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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. The 2.8% GDP growth in 2014 was driven by the non-oil economy and continued public investment. The European Bank for Reconstruction and Development forecasts slow GDP growth of 1.5% in 2015 as a result of the global drop in oil prices. Oil and gas products account for roughly 95% of Azerbaijan’s export revenue. Economic diversification and greater foreign investment to further develop its energy sector continue to be the stated goals of President Aliyev and the government, but inefficient government bureaucracy, weak legal institutions, requests for illicit payments for cross-border transactions, and predatory behavior by politically-connected monopolistic interests hinder investment outside of the oil and gas sector and present challenges for U.S. companies. Azerbaijan has worked to improve its regulatory system over the past several years, but limited transparency and allegations of corruption remain key problems in this area.

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 may not own land. The 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 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 February of 2015, Azerbaijan devalued its local currency the manat (AZN) by 35% to adjust to the drop in oil prices by putting 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. Corporate Social Responsibility (CSR) 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.
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 the 2014-2015 drop in oil prices – and their concomitant impact on oil revenues – may prompt the Azerbaijani government to pursue more comprehensive reforms, including completing its World Trade Organization (WTO) accession process.

Other Investment Policy Reviews

In the past three years, Azerbaijan has not conducted an Organization for Economic Cooperation and Development (OECD), investment policy review. 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 of Foreign Direct Investment

Foreign investment in Azerbaijan is regulated by a number of international treaties and agreements, as well as domestic legislation. These include 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.

Industrial Promotion

The Government of Azerbaijan has targeted the following sectors for attracting investment: energy, transportation, agriculture, tourism, and information and communication technology.

Limits on Foreign Control

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 and communications. 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%, while the total share of foreign capital in such equities cannot exceed 50% - with the exception of international financial institutions of which Azerbaijan is a member.

Privatization Program

Large-scale privatization has been particularly slow in Azerbaijan, and lags significantly behind that of other 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.

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 registration of representative or branch offices of foreign non-commercial entities was not, however, transferred to the Ministry of Taxes and can be accessed in English at the following website: http://taxes.gov.az/modul.php?lang=_eng&name=birpencere&bolme=registration; such entities are still required to register with the Ministry of Justice. The “online registration” system of legal entities has been available since 2012.

The World Bank’s, Investing Across Borders 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 finally in 2015. A hindrance to foreign direct investment is the difficulty of getting established Azerbaijani businesses to adapt to standard investor-friendly practices, such as those associated with the concept of good corporate governance or international accounting norms.

**Investment Trends**


*Table 1*

<table>
<thead>
<tr>
<th>Measure</th>
<th>Year</th>
<th>Index or Rank</th>
<th>Website Address</th>
</tr>
</thead>
<tbody>
<tr>
<td>TI Corruption Perceptions index</td>
<td>2014</td>
<td>126 of 175</td>
<td>transparency.org/cpi2014/results</td>
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<td>Global Innovation Index</td>
<td>2014</td>
<td>101 of 143</td>
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<td>World Bank GNI per capita</td>
<td>2013</td>
<td>7,350 USD</td>
<td>data.worldbank.org/indicator/NY.GNP.PCAP.CD</td>
</tr>
</tbody>
</table>

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 AZN (manats), in accordance with the Constitution. Foreign companies and individuals may have both AZN 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.

In 2014, the county’s strategic monetary reserves grew by 2.4 percent to over USD 51.4 billion USD in November 2014, which included both foreign currency reserves (USD 15 billion) and Azerbaijan’s sovereign wealth fund assets (USD 36.4 billion). However, due primarily to the erosion of Azerbaijan’s balance of payments following the nearly 60% drop in oil global prices in 2014 – 2015, foreign currency reserves dropped 26% over a three-month period, falling to USD 11.1 billion by the end of February 2015. Consequently, the Central Bank dropped the manat’s peg in favor of a dollar/euro-weighted currency basket on February 16, 2015. On February 21, 2015, the Central Bank devalued the currency by 35% and set the new manat (AZN) rate at 1.05 against the USD.

Remittance Policies

Foreign investors are subject to a corporate branch remittance tax of 10% 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.

For further guidance on corporate tax policies see:


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 per cent of market value as compensation to the owners. In practice, however, this does not happen. Neither national law nor administrative policies provide adequate protections for the rights of citizens in Azerbaijan. There are no effective domestic mechanisms for legal protection; nor any case law to support this provision. Moreover, there is no effective mechanism for formalizing unregistered properties, and no fair legal framework to deal with state expropriations of officially non-registered property. Evictions are therefore carried out in an arbitrary manner. Citizens in affected areas have no effective remedies in regard to obtaining fair compensation or adequate housing.”


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.

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

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. This 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, 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/rankings).

**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:

**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**

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 16 July 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 TRIMS.

**Investment Incentives**

Since 2013, new amendments to the Tax Code have created an exemption from income, land, and property taxes for business parks in Azerbaijan, for example in the area of information technology. The amendments also provide for tax and customs privileges for the residents of industrial and technological parks for a term of seven years.
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 that 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 sectorial limits. 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 will lead to deportation/removal from Azerbaijan.

In 2014, the Cabinet of Minister's 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 industries that fall under this provision include: education, finance and insurance, information and communication technology, manufacturing, mining, power, gas, steam and artificial atmosphere supply, transportation, water supply, waste 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 1,379 AZN (approximately 1,277 USD).

Despite these regulations, major U.S. and other international firms have 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. Right to Private Ownership and Establishment

The Land Code recognizes state, municipal, and private ownership of land in Azerbaijan. All types of ownership rights are equal. Only Azerbaijani citizens and Azerbaijani legal entities, including enterprises with foreign investment, may legally own land in Azerbaijan, according to the 1999 Land Code.

Under Azerbaijani law, private entities may freely establish, acquire and dispose of interests in business enterprises. However, in practice, access to markets, credit and other business operations is often impeded by licensing and other regulatory requirements, and by politically connected business interests that can mobilize the powers of the state to their advantage. In sectors of interest to certain senior government and political figures, competition is actively impeded through administrative barriers. Legislation regulating real property rights include the Law on Mortgage (2005), the Land Code of the Republic of Azerbaijan (1999), the Law on Land Reform (1996), the Law on Land Leasing (1999), and the Law on Land Market (1999).

7. 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 corrupt and inefficient. In 2015, the Index of Economic Freedom gave Azerbaijan less than favorable scores regarding the protection of private property rights.


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% in 2013. Moreover, the estimated value of unlicensed software in Azerbaijan was USD 103 Million in 2013, compared to USD 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,
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, and published government statistics indicate that IP protections are gradually improving.

**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:

**YUSIF ABASOV**  
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

**8. 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.

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 banking, finance, and the energy sector (SOCAR).

9. 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.

As the banking supervisory authority, the Central Bank issues licenses to banks and non-bank credit organizations, and also establishes minimum charter capital, net worth, and other financial requirements.

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 may face significant increases in nonperforming loans. Average lending growth for the sector in 2015 is expected to grow between 10%-13%. The prevalence of cash transactions – estimated at 70% by Central Bank authorities – hinders the development of the financial system. Non-resident foreigners may legally establish bank accounts in Azerbaijan. There have been no public cases of hostile takeovers in Azerbaijan.

As of the end of the third quarter of 2014, there were 44 banks registered in Azerbaijan, including 22 banks with international activities. 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 in the range of 16-34 percent. Total banking sector assets stood at approximately 26 billion USD as of February 2015, with the top five banks holding almost 58% of this figure. The state-owned International Bank of Azerbaijan (IBA) accounts for approximately 35-50% 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 (CBA) has been focused on encouraging consolidation in the sector, and in August 2012 the CBA raised the minimum capital requirement from 10 million AZN to 50 million AZN, effective January 1, 2014. As of February 2015, 23 banks had assets which totaled approximately AZN 50-60 million, 9 banks had assets of AZN 60-100 million, and 9 banks had assets over AZN 100 million. 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 growth of the stock market 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 March 2015, Fitch Ratings affirmed Azerbaijan’s Long-term foreign and local currency Issuer Default Ratings (IDR) at ’BBB-’. Standard & Poor’s lowered the outlook on Azerbaijan’s BBB-credit rating to negative on January 30, 2015 citing the oil-price decline and pressure on the manat (AZN) from “weaker terms of trade.” In February 2015, Moody’s warned that the assets of Azerbaijani banks were at risk. This assessment came immediately after the devaluation.

10. 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 State Oil Company of the Azerbaijan Republic (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. 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. SOFAZ publishes an annual report, complies with the Extractive Industries Transparency Initiative, and submits its books to an independent audit. The fund’s assets totaled USD 37 billion as of March 2015.

11. Corporate Social Responsibility

Corporate Social Responsibility (CSR) is a relatively new concept in Azerbaijan. Producers and consumers do not have a general awareness of corporate social responsibility, including environmental, social, and governance issues. No information is currently available on legal corporate governance, accounting, and executive compensation standards to protect shareholders in Azerbaijan. Larger foreign entities tend to follow generally accepted CSR 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 corporate social responsibility for businesses in Azerbaijan.

OECD Guidelines for Multinational Enterprises

No information is available on the extent to which Azerbaijan encourages foreign and local enterprises to follow generally accepted CSR principles in the OECD Guidelines for Multinational Enterprises or the United Nations Guiding Principles on Business and Human Rights, endorsed by the UN Human Rights Council.

12. Political Violence

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

13. 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. U.S. 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. 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. Eight 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 2014, Azerbaijan’s modest improvements in combating petty corruption were reflected by the global anticorruption watchdog Transparency International, which ranked Azerbaijan 126 out of 175 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 tax authorities has improved recently 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.

\textit{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 is currently undergoing validation under the new “EITI Standard,” which requires more detailed reporting, including payments made by individual companies.
Resources to Report Corruption

Contact at Government of Azerbaijan responsible for combating corruption:

Vusal Huseynov
Executive Secretary
Commission on Combating Corruption
Baku, Azerbaijan
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vusal.h@pa.gov.az

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

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Executive Director
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(+994 12) 497 81 70
rena@transparency.az

14. Bilateral Investment Agreements

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


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.

Bilateral Taxation Treaties

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. Over the past year, Azerbaijan has made progress in finalizing an intergovernmental agreement with the United States on implementing the Foreign Account Tax Compliance Act (FATCA). As of May 2014, the United States and Azerbaijan had reached an agreement in substance on what is known as the “IGA Model 1a” agreement and we expect this IGA will be signed in 2015.
15. OPIC and Other Investment Insurance Programs

The Overseas Private Investment Corporation (OPIC) and the U.S. Export-Import (Ex-Im) Bank are open for business in Azerbaijan, providing political risk insurance, as well as financing and loan guarantees. Azerbaijan is also a member of the Multilateral Investment Guarantee Agency (MIGA), and the European Bank for Reconstruction and Development (EBRD). The World Bank, Asian Development Bank, and other third-country institutions are active in providing financing and insurance for investment in Azerbaijan.

OPIC has repeatedly provided funds for numerous banks operating in Azerbaijan in order to expand their small and medium enterprise (SME) lending portfolios, including 4.8 million USD to Rabita Bank in 2008 and 7.3 million USD to Turan Bank in 2009. In 2011, OPIC provided Muganbank a loan guarantee for 10 million USD to expand its operations, targeting SME borrowers. OPIC has also provided 1 million USD and 3 million USD, respectively, to FinDev and CredAgro for microfinance lending. In 2012, OPIC provided loan insurance to Viator Microcredit Azerbaijan LLC (500,000 USD), NBCO Vision Fund Azercredit LLC (2 million USD), and FinDev again (1 million USD). In 2013, OPIC signed a memorandum with Turanbank for a loan in the amount of 7 million USD with a term of seven years for SME financing.

In its 2014 annual report, the Export-Import Bank of the United States (Ex-Im Bank) stated that it has outstanding insurance and loan guarantees for Azerbaijan in the amount of 419.4 million USD, primarily in support of aviation sales. In 2011, Ex-Im Bank closed a 116.6 million USD loan with a ten-year repayment period to finance the Azerbaijani space agency’s purchase of the AzerSat-1 satellite from Orbital Sciences.

16. Labor

A Labor Code that took effect in 1999 still regulates overall labor relations and recognizes international labor rights. The work week generally is considered to be 40 hours. The right to strike exists, though industrial strikes are rare. Azerbaijan is a member of the International Labor Organization (ILO) and has ratified more than 57 ILO Conventions. In practice, labor unions are strongly tied to political interests. Collective bargaining is not practiced. Azerbaijan has regulations to monitor labor abuses, health, and safety standards in low-wage assembly operations, but enforcement is less effective.

Azerbaijan has an abundant supply of semi-skilled and unskilled laborers. However, the relatively limited supply of highly skilled labor remains one of the biggest challenges in Azerbaijan’s labor market. As of 2015, government sources estimate the rate of unemployment at five percent, but other sources estimate the figure at 15% or higher, with underemployment being much higher.

The average monthly salary as of March 2015 was USD 440. Upon termination of employment, employers must pay departing employees monetary compensation for unused vacation leave. Azerbaijan currently is working with the World Bank and the European Union on a program to reform the state pension system.
17. 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 – currently there are no foreign trade zones or free ports operating in Azerbaijan. Certain ministries – the Ministry of Economy and Industry, the Ministry of Finance, and the Ministry of Communications and High Technologies – continue to discuss plans for creating special economic zones, including a petrochemical complex, 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.

18. Foreign Direct Investment and Foreign Portfolio Investment Statistics

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

<table>
<thead>
<tr>
<th>Economic Data</th>
<th>Host Country Statistical source*</th>
<th>USG or international statistical source</th>
<th>USG or International Source of Data: BEA; IMF; Eurostat; UNCTAD, Other</th>
</tr>
</thead>
<tbody>
<tr>
<td>Host Country Gross Domestic Product (GDP) ($M USD)</td>
<td>2014 73.7</td>
<td>2013 73.5</td>
<td><a href="http://www.worldbank.org/en/country">www.worldbank.org/en/country</a></td>
</tr>
<tr>
<td>Foreign Direct Investment</td>
<td>Host Country Statistical source*</td>
<td>USG or international statistical source</td>
<td>USG or international Source of data: BEA; IMF; Eurostat; UNCTAD, Other</td>
</tr>
<tr>
<td>U.S. FDI in partner country ($M USD, stock positions)</td>
<td>2013 24.4</td>
<td>N/A</td>
<td>N/A</td>
</tr>
<tr>
<td>Host country’s FDI in the United States ($M USD, stock positions)</td>
<td>2013 N/A</td>
<td>2013 N/A</td>
<td>N/A</td>
</tr>
<tr>
<td>Total inbound stock of FDI as % host GDP</td>
<td>2013 N/A</td>
<td>2013 N/A</td>
<td>N/A</td>
</tr>
</tbody>
</table>

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)

<table>
<thead>
<tr>
<th>Inward Direct Investment</th>
<th>Outward Direct Investment</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total Inward</td>
<td>Total Outward</td>
</tr>
<tr>
<td>13,750</td>
<td>9,005</td>
</tr>
<tr>
<td>100%</td>
<td>100%</td>
</tr>
<tr>
<td>Turkey</td>
<td>Turkey</td>
</tr>
<tr>
<td>2,477</td>
<td>4,382</td>
</tr>
<tr>
<td>18%</td>
<td>49%</td>
</tr>
<tr>
<td>Norway</td>
<td>Georgia</td>
</tr>
<tr>
<td>2,285</td>
<td>2,774</td>
</tr>
<tr>
<td>17%</td>
<td>31%</td>
</tr>
<tr>
<td>United Kingdom</td>
<td>Switzerland</td>
</tr>
<tr>
<td>1,965</td>
<td>611</td>
</tr>
<tr>
<td>14%</td>
<td>7%</td>
</tr>
<tr>
<td>Iran, Islamic Republic of</td>
<td>France</td>
</tr>
<tr>
<td>1,088</td>
<td>142</td>
</tr>
<tr>
<td>8%</td>
<td>2%</td>
</tr>
<tr>
<td>Netherlands</td>
<td>United Kingdom</td>
</tr>
<tr>
<td>780</td>
<td>136</td>
</tr>
<tr>
<td>6%</td>
<td>2%</td>
</tr>
</tbody>
</table>

"0" reflects amounts rounded to +/- USD 500,000.
Source: IMF Coordinated Direct Investment Survey

Table 4: Sources of Portfolio Investment

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

19. Contact for More Information

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