

Congress of the United States

Washington, DC 20515

November 25, 2003

The Honorable Joseph E. Schmitz
Inspector General
U.S. Department of Defense
Washington, DC 20301

Dear Mr. Schmitz:

We are writing to ask you to investigate two important issues relating to the reconstruction of Iraq:

- (1) The prices Halliburton has charged to import gasoline into Iraq; and
- (2) The use of the funds in the Development Fund for Iraq, the successor to the U.N. Oil for Food Program.

These two issues are related because, as of November 18, 2003, over \$725 million from the Development Fund for Iraq has been obligated to pay for Halliburton's fuel imports.

Halliburton's Fuel Prices

Halliburton has charged an average of \$2.65 per gallon to import over 60 million gallons of gasoline from Kuwait into Iraq under a contract with the U.S. Army Corps of Engineers.¹ To date, Halliburton has been paid a total of more than \$380 million for all gasoline imports into Iraq, and more than \$160 million for imports from Kuwait in particular.² An additional \$690 million has been approved for future fuel imports under the recently approved Iraq supplemental.³

The price Halliburton has charged to import gasoline from Kuwait needs thorough investigation. SOMO, the Iraqi state oil company, is able to import gasoline from Kuwait for just \$0.96 per gallon – less than half of what Halliburton charges.⁴ Similarly, the Pentagon's own fuel distribution office, the Defense Energy Support Center, currently pays between \$1.08

¹ E-mail from U.S. Army Corps of Engineers to Minority Staff, Committee on Government Reform (Oct. 21, 2003).

² *Id.*

³ H.R. 3289, Emergency Supplemental Appropriations Act for Defense and for the Reconstruction of Iraq and Afghanistan, 2004 (Joint Explanatory Statement of the Committee of Conference) (Oct. 30, 2003).

⁴ Letter from Mohammed M. Al-Jibouri, General Manager, State Oil Marketing Organization, to Minority Staff, Committee on Government Reform (Oct. 16, 2003).

and \$1.19 per gallon to import gasoline from Kuwait for military purposes – again less than half of what Halliburton charges.⁵ Based on SOMO's prices, Halliburton may have overcharged the U.S. government by about \$150 million to date.⁶

A variety of experts in the field, including independent industry consultants, foreign purchasers, and U.S. government experts, have all raised concerns with Halliburton's prices. For example, experts inside the Pentagon have been critical. Jeffrey Jones, the Director of the Defense Energy Support Center, stated: "without knowing what the \$2.65 price is composed of, it seems extraordinarily high – at least double what it should be."⁷

Mohammed al-Jibouri, the head of the Iraqi state oil company, SOMO, suggested that Halliburton and its subsidiary, Kellogg, Brown & Root "are not actually accustomed to this business. They probably don't know the region well."⁸

A leading independent industry expert, Philip Verleger, said: "This sort of thing stinks. All of the products are available in the Gulf at spot prices around 70 to 80 cents per gallon. I know of no fuel purchasing organizations in the world . . . who can justify margins anywhere close."⁹ Another expert on the Middle East oil market, Walid Khadduri, the senior editor of the

⁵ Telephone conversation between John Bartenhagen, Director, Direct Delivery Fuels Unit, Defense Energy Support Center, and Minority Staff, Committee on Government Reform (Oct. 31, 2003). This price includes transportation from Kuwait to a base approximately 150 miles inside Iraq.

⁶ SOMO charges \$0.97 for gasoline imported from Turkey and \$0.96 for gasoline imported from Kuwait. Halliburton charges \$1.22 for gasoline imported from Turkey and \$2.65 for gasoline imported from Kuwait. Thus, part of Halliburton's overpayment is 20.5% of the \$218,180,907 spent for gasoline from Turkey, or \$44,727,086, and another part is 63.8% of the \$162,503,305 spent for gasoline from Kuwait, or \$103,677,109. Combined, Halliburton's total overpayment is \$148,404,195, compared to SOMO prices.

⁷ Telephone conversation between Jeffrey Jones, Director, Defense Energy Support Center, and Minority Staff, Committee on Government Reform (Oct. 31, 2003).

⁸ *New Information May Bolster Questions on Halliburton*, New York Times (Oct. 22, 2003).

⁹ *Price Revelation Threatens Halliburton's Gasoline Contract*, Octane Week (Nov. 10, 2003).

Middle East Economic Survey, said Halliburton's price is "way above market price and they have to justify that."¹⁰

In light of these facts, we request that you investigate and respond to the following questions:

- (1) Why is Halliburton charging such high prices to import gasoline into Iraq?
- (2) What are the terms of the contracts between Halliburton and its subcontractors for purchasing and transporting gasoline into Iraq?
- (3) Halliburton is importing gasoline from Turkey for \$1.22 per gallon. Why is there such a discrepancy between Halliburton's charges for importing gasoline from Kuwait and Turkey? Given this discrepancy, why is any gasoline being imported from Kuwait at vastly higher prices?
- (4) Who within the Defense Department and the Coalition Provisional Authority approved of Halliburton's charges?
- (5) What mechanisms are available to recoup funds overpaid under this arrangement?
- (6) Prior to contracting with Halliburton, what steps were taken to evaluate whether gasoline could be imported at lower prices? Specifically, what government agencies were consulted?
- (7) Did Halliburton violate any laws or regulations in the development and implementation of the fuel importation program? If so, which laws or regulations, and what sanctions are available?
- (8) Did Halliburton violate the terms of its contract with the Department of Defense in the development and implementation of the fuel importation program? If so, which provisions, and what sanctions are available?
- (9) Are government procurement officials, or other agency officials, at fault for the way the Halliburton fuel importation program was negotiated or supervised?

¹⁰ 2 in House *Question Halliburton's Iraq Fuel Prices*, New York Times (Oct. 16, 2003).

Use of Development Fund for Iraq

A significant portion of the funding used to pay Halliburton has come from the Development Fund for Iraq (DFI). According to the Corps's website, \$725 million from the Development Fund has been obligated to pay Halliburton for importing fuel into Iraq through November 18.¹¹ This and other questionable expenditures raise significant issues about how the CPA is administering these funds.

The Development Fund is the successor to the U.N.'s humanitarian Oil for Food Program, which was intended to provide for the basic needs of Iraqis while U.N. sanctions were in effect. U.N. Security Council Resolution 1483 formally transferred control of these assets to the CPA and placed them in the Development Fund. Under this resolution, the Development Fund received \$1 billion in assets from the Oil for Food Program on May 28. This money was supposed to be used "in a transparent manner to meet the humanitarian needs of the Iraqi people . . . and for other purposes benefiting the people of Iraq."¹²

To ensure that the Development Fund is administered appropriately, Security Council Resolution 1483 called for the creation of an International Advisory and Monitoring Board (IAMB) to oversee disbursements. The IAMB was to be comprised of four members representing the United Nations, the International Monetary Fund, the World Bank, and the Arab Fund for Social and Economic Development.¹³ The IAMB was intended as the primary vehicle for guaranteeing the transparency of the DFI and for ensuring that DFI funds are used properly.

¹¹ U.S. Army Corps of Engineers, *Frequently Asked Questions: Engineer Support to Operation Iraqi Freedom* (Nov. 18, 2003) (online at <http://www.hq.usace.army.mil/CEPA/Iraq/March03-table.htm>).

¹² United Nations Security Council Resolution 1483 (May 22, 2003). When the CPA assumed responsibility for these funds, it explicitly agreed to these terms. See Coalition Provisional Authority, *Memorandum No. 4: Contract and Grant Procedures Applicable To Vested and Seized Iraqi Property and The Development Fund for Iraq* (Aug. 19, 2003) ("As steward for the Iraqi people, the CPA will manage and spend Iraqi Funds, which belong to the Iraqi people, for their benefit [T]hey shall be managed in a transparent manner that fully comports with the CPA's obligations under international law, including Resolution 1483"). Although the CPA does not follow federal acquisition regulations, this memorandum also requires that contracts provide "the greatest value" to the CPA "based on price and all other factors." *Id.*

¹³ United Nations Security Council Resolution 1483 (May 22, 2003).

Unfortunately, the creation of the IAMB has been severely delayed as CPA's objections prevented the establishment of the IAMB for five months. Without an operational IAMB, there was no international auditor to ensure that Development Fund monies were being spent properly. Potential donor countries expressed dissatisfaction with the resulting lack of transparency and international involvement.

Several questions have been raised about specific uses of the Development Fund for Iraq. In previous letters, for example, Reps. Waxman and Dingell have questioned whether it was appropriate to use the Fund to pay inflated prices to Halliburton to import gasoline.¹⁴

Other questions have been raised about the use of the Fund to pay for items that clearly are not intended for humanitarian purposes. For example, the CPA is attempting to use the Development Fund to buy 34,000 AK-47 assault rifles and 14 million boxes of ammunition.¹⁵ Purchasing weaponry to arm Iraqis seems to directly contradict the intent of the Oil for Food program. While security problems in the country are profound, other funding sources are available for any necessary weapons purchases. It also makes little sense in a country where existing arms stockpiles are available.

Even Pentagon officials have raised concern with these purchases of weapons. Huge caches of existing AK-47s have been found and secured throughout Iraq, including a cache of 100,000 AK-47s found by the U.S. Marines near Tikrit.¹⁶ According to Capt. Jeff Fitzgibbons, the spokesman for the Joint Task Force that commands the military occupation in Iraq: "It would seem odd to me that we're out there looking to buy more weapons for a place where we've already captured and set aside so many of them. It would raise a red flag for me, that's for sure."¹⁷

In addition to obtaining funds from the former Oil for Food Program, the Development Fund also receives proceeds from the sale of Iraqi oil, as well as previously frozen Iraqi assets and Iraqi funds seized during the war. The CPA's use of oil profits is one area in which concern may increase as oil sales accelerate. To date, the CPA has awarded 143 projects worth several

¹⁴ See, e.g., Letter from Reps. Waxman and Dingell to Lt. Gen. Robert B. Flowers, U.S. Army Corps of Engineers (Oct. 21, 2003).

¹⁵ *Arms Plan for Iraqi Forces Is Questioned*, Los Angeles Times (Aug. 8, 2003); *The Struggle for Iraq: The Occupation; Companies Get Few Days To Offer Bids On Iraq Work*, New York Times (Oct. 19, 2003).

¹⁶ *Arms Plan*, *supra* note 15.

¹⁷ *Id.*

hundred million dollars. But by next year, the Administration predicts that oil revenues will reach \$12 billion.¹⁸ Because the CPA will have virtually unfettered control over how to spend this money, there is an urgent need for enhanced transparency and oversight.

Any misuse of funds in the Development Fund would be a serious matter. International skepticism about the management of the Development Fund threatens to undermine U.S. efforts to convince our allies to help fund Iraqi reconstruction and likely will increase mistrust of the Administration among Iraqis. For this reason, we believe an investigation by the Inspector General is crucial. We request that you examine the following questions:

- (1) What process did the CPA use to determine whether it was in the humanitarian interest of the Iraqi people to obligate \$725 million from the Development Fund to Halliburton for gasoline imports?
- (2) What process does the CPA use to ensure that Halliburton's gasoline prices are reasonable?
- (3) Is it appropriate for the CPA to use the Development Fund to purchase AK-47s and other weapons, particularly when captured weapons appear readily available?
- (4) Why did the CPA prevent the establishment of the International Advisory and Monitoring Board for five months? During that time, what international mechanism was available to provide transparency and accountability of the Fund?
- (5) What transparency and accountability measures is the CPA subject to in the expenditure of proceeds from Iraqi oil sales, frozen Iraqi assets, and Iraqi funds seized during the war?
- (6) What measures control the process by which the CPA spends Iraqi oil proceeds, frozen Iraqi assets, and Iraqi funds seized during the war?
- (7) Has the CPA complied with all applicable laws, regulations, and guidelines in spending Iraqi oil proceeds, frozen Iraqi assets, and Iraqi funds seized during the war?

¹⁸ *Struggle for Iraq*, *supra* note 15.

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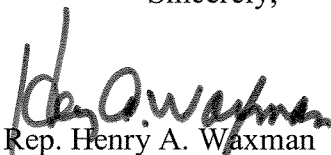
Conclusion

Transparency and accountability are essential if the efforts to reconstruct Iraq are to succeed. We hope you will help restore transparency and accountability to this process by undertaking the important investigations described in this letter.

Sincerely,



Senator Joseph Lieberman
Ranking Minority Member
Committee on Governmental
Affairs
U.S. Senate



Rep. Henry A. Waxman
Ranking Minority Member
Committee on Government
Reform
U.S. House of Representatives



Rep. John D. Dingell
Ranking Minority Member
Committee on Energy and
Commerce
U.S. House of Representatives