



**USAID**  
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**TRADE AND INVESTMENT REFORM  
SUPPORT PROGRAM IN AZERBAIJAN**



# QUARTERLY REPORT

**JULY 01 – SEPTEMBER 30, 2008 (Q4, 2008)**

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PROGRAM IN AZERBAIJAN**

**Contract No. AFP-I-00-04-00002-00, Task Order #10  
under the SEGIR Commercial, Legal and Institutional Reform Indefinite  
Quantity Contract (CLIR IQC)**

**Chemonics International, Prime Contractor  
AECOM International (formerly The Services Group), Subcontractor  
Economic Integration Forum, Subcontractor**

The author's views expressed in this publication do not necessarily reflect the views of the United States Agency for International Development or the United States Government.

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Cover Photo: USDA trainer Roberto Pantaleon trains Border Inspectors on how to conduct inspections of truck/vehicles, cargo, airplanes, mail, and passenger luggage.

## ACRONYMS

ABA-ROLI	American Bar Association Rule of Law Initiative
AIC	Azerbaijan Investment Company
AZE	Working Party file code for questions on Azerbaijan accession to the WTO
CAC	Codex Alimentarius Commission
CDG	Corporate Governance Division (within Ministry of Economic Development)
CLIR IQC	USAID Commercial, Legal and Institutional Reform Indefinite Quantity Contract
DTRA	US Defense Threat Reduction Agency
EIF	Economic Integration Forum
ERRA	Energy Regulators Regional Association
FORECAST	USAID Focus on Results: Enhancing Capacity Across Sectors in Transition Countries program (implemented by World Learning)
FSSP	USAID Financial Sector Strengthening Program
GOAJ	Government of Azerbaijan
GMO	Genetically Modified Organisms
IFC	International Finance Corporation
IFRS	International Financial Reporting Standards
IPP	independent power producer
IPPC	International Plant Protection Convention
IPR	Intellectual Property Rights
LOE	Level of Effort (in person-days)
MED	Ministry of Economic Development (Government of Azerbaijan)
MOU	Memorandum of Understanding
MP	Member of Parliament
NARUC	National Association of Regulatory Utility Commissioners
OECD/DAC	Organisation for Economic Co-operation and Development/ Development Cooperation Directorate
OIE	<i>Office International des Epizooties</i>
PDP	USAID Parliamentary Development Program
PSCEP	USAID Private Sector Competitiveness Enhancement Program
SCMSP	State Committee on Management of State Property
SME	Small and Medium-Size Enterprise
SO	USAID Strategic Objective
SOE	state-owned enterprise
SOW	Scope of Work
SPA	State Procurement Agency
SPS	Sanitary and Phyto-Sanitary
SSRRE	State Service for Registration of Real Estate
TBT	Technical Barriers to Trade
TC	Tariff Council
TIRSP	USAID Trade and Investment Reform Support Program in Azerbaijan
TSG	The Services Group
UNCITRAL	United Nations Commission on International Trade Law

USAID	U.S. Agency for International Development
USEA	U.S. Energy Association
US FTC	U.S. Federal Trade Commission
USTDA	U.S. Trade Development Agency
WTO	World Trade Organization
WTO GPA	World Trade Organization Government Procurement Agreement

## **EXECUTIVE SUMMARY**

The third quarter of 2008 (our fourth quarterly report of the project year) showed significant progress on both components. In Component One, the critical activity was support for the Working Party meeting held in Geneva. The TIRSP Component One team enabled its next working party meeting through providing effective replies to questions raised by working party members, preparing other supporting materials (e.g. ACC/9), promoting more liberalized market access offers, and advancing reform.

### **WTO Support (Component One) Activities**

- TIRSP advisors continued providing support preparing replies to questions raised by working party members, and TIRSP worked closely with the Ministry of Economic Development (MED), the State Agency for Standardization, Metrology and Patents (SASMP) and the copyright office to finalize intellectual property replies, and the ACC/9-TIRSP checklist.
- The TIRSP legal team completed draft amendments to the law on government procurement for the State Procurement Agency (SPA).
- TIRSP lawyers analyzed the draft Customs Code to align it with the World Customs Organization (WCO) and Kyoto Convention.
- The TIRSP legal team prepared further amendments for introduction into the Draft Law on Technical Regulations and the Draft Amendments to the Food Law.
- TIRSP initiated and completed the development of an institutional development plan and e-procurement plan for the State Procurement Agency.
- TIRSP legal team also presented proposals on establishing the customs body appeal and the bindings ruling unit to Customs Committee officials. TIRSP held two roundtables on these proposals.
- TIRSP promoted membership in Codex Alimentarius based on a roadmap provided earlier to the GOA.

### **The Business Environment Component (Component Two) Activities**

Component Two activities advanced program goals in 1) investor protection, promotion, and institutional governance; 2) sanitary and phyto-sanitary (SPS) and agricultural policy; 3) infrastructure reform; and 4) demand-driven trade and investment activities. Component Two activities included the following:

- TIRSP continued advising the Azerbaijan Investment Company (AIC) in cooperation with USAID's Financial Services Strengthening Project (FSSP). The team prepared Basic Principles of AIC, Principles of Conduct for Management, Sample Indices of Codes of Conduct, and a summary Action Plan to help AIC management both exercise proper oversight and improve internal decision-making processes.
- Late in the quarter TIRSP received detailed comments on the Competition Code from the US Federal Trade Commission (FTC), and worked to incorporate amendments to be included in the Third Readings scheduled for November 2008.

- The TIRSP team advised the Economic Commission, Presidential Administration, MOED, and the American Chamber of Commerce in Azerbaijan (AmCham) to monitor progress on the draft Law on Investment Activity.
- TIRSP Property Tax Specialist Jerome Anderson examined the current property tax system and explored integration of land and property taxes for *ad valorem* property tax. Comprehensive recommendations were provided to the GOAJ based on Mr. Anderson's research.
- TIRSP developed and advocated a property tax pilot program to best demonstrate and explore property tax region moving the country closer to international best practice. A law developed from the pilot should be adopted by the end of 2008 so a phased implementation may begin in early 2009.
- TIRSP consultant Simeon Sahadachny advised on draft amendments to the Procurement Law prepared by the State Procurement Agency. TIRSP suggestions, most of which were reviewed and accepted by the SPA, mark significant progress in the evolution of the Procurement Law towards alignment with international standards.
- The Corporate Governance Task Force requested that a revised version of the draft SOE Law by an Azerbaijani lawyer; Nazli Ahmadova from Apex Advisors redrafted the law, and TIRSP local and international experts are currently reviewing it. TIRSP reviewed the most recent versions of the draft law on collateral and the draft law on state cadastre of real estate in August, and detailed recommendations were provided to the State Service for Registration of Real Estate (SSRRE) for introducing further amendments to the draft.
- TIRSP continued its dialogue this quarter with the Department of Entrepreneurship Development within MED on promoting bankruptcy reform, and paved the way for short term international advisory in late 2008 and early 2009.
- TIRSP completed and published a 200-page SPS reference manual for identification of plant disease, weeds, and pests found in Azerbaijan.
- TIRSP helped the State Plant Protection Service develop a website ([www.azerinppo.az](http://www.azerinppo.az)) for import and export requirements and processes for all plant and plant derived products.
- USAID in partnership with USDA developed and presented an SPS risk assessment course specifically for Azerbaijan.
- TIRSP worked with USDA to introduce participants to the development of international standards for food safety within the Codex Alimentarius Commission (CAC), developing a National Codex Office and Committee, joining the CAC, and a timeline for joining the CAC in the context of WTO accession.
- TIRSP also delivered Border Inspection training on Plant and Plant products in September, and hosted a USDA team from Turkey and United States to determine potential activities that the USDA could undertake to strengthen the Azerbaijan animal and plant services.
- TIRSP Senior Agricultural Policy Specialist Dyaa and the TIRSP team completed its revision of the draft Food Security Program (FSP) for consideration in the coordination meeting in the Cabinet of Ministers.
- TIRSP provided timely technical information to MED on "Determining Strategic Wheat Stock Levels", "Recent International Experiences in Food Security Programs", "Market Based Agricultural Finance and Risk Management", and "Food Consumption and Daily Caloric Intake."
- The management of Azerigaz, the state-owned gas distribution company, accepted the TIRSP proposal on conducting the gas pilot. Pilot activities included shadowing meter readers and examining operations of gas distribution companies within Azerigaz. Using the

knowledge gained through the gas pilot study, the TIRSP utilities team prepared a tariff adjustment plan.

- Mr. Ramazanov requested USAID assistance in designing tariffs for the Wind Power pilot project that is being built north of Sumgayit. TIRSP scheduled site visits, submitted data requests, and prepared a work plan to develop a wind power tariff model.
- TIRSP prepared the Draft Charter; draft Decree, two cover letters to USAID for review in August and September. In the next reporting period TIRSP will work to incorporate comments.
- TIRSP participated in the Energy Regulators Regional Association (ERRA) training seminar in July, preparing ten presentations on various utility regulation and tariff topics for the seminar.

## **COMPONENT ONE – WTO ACCESSION**

### **Summary**

The focus of this reporting period of Component One was assisting Azerbaijan in enabling its next working party meeting through providing effective replies to questions raised by working party members, preparing other supporting materials (e.g. ACC/9), promoting more liberalized market access offers, and advancing reform. TIRSP continued working in this reporting period on a comprehensive analysis of the prospective impact of trade and investment liberalization, especially for those economic sectors likely to be characterized as non-competitive in the post-WTO accession period.

Progress was made on all aspects of Component One. The replies to questions raised by the US and EU as well as other supporting documents (ACC/9 and revised legislative action plan) were ready for submission to the WTO Secretariat by end of this period. Further amendments were made to improve the Draft Law on Technical Regulations, the Draft Amendments to the Food Law, and the Draft Amendments to the Law on Government Procurement, and the Draft Law on Anti-Dumping, Countervailing, and safeguard measures. Institutional reform proposals were completed for customs appeal unit and binding rulings unit and presented to the State Customs Committee. Institutional reform proposals were also prepared for improving statistics data collection and e-procurement. Last, key elements of partial equilibrium model were developed and elements of draft report on assessing impact on vulnerable sectors were prepared.

### **The Accession Process**

#### *Working Party Meeting Support*

Through the reporting period TIRSP advisors continued providing support in preparing replies to questions raised by working party members and continued providing advice to promote the development of revised market access offers responsive to working party members' requests.

During August a first draft of replies was circulated to ministries for comment. TIRSP further completed ACC/9 intellectual property checklist and a revised legislative action plan for submission to the WTO.

In September TIRSP assisted in incorporating comments received from ministries and worked closely with the Ministry of Economic Development (MED), the State Agency for Standardization, Metrology and Patents (SASMP) and the copyright office to finalize intellectual property replies, the ACC/9-TIRSP checklist, and replies to questions on standards and technical regulations.

### **Legal Reform**

TIRSP continued to monitor the new legislative agenda adoption process on the foreign trade regime's WTO conformity throughout the reporting period. Work also continued on advancing the legal reform process and bringing draft legislation into greater conformity with WTO agreements.

In July the team focused efforts on aligning all legislation under the Presidential legislative action plan with WTO requirements. The TIRSP legal team also completed draft amendments to the law on government procurement for the State Procurement Agency (SPA).

TIRSP lawyers completed an analysis of the draft Customs Code for compliance with WTO and to align it with the World Customs Organization (WCO), Kyoto Convention (the “International Convention on the Simplification and Harmonization of Customs Procedures”), and similar instruments.

The TIRSP legal team prepared further amendments for introduction into the Draft Law on Technical Regulations and the Draft Amendments to the Food Law. Draft model regulations on valuation of interest charges were prepared. In September, TIRSP learned that the draft amending the law on government procurement was submitted to the Cabinet of Ministers.

In supporting legal reform, TIRSP has been providing legal research, analysis, and drafting as well as significant on-the-job training to relevant ministries and state bodies as requested.

### **Institutional Reform**

TIRSP continued facilitating institutional reform through promoting recommendations to join Codex and improve procurement data collection throughout this reporting period.

TIRSP initiated and completed the development of an institutional development plan and e-procurement plan for the State Procurement Agency (SPA). TIRSP then delivered a roundtable at the SPA on government procurement in July.

Model legislation and organizational structures and functions of both a customs appeal unit and a customs binding rulings unit were prepared by the TIRSP legal team. The team then presented proposals on establishing the customs body appeal and the bindings ruling unit to Customs Committee officials. TIRSP held two roundtables on these proposals.

Additionally, TIRSP reviewed the recently enacted law on insurance activities and conducted a preliminary assessment of the status of the Customs Committee’s risk management program to determine what technical assistance support the TIRSP could provide.

Last, TIRSP continued to promote membership in Codex Alimentarius based on the roadmap provided earlier to the GOAJ.

### **Macroeconomic Policy/Impact Analysis**

During this reporting period TIRSP launched the development of a WTO Accession Transition Strategy that maximizes the impact of trade/investment integration processes on (1) economic diversification, (2) enhanced factor productivity, and (3) robust investment and employment growth in high potential sectors of the non-oil economy; and minimizes the transitional flow of productive factors from non-competitive to competitive sectors/regions. The first Draft Report is expected in October 2008.

TIRSP also launched the design and development of Partial Equilibrium/Computable General Equilibrium (PE/CGE) Model to assess the impact of trade liberalization. The structure of the PE/CGE Models was completed at the end of August 2008. During September, TIRSP experts

developed the PE/CGE Model for implementation using Excel worksheets. Following simulation, scheduled for November 2009, the results will be presented to the relevant counterparts. TIRSP will then deliver documentation and training to the staff of MED in late 2009.

## **Component Two – Trade and Investment Reform**

### **Introduction**

The Component Two agenda presents a broad-based portfolio of business environment activities as its starting point. In the first months of the project, specialists completed assessments in areas key to Azerbaijan's enabling environment and TIRSP activities. These assessments led to the strategy laid out in the Year One Work Plan, which organized project activities into four main areas of focus: 1) investor protection, promotion, and institutional governance; 2) sanitary and phyto-sanitary (SPS) and agricultural policy; 3) infrastructure reform; and 4) demand-driven trade and investment activities. The final category allows TIRSP to work flexibly and responsively to meet Azerbaijan's development needs in the diverse areas which fall under Component Two.

### **Investor Protection, Promotion, and Institutional Governance**

#### ***Collective Investment Fund Support and Promotion***

This quarter, TIRSP continued its work advising the Azerbaijan Investment Company (AIC), in cooperation with the USAID Financial Services Strengthening Project (FSSP). TIRSP fielded Peter Zoll, a short-term investment fund governance expert, to prepare a document outlining strategic options for the medium- and long-term development of the AIC that specifically focused on clearly defining and separating the functions of the Supervisory Board and Senior Management and to eliminate inefficiencies and lend authority to management. TIRSP presented its recommendations during this reporting period, which were well received by AIC.

Additionally, TIRSP prepared a the Basic Principles of AIC, Principles of Conduct for Management, Sample Indices of Codes of Conduct, and a summary Action Plan to help AIC management both exercise proper oversight and improve internal decision-making processes.

*Expected activities and outputs in the next quarter:*

- Develop and endorse the adoption of core governance principles by AIC;
- Develop and endorse the adoption of Code of Conduct by AIC;
- Adoption of roles definition for supervisory board and management; and
- Formation of executive committee within management.

#### ***Competition Policy/Anti-Monopoly Regulation***

The project continues to monitor the progress of the passage of the Competition Code through the Milli Majelis, through TIRSP connections within the Economic Commission. This quarter, the project received detailed comments on the Competition Code from the US Federal Trade Commission (FTC). The FTC comments were aligned with those of our own experts and the project is currently translating the FTC comments and exploring ways these can be effectively and succinctly presented to the Milli Majelis before the Competition Code's Third Reading. The Third Reading is currently scheduled for November 2008.

*Expected activities and outputs in the next quarter:*

- Obtain the recommendations of the Economic Commission on the Third Reading version of the law, review and provide feedback as soon as possible; and

- Continued dialogue with the FTC prior to the autumn session regarding the formal submission of their comments.

### ***Investment Activity Law Reform***

The project has maintained a steady dialogue with the Economic Commission, Presidential Administration, MED, and the American Chamber of Commerce in Azerbaijan (AmCham) to monitor progress on the draft Law on Investment Activity. We are working to obtain the draft FDI law generated by MOED so we can provide additional commentary on the law before its formal submission to the Milli Majelis. The project has lined up Investment Law specialist Tom Dimitroff to travel to Azerbaijan in the next quarter, pending the project's obtaining the new draft.

*Expected activities and outputs in the next quarter:*

- Obtain the draft FDI Law generated by MOED before its formal submission to the Majilis.
- Conduct a complete analysis of new draft (once obtained) and coordinate our response with the AmCham, MED, Presidential Administration, and Economic Commission.

### ***Tax Policy and Administration***

*Property tax issues.* Responding to feedback from Ministry of Taxes (MoT) Prof. Mirdamed Sadiqov, the Head of Tax Policy and Revenue Department, TIRSP fielded ST Property Tax Specialist Jerome Anderson to study the current property tax system and ascertain the feasibility of integrating the land and property taxes into an integrated *ad valorem* property tax. Mr. Anderson and the TIRSP team conducted the bulk of the research in the previous period and then presented the main findings and proposed reforms to USAID/Azerbaijan and GOAJ during this reporting period.

The study led TIRSP to advocate the following recommendations to counterparts at MoT:

- consolidate land and property tax administration to end the current division between the taxes for physical and legal persons;
- move to market valuation, in place of the current forms of valuation based on Soviet construction cost and land characteristic-based formulae;
- decrease reliance on property registration, which is now incomplete at best, for identifying the property and land tax base;
- only after the above-mentioned reforms are designed should consideration be given to consolidating the property and land taxes because the major problems with the taxes currently are not related to separate land and property taxes; and
- improve the current system of intergovernmental finance to more properly define expenditure assignments at the municipal level.

By adopting these recommendations, TIRSP holds that the GOAJ can move toward a more balanced tax system, a more rational division of responsibilities to provide government services, and a property tax that supports not only municipal finance but also the development and long-term sustainability of the real estate market.

TIRSP advocated for a pilot program to develop an improved property tax regime in Azerbaijan based on the findings of the property tax study. The pilot study that TIRSP recommended would ascertain the existing collection rates for all the property and land taxes to identify problems,

analyze how best to construct the fiscal cadastre, and compare the values currently used in property and land taxation against market values to determine how the existing base differs from true market value. At the conclusion of the foregoing analyses, a law can then be drafted that moves Azerbaijan property tax closer to international best practice. The law should be adopted by the end of 2008 so a phased implementation may begin in early 2009.

*Expected activities and outputs in the next quarter:*

- Enhancement of the revenue impact analysis of the proposed personal income tax, corporate income tax and value added tax amendments; and
- Obtaining buy-in from MoT and Cabinet of Ministers for a pilot program that would build fiscal cadastres in at least two municipalities and develop computer-assisted mass appraisal (CAMA) models to value the properties.

### ***Public Procurement***

During the week of July 7-11, 2008 TIRSP fielded Simeon Sahadachny to review and discuss the draft amendments that had been prepared by State Procurement Agency (SPA) based on the detailed proposal submitted earlier by TIRSP for comprehensive amendment of the Procurement Law. The TIRSP team also considered some additional draft amendments developed by SPA. In the previous reporting period, TIRSP commented on the ensemble of amendments proposed by SPA and also identified a limited number of additional priority amendments that would bring the Procurement Law more into line with international best practice standards including the WTO Agreement on Government Procurement (GPA), the EU Directives on public procurement, and the UNCITRAL Model Law on Procurement.

In the course of the work, SPA indicated its acceptance of most of the TIRSP recommendations, which were then reflected in a draft text. On a limited number of points SPA indicated that it would further consider the precise content of the amendment, in particular the proposed amendments concerning central collection and reporting of data, and accessibility of data to the general public.

The enactment of the amendments that reflect TIRSP suggestions would mark significant progress in the evolution of the Procurement Law towards alignment with the above-mentioned international standards, particularly the extension of the scope of application to include BOT and concession types of contracts, as well as barter contracts, which might be expected to help reduce the practice of excluding mega-infrastructure projects from the application of the Law.

*Expected activities and outputs in the next quarter:*

- Finalize SPA proposals to the Public Procurement Law and facilitate submission to the Cabinet of Ministers; and
- Review and finalize institutional support plan based on finalized proposal.

### ***Corporate Governance Strengthening***

*SOE Law Reform.* The Corporate Governance Task Force, led by Sanan Tapdigov from MED, has requested that a revised version of the draft SOE Law be produced, preferably by a well-regarded Azerbaijani lawyer familiar with Azerbaijani legal practices. The project retained Nazli Ahmadova from Apex Advisors to redraft the law and work closely with the Corporate Governance Division of

MOED. A first draft of the law was received at the end of this quarter, and TIRSP local and international experts are currently reviewing it to ensure that the draft conforms to OECD principles on SOE corporate governance.

*Expected activities and outputs in the next quarter:*

- Development of a consensus draft of the SOE law;
- Review of the Task Force Corporate Governance Code recommendations (provided such have been released during the next quarter); and
- Formalize OECD Corporate Governance Conference plans and provide dedicated logistics assistance.

### ***Property Rights Registration***

TIRSP reviewed the most recent versions of the draft law on collateral and the draft law on state cadastre of real estate in August. The Collateral Law was found to be in line with best international practices. As for the cadastre draft, detailed recommendations were provided to the State Service for Registration of Real Estate (SSRRE) for introducing further amendments to the draft.

TIRSP will follow up and promote these proposals and will hold further discussions with SSRRE officials during the next reporting period.

*Expected activities and outputs in the next quarter:*

- Monitor SSRRE progress on moving the Collateral Law through the formal submission process;
- Include a discussion of the Collateral Law on the agenda of laws to be presented to Majilis deputies, Commission members and GOAJ representatives as part of the TIRSP/PDP training initiative; and
- Review the SSRRE registry implementation plan if developed and released this quarter.

### ***Streamlining Business Closure***

*Bankruptcy law.* Bankruptcy reform continues to be a prime area of interest for the GOAJ, as it is a major indicator in the World Bank Doing Business rankings. The project is continuing its dialogue with the Department of Entrepreneurship Development within MED on how bankruptcy reform can be promoted among various GOAJ actors. TIRSP anticipates fielding ST expert Michael Palmer during the next quarter to ensure that momentum in this important area is not lost.

*Expected activities and outputs in the next quarter:*

- A presentation to GOAJ counterparts on immediate reform efforts in bankruptcy;
- Based on consensus around immediate reform efforts, a package of revisions (including explanatory notes) to the Law on Insolvency and Bankruptcy designed to increase the efficiency, speed and recovery rate of the bankruptcy process; and
- A memo outlining an action plan for mid- to long-term reform efforts in bankruptcy.

## Sanitary and Phyto-Sanitary Oversight (SPS) and Agricultural Policy

### *Sanitary and Phyto-Sanitary (SPS) Oversight*

*Institutional capacity building of State Plant Protection Service.* This quarter, TIRSP in close cooperation with the Phytosanitary Service, completed and published a 200-page reference manual that provides a detailed listing, color photographs, and identification methods of all plant disease, weeds, and pests (regulated and non-regulated) found in Azerbaijan. The manual is designed to help the government improve control of these materials and improve trade by clearly defining what is prohibited by Azerbaijan. The booklet also supports key IPPC requirements. The booklet includes written descriptions, life cycle photographs, and drawings and will be provided to government officials, producers, exporters and importers.

TIRSP helped the State Plant Protection Service develop a website ([www.azerinppo.az](http://www.azerinppo.az)) focused on import and export requirements and processes for all plant and plant derived products. The website provides information to government officials, citizens, importers, exporters, trading partners, and industry on laws and regulations, tariffs, fees, import and export guidelines. It has a print on demand capability to allow the printing of brochures and booklets on plant diseases, pest, and weeds. It has linkages to trading partner web sites, and has the ability to send questions directly to the ministry so that answers can be provided in a simple, quick manner. The website acts as a key information portal for trading partners on any changes that are being made by the government with regards to plant protection in compliance with IPPC norms. Additionally, the website helps ensure that Phytosanitary officers understand the requirements of importing partners. The website is in Azerbaijani, Russian, and English.

*Training Activities.* Based on discussions with various Azerbaijan Ministries and with the private sector, USAID in partnership with USDA developed and presented a risk assessment course specifically for Azerbaijan in July. Dr. Latimer, an expert in microbiological risk assessment, covered how to conduct a risk assessment based on the Codex Risk Assessment Process, i.e., hazard identification, hazard characterization, exposure assessments, and risk characterization. She also explored data requirements, processes, and approaches for conducting a risk assessment by introducing Monte Carlo simulation approaches. The training session drew upon examples of scientific risk assessment and policy formulation at USDA/FSIS and provided a guide for conducting risk assessments. To enhance participants' familiarity in developing quantitative microbial risk assessment models, she provided an optional hands-on section on modeling using risk assessment software.

In addition to the training on risk assessment, Dr. West, USDA Food Safety and Inspection Service Trainer, introduced the participants to the development of international standards for food safety within the Codex Alimentarius Commission and how risk analysis is used in this process. Dr. West also gave an offsite presentation and held discussions with senior-level officials from GOAJ about Codex Alimentarius, developing a National Codex Office and Committee, joining the CAC, and a timeline for joining the CAC in the context of WTO accession by 2009.

TIRSP, as a part of the joint USAID/USDA program, delivered the Border Inspection training on Plant and Plant products in September. This four-day training provided more than 30 attendees with information on how to conduct border inspections of truck/vehicles, cargo, airplanes, mail, and passenger luggage in accordance with IPPC norms. The training session drew upon examples of different inspection and safeguarding techniques based on pest risk. To enhance students' familiarity in the inspection and interception of pest and diseases, a "hands on" training session was

conducted, where the participant inspected and cut different agricultural commodities, including wood, looking for the presence of pests. In attendance were representatives from various ministries, including health, plant protection, veterinary services, economic development, standards, and the State customs. The training will help to improve border inspections and passenger baggage inspections.

*Other Activities.* TIRSP hosted a USDA team from Turkey and United States to determine potential activities that the USDA could undertake to strengthen the Azerbaijan animal and plant services. One outcome of the meetings is that the Chief Veterinary Officer has agreed to lift the ban on US poultry products which has been in place since July 2008.

The project also developed an easy to use guide that allows importers and exporters to better understand the requirements and costs associated with Phytosanitary inspections/certificates.

### ***Food Security and Agricultural Policy***

During this period TIRSP Senior Agricultural Policy Specialist Dyaa and the TIRSP team completed its revision of the draft Food Security Program (FSP), which incorporated major changes in both the strategic orientation and the format to coincide with international best practices and results-based management. TIRSP presented its recommendations for improving the draft FSP and Plan of Action to MED in early July for consideration in the coordination meeting in the Cabinet of Ministers.

TIRSP's efforts to revise the FSP centered on the ultimate goal of the program – to meet the internationally agreed upon concept of food security so that “[a]ll [Azerbaijani] people, at all times, have physical, social and economic access to sufficient, safe and nutritious food to meet their dietary needs and food preferences for an active and healthy life.” The program incorporated objectives across various periods and for all segments of the population and addressed food availability, stability, access and utilization at the national, local and household levels. In addition, the program focused on market-based, sustainable agricultural and rural development measures to increase agricultural productivity in targeted areas where Azerbaijan enjoys a comparative advantage, which will create employment opportunities and increase incomes.

The Government of Azerbaijan's Food Security Program was adopted on August 25, taking into account all key recommendations of TIRSP. Furthermore, TIRSP worked with the MED on a targeted analysis of the revised Food Security Program and related operational plan with specific comments for further improvements designed to ensure the effective implementation of a sustainable market-based program/strategy.

TIRSP also provided timely technical information to MED on “Determining Strategic Wheat Stock Levels”, “Recent International Experiences in Food Security Programs”, “Market Based Agricultural Finance and Risk Management”, and “Food Consumption and Daily Caloric Intake.”

### **Infrastructure Reform**

#### ***Utilities Sector***

TIRSP continued to assist in reforming the regulatory, institutional, service, infrastructure, and other key elements in Azerbaijan's provision of electricity, gas, and water utility services.

*Implementing the Gas Pilot Study.* In the previous reporting period, the management of Azerigaz, the state-owned gas distribution company, accepted the TIRSP proposal on conducting the gas pilot. The TIRSP utilities team worked with Azerigaz to gain access to the staff, field managers, facilities, documentation and data. Following approval of the workplan, the TIRSP team implemented the pilot during this reporting period.

During the pilot study TIRSP conducted several field visits to the citygate, where the gas from high pressure (HP) lines enters the Sabail Distribution. Field operators explained the metering and the low pressure (LP) distribution system as it fans out into the distribution network of Sabail. TIRSP observed that although the system was old and exposed, there were adequate safety systems and metering.

On several occasions, TIRSP utilities team members accompanied the meter readers on their meter reading routes and visits to customer premises to learn firsthand the metering and billing process and practices. Staff discovered that the Sabail Distribution Unit has one of the more modern meter reading and billing systems utilizing automated meter reading (AMR) technology. The meters are read monthly through a small hand-held computer device, carried by the reader on his daily reading route. The device provides customer data to the reader, including name, address, meter number, account number, previous consumption, and payment history. Readers use the device to scan the meter from a distance of approximately one meter. Once the current reading is scanned the device immediately registers current consumption, calculates current charges, balance due including previous balance, and prints the bill which is delivered to the consumer on site or posted on the customer's door.

After the meter reader has completed his day's meter reading routes he returns to the main office and uses the device to upload the data into the database computer, which then transmits all the data to the customer information system (CIS). This is similar to the AMR system used by utilities in advanced countries. The TIRSP utilities team was not able to verify what follow up system is in place for pursuing non-payments, providing notice, and shut-off provisions. TIRSP learned that all payments are made through the designated banks. A daily payment-report is sent to the Sabail district. Actual payments are however made into the Azerigaz account.

The TIRSP team learned that not all gas distribution companies within Azerigaz have such modern operations, due primarily to insufficient cash flows from the gas operations.

TIRSP team also reviewed the procedure for new customer connections. This is an important issue to ensure that consumers have ready access to the gas service. We found the system to be very cumbersome, requiring multiple windows, permits and excessive costs. TIRSP is preparing a separate report on this issue, which will be completed in the next reporting period.

*Gas Tariff Issues.* The TIRSP team observed that during the summer months the actual consumption for most residential consumers was less than 0.1 thousand cubic meters (tcm), resulting in a monthly bill of approximately 2- 3 AZN. This low monthly bill does not cover the cost of distribution network, metering, billing, accounting, collections, etc., much less commodity costs, storage costs, and losses.

The approved gas tariff charged domestic users has a margin of 5 AZN, the difference between wholesale price of 42 AZN and the 47 AZN retail tariffs, which is deemed to cover transportation costs, storage fee, and distribution network, metering, billing etc. It also includes cost of network

losses, which are estimated to be approximately five percent. Commercial, industrial, and other non-domestic consumers on the other hand are charged a margin of 58 AZN, which is more than ten times that for domestic users.

TIRSP found that the domestic users are heavily subsidized by large consumers particularly by those served at HP. Azerigaz readily acknowledges this fact, however it argues that average revenue per tcm adequately recovers its full service costs and thus finds no compelling reason to raise domestic tariffs. Moreover it says it is merely following the GOAJ policy to keep domestic tariffs low.

TIRSP utilities experts noted that this cross-subsidization creates: 1) competitive disadvantage for industry; 2) disincentives for efficient use of natural gas by industry, switching to less efficient alternatives; 3) creates incentives for inefficient and wasteful use by domestic consumers. As the fastest growing consumer category, domestic users exasperate the revenue recovery gap.

Moreover, SOCAR (i.e. GOAJ) already subsidizes all gas consumers by charging 42 AZN per tcm (approximately US\$50) against an international market price of more than \$250 per tcm.

Using the knowledge gained through the gas pilot study, the TIRSP utilities team prepared a tariff adjustment plan. The central recommendation TIRSP provided to Azerigaz is the introduction of a monthly service fee, which reflects fixed and variable distribution costs for the category, separate from commodity charges. TIRSP presented its plan to Mr. Nizami Samadzadeh, Vice Chairman at Azerigaz, and his team. However as noted above he expressed unwillingness to adjust tariffs until Azerigaz receives clear instructions from the GOAJ, meaning Cabinet of Ministers or the President.

In the next reporting period, the TIRSP utilities team will develop a comprehensive gas tariff plan and advocate adoption of TIRSP recommendations based on data from the Sabail pilot.

*Electric Tariff Issues.* In August 2008, Mr. Ramazanov, Energy Advisor of MED and Mr. Gulmohamad Jawadov, Deputy Minister of Industry and Energy (MIE) requested assistance from USAID in developing electric retail tariffs.

In September the TIRSP utilities team submitted to Mr. Ramazanov an extensive request for data on cost, consumption, and loads, segregated by function: generation, transmission and distribution. TIRSP received the data that they had readily available, mainly on generation and transmission costs, and financial and operations costs. Unfortunately much of the data was either not relevant or in an unusable format. Moreover, TIRSP did not receive data on loads and usage by class of customer, which is critical for designing retail tariffs and by customer- category and time differentiated tariffs, two-part tariff etc. In particular the capital cost data, i.e. LT-debt, interest costs, debt service etc, is necessary to develop Revenue Requirements using ROR analysis.

While awaiting more usable data, TIRSP developed an Excel-based model and calculation algorithm for analyzing tariffs. The utility team completed the model during the reporting period, but the team intends to test it against more reliable data in the following period. TIRSP expects to develop proposed tariffs within 30 days of receiving necessary and good quality data. Some effort will be spent on validating the data provided. Where detail data is unavailable, estimation techniques will be utilized.

In the next reporting period the TIRSP utilities team will present the calculations and methodology to the two Ministries and then to Tariff Council for adoption and approving revised tariffs. TIRSP is currently drafting a concept paper how to implement cost based electricity tariffs and the expected impact on current consumers. TIRSP plans to hold a seminar in December to explain and discuss model and data requirements with MED, MIE, Azerenergy, Baku, Sumgayit and other distribution companies.

*Wind Power Tariffs Issues.* In September Mr. Ramazanov requested USAID assistance in designing tariffs for the Wind Power pilot project that is being built north of Sumgayit. During this reporting period, TIRSP scheduled site visits, submitted data requests, and prepared a workplan to develop a wind power tariff model. TIRSP expects to complete and test the tariff model and present findings and recommendations to MED, MEI, and the Tariff Council in December.

*Water Commission Charter.* As requested by the USAID, TIRSP prepared and gave the Draft Charter; draft Decree, two cover letters to USAID for review in August and September. In the next reporting period TIRSP will work to incorporate USAID comments and plan the next steps.

*Other activities.* TIRSP participated actively in Energy Regulators Regional Association (ERRA) training seminar in July. TIRSP assisted ERRA organizers and other instructors in developing course agenda and topics. The TIRSP utilities team prepared ten presentations on various utility regulation and tariff topic for the seminar. All presentations are available on the ERRA website and on Project Database.

TIRSP utility experts carried out discussions with the Deputy Minister of Energy on strengthening the Tariff Council. Additionally, TIRSP started and completed drafting of Water charter, decree and cover letters during this reporting period.

The project prepared and submitted to the Advisor of the Minister of Economy a detailed data request for tariff calculations for electric services of Azerenergy for generation and transmission and distribution

### ***Telecommunications Sector***

This quarter the project continued its recruit for a telecommunications specialist or team of specialists to promote TIRSP's reform recommendations to the Ministry of Communications and Information Technology (MCIT). The project anticipates fielding a consultant early in the next quarter.

*Expected activities and outputs in the next quarter:*

- Delineation of a telecommunications work plan after consultation with USAID and MCIT;
- Commencement of telecommunications support based on agreed upon work plan.

### **Demand-Driven Trade and Investment Activities**

#### ***Customs Code Review***

TIRSP facilitated the establishment of a customs administrative appeal body and a customs binding rulings unit to bring Azerbaijan into compliance with the WTO agreements on protecting the rights of traders and investors. TIRSP advisors delivered and discussed a tabular analysis of the Draft

Customs Code of Azerbaijan with the Ministry of Economic Development WTO Coordinator and the State Customs Committee. TIRSP held a roundtable on appeals and rulings held in two sessions on September 4, 2008 at the State Customs Committee. The purpose of the roundtables was to prepare the Customs Committee for the eventual implementation of both the binding rulings and administrative appeals procedures, which are authorized by the draft Customs Code, and to begin discussion of specific institutional changes that will be required.

One session was held for Customs Officers responsible for tariff classification and origin determinations, and a second session was held for Customs Officers responsible for customs valuation. The roundtable was attended by the five Customs officers responsible for these matters, including the heads of the departments. At the roundtable, TIRSP experts presented and discussed model legislation to establish Customs Body Appeal, model legislation to establish Customs Bindings Ruling Unit (rules of origin), the organizational structure and functions of Customs Body Appeal and Customs Bindings Ruling Unit (rules of origin).

### ***Strengthening the NGO Council***

The GOAJ requested USAID support in its efforts to enhance state support for non-governmental organizations by establishing a grants program administered by the new NGO Council under the auspices of the President of the Republic of Azerbaijan. Following a competitive process, the GOAJ intends to award through the NGO Council grants in several fields including, but not limited to economic development and institutional strengthening. T

During this reporting period TIRSP sponsored a grants expert to evaluate their efforts to date and provide recommendations to improve the government procurement framework. TIRSP assessed the current documentation and grant making process proposed by the GOAJ for the NGO Council and drafted recommendations for implementing best practices in the government grants program to ensure a fair and equal application, evaluation, and management process.

## ANNEX A. USAID NEWS STORY



**USAID**  
FROM THE AMERICAN PEOPLE

**TRADE AND INVESTMENT REFORM  
SUPPORT PROGRAM IN AZERBAIJAN**

### NEWS STORY

#### U.S. Co-Funds Plant Health Border Inspection Training



USAID's Trade and Investment Reform Support Program (TIRSP) in Azerbaijan and the United States Department of Agriculture (USDA), in collaboration with the Government of Azerbaijan, conducted a four-day "Border Inspection Training for Plant Health" workshop on September 23, 2008.



*Participants acquired the basic skills necessary to identify and intercept plant pests and diseases at ports of entry.*

The workshop addressed the policy and regulatory framework governing international trade in plants and animals; procedures for examining and monitoring imports, containers, passengers, baggage, and mail; and treatment of shipments at the port of entry. Program participants acquired the basic skills necessary to identify and intercept plant pests and diseases at ports of entry, preventing the introduction of new pests and diseases to Azerbaijan and providing greater assurances that Azerbaijan's exports are free from pests.

The event brought together 30 participants, including representatives from the Ministry of Agriculture and Industry.

The seminar provided the Government of Azerbaijan with the knowledge and skills necessary to protect the health of its domestic agricultural producers, ensure the safety of exported products to its trading partners, and comply with the WTO's international standards for plant health border inspections.

The event was highly publicized by several print and electronic media outlets.

## ANNEX B. BUDGETED LEVEL OF EFFORT REMAINING (AT END OF Q4, 2008)

Name	Description	Company	Total Approved LOE	LOE Used		Total LOE Remaining
				through September 30, 2008	LOE Used Jul-Sep	
Abdou, Dyaa	Agriculture Policy Specialist	AECOM	55	55	44	0
Anderson, R. Jerome	Property Tax Specialist	Chemonics	50	50	12	0
Brown, Darrell	Commercial Lawyer	Chemonics	27	24	0	3
Burcroff, Richard	Senior Agricultural Policy Specialist	Chemonics	28	28	0	0
Caner, Selcuk	Econometrician and Tax Expert	AECOM	65	45	35	20
Cohen, Roshana	Grants Expert	Chemonics	2	2	2	0
Deeb, Thomas	(SPS) Specialist	AECOM	140	136	28	4
DeGrande, Dustin	Chemonics Home Office Manager – Start-Up Specialist	Chemonics	13	13	0	0
Dimitroff, Thomas	Investment Attorney	E F	4	4	0	0
Dobrilovic, Stevan	Senior Land Lawyer	Chemonics	8	2 875	0	5.125
Farhat, Farhat Youwakim	Senior WTO Accession Advisor	E F	182	167 25	51 25	14.75
Fitzpatrick, Dan	Collateral Law and Privatization Specialist	Chemonics	46	43 5	0	2.5
Garrison, William	Telecom Sector Specialist	Chemonics	19	17	0	2
Hjort, Kim	SPS and TBT Specialist	E F	88	72.75	1	15.25
Hoffman, Tom	SPS/Food Safety Specialist	AECOM	19	19	0	0
Irvin, Benjamin	Trade Remedies Specialist	E F	86	83	0	3
Khadka, Rup	Tax Policy and Administration Expert	AECOM	59	55	0	4
Laro, Marlene	Tax Lawyer	AECOM	12	12	0	0
Lewarne, Steven	Macroeconomist and Work Plan Advisor	AECOM	9	8	0	1
Lord, Montague	Senior Economist	E F	38	31	28	7
Maier, Polly	IPR Specialist	E F	58	41.77	9.53	16.23
Millan, Hector	WTO Advisor & Tariff Negotiations Specialist	Chemonics	30	30	0	0
Moissejev, Andrey	Modeling and Trade Information Expert	AECOM	141	115	36	26
O'Shea, Brian	Customs Specialist	E F	65	56	18.5	9
Palmer, Michael	Business Closure and Mediation Specialist	Chemonics	27	27	0	0
Protasi, Juan Carlos	Industrial Zone Expert	AECOM	18	18	0	0
Sahaydachny, Simeon	Procurement Specialist	E F	78	78	20	0
Schanck, Jeremy	Chemonics Home Office Director - Workplanning	Chemonics	28	27	13	1
Schiffman, Steve	IPR Specialist	E F	33	31	0	2
Snelbecker, David	Trade Policy Reform Expert	AECOM	9	9	0	0
Vogel, Robert	Cooperative and Municipal Bank Finance Specialist	AECOM	18	18	0	0
Wright, Geoff	Trade, Int'l Transaction, and Competition Policy Specialist	AECOM	23	23	0	0
Zaldastanishvili, Diana	Project Management Specialist	Chemonics	20	20	0	0
Zoll, Peter	Investment Fund Governance Expert	Chemonics	49	32	18	17
<b>TOTAL</b>			<b>1442.00</b>	<b>1289.15</b>	<b>260.28</b>	<b>152.86</b>

## ANNEX C. PROJECT DELIVERABLES

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### Azerbaijan TIRSP Project Deliverables

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03. Azerbaijan TIRSP Q3 2008 Quarterly Report

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### Azerbaijan TIRSP Consultant Deliverables

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AIC Governance Manual that supports full compliance with OECD/IOSCO governance practices (no later than July 15)

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Comprehensive and detailed assessment report that describes the current legal regime regulating open collective funds, highlights regulatory and legal changes required to move the system to an IOSCO best practices basis, recommends specific legal/regulatory changes wherever these are required, and recommends alternative open collective investment fund structures appropriate for implementation in Azerbaijan (no later than July 31)

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Trip reports at the end of each trip to Azerbaijan summarizing the results of the trip and contemplated next steps (total of three trips)

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An AIC draft code of ethics

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Report assessing the feasibility of moving to a combined ad valorem property tax. The report should recommend a proposed implementation roadmap for the GOAJ, including: Legal reform (including draft legislation for the combined tax), Institutional reform (including necessary IT procurement, training, facilitation of interface between state/municipal governments, property registry, cadastre, etc), Taxpayer education/public relations, Suggestions for a pilot program in selected municipalities in Azerbaijan

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Agricultural Policy Mission Report: main results and recommendations

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A brief memorandum putting forth recommendations for best practices in establishing and managing a GOAJ grants program, specifically in processing grant applications and awards.

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A functioning CGE Model and a revised PE Model provided to MED along with user guidelines.

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A utility to compute fees reflective of cost of services rendered.

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Revised specific rates converted to ad valorem rates in support of revised tariff offer.

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Draft amendments to the law on public procurements

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Report outlining specific proposals to modernize the system of collecting and reporting statistics on government procurement

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Government procurement institutional strengthening plan

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E-Procurement development plan

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A user manual for operation of the partial equilibrium model

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Draft Amendments to Cabinet of Ministers Resolution of the Republic of Azerbaijan "On Approval of Additional Rules and Regulations for the Purpose of Protection of the State Border of the Republic of Azerbaijan" No.140 dated March 9, 1993 prepared.

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Recommendations to reduce the list of goods subject to mandatory certification.

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Draft Cabinet of Ministers Resolution "On Establishment and Rules of Operation of TBT Enquiry Points."

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ACC/8 – SPS Conformity Checklist for the law on Veterinary and proposed amendments.

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ACC/8 – SPS Conformity Checklist for the law on phytosanitary and proposed amendments.

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Manual for computation of ACC/4-Aggregate Measurement of Support (AMS).

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Comments on ACC/4 and computation of Aggregate Measurement Support.

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Comments on proposed revisions to draft SPS laws.

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Comments on proposed replies to SPS/TBT questions raised by working party members.

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Draft model law on regulating the import and production of optical disks.

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Detailed proposal for establishing an inter-agency commission on IP enforcement.

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Comments/reviews of various draft IP-related laws, as requested by WTO Team Leader.

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Final ACC/9 for submission to the WTO Secretariat

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