

Validation of AZERBAIJAN
Validation Report
Sustainable Development Strategies Group (SDSG), Independent Validator
09 October 2016

1. BACKGROUND

Azerbaijan was accepted as an EITI Candidate in 2007 and was the first country to become EITI compliant in 2009. It has produced EITI reports in a timely fashion since 2005, however, concerns surrounding civil society participation prompted the EITI Board to request the country to undergo early Validation in 2015 against the EITI Standard. The Board found that Azerbaijan was not compliant but had made meaningful progress in implementing the EITI, thus designating it a Candidate rather than Compliant country. The Board established corrective actions for Azerbaijan to be completed by 15 April 2016 regarding civil society engagement, the work plan, public debate, and impact, adding that it was not possible to assess compliance with requirements 2, 3, 4, and 5 on EITI disclosures in the absence of an approved 2013 EITI Report. The EITI Board decided on 1 June 2016 that Azerbaijan should undergo a second Validation commencing on 1 July 2016 to verify whether these corrective actions have been completed and outstanding requirements met.

Pursuant to the revised Validation procedure approved by the Board in February 2016, the International Secretariat was tasked with the first phase of reviewing relevant documents, conducting stakeholder consultations, and producing the team's initial assessment of progress (the "Initial Assessment"). SDSG was appointed as the independent Validator to evaluate whether the Secretariat's work was carried out in accordance with the Validation Guide through a review of relevant documentation and the Initial Assessment, a risk-based approach for spot checks, and further consultations with stakeholders. SDSG will review and amend the Secretariat's Assessment, as needed, and summarize its evaluation in a Validation Report for submission to the Board.

- [Comments on the Initial Assessment](#)

The Secretariat's work entailed a review of relevant documents from 21 June-20 July 2016, a country visit by a three-person team from the Secretariat that conducted stakeholder consultations from 3-9 July 2016, and the production of the Initial Assessment. These tasks were undertaken by the Secretariat's team in accordance with the 2016 Validation Guide. Well organized and clear, the Initial Assessment thoroughly discusses the requirements and evaluates Azerbaijan's level of progress. Supporting documents and stakeholder input are cited, where appropriate and available. The Assessment should, however, consistently use the designations with respect to level of progress assigned by the 2016 Validation Guide (satisfactory, meaningful, inadequate, or no progress). With their specific definitions, these are intended to facilitate consistency across assessments and Validations. It may be confusing when the Assessment uses other terms to describe levels of progress or compliance, such as "significant progress." Similarly, it may also be confusing when a requirement is assessed as being met with satisfactory progress when it is more accurately not applicable.

- [Work Performed by the Independent Validator](#)

The Secretariat requested submission of the Validation Reports for Azerbaijan and four other countries before the Board meeting in Astana in late October. Both pdf and editable versions of the Initial Assessments for these countries were transmitted to the SDSG Validation Team in September 2016, with MSG comments for most of these pending. The Validation Team committed to undertake this task through: (1) In-depth review and marking up of the EITI Assessment by the team; (3) Detailed review and comments by Multi-Stakeholder Specialist of Requirements 1 and 7; (4) Detailed review

and comments by Financial Specialist of Requirements 2 through 6; and (5) Overall drafting lead and detailed review of all assessments by the Team Leader.

- [Comments on the Limitations of the Assessment](#)

The most significant challenge for the Validation Team has been the compressed time frame within which to undertake its review of EITI implementation in Azerbaijan. Stakeholder outreach was not practicable and detailed review of documentation beyond the Initial Assessments was necessarily limited. It should be noted, however, that the Validator is not expected to duplicate the data collection and consultation work completed by the Secretariat. Neither is it permitted to consider activities conducted after 01 July 2016, per express directive of the Board. Notwithstanding these limitations, the Validation Team has carefully reviewed the Secretariat's Initial Assessment and applicable references to determine Azerbaijan's level of progress against the different requirements of the 2016 Standard.

2. [GENERAL COMMENTS](#)

- [Progress on EITI Implementation](#)

Azerbaijan's progress on EITI implementation may be described as strikingly uneven – its sustained commitment to timely reporting and focus on EITI mainstreaming are impressive and commendable, however, these and other positive aspects remain at risk of being overshadowed by counter-productive challenges to civil society engagement, and the apparent inability of the EITI process to generate broader public debate and demonstrate clear and more widespread impact. Greater focus should be considered by the MSG with respect to EITI requirements that relate to impacts on the ground for citizens and communities, for example, on management of revenues. Recent efforts to heighten public awareness and address civil society concerns warrant findings of meaningful, though not satisfactory, progress. Information and data on the relatively small mining sector is insufficient. In general, disclosures under Requirements 2 through 6 can be strengthened with more focus on meeting their broader objectives. Further reflection is also called for to link work plan objectives and implementation to national priorities.

- [Impact of EITI implementation](#)

Positive impacts of EITI implementation were noted by stakeholders consulted for the Assessment who had varying levels of familiarity with EITI. These include, but are not limited to: EITI has stressed the importance of accountability especially on the part of government and industry; it can facilitate trust and dialogue among stakeholders; it has contributed to greater understanding of, and technical knowledge about, the extractive sector; participation in the EITI can lend credibility to and support an environment for investments. At the same time, however, awareness about EITI appears to still be quite limited although the MSG, and more so civil society, have undertaken public information events around the 2014 EITI Report. The Assessment provides important insights with statements such as "EITI appears to have played a limited role in stimulating national debate about sector management and spending of oil revenues," "EITI reports do not appear to have played any significant role in stimulating government reforms in the extractive sector," and "there is insufficient evidence to demonstrate these efforts (on EITI) have had an impact on NR governance." The MSG should more rigorously analyse impacts, or the lack thereof. Contributing factors may include stakeholders' uncertainty in designing measurable objectives, in applying appropriate methodologies for assessing impact, and the lack of sustained outreach information efforts across the country. EITI does not appear to have had genuine, demonstrable impact on the day-to-day lives of people and communities. In other words, there is little evidence of a "human face" to the positive experience of EITI in Azerbaijan.

- The Independent Validator's Assessment of Compliance

| Figure 1 – Validator's assessment EITI Requirements | | LEVEL OF PROGRESS | | | | | Note |
|---|--|--------------------------|------------|------------|--------------|--------|------|
| | | No Progress | Inadequate | Meaningful | Satisfactory | Beyond | |
| Categories | Requirements | | | | | | |
| MSG oversight | Government engagement (#1.1) | | | | * | | |
| | Industry engagement (#1.2) | | | | * | | |
| | Civil society engagement (#1.3) | | | ← | | | 1 |
| | MSG governance (#1.4) | | | | | | |
| | Work plan (#1.5) | | | | ← | | 2 |
| Licenses and contracts | Legal framework (#2.1) | | | | | | |
| | License allocations (#2.2) | | | | | | 3-NA |
| | License register (#2.3) | | | | ← | | 4 |
| | Policy on contract disclosure (#2.4) | | | | | | |
| | Beneficial ownership (#2.5) | | | | | | |
| Monitoring production | State participation (#2.6) | | | | | | |
| | Exploration data (#3.1) | | | | | | |
| | Production data (#3.2) | | | | | | |
| | Export data (#3.3) | | | | | | |
| | Revenue collection | Comprehensiveness (#4.1) | | | | ← | |
| In-kind revenues (#4.2) | | | | | | | |
| Barter agreements (#4.3) | | | | | | | |
| Transportation revenues (#4.4) | | | | | | | |
| SOE transactions (#4.5) | | | | | | | |
| Direct subnational payments (#4.6) | | | | | | | |
| Disaggregation (#4.7) | | | | | | | |
| Data timeliness (#4.8) | | | | | | | |
| Data quality (#4.9) | | | | | ← | | 6 |
| Revenue allocation | Revenue management & expenditures (#5.1) | | | | | | |
| | Subnational transfers (#5.2) | | | | | | |
| | Distribution of revenues (#5.3) | | | | | | |
| Socio-economic contribution | Mandatory social expenditures (#6.1.a) | | | | | | |
| | Discretionary social expenditures (#6.1.b) | | | | | | |
| | SOE quasi-fiscal expenditures (#6.2) | | | | | | |
| | Economic contribution (#6.3) | | | | | | |
| Outcomes and impact | Public debate (#7.1) | | | | ← | | 7 |
| | Data accessibility (#7.2) | | | | | | |
| | Follow up on recommendations (#7.3) | | | | * | | |
| | Outcomes & impact of implementation (#7.4) | | | | | | |

Notes:

*Requirement was met in the 2015 Validation. It has not been not re-assessed.

1 – Validator disagrees and finds inadequate, rather than meaningful, progress has been made.

3 – Validator finds this requirement is not applicable.

2-7 – Validator disagrees and finds meaningful, rather than satisfactory, progress has been made.

Please see detailed findings for further discussion.

3. DETAILED FINDINGS

The Assessment focused on corrective actions identified by the Board and outstanding requirements from Azerbaijan's 2015 Validation. The Assessment states "Requirements that were considered met were not re-assessed." We recommend that where applicable, the Secretariat should confirm that no concerns have been noted that disturb this finding. This Validation Report likewise focuses on the corrective actions identified by the Board and outstanding requirements from the 2015 Validation of EITI in Azerbaijan.

1.1 Government engagement. This requirement was previously met and not reassessed.

1.2 Company engagement. This requirement was previously met and not reassessed.

1.3 Civil society engagement. In light of the specific aspects under this requirement and its broader objectives, we disagree with the Assessment that Azerbaijan has made meaningful progress and find that its progress is INADEQUATE. We did not find sufficient evidence in the MSG's opinion on the initial assessment to change this finding.

Annex E of the Initial Assessment contains a comprehensive, detailed, rigorous, and thoughtful analysis of the challenges surrounding civil society participation in EITI. It would be very helpful to provide, or at least summarize, the Secretariat's findings in the body of the Assessment.

Expression: We disagree with Secretariat's initial assessment regarding expression. While the 2015 Annual Progress Report provides evidence that Coalition members have been able to participate in a number of commendable public events, civil society representatives continue to face substantial restrictions from expressing views related to the EITI process and in expressing opinions about the EITI process without restraint, coercion, or reprisal. Annex E, states, "despite some positive developments in 2016, there are few signs of a commitment by the government to improve the environment for civil society." As stated in Annex E:

- "Three Coalition members remain in exile for fear of being arrested."
- Most EITI events "remain under some form of government control and are subject to government approvals."
- Civil society representatives face a "certain fear of reprisal or intimidation" when expressing views on the situation for civil society as well as on natural resource governance issues.
- "In the aftermath of the EITI Board decision on Azerbaijan in April 2015, an alternate CSO MSG member who is also a member of the EITI Board was portrayed in local media of being responsible for the downgrading of Azerbaijan and was accused of betrayal against the state."
- "There have been examples of civil society representatives substantively engaged in the EITI process that have faced intimidation because of views expressed in relation to the EITI process."

Annex E further notes that "even if requirements 1.3.d, 1.3.e.i, and 1.3.e.iv state that civil society should be able to speak freely and express opinions without restraint, it does not appear as if single incidents or a small number of incidents motivate the conclusion that the requirement has not been met. Some kind of overall assessment is required, looking at whether there is a pattern restricting freedom of speech." Substantive evidence provided at Annex E, including, but not limited to, the evidence noted above, points to a significant number of incidents, and evidence of views regarding fear of reprisal and intimidation that are widely felt by civil society representatives and reflect a pattern of government actions to restrain freedom of expression.

Operation: We agree with the Secretariat’s initial assessment regarding operation, and agree that requirements 1.3(b) and 1.3(c) are not met. In particular, Annex E states that:

- “Several prohibitive regulations were enacted between July 2015–February 2016. The implementation of these regulations, in particular related to NGO registration as well as registration of grants by foreign donors and recipient NGOs, has further restricted the operation of civil society, resulting in hibernation of much independent civil society activity.”
- Issues include, among others, lack of access to funds or ability to register grants, difficulty accessing funds in bank accounts, and difficulties with NGO registration.
- “With regards to those facing challenges with registration, the International Secretariat understands that the majority of these NGOs have attempted to register over a number of years but that the MoJ have not granted the registration. Some of these NGOs have now submitted their cases to the European Court of Human Rights.”
- “Over the last two years, at least 22 Coalition members including MSG members and Coalition Council members have been exposed to special checks and interrogations when crossing borders.”
- “Although the restrictions observed are for the most part not directly linked to the engagement of civil society representatives in EITI activities, the wider environment is affecting civil society representatives’ ability to participate in the EITI process.”
- “The lack of funding and restrictive environment has created a jam in the civil society space that NGOs perceive to be offered by the EITI, affecting the functioning of the Coalition.”
- Internal tension “had escalated to the brink of break-up of the Coalition.”

Association: We emphasize that restrictions on access to funding do have a negative effect on communication and cooperation among civil society representatives, as noted directly above. We otherwise agree with the Secretariat’s assessment that civil society involved in the EITI process are not restricted from engaging with other national or international civil society groups.

Engagement: We agree with the Initial Assessment that civil society representatives are fully, actively, and effectively engaged in the design, implementation, monitoring and evaluation of the EITI process. We agree that requirements 1.3.a and 1.3.e.ii are met.

Access to Public Decision-Making: We agree with the Secretariat’s initial assessment on this point.

In summary, we agree that the positive steps the government has taken to ease the situation for NGOs involved in the EITI should be commended, and that Requirements 1.3.a and 1.3.e.ii-iii are met. We agree that further work is need to meet Requirements 1.3.b-d and Requirements 1.3.e.i and 1.3.e.iv.

1.4 MSG Governance. We agree with the Assessment that Azerbaijan has made MEANINGFUL progress in meeting this requirement.

The Secretariat noted concerns relating specifically to Requirement 1.4.a.ii that civil society groups involved in the EITI as members of the MSG must “operationally, and in policy terms, be independent of government and/or companies.” The Secretariat’s evaluation notes that corrective action corresponding to this concern are assessed under 2.3 of the civil society protocol, and finds that Azerbaijan has made meaningful progress. Preferably, the discussion should be provided directly in the section discussing Requirement 1.4.

1.5 Work Plan. We disagree with the Secretariat’s assessment and find that Azerbaijan has made MEANINGFUL progress.

One of the corrective actions determined by the Board was for the EITI-Azerbaijan MSG to agree on a fully costed Work Plan that sets out objectives for implementation linked to national priorities for the extractive sector. (*Minutes from the 29th EITI Board meeting, p.27*) The 2016 Work Plan's objectives are: enhancing public awareness of profits from natural resources, EITI mainstreaming, and establishing a framework for healthy and advanced relations among EITI parties. As noted in the Assessment, the country's Work Plan does not explain the rationale behind these three stated objectives.

Under each of these three major objectives of the Work Plan, several activities are listed mostly with specific time frames and others that are ongoing ("year-round"). Most significantly and with respect to requirement 1.4.b.i, capacity constraints and capacity building programs are noted for state bodies, the national Secretariat, and companies but there are few concrete details with respect to civil society. Instead, activity 2.2.1 generally states "Solving issues concerning the capacity constraints of the Coalition." Given the already significant challenges surrounding civil society engagement in EITI, the Work Plan should provide greater and more specific activities around these concerns.

A review of legal obstacles in EITI implementation is noted and addressed generally under activity 2.3 of the Work Plan.

Finally, the Work Plan fails to meet the standard of having "fully costed" activities. Certain activities are simply noted as having grants allocated therefor, without specifying the amount or source as required under requirement 1.5.d. More focus is also needed with respect to ensuring these activities are "measurable," especially given the limited impacts of EITI, as will be discussed later.

2.1 Legal Framework and Fiscal Regime. We agree that Azerbaijan has made SATISFACTORY progress in meeting this requirement.

However, the 2014 EITI Report lists the laws applicable to the extractive sector with a very limited overview and narrative description of how they apply, leaving the reader without a solid understanding of how the sector is regulated. The outline of the fiscal regime, though more descriptive, could also provide a better foundational understanding of how the system works. The Assessment mentions the limitations of the fiscal regime description, but the list of applicable laws falls short as an "explanation" and does not highlight that the list of reforms lacks a description of the nature, direction, or magnitude of the proposed change. Without a solid contextual base, the technical information provided with regard to EITI Requirements 2-6 is much less coherent.

The NGO Coalition's review of the 2014 EITI Report stated that local governments receive no payments from the extractive sector, which is echoed in the discussion of sub-national payments. This highly centralized fiscal regime relates to issues around allocation and management of revenue, and should be considered in an analysis of why the EITI in Azerbaijan struggles with respect to public awareness and deeper impact across the country. It is recommended that the MSG document their discussions on the adequacy of the legal and fiscal regime as well as any ongoing reforms in the extractive industries.

2.2 License Allocations. The Initial Assessment uses the effective date of the BP/SOCAR PSA to defer disclosure of the transaction until 2015, though the bidding occurred in 2014, and concludes that no licenses were awarded or transferred in the 2014 reporting year. As a result, this requirement was deemed in the Assessment as met with satisfactory progress. It should more accurately be described as NOT APPLICABLE.

Moreover, "licenses" cover a range of governmental permits and concessions pursuant to 2.3.a of the Standard, and the discussion under the requirement focuses solely on production sharing agreements

(PSAs). There is no information provided about other licenses. This is potentially concerning especially given the Independent Administrator's admission that "obtaining information about licensing allocation processes pertaining to specific licenses had been challenging given that very little information was available in the public domain."

The Assessment further noted that licenses are negotiated on a case-by-case basis and that there are no standard technical and financial criteria for license allocations. This process neither encourages nor facilitates transparency, and would be prone to corruption. It is recommended in light of 2.2.a that the EITI Report explain any significant legal or practical barriers preventing comprehensive disclosure, including an account of the government's plans to overcome such barriers and anticipated timescale for achieving them. It is also recommended that the MSG discuss and comment on the efficiency and effectiveness of licensing procedures, pursuant to 2.2.e.

2.3 Register of licenses – We disagree with the Assessment that Azerbaijan has made satisfactory progress and find it has made MEANINGFUL progress.

The Independent Administrator confirmed that there was no publicly available register of active PSAs and created one for purposes of the 2014 EITI Report (pursuant to Req. 2.3.c). Thus, Azerbaijan had not maintained such a publicly available register, and there is no evidence of any discussions or decision to ensure that it would be updated with timely and comprehensive information regarding licenses, pursuant to 2.3.b of the Standard. Moreover, the Assessment states that a PSA held by AIMROC for the Chovdar gold field was active in 2014 but was not discussed in either the EITI Report or by the MSG. The Assessment takes two seemingly contradictory positions in this regard: (i) that AIMROC is not a company covered in the 2014 EITI Report (presumably, though not stated, because it made no reportable payments to the government in 2014), thus the inclusion of its PSA in the registry is not required; and (ii) the inclusion of the AIMROC PSA is required, but lowering the assessment due to its exclusion would be disproportionate. In any event, where a register or cadastre does not exist or is incomplete, the EITI Report should disclose any gaps in the publicly available information and document efforts to strengthen these systems (Req. 2.3c).

2.4 Contract Disclosures. We agree that Azerbaijan's progress is SATISFACTORY.

The 2014 EITI Report confirms there is no law on disclosure but that contracts may be disclosed upon mutual consent of the parties. According to the 2013 EITI Report and again in the 2014 EITI Report, Azerbaijan has voluntarily disclosed five contracts and uploaded these on the EITI website. Such disclosure is encouraged but not required under the 2016 Standard. Furthermore, the EITI Report, where applicable, "should provide an overview of publicly available contracts/licenses, and include a reference or link to the location where these are published." (Req. 2.4.b) The 2014 EITI Report provides a general reference to the EITI website where the disclosed contracts are available, however, it does not provide an overview of these.

2.5 Beneficial ownership. We concur with Secretariat's assessment of this requirement.

2.6 State participation in EI. We agree with the Assessment that Azerbaijan has made MEANINGFUL progress in meeting this requirement.

3.1 Exploration. We agree with the Assessment that Azerbaijan has made SATISFACTORY progress in meeting this requirement.

The 2014 EITI Report lists, however, only static volumes of reserves, by commodity. A discussion of economically recoverable reserves, values, and an indication of whether reserves (by commodity) are increasing or decreasing, with a sense of magnitude, would provide a much more detailed

understanding of the potential of the sector – the stated goal of EITI Requirement 3 – and should be encouraged.

- 3.2 Production Data. We agree that Azerbaijan’s progress is SATISFACTORY, but note that disclosure from the mining sector is entirely based on company self-reporting. While common, better practices call for government or independent verification.
- 3.3 Export Data. We agree with the Assessment that Azerbaijan has made SATISFACTORY progress in meeting this requirement.
- 4.1 Comprehensive disclosure of taxes and revenues. We disagree with the Assessment and find that Azerbaijan has made MEANINGFUL, and not satisfactory, progress in meeting this requirement.

The MSG defines transactions as material where the “sum or volume exceeds zero.” No information is provided in the EITI Report, however, on the MSG’s rationale for this definition. The 2014 EITI Report seems to have an internal inconsistency when it defines the materiality threshold as having “been set at zero” (p.49) rather than exceeding zero. Said Report also states that 39 companies, including two mining companies, constitute the “total universe of companies active in 2014.” According to the Ministry on Ecology and Natural Resources, however, there are mining companies not mentioned in EITI relating to at least two PSAs and “approximately 500-600 mining companies with rights to mine by local executive committees (Rayons)” whose “production was not considered substantial,” dealing mainly with construction materials. Given the materiality threshold, even insubstantial payments should be considered as these would exceed zero.

There is no information about these companies nor about what type of mining permits may even be involved. This lack of information impacts not only progress under this requirement but potentially others as well, including license allocations and registers. The Assessment then states that “some mining companies appear to be excluded from the EITI report” though it is “unlikely that any of these companies are making payments to the government.” Given the lack of information, there appears to be insufficient evidence to warrant such a conclusion. While there is satisfactory disclosure under this requirement for the oil and gas sector, not all aspects are being implemented in light of the data gaps for the mining sector.

- 4.2 In-Kind Revenues. We agree with the Assessment that Azerbaijan has made SATISFACTORY progress in meeting this requirement.
- 4.3 Infrastructure provisions and barter arrangements. We agree with the Assessment that this requirement is NOT APPLICABLE.
- 4.4 Transportation revenues. We agree with the Assessment that Azerbaijan has made SATISFACTORY progress in meeting this requirement.
- 4.5 Transactions related to SOEs. We agree with the Assessment that Azerbaijan has made SATISFACTORY progress in meeting this requirement.

The Assessment confirms that the 2014 EITI Report comprehensively addresses the role of SOCAR, which is the only SOE. The Assessment implies, but should affirmatively state (if accurate) that the 2014 EITI Report reconciles (i) all in-kind payments made by companies to SOCAR and (ii) all transactions between SOCAR and the government.

- 4.6 Subnational payments. The Assessment found that this requirement is NOT APPLICABLE to Azerbaijan. Our observations are noted below.

While the 2014 EITI Report explains that there are taxes levied at the local level, both the Independent Administrator and the MSG confirmed that no-subnational payments were made by companies to the government in 2014. It is difficult to imagine that oil and gas and mining companies would not be required to pay local taxes or any “license fees, rental fees, entry fees and other considerations for licences and/or concessions” (Req. 4.1.b.vii) at the local level, which would presumably meet the materiality threshold of exceeding zero. This would then mean that governments and communities at the local level are direct recipients or beneficiaries of these extractive activities. As this appears to be the case, however, this should merit further review and consideration, particularly as this relates directly to revenue allocation, revenue management, and to the objective of EITI to create greater positive impact across the country.

- 4.7. Level of disaggregation. We agree that Azerbaijan’s progress is SATISFACTORY. The 2014 EITI Report provides data by company, government entity, and revenue stream. In consultation with the Secretariat, it is also confirmed that the Report provides project-level revenue data.
- 4.8 Data timeliness. We agree with the Assessment that Azerbaijan has made SATISFACTORY progress in meeting this requirement. This a clear strength in their implementation of EITI.
- 4.9 Data quality and assurance. We disagree with the Assessment and find that Azerbaijan has made MEANINGFUL, and not satisfactory, progress in meeting this requirement

The Assessment contains a good discussion of the ToR requirements set forth in 4.9b.iii and notes that the 2014 EITI Report does not recite some of the specific agreements that the MSG (or MSG and Independent Administrator) are required by the Standard to have reached. 4.9.b of the Standard requires that reconciliation be made applying international auditing standards, but the Independent Administrator's opinion states that "reconciliation procedures carried out were not designed to constitute an audit or review in accordance with International Standards on Auditing or International Standards on Review Engagements." Therefore, find that Azerbaijan has made meaningful, but not satisfactory, progress in meeting this requirement.

Based on the results of the Independent Administrator's risk-based testing of company reports, along with the other assurance measures outlined in the Assessment, we concur with the Secretariat's willingness to rely on the quality of the reported data. However, the Independent Administrator qualified its opinion because it had not verified every transaction (which is not required by auditing standards) and further qualified it as to any adjustment that would have been required in the event every transaction had been verified. The MSG should be encouraged to eliminate these qualifications with regard to future EITI reports.

- 5.1 Distribution of extractive industry revenues. We agree with the Assessment that Azerbaijan has made SATISFACTORY progress in meeting this provision.

Subsequent EITI reports should, however, provide a clearer and more traceable summary of the extractive sector revenues, whether cash or in kind, that are recorded to the national budget and with explanations regarding the allocation of revenues that are not recorded to the national budget.

- 5.2 Subnational transfers. We agree with the Assessment that this requirement is NOT APPLICABLE to Azerbaijan for the 2014 reporting period.

The 2014 EITI Report and the Assessment confirm the inapplicability of this requirement, however, concerns are often noted around the centralized nature of revenues and failure of benefits to translate locally. It would be helpful to provide more than the statement, “Azerbaijan is a unitary state” to discuss the inapplicability or absence of sub-national transfers. This issue should merit further review and consideration, particularly as this relates directly to the objectives of EITI to heighten public awareness about EITI and create greater positive impact across the country.

5.3 Revenue management and expenditures. Disclosure under this requirement is not mandatory.

The MSG is encouraged to disclose the information under this requirement, but the Assessment states that it does not appear to have held any substantive discussions in this regard. The issues under this requirement include revenue sustainability and use of extractive sector revenues in areas beyond the capital. These issues are key to raising awareness, generating public debate, and facilitating greater impact.

6.1 Social expenditures by extractive companies. We agree with the Assessment that this requirement is NOT APPLICABLE to Azerbaijan for the 2014 reporting period.

There are currently no social expenditures that are required by law or contract. The Assessment notes that the MSG continues to discuss the inclusion of voluntary social expenditures, which is also advocated by the NGO Coalition. It would be helpful for the MSG to explain why it has previously deemed social costs an ‘irrelevant stream,’ and perhaps adopt the term ‘inapplicable’ if that is what is meant. Disclosure of such voluntary expenditures would not appear to be difficult, however, based on the Assessment’s finding that some companies are already reporting on their voluntary social expenditures in their sustainability reports.

6.2 Quasi-fiscal expenditures. We agree with the Assessment that Azerbaijan has made MEANINGFUL progress in meeting this requirement.

The MSG has not agreed on a definition of quasi-fiscal expenditures. It is thus difficult to determine whether these expenditures have been comprehensively disclosed, and there is limited explanation of the legal basis for the expenditures that have been disclosed.

6.3 The contribution of the extractive sector to the economy. We agree with the Assessment that Azerbaijan has made SATISFACTORY progress in meeting this requirement.

7.1 Public debate. We disagree with the Assessment that Azerbaijan has made satisfactory progress in meeting this requirement, and find that it has made MEANINGFUL progress.

The 2015 Validation Report noted that there was limited detail and evidence that EITI had contributed significantly to public debate on the extractive sector in Azerbaijan. The Board’s corrective actions called for the MSG to ensure that the EITI Report contributes to public debate. The MSG has since made clear efforts to ensure that the 2014 EITI is comprehensible and publicly accessible. The Assessment does not discuss, however, whether the MSG has agreed on a clear policy on the access, release, and re-use of EITI data (7.1.b).

Significantly more public information and awareness activities around the 2014 EITI Report were held in 2015 and thus far in 2016, including regional events, forums held in universities, and local community events. EITI materials were disseminated or planned to be disseminated in various forms and in two languages, and social media outreach efforts were evident. The Assessment observes that there has been some increased public debate due to these events.

The Assessment notes some disagreement regarding who plans and holds these public information events. It appears there may be a general impression that this is the responsibility of civil society organizations, and they were in fact largely responsible for recent events. The Assessment finds that Azerbaijan has made satisfactory progress in meeting this requirement despite the lack of action from government and companies. This uneven approach is both unfair and unsustainable, however, and is in direct opposition to Azerbaijan's stated objective in the work plan to foster healthy and advanced relationships among the parties. The MSG is required to ensure outreach events by and for all the stakeholder groups, and efforts should be taken to clarify their roles, expectations, and responsibilities.

- 7.2 Data accessibility. This requirement was not reassessed.
- 7.3 Discrepancies and recommendations from EITI Reports. This requirement was not reassessed.
- 7.4 Review the outcomes and impact of EITI implementation on NR governance. We agree with the Assessment that Azerbaijan has made MEANINGFUL progress in meeting this requirement.

The Assessment notes that Azerbaijan has met significant aspects of Req. 7.4. In compliance with Req. 7.4.c, for example, the MSG has observed deadlines with respect to the EITI Report and the Validation process. Given the rushed nature of producing their 2015 APR, however, it appears that not all MSG members were able to participate in its development and review, much less for those not on the MSG (7.4.b). As further noted in the Assessment, the MSG has published AARs over the past three years that address most of the aspects under Req. 7.4.a. However, the 2015 APR does not rigorously document the impacts of EITI implementation and outcomes of the stated objectives as set out in the work plan, nor does it adequately provide a narrative account of efforts to strengthen impact of EITI implementation on NR governance.

4. RECOMMENDATIONS

We agree with the recommendations discussed in the Initial Assessment, and note below, in italics, modified or additional recommendations.

- 4.1 *Azerbaijan has taken positive steps to ease the situation for NGOs involved in the EITI, however, further progress is needed to meet the different aspects of Requirements 1.3b-d, 1.3.e.i, 1.3.e.iv, and 1.4.a.ii. Specifically, the government should address the remaining issues related to the environment for civil society participating in the EITI, notably legal and practical obstacles related to registration of NGOs, accessibility of registration extracts, registration of grants and any other obstacles affecting the ability of NGOs to operate. The government should ensure that there is an enabling environment for civil society to express their views and debate on natural resource governance issues. Civil society should take steps to agree a policy for political and operational independence, and consider issues affecting coalition governance.*
- 4.2 The MSG should *articulate*: a clearer explanation of the links between the work plan objectives, the extractive sector, *and national priorities*; and the rationale behind the selected objectives. The MSG is encouraged to expand the consultation on the work plan objectives to include key stakeholders beyond MSG members. Moreover, *the MSG should ensure that activities in the work plan can be monitored effectively, which requires measurable, goals, and timetables.*
- 4.3 The MSG is encouraged to consider more timely reporting on license allocation, i.e. when they occur, and is advised to update the license register to include all active contracts, including

contracts pertaining to companies not covered in the scope of the EITI Report. *The MSG should ensure the maintenance of a publicly available register of licenses that will be updated with time and comprehensive information. It is encouraged to consider commenting on the efficiency and effectiveness of the ad hoc approach to awarding licenses, and to provide an overview of the contracts and licenses that are publicly available.*

- 4.4 *The MSG should work on obtaining more comprehensive data regarding the mining sector, including the number of operating companies and permits issued, including on the local level. The MSG should clarify the terms attached to the government's share in the two active mining PSAs.*
- 4.5 *The MSG should agree on a clear policy on the access, release, and re-use of EITI data (7.1.b). It is encouraged to ensure outreach events by and for all the stakeholder groups, and take efforts to clarify their roles, expectations, and responsibilities.*
- 4.6 *In view of Azerbaijan's disclosure of contracts, the EITI Report should provide an overview of these contracts and licenses. Future EITI reports should include commentary confirming whether there are any ongoing reforms related to contract transparency. Given that all PSAs in Azerbaijan are ratified by Parliament, the MSG should consider increasing its efforts to make the remaining PSAs available on the EITI Azerbaijan website.*
- 4.7 *The MSG is encouraged to ensure that future EITI Reports summarize the legal framework, fiscal regime, the applicable rates, and how the various taxes and payments are calculated, so that stakeholders can gain an understanding of how the extractive sector is managed. With regard to reforms listed in future EITI Reports, it is recommended that these be described in a way that stakeholders can understand the nature of the change, its magnitude, and its potential impact.*
- 4.8 *The MSG should ensure that SOCAR discloses all details regarding its equity stake and changes in ownership. The MSG could consider extending this to SOCAR subsidiaries operating in the downstream sector. In future reports, the MSG may wish to consider requiring a table that ties the payment and revenue amounts set forth in section 1.4 to the allocation numbers set forth in section 3.6 and including a discussion of the amounts transferred by SOFAZ to the national budget (how determined) and retained by SOFAZ.*
- 4.9 *In order to promote a better understanding of the potential of the extractive sector in Azerbaijan, the MSG is encouraged to include information regarding the value of total reserves (by commodity) that are economically recoverable. It is further recommended that the MSG discuss how to address concerns regarding the reliability of data from the mining sector. The MSG should consider including sources of data on how export volumes and values are calculated.*
- 4.10 *The MSG is encouraged to consider expanding the reporting on sales of in-kind revenue to include additional information such as the type of product, price, market and sale volume.*
- 4.11 *The MSG is encouraged to expand the reporting on transportation to include a full description of the transportation arrangements including the products transported, transportation route(s), disclosure of tariff rates and the methodologies used to calculate them, and disclosure of volume of the transported commodities.*
- 4.12 *The MSG is encouraged to ensure that the Independent Administrator include an overview of companies and government agencies that have published their audited financial statements online, and how these can be accessed. In the future, the MSG is encouraged to ensure that*

reconciliation is conducted in accordance with proper audit standards.

- 4.13 The MSG may wish to consider extending EITI Reporting to include information on revenue management and expenditures. It is encouraged to explore opportunities to report on discretionary social expenditures in future EITI reports.
- 4.14 The MSG is encouraged to undertake an analysis of the impact of EITI implementation with a view to identifying weaknesses and opportunities for increasing impact. It is recommended that broader stakeholders have an opportunity to contribute to such an analysis.
