

OIL FOR FOOD

Security Council Resolution 986

14 April 1995

The Security Council,...

Convinced of the need as a temporary measure to provide for the humanitarian needs of the Iraqi people until the fulfilment by Iraq of the relevant Security Council resolutions, including notably resolution 687 (1991) of 3 April 1991, allows the Council to take further action with regard to the prohibitions referred to in resolution 661 (1990) of 6 August 1990, in accordance with the provisions of those resolutions,...

Acting under Chapter VII of the Charter of the United Nations,

1. *Authorizes* States, notwithstanding the provisions of paragraphs 3 (a), 3 (b) and 4 of resolution 661 (1990) and subsequent relevant resolutions, to permit the import of petroleum and petroleum products originating in Iraq, including financial and other essential transactions directly relating thereto, sufficient to produce a sum not exceeding a total of one billion United States dollars every 90 days for the purposes set out in this resolution and subject to the following conditions:

(a) Approval by the Committee established by resolution 661 (1990)...;

(b) Payment of the full amount of each purchase of Iraqi petroleum and petroleum products directly by the purchaser in the State concerned into the escrow account to be established by the Secretary-General for the purposes of this resolution; ...

8. *Decides* that the funds in the escrow account shall be used to meet the humanitarian needs of the Iraqi population and for the following other purposes, and *requests* the Secretary-General to use the funds deposited in the escrow account:

(a) To finance the export to Iraq, in accordance with the procedures of the Committee established by resolution 661 (1990), of medicine, health supplies, foodstuffs, and materials and supplies for essential civilian needs...;

(b) To complement, in view of the exceptional circumstances prevailing in the three Governorates mentioned below, the distribution by the Government of Iraq of goods imported under this resolution, in order to ensure an equitable distribution of humanitarian relief to all segments of the Iraqi population ...; ...

17. *Affirms* that nothing in this resolution affects Iraq's duty scrupulously to adhere to all of its obligations concerning servicing and repayment of its foreign debt, in accordance with the appropriate international mechanisms;

18. *Also affirms* that nothing in this resolution should be construed as infringing the sovereignty or territorial integrity of Iraq;...

MANAGEMENT OF THE OIL-FOR-FOOD PROGRAMME
VOLUME II - CHAPTER 3
THE SECURITY COUNCIL - RESPONSE TO SURCHARGES AND KICKBACKS

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This Chapter addresses two questions:

1. To what degree were the Security Council and its 661 Committee aware of Iraq's efforts to extract surcharges and kickbacks outside of the Programme?
2. What steps did the Security Council and its 661 Committee take to respond to reports and other information reflecting Iraq's effort to extract illegal payments from transactions under the Programme?

Part II of this Chapter reviews oil surcharges, and Part III reviews humanitarian kickbacks—as these issues arose before the Security Council and its 661 Committee. Although Iraq's schemes of manipulation varied over time, several common themes emerge:

- The awareness of Security Council members as early as 1998 of the likelihood that Iraq sought to extract side payments in connection with Programme transactions and confirmation of this Iraqi policy by late 2000;
- The constraints of the consensus rule of decision-making on the effectiveness of the Security Council and 661 Committee in their responses to reports of oil surcharges; and
- The general inattention of the Security Council and 661 Committee to reports indicating the payments of humanitarian kickbacks—from which Iraq ultimately derived far more in revenues than from oil surcharges.

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Iraq did not initiate its formal oil surcharge policy until late 2000—about three years after the start of the Programme.²⁸¹ But, as discussed below, the Programme had long been vulnerable to this kind of exploitation, in no small part because of the 661 Committee's inattention to its oversight powers. First, the 661 Committee failed to ensure an adequate number of oil overseers to monitor Iraq's oil transactions. Second, it failed to require or ensure that Iraq sell its oil to established end-users rather than to various middlemen companies. By November 1998, the prevalence of unknown middlemen buyers provoked public—and prophetic—reports that Iraq could one day exploit the Programme by extracting illegal side payments from oil buyers.

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The SOMO standard sales contract, with its end-user requirement, had been circulated among those involved in the negotiation of the Iraq-UN MOU in the spring of 1996, including Amstein Wigestrund—an oil expert who would later be appointed an oil overseer.³¹³ When interviewed by the Committee, Mr. Wigestrund recalled that the United Nations focused mainly on ensuring that oil was sold at a fair market price and that payments went into the escrow account. According to Mr. Wigestrund, the end-user requirement was relatively less important to negotiators for the United Nations, as the United Nations did not care who bought the oil so long as measures were in place to assure that the oil would be sold at a fair market price.³¹⁴

Accordingly, neither the Security Council nor the 661 Committee decided to condition the approval of oil sales on SOMO's end-user requirement. The 661 Committee's rules required the oil overseers to examine SOMO's oil sales contract for various provisions (e.g., use of a fair-market-value pricing mechanism approved by the 661 Committee and payment by way of a letter of credit to the escrow account). But the rules stood silent on an end-user requirement.³¹⁵

Iraqi Surcharge

Potential corruption of the Programme surfaced in mid-November 1998 with the publication of an article in *Platts Oilgram News*—one of the world's leading oil industry publications. The article stemmed from a review of the approved Iraqi oil prices, which reflected that Iraqi oil was underpriced and therefore allowed for the possibility of kickback payments to the Iraqi regime. Prior to publishing this article, the author had confirmed his suspicions that pricing was too low with Mr. Lorenz, who recently had retired as an overseer; Mr. Lorenz told the author that, in November 1998, oil sold by Iraq under the Programme was below fair market price. When

In any event, after Mr. Kramar's refutation of the *Platts* article, the issue went no further within the United Nations. Curiously, there was no effort made to contact Mr. Lorenz to discuss the concerns he had voiced in the article. Nor is there any indication that the United States or OIP forwarded the article to all other members of the 661 Committee or that the article otherwise surfaced before the 661 Committee.³²⁸

Faced with this rejection of its request for payment of a surcharge from the Programme, Iraq resorted to a covert surcharge policy. The media soon reported that Iraq was advising its oil purchasers to pay a surcharge of fifty cents per barrel of oil outside the United Nations escrow account and that Iraq was pressing the United Nations to allow it to sell oil at a lower price in order to allow its customers a greater profit margin from which to pay the surcharge upon reselling the oil.³³¹

On December 13, 2000, all three overseers advised the 661 Committee of information they had received substantiating the existence of Iraq's surcharge policy. Mr. Tellings remarked that some buyers had confirmed the surcharge requests and had put their reports in writing. Mr. Buur-Jensen said that he did not have "letters indicating precisely how much of a surcharge was being asked," but that "sufficient information had been received in various forms from those in the process of purchasing oil to enable him to state that surcharges were in fact being requested." Mr. Kramar advised that based on reports of other buyers it "appeared to be true that [one company] had refused to pay a surcharge" and that "[o]ther vessels currently waiting to load had also been requested to pay a surcharge but so far none had done so."³³⁷

With respect to whether Iraq was receiving surcharges, the overseers noted that “end-users can consistently only buy Iraqi crude oil at a premium of 20–50 cents per barrel” over the official selling price. Whether this premium was used to pay surcharges was stated to be “unknown to the Oil Overseers,” and SOMO “categorically denied the allegations.” But the overseers noted that “direct contacts with traders and end-users in the oil industry confirm in broad terms what has been written in the professional press on this matter.”³⁴⁶

The overseers further noted that the current pricing conditions had led to a dramatic decrease in oil sales revenue for the Programme. Since the beginning of December 2000, Iraq had foregone “at least 100 millions barrels of export volume,” resulting in approximately \$2.2 billion in lost revenue for the Programme.³⁴⁷

At a formal session on February 26, 2001, the overseers again briefed the 661 Committee. Mr. Buur-Jensen once more stated that SOMO denied the receipt of surcharges, but he added that “information received from the oil industry and the professional press would seem to confirm it.” He stated that “[t]he low export levels in December and January were attributable to excessive premiums that had discouraged purchasers.”³⁴⁸

At the February 26 meeting, neither Russia nor any other members of the 661 Committee expressed doubt about whether Iraq was requiring oil buyers to pay surcharges. The course of future discussion therefore turned to what remedial steps the 661 Committee should take. But, as detailed below, the 661 Committee could not reach consensus on how to proceed.

In August 2002—nearly a year after the advent of retroactive pricing—Russia presented a proposal to reconsider retroactive pricing and, in doing so, acknowledged that Iraq, in fact, had an oil surcharge policy. Its representative stated that surcharges “had been imposed because Iraq’s need to offset the cost of maintaining its oil industry had been ignored for many years.” He stated that:

The current situation, which had been confirmed to the Russian Federation in contacts with Iraqi representatives in Baghdad, was that Iraq would be prepared to abolish surcharges immediately if the Committee was finally able to solve two key problems affecting the humanitarian programme: ending retroactive pricing, and approving the cash component for the oil industry.

Russia therefore proposed to accept the Iraqi conditions so that “[t]he surcharges so often discussed would disappear, and Iraqi oil could be extracted and exported under normal conditions.”³⁴⁹

Despite these admissions by Russia before the 661 Committee, the Government of Russia has continued to this day to question whether Iraq had an oil surcharge policy. Russian Foreign Ministry officials steadfastly have maintained during the course of repeated interviews with the Committee that there is a lack of evidence that Iraq imposed oil surcharges.³⁴⁷

Humanitarian Kickbacks

In 2000, Iraq’s practice of extracting humanitarian kickbacks from goods suppliers was first mentioned at a Security Council meeting and at a formal meeting of the 661 Committee. On March 24, 2000, the United States raised numerous concerns in the Security Council about the Government of Iraq’s conduct relating to humanitarian aspects of the Programme. Specifically,

Although the United States had presented a non-paper on humanitarian kickbacks in March 2001, and the 661 Committee subsequently met formally and informally to address kickbacks, there was only minimal discussion of this issue. Then, after the relative flurry of attention in spring 2001, the 661 Committee did not resume discussions regarding humanitarian kickbacks until after the war in Iraq (in 2003), in relation to the transitioning of responsibility for the Programme to CPA, which is discussed in the next Section. In fact, the last mention of humanitarian kickbacks at a formal 661 Committee meeting, before the war, was merely an oblique reference in a discussion of port fees on April 5, 2001.⁴⁶⁶

During the approximately thirty formal meetings after this reference, the 661 Committee did not further discuss the United States proposals regarding humanitarian kickbacks. Indeed, the 661 Committee did not even discuss the existence of humanitarian kickbacks or strategies to combat them. Likewise, during this time period, the Security Council did not discuss the issue of humanitarian kickbacks in its formal or informal meetings. A United Kingdom official stated that there was “little appetite for further discussion” of humanitarian kickbacks because the Security Council was concentrating on broader political issues such as the revised sanctions policy and implementation of the goods review list. Moreover, the official stated that “after September 11, 2001 happened, politics changed,” and there was a focus on disarmament and inspections as well as retroactive pricing.⁴⁶⁷

In any event, prior to the war in Iraq, the 661 Committee never reached consensus on whether Iraq was seeking and goods suppliers paying humanitarian kickbacks—let alone what if any action the 661 Committee should take. As demonstrated above, the meeting records provide little assistance in understanding reasons for the 661 Committee’s inaction on kickbacks. However, in the Independent Inquiry Committee’s discussions with government officials, a number of interrelated themes emerged, including: (1) lack of proof; (2) absence of company complaints; (3) focus on dual use; (4) reliance on OIP to address pricing; and (5) disagreement on the appropriateness of investigation.