

**The Committee On The
Extractive Industries
Transparency Initiative Of
The Republic Of Azerbaijan**

Independent Accountants' Report
for the 6 months period ended 30 June 2005

The Committee On The Extractive Industries Transparency Initiative Of The Republic Of Azerbaijan

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AZ1000, Bakı ş. Ü. Hacıbəyov küç., 38, m.26 Phone: (+99 412) 937 321 / 927 856
Suite 26, 38 U. Hadjibeyov St., Baku Fax: (+99 412) 932 174
GSM: (+99 450) 326 7448
Internet: www.agn.org www.agnmak.com Email: makagnbaku@azerin.com

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Independent Accountants' Report

To:

The Committee on the Extractive Industries Transparency Initiative ("EITI") of the Republic of Azerbaijan

We have examined the accompanying Assertion of the Committee of the EITI of the Republic of Azerbaijan (the "Committee") shown in Appendix 1, that the schedule of payments/allocations received during the 6 months period ended 30 June 2005 by the government of the Republic of Azerbaijan (the "Government") from the extractive industry companies (the "Companies") is prepared in accordance with the Memorandum of Understanding dated 24 November 2004 signed between the National Committee on EITI, the local and foreign companies operating in the Extractive Industries of Republic of Azerbaijan, specified in Appendix 2, and the non-governmental organizations specified in Appendix 3 (the "MOU").

Respective Responsibilities of the Management and Accountants'

The Committee on the EITI of the Republic of Azerbaijan and Companies (as per appendix 2) are responsible for the assertion.

Our responsibility is to express an opinion on the assertion based on our examination.

Basis of Opinion

Except as described in the next paragraph, we conducted our examination in accordance with International Standards on Assurance Engagements. Those Standards includes examining, on a test basis, evidence supporting the amounts and disclosures in the assertion of the Committee on the EITI of the Republic of Azerbaijan and related schedules. Our examination includes performance of such other procedures as we considered necessary in the circumstances. We believe that our examination provides a reasonable basis for our opinion.

The information available to test the Assertion of the Committee was submissions by the Companies party to the MOU and the supporting details of payments/allocations received by the Government that were provided by the Committee. Our work did not extend to reviewing all payments/allocations received by the government nor all payments/allocations made by the Companies. If payments/allocations were made by the Companies but omitted from both the Companies' and Government's submissions, our work was insufficient to detect them.

Opinion

In our opinion, based on results of checking set out in the attached summaries, and except for an adjustments, if any, which may have been required if we had tested all payments/allocations made by the Companies and all payments/allocations received by the Government, the accompanying Assertion of the Committee on the EITI of the Republic of Azerbaijan, that the schedule of payments/allocations received during the 6 months period ended 30 June 2005 is prepared in accordance with the aforementioned requirements, is fairly stated in all material respects.

This report is intended for the use of the signatory parties to the MOU and should not be used by other parties or for other users than as prescribed by the MOU.

December 20, 2005

AGN MAK Azerbaijan Ltd
Suite 13, 13 U.Hadjibeyov St.,
Baku, AZ1000
Azerbaijan Republic
Tel: + 994 (124) 12 492 78 56
Fax: + 994 (124) 12 598 19 26
www.agnmak.com

Summaries Of Accountants' Examination

The Summary

To examine the Assertion of the Committee on the EITI of the Republic of Azerbaijan (Appendix 1) we have compared the schedule of payments/allocations received during the 6 months period ended 30 June 2005 by the Government (the "Government's schedule") and the schedules prepared by the Companies (parties to the MOU) (the "Companies' schedule") specified in Appendix 2. We have carried out procedures as considered necessary under the circumstances to verify the differences between the above schedules. Our findings are presented below.

The Government Interest In The Foreign Companies' Extractive Output (Crude Oil)

Government's schedule	4.3 mln barrels
Companies' schedule	5.7 mln barrels

1.033 million barrels not included in the Governments' schedule relate to the amount transferred to the Government by an extractive industry companies which was delivered in kind on June 12, 2005 and subsequently sold in July 2005.

0.325 million barrels not included in the Governments' schedule relate to the quantity transferred to the Government by an extractive industry companies which was used for BTC line filling in May and June 2005.

0.017 million barrels not included in the Governments' schedule relate to the quantity delivered at no cost in accordance with the PSA to SOCAR by an extractive industry company.

We confirmed the overall amount allocated to the Government by receiving a confirmation from Azerbaijan International Operating Company ("AIOC") ("BP"), who is the operator of ACG Oil field, and another company, which is the Party of MOU, of the total amount allocated to the government.

The Government Interest In The Foreign Companies' Extractive Output (Gas)

Government's schedule	628,168 thousand cubic meters
Companies' schedule	581,867 thousand cubic meters

An amount of 34,419 thousand cubic meters of gas included in the Government's schedule relates to the use of different measurement units (normal cubic meters used by an extractive industry companies and standard cubic meters used by SOCAR) of the volume of gas.

The Companies' schedule did not include 11,882 thousand cubic meters of gas transferred to the Government by one extractive company which is a party to the MOU. This company omitted to report this amount as it declared it was unaware that this was a reportable item under the terms of the MOU.

Other Inflows To Government From The Foreign Extractive Industry Companies (Transit Duties)

Government's schedule	USD 8.8 mln
Companies' schedule	USD 8.3 mln

Transit duties relating to the Northern Route of USD 0.8 mln. were not included in the Government's Schedule but reported by the Companies. We confirmed these amounts by obtaining a confirmation from AIOC on the details of transit fees. These amounts were not included in the Government's schedule because they were paid to SOCAR as part of commercial activities and are not reportable under the terms of the MOU.

A payment of USD 1.3 mln. was included in the Government Schedule but it was accrued in 2004 and included by the Companies in their payments to The Government in 2004. The Government included this amount in the current period as the returns are prepared on a cash basis under the terms of the MOU and this represents a timing difference at 31 December 2004.

We confirmed this amount by reference to the bank and accountancy documents relating to the transaction.

The Government Interest In The Local Companies' Extractive Output (Crude Oil)

Government's schedule	Nil
Companies' schedule	0.1 mln barrels

Local companies' extractive output of 0.1 million barrels relates to incorrect reporting under the MOU by one local extractive industry company of crude oil sold to SOCAR per local market prices. This is a commercial activity and is not reportable under the MOU.

Other Inflows To Government From The Local Companies

Profit tax

Government's schedule	AzM 42.8 bln
Companies' schedule	AzM 42.7 bln

The Government's schedule includes profit tax amounting to AzM 0.1 bln which has been reconciled as a rounding differences.

Royalties (Mining tax)

Government's schedule	AzM 195.9 bln
Companies' schedule	AzM 195.9 bln

Other taxes

Government's schedule	AzM 356.7 bln
Companies' schedule	AzM 356.5 bln

The Government's schedule includes other taxes amounting to AzM 0.2 bln which has been reconciled as a rounding differences.

Appendix 1.

Assertion Of The Committee On The Extractive Industries Transparency Initiative (“EITI”) Of The Republic Of Azerbaijan

The schedule of payments/allocations received during the 6 months period ended 30 June 2005 by the Government of the Republic of Azerbaijan (the “Government”) from the local and foreign companies operating in the Extractive Industries of the Republic of Azerbaijan, specified in Appendix 2 (collectively - the “Companies”) is prepared in accordance with the Memorandum of Understanding dated 24 November 2004 signed between the National Committee on EITI, the local and foreign companies operating in the Extractive Industries of Republic of Azerbaijan and the non-governmental organizations detailed in Appendix 3.

The Chairman of the EITI Committee

Appendix 2.

List Of Extractive Industries Companies Party And Not Party To The Memorandum Of Understanding

Companies – Parties to the MOU

BP Exploration (Caspian Sea) Limited,
State Oil Company of the Republic of Azerbaijan,
Total E&P Azerbaijan B.V,
ITOCHU Oil Exploration (Azerbaijan) Inc.,
Statoil,
Turkish Petroleum A.O.,
Commonwealth Oil and Gas,
Exxon Azerbaijan Limited,
ConocoPhillips,
Amerada Hess (ACG) Limited,
Devon Energy Caspian Corporation,
Lukoil Overseas,
Unocal Khazar,
Shengli Oil,
Salyan Oil Limited,
Karasu Operating Company,
Shell Azerbaijan Exploration and Production,
Middle East Petroleum,
Anshad Petrol JV,
Shirvan Oil JV,
Azgerneft JV
Inpex,

Companies – Not Parties to the MOU

Chevron Overseas Petroleum Azerbaijan Limited,
Agip,

Japan Azerbaijan Oil Co. Ltd (“JAOC”),
Azerbaijan International Operating Company (“AIOC”)¹

¹ AIOC is the operating company of the ACG oilfield. The partners of AIOC are BP Exploration (Caspian Sea) Limited, Exxon Azerbaijan Limited, Statoil, Inpex, SOCAR, Devon Energy Caspian Corporation, ITOCHU Oil Exploration (Azerbaijan) Inc., Amerada Hess (ACG) Limited, Turkish Petroleum A.O., Unocal Khazar.

Appendix 3.

List Of Non-Governmental Agencies Party To The Memorandum Of Understanding

Community of the Young Lawyers
Economic and Political Research Center
National Group for International Human Rights
Gandja Kepez Municipality
International Ecoenergy Academy
Public Finance Monitoring Center
Citizen Initiative Center
Humanitarian Research Center
Agroeco Consulting Center
Green Movement
Economic Research Center
“Buta” Humanitarian Children Fund
Ecolecs Organization
Assistance to continuing development “Chevre” Social Community
Committee on the protection of the oilmen’s rights
Multimedia Information and Technology Center
“Expert” Economic Journal
“Knowledge” Gandja
League on the protection of the citizens’ labor rights
Gandja Children’s Fund
Azerbaijan Educational Youth Organization-Sabunchu department
Democratic Reform Society
Merchant and Reformists’ Community
“Sponsor”
Association of the “Participators of the Venchur Projects”
IHQMB
HVA Regional zone (Gandja)
Azerbaijan Fund of XXI century Human Rights
National Ecological Forecasting Center