



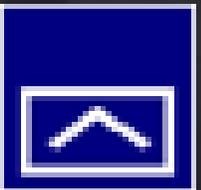
IPLOCA Regional Meeting

Four Seasons Hotel, Baku

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Legal Aspects of Oil & Gas Sector Regulation in Azerbaijan

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OF AZERBAIJAN**

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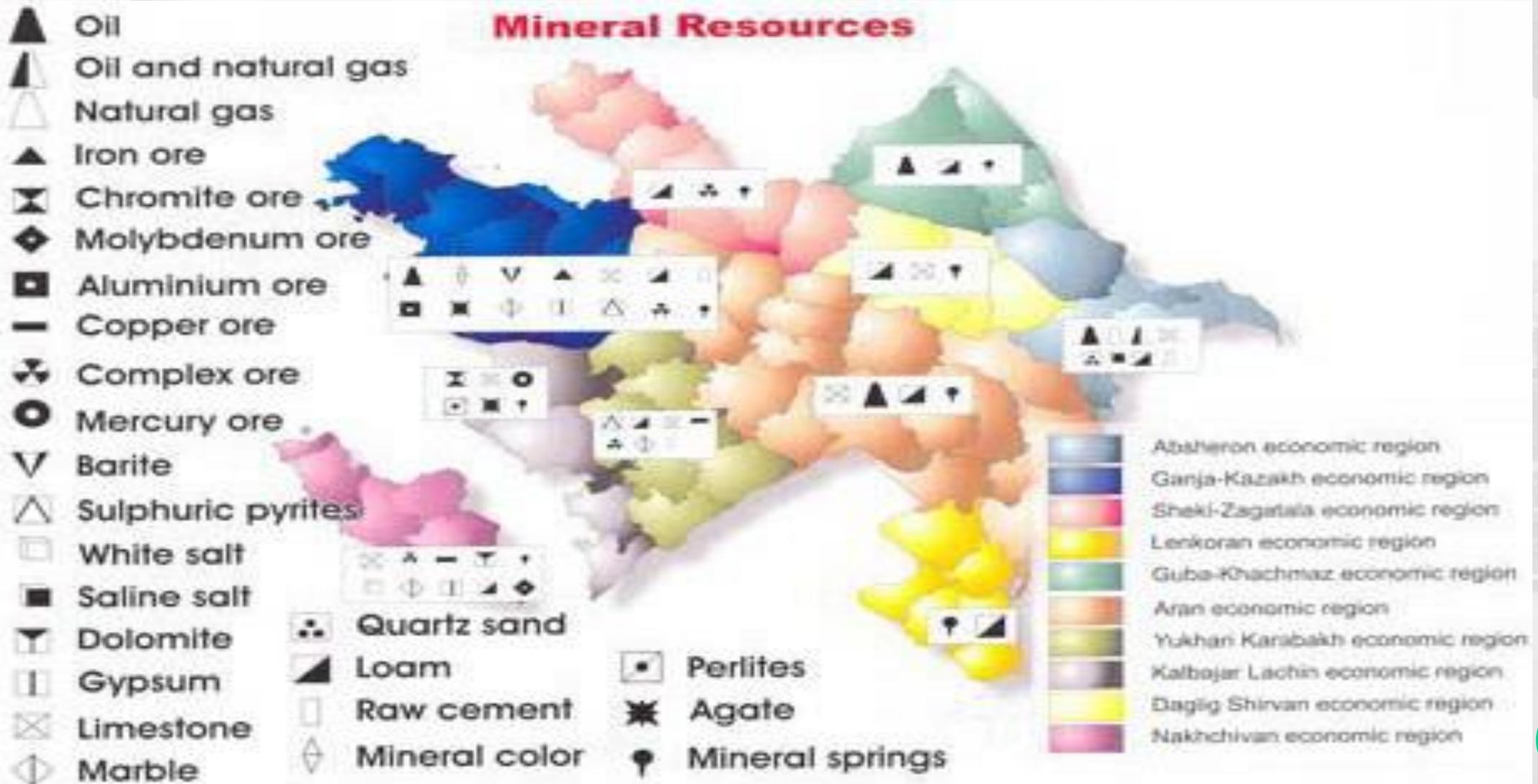
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NATURAL RESOURCES OF AZERBAIJAN



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ENERGY RESOURCES OF AZERBAIJAN: OIL

- Oil & gas are the main national wealth of the country. Main oil&gas fields are located in Apsheron Peninsula and the Caspian Shelf;
- Azerbaijan is one of the world's oldest oil-producing countries. The country's oil industry experienced a boom at the end of the 19th and the beginning of the 20th century. During World War II, the Soviet Republic of Azerbaijan produced approximately 500,000 barrels per day;
- The years of independence marked a new era of oil exploration and production. Azerbaijan holds 7,000,000,000 barrels of proven oil reserves as of 2021, ranking 20th in the world and accounting for about 0.5% of the world's total oil reserves;

Oil & gas industry still is the leading sector of the country's economy. (The most important event of the previous decade is the first "Production Sharing Agreement" ("PSA")-"Contract of the Century" on joint exploration of Azeri, Chirag, Guneshli fields (ACG), located in the Azerbaijani sector of the Caspian Sea was signed between SOCAR and 11 foreign oil companies.

At present there are more than 30 PSAs on "offshore" and "onshore" oil fields.

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ENERGY RESOURCES OF AZERBAIJAN: NATURAL GAS

Reserves of natural gas of Azerbaijan increased from 4.4 trillion cubic feet in 2002 to 60 trillion cubic feet in 2021 growing at an average annual rate of 34.81%. However, there is still insufficient infrastructure to move associated gas from many of the Caspian offshore oil fields and therefore, some of it is being flared;

Here are the major Natural gas fields in Azerbaijan: “Shah Deniz” – largest gas field in the Caspian Sea; “Absheron”; “Ashrafi”; “Dan Ulduzu”; “Karabakh”; “Umid”; “Nakhchivan” and “Shafag-Asiman” gas fields;

Currently Azerbaijan's gas exports to Europe amount to 10 billion cubic meters a year, compared to the 185 billion cubic meters Russia supplied to Europe in 2021. Azerbaijan has plans to expand those exports up to 20 billion cubic meters per year.

President of Azerbaijan Mr. Ilham Aliyev in his recent interview stated that about 19 billion cubic meters of Azerbaijani gas will be exported in 2022. Of this volume, more than 8 billion cubic meters will be exported to Turkey and more than 7 billion cubic meters to Italy. The remaining gas will be divided between Georgia, Bulgaria, and Greece.

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THE MAP OF AZERBAIJANI OIL AND GAS FIELDS



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OIL AND GAS PIPELINES

The total length of the main pipeline in within the Republic of Azerbaijan is 4,600 kilometres (2,900 mi), where the centre of the country's oil industry and nexus of its pipelines are at Baku.

Historically, the first oil pipeline was formed in Absheron district in connection with oil production in the country.

The first pipelines were constructed in the 19th century to transport crude oil from the oil fields to the refineries. The first pipeline was constructed in 1878 by Baku Oil Refinery, connecting to Balakhani Mines. Then the 800-kilometre-long (500 mi) Baku–Batumi oil pipeline was put into operation in the beginning of the 20th century.

Oil and gas field exploitation in Absheron and the Caspian Sea required the construction of new pipelines to Baku. Here are the main oil pipelines built to bring the produced oil to Baku, such as: Alibayramly–Baku, Neftdashlari–Baku, and Siyazan–Baku. Natural gas is transported through Garadagh–Agstafa, Garadagh–Baku, Siyazan–Baku, Neftdashlari–Baku, and Zira–Baku pipelines.

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Oil and gas Pipelines:

The main route options for oil and gas export pipelines from Azerbaijan to Europe are:



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Oil and gas Pipelines:

“Baku–Grozny–Tikhoretsk–Novorossiysk” oil pipeline (with maximum transportation capacity of 5 million tons per year):

The agreement for the northern route was signed on February 18, 1996, in Moscow. This pipeline transports Azerbaijani oil into the Russian Federation to the Black Sea port of Novorossiysk. The total length of the Baku–Grozny–Tikhoretsk–Novorossiysk (BGTN) oil pipeline is 1,347 km (837 mi), including 231 km (144 mi) in Azerbaijan.

The transportation of Azerbaijani oil through the northern route started on October 25, 1997. A trilateral agreement signed among AIOC (Azerbaijan International Operating Company), SOCAR and Transneft (the Russian state-owned pipeline company) includes all legal and technical issues of transportation of oil to Novorossiysk.

It was intended to transport 2.5 thousand tons of crude oil per day through Dubandi–Boyukshor–Siyazan–Shirvanovka pipeline.

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Oil and gas Pipelines:

Baku–Tbilisi–Supsa oil pipeline:

“Baku–Tbilisi–Supsa” is the western route, made through an agreement between the Presidents of Azerbaijan and Georgia on March 8, 1996.

It has a total length of 920 km (570 mi) with 480 km (300 mi) in Azerbaijan.

It transports primary Azeri oil from Azeri–Chirag–Gunashli fields through Baku. Trilateral contracts were signed among AIOC, SOCAR and the Georgian government.

This line was put into operation on April 17, 1999, and exports appr. 15 million tons of oil per year to mainly Western countries.

It has lower operating costs than the northern route, where the transporting a ton of oil to Novorossiysk costs US\$15.67, but to Supsa is \$13.14.

From the Georgian port of Supsa, oil is usually shipped then via the Bosphorus delivered by oil tankers to the customers.

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Oil and gas Pipelines:

Baku–Tbilisi–Ceyhan oil pipeline:

“Baku–Tbilisi–Ceyhan” pipeline transports oil to the Turkish port of Ceyhan on the Caspian Sea for export to European markets through the Mediterranean. It has a total length of 1,768 km (1,099 mi) with 443 km (275 mi) in Azerbaijan, 249 km (155 mi) in Georgia and 1,076 km (669 mi) in Turkey. Since 2006, 50 million tons of oil per year is exported through this pipeline.

The maximum discharge of the pipeline capacity is app. 1 million barrels (160,000 m³) of oil per day;

The initial partners of BTC were the following companies: BP, SOCAR, Chevron, Statoil, GIOC, TPAO, Eni, Total S.A., Itochu, Inpex, ConocoPhillips, and Hess Corporation where the operator of the pipeline was BP.

The first document on the construction of the BTC pipeline was signed between Azerbaijan and Turkey on 9 March 1993 in Ankara. The Turkish route meant a pipeline from Azerbaijan would run through Georgia or Armenia, but the route through Armenia was politically impossible due to Armenian occupation of more than 20% of the Azerbaijani territories. Therefore, it left the circuitous Azerbaijan-Georgia-Turkey route, longer and more expensive to build than the other option, and of course, with the higher transit costs.

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Oil and gas Pipelines:

The South Caucasus gas pipeline (also known as “Baku–Tbilisi–Erzurum” (“BTE”) or “Shah Deniz” pipeline)

BTE is a natural gas pipeline from the Shah Deniz gas field in the Azerbaijan sector of the Caspian Sea to Turkey. It runs parallel to the Baku–Tbilisi–Ceyhan pipeline. The length of the BTE pipeline is 692 km (430 mi) and maximum discharge capacity: 25 billion cubic metres per annum.

TBTE pipeline is owned by the South Caucasus Pipeline Company, a consortium led by BP and SOCAR. The shareholders of the consortium are: BP (UK) 28.83%; TPAO (Turkey) 19%; SOCAR (Azerbaijan) 16.67%; Petronas (Malaysia) 15.5%; Lukoil (Russia) 10%; and Naftiran Intertrade (Iran) 10%.

The technical operator of the pipeline is BP and the commercial operator is Statoil. According to the PSA agreement, the commercial operatorship of the SCP was transferred to SOCAR starting on 1 January 2015.

As the BTE pipeline has the potential to be connected to Turkmen and Kazakh producers through the planned Trans-Caspian Gas Pipeline, Azerbaijan proposed expanding capacity of BTE up to 60 billion cubic metres (2.1 trillion cubic feet) by building a second line of the pipeline.

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Oil and gas Pipelines:

Trans-Anatolian (“TANAP”) gas pipeline:

TANAP is planned to transport natural gas across Turkey, expanding the capacity from the South Caucasus pipeline. The pipeline cost is apprx. US\$8.5 billion.

The capacity of the pipeline is 16 billion cubic metres (570 billion cubic feet) of natural gas per year at initial stage and would be increased later up to 23 billion cubic metres (810 billion cubic feet) by 2023, 31 billion cubic metres (1.1 trillion cubic feet) by 2026, and at the final stage 60 billion cubic metres (2.1 trillion cubic feet) to be able to transport additional gas supplies from Azerbaijan and, if the Trans-Caspian Gas Pipeline, from Turkmenistan. Its capacity would be increased by adding parallel loops and compressor stations according to the increase of available supplies.

On November 21, 2018 TANAP and TAP have been joined along the shores of the Maritsa River at the Turkish-Greek border. As a result of the joining of these two pipelines, Azerbaijani natural gas from the Shah Deniz-2 field is being transported to Italy via Azerbaijan, Georgia, Turkey, Greece, Albania, and the Adriatic Sea.

The TANAP is operated by SOCAR. SGC holds 58% stake in the project. Turkey's pipeline operator BOTAŞ own 30%, while BP acquired 12% in the project on March 13, 2015. TANAP is headquartered in Ankara, Turkey.

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Oil and gas Pipelines:

Trans Adriatic gas pipeline (“TAP”):

Wholly outside of Azerbaijan, TAP connects TANAP to European pipelines. TAP has been supported by European institutions and seen as a "Project of Common Interest" to enhance energy security and diversify gas supplies for European markets. It is operated by a Swiss joint venture and owned by BP (20%), SOCAR (20%), Snam (20%), Fluxys (19%), Enagás (16%) and Axpo (5%). Construction of TAP started in 2016 and commissioned in 2020.

The initial capacity of TAP is 10 billion cubic metres (350 billion cubic feet) of natural gas per year, of which 8 billion cubic metres is delivered to Italy, 1 billion to Greece, and 1 billion to Bulgaria. It is planned to be expanded up to 20 billion cubic metres.

Total construction costs were about €4.5 billion. A third of it was spent for constructing the section within Albania.

Construction of TAP started on 16 May 2016 and on 15 November 2020, the pipeline began commercial operations. The first Azerbaijani gas was delivered to Italy on 30 December 2020.

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Legal Regime:

Azerbaijan reinstated its statehood in 1991 by adoption of the Constitutional Act on state independence dated October 18, 1991.

Legal basis of activity in the energy sector of Azerbaijan is formed by the Constitution of Azerbaijan, the Laws, Presidential Decrees, Decisions of the Cabinet of Ministers and legislative system consisting of normative acts of central executive power bodies, as well as international treaties, which Azerbaijan is a signatory to, which are considered as an integral part of the system based on the Constitution.

The Ministry of Justice of Azerbaijan has developed the single internet portal for the judicial system, which provides an access to all legal and normative acts of Azerbaijan. The portal includes all the legislative information related to the Azerbaijani energy sector as well. All new legal and normative acts issued or amended are included in the portal and are regularly updated. The “E-qanun” portal is available to the public, which makes it easy to get the necessary legislative information from a single source.

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Legal Regime – Energy legislation:

The legal framework for the regulation of oil&gas issues in Azerbaijan after its state independence was laid down with the adoption of the following laws:

Law “On Nature Protection and Nature Usage”, February 25, 1992;

Law “On Usage of Energy Resources, May 30, 1996;

Law “On Subsoil” February 13, 1998;

Law “On Power Engineering” April 03, 1998;

Law “On Gas Supply” June 30, 1998;

Law “On Energy” November 24, 1998 and

Law "On the application of a special economic regime for export-oriented oil and gas activities" №766-IIIQ, adopted on 02.02.2009 (with effective date as of 17.04.2009 and which will be effective till 31.12.2024).

The Subsoil Law governs the exploration, use, protection, safety and supervision over the use of subsoil resources including, but not limited to, oil located both within Azerbaijan and on the Azerbaijani sector of the continental shelf of the Caspian Sea. However, the Code of the Azerbaijan SSR on Subsoil, dated 26 November 1976, which was repealed with the adoption of the Subsoil Law, specifically excluded oil and gas from the definition of subsoil resources.

While the Energy Law is intended to complete the legal framework for the use of subsoil resources, including oil&gas, the Law on Usage of Energy Resources Law sets forth the social, economic and legal bases of state policy in the area of energy resource use.



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Legal Regime – Energy Legislation:

Azerbaijan's energy legislation dates mostly from the second half of the 1990s.

As it is stated above, the 1998 Law on Energy is a framework law regulating the exploration, development, production, processing, storage, transportation, distribution and use of all “energy materials and products”. Any person planning to carry out energy activities must obtain a relevant special permit from the MoE based on an energy contract or an application submitted prior to project initiation.

The 1998 Law on Gas Supply regulates the production, processing, transportation, storage, distribution, sale and use of all types of gas.

Oil and gas exploration and production projects involving international partners operate almost exclusively under production sharing agreements (PSAs), each of which has the status of a separate law.

All of the existing deals of Azerbaijan on transit, transportation and export of natural gas through the pipeline system within and outside of the territories of Azerbaijan with the countries involved are considered to be international agreement under the Azerbaijani law and accordingly, ratified as a law by the Azerbaijani legislator.



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Legal Regime – Competent authorities for Energy sector:

According to the Presidential Decree dated 28 March 2000, No. 310 on measures to improve the issuance of special permits (licenses) for certain types of business activities in Azerbaijan, the production and processing of oil, oil products, and natural gas can only be conducted by state entities and joint-stock companies in which the controlling stake belongs to the Azerbaijani state.

Pursuant to the regulations of the Ministry of Energy (“MoE”) approved by Presidential Decree No. 404 on 15 May 2006, MoE participates in the preparation and implementation of state policy in the areas of the production, transportation, and processing of oil&gas. Specifically, based on the instructions of the President, MoE may prepare, negotiate, execute and oversee the implementation of PSAs and other agreements (including export of oil and gas) on behalf of the state with respect to the development of hydrocarbon reserves in Azerbaijan.

While the regulations of MoE provide that the regulation of oil and gas matters is generally vested in this ministry, however, SOCAR still continues to play an important (in fact, on most issues, a leading) role in such matters, especially in relation to the practical implementation of oil as well as gas projects.



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Legal Regime - Licensing:

Under the Subsoil Law, subsoil resources such as oil&gas are the sole and exclusive property of the state of Azerbaijan. There is a legal distinction between surface rights and subsurface mineral rights. No person or legal entity may engage in oil or gas exploration and production without prior obtaining a license (an activity permit for a particular area), where the Subsoil Law provides that a production license must be issued for a particular subsoil block and is the ultimate deed granting subsoil use rights to that block.

An exploration license can be issued for a term of up to five years and a production license for up to 25 years. A combined exploration and production license may be issued for up to 30 years. The license term (exploration, production or combined) is extendible, subject to the subsoil user's compliance with the terms of the license. An extension can be granted for a term agreed between the subsoil user and the licensing authority.

Unlike the Subsoil Law, the Energy Law provides that production rights for a specified block are granted exclusively on the basis of an 'energy contract'.

Notwithstanding the regimes set forth in the Subsoil and Energy Laws, almost all of the major oil deals in Azerbaijan have been and are still being approved by Milli Mejlis – the country's legislature. In the absence of a PSA law and/or a law on petroleum, every oil deal in the form of a PSA – the prevailing form of oil&gas agreements in Azerbaijan – is approved into law prevailing over any other conflicting Azerbaijani laws (arguably, except for the Constitution, acts adopted by public referendums and international agreements).



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Legal Regime – Role of SOCAR:

The role of SOCAR in Azerbaijani oil&gas sector is aligned with: i) the role of the government entity representing and acting on behalf of the Azerbaijani state in almost all of the major oil&gas related projects; and at the same time, ii) actively promoting its own projects as a commercial partner (for example, the case with TANAP, SOCAR acts in close cooperation with foreign counterparties (such as BOTAS and/or TPAO) in promoting the projects it is involved in.

Besides the projects involving SOCAR in the pipeline projects such as TANAP and TAP, there are some other commercial projects, where SOCAR is actively involved in, which related to construction of offshore drilling rigs in the Caspian Sea, development of refineries in Azerbaijan and Turkey, etc. SOCAR operates the country's oil refinery, gas processing plant including several oil and gas export pipelines throughout the country, owns fuel filling station networks under the SOCAR brand in Azerbaijan, Turkey, Georgia, Ukraine, Romania and Switzerland.

According to the Order of the President of Azerbaijan Mr. Ilham Aliyev dated November 06, 2022 SOCAR has been transferred to the management of newly established state owned public legal entity named “Azerbaijan Investment Holding”.



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Thank You!

Do you have any questions?

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