foreign investors against nationalization and requisition, except under certain specified circumstances. The Government of Azerbaijan has not shown any pattern of discriminating against U.S. persons

or entities by way of an illegal expropriation. The Bilateral Investment Treaty (BIT) between the United States and Azerbaijan provides U.S. investors with recourse to settle any investment dispute using the International Center for the Settlement of Investment Disputes (ICSID). The average length of time it takes for international business disputes to be resolved, either through the use of domestic courts or alternative methods of dispute resolution like mediation and/or arbitration, varies widely.

In 2015, Azerbaijan devalued its local currency, the manat (AZN), by 35 percent in February and again by 48 percent in December as a result of continued low world oil prices and relieve pressure on the Central Bank’s foreign currency reserves. In general, however, there are no restrictions on converting or transferring funds associated with an investment into freely usable currency at a legal, market-clearing rate. Azerbaijan has an underdeveloped financial services sector – of which banking comprises more than 90 percent – that inhibits economic stability, growth, and diversification. Many state-owned enterprises (SOE's) enjoy quasi-governmental or near-monopoly status in their respective sectors, with unclear lines of separation between regulatory bodies and state corporate interests. Responsible Business Conduct (RBC) is a relatively new concept in Azerbaijan and local companies generally consider basic charitable donations and paying taxes as acts of social responsibility. There have been no known acts of political violence against U.S. businesses or assets, nor against any foreign owned entity.

Table 1

Measure	Year	Index or Rank	Website Address
TI Corruption Perceptions index	2014	126 of 175	transparency.org/cpi2014/results
World Bank’s Doing Business Report “Ease of Doing Business”	2015	63 of 189	doingbusiness.org/rankings
Global Innovation Index	2015	93 of 143	globalinnovationindex.org/content/page/data-analysis
U.S. FDI in partner country (\$M, stock positions)	2015	\$1,493.10	FDI Intelligence from The Financial Times Ltd
World Bank GNI per capita	2014	\$7590	data.worldbank.org/indicator/NY.GNP.PCAP.CD

1. Openness To, and Restrictions Upon, Foreign Investment

Attitude toward Foreign Direct Investment

Over the past few years, the Government of Azerbaijan has worked to integrate the country more fully into the global economic marketplace, attract increased foreign investment, diversify its economy, and maintain positive growth. Attracting foreign direct investment to support economic diversification continues to be the stated goal of President Aliyev and his government. Less than expected oil production over the past several years coupled with continued low world oil prices – and their concomitant impact on budget revenues – prompted the Azerbaijani government to pursue more comprehensive reforms. In February 2016, the government introduced amendments to the Tax Code, which provides tax benefits to legal and physical entities engaged in certain investment activities. With these amendments, these physical and legal entities can be exempt from paying taxes for 50 percent of their revenues and incomes, respectively, for up to seven years. Moreover, the government approved amendments to the law On Customs Tariff, under which legal and physical entities can be exempted from customs duties and value-added tax (VAT) on import of capital equipment for up to seven years. In addition, any organization or industrial or technology park operator who plans to import capital equipment in certain sectors may apply for permission to construct production facilities, or conduct research, test, and development activities.

Other Investment Policy Reviews

Azerbaijan has not conducted an Organization for Economic Cooperation and Development (OECD) investment policy review in the past three years. Over the past few years, Azerbaijan has made gradual progress in the World Bank's, Doing Business Report: <http://www.doingbusiness.org/data/exploreeconomies/azerbaijan>

Laws/Regulations on Foreign Direct Investment

Foreign investment in Azerbaijan is regulated by a number of international treaties and agreements, as well as by domestic legislation. These include the Bilateral Investment Treaty (BIT) between the United States and the Government of the Republic of Azerbaijan, which encourages the reciprocal protection of investment, dated August 1, 1997; the Azerbaijan-EC Cooperation Agreement dated April 22, 1996; Law on Protection of Foreign Investment dated January 15, 1992 (the Foreign Investment Law); the Law on Investment Activity dated January 13, 1995 (the Investment Activity Law); the Law on Investment Funds dated October 22, 2010 (the Investment Funds Law); the Law On Privatization of State Property dated May 16, 2000 (the Privatization Law); and the Second Program for Privatization of State Property of the Republic of Azerbaijan dated August 10, 2002 (the Second Privatization Program), as well as laws regulating specific sectors of the Azerbaijani economy. This legislation permits foreign direct investment in any activity in which a national investor may also invest, unless otherwise prohibited by law. Azerbaijani law is evolving in accordance with the government's strategic goal of creating a welcoming environment for foreign businesses; as such, foreign investments are protected by guarantees provided under Azerbaijani law. The website of Azerbaijan's National Council, <http://meclis.gov.az/>, lists all laws of the Republic of Azerbaijan, but it is only available in the Azerbaijani language.

Business Registration

All companies operating in Azerbaijan are required to be registered. Without formal registration, a company may not do business in Azerbaijan (e.g., maintain a bank account, clear goods through customs). As part of the ongoing business law reforms, a "One Window" principle was introduced on January 1, 2008. The registration procedures involving several

governmental bodies (Ministry of Justice, Social Insurance Fund, and State Statistics Committee) have been eliminated; therefore businesses only have to register with the Ministry of Taxes. The established period for state registration with the Ministry of Taxes is officially set at three days for commercial organizations. Online registration is available at <http://taxes.gov.az/modul.php?lang=eng&name=birpencere&bolme=registration> and works adequately.

Azerbaijan ranks 63rd in Ease of Doing Business and 7th in Starting a Business out of 189 countries in The World Bank's Doing Business Report (rankings are available at: <http://www.doingbusiness.org/rankings>).

Industrial Promotion

President Aliyev has targeted the following sectors for attracting investment: agriculture, transportation, tourism, and information/communication technology.

The Azerbaijan Export and Investment Promotion Foundation (AZPROMO) is a joint public-private-initiative, established by the Ministry of Economy and Industry of Azerbaijan in 2003 with the goal of contributing to economic development and diversification by attracting foreign investment in non-oil sectors of the economy and stimulating expansion of Azerbaijan's exports of non-oil goods to overseas markets. AZPROMO has been involved in a number of business forums and training events both in Azerbaijan and internationally. According to a Cabinet of Ministers decision, small enterprises in Azerbaijan are defined as those with less than 25 employees and medium enterprises as those with less than 125 employees.

Limits on Foreign Control and Right to Private Ownership and Establishment

Azerbaijan imposes above average restrictions on foreign equity ownership compared to countries in the Eastern Europe and Central Asia region included in the IFC's Investing Across Borders Report. Restricted sectors on investment include those relating to national security and defense. The Government of Azerbaijan also exerts some measure of control over other key sectors, such as agriculture, communications, oil, and mining. According to Azerbaijan's laws, the state must retain a controlling stake in companies operating in the mining or oil and gas sectors. Thus, foreign (as well as domestic) capital participation is limited to a maximum of 49 percent ownership. Foreign ownership in the media sector is strictly limited as well. Unless any relevant international agreement with Azerbaijan provides otherwise, foreign shareholding in media companies is limited to 33 percent for newspaper publishers and is prohibited for TV broadcasting companies; currently, there are no such international agreements in place. While restrictions on foreign equity ownership in the financial services sectors (banking and insurance) have already been abolished, there are still sector-wide limits for total foreign capital participation.

Foreign investments enjoy complete and unreserved legal protection granted by the Law on Protection of Foreign Investment, in addition to any other guarantees contained within international agreements or treaties. This law stipulates that Azerbaijan will treat foreign investors, including foreign partners in joint ventures, in a manner not less favorable than the treatment accorded to national investors and allows the repatriation of profits, revenues and other investment-related funds as long as applicable taxes have been paid. Azerbaijan has endorsed limits on foreign control in the domestic insurance market. In compliance with the amendments to the Law on Insurance Activity, approved by the Azerbaijani Parliament in

2013, the share of foreign capital for one individual in the equity capital of insurance companies cannot exceed 10 percent, while the total share of foreign capital in such equities cannot exceed 50 percent. International financial institutions of which Azerbaijan is a member are exempt from these limits.

Privatization Program

Large-scale privatization has been particularly slow in Azerbaijan, and lags significantly behind other CIS countries within the Commonwealth of Independent States (CIS). However, within the CIS, Azerbaijan scores higher than average with regards to small-scale privatization programs, which have also been comparatively more successful. Under Azerbaijani law, foreign investors can participate – according to existing legislation – in the privatization programs of state and municipal properties, and can invest in Azerbaijan through joint ventures with local companies or by establishing subsidiaries that are wholly-owned, as well as through representative offices and branches of foreign legal entities.

In January 2016, Azerbaijani President Ilham Aliyev ordered the government to draw up a major privatization program in a bid to revive the country's economy, as it works to overcome the impacts of low world oil prices. Currently, the only sector targeted for privatization is public utilities. Although there is a public bidding process for the privatization programs, it is not transparent.

Screening of FDI

In 2008, Azerbaijan transferred responsibility for registering representative offices of foreign businesses, and the creation of business entities with foreign ownership, to the Ministry of Taxes based on the so-called “one-stop-shop” principle that greatly simplifies the registration process and reduces waiting times. The “online registration” system of legal entities has been available since 2012 and can be accessed in English at the following website: http://taxes.gov.az/modul.php?lang=_eng&name=birpencere&bolme=registration. The registration of representative or branch offices of foreign non-commercial entities was not, however, transferred to the Ministry of Taxes; such entities are still required to register with the Ministry of Justice.

The World Bank's Investing Across Borders (IAB) report offers an informative overview on how to start a business in Azerbaijan:

“It takes 7 procedures and 11 days to establish a foreign-owned limited liability company (LLC) in Azerbaijan. This is faster than the regional IAB average for Eastern Europe and Central Asia and much faster than the IAB global average. There are no additional procedures required of a foreign-owned company establishing a subsidiary in Baku, Azerbaijan's capital, other than the requirement to provide an apostille or notarized and translated copy of the incorporation documents and charter of the parent company abroad. A foreign-owned company does not need to get an investment approval to establish itself in Azerbaijan. The company registration is completed at a one-stop shop that also serves for registration for VAT. The Ministry of Taxes issues the business registration within 3 business days and the VAT number within 5 days of application. In order to open a bank account (in local or foreign currency), the company submits a Ministry of Taxes registration form to the appropriate bank. The whole process can be done online and usually takes only 2–3 days. There is no minimal capital requirement for LLCs, although the capital must be fully paid in prior to the state registration.”

Source: <http://iab.worldbank.org/data/exploreeconomies/azerbaijan#starting-a-foreign-business>

Competition Law

Over the past few years, Azerbaijan has been engaged in the process of updating several key pieces of legislation that impact the business environment. The State Committee for Antimonopoly Policy and Support of Entrepreneurship reviews transactions for competition-related concerns, whether domestic or international in nature. A new version of the Competition Code was undergoing revision in Parliament in late 2014, and some observers expect the law to pass in 2016. A hindrance to foreign direct investment is the difficulty of getting established Azerbaijani businesses to adopt standard investor-friendly practices, such as those associated with the concept of good corporate governance or international accounting norms.

2. Conversion and Transfer Policies

Foreign Exchange

There are no restrictions on converting or transferring funds associated with an investment into freely usable currency at a legal, market-clearing rate. Foreign exchange transactions are governed by the Law on Currency Regulation. The Central Bank administers the overall enforcement of currency regulation. It requires that local cash sales be conducted in Azerbaijani manats (AZN), in accordance with the Constitution. Foreign companies and individuals may have both manat and foreign currency accounts at a local bank. Currency conversion is carried out through the Baku Interbank Currency Exchange Market (BICEX) and the Organized Interbank Currency Market. The average time for remitting investment returns is two to three business days. Some requirements on disclosure of the source of currency transfers have been imposed in an attempt to reduce illicit transactions. Azerbaijan's foreign currency reserves declined from \$11 billion in March 2015 to \$4 billion in March 2016, due to Central Bank interventions to support the country's manat currency. The country's strategic currency reserves amounted to \$37.5 billion in December 2015, which included both the Central Bank's foreign currency reserves (\$4 billion) and Azerbaijan's sovereign wealth fund (SOFAZ) assets (\$33.5 billion). Since the December 21, 2015 devaluation of the manat, there has been a managed floating currency that has fluctuated between 1.55 to 1.8 manats to the dollar. On January 13, 2016 the Central Bank annulled the license of foreign exchange offices; therefore, currency exchange can be conducted only in banks and airports.

Remittance Policies

Foreign investors are subject to a corporate branch remittance tax of 10 percent on the remittance of all profits derived from business activities in Azerbaijan. There have not been any recent changes or plans to change investment remittance policies that either tighten or relax access to foreign exchange for investment remittances. There do not appear to be time limitations on remittances, including dividends; return on investment, interest and principal on private foreign debt; lease payments; royalties; and management fees. There do not appear to be limitations on the inflow or outflow of funds for remittances of profits or revenue. Azerbaijan is a Financial Action Task Force (FATF) permanent member and is listed as a country of concern. (The continuum of FATF listings are countries of primary concern, countries of concern, and monitored.) The main obstacle Azerbaijan faces is the endemic

level of corruption, but other generators of illicit funds include robbery, tax evasion, smuggling, trafficking, and organized crime.

For further guidance on corporate tax policies see:

[http://www.ey.com/Publication/vwLUAssets/EY-business-guide-azerbaijan-2015/\\$FILE/EY-business-guide-azerbaijan-2015.pdf](http://www.ey.com/Publication/vwLUAssets/EY-business-guide-azerbaijan-2015/$FILE/EY-business-guide-azerbaijan-2015.pdf)

3. Expropriation and Compensation

The Law on the Protection of Foreign Investments protects foreign investors against nationalization and requisition, except under certain specified circumstances. The nationalization of property can occur when authorized by parliamentary resolution, although there have been no known cases of official nationalization or requisition against foreign firms in Azerbaijan. Requisition – by a decision of the Cabinet of Ministers – is possible in the event of natural disaster, an epidemic, or other extraordinary situation. In the event of nationalization or requisition, foreign investors are entitled to prompt, effective, and adequate compensation.

According to a local research organization (The Public Association for Assistance to a Free Economy), “Azerbaijani legislation allows the government to expropriate property in limited cases only, such as: a) for the construction of highway and communications infrastructure; b) for the protection of state borders; c) for the construction of defense and security premises; d) construction of extractive facilities. National law provides that a court order is required to expropriate property in Azerbaijan. Under national law, the government is required to purchase any property it expropriates at market value and pay an additional 20 percent of market value as compensation to the owners.”

Source: http://www.freeeconomy.az/site/assets/files/1308/property_rights_in_azerbaijan.pdf

The Government of Azerbaijan has not shown any pattern of discriminating against U.S. persons by way of direct expropriations. Indirect expropriation, such as confiscatory tax regimes, is sometimes employed against international companies due to widespread corruption and monopolistic attempts to stifle competition.

4. Dispute Settlement

Legal System, Specialized Courts, Judicial Independence, Judgments of Foreign Courts

The Azerbaijani legal system is based on Civil Law. Disputes or disagreements arising between foreign investors and enterprises with foreign investment, state bodies of Azerbaijan, and/or enterprises, public organizations and other legal entities of Azerbaijan, are to be settled in the court systems of Azerbaijan or, on agreement between the parties, in a court of arbitration, including international arbitration bodies. However, the current judicial process is not reliable in practice. While the laws on the books promote foreign investment, in practice investment disputes can arise when a foreign investor or trader's success threatens well-connected or favored local interests.

The judiciary consists of the Constitutional Court of the Republic of Azerbaijan, the Supreme Court of the Republic of Azerbaijan, the appellate courts of the Republic of Azerbaijan, trial courts, and other specialized courts. The Supreme Court and appellate courts have civil, criminal, administrative, economic, and military panels. Trial court judgments may be

appealed in appellate courts and the judgments of appellate courts can be appealed in the Supreme Court. The Supreme Court is the highest court in the country. Under the Civil Procedure Code of Azerbaijan, the judgments of the appellate court are published within three days of issuance but may, in exceptional circumstances, be published within ten days. The Constitutional Court has the authority to review laws and court judgments for compliance with the Constitution. The decisions of the Constitutional Court are published. Additionally, on February 3, 2016, President Aliyev established Boards of Appeal in the State Committee for Property Issues and the State Customs Committee to ensure transparency and impartiality in the review of complaints from entrepreneurs concerning their business operations.

The procedure for the enforcement of foreign judgments in Azerbaijan is established by the Civil Procedure Code. The Code only requires the enforcement of foreign judgments either pursuant to an international treaty or based on the principle of reciprocity and provides that foreign arbitral awards may be enforced in Azerbaijan, only so long as they do not contravene local legislation or public policy, and if reciprocity exists. A Bilateral Investment Treaty between the United States and Azerbaijan – which came into effect in 2001 – provides U.S. investors with recourse for the settlement of investment disputes through the International Center for the Settlement of Investment Disputes.

The Law on Protection of Foreign Investments, dated January 15, 1992 (the Foreign Investment Law), provides guidance to foreign investors seeking to resolve investment disputes, either through Azerbaijani courts or alternatively through dispute resolution procedures agreed to by the parties involved. Resolution of investment disputes may include international arbitration, either in Azerbaijan or abroad. The Law on International Arbitration, dated November 18, 1999 (the Arbitration Law), provides guidance on the conduct of international arbitration in Azerbaijan.

Azerbaijan has entered into several other bilateral treaties – principally with neighboring states – to facilitate the enforcement of foreign judgments, and is a party to the 2004 Commonwealth of Independent States (CIS) Convention on Mutual Legal Assistance in Civil, Family and Criminal Cases. In addition, Azerbaijan is a party to the Convention on Resolving Business Disputes, dated March 20, 1992 (also known as the Kyiv Convention). Azerbaijan is also a member of the Multilateral Investment Guarantee Agency (MIGA).

Bankruptcy

Azerbaijan's Bankruptcy Law, which does not function effectively and is rarely used, continues to be a hindrance to economic development, as does the country's weak credit reporting institutions. Under this law, which applies only to legal entities and entrepreneurs, not individuals, bankruptcy proceedings may be commenced by either a debtor facing insolvency or any creditor. In general, the legislation is focused on liquidation procedures. For example, a court-approved "rehabilitation plan" may not exceed two years.

The World Bank's Doing Business Report includes in its country rankings the ease of "resolving insolvency" (rankings are available at: <http://www.doingbusiness.org/data/exploreeconomies/azerbaijan/resolving-insolvency>). Azerbaijan ranks 84 out of 189 countries in this category.

Investment Disputes

Over the past 10 years, there has not been any visible pattern of investment disputes that have specifically discriminated against U.S. persons or other foreign investors. Property disputes have occasionally appeared in local media, as discussed above.

International Arbitration

The Law on International Arbitration guides the process of international arbitration in Azerbaijan:

“Under these rules, parties may select independent arbitrators of any nationality, proceedings may be conducted in any language chosen by the parties, the applicable law (except for those matters that must be exclusively resolved under Azerbaijani legislation) and arbitration procedure may be chosen by the parties, and, in general, parties may stipulate the terms of the arbitration process. Where the terms have not been stipulated by the parties, any omission may be resolved by the Supreme Court of the Republic of Azerbaijan.”

Source:

http://www.bakermckenzie.com/files/Uploads/Documents/Supporting%20Your%20Business/Global%20Markets%20QRGs/DBI%20Azerbaijan/bk_dbi_azerbaijan_judicialsystem.pdf

ICSID Convention and New York Convention

Azerbaijan is a member of the International Convention on the Settlement of Investment Disputes between States and Nationals of Other States (ICSID convention). Azerbaijan is also a party to the 1958 Recognition and Enforcement of Foreign Arbitral Awards (New York Convention), which provides for the recognition of foreign arbitral awards resulting from international arbitration.

Duration of Dispute Resolution – Local Courts

The length of time it takes to obtain a resolution on an investment/commercial dispute proceeding within Azerbaijan varies considerably.

5. Performance Requirements and Investment Incentives

WTO/TRIMS

Azerbaijan is not a member of the World Trade Organization (WTO). Azerbaijan's Working Party was established on July 16, 1997 and the first meeting of the Working Party was held in June 2002. Negotiations regarding market access are underway on the basis of revised offers in goods and services. Since December 2013, multilateral work has been proceeding on the basis of a Draft Working Party Report. The twelfth meeting of the Working Party took place in Geneva in March 2015.

Ongoing issues pending resolution include the application of discriminatory tax exemptions in Azerbaijan, production sharing agreements, local content requirements and investment incentives, state trading enterprises, permit requirements for alcohol and tobacco products, Azerbaijan's commitment to join the Information Technology Agreement, existing technical barriers to trade (product standards and certification), transition periods for implementing WTO Agreements, and agricultural and non-agricultural export subsidies. Since Azerbaijan is not a WTO member, it has also not ratified the *Agreement on Trade Related Investment Measures (TRIMs)*.

Investment Incentives

In 2016, an investment promotion certificate was introduced in Azerbaijan by the Presidential decree on additional measures in investment promotion. Investment certificate holders are exempt from paying 50 percent of income tax and land tax and from paying customs duties on machinery, equipment, and devices imported for investment purposes in priority industries of the economy for up to 7 years. The priority projects include work in industrial parks, creation of manufacturing plants, and research work.

Research and Development

There are no restrictions on the ability of U.S. and/or other foreign firms to participate in government-financed and/or subsidized research and development programs in Azerbaijan.

Performance Requirements

Performance requirements are generally not imposed on new investments, but investors who participate in the privatization process often assume specific obligations regarding future investment and employment. Foreign investors are not normally required to purchase from local sources or export a certain percentage of output. Except for certain state monopolies, there is no explicit requirement that nationals own shares in enterprises. Investors in Production Sharing Agreements (PSAs) assume obligations and requirements as provided within the PSA.

There is, however, an overall limit on the number of foreign workers permitted in Azerbaijan, as well as specific additional limits in the numbers of foreign workers permitted in particulate sectors, such as mining, oil and gas, and the media sectors. Employers wishing to hire foreign workers in Azerbaijan must obtain a license from the Ministry of Labor. Foreigners who wish to work in Azerbaijan must register with local authorities at their place of residence and obtain work permits from the State Migration Service. If foreign workers enter Azerbaijan without work permits, and have to extend their visits for more than 90 days within one calendar year, they are required to submit work permit applications within 30 days of arrival. Not submitting this documentation can lead to deportation/removal from Azerbaijan and potentially steep fines.

In 2014, the Cabinet of Ministers ruled that business travelers in specific industries may work in Azerbaijan for up to 90 days per year without having a work permit. The eight industry sectors that fall under this provision are: education; finance and insurance; information and communication technology; manufacturing; mining; power, gas, steam and artificial atmosphere supply; transportation; and water supply and sewage treatment. According to this new provision, business travelers in sectors not covered above may need to apply for work permits even for trips under 90 days.

Sole proprietors, heads of representative offices, and branches of foreign legal entities and their deputies, short-term (three months or less) , accredited foreign media representatives, education specialists, diplomats and international civil servants do not require work permits. As of July 2009, the State Migration Service (SMS) decreed a one-stop shop system for work and residency permits. According to this single window principle, within seven days of application, foreigners applying for residence and work permits should receive these documents, although not all applicants experience this level of efficiency. As of 2015, the fee

to acquire a one-year license for a migrant worker is equal to 1,000 manats (approximately \$600).

Despite these regulations, major U.S. and other international firms have reportedly encountered problems registering their expatriate employees with the State Migration Service.

Data Storage

There are no requirements for foreign IT providers to turn over source code or provide access to surveillance (backdoors into hardware/software or turn over keys for encryption).

6. Protection of Property Rights

Real Property

In 2006, the Government centralized the processing of residential real estate transactions through a network of notary offices under the Ministry of Justice. Since 2013, Azerbaijan's State Real Estate Registry Service at the Committee for Property Issues has been the lead agency that manages the real estate registration system. Azerbaijan has been working with the World Bank to improve the property registration system, but the system remains awash with bureaucratic requirements and is generally seen as prone to corruption and inefficient. In 2016, the Index of Economic Freedom gave Azerbaijan less than favorable scores regarding the protection of private property rights.

The World Bank's Doing Business Report includes Azerbaijan in its country rankings on the Ease of Registering Property. Rankings are available at:

<http://www.doingbusiness.org/data/exploreeconomies/azerbaijan/#registering-property>.

Azerbaijan ranked 22nd out of 189 countries in this category in 2015.

References: <http://www.heritage.org/index/country/azerbaijan>

Intellectual Property Rights

In Azerbaijan, the legal structure covering IP protections is relatively strong. However, the level of enforcement within the country could be improved. Piracy and blatant infringements on intellectual property rights, such as fake international computer shops that are open for business in the capital, are commonplace. The Business Software Alliance put the software piracy figure at 85 percent in 2013. Moreover, the estimated value of unlicensed software in Azerbaijan was \$103 million in 2013, compared to \$52 million in 2009.

In the mid-1990s, Azerbaijan began implementing a national system for registering and protecting intellectual property rights (IPR) with the assistance of the World Intellectual Property Organization (WIPO), of which it is a member. Intellectual property rights in Azerbaijan include protections on all types of property, including inventions, industrial designs, utility models, trademarks, geographic names, domain names, and copyright and related rights. The process of registering each type of intellectual property is relatively straightforward. Azerbaijan enacted improved copyright legislation (Law on Copyright and Related Rights) in 1996 (amended in 2008), patent legislation (Law on Patents) in 1997, and trademark protection legislation (Law on Trademarks and Geographic Names) in 1998. The law On Securing Intellectual Property Rights and Combating Piracy, which was ratified in October 2012, brought Azerbaijan's intellectual property regime more closely in line with the

WTO Trade-Related Intellectual Property Rights (TRIPS) agreement and satisfied many of the requirements of the WTO Working Party as part of Azerbaijan's WTO accession process.

Azerbaijan also is a party to the Convention Establishing the World Intellectual Property Organization, the Paris Convention for Protection of Industrial Property, and the Berne Convention for the Protection of Literary and Artistic Works. Azerbaijan is a party to the Geneva Phonograms Convention, and acceded to the two WIPO Internet treaties in 2005. Violation of intellectual property rights can result in civil, criminal, and administrative charges.

Azerbaijan tracks and reports on seizures of counterfeit goods, but does not publish statistics on this.

Resources for Rights Holders

For additional information about treaty obligations and points of contact at local IP offices, please see WIPO's country profiles at <http://www.wipo.int/directory/en/>.

Embassy POC:

Aleksey Sanchez
ECONOMIC AND COMMERCIAL SECTION
U.S. Embassy Baku, Azerbaijan
+994 12 488-3300
BakuCommercial@state.gov

A list of local lawyers is available at: http://azerbaijan.usembassy.gov/legal_info.html

Additional Resources in Azerbaijan include:

The American Chamber of Commerce in Azerbaijan:

+994 12 497-1333
Fax: +994 12 497-1091
chamber@amchamaz.org
<http://amchamaz.org/>

7. Transparency of the Regulatory System

The Government of Azerbaijan has worked to improve its regulatory system over the past several years, using transparent policies and effective laws to foster competition and establish clear rules of the game. Legal, regulatory, and accounting systems are slowly approaching international norms. However, continued limited transparency and allegations of corruption in the regulatory system remain a problem. Draft bills are not made available for public comment or run through a public consultation process. Azerbaijan has yet to develop informal regulatory processes managed by private sector associations. This limited transparency and inconsistent enforcement of rules to foster competition are serious impediments to foreign direct investment.

In August 2013, Azerbaijan's Parliament passed a law on the regulation of inspections in entrepreneurship and the protection of the rights of entrepreneurs. Following the law, businesses are to be divided into high, medium, and low risk groups, with the frequency of inspections regulated by these risk categories. Entrepreneurs who have not committed any legal infraction for a set period of time are categorized as low risk groups, which will result in

less frequent inspections and may reduce opportunities for soliciting informal payments. On October 19, 2015, President Aliyev signed a decree that inspections for entrepreneurs will be suspended for two years, starting from November 1, 2015.

In October 2011, the President of Azerbaijan issued a decree calling on the Cabinet of Ministers to develop a Law on Licenses and Permits. The IFC and USAID have provided assistance in this effort. Despite plans to adopt 29 national accounting standards, so as to be in line with International Financial Reporting Standards (IFRS) by 2009, as of 2015 audited financial statements have only been adopted in the banking and finance sectors, and in the energy sector by the State Oil Company of the Azerbaijan Republic (SOCAR).

8. Efficient Capital Markets and Portfolio Investment

Azerbaijan has an underdeveloped financial services sector – of which banking comprises more than 90 percent – that inhibits economic stability, growth and diversification. Non-bank financial sector staples such as capital markets, insurance, and private equity are in the early stages of development. An effective regulatory system that encourages and facilitates portfolio investment, foreign or domestic, is not fully in place. There is not sufficient liquidity in the markets to enter and exit sizeable positions, and existing policies limit the free flow of financial resources into the product and factor markets. However, the Government of Azerbaijan and Central Bank respect IMF Article VIII by refraining from restrictions on payments and transfers for current international transactions, and credit is allocated on market terms. Foreign investors are also able to obtain credit on the local market, and the private sector has access to a variety of credit instruments.

In February 2016, the Financial Market Supervisory Body, a new financial supervisory authority, was established in Azerbaijan to take over all functions of the Azerbaijan State Committee for Securities, State Insurance Supervision Service under the country's Ministry of Finance and Financial Monitoring Service under the Central Bank of Azerbaijan. The Financial Market Supervisory Body aims to license, regulate and control the securities market, investment funds, insurance, credit organizations (banks, non-banking credit organizations and operator of postal communication) and payment systems, as well as to improve the oversight system on money laundering, preventing the financing of terrorism, and provide transparency and efficiency in this sphere.

Money and Banking System, Hostile Takeovers

Over the past decade, the banking sector has benefited from the government's investment of oil revenues in the non-oil economy, and the rapid expansion of higher margin retail and micro-lending. With oil revenues declining, Azerbaijan's banking sector faced significant increases in nonperforming loans. The prevalence of cash transactions – estimated at 70 percent by Central Bank authorities – hinders the financial system's development. Non-resident foreigners may legally establish bank accounts in Azerbaijan. There have been no public cases of hostile take-overs in Azerbaijan.

By February 2016, there were 36 banks registered in Azerbaijan, including 22 banks with international activities. Twelve banks were either closed or consolidated following the December 21 devaluation, as a result of non-performing loans, lack of liquidity, and overall economic downturn due to decreased revenue from oil exports. Because banks rarely compete directly against each other for market share, they have little incentive to offer

competitive terms. Commercial loan interest rates offered by banks in 2014-2015 varied between 16-34 percent.

Total banking sector assets stood at approximately \$22 billion as of January 2016, with the top five banks holding almost 58 percent of this figure. The state-owned International Bank of Azerbaijan (IBA) accounts for approximately 35-50 percent of the country's banking assets and has received several large cash infusions over the past several years from the government to ensure its solvency. The Central Bank of Azerbaijan has been focused on encouraging consolidation in the sector, and in August 2012 the CBA raised the minimum capital requirement from 10 million manats to 50 million manats, effective January 1, 2014.

Several recent projects designed to strengthen Azerbaijan's financial services sector, including the Capital Market Modernization Project (CMMP), the diversification of the State Oil Fund's (SOFAZ) investment strategy, and pension reform represent opportunities for U.S. firms that provide asset management and global custodian services.

Although the Baku Stock Exchange (BSE) was established in 2000, the securities market still is at an early stage of development. The CMMP is an attempt by the Government of Azerbaijan to build the foundation for a modern financial capital market, including the development of market infrastructure and automation, and the strengthening of the legal and market frameworks for capital transactions. One major hindrance to the stock market's growth is the difficulty in encouraging established Azerbaijani businesses to adapt to standard investor-friendly practices of good corporate governance that are required of publicly listed companies.

In February 2016, Fitch Ratings downgraded Azerbaijan's long-term foreign and local currency Issuer Default Ratings (IDR) to BB+ from BBB-. The outlook is negative. Standard & Poor also downgraded Azerbaijan's credit rating to BB+ from BBB- on January 29, 2016 and forecast that country's economy would shrink this year as exports fall and the currency devaluations curbs consumption. In February 2016, Moody's Investors Service downgraded Azerbaijan's government bond and issuer ratings to Ba1 from Baa3 and placed the ratings on review for further downgrade.

9. Competition from State-Owned Enterprises

In Azerbaijan, state-owned enterprises (SOEs) are active in the oil and gas, power generation, water supply, railway, and air passenger and cargo sectors. There is no published list of SOEs. Statistics are not available on the percentage of resources SOEs allocate to research and development (R&D). While there are no SOEs that officially have been delegated governmental powers, companies such as the SOCAR, Azerenerji (electricity) and Azersu (water) – all of which are closed joint-stock companies with majority state ownership and limited private investment – enjoy quasi-governmental or near-monopoly status in their respective sectors.

Many powerful state-owned enterprises can use their regulatory authority to block new entrants into the market – a clear conflict of interest. In sectors that are open to both the private sector and foreign competition, SOEs generally receive a larger percentage of government contracts or business than their private sector competitors. While SOEs regularly purchase or supply goods or services from private sector firms, domestic or foreign, private enterprises cannot compete with SOEs under the same terms and conditions with respect to market share, products and services, or incentives. Private enterprises do not have the same

access (including terms) to financing as SOEs. However, SOEs are subject to the same tax burden and tax rebate policies as their private sector competitors. The SOEs are also afforded material advantages such as preferential access to land and raw materials, advantages that are not available to private enterprises. There is little information available on Azerbaijani SOEs' budget constraints due to the limited transparency in their financial accounts.

OECD Guidelines on Corporate Governance of SOEs

Information is not available on the extent to which SOEs in Azerbaijan adhere to the OECD Guidelines on Corporate Governance for SOEs:

Sovereign Wealth Funds

Azerbaijan's sovereign wealth fund is the State Oil Fund of Azerbaijan (SOFAZ). Its mission is to transform depleting hydrocarbon reserves into financial assets generating perpetual income for current and future generations and to finance strategically important infrastructure and social projects of national scale. Since it was established in 1999, SOFAZ has financed several projects relating to infrastructure, housing, energy infrastructure, and education. According to its bylaws, SOFAZ is not permitted to invest domestically. SOFAZ publishes an annual report and submits its books to an independent audit. The fund's assets totaled \$33.5 billion as of January 1, 2016.

10. Responsible Business Conduct

Responsible business conduct (RBC) is a relatively new concept in Azerbaijan. Producers and consumers do not have a general awareness of responsible business conduct, including environmental, social, and governance issues. No information is available on legal corporate governance, accounting, and executive compensation standards to protect shareholders in Azerbaijan. Larger foreign entities tend to follow generally accepted RBC principles – mainly in line with their international corporate ethos – and aim to educate their local partners, who generally consider basic charitable donations and paying taxes as acts of social responsibility. The American Chamber of Commerce in Azerbaijan established a Corporate Social Responsibility Committee in October 2011 to encourage companies to embrace the concept of social responsibility and encourage a positive impact through activities and dialogue with relevant stakeholders. The Chamber also has published a guide on RBC/corporate social responsibility for businesses in Azerbaijan. The standards of corporate governance, evaluation methodology of the application of these standards and the Code of ethical behavior in corporate governance sphere were developed by the Ministry of Economy in 2011. The ministry's task is to hold meetings with entrepreneurs and explain the importance of using corporate governance standards.

11. Political Violence

There have been no known acts of political violence against U.S. businesses or assets, nor against any foreign owned entity.

12. Corruption

Pervasive corruption – including bribery of public officials – continues to be a major challenge for U.S. and other international firms operating in Azerbaijan. Although anti-corruption legislation is in place and the government has taken some steps to tackle low-

level corruption, corrupt practices remain a barrier to greater foreign investment. Azerbaijan does not require private companies to establish internal codes of conduct that, among other things, prohibit bribery of public officials, nor does it provide protections to NGO's involved in investigating corruption. Nevertheless, some private companies use internal controls, ethics, and compliance programs to detect and prevent bribery of government officials. United States firms have identified pervasive corruption as an obstacle to FDI in the following sectors: government procurement, awarding of licenses or concessions, transfers, performance requirements, dispute settlement, regulatory system, customs, and taxation.

The Government of Azerbaijan recognizes that corruption is a problem, and has been a participant in regional anti-corruption initiatives, but to date laws and regulations to combat corruption have not been effectively or consistently enforced. Azerbaijan has made modest progress in implementing a 2005 Anticorruption Law, which created a commission with the authority to require full financial disclosure from government officials.

On September 5, 2012, President Aliyev issued a decree for a National Action Plan on Open Government and a National Action Plan on Combating Corruption. The government is reviewing both of these plans to develop a new action plan to be adopted in 2016. ASAN service centers created by the State Agency for Public Service and Social Innovations under the President of the Republic of Azerbaijan were established in July 2012 by Presidential decree and became operational in February 2013. Eleven centers provide 30 government services from nine state entities, including the registration of commercial legal entities and tax payers, notary services, state registration of civil status acts, and the renewal of identity cards/passports of citizens. ASAN centers are intended to provide more transparent and accountable services through a "one window" model that reduces opportunities for rent-seeking and petty government corruption.

In 2015, Azerbaijan's modest improvements in combating petty corruption were reflected by the global anticorruption watchdog Transparency International, which ranked Azerbaijan 119 out of 168 countries on its Corruption Perceptions Index. Popular opinion identifies the State Customs Committee as the institution of greatest concern to businesses in Azerbaijan, followed by the Ministry of Taxes – though the reputation of the customs and tax authorities has begun to improve recently as corruption-reducing reforms are implemented. Transparency's 2013 Global Corruption Barometer – which examined bribery involved in people's contact with customs, education, the judiciary, land related services, medical services, the police, registry and permit services, tax authorities and utilities – found that roughly 50 percent of Azerbaijani respondents had paid a bribe to one of the nine service providers in the twelve preceding months.

UN Anticorruption Convention, OECD Convention on Combatting Bribery

Azerbaijan signed and ratified the UN Anticorruption Convention and is a signatory to the Council of Europe Criminal and Civil Law Conventions. Azerbaijan is not currently a party to the OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions.

Azerbaijan has also been a participant in the Extractive Industries Transparency Initiative (EITI). In 2009, Azerbaijan became the first participating country to become fully compliant with EITI requirements. Azerbaijan [was downgraded to "candidate" country at the 29th EITI Board meeting in Brazzaville](#) in April 2015, due to [deep concerns](#) about the ability of civil society to engage fully in the EITI process in Azerbaijan. The EITI will review in May 2016

Azerbaijan's status for its compliance with measures EITI recommended for Azerbaijan to undertake in order for it to be reestablished as a candidate country.

Resources to Report Corruption

Contact at Government of Azerbaijan responsible for combating corruption:

Kamal Jafarov
Acting Executive Secretary
Commission on Combating Corruption
Baku, Azerbaijan
(+994 12) 492-04-65
kamal.jafarov@antikorrupsiya.gov.az

Contact at Transparency Azerbaijan (local chapter of Transparency International):

Rena Safaraliyeva
Executive Director
Transparency Azerbaijan
Baku, Azerbaijan
(+994 12) 497 81 70
rena@transparency.az

13. Bilateral Investment Agreements

Bilateral Taxation Treaties

Azerbaijan has signed 48 Bilateral Investment Treaties (BIT) – including one with the United States – and 40 Tax Treaties to protect against double taxation.

The 2001 BIT between the United States and the Government of the Republic of Azerbaijan encourages the reciprocal protection of investment.

Azerbaijan also has bilateral investment treaties with the following countries: Albania, Austria, Belarus, Belgium, Bulgaria, Czech Republic, China, Croatia, Egypt, Estonia, Finland, France, Georgia, Germany, Greece, Iran, Israel, Italy, Jordan, Kazakhstan, Korea, Kyrgyzstan, Latvia, Lithuania, Lebanon, Macedonia, Montenegro, Moldova, Norway, Pakistan, Poland, Qatar, Romania, Russia, Serbia, Saudi Arabia, Syria, Switzerland, Tajikistan, Turkey, UAE, Ukraine, the United Kingdom, and Uzbekistan.

The United States currently does not have a tax treaty with Azerbaijan. The United States and Azerbaijan are however parties to the OECD Convention on Mutual Administrative Assistance in Tax Matters. Azerbaijan signed an intergovernmental agreement with the United States to implement the Foreign Account Tax Compliance Act (FATCA) on October 9, 2015, based on the "IGA Model 1a" form.

14. Foreign Trade Zones/Free Ports/Trade Facilitation

Although the government announced its intention to create special economic zones in 2003 – and passed a law to establish such zones in 2009 – there are no foreign trade zones or free ports operating in Azerbaijan yet. President Aliyev signed a decree on March 17, 2016 on measures to create a free trade zone special economic area next to the Alat seaport, located 65 km of Baku. According to the decree, the Ministry of Economy should submit

proposals on the creation of the free trade zone, including legislation, development concept, types of entrepreneurial activity, infrastructure and management to President Aliyev within six months. There may be commercial opportunities for international firms to be involved in this project with consulting, management, and engineering.

The Ministry of Communications and High Technologies has discussed plans to create other special economic zones, including a petrochemical complex and regional innovation zones to boost development of the telecommunications sector and turn Azerbaijan into a regional information and communications technologies hub, and a special zone to encourage the production of renewable energy. Such projects represent consulting, engineering, and other commercial opportunities for international firms.

15. Foreign Direct Investment and Foreign Portfolio Investment Statistics

Table 2: Key Macroeconomic Data, U.S. FDI in Host Country/Economy

	Host Country Statistical source*		USG or international statistical source		USG or International Source of Data: BEA; IMF; Eurostat; UNCTAD, Other
Economic Data	Year	Amount	Year	Amount	
Host Country Gross Domestic Product (GDP) (\$M)	2015	\$34.3 billion	2014	\$75.2 billion	www.worldbank.org/en/country
Foreign Direct Investment	Host Country Statistical source*		USG or international statistical source		USG or international Source of data: BEA; IMF; Eurostat; UNCTAD, Other
U.S. FDI in partner country (\$M, stock positions)	2014	\$89.3 million	2014	\$15 million	BEA data available at http://bea.gov/international/direct_investment_multinational_companies_comprehensive_data.htm
Host country's FDI in the United States (\$M, stock positions)	2015	N/A	2015	N/A	N/A

Total inbound stock of FDI as % host GDP	2015	<0%	2015	<0%	N/A
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*<http://www.stat.gov.az/source/finance/indexen.php>

Table 3: Sources and Destination of FDI

Direct Investment from/in Counterpart Economy Data					
From Top Five Sources/To Top Five Destinations (US Dollars, Millions)					
Inward Direct Investment- from 2014 statistics			Outward Direct Investment		
Total Inward	11,697.7	100%	Total Outward		100%
Turkey	481.4 million	4%			
U.K.	153.5 million	1%			
Netherlands	103.8 million	0.8%			
UAE	90.2 million	0.77%			
U.S.A.	89.3 million	0.76%			

"0" reflects amounts rounded to +/- \$500,000.

Table 4: Sources of Portfolio Investment

*<http://www.stat.gov.az/source/finance/indexen.php>

IMF Coordinated Portfolio Investment Survey data are not available for Azerbaijan.

Section 5 - Government

Chiefs of State and Cabinet Members:

For the current list of Chief of State and Cabinet Members, please access the following - [Central Intelligence Agency online directory of Chiefs of State and Cabinet Members of Foreign Governments](#)

Legal system:

civil law system

International organization participation:

ADB, BSEC, CD, CE, CICA, CIS, EAPC, EBRD, ECO, EITI (compliant country), FAO, GCTU, GUAM, IAEA, IBRD, ICAO, ICC (NGOs), ICRM, IDA, IDB, IFAD, IFC, IFRCs, ILO, IMF, IMO, Interpol, IOC, IOM, IPU, ISO, ITSO, ITU, ITUC (NGOs), MIGA, NAM, OAS (observer), OIC, OPCW, OSCE, PFP, SELEC (observer), UN, UN Security Council (temporary), UNCTAD, UNESCO, UNHCR, UNIDO, UNWTO, UPU, WCO, WFTU (NGOs), WHO, WIPO, WMO, WTO (observer)

Section 6 - Tax

Exchange control

There are no restrictions on the import or export of capital. Supporting documentation, including tax payment documents and bank statements, must be submitted when cash withdrawals exceed amounts previously imported into the country. Repatriation payments may be made in any currency, and both residents and nonresidents can hold bank accounts in any currency

Treaty and non-treaty withholding tax rates

Information unavailable

Methodology and Sources

Section 1 - General Background Report and Map

(Source: [CIA World Factbook](#))

Section 2 - Anti – Money Laundering / Terrorist Financing

	Lower Risk	Medium Risk	Higher Risk
FATF List of Countries identified with strategic AML deficiencies	Not Listed	AML Deficient but Committed	High Risk
Compliance with FATF 40 + 9 recommendations	>69% Compliant or Fully Compliant	35 – 69% Compliant or Fully Compliant	<35% Compliant or Fully Compliant
US Dept of State Money Laundering assessment (INCSR)	Monitored	Concern	Primary Concern
INCSR - Weakness in Government Legislation	<2	2-4	5-20
US Sec of State supporter of / Safe Haven for International Terrorism	No	Safe Haven for Terrorism	State Supporter of Terrorism
EU White list equivalent jurisdictions	Yes		No
International Sanctions UN Sanctions / US Sanctions / EU Sanctions	None	Arab League / Other	UN , EU or US
Corruption Index (Transparency International) Control of corruption (WGI) Global Advice Network	>69%	35 – 69%	<35%
World government Indicators (Average)	>69%	35 – 69%	<35%
Failed States Index (Average)	>69%	35 – 69%	<35%
Offshore Finance Centre	No		Yes

Section 3 - Economy

General Information on the current economic climate in the country and information on imports, exports, main industries and trading partners.

(Source: [CIA World Factbook](#))

Section 4 - Foreign Investment

Information on the openness of foreign investment into the country and the foreign investment markets.

(Source: [US State Department](#))

Section 5 - Government

Names of Government Ministers and general information on political matters.

(Source: [CIA World Factbook](#) / <https://www.cia.gov/library/publications/world-leaders-1/index.html>)

Section 6 - Tax

Information on Tax Information Exchange Agreements entered into, Double Tax Agreements and Exchange Controls.

(Sources: [OECD](#) [PKF International](#))

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Gary Youinou

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