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**CENTRAL ASIAN REPUBLICS OIL &
GAS SECTOR REFORM PROGRAM
DELIVERY ORDER NO.17**

UZBEKISTAN

Status Report

Prepared for:

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EXECUTIVE SUMMARY

After comparing the current legal and regulatory climate with an “ideal” for the RUZ, the following recommended changes are proposed for the oil and gas sector in order to enhance investment opportunities:

- ▶ Uzbekistan should prepare a long-term strategic plan for the development and use of its oil and gas resources, under the Presidential Energy Resource Program being developed by the Tashkent Energy Center.
- ▶ Uzbekistan should create an Oil and Gas Legislation Steering Committee of RUZ officials, oil and gas investors, and USAID advisors to analyze and redraft the current (fourth) version of the proposed oil and gas legislation.
- ▶ The RUZ should immediately create an independent Petroleum Authority, responsible for the promulgation and enforcement of rules and regulations.
- ▶ Uzbekistan should adopt a Program for Restructuring and Privatization of the Oil and Gas Sector. Within the Program, Uzbekneftegas should be rechartered as a National Oil and Gas Corporation to conduct exploitation of oil and gas reserves on behalf of the State. In addition, Uztransgas should be transformed as National Oil and Gas Corporation Uzbekneftegasprovod, responsible for all formally State-owned pipeline transmission operations. All other State activities should be divested.
- ▶ Uzbekistan should ensure that National Oil and Gas Corporation Uzbekneftegas has the exclusive right to negotiate and sign all oil & gas contracts and agreements. The PA should be required to approve any contract or agreement entered into by Uzbekneftegas, based on legal and regulatory requirements.
- ▶ Uzbekistan should create a legal and regulatory climate for oil and gas development which complements the Central Asian region.

Through a Memorandum of Understanding that is in the final stages of negotiation with the RUZ, USAID will provide legal and regulatory assistance to the oil and gas sector through projects which will provide relief for the recommended changes, such as drafting legislation and decrees, proposing implementing rules and regulations, creating an independent Petroleum Authority, developing a cost-of-service pipeline tariff methodology, restructuring and privatization of Uzbekneftegas, and other projects designed to enhance the climate for investment. In addition, training sessions are being developed for strategic resource planning,

international accounting standards, revenue re-investment, international petroleum economics, and project financing.

CHAPTER 1

CURRENT OIL AND GAS INVESTMENT ENVIRONMENT

Historically, the Republic of Uzbekistan (RUZ) has played a key political, economic, and military role in Central Asia. A stable and independent RUZ is considered vital to the United States' long-term interests in this area of the world. Recognizing their mutual interest in many areas of world economic and political activity, the Government of the United States and the Government of the RUZ have agreed to cooperate in "facilitating the provision of humanitarian, technical, and economic assistance." This formal agreement led to a charge to USAID to provide advisory services to the RUZ on "legal and regulatory issues related to the development of the oil and gas sector." The goal of this effort is to coordinate and provide technical assistance and training to the RUZ in the area of legislative and regulatory reform of the oil & gas sector in order to create a stable and competitive domestic energy industry capable of attracting foreign private investment..

Two factors stand out about the RUZ. First, the country enjoys a diversified economy that is not totally dependent on the oil & gas industry. Secondly, the Government is rather stable with the same key figures holding power today as they did six years ago. The result has been a pragmatic approach to economic change, and slower acceptance of reform in their oil & gas sector than in neighboring countries. President Islam A. Karimov and the RUZ Cabinet of Ministers have kept to their often iterated step-by-step approach in the legislative area of oil & gas reform, and have rebuffed the efforts of the World Bank and the International Monetary Fund to move more quickly in this area. Despite having expressed support for increased foreign investment, these political leaders continue tight centralized control of major economic sectors. Although movement toward legislative and regulatory reform is occurring in the oil and gas sector, it may progress rather deliberately at a pace more suitable to the RUZ than potential investors.

1.1 AUTHORITY STRUCTURE

Several ministries and committees in the Republic of Uzbekistan (RUZ) command a strong influence in the legal and regulatory environment of the oil and gas sector. These include the Ministry of Foreign Economic Relations; Ministry of Foreign Affairs; Ministry of Land, Reclamation and Water Economy; Ministry of Finance; and Ministry of Justice. Other powerful organs are State Committees such as: Geology and Mineral Resources; Protection of Natural Resources; Forestry; Science and Technology; Prognoses and Statistics; State Property Management and Entrepreneurial Support; and Labor Safety in Industry and Mining, which all carry out the decisions of the Cabinet of Ministers in their respective sectors and exercise administrative and economic control.

1.11 Cabinet of Ministers

RUZ President Islam A. Karimov is the Head of State and Executive Authority while simultaneously the Chairman of the Cabinet of Ministers. The RUZ describes itself as “a sovereign democratic republic with separation of powers between the legislative, executive and judicial authorities.” According to the Constitution of the RUZ, the Cabinet of Ministers is the Government of the Republic. The President exercises power over the Cabinet who implements his decisions. The Prime Minister, Deputy Prime Ministers, Ministers, Chairmen of State Committees, Heads of other bodies of economy and administration and the head of the Government of the Republic of Karakalpakstan are all *ex-officio* members of the Cabinet of Ministers.

The Cabinet of Ministers recently formed the Complex for Fuel and Energy as the main advisor to the President in the oil and gas sector. The Complex is composed of specialists and advisors that recommend the development of Presidential Decrees, Resolutions, and Acts which impact the sector and ensure they are implemented.

1.12 Presidential Apparat

The Presidential Apparat apparently has influence in the RUZ authority structure, although it does not wield direct power on its own. It is made up of hand-picked advisors to the President. Attached to the Apparat are the Academy for Formation and Development and the Center for Macroeconomic Studies and Investigations. These institutions are known to influence Presidential decision-making in the oil and gas sector.

1.13 Presidential Soviet

The Presidential Soviet advises the President and maintains a great influence on the affairs of the State. The Soviet members are directors of other governmental agencies and each sector of the economy is represented. Their advice can and often does result in the adoption of Presidential Decrees and Proclamations.

1.14 Oliy Majlis

Within the Oliy Majlis (Parliament), the Committee for Energy, Communications and Transport is primarily responsible for oil and gas legislation. Legislation is initially directed to the Committee for analysis and comment before actually being presented to the Parliament for a first reading. While this Committee has the ability to criticize and theoretically “reject” recommended legislation, its real task is to assure that the draft legislation complies with the existing legal framework. This Committee, along with the Ministry of Justice, has the right (though not necessarily the obligation) to hold public hearings on any proposed legislation. The

Committee is well-versed in legislation that might affect the use of natural resources, environmental concerns, and tax issues. However, it is unclear how much exposure the Committee has in the passage of legislation involving oil and gas. Operational concerns to be addressed by legislation are generally not discussed with the international oil and gas community directly, although the Committee is known to consult with specialist and advisors in the sector.

1.15 Khokimiyat

A complicating factor in the authority structure of the RUZ is the presence of the regional, district, and city Khokims, who serve as heads of both representative and executive authorities of their respective territories. The Khokims of the regions are appointed and dismissed by the President and are his official representatives. The Khokims “make decisions within their vested powers which are binding on all enterprises, institutions, organizations, associations, officials and citizens in their relevant territory.”

The Khokimiyat’s influence in the oil and gas sector, when it exists, usually impacts investment and operational efficiency in a negative way. The Khokimiyat have brought forward legitimate questions of regional environmental concern, but in some cases have been more interested in extracting a benefit from a company’s presence through financial burdens on operations or disavowal of rights granted by license or legislation.

1.16 Uzbekneftegas

Uzbekneftegas defines itself as “a business association of voluntary members including government, quasi-government groups, leasehold, collective and joint venture companies, enterprises and organizations, as well as legal entities of other states which have a stake in the development of the sector.” Uzbekneftegas employs nearly 90,000 people and might be referred to as a conglomerate holding company with widely diverse assets. In addition to oil and gas interests, it owns and operates activities in farm land and associated livestock, railroads, food and supply services, industrial and housing construction, etc. As of January 1, 1997 the Corporation was restructured into 14 State Joint Stock (JS) Associations and State Enterprises as follows:

- ▶ State JS Association Uzneftegasdobicha: exploration and exploitation, drilling, new field development, production of oil and gas, and gas processing.
- ▶ State JS Association Uzneftegastroj: construction and development of petroleum, transport, and processing facilities; and industrial and housing construction.
- ▶ State JS Association Uztransgas: transportation and sale of gas to major industrial users in the RUZ, export of gas, and construction of gas transmission pipelines.

- ▶ State JS Association Uzgosnefteproduct: purchasing and marketing of petroleum products, construction of oil and oil products storage facilities and gasoline stations.
- ▶ State Geological Enterprise Uzbekneftegasgeology: exploration and deep well drilling.
- ▶ State Geophysical Enterprise Uzbekgeophysics: identification of oil and gas reservoirs, recommendations for geophysical surveys and exploration drilling of oil and gas wells.
- ▶ State Production JS Association Uzneftepererabotka: processing of oil and gas condensate, lubricant oils, coke, LPG, and construction of oil processing facilities.
- ▶ State Scientific-Production JS Association Neftegasnauka: exploration and production research and new technological designs and devices.
- ▶ State Trading Production JS Association Neftegasnabzheniye: oil and gas trading services, production of commodities and food for employees, and supply of food products to employee catering facilities from ancillary farming units.
- ▶ State Foreign Economic Relations JS Association Uzvneshneftegas: foreign economic relations to attract overseas investment; technology and experience in exploration, exploitation, and development of oil and gas fields; transportation and processing of oil and gas; administration of export and import transactions; and coordination of RUZ energy-related products and services in the international marketplace. It is also charged with establishing joint ventures and provision of various other related services.
- ▶ State Production And Technological Communication Management Uzneftegasvyaz: provides reliable methods of communication for all associations and enterprises of Uzbekneftegas.
- ▶ State JS Association Uzbekneftegaskomplekt: procurement and supply of manufacturing equipment, tools, instruments, chemical agents and materials of production, and technical design to the various enterprises of the corporation.
- ▶ State Control And Inspection Uzneftegasinspektsiya: executes control and rational use of petroleum products and gas and their storage. Maintains the construction quality, safety and security of gas exploitation.

Although any one of the 13 associations or enterprises is relatively independent in decisions concerning its own organization, within its own structure is a commission which has final decision-making authority. This commission may be made up of heads of other enterprises (within Uzbekneftegas itself) or persons with a policy-making position within the enterprise.

Contract proposals are initiated within the enterprise and passed on to its commission for economic review and political appropriateness.

1.17 Agencies and Institutions with Monitoring/Regulatory Functions

Many of the national committees have a regulatory role that affects the oil and gas industry including: State Committee for Nature Protection, State Committee for Supervision of Labor Safety in Industry and Mining, State Committee of Science and Technology, State Committee for Geology and Mineral Resources, and the Ministry of Land Reclamation and Water Economy. Of these, environmental awareness is increasingly taking a more active and public role as monitored and enforced by the State Committee for Nature Protection.

Potential investors in the oil and gas sector are concerned that no independent regulatory authority exists to enforce rules and regulations of upstream oil and gas operations. While there is not an official organ similar to an independent state regulatory commission, the functions of inspection, monitoring, auditing, and inquiry are performed in certain areas. Within Uzbekneftegas itself, Uzneftegasinspeksiya has this responsibility and has the authority to shut down a particular operation for a variety of reasons: poor oil field practice, uneconomic performance, personnel safety, and other typical causes for regulatory interference. Most important of these regulatory roles is that played by the Ministry of Finance in domestic operations and that of the Ministry of Foreign Economic Relations in operations involving foreign participation. The Ministry of Finance stringently monitors all oil and gas operations involving state participation and funding. Both ministries were closely involved in the recently completed 500 million USD Mubarek refinery (located in Bukhara) upgrade, whereby the state provided 60 percent of the financing and the remaining 40 percent was from foreign banking conglomerates (including the Governments of France and Japan).

An independent regulatory agency for the oil and gas sector is not currently being considered in Uzbekistan. Present discussion and current drafts of new legislation envision a new bureaucracy within the Cabinet of Ministers, called the Petroleum Authority, to perform certain administrative functions as prescribed by law, with approval and authority to promulgate rules and regulations reserved to the Cabinet of Ministers. According to the most current drafts, Uzbekneftegas is authorized to "assist" the Petroleum Authority in carrying out its functions.

1.2 FISCAL TERMS

There appears to be no standardized fiscal terms for the upstream oil and gas sector. In fact, when fiscal terms are informally discussed with RUZ officials the usual response will be to promote financial incentives instead. In the absence of an RUZ oil and gas law, all projects are governed and protected by existing laws on foreign investment. The basic law "On Foreign Investment and Guarantees for Foreign Investment Activities" adopted on May 5, 1994 has been amended several times with added enhancements for foreign investment. Resolution No. 76 of

the Cabinet of Ministers "On the Order of Creation and Activity of Enterprises with a Share of Foreign Investment..." adopted on March 2, 1995 also favorably addresses most foreign investor concerns such as: property ownership, dispute resolution, import/custom fees and exemptions, profit transfer, and intellectual property/patent rights. However, a 1997 Resolution of the Cabinet of Ministers restricting currency conversion has resulted in companies being forced to negotiate case-by-case exemptions for themselves with the resulting insecurity and cumbersome Government intervention.

The new tax code, which takes effect January 1, 1998, places the revenue tax rate for legal entities at 35 percent of gross revenue less deductible expenses. It permits depreciation at 15 percent of the cost of geological research and preparatory work done for extraction of minerals. It affirms a tax holiday of seven years for enterprises with more than 30 percent foreign investment which invest capital in projects included in the "Investment Program of Uzbekistan". Enterprises with more than 50 percent foreign investment are entitled to further privileges and the Cabinet of Ministers can add privileges to these, dependent on the Government's need for the project in question.

Draft oil and gas legislation was initiated by a World Bank funded project in 1994. In April, 1997 a fourth draft was selectively released for comment. In Section 8, license fees, royalties, rental payments, etc. are all enumerated in considerable detail as are the various penalties for license or contractual violations. However, some fiscal issues are not well defined. Section 21.3.3., for example, indicates that the Cabinet of Ministers acting on behalf or via the "Petroleum Authority" will examine each individual situation and make a decision based on numerous factors. The fees, payments, and penalties outlined in the draft law are generally within international norms.

Probably more important to foreign investors is Section 29 in which the Government of the RUZ guarantees the stability of the applicable terms for the life of the contract. "The Cabinet of Ministers guarantees the fiscal stability of any license for petroleum agreement granted or entered into; and where the licensee is obliged at any time under any law to pay any amounts to any level of government, other than the payments under this Law and the Petroleum Regulations and other than reasonable payments for governmental services, the Petroleum Authority shall adjust the fiscal terms of the license or petroleum agreement, at the request of the licensee or contractor, in such a manner that the overall fiscal burden applicable at the date of the granting of the license or making of the petroleum agreement is maintained."

1.3 FOREIGN INVESTMENT AND DONOR ACTIVITIES

In general, the volume of foreign investment is reported to have grown by 23 percent in the past year. The Central Bank has reported that foreign capital accounted for 18.8 percent in 1996, up from 6.6 percent in 1994 and 13.7 percent in 1995 of total investment. As of January 1997 approximately 3,000 joint ventures between the RUZ and foreign companies have been created.

Uzbekistan's main concern continues to be that of national self-sufficiency, so investment promotion in the oil and gas sector emphasizes the Government's push to not only erase dependence on fuel product import, but to become a petroleum product exporter of significance.

Donor agencies are providing at least partial assistance in the rehabilitation of the Ferghana and Alti-Arik oil refineries. In addition, discussions of up to 200 million USD investment by Enron/OPIC in the Gadzhak fields of the Surkhandarya Region has been ongoing.

1.4 OTHER KEY ISSUES

One of the problems the RUZ has in attracting investors for oil and gas projects is that the RUZ often demonstrates their real agenda of solving a societal or strategic infrastructure need rather than offering attractive commercial returns. In addition, the RUZ emphasizes redevelopment and further exploration of old and exhausted fields, such as those in the Bukhara Region, whereas serious investors are more interested in exclusive exploration licenses in areas of their own choice. Many of these developed areas have suffered considerable environmental damage and the specter of huge potential cleanup costs also holds back investor interest.

With its geographic position in Central Asia, Uzbekistan must depend on good relations with its neighboring countries in order to guarantee transport and delivery of oil and gas and related products. Overland truck traffic is hampered by outdated equipment and poor roads and can be subject to unavoidable hazards and risks. Increased oil and gas production will require huge infrastructure costs in pipelines and equipment. No matter what direction Uzbekistan chooses to transport, it is far distant from a reliable market with customers willing and able to pay for product received. The RUZ is competing for investor capital with mineral-rich neighbors with whom it may or may not share common economic goals. Unfortunately, unreliable markets for oil and gas are a serious deterrent for investors.

CHAPTER 2

IDEAL FRAMEWORK FOR ENHANCING OIL & GAS INVESTMENT

The current RUZ legal and regulatory framework for the oil and gas sector should be considered in relation to an ideal framework, in order to identify problem issues and the proposed course of action by the Government to resolve those issues. An ideal framework is proposed, taking into account the current legal, political, economic, and social situation.

2.1 OIL AND GAS POLICIES

Oil and gas policies are broad and general guidelines, the capstone for setting overall government objectives such as developing strategies for exploitation of oil and gas resources, priorities for oil and gas investments, allocation of state resources, and attraction of foreign investment. Such policies should be set at the highest level of government.

In the RUZ, the highest policy making body for the oil and gas sector is the Cabinet of Ministers. Uzbekneftegas is responsible for implementing the policies, along with other organs of Government in specialized areas. Uzbekistan has not shown the same openness to western approaches in the oil and gas sector as it has in some others, such as the agricultural sector. President Karimov is however, increasingly turning public attention to the oil and gas sector as a source of revenue, capital investment, and technology needed to bring the RUZ to the level of self-sufficiency, always at the forefront of RUZ political interest.

The RUZ should consider adopting policies for the oil and gas sector which will serve to minimize State investment and maximize production potential, private investment, and efficiency in performance and operations, while simultaneously emphasizing market growth and reliable transportation systems. These policies should be clearly stated and mobilized through the passage of legislation, rules and regulations, restructuring and privatization of selected associations and enterprises of Uzbekneftegas, and the creation of an independent Petroleum Authority (PA). The RUZ should also develop policies that enhance their competitiveness in the sale of natural gas to regional neighbors.

2.2 OIL AND GAS LEGISLATION

The first priority should be the passage of appropriate oil and gas legislation, prescribing the framework of the Government's authority in the sector. Such legislation should be concise and operative in a form that is (1) acceptable to the Cabinet of Ministers and the Oliy Majlis, who will enact it, and the Government, who will implement it, and (2) adopts international oil and gas practices and standards.

The RUZ should ensure that its oil and gas legislation clearly denotes authority and responsibilities to the proper Government organs. It should be comprehensive in nature, but not too detailed, so that flexibility and a focus on policy goals can be realized. The legislation should create an independent PA, provide a favorable environment for investment, serve as the foundation for restructuring and privatization of selected associations and enterprises of Uzbekneftegas, and ensure that model contracts and agreements conform to international standards.

2.3 OIL AND GAS RULES AND REGULATIONS

Oil and gas rules and regulations are adopted and enforced by the independent PA and cover the mechanics for the management of operations in the oil and gas sector. Rules and regulations are specific, but are flexible and transparent, taking an objective and result-oriented approach rather than a prescriptive mechanism. The PA should be empowered with a transparent methodology to adjust to changing circumstances and reissue rules and regulations without undue political or industry influence.

The PA would function as an autonomous, non-political, quasi-judicial, and technical body of Government. The concept of an independent PA is important, since it provides consistency and stability to decisions and allows investors (and potential investors) reasonable assurances that their investments are insulated and will not be damaged by purely political reasons. The PA would function as the “one-stop” agency which would represent the RUZ on all oil and gas regulatory issues in an impartial and transparent manner. The PA would be responsible for: conservation and management of natural resources; maintenance of oil and gas upstream and field operations data and information; issuance of permits and licenses and collection of their corresponding fees; and approval of oil and gas contracts between the RUZ and investors through the promulgation and enforcement of rules and regulations, prescribed under the framework of laws and legislation enacted by the Government.

2.4 NATIONAL OIL AND GAS CORPORATIONS: UZBEKNEFTEGAS AND UZBEKNEFTEGASPROVOD

Uzbekneftegas’ role should be to carry out exploitation of oil and gas resources on behalf of the State as the National Oil and Gas Corporation. In general, the model for National Oil Companies (NOCs), such as envisioned for Uzbekneftegas, has evolved from the need to control, protect, and develop indigenous capability to exploit an important national resource. In many countries, NOCs are assigned exclusive authority to exploit oil and gas reserves. They operate oil and gas fields on their own behalf as any oil company would. Where NOCs lack the necessary technology and risk capital, they have been authorized to enter into and manage contracts (production sharing) with foreign oil companies. Both Indonesia, which pioneered this concept, and Malaysia have used this arrangement for over 25 years to successfully attract significant foreign investment in their oil and gas sector. As a result, the NOCs in these countries have

developed into sophisticated and technically competent oil companies which are venturing out into the international arena.

Uzbekneftegas should be restructured and reformulated with the tasks of the model NOC, as described above. It should retain Uzneftegasdobicha, Uzbekneftegasgeology, Uzbekgeophysics, and Uzneshneftegas departments, to ensure expertise in exploration, drilling, and production operations and to attract foreign investment. In addition, Uztransgas should be transformed into National Oil and Gas Corporation Uzbekneftegasprovod, responsible for the construction and operation of the oil and gas transmission system within the RUZ. Uzbekneftegasprovod could eventually be restructured and privatized, as investors become interested in transmission ownership and operations. Uzneftegasinspeksiya should be dismantled and transformed to an inspection arm of the PA.

The RUZ and Uzbekneftegas should immediately consider privatizing Uzneftegastroy, Uzgosnefteproduct, Uzneftepererabotka, Neftegasnauka, Neftegasnabzheniye, Uzneftegascvyaz, and Uzbekneftegaskomplekt. These associations and enterprises are service providers and/or feature downstream activities that do not add value and are not central to the core functions of Uzbekneftegas, Uzbekneftegasprovod, and the strong RUZ interest in self-sufficiency.

2.5 OIL AND GAS CONTRACTS AND AGREEMENTS

Oil and gas contracts and agreements with investors may be based upon internationally accepted models and negotiated and signed by National Oil and Gas Corporation Uzbekneftegas. However, the contracts and agreements should be approved by the independent PA to ensure that they meet all legal and regulatory requirements and that they are based upon international practices and standards. Concessions, joint ventures, and production sharing agreements should serve as vehicles for investors and the RUZ to commence and fulfill requirements for oil and gas operations.

2.6 USAID'S TECHNICAL ASSISTANCE AND TRAINING PROJECT

To assist the RUZ in legal and regulatory reform in the oil and gas sector, the United States Agency for International Development (USAID) has proposed signing a Memorandum of Understanding (MOU). Annex 1 of the MOU describes a list of projects and training programs that USAID would undertake over the next year. These activities include drafting potential implementing rules and regulations, legislation and decrees, and evaluating and revising draft and already adopted legislation and regulations. In addition, through its contract with Hagler Bailly, USAID will provide experts in appropriate fields to complete specific studies or projects in the oil and gas sector. Other projects include assistance in the creation and development of a cost-of-service based pipeline tariff methodology, restructuring and privatization of the National Oil and Gas Corporation Uzbekneftegas, and initiating an independent PA.

Further, USAID will provide in-country training by internationally recognized experts, both from industry and institutions of higher learning. Training will concentrate on legal, regulatory, and economic issues in the oil and gas sector as it relates to the RUZ specifically and to world markets. Training will be provided to a broad range of Uzbekistan specialists, with participation solicited from ministries, agencies, committees, commissions, associations, enterprises, universities and private entities as appropriate. USAID's technical assistance and training would be coordinated by a resident advisor living in Tashkent.

All of the individual activities in the MOU promote legal and regulatory institutional reform in the oil and gas sector, develop indigenous capabilities, and improve the ability of the RUZ to attract and manage foreign investment opportunities.

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CHAPTER 3

RECOMMENDED CHANGES IN STRUCTURE OF OIL AND GAS SECTOR

Proposed are recommended changes for the oil and gas sector of Uzbekistan, based upon the current status of laws, rules and regulations, process, structure, and institutions and ideal framework for enhancing oil and gas investment, as presented. It should be noted that these recommendations are expressed solely on the study of Uzbekistan laws and regulations, published information, and informal discussions with RUZ officials. It is clear that changes are needed to rationalize the organization of the oil and gas sector and to provide better opportunities for investment. The recommendations describe how USAID's specific technical assistance and training activities included in the MOU will help support the proposed changes.

3.1 OIL AND GAS POLICIES

- ▶ *Uzbekistan should prepare a long-term strategic plan for the development and use of its oil and gas resources, under the Presidential Energy Resource Program being developed by the Tashkent Energy Center.*

USAID has been invited to participate in developing drafts of the long-term strategic plan for oil and gas as a component of the Presidential Energy Resource Program. The plan should encourage policies which minimizes State investment and maximizes production potential, private investment, and efficiency in performance and operations, and emphasizes markets and transportation systems. It should identify regional gas markets and favorably consider competing for those markets. Through the implementation of the MOU, USAID anticipates appointing resources to undertake this project.

3.2 OIL AND GAS LEGISLATION

- ▶ *Uzbekistan should create an Oil and Gas Legislation Steering Committee of RUZ officials, oil and gas investors, and USAID advisors to analyze and redraft the current (fourth) version of the proposed oil and gas legislation.*

The Steering Committee should ensure that the redrafted version contains all of the elements which were discussed in Chapter 2 (create an independent PA, provide an environment for investment, serve as the foundation for restructuring and privatization of selected associations and enterprises of Uzbekneftegas, and ensure that model contracts and agreements conform to international standards). Once the redrafted version is passed out of the Committee, it should be monitored and promoted throughout the legislative process until formally adopted by influential Committee members. In the foreseeable future, the Steering Committee should consider addressing all forms of proposed legislation that may impact the oil and gas sector. USAID advisors from Hagler Bailly should serve as consultants to the RUZ during this process, and as Committee members take the lead in the development of redrafts of proposed legislation.

3.3 OIL AND GAS RULES AND REGULATIONS

- ▶ *The RUZ should immediately create an independent PA, responsible for the promulgation and enforcement of rules and regulations.*

In the draft MOU, USAID has offered assistance in the creation and development of the PA and anticipates doing so. In addition, USAID advisors from Hagler Bailly propose that a Working Committee be established to draft implementing rules and regulations, as described in Chapter 2.

I. National Oil and Gas Corporations: Uzbekneftegas and Uzbekneftegasprovod

- ▶ *Uzbekistan should adopt a Program for Restructuring and Privatization of the Oil and Gas Sector. Within the Program, Uzbekneftegas should be rechartered as a National Oil and Gas Corporation to conduct exploitation of oil and gas reserves on behalf of the State. In addition, Uztransgas should be transformed as National Oil and Gas Corporation Uzbekneftegasprovod, responsible for all formally State-owned pipeline transmission operations. All other State activities should be divested.*

USAID has proposed in its MOU to assist the RUZ in the development and implementation of a Program for Restructuring and Privatization of the Oil and Gas Sector. This Program should address a number of elements, including but not limited to: strategy and process; goals and objectives; valuation of assets; reduction of debt; cost of asset refurbishment; risk/return assessments; share holding structure; level of Governmental intervention; reduction of subsidies and social costs; financial and economic impact issues; etc.

The RUZ should review the role of National Oil & Gas Corporations in other developing countries, and restructure Uzbekneftegas accordingly. The reformulated corporation should be charged with the exploitation of oil & gas reserves through its own efforts, and also be empowered to negotiate contracts and agreements with the international oil and gas community. Uzbekneftegas should retain in-house exploration, drilling, production, and foreign relations operating units as newly constituted departments. The RUZ and Uzbekneftegas should undertake a program of divestment and privatization of its other associations and enterprises, which are service providers or are not central to its core function. Uzbekneftegas should be required to comply with all rules, regulations, and procedures established by the independent PA.

Uzbekneftegasprovod should be made into a National Oil and Gas Corporation, responsible for the operation of all formally State-owned oil & gas transmission pipelines, including those operated by Uztransgas. Uzbekneftegazprovod should eventually be considered as a candidate for restructuring and privatization as investors become interested in ownership of transmission assets.

II. Oil and Gas Contracts and Agreements

- ▶ *Uzbekistan should ensure that National Oil and Gas Corporation Uzbekneftegas has the exclusive right to negotiate and sign all oil & gas contracts and agreements. The PA should be required to approve any contract or agreement entered into by Uzbekneftegas, based on legal and regulatory requirements.*

Legislation should be adopted which assigns the National Oil and Gas Corporation Uzbekneftegas the exclusive right to negotiate and sign contracts with investors, relying upon international model agreements for concessions, joint ventures, production sharing agreements, etc. Such model contracts and agreements should meet requirements of flexibility according to specific conditions, provide for generic terms and provisions regarded as standard international practice, and objectively balance concerns of investors with that of the State. These contracts and agreements should be in full compliance with all rules, regulations, and procedures established by the independent PA, which has the right of approval.

III. Regional Cooperation Within the Central Asian Republics

- ▶ *Uzbekistan should create a legal and regulatory climate for oil and gas development which complements the Central Asian region.*

In order to be competitive in the attraction of investment opportunities in its oil and gas sector, the RUZ must develop a legal and regulatory framework which is consistent and complementary to the Central Asian region. In this context, USAID has already begun assistance with other republics in Central Asia and should encourage the RUZ to adopt similar policies and programs which will serve to attract investment.