

Ways Of Improving Azerbaijan's Performance In Resource Governance Index (RGI)

Summary

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AZ_RGI.pdf](http://eurasiahub.khazar.org/pdf/AZ_RGI.pdf)*

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Resource Governance Index measures governance of oil, gas and mining industries. The index reflects quality of governance of resource rich governments based on a composite assessment of transparency, accountability and disclosure practices. Azerbaijan was ranked as 47th among 81 countries in the last index (2017) and was placed among the largest group of countries that performed “weak”, coming after “good” and “satisfactory” performing countries.

RGI rightfully reflects the current state of the extractive industries governance in Azerbaijan. As the Index demonstrates, Azerbaijan has poor legal framework in extractive industries and its institutional set up is also weak in comparison to the advanced practices of other countries.

The main goals of the country should be to improve natural resource governance, legal and fiscal frameworks for attracting investors. The dominance of product sharing agreements (PSAs) in the country without any alternatives evokes questions. PSAs have been recognized for not bringing sufficient dividends to the countries both in the region and across the world. Thus, they should be replaced by more transparent, accountable contracting procedure that would be based on open tender.

The government should be the main initiator for changing PSAs to alternative fiscal regimes, as international corporations are in winning position with the current set up.

The government should recognize the fact that close door negotiations will create a fertile ground for international corporations for winning the best deal that would allow them to exploit natural resources of the country. Moreover, the absence of highly skilled experts on the government's side will also put the government in a weak position during the negotiations. Therefore, increasing level of transparency and establishment of a more transparent legal framework are keystones for facilitating positive developments in Azerbaijan.

Azerbaijan's state oil company- SOCAR will soon be in the center of attention both domestically and globally. With its expanding investments both in the region and in the world SOCAR is also undertaking huge responsibilities. Successful implementation of these commitments undoubtedly depends on the transparency of the company's operations. Unfortunately, it is too early to speak of any positive developments in this area. To become a reliable partner, SOCAR should not only practice transparency within its foreign investment portfolio, but also maximize its transparency and accountability domestically. Only with implementation of these conditions SOCAR can undertake new projects and join the “club” of reliable national oil companies.

Successful management of resource revenues largely depends on the good governance of a country's financial institutions. Governance system should encompass both internal and external evaluation and accountability. All branches of the government, particularly legislative branch should implement its functions without limitations and the executive branch should build up a

strategy in this field and mainstream it into their daily work. Within this kind of a set up both the State Oil Fund and the Ministry of Finance could become more pro-active and suggest new ideas in efficient management of resource revenues.

Azerbaijani government has been using the resource revenues for the longest period of time among the countries of the region. Since 2004 the government has received more than 130 bln. USD from extractive industries in total. Only 40 bln. USD from these revenues are assets of the Oil Fund. 100 bln. USD has been already spent and 80% of this money was spent through the state budget. This approach is hardly rational, given that the budgetary spending was based on the revenues from a finite resource.

New fiscal rules adopted in Azerbaijan recently suggest that in the future the level of spending will temper down and particularly the Oil Fund will invest into larger scale and efficient projects.

Recommendations to the government

The State Commission on the Extractive Industries of the Republic of Azerbaijan is the key structure to influence Azerbaijan's performance in the Index. After leaving EITI, the Commission was established based on a decree of the president and is the main entity to guarantee transparency and accountability of extractives in the country. The fact that the Commission is comprised of several deputy ministers demonstrates that its an authoritative entity.

In our opinion, if the Commission reviews the provisions in the current document and improves annual transparency report on the extractive industry it can make a substantial contribution to the strengthening of the country's position in the next Index. In addition to this, the Commission should also prepare an action plan to ensure Azerbaijan's membership in EITI again.

The State Oil Fund should also strengthen control of the implementation of newly adopted fiscal rules and work towards establishing a framework for its own operations domestically.

The Ministry of Finance should coordinate its work with the Oil Fund to ensure both the budget control and efficient implementation of fiscal rules. The ministry should also place full and timely information on the level of public debt in the budget report and official website.

Recommendations to the other stakeholders

SOCAR should strengthen its status as a corporation and increase its accountability. For this, the company should prepare both its financial and sustainable development reports based on the requirements set for national oil companies and add missing components for the transparency report (e.g. dividends, social projects, quasi-fiscal spending and etc.)

At the same time, the role of SOCAR in the energy management structure of the government should be more clearly defined, meaning its share of responsibility with the Ministry of Energy and other government entities should be clearly depicted in the relevant state documents.

The issue of transparency and the government's accountability in the extractive industries should remain a priority on the civil society's the agenda, despite Azerbaijan's withdrawal from the EITI. For this the representatives of civil society should raise the issues mentioned in this document based on the recommendations provided above within its partnership with the Commission.