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Implementation of the European Neighbourhood Policy in Azerbaijan Progress in 2012 and recommendations for action

Accompanying the document

JOINT COMMUNICATION TO THE EUROPEAN PARLIAMENT, THE COUNCIL, THE EUROPEAN ECONOMIC AND SOCIAL COMMITTEE AND THE COMMITTEE OF THE REGIONS

European Neighbourhood Policy: Working towards a Stronger Partnership

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1. OVERALL ASSESSMENT AND RECOMMENDATIONS

This document reports on the progress made between 1 January and 31 December 2012 in implementing the EU-Azerbaijan European Neighbourhood Policy (ENP) Action Plan, although developments outside this reporting period are also taken into consideration when deemed relevant. It is not a general review of the political and economic situation in Azerbaijan. Information on regional and multilateral sector processes is contained in the Eastern Partnership Implementation Report.

EU-Azerbaijan political dialogue in 2012 included visits to Azerbaijan by the President of the European Council in July, by Commission Vice-President Kroes in November, and by Commissioners Füle in April and Oettinger in August, as well as visits to Azerbaijan by several MEPs. The Second EURONEST Parliamentary Assembly took place in Baku in April, the first such meeting outside the EU.

Despite progress in the implementation of the Action Plan in 2012, Azerbaijan needs to step up its efforts if it is to meet all Action Plan commitments on democracy, including the electoral process, the protection of human rights and fundamental freedoms, and the independence of the judicial system - particularly in terms of implementation.

Positive developments included the release in June of all remaining activists who participated in the May 2011 protests. However, issues related to electoral legislation, freedom of expression, freedom of the media and freedom of association and assembly still need to be addressed. Appropriate corrective measures by the Azerbaijani authorities to meet their commitments towards the EU, the Council of Europe and the Organisation for Security and Cooperation in Europe (OSCE) are especially pressing, bearing in mind the upcoming presidential elections in October 2013.

Corruption continues to be the main obstacle to economic diversification and the development of entrepreneurship in Azerbaijan, including in the region. The perceived lack of accountability is the source of anger and resentment. The EU will monitor closely the outcome of numerous initiatives and the new tools created by the authorities to curb corruption, in particular the 2012/2015 Action Plan adopted on 5 September 2012, to see whether these can yield long awaited deliverables.

The macroeconomic fundamentals of the Azerbaijani economy remain largely positive. The generally improving business climate would benefit from clearer rules on competition, increased budget transparency and in particular from sustained action against corruption. Efforts will also be needed to revive World Trade Organisation (WTO) accession talks. The EU continues to see strong benefits for Azerbaijan participating in the multilateral rules-based system.

Significant progress has been made under the Strategic Partnership on Energy between the EU and Azerbaijan, on the basis of the joint statement signed by Presidents Barroso and Aliyev in January 2011. The Azerbaijani and the Turkish Parliaments have now ratified the bilateral agreements on the construction of the Transanatolian Pipeline for transit of gas to the EU. The realisation of the Southern Energy Corridor has come one step closer and only awaits the decision of the Shah Deniz II consortium on the preferred route to the EU market – this decision is expected in the first half of 2013 and the Final Investment Decision by October 2013. Talks with Azerbaijan and Turkmenistan on the Transcaspian Pipeline have continued, with the last round taking place in September 2012.

Negotiations on an Association Agreement gained momentum in September, following several months of little progress. Negotiations on a Deep and Comprehensive Free Trade Area (DCFTA)

can only be launched after Azerbaijan has acceded to the WTO. Negotiations got underway on EU-Azerbaijan Visa Facilitation and Readmission Agreements were successfully launched.

There has been no progress in the talks mediated by the OSCE Minsk Group co-chairs aimed at settling the Nagorno Karabakh conflict. Front-line incidents, the Safarov case and the opening of the airport in Nagorno Karabakh have shifted priorities towards defusing tension rather than seeking a solution. There was also no progress on the incident investigation mechanisms supported by both sides at the Sochi Summit in January 2012. The European Union Special Representative on the South Caucasus and the crisis in Georgia visited the region on three occasions to support the work of the OSCE Minsk Group, and the EU funded project 'European Partnership for the Peaceful Settlement of the Conflict in Nagorno Karabakh', aimed at developing confidence-building measures, entered its second phase.

Azerbaijan addressed only a few of the key recommendations contained in the last year's ENP progress report. It started implementing the Human Rights Action Plan, continued judicial reform and took some steps to address the problem of demolitions and forced evictions. It did not cooperate with rapporteur of the Parliamentary Assembly of the Council of Europe on political prisoners. Progress is needed also on the other key recommendations. On the basis of this year's report and with a view to the sustained implementation of the ENP Action Plan in 2013, Azerbaijan is invited to:

- Ensure implementation of the January 2013 resolution of the Parliamentary Assembly of the Council of Europe on the honouring of obligations and commitments by Azerbaijan.
- Continue implementation of the Human Rights Action Plan adopted in December 2011.
- Step up efforts with Armenia to reach agreement on the Madrid Principles, in accordance with the commitments made by the Presidents of Armenia and Azerbaijan within the Minsk Group.
- Ensure unimpeded access to representatives of the EU to Nagorno Karabakh and surrounding regions in support of conflict transformation activities in full complementarity with the Minsk Group activities.
- Promote an environment conducive to progress in the conflict settlement, encourage and support related peace-building activities.
- Adopt the Law on Defamation which provides for the abolition of criminal liability for defamation and insult.
- Bring electoral legislation into line with the OSCE/ODIHR recommendations and ensure effective implementation.
- Continue to bring legislation on freedom of assembly, freedom of association and freedom of the media into line with international standards, and ensure its implementation.
- Step up efforts to investigate cases of harassment against journalists and activists.
- Step up efforts to make the judiciary independent.
- Address outstanding issues in public financial management, notably on transparency and accountability in relation to the budget cycle.

- Implement the National Anti-Corruption Action Plan.
- Adopt and implement a competition law to create more predictability and transparency in the market.

2. POLITICAL DIALOGUE AND REFORM

In April, Parliament adopted amendments to the **Electoral Code** in April, most of which relate to the handling of complaints and a public funding system. However major improvements linked to the Office for Democratic Institutions and Human Rights (ODIHR) recommendations are still pending, such as the composition of the electoral commissions, the registration process and the investigation of complaints. The arrests of two high level opposition members following the Ismayilli events on 23 February 2013 confirm that initial concerns remain relevant. An internet-disseminated video showing a Member of Parliament negotiating a bribe in exchange for a seat was broadly seen as evidence that the electoral process is still permeated with corruption. In a positive development, the MP in question was arrested in February 2013.

Concerning **freedom of association**, a new penalty for providing false information during the state registration of legal entities was introduced in the *Code of Administrative Offences* in early 2012. Later, in March, Parliament passed a law amending the *Criminal Code*, according to which criminal liability can be applied to legal entities for criminal acts committed by officials acting in favour of a legal entity or in order to protect its interests. The Government finally agreed to re-register the US National Democratic Institute, suspended since March 2011. However the Human Rights House request for registration is still pending.

Freedom of assembly remained a serious concern. While people imprisoned in the wake of the protests of April 2011 were granted an early release by a Presidential decree, the authorities continued to exert very tight control and to impose serious restrictions. Peaceful protests in central Baku, which intensified in the run-up to the Eurovision Song Contest, were clamped down on, and participants were temporarily detained. Opposition forces staged rallies in authorised venues, in the outskirts of Baku. However, rallies in downtown Baku continue to be refused authorisation. November amendments to the Law on Freedom of Assembly provided for drastic increases in fines for organising and taking part in peaceful rallies, which may further restrict the freedom of assembly in the run-up to the 2013 presidential elections.

Freedom of expression and of the media remained a serious concern. Currently several journalists are being detained on various charges. Harassment, intimidation and violence towards independent and opposition journalists continued. In March, a campaign of blackmail and intimidation was conducted against an investigative journalist. In April a journalist was beaten by employees of the State Oil Company while filming the demolition of houses. Investigations into these events have been launched but they advance slowly and have not so far produced any results. The author of photos and videos produced as part of the *Sing for Democracy* campaign is allegedly facing hooliganism charges and could be jailed for up to five years. The long-awaited *Draft law on defamation*, which (in consultation with the Venice Commission) would introduce substantial improvements, has not yet been submitted to Parliament. A new law banning the street selling of newspapers has reduced the dissemination of critical newspapers and alternative views. On the positive side, the authorities released a prominent youth activist in May and the President pardoned and released a total of 87 detainees, some of whom were journalists and activists.

Azerbaijan continued its **justice** reform programme, funded by the EU and other donors. Under the Comprehensive Institutional Building Programme (CIB), the government accepted in July the

Institutional Reform Plan on Human Rights and Rule of Law, Visa Facilitation and Readmission issues, areas in which the implementation of reforms will be funded mostly by the EU. A long-awaited *Law on suspects and accused* entered into force in July. The authorities established a working group of civil society representatives to draft legislation on legal aid.

The lack of **judicial independence** persisted, making **access to fair trials** difficult. **Equality of arms**, especially the rights of the defence, remained problematic due to the quantitative and qualitative lack of legal representation, especially when it concerns state-appointed lawyers. **Ill-treatment**, mostly during police custody, remained unpunished. Enforcement by national authorities of judgments of the European Court of Human Rights remained a concern.

Azerbaijan finalised its second **anti-corruption** strategy. Citizens are asked to inform the authorities about corruption, notably via hotlines. A new National Anti-Corruption Action Plan (NACAP) 2012-2015, approved in September, provides for better legislation on criminal prosecution, including the preparation of a law on personal protection of witnesses and collaborators in corruption cases, enforcement rules and rules restricting the immunity of judges suspected of corruption. In addition, the Prosecutor General in January delineated the jurisdiction of the Anti-corruption Department (ACD) in pre-investigation and investigation phases, and the scope of legal aid in criminal matters. Transparency International's Corruption Perception Index 2012 ranks Azerbaijan 139th out of 174 countries; this low position reflects the country's limited progress in defeating corruption.

Concerning **democratic control over the armed and security forces**, the President promulgated in February the *Law on military duty and military service*, which abolished the corruption-tainted military commissariats. Despite this positive development, the *Law on Alternative Military Service* is still pending and corruption in the army remains a concern.

Finally, **local democracy** is an important issue in a governance context where little attention has been given either to decentralisation or to subsidiarity. More attention should be directed to supporting participatory decision-making at local level and helping local authorities to operate in an open and inclusive way.

Other human rights and governance-related issues

The office of the Human Rights Commissioner (**Ombudsman**) despite its very broad mandate and its keen interest in working with the EU has not yet been able to realise its potential in ensuring the effective promotion and protection of human rights. The authorities did not allow the Parliamentary Assembly of the Council of Europe (PACE) *rapporteur* on **political prisoners** to visit the country in 2012 in this capacity. Nonetheless, the *rapporteur* prepared a report on political prisoners in Azerbaijan that was adopted by the PACE Committee on Legal Affairs and Human Rights in June 2012 and was debated in January 2013 at the PACE Plenary. The Plenary, rejected the report on 23 January 2013 (125 votes against, 79 in favour and 20 abstentions). On the same occasion, however, the Parliamentary Assembly endorsed a resolution on the "honouring of obligations and commitments by Azerbaijan". PACE called on Azerbaijan to implement fully its commitments towards the Council of Europe.

Concerning the **prevention of torture, ill-treatment and impunity**, the authorities submitted to Parliament in June draft amendments to the *Criminal Code* clarifying the difference between torture and ill-treatment by government agents. The independent NGO "Committee against Torture" received 112 appeals in the first nine months, ranging from ill-treatment and torture in prison services to police stations, military institutions and orphanages.

In terms of **freedom of religion**, most religious groups were able to worship publicly without government interference. There were reports of targeted raids by the authorities at places of worship and detentions of members of Muslim groups considered radical, and of and neo-protestant groups. In October the police clashed with activists who were protesting against the ban on the hijab in secondary schools. The same month, the Venice Commission and the OSCE/ODIHR concluded that the *Law on Freedom of Religious Belief* contained a series of somewhat restrictive provisions, which were not in accordance with international standards.

Ensuring **women's rights** as envisaged by the *Law on Prevention of Domestic Violence* remains a challenge in the absence of implementation mechanisms. Cases of indirect discrimination against women at work were also signalled during the reporting period.

In terms of **children's rights**, a presidential Decree was issued in May approving the *Rule of state control on the implementation of Children's rights* was issued and setting up a Commission under the Cabinet of Ministers to carry out periodic and *ad hoc* monitoring. The number of children in institutions remains quite high, with a need to make further progress on alternative care services and support for fostering arrangements.

In 2012, the issue of services for **socially vulnerable** and/or **disabled people** was given due attention at policy level, following the implementation of the new *Law on Specialised Social Services* that was adopted in December 2011. The Ministry of Labour and Social Protection (MLSP) coordinated with NGOs to address the needs of certain categories of vulnerable groups. The Government started piloting the use of NGOs as service providers, with disabled children being the target group this year.

In the field of **labour and trade unions** a Tripartite National Occupational Health and Safety Council was established in January, with the support of an EU-funded twinning project. Since January, Azerbaijan has ratified ILO Conventions on maternity protection and workers with family responsibilities, in line with UN requirements. Under an EU twinning project, Azerbaijan formulated certification standards for working places in accordance with international standards. State control over the signing of labour contracts has strengthened, targeting illegal employment and non-formalised labour relations.

Violation of **property rights** continued to cause concerns. Complaints about forced evictions and demolitions in breach of the national legislation peaked in the run-up to the Eurovision song contest. This resulted in a number of court cases, several of which went to the European Court of Human Rights. The State Committee for Property Affairs started work on the online registration of property rights. The *Rules for the preparation of plans and instructions to move people* implementing the *Law on the purchase of land for state needs* were adopted by in February, providing for adequate compensation for anyone affected. Amendments to the *law on Procurement of land for public use* make provision for tax exemption for compensation payments. In addition, the *NACAP* features some measures to promote transparency and access to information.

The protection of fundamental rights and freedoms in the **Nakhchivan** Autonomous Republic (NAR) of Azerbaijan continued to cause particular concern. There were reports of oppressive measures taken by local authorities against human rights activists, journalists and entrepreneurs. Impunity for violations of fundamental rights and freedoms and for corruption continued to prevail. A delegation of Member States' Embassies and the local EU Delegation visited NAR in February 2013 and had discussions with various actors with mixed results.

In the field of **public administration reform**, a State Agency for Public Services and Social Innovations was established in July. Its purpose is to provide public services to citizens under the "one-stop-shop" principle and optimise E-government services.

Azerbaijan joined the **Open Government Partnership** in 2012 and an *Open Government National Action Plan 2012-2015* was adopted in September. The *NACAP 2012-2015*, features the preparation of the draft Civil Service Code, which would include rules for staff performance appraisals and upgraded ethical conduct rules.

On **cooperation with NGOs**, the Presidential Administration initiated a dialogue in July between the government and civil society. Participants raised such issues as state registration of NGOs, taxation of NGOs, grants, restrictions for conducting events in the regions, and persecution of civil activists.

Cooperation on foreign and security policy, conflict prevention and confidence building measures

In 2012 Azerbaijan aligned with six out of 62 EU CFSP declarations it had been invited to support (compared to 12 out of 82 in 2011). Azerbaijan thus has the lowest alignment rate among the Eastern partners that have been invited to support such declarations. Negotiations between Armenia and Azerbaijan to resolve the Nagorno-Karabakh conflict have regrettably slowed down. The Armenian and Azerbaijani presidents have not reconvened since the Sochi meeting in January, and the Foreign Ministers mostly limited their availability for meetings in the OSCE Minsk Group Co-Chair format to separate approximation talks.

The security situation remained volatile. In June, there were serious tensions at the Armenian-Azerbaijani border with a minimum of eight servicemen reported killed. This coincided with the visit of US Secretary of State Clinton to the region.

The latest dynamics in bilateral relations impacted negatively on trust between the parties and run counter to the Presidents' readiness expressed at the beginning of 2012 to speed up agreement on basic principles on the basis of work done thus far. The EU has therefore repeatedly urged restraint in actions and public statements, in order not to escalate an already difficult situation.

September saw the launch of the second phase of the EU-funded civil society programme European Partnership for the Peaceful Settlement of the Conflict over Nagorno-Karabakh (EPNK). Its aim is to support peace-building efforts by facilitating dialogue between civil society, the media and policy-makers.

3. ECONOMIC AND SOCIAL REFORM

Macroeconomic framework and functioning market economy¹

After the halt in 2011, **GDP growth recovered slightly** fuelled by the expansion of the non-oil sector that is mainly driven by fiscal transfers from the windfall hydrocarbon sales. GDP growth accelerated to 2.2% in 2012 benefiting from a nearly 20% increase of investments and robust household demand. The **non-oil industry expanded by 9.7%** in 2012, helping to further diversify

¹ Figures on GDP, inflation, trade and employment are generally from Eurostat based on data supplied by the national statistical offices; or IMF or Commission Staff estimates, as indicated in the Statistical Annex. When other data sources are used these are then indicated.

of the economy. Oil production, down 5%, remained in the contraction mode for the second year in a row.

The authorities continued to rely on hydrocarbon proceeds to finance investments in the non-oil sector. State budget expenditures retained double-digit growth pace in 2012 due to higher transfers from the oil wealth fund SOFAZ. The growing reliance on oil export proceeds to finance recurrent expenditure weakens the budget fundamentals and raises concerns about the long-term sustainability of the public finances. When SOFAZ transfers are excluded, the state budget recorded a deficit of estimated 18.0% of GDP in 2012, which is an increase of one percentage point year-on-year.

Despite an expansionary fiscal policy, **inflation pressures subsided**, mainly due to lower food prices on global markets and good local agricultural production. The average annual inflation dropped to 1.1% in 2012 from 7.9% in 2011. The current account surplus declined to 22% of GDP in the first three quarters of the year due to reduced oil output. Still, the **huge current account surplus** enables Azerbaijan to continue building up foreign exchange assets that provide sufficient space for countercyclical policies in case of a steep decline of oil prices. The combined international assets of the central bank and SOFAZ rose to USD 45.8 billion (EUR 34.7 billion) at the end of 2012 (approximately 67% of GDP).

In an attempt to strengthen the capital base of the banking system, the Central Bank of Azerbaijan increased fivefold the minimum capital requirement for commercial banks. The new regulation will enter into force in 2014. However, the banking sector remains negatively affected by high provisioning expenses and a weak capital position of the International Bank of Azerbaijan. The state intervened in early 2012 to help the bank to meet the minimum capital requirement. There was no progress with the planned privatisation of the bank, which is necessary in terms of improving management practices, strengthening competition in the sector and reducing contingent liabilities on the state.

Social situation, employment and poverty reduction

It is expected that unemployment figures for 2012 will be slightly below the 5.4% registered for 2011. As of 1 October, national figures indicated that some 37,400 people were officially registered as **unemployed** in Azerbaijan, 42.3% of whom were women. The largest number of unemployed were registered in Baku (13,138 people, of whom 649 people received unemployment benefits). The average unemployment benefit in Azerbaijan was AZN 208.9.

The average **monthly wage** in Azerbaijan for January - September grew by 6.9% against the beginning of 2012 (AZN 363.1). The State Statistical Committee reports that the average monthly wage in Azerbaijan for September was AZN388.2. However, strong and growing disparities between Baku and the regions and between the various socio-economic groups could be a threat to social harmony.

The State Labour Inspection under the Ministry of Labour and Social Protection made efforts to address the problem of informal employment by strengthening its checks on labour contracts to eliminate illegal employment. Work is underway to establish a labour safety development agency to improve the quality of the labour market in the country in accordance with international standards.

As of August, targeted **social assistance** per family made up approximately. EUR 110 per person. In August, targeted social assistance had been granted to 141,378 families, in total 629,129 eligible persons. 58,627 of these families had three or more children, and 12,552 families were made up of **internally displaced people**. Administration of social assistance remained a challenge in terms of

delivering benefits to beneficiaries and assessing who qualifies. Mandatory insurance for cars and real estate was imposed as of 2012.

4. TRADE-RELATED ISSUES, MARKET AND REGULATORY REFORM

The EU is Azerbaijan's main trading partner accounting for 42.5% of its trade volume in 2011². **Bilateral trade** flows decreased and during the first eleven months of 2012 amounted to EUR 15.3 billion. EU exports to Azerbaijan consisted mainly of machinery and transport equipment. EU imports from Azerbaijan consisted mainly of mineral fuels.

Although Azerbaijan continued regular negotiations, there was only limited progress in **WTO accession** in 2012. In November, Azerbaijan submitted revised offers on goods and services.

The new **Customs Code** entered into force in January 2012. In coordination with other institutions, the State Customs Committee (SCC) adopted normative acts (secondary legislation) aimed at implementing the new Customs Code. Draft rules on determination of preferential and non-preferential origin of goods stipulated in the articles of the Customs Code were submitted to the Cabinet of Ministers. The SCC approved a new Code of ethical behaviour for the customs officials in January 2012.

In the **sanitary and phyto-sanitary** (SPS) field, Azerbaijan further worked towards approximation with WTO-SPS and *Codex Alimentarius* rules. It strengthened laboratories including by accrediting two central laboratories under ISO standards and by refurbishing and equipping five regional veterinary laboratories. In 2012 Azerbaijan became member of the European and Mediterranean Plant Protection Organisation. In November 2012, the Food and Veterinary Office (FVO) of the European Commission carried out a mission to Azerbaijan on aflatoxin contamination in hazelnuts to verify the implementation of an action plan addressing the issues identified in 2009.

In the area of **technical regulations**, and following the decree of April 2012, a number of services were established within the Committee on Standardisation, Metrology and Patents: State Control Service for Technical Regulation and Standardisation; State Metrology Service; and State Accreditation Service.

The World Bank's 'Doing Business 2013' annual report noted that the **business climate** benefitted from easy property registration in Azerbaijan. Nevertheless, compared to the previous year, Azerbaijan fell slightly to 67th place (out of 185) in the overall World Bank's ease of doing business ranking. State-driven investments largely prevail over private, and the monopolisation of the economy remains a strong deterrent to foreign direct investment. The National Fund for Entrepreneurship Support funded a number of projects. However, procedures for granting loans should be simplified.

In April 2012 the Ministry of Economic Development launched an internet portal setting out information on business licences and permits issued by central and local executive bodies to facilitate company **establishment** and to increase awareness among citizens and entrepreneurs.

The role of the Central Bank of Azerbaijan remained unchanged. In July Azerbaijan raised the minimum capital requirements to EUR 50 million per bank. At present, less than 25% of the operating banks meet this requirement. Azerbaijan approved new reporting rules on transactions in the securities market and rules on conducting activities on asset management in the security market. Azerbaijan should do more to improve its legal framework and the regulatory and institutional

² Data for 2012 was not available at the time of writing.

capacities of the State Committee for Securities to supervise the capital market and **financial service** providers. A Twinning Project was launched in November, seeking to approximate the legal and regulatory framework for the securities market in Azerbaijan to the EU *acquis* and to build capacity in the State Committee for Securities.

Other key areas

Azerbaijan amended a **Tax** Code. Private universities were exempted from VAT payment. The Ministry of Taxes (MoT) launched the e-registration of legal entities, with a view to reducing the costs and number of procedures for starting a business. It also launched a new Two-Way Messaging Service in August, which allows tax offices to send information about legal requirements and tax liabilities to taxpayers. A twinning supported the MoT in running the new Computer Assisted Audit system. Azerbaijan was negotiating agreements for avoidance of double taxation with Slovakia, Portugal and Malta.

The **Competition** Code has still not been adopted. A new draft was submitted to the Ministry of Economic Development prior to its third reading in the Parliament.

In the field of **intellectual property rights** (IPR), Azerbaijan made some progress with the adoption, in May, of the Law on Enforcement of IPR and on combating piracy. The Law aims to improve the enforcement infrastructure and brings Azerbaijan's legislation closer to conformity with the WTO TRIPS and the EU Enforcement Directive. The Copyright Agency submitted proposals for amendments to the Civil Procedural Code, the Criminal Code, the Criminal Procedure Code and the Code of Administrative Offences. A Centre for provision of intellectual property rights was established under the Copyright Agency.

An EBRD/UNCITRAL initiative carried out a legal assessment of the **public procurement** legislation in Azerbaijan against the 2011 UNCITRAL Model Law on Public Procurement. The draft report includes recommendations for modernising the legislative framework so as to bring it up to the best international standards.

Azerbaijan made significant progress in aligning its **statistical** classifications to the European standards. The State Statistical Committee of Azerbaijan started to implement the European System of National Accounts 2010. Following an EU assessment of the statistical system in 2010 and the revision of the Statistical Law in November 2011, Azerbaijan established an internal coordinating committee for quality management to launch a quality assurance framework.

In the area of **Public Finance Management** (PFM), Azerbaijan made some progress in implementing of the Ministry of Finance (MoF) Action Plan. The presentation of the State and Consolidated Budget 2012 was published on the Ministry's website. This is a first step towards an improved budget statement providing official information on the main fiscal and expenditure policies and indicators for 2012 and on relevant macroeconomic developments and forecasts. The 2012 Public Investment Programme was, for the first time ever, published on the MoF website, albeit in a summary format. Azerbaijan adopted action plans on anti-corruption and on the Open Government Initiative, both covering 2012-2015. They are concerned with such issues as corruption prevention, transparency, accountability and oversight. The EU and Azerbaijan cooperated on PFM reforms under the ongoing budget support programmes, and specifically in the area of **internal audit**, through a twinning project in support of Public Internal Finance Control and by supporting the civil society monitoring of PFM reform. However, the dialogue on PFM encountered a serious setback when the authorities did not approve the sector budget support programme in public finance policy. The resumption of a dialogue on PFM and budget support programmes is subject to a timely

development of a credible and comprehensive multi-annual Public Finance Management Action Plan.

In the field of **external audit**, the Chamber of Accounts drew up a Strategic Development Plan for 2012-2014. This supports the application of international standards on national accounting, financial audit, performance audit and human resources.

No progress was noted in the areas of **enterprise policy** and **movement of capital**.

5. COOPERATION ON JUSTICE, FREEDOM AND SECURITY

The EU and Azerbaijan decided to establish a **Mobility Partnership** and talks between the two sides started.

Negotiations on **visa facilitation and readmission agreements** with Azerbaijan began in March, with a second round in May-June and a third round in November, focusing primarily on the broad scope of such agreements.

Final drafts of the **Migration Code** and the Readmission Strategy, which take into consideration international practice and EU legislation, were submitted to the Cabinet of Ministers.

The State Border Service continued bilateral negotiations with Frontex, which visited Azerbaijan in August to discuss the signing of a *Working Agreement* and expansion of activities within the International Conference on Border Affairs. The Working Arrangement was initialled in October. Within the EU-funded South Caucasus Integrated Border Management Programme (SCIBM), the Azerbaijani State Border Guard Service and the Georgian Ministry of Internal Affairs prepared an agreement on how their border representatives would operate.

Azerbaijan continued its cooperation with INTERPOL and within the CIS in terms of **combating organised crime**. The Secretary General of INTERPOL visited the country in September. Azerbaijan signed the INTERPOL E-Passport Initiative in 2010, but has still not implemented it. As a result Interpol officials on duty still do not have visa-free access to the country.

Progress was noticed on **money laundering** as in July the Council of Europe Committee of Experts on the Evaluation of Anti-Money Laundering Measures and the Financing of Terrorism (MONEYVAL) lifted formal reporting regime in respect of Azerbaijan, reflecting the progress the country had made in meeting its recommendations.

Azerbaijan continued to implement the National Action Plan on the Fight against **Trafficking in Human Beings** (2009-2013) which included training schemes for enforcement agencies.

In the **fight against terrorism**, Azerbaijan reported having broken up some terrorist groups. There were some cyber attacks posing serious threats to the country's IT, media and financial sector. It ratified the Council of Europe Convention on Cybercrime in 2009, but has not yet signed its Additional Protocol concerning the criminalisation of acts of a racist and xenophobic nature committed through computer systems. Azerbaijan organised forums on fighting cyber crimes. Legislation is still based on the principles of regulation and investigation and less on prevention.

With regard to the **fight against drugs trafficking**, Azerbaijan continued to implement the five year action programme (2007-2012) to combat drug addiction. The emphasis was on law enforcement and cooperation with regional CIS partners. Azerbaijan developed cooperation with the Central Asian Regional Information and Coordination Centre (CARICC) initiated by

UNODOC. The number of reported drug smuggling cases increased significantly. Azerbaijan started work on formulating a National Strategy and an action plan for combating illegal trafficking in narcotics. The number of government-sponsored programs for tackling drug consumption is still low, particularly among youngsters. In April, the EU held a Dialogue on Drugs with Azerbaijan, Georgia, the Republic of Moldova and Ukraine in Brussels. Azerbaijan attended the first Reitox weekend of the European Monitoring Centre for Drugs and Drug Addiction (EMCDDA) in Lisbon in May. It expressed interest in cooperating with the EMCDDA and in establishing a national drug monitoring scheme.

No significant progress can be recorded in the field of **judicial and law-enforcement cooperation**, and a number of Hague conventions in the field of international legal cooperation and litigation, as well as the protection of children, remain unsigned.

6. TRANSPORT, ENERGY, ENVIRONMENT, THE INFORMATION SOCIETY, RESEARCH AND INNOVATION

In **transport**, Azerbaijan made progress in issuing digital tachographs, as required under the European Agreement concerning the Work of Crews of Vehicles engaged in International Road Transport (AETR). Through a twinning project the EU helped Azerbaijan to introduce the EU and international maritime safety and security standards, including the relevant IMO conventions, and to strengthen the capacity of the State Maritime Agency. The launching of negotiations on a Common Aviation Area Agreement in January 2013 was a major development in the EU-Azerbaijan transport relations. This agreement, once concluded and implemented, will strengthen economic, people-to-people and tourism contacts between the EU and Azerbaijan. Negotiations will be continued in 2013 and based on progress, could in principle be concluded in 2013.

Azerbaijan modernised its railway infrastructure; the construction of the Baku-Tbilisi-Kars railway advanced in 2012. Construction began on a new and high-capacity port and a logistics centre. Azerbaijan is encouraged to exploit its full potential as a transit country by becoming a contracting state to the Convention concerning International Carriage by Rail (COTIF) and joining the Intergovernmental Organisation for International Carriage by Rail (OTIF).

In the field of **energy**, Azerbaijan dynamically continued cooperating with the EU on developing the Southern Gas Corridor in line with the 2011 Joint Declaration signed by Presidents Barroso and Aliyev. Negotiations on exports from the Shah Deniz II gas field (an enabler of the Southern Gas Corridor) progressed. In February, the Shah Deniz II consortium selected the Trans-Adriatic Pipeline (Italy-Albania-Greece) as the sole pipeline option for the Italian leg of the European evacuation route. In June, the consortium chose Nabucco West (from the western Turkish border to Baumgarten, Austria) as the potential pipeline for Central and Eastern Europe. A final decision on investments and the export route is officially scheduled for autumn 2013. For gas transport through Turkish territory, Azerbaijan and Turkey signed and ratified landmark agreements to construct the Trans-Anatolia Gas Pipeline. Preparations for the construction of the pipeline are underway.

Trilateral EU-Azerbaijan-Turkmenistan negotiations on a trans-Caspian gas pipeline system, designed to feed additional supplies from Turkmenistan into the corridor, continued intensively. Azerbaijan voiced its readiness to ensure the transit of Turkmen gas.

Azerbaijan continued to supply gas to Georgia, Turkey, Iran (swaps) and Russia. Oil exports from Azerbaijan decreased as domestic oil production declined, while Turkmenistan increased its oil transit via the Baku-Tbilisi-Ceyhan pipeline. Negotiations to ship Kazakh oil via this pipeline continued. Feasibility studies continued for the development of the Azerbaijan-Georgia-Romania

Interconnection (AGRI) project, aiming to export liquefied natural gas (LNG) through the Black Sea. Negotiations with Ukraine on possible Azerbaijani LNG deliveries continued. Azerbaijan's State Oil Company (SOCAR) consolidated its regional and international position. It acquired ESSO Switzerland, further expanded on the downstream markets (Romania, Ukraine) and developed plans to construct an oil refinery in Kyrgyzstan. The development of new hydrocarbon fields made good progress. The EU's energy reform support programme played a significant role in catalysing the further development of renewable energy sources. Under this programme, the government finalised a draft of a new energy sector strategy; and mid-term action plans and secondary legislation on energy efficiency and the increased use of renewable energy. Azerbaijan restructured its institutions dealing with renewable energy and energy efficiency. It continued to construct renewable energy installations including in public buildings such as schools and hospitals. A National Strategy on the use of alternative and renewable energy sources 2012-2020 remained in a preparatory phase. Implementation of the EU-Azerbaijan Memorandum of Understanding on a strategic partnership in the field of energy progressed through several actions, in particular through an EU-Azerbaijan wind energy workshop held in March in Baku.

On **climate change**, Azerbaijan signed up in June to the Beijing Amendment to the Montreal Protocol on Substances that Deplete the Ozone Layer and a corresponding law was approved. Azerbaijan participated in preparations for the forthcoming regional EU Clima East project (EUR 18 million) that will be implemented in the period 2013-2016. The Regional Environmental Centre for the Caucasus (REC-C) continued implementing an EU-funded project on adaptation to climate change. Azerbaijan is encouraged to build capacity and engage in the new carbon market mechanism to be developed following the 17th and 18th sessions of the United Nations Framework Convention on Climate Change Conference of the Parties. Azerbaijan is also encouraged to make additional efforts to fully implement the Cancun and Durban agreements and in particular devise a low-carbon development strategy. Azerbaijan is also encouraged to pledge a nationally appropriate mitigation action.

As regards the **environment**, Azerbaijan introduced the Euro-3 standard for vehicle emission limits as of July 2012. As a result, the State Customs Committee imposed a ban on imports of vehicles that do not meet Euro-3 requirements. In the context of the Aarhus Convention, the Public Ecological Council, consisting mainly of NGOs and public representatives, was established under the Ministry of Ecology and Natural Resources. The Government presented a draft law to Parliament on the application of new procedures for environmental impact assessments. Azerbaijan is encouraged to strengthen its environmental legislation and administrative capacity, to apply procedures for environmental impact assessment consistently and to pay particular importance to public participation.

REC-C continued its activities. Its financial and institutional sustainability of REC-C still need strengthening.

In the field of **civil protection**, Azerbaijan continued to participate in the EaP flagship project on prevention, preparedness and response to natural and man-made disasters (PPRD East). The development of Electronic Regional Atlas which is a part of the programme did not progress much due to difficulties with the accessibility of the data. Azerbaijan is encouraged to take advantage of the guiding document on Risk Assessment Policy for the EaP region produced under the PPRD East programme.

Azerbaijan is among the 168 governments that adopted the "Hyogo Framework for Action: Building the Resilience of Nations and Communities to Disasters", but work on Disaster Risk Reduction is still only at the beginning and it will require considerable further effort to develop capacities and processes.

Concerning the **information society**, Azerbaijan expanded the coverage of broadband internet services. The Ministry of Communications announced that the level of internet penetration in the capital had reached approximately 90% and over 60% in the regions. An IT Development State Fund was created in March. Its purpose is to promote activity in the ICT sector, expand the introduction of innovations and scientific research. Azerbaijan approved rules for the use of emergency communications and established a Special Communication and Information Security State Agency. Regarding e-Government, Azerbaijan established a State Agency for Public Service and Social Innovations, responsible for public electronic services.

The State Committee on Standardisation, Metrology and Patents approved new standards on information technology — security techniques and security methods — which came into force in June. Azerbaijan actively participated in the implementation of the Trans-Eurasian Information Super Highway project connecting Europe with the Asia-Pacific region. The country will also be connected to the European-Persian Express Gateway (EPEG), which will run under the Caspian Sea from Iran to Russia. Construction of the main route of the Azerbaijani segment of the EPEG line was completed, and the network was being tested.

On **audiovisual policy**, the State Committee on Standardisation, Metrology and Patents started the phasing-in of three patents — digitalisation, e-governance application and e-services — for intellectual property rights registration and protection. The system is designed to expand scientific research, inventions, increase innovative products and develop the electronic technology market. Promotion of media freedom remained a challenge and no visible improvement was noted compared to the previous years.

Concerning **research and innovation**, two more projects under the EU's Seventh Framework Programme for Research and Technological Development (FP7) focusing on Azerbaijan were approved. They support closer Azerbaijani research collaboration with the European Research Area (ERA) and cover such topics as nanotechnology, energy and new materials. This increased the number of on-going FP7-funded projects that include Azerbaijani partners to thirteen. The total EU contribution to these projects amounts to EUR 22 million, more than EUR 1 million of which is given to the twelve participating Azerbaijani institutions.

7. PEOPLE-TO-PEOPLE CONTACTS, EDUCATION AND HEALTH

Azerbaijan continued its efforts to make much needed improvements to its **education** system, in spite of a relatively low education budget. National policies continued to develop, but implementation capacities at the level of education providers and supporting institutions remain an important bottleneck; salaries for teachers remained low. The part the education system plays in diversifying the economy is too limited to generate real medium-term changes in the labour market. With the development of a National Qualifications Framework, stronger quality assurance procedures, more relevant occupational standards and new curricula, a more active role in the Bologna process and a planned extension of the secondary education from eleven to twelve years, Azerbaijan is aligning its education system with international and European trends. Funding arrangements for higher education institutions changed, linking university funding to pro capita participation and student choices. Azerbaijan worked also to boost academic mobility under its revised State Programme on Youth Education Abroad in 2007-2015. Azerbaijan established a database on specialised secondary educational institutions and sought to enhance its e-service so as to allow for electronic recognition of degrees from foreign universities.

As far as participation in EU **higher education** programmes is concerned, five projects from Azerbaijan were selected under **Tempus IV**. They include student support, the establishment of

European Computer Driving Licence (ECDL) test centres, the development of a training network for better education in energy efficiency, and the setting up of EU studies, as well as new bachelor and master programmes in sustainable tourism management. Azerbaijan benefited from three scholarships for **Erasmus Mundus** joint master courses; there were also 301 grants for short-term mobility organised within a university consortium. Three institutions and one individual researcher participated in **Marie Curie Actions** to support researchers' training, mobility and career development.

Azerbaijani young people and youth organisations continue to benefit from the **Youth in Action** Programme. For 2012 and 2013, the ENPI provides additional funds to boost cooperation among young people, youth workers and youth organisations from the EU and the Eastern Partnership countries. In 2012, the newly created Eastern Partnership Youth Window within the programme enabled a significantly higher number of young Azerbaijanis to take part. 166 projects were selected in 2012 involving 564 young Azerbaijanis.

Cultural exchange and cooperation between Azerbaijan and the EU Member States expanded throughout the year, with a number of important exhibitions and events.

Azerbaijan continued, with international donors, to pursue **health** sector reform. The average salary of doctors in public hospitals remained low, and the level of out-of-pocket payments is relatively high. Azerbaijan made good progress in addressing maternal and child health and in upgrading rural health centres. There was a further increase in health expenditure. Azerbaijan is focusing on building or renovating medical facilities and is working towards strengthening regional medical institutions by hiring additional staff and developing medical staff qualifications. It strengthened the information system on infectious diseases and epidemiological surveillance. More attention is needed to improve the quality of services and to ensure equitable access to care.