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TESTIMONY PRESENTING

MINORITY STAFF REPORT
ON
ILLEGAL SURCHARGES ON OIL-FOR-FOOD CONTRACTS
AND
ILLEGAL OIL SHIPMENTS FROM KHOR AL-AMAYA

*HEARING ON OIL FOR INFLUENCE: HOW SADDAM USED OIL TO REWARD
POLITICIANS UNDER THE UNITED NATIONS OIL-FOR-FOOD PROGRAM*

MAY 17, 2005

The Minority staff report complements the other Subcommittee staff reports released today and last week. Whereas those reports focus on allocation holders and purchasers of Iraqi oil, the Minority staff report examines what eventually happened to that oil – how so much of that oil got into the United States – and what the United States did to attempt to put an end to the illegal surcharge payments being demanded by Saddam Hussein. Additionally, the Minority staff report examines the largest single incident of oil being exported from Iraq by ship in violation of the U.N. sanctions—what is sometimes referred to as “the Khor al-Amaya shipments,” in reference to the Iraqi port where these shipments originated.

Illegal Surcharges

From September 2000 until September 2002, the Iraqi government demanded that purchasers of Iraqi oil under the Oil-for-Food program pay a per-barrel surcharge to the Iraqi regime. These surcharges were above the Official Sales Price (OSP) for Iraqi oil approved by the U.N., and were to be paid into accounts outside the control of the United Nations. These payments violated the U.N. sanctions on Iraq. The surcharge amount varied, from a low of 10 cents per barrel to a high of 30 cents per barrel. Detailed internal records kept by the Iraqi Oil Ministry’s State Oil Marketing Organization (SOMO) show that, during this period, Iraq collected about \$228 million in illegal surcharges.

Throughout this period, the United States was one of the largest customers of Iraqi crude oil, importing an average of about 660,000 barrels of oil per day, for a total of about 525 million barrels.

U.S. companies did not buy this oil directly from Iraq, but rather from oil traders, allocation holders, and various other “middlemen” that were unique to the Iraqi oil trade. Using SOMO records on surcharge amounts assessed and collected, and U.S. Energy Information Administration data on U.S. oil imports, the Minority staff estimates that about \$118 million in illegal surcharges were paid on Iraqi barrels of oil sent to the United States. That means that oil imported into the U.S. financed about 52 percent of the illegal surcharges paid to the Hussein regime. Oil destined for other countries accounted for about \$110 million in illegal surcharges, or about 48 percent of the total illegal surcharges paid. This information is depicted in this chart. These percentages roughly correspond to the percentages of Iraqi oil sent to the U.S. and elsewhere during this period.

With one notable exception, the Subcommittee Minority staff has not seen evidence showing that U.S. companies knowingly purchased oil on which a surcharge had been paid. U.S. companies buying Iraqi oil from traders typically included a clause in their contracts requiring the seller to warrant that no surcharge had been paid. However, other than this one notable exception, the Subcommittee Minority staff did not investigate whether any U.S. companies knowingly purchased oil on which a surcharge had been paid.

The notable exception involves a U.S. company called Bayoil. Bayoil is a privately held company headquartered in Houston, Texas, with affiliates in the Bahamas, Switzerland, and Luxembourg. During the surcharge period Bayoil was the largest provider of Iraqi oil for the United States. Bayoil provided about 200 million barrels to U.S. oil companies, or almost 40 percent of American imports of Iraqi oil during this period.

Our examination of Bayoil’s activities has found extensive evidence that Bayoil paid or financed illegal surcharges on Iraqi oil. Using Bayoil, Iraqi and other documents, we were able to trace the history of 102 cargoes of Iraqi oil that Bayoil purchased and imported into the United States. We found that, together, the illegal surcharges paid on those cargoes totalled at least \$37 million.

Documents obtained by the Subcommittee also indicate Bayoil knowingly participated in a trade boycott in violation of U.S. law. One of the Bayoil officers signed and notarized a statement attesting that Bayoil had never sold and would never sell oil to Israel. In interviews with Subcommittee staff, senior Hussein-regime officials currently in detention, including former Vice President Taha Yasin Ramadan and former Presidential Secretary Abid Hamid Mahmoud, confirmed that Iraq prohibited the purchasers of Iraqi oil from subsequently selling it to Israel.

We also found evidence that Bayoil persistently and openly lobbied U.S. and U.N. officials to influence the pricing of Iraqi oil and oppose U.S. efforts to address the surcharge problem by raising the official sales price. Bayoil also helped Iraq and Russia devise objections to U.S. and U.K. pricing proposals to stop the surcharges, and even on occasion drafted documents for Russian companies to send to U.N. officials protesting pricing policies that set Iraqi oil prices very close to world market rates.

We also found a significant contrast in the efforts of U.S. officials to stop the illegal surcharges. At the United Nations, U.S. and U.K. officials worked aggressively and creatively to develop pricing policies for Iraqi oil to prevent Saddam from imposing surcharges. After two years of effort, the United States and United Kingdom moved the United Nations to a so-called “retrospective pricing system,” which delayed setting a price on Iraqi crude until after the oil had been loaded onto the ships. This delay allowed the United Nations to set prices which closely reflected actual market prices and made it uneconomical for Iraq to also demand payment of a per-barrel surcharge. By September 2002, this system finally “squeezed out” the surcharges.

In contrast, at the same time the United States was making it harder for Saddam to impose illegal surcharges, the United States took only minimal steps to ensure that U.S. companies were not paying surcharges. In late 2000 and early 2001, the State Department and the Treasury Department’s Office of Foreign Assets Control—the office with primary responsibility for enforcing U.S. sanctions—informed U.S. oil companies that it would be illegal to pay any surcharges. Despite the knowledge that Saddam was continuing to impose surcharges on Iraqi oil, and that the U.S. was importing very large amounts of Iraqi oil, the State Department and OFAC took no additional steps to ensure no American companies were paying surcharges, or even to inquire about the nature of the trade in Iraqi oil.

U.S. authorities also failed to respond to requests by United Nations officials for assistance in obtaining information about potential sanctions violations by Bayoil. In early 2001, the U.N.’s Oil Overseers obtained information that Bayoil may have diverted to Europe shipments of Iraqi oil that the U.N. had approved for sale to North America. Shortening the final destination in this manner would have violated the sanctions and Bayoil’s U.S. license. It also would have earned Bayoil additional profits, which was of particular concern at that time because such profits could have been used as a source of funds to pay illegal surcharges.

In early June 2001, the U.N. Oil Overseers formally asked Bayoil to provide details about these shipments. Bayoil refused. The U.N. then requested the U.S. Mission to the U.N. to require Bayoil to provide the information, since Bayoil was a U.S. company. In mid August 2001, the State Department formally asked OFAC to obtain the information from Bayoil.

Meanwhile, the U.N. Overseers continued to demand that Bayoil provide them with a complete accounting of the shipments in question. Twice the Overseers threatened to inform the Security Council of Bayoil’s lack of co-operation. Each time Bayoil claimed the U.N. Overseers were prejudiced against them and refused to provide the information.

The U.N. again complained to the U.S. Mission to the U.N. In early 2002, the State Department again asked OFAC – informally it appears – to get the information from Bayoil. In late April 2002 – eight months after the State Department’s initial request – OFAC asked Bayoil to report on its licensed activities. In May 2002, Bayoil responded by stating that it had not engaged in any licensed activities since 1997. OFAC then telephoned Bayoil to ask permission to release Bayoil’s response to the State Department and the U.S. Mission to the U.N. In July 2002, Bayoil agreed on the condition that the response not be disclosed to anyone else, which presumably included the United Nations.

In the end, OFAC never provided Bayoil’s letter – which was non-responsive to the U.N.’s concerns in any event – to either the State Department or the United Nations. The U.S. government failed to provide the U.N. with any meaningful assistance, and the U.N. never obtained the requested information. Neither OFAC nor the State Department conducted any further inquiry into Bayoil’s role in the Iraqi oil trade.

Last month the Justice Department indicted Bayoil and its three principal officers for various crimes resulting from the payment of illegal surcharges to Iraq.

Illegal Khor al-Amaya Shipments

The Minority staff report also examines the Khor al-Amaya shipments. Over several weeks in February and March 2003, Iraq loaded 7 large oil tankers with a total of over 7.7 million barrels of oil at the port of Khor al-Amaya in southern Iraq, at the entrance to the Persian Gulf. These were the first loadings at Khor al-Amaya since the port had been damaged during the Iran-Iraq war in 1980. Iraqi oil exports from Khor al-Amaya were not authorized under the Oil-for-Food program and did not have U.N. approval. They constituted the largest single instance of an illicit oil shipment out of Iraq by ship during the sanctions period.

The oil tankers had been chartered by a Jordanian company acting on behalf of the Jordanian government. In exchange for the 7.7 million barrels oil, the government of Jordan wired over \$53 million in hard currency to the government of Iraq. Subcommittee interviews with high-ranking Iraqis currently in detention, including former Vice President Taha Yasin Ramadan, confirm that these shipments were authorized at the highest levels of the Iraqi government and the oil proceeds went to bank accounts under the control of the Hussein regime.

Each of the large tankers docked at the Khor al-Amaya terminal, filled its tanks with Iraqi crude oil, and then sailed for the port of Fujairah, in the United Arab Emirates, as shown on the second chart. Other shipping interests in the Persian Gulf who saw the oil tankers characterized the shipments as blatant violations of U.N. sanctions. Press reports raised questions about how the ships were able to travel the Persian Gulf with impunity.

U.N. inspectors and oil overseers interviewed by the Subcommittee stated they were surprised by the presence of the oil tankers. One U.N. oil overseer directly contacted the captain of the first ship to dock at Khor al-Amaya and told the ship it was carrying oil in violation of U.N. sanctions.

In contrast, shipping communications obtained by the Subcommittee indicate that U.S. personnel appear to have had advance warning of the shipments and allowed them to continue. These communications involve a ship's captain, some shipowners, the Jordanian company that chartered the 7 ships, and an American shipbroker which was also involved in some of the charters. These communications indicate the ships traveled with the full knowledge and acquiescence of the Maritime Interdiction Force (MIF), the naval force patrolling the Persian Gulf to prevent smuggling of oil from Iraq. The MIF was then under the command of a U.S. naval officer. The messages indicate, for example, that the Jordanians instructed their ship captains to contact Commander Harry French, a U.S. naval officer then assigned to the MIF, with the following message: "We are loading crude oil from the terminal at Khor al-Amaya for Millenium [the Jordanian company]: do you have any objection?"

Shipping records obtained by the Subcommittee and contemporaneous reports indicate the MIF officers never objected to any of these shipments. Instead, the MIF allowed the ships to pick up their cargoes and leave unfettered.

When objections were raised publicly to the Khor al-Amaya loadings, the U.S. company involved in chartering the ships for Jordan became concerned about the legality of the Khor al-Amaya shipments and decided to check with U.S. authorities to ensure that the company was not party to a transaction that violated U.S. law, U.N. sanctions, or U.S. foreign policy. The General Counsel for the company called the U.S. Commerce Department to discuss the shipments. He was eventually put in touch with an official from the State Department, Amy Schedlebauer. The General Counsel explained to her the circumstances of the shipments. Two hours later she called back and said, according to a contemporaneous email from the General Counsel describing the conversation, that her office was "AWARE OF THE SHIPMENTS AND HAS DETERMINED NOT TO TAKE ACTION." The General Counsel told her there was another shipment on the way, and the State Department officer "repeated the quoted response and would say no more."

It is not clear who instructed the State Department official to convey this information to the U.S. company, or who within the Department of Defense instructed Commander Harry French not to object to the Khor al-Amaya shipments. Despite written requests by the Subcommittee Chairman and Ranking Member, and repeated verbal requests from both Majority and Minority staffs for unclassified briefings, neither the State nor Defense Departments has provided any information on why the United States permitted these apparent violations of the Iraqi sanctions.

Thank you.