REPORT ON PROGRAMME MANIPULATION
CHAPTER ONE
SUMMARY OF REPORT ON PROGRAMME MANIPULATION

SUMMARY OF REPORT

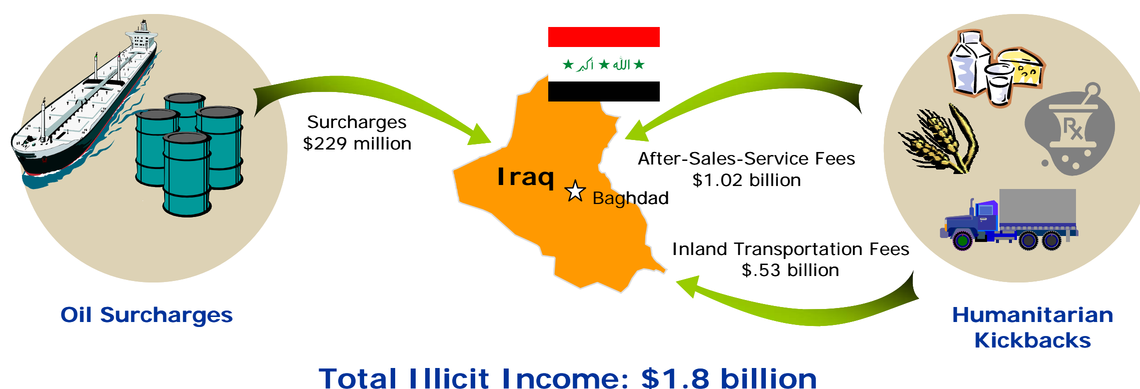
Today, the Independent Inquiry Committee ("the Committee") issues its fifth and final substantive report concerning the United Nations Oil-for-Food Programme ("the Programme"). This Report illustrates the manner in which Iraq manipulated the Programme to dispense contracts on the basis of political preference and to derive illicit payments from companies that obtained oil and humanitarian goods contracts. Today's Report complements the Committee's recent report addressing the adequacy of the Programme's management by the United Nations.

Under the Programme, the Government of Iraq sold $64.2 billion of oil to 248 companies. In turn, 3,614 companies sold $34.5 billion of humanitarian goods to Iraq. Beyond the narrative set forth in this volume, the Committee releases today a set of eight comprehensive tables identifying contractors under the Programme and other actors of significance to Programme transactions (such as non-contractual beneficiaries of Iraqi oil allocations and parties that financed oil transactions). These tables can be accessed at the Committee's website: http://www.iic-offp.org.

Several of the tables identify specific illicit payments made in connection with oil and humanitarian contracts under the Programme. Oil surcharges were paid in connection with the contracts of 139 companies, and humanitarian kickbacks were paid in connection with the contracts of 2,253 companies. The tables identify whether and, if known, how much was paid to the Government of Iraq with respect to particular Programme contracts. The principal basis for this illicit payment data is information received from various ministries of the Government of Iraq, as well as data retrieved from numerous banking institutions and, in some cases, from the company contractors themselves.

A preface to the tables explains the basis for the Committee's calculations. The Committee emphasizes that the identification of a particular company's contract as having been the subject of an illicit payment does not necessarily mean that such company—as opposed to an agent or secondary purchaser with an interest in the transaction—made, authorized, or knew about an illicit payment.

Chart A – Illicit Income Received by Iraq under the Programme



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Today's report includes the following chapters that are summarized below:

- Oil Transactions and Illicit Payments
- Humanitarian Goods Transactions and Illicit Payments
- The Escrow Bank and Conflicting Interests
- Oil and Goods Inspection Companies
- Conduct of Two Humanitarian Coordinators
- Financial Review of the Former Secretary-General

Chapter Two: Oil Transactions and Illicit Payments

Following six years of international economic sanctions, Iraq resumed its export of crude oil in December 1996 under the Oil-for-Food Programme. Under the rules of the Programme, Iraq was free to sell its oil so long as it was sold at what the United Nations decided was a fair market price and the proceeds of each sale were deposited to a UN-controlled escrow account to be used only for humanitarian and other purposes allowed by the Security Council.

It was a basic assumption of the Programme that Iraq—not the United Nations—would choose its oil buyers. Yet the decision to allow Iraq to choose its buyers empowered Iraq with economic and political leverage to advance its broader interest in overturning the sanctions regime. Iraq selected oil recipients in order to influence foreign policy and international public opinion in its favor. Several years into the Programme, Iraq realized that it could generate illicit income outside of the United Nations' oversight by requiring its oil buyers to pay "surcharges" of generally between ten to thirty cents per barrel of oil. As described more fully below, the surcharge policy started in the autumn of 2000 and lasted through the autumn of 2002. Payments flowed mostly to Iraqi-controlled bank accounts in Jordan and Lebanon, as well as by cash deposit to Iraqi embassies in Moscow and elsewhere. The Iraqi regime ultimately derived $228.8 million of illicit income from the payment of surcharges in connection with oil contracts under the Programme.

At the outset of the Programme, Iraq preferred to sell its oil to companies and individuals from countries that were perceived as "friendly" to Iraq, and, in particular, if they were permanent members of the Security Council in a position potentially to ease the restrictions of sanctions. Russian companies received almost one-third of oil sales under the Programme. Through its Ministry of Fuel and Energy, Russia coordinated with Iraq on the allocation of crude oil to Russian companies. French companies were the second largest purchaser of oil under the Programme.

Correlatively, the Government of Iraq denied or reduced allocations of oil for companies from countries in disfavor. At the beginning of the Programme, Iraqi Vice President Taha Yassin Ramadan and Oil Minister Amer Rashid convinced Saddam Hussein to give allocations to United

States companies in an effort to persuade the United States government to soften its attitude toward Iraq. According to Mr. Ramadan, when there was no perceived change, the oil allocated to United States companies was given to Russian companies. Iraq's explicit policy of favoring companies from certain countries did not prevent companies from disfavored countries from obtaining Iraqi crude oil. A substantial volume of oil under contract with Russian companies was purchased and financed by companies based in the United States and other countries.

Iraq dispensed oil allocations to and on behalf of a wide array of individuals and groups whom it considered influential in their respective countries and who espoused pro-Iraq views or organized anti-sanctions activities. Many instances of these allocation decisions are discussed throughout Chapter 2 of this Report.

Iraq's political beneficiaries often used little-known intermediary companies to enter into oil contracts for oil allocated to them, and then the oil was sold to an established oil company or trader. Oil companies and traders paid the intermediary company a premium above the United Nations official selling price. The premium was used by the intermediary in turn to pay the beneficiary or another person or entity who was designated to receive those funds.

These layers of individuals and companies between the allocation and end-use of Iraq's crude oil resulted in transactions where the United Nations could not determine from the face of the contract who actually was benefiting from or controlled the purchase of oil. This lack of transparency took on added significance in the autumn of 2000 when Iraq initiated its policy of collecting illicit surcharges on every barrel of oil sold under the Programme.

During the two years that the illicit surcharge scheme persisted, Iraq's State Oil Marketing Organization ("SOMO") assessed surcharges of between ten and thirty cents per barrel. Every contracting customer, if not each beneficiary, was advised of the requirement. Surcharges were levied on each barrel lifted, that is, loaded by a tanker at the port.

Iraq's attempt to impose a fifty-cent surcharge rate at the end of 2000 sparked a crisis in the market for Iraqi crude oil as the United Nations oil overseers warned traders and companies that such payments were illegal. After many of Iraq's regular customers balked at buying Iraqi oil, a group of four oil traders took a much greater role in the market during Phase IX of the Programme from December 2000 to July 2001. These four companies were Bayoil Supply & Trading Limited ("Bayoil"), the Taurus Group ("Taurus"), Glencore International AG ("Glencore"), and the Vitol Group ("Vitol").

All four had had limited access to direct contracts under the Programme, and had used intermediaries to maintain their access to Iraqi crude. In Phase IX, these companies purchased crude oil through intermediary entities: Bayoil mainly through Italtech SRL, an Italian-based company; Taurus mainly through Fenar Petroleum Ltd. ("Fenar") and Alcon Petroleum Ltd. ("Alcon"), Liechtenstein-based companies; Glencore through its own Swiss-based company, and Petrogaz Distribution S.A.; and Vitol mainly through Mastek Sdn. Bhd., a Malaysian-based company, among others.

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Two more companies—Trafigura Beheer BV and Ibex Energy/Multi-Prestation SARL—devised a plan in 2001 to smuggle oil by "topping off" tankers with additional oil not authorized for sale under the Programme. This plan relied on bribing a United Nations oil inspector to look the other way, but happened only twice because of an alert issued to authorities by the captain of the oil tanker involved.

Companies often disguised surcharge payments by funneling them through offshore bank accounts or labeling them as legitimate oil-related expenses. For example, Taurus-controlled entities were advised by one bank official to change their references on payments from "commissions" to "loading fees."

Oil companies and oil traders began including a standard disclaimer in their contracts to provide that the seller had not paid surcharges. This was done notwithstanding the near-universal market recognition that Iraqi oil could not be purchased without payment of a surcharge. Yet the inclusion of contractual disclaimers did not appear to dampen the incidence of surcharge payments; and, in one instance, an agent for Bayoil admitted to fabricating an after-the-fact disclaimer to help disguise the payment of surcharges.

Labels and disclaimers aside, oil companies and traders were saddled with higher premiums over the official selling price to account for the payment of the illicit surcharge at some level in the contractual chain. When contacted by the Committee, companies often attributed the premium they paid to ordinary market forces and not a deliberate attempt to pay surcharges through another party. However, most participants involved in the Iraqi crude oil market admitted awareness of Iraq's surcharge demands. Some participants have candidly conceded arranging with oil companies to use a portion of the premium payments for the payment of surcharges.

By the autumn of 2002, the Government of Iraq decided to discontinue its surcharge policy because of the decrease in demand due to the continued imposition of "retroactive pricing" by members of the 661 Committee. By that time, of course, the Government of Iraq had effectively succeeded in using the sale of oil under the Programme as a tool of foreign policy and a sizeable source of illicit revenue.

Chapter Three: Humanitarian Goods Transactions and Illicit Payments

Iraq's largest source of illicit income from the Programme came from "kickbacks" paid by companies that it selected to receive contracts for humanitarian goods under the Programme. These payments to the Iraqi regime were disguised by various subterfuges and were not reported to the United Nations by Iraq or the participating contractors. As set forth in the Committee's recent Programme Management Report, available evidence indicates that Iraq derived more than $1.5 billion in income from these kickbacks.

As with its selection of oil purchasers, political considerations influenced Iraq's selection of humanitarian vendors. For the first several years of the Programme's operation, however, Iraq did not have in place a formal kickback policy. The kickback policy emerged only over time as the Programme extended for a longer period and involved larger amounts than anticipated. The policy began in mid-1999 from Iraq's effort to recoup purported costs it incurred to transport

goods to inland destinations after their arrival by sea at the Persian Gulf port of Umm Qasr. Rather than seeking approval from the United Nations for compensation of such costs from the Programme's escrow account, Iraq simply required humanitarian contractors to make such payments directly to Iraqi-controlled bank accounts or to front companies outside Iraq that, in turn, forwarded the payments to the Government of Iraq. Not only were these side payments not authorized under the Programme, but it was an easy matter for Iraq to impose "inland transportation" fees that far exceeded its actual transportation costs.

By mid-2000, Iraq instituted yet a broader policy to impose generally a ten percent kickback requirement on all humanitarian contractors—including contractors shipping goods by land as well as contractors shipping to Umm Qasr. This broader policy was in addition to the requirement for contractors to pay inland transport fees. Iraq dubbed its more general kickback requirement as an "after-sales-service" fee. After-sales-service provisions often were incorporated into contracts as a basis to inflate prices and permit contractors to recover from the United Nations escrow account amounts they had paid secretly to Iraq in the form of kickbacks. Contractors ordinarily made these payments before their goods were permitted to enter Iraq. For ease of reference, this form of kickback is referred throughout as an after-sales-service fee, although Iraq often collected a ten percent fee without labeling it an "after-sales-service" fee or without inserting an after-sales-service provision in the applicable contract.

Many companies freely went along with Iraq's demands. Others made payments to third parties or agents while disregarding the likely purpose of these payments or perhaps unwittingly. Kickbacks were paid in connection with the contracts of more than 2,200 companies in the form of inland transportation fees, after-sales-service fees, or both.

This Report provides case studies of twenty-three companies (or related company groups) for which kickbacks were paid in connection with one or more of their contracts for humanitarian goods under the Programme. These companies fall roughly into four groups: (1) Iraqi *front companies* (i.e., companies that were controlled covertly or owned in part by the Government of Iraq); (2) *major foodstuff providers* that ranked at the top of the list in terms of the total value of contracts obtained under the Programme; (3) *major trading companies* that specialized in obtaining contracts from Iraq to sell goods that they acquired from other companies and countries; and (4) *major industrial and manufacturing companies*—mostly from Europe and North America—that did not necessarily have large numbers of contracts, but that apparently paid or caused a third party to pay kickbacks and did so despite organizational resources that might be expected to safeguard against such practices.

The sample of companies that are discussed in this Report accounted for $7.86 billion of humanitarian sales—approximately twenty-three percent of Iraq's purchases under the Programme. The Committee estimates that more than $500 million in illicit payments were made in connection with these companies' contracts, accounting for approximately one-third of all illicit payments made to the Iraqi regime in connection with Iraq's humanitarian purchases under the Programme. Moreover, several of these companies also bought oil from Iraq and paid illegal surcharges.

The larger number of companies that were contacted by the Committee and confronted with the evidence of illicit payments generally offered one of four justifications. First, some suppliers asserted that they had been unaware of any side payments to the Iraqi regime and that any such payments were made by employees or agents based in Iraq that acted without authorization. Second, some suppliers stated their belief that inland transportation and after-sales-service fees involved legitimate expenses that could be paid to the Iraqi regime. Third, some suppliers denied paying kickbacks and questioned the authenticity or reliability of the Committee's evidence. Fourth, some suppliers acknowledged paying kickbacks, noting that they were a cost for all companies of doing business with Iraq under the Programme.

Chapter Four: The Escrow Bank and Conflicting Interests

In 1996, the Secretary-General selected Banque Nationale de Paris S.A. ("BNP"), a French banking corporation, to serve as the escrow bank under the Programme. Under its banking services agreement with the United Nations, the provisions of Resolution 986 and the Iraq-UN MOU were "essential and fundamental terms and conditions" governing its provision of services. The banking services agreement required BNP to confirm all letters of credit issued by other banks under the Programme. However, the banking services agreement also allowed BNP, including its branch, subsidiary, and affiliate banks, principally in Geneva, Switzerland, to issue letters of credit on behalf of private party oil purchasers. The agreement did not otherwise restrict BNP's relations with companies that furnished financial backing for letters of credit issued from BNP and its affiliates under the Programme. Ultimately, BNP or one of its affiliates issued approximately three-fourths of the letters of credit that financed oil purchase transactions under the Programme.

Once it chose to issue letters of credits for oil transactions, BNP's loyalties were divided between serving the interests of the United Nations to promote the transparency of transactions conducted under the Programme and serving the interests of its private clients to maintain the confidentiality of their business and financing arrangements. These competing interests clashed with the advent of Iraq's oil surcharge scheme and the scheme's reliance on financing arrangements to conceal the true nature of oil purchase transactions.

The United Nations and its overseers were aware in a general sense of the prevalence of shell company purchase arrangements. BNP, however, had unique access to such information through its privity with parties engaged in such transactions. In some instances, BNP's private party financing relationships accompanied the assignments of rights and resale of oil among corporate entities. In these transactions, a typically larger, more significantly capitalized corporate entity sought to finance letters of credit in the name of a shell company. Often, these third party financing arrangements were presented to BNP's Geneva component, and the financing entity specifically requested that the Bank not disclose its participation in the transaction. Therefore, such transactions were not called to the attention of the United Nations, conflicting with provisions of the banking services agreement and SOMO's approved standard sales contract that prohibited unapproved assignments of rights and the resale of oil.

In the midst of well-publicized allegations of payments of illicit surcharges, BNP was inhibited from taking steps to review its practices to prevent such payments. Customer accounts were used

by some of its more thinly capitalized customers, often entities with little history with the Bank, to make more than $10 million in illegal surcharge payments. Such entities included Italtech, Alcon, Fenar, and Glasford Shipping Limited, as well as one customer (Augusto Giangrandi of Italtech) who was known by the bank to be suspected of money laundering activity. Although there is no evidence that BNP knew of or approved of the use of its own facilities to pay illegal surcharges, BNP was uniquely positioned to probe such payments—and failed to do so.

Chapter Five: The Oil and Goods Inspection Companies

The Programme's integrity rested in part on the performance of its inspection contractors that monitored the export of Iraqi oil and the import of humanitarian goods. The United Nations selected a Dutch company, Saybolt Eastern Hemisphere BV ("Saybolt"), to conduct inspections of oil exports; and it selected a British firm, Lloyd's Register Inspection Ltd. ("Lloyd's"), to conduct inspections of humanitarian goods imports. Lloyd's was later replaced by a Swiss company, Cotecna Inspection S.A. ("Cotecna"). Because of time and resource limitations, the Committee has not undertaken a full-scale performance review of all aspects of these contractors' activities; it has focused on allegations of significant wrongdoing and corruption.

With respect to Saybolt, the available evidence does not establish that it systematically failed to perform in accord with its contractual obligations. This conclusion is based on a review of records and interviews of non-Saybolt employees, but is qualified by the fact that Saybolt declined to cooperate with the Committee's requests to interview its inspectors. More significantly, Saybolt's performance was marred by two instances of improper conduct by Saybolt employees. The first is the acceptance of a bribe by a Saybolt employee to allow the "topping off" of an oil tanker at Mina al-Bakr without the approval of the United Nations. The second instance involved a decision by Saybolt's managing director, Peter Boks, to recommend to Iraq's Minister of Oil an allocation of oil for a Dutch company that was also a client of Saybolt. SOMO records reflect several allocations of oil to this company and reflect the name of Saybolt and Mr. Boks on its allocation lists. The Committee does not have evidence that Mr. Boks financially benefited from his recommendation of Petroplus or that, in return for the Ministry of Oil's allocations to Petroplus, he compromised performance of his duties under Saybolt's contract with the United Nations.

As to Lloyd's and Cotecna, the Committee's review has not disclosed systematic non-performance of their contractual obligations. Two investigative matters remain open with respect to Cotecna, and these will be referred for further review by the United Nations Office of Internal Oversight Services, Investigations Division. This includes information concerning payments made by Cotecna for the benefit of its officer Michael Wilson and an official of a United Nations specialized agency, the World Intellectual Property Organization. These payments occurred shortly after Cotecna was awarded its United Nations inspection contract. The Committee draws no conclusions concerning these allegations.

Chapter Six: Conduct of Two Humanitarian Coordinators

The Programme's field activities were supervised by a Humanitarian Coordinator, who was the most senior-level United Nations official stationed in Iraq and reported directly to the Executive

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Director of the Office of the Iraq Programme. The Committee has investigated allegations concerning the conduct of two former Humanitarian Coordinators—Hans von Sponeck and Tun Myat—with respect to their dealings with certain contractors under the Programme. The Committee does *not* find that the interactions of Mr. von Sponeck and Mr. Myat with Programme contractors violated existing United Nations Staff Regulations and Rules. However, their activities illustrate two distinct ethical dilemmas confronted by United Nations staff members—one involving post-employment business activities (Mr. von Sponeck) and another involving responses to requests for official assistance from persons of their home countries (Mr. Myat). These activities suggest the need for further personnel policy reforms to redress the appearance and possibility of conflicts of interest. In addition, Mr. Myat failed for five years to file required financial disclosure forms. This omission—unrealized and unredressed by the United Nations at the time—underscores the need for rigorous monitoring and enforcement of the Organization's existing ethical standards for senior-level officials.

Chapter Seven: Financial Review of the Former Secretary-General

Prior reports of the Committee have detailed corruption schemes involving persons that associated with former Secretary-General Boutros-Ghali. This includes not only the Iraqi scheme in 1996 to bribe Dr. Boutros-Ghali through Samir Vincent, but also Benon Sevan's corrupt receipt of oil allocations from 1998 to 2001, which involved diversion to Mr. Sevan of oil sales proceeds through a Swiss bank account controlled by Fred Nadler (Dr. Boutros-Ghali's brother-in-law). The Committee does not have evidence that Dr. Boutros-Ghali took part in or was aware of any of this corrupt activity. Moreover, as detailed below, a review of the known bank accounts controlled by and/or associated with Dr. Boutros-Ghali and his spouse, Leia Boutros-Ghali, has not revealed evidence that these accounts were used to receive or transfer any illicit funds provided by the former Iraqi regime. Although there were financial transactions with Fred Nadler and an account of Fred Nadler that received proceeds from Iraqi oil sales, no evidence has been found that Dr. Boutros-Ghali knowingly received proceeds of oil sales under the Programme or was in any way involved with these corrupt activities.