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SOCAR and the Regulation of the Energy Sector

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Introduction



State Oil Company of the Azerbaijan Republic (SOCAR)

- ❖ Established in 1992 by Presidential Decree No. 200
- ❖ Original purposes:
 - ❖ implementation of a unified state policy for the use of oil and gas reserves
 - ❖ improvement of the management structure of the oil and gas industry
 - ❖ ensuring the development of the fuel and energy complex
 - ❖ increasing efficiency in the use of the production capacity of oil extraction and oil processing enterprises

Introduction



State Oil Company of the Azerbaijan Republic (SOCAR)

- ❖ **Structure:** production firms, enterprises, scientific research, design, foreign trade and other organizations, bank, insurance company, fuel exchange, various other units and divisions and social assets
- ❖ **At one time:**
 - ❖ **171 business units**
 - ❖ **16 departments**
 - ❖ **80,000 employees**

Regulatory Functions



❖ **State Regulatory Functions:**

- ❖ approving development programs and the plans of oil and gas processing plants
- ❖ representation vis-à-vis state authorities of the interests of enterprises and organizations within its structure
- ❖ State representative to implement the policy of Azerbaijan in attracting investment for the development of the oil and gas industry, infrastructure and the export of hydrocarbons
- ❖ Serving as the *de facto* governing authority for state oil and gas enterprises and activities

Restructuring Efforts



❖ **Initial Measures:**

- ❖ New Charter of April 1994
- ❖ Presidential Instruction No. 651 of 2001, “On the Privatization of Enterprises Forming Part of the Fuel and Energy Complex”
- ❖ Presidential Decree No. 844, dated January 24, 2003, “On the Restructuring of the State Oil Company of the Azerbaijan Republic” (as amended by Presidential Decrees No. 127 , 198 and 340, dated September 18, 2004, February 23, 2005 and December 22, 2005)

SOCAR Restructuring



❖ 2003 Presidential Decree

- ❖ Approved a new SOCAR Charter
- ❖ Merged the Offshore and Onshore Oil and Gas Production Associations into Azneft and Foreign Economic Relations Dept. and Azerbaijan Oil Supply Unit into MEOD
- ❖ Established a new Pipeline Division and reorganized the Shelf Project Constructions Unit into the Deep Water Jackets Plant
- ❖ Reorganized the Azerneftyanajag Refinery
- ❖ Opened certain offshore construction units for privatization
- ❖ December 2005 Decree added a Division for Social Development and a Security Division

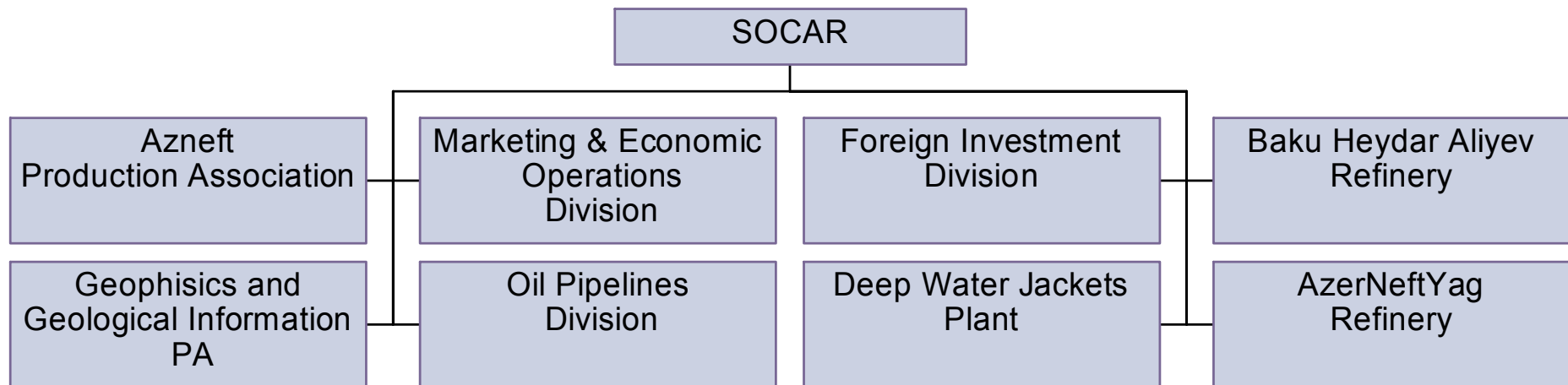
SOCAR Restructuring



❖ **2003 Presidential Decree**

- ❖ Greatly streamlined the organizational structure and management of SOCAR
- ❖ Established a SOCAR holding company structure, operating through eight divisions organized as independent enterprises managed by separate directors
- ❖ Enabled more efficient and effective on the ground management of the key business units of SOCAR
- ❖ Fostered the financial restructuring of SOCAR

Structure of SOCAR 2003



SOCAR Restructuring



❖ Commercialization and Restructuring Program:

- ❖ The Government and SOCAR, with the assistance of the World Bank and the EBRD, sought to fine-tune and deepen the restructuring pursuant to the 2003 Presidential Decree
- ❖ In 2004 under a USTDA grant, administered by the EBRD, SOCAR retained a Consortium consisting of **SHH International, Taylor-Dejongh, PFC Energy** and **ICF Consulting** to study the company and advise on its commercialization and restructuring
- ❖ SOCAR appointed a Commercialization and Restructuring Task Force to facilitate the implementation of the restructuring, coordinate with the Consultants and consider recommendations prepared by the Consultants

USTDA/EBRD SOCAR Commercialization and Restructuring Project (2004-2006)



❖ Objectives:

- ❖ Establish clear vision of the Company according to best international oil industry practices
- ❖ Identify potential options for achieving this vision
- ❖ Create a roadmap, with milestones and monitoring indicators, for implementation
- ❖ Identify key issues that will arise in the implementation of the plan, minimizing social impact

USTDA/EBRD SOCAR Commercialization and Restructuring Project (2004-2006)



❖ **During a 12-month period the Consultants Team completed:**

- ❖ An initial diagnostic of the company and each of its business groups, trading, associated businesses and activities
- ❖ An assessment of the strengths and weaknesses we identified, together with a comparative study of similarly situated State Oil Companies
- ❖ Preliminary recommendations to further streamline SOCAR's organizational structure, legal form and governance structure
- ❖ An assessment of performance improvement options
- ❖ The Consultants commend SOCAR management for openness, seriousness in addressing restructuring

International Accounting Standards



- ❖ The Law on Accounting, dated June 29, 2004, contemplates the adoption of IFRS within all legal entities and commercial organizations “having public significance” by January 1, 2008
- ❖ The list of specific entities designated as having public significance and required to keep their accounting and submit financial statements in accordance with IFRS was adopted by the Cabinet of Ministers in July 2005
- ❖ SOCAR and 5 of its enterprises were designated as organizations “having public significance”

Transfer of Regulatory Functions

- ❖ Presidential Decree No. 458, dated April 18, 2001, established the Ministry of Fuel and Energy
- ❖ The Ministry was placed in charge of: forming and implementing state policy in the fuel and energy sector, exercising control over the efficient use of energy resources and ensuring the protection of the interests of the state in this sphere
- ❖ Presidential Decree No. 150 of December 6, 2004, announced a reorganization of state regulatory authority in the energy sector and the transfer of functions to a newly-established Ministry of Industry and Energy
- ❖ On May 16, 2006 a new Internal Regulation of the Ministry of Industry and Energy was adopted

Regulation of the Ministry of Industry and Energy of the Azerbaijan Republic (2006)



- ❖ **General:** To carry out state policy and regulation of the industrial and fuel-energy complex and legal entities and individual entrepreneurs carrying out their activity in connection with the relevant fields
- ❖ **Functions include:**
 - ❖ **Issuing of special permissions (licenses) for relevant activities provided under the legislation**
 - ❖ **Representing state interests within relevant state enterprises and enterprises controlled by the state and monitoring of their activity**
 - ❖ **Preparing drafts of PSAs and other agreements in the hydrocarbon sector, conducting negotiations over these agreements, signature of subsoil agreements and monitoring performance under signed agreements**

Future



- ❖ SOCAR is still very much involved in the negotiation process
- ❖ The ultimate roles to be played by SOCAR and the Ministry of Industry and Energy in subsoil regulation are still evolving
- ❖ Whatever the ultimate result, SOCAR has made great progress and is on the right track in pursuing its restructuring
- ❖ As a result, SOCAR has become a more efficient, more effective, more responsive partner for the international oil company representatives present at this conference

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