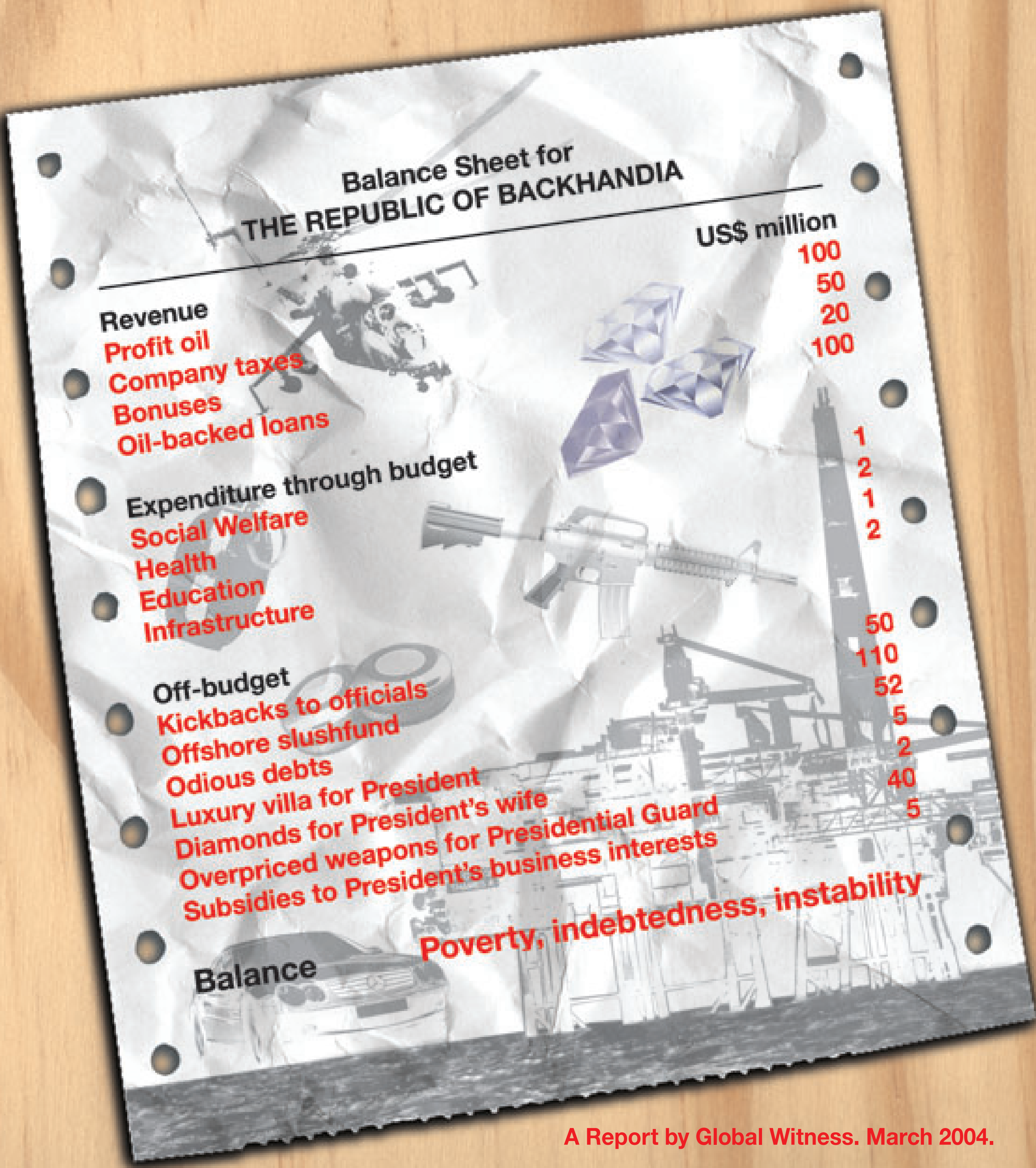
global witness

Time for Transparency

Coming clean on oil, mining and gas revenues



A Report by Global Witness. March 2004.

Contents

Global Witness investigates and exposes the role of natural resource exploitation in funding conflict and corruption. Using first-hand documentary evidence from field investigations and undercover operations, we name and shame those exploiting disorder and state failure. We lobby at the highest levels for a joined-up international approach to manage natural resources transparently and equitably. We have no political affiliation and are non-partisan everywhere we work. Global Witness was co-nominated for the 2003 Nobel Peace Prize for our work on conflict diamonds.

Summary for Policymakers

What is the problem?

- Governments of resource-rich developing countries often do not provide information about their revenues from natural resources, nor do multinational extractive companies publish information about payments made to the governments of those countries. Such opacity hides billions of dollars worth of financial impropriety, as this report reveals.

Why does it matter?

- Ordinary citizens, the real owners of natural resources, are left without the information to call their governments to account over the management of their revenues. Dispossessed, they are often left marginalized and at the mercy of donor assistance. In Angola, for example, one in every four oil dollars earned goes missing. At the same time, one in four Angolan children dies before the age of five from preventable diseases.

In countries like Equatorial Guinea, the oil is offshore and so are the revenues. Credit: Robert Grossman/Africaphotos.com

- Businesses see their legitimate revenues misappropriated and squandered and are left vulnerable to accusations of complicity with corruption and its attendant reputational risk. Crooked elites can extract all sorts of 'facilitation payments' from firms that would probably prefer not to pay bribes.
- States that mismanage resources may fail, forcing the international community to give more aid, and creating instability that threatens the supply of vital industrial commodities.

What can be done?

- All resource-rich developing countries and resource extraction companies should actively participate in the UK government's Extractive Industries Transparency Initiative and seek to voluntarily disclose their revenues from resource extraction. However, voluntary disclosure will not work everywhere that transparency is most needed because many political and business elites have a vested interest in avoiding transparency to protect their illicit profits.
- A set of joined-up policies is needed to make resource extraction companies publish what they pay to governments on a country-by-country basis and to make host governments publish what they earn.
- Simple adjustments to existing policies of company disclosure, 'books and records' provisions in anti-corruption legislation, and international accounting standards can be used to require multinational companies to 'publish what they pay'.
- Export credit agencies, bilateral and multilateral bodies, and banks should make all their lending and insurance conditional on governments publishing their receipts from resource extraction.
- International financial institutions like the World Bank should mainstream revenue transparency across their lending and technical assistance portfolios by making it a condition of all their financial support and by including it in their national poverty reduction strategy consultations.

This approach is fully consistent with, and a stepping-stone towards, international objectives of promoting accountable government, democratic debate over resource management, and ensuring energy security through a more sustainable operating environment.

Revenue Transparency:
A Priority for Good Governance and Energy Security

Across the globe, revenues from oil, gas and mining that should be funding sustainable economic development have been misappropriated and mismanaged. This Global Witness report considers five major examples of this problem: Kazakhstan, Congo Brazzaville, Angola, Equatorial Guinea and Nauru.

In these countries, governments do not provide even basic information about their revenues from natural resources. Nor do oil, mining and gas companies publish any information about payments made to governments. Huge amounts of money are therefore not subject to any oversight and crooked elites can extract all sorts of 'facilitation payments' from firms that would probably prefer not to pay bribes. Investigations also reveal that some companies have played a willing role in facilitating off-the-books payments, misappropriation of state assets, and other nefarious activities such as arms shipments, as part of an anti-competitive, under-the-table method of winning business with unaccountable regimes. Ordinary citizens, who often own a country's resources under its constitution, are thus left without the information to call their governments to account over the management of their revenues. The end result is a litany of corruption, social decay, increased poverty, reinforcement of authoritarian government and political unrest, which can ultimately lead to state failure and the spread of instability across regions.

In **Kazakhstan**, the largest-ever foreign corruption investigation in US legal history has uncovered a major international corruption scandal that 'defrauded the Government of Kazakhstan of funds to which it was entitled from oil transactions and defrauded the people of Kazakhstan of the right to the honest services of their elected and appointed officials'.[1] The scheme was based around Kazakh President Nursultan Nazarbayev and Oil Minister Nurlan Balgimbayev demanding that international oil companies such as Chevron (now Chevron-Texaco) and Mobil (now ExxonMobil) pay a series of unusual fees to middleman James Giffen on behalf of the Republic of Kazakhstan. This arrangement, the indictment alleges, helped Giffen to skim money from the deals and send some US$78 million in kickbacks to President Nazarbayev and others through dozens of overseas bank accounts in Switzerland, Liechtenstein and the British Virgin Islands. Only Giffen is charged in this indictment. Another US$1 billion of Kazakh oil money has also been uncovered offshore and out-of-sight under Nazarbayev's direct control in a secret fund in Switzerland. Ironically, the only reason that such information has emerged is because President Nazarbayev inadvertently revealed the true state of affairs whilst trying to discredit a presidential rival.[2]

Congo Brazzaville is one of the petro-states most closely associated with the legacy of influence peddling and dirty deals in Africa by the now-notorious French state oil company Elf Aquitaine (now Total). Elf treated Congo as its colony, buying off the ruling elite and helping it to mortgage the country's future oil income in exchange for expensive loans. The company even financed both sides of the civil war, as it also did in Angola.

Although former senior Elf officials have been jailed in France for 'misuse of company assets', their legacy of opacity and hair-raising accounting endures. Despite huge existing debts and a supposed programme of cooperation with the international community to restructure Congo's finances, the government has entered into ever more arcane and tortuous deals to avoid financial scrutiny from the international community and its own citizens. Indeed, the national oil company *Société Nationale des Pétroles du Congo* makes a multi-million dollar profit but, according to the IMF, does not pay a single penny of this money into the government's coffers.

In **Angola**, new evidence from IMF documents and elsewhere confirm previous allegations made by Global Witness that over US$1 billion per year of the country's oil revenues – about a quarter of the state's yearly income – has gone unaccounted for since 1996. Meanwhile, one in four of Angola's children die before the age of five and one million internally-displaced people remain dependent on international food aid. This report highlights the latest revelations from the 'Angolagate' scandal, in which political and business elites in France, Angola and elsewhere exploited the country's civil war to siphon off oil revenues. Most recently, evidence has emerged in a Swiss investigation of millions of dollars being paid to President Dos Santos himself. The government continues to seek oil-backed loans at high rates of interest which are financed through opaque and unaccountable offshore structures. A major concern exists that Angola's elite will now simply switch from wartime looting of state assets to profiteering from its reconstruction.

In **Equatorial Guinea**, oil companies appear keen to do business with the brutal regime of President Obiang Nguema. The country's government has been tarnished by allegations of corruption, political violence, human rights abuses, and narcotics trafficking. Although the country's oil boom has resulted in a dramatic increase in GDP, its living standards remain among the worst in Africa. This may be because much of the country's oil money stays abroad: journalists have recently uncovered evidence that major US oil companies are paying revenues directly into an account under the president's control at Riggs Bank in downtown Washington DC.

Riggs Bank has also managed the purchase of million-dollar mansions for Obiang and his family. The line between state revenues and the president's personal finances seems unclear. The government maintains that it is completely open and transparent about its oil revenues but, so far, the only way that any information has entered the public domain is when it has been dragged there by the international media.

Finally, the opaque and unaccountable management of phosphate reserves has transformed tiny **Nauru** from the richest nation in the world (per capita) to a bankrupt wasteland. Phosphate mining took place in a country synonymous with secret banking and money-laundering, where over US$80 billion was laundered during Russia's economic transition in the 1990s. In this tax-free, reporting-free environment, the island's phosphate revenues were squandered by irresponsible officials, frivolous speculation, and in the words of one observer, 'a steady stream of carpetbaggers and outright crooks'.[3] The money has now dried up. Bankrupt, in social and political turmoil, and facing possible extinction from rising seawaters, Nauru is a sinking ship.

The major finding of this report is that none of the revenue embezzlement scandals discussed herein could have happened if multinational companies had been required to disclose publicly their basic payments for resources to the state.

More generally, transparency in the management of revenues from natural resources is fundamental for successful development and poverty reduction. Oil, mining and gas are critically important economic sectors in about 60 developing or transition countries.[4] Amongst the 3.5 billion people in those countries, some 1.5 billion live on less than US$2 per day and constitute over two-thirds of the world's poorest people. Twelve of the world's 25 most mineral-dependent states and six of the world's most oil-dependent states are classified by the World Bank as Highly Indebted Poor Countries with amongst the world's worst Human Development Indicators.

The status quo in the resource extraction business is a lose-lose situation for all parties:

- **Businesses** see their legitimate revenues paid to governments being misappropriated and squandered, which leads to social divisiveness and an unstable business environment. Investors managing some US$6.9 trillion of funds recently highlighted the significant business risk represented by lack of transparency, stating that: 'legitimate, but undisclosed, payments to governments may be accused of contributing to the conditions under which corruption can thrive'. Failing to disclose net payments not only lays companies open to 'accusations of complicity in corrupt behaviour'; it also undermines their social 'license to operate', making them 'vulnerable to local conflict, and insecurity, and possibly compromising their long-term commercial prospects in these markets'.[5] A recent example of these problems is the continuing unrest in Nigeria's oil region which has led to significant interruptions in oil output.

- **Ordinary citizens**, who often are the real owners of the resources, are left dispossessed and reliant on donor assistance.

- **Taxpayers in the North** are required to compensate for state failure in the South in the form of aid: this is inefficient and undermines the current donor emphasis on improving governance in non-transparent countries.

- **The international community** faces instability that, in some cases, directly threatens the security of energy supplies. Current policies of energy security seem to rely on leaving failed and failing states alone whilst the resources keep flowing out. The lessons from this report are that this approach does not work: initial problems with accountability are left to become fatal flaws in a state's whole architecture, eventually causing a collapse that interrupts resource flows and renders states vulnerable to infiltration by criminal and terrorist groups.

The international community has taken its first steps towards recognising the importance of improved transparency and accountability of natural resource revenues, but its proposed solutions are neither efficient nor comprehensive. UK Prime Minister Tony Blair and his Department for International Development have convened a forum called the **Extractive Industries Transparency Initiative** (EITI) to promote action by governments and companies on this issue. Whilst the EITI has done some valuable work, including identifying the main revenue streams in the resource extraction business and developing a series of templates for collecting data, it remains poorly resourced and relies purely on voluntary reporting by companies and governments. The 2003 declaration of the G8 summit in Evian similarly highlighted a voluntary approach to promoting transparency in the extractive sector.

This voluntary approach will not work in the majority of countries where it is most needed. The massive financial improprieties uncovered in this report show that political and business elites currently have a vested interest in avoiding transparency. Indeed, when BP wanted to disclose payments in Angola, it immediately faced the threat of losing its licence to less scrupulous competitors. If disclosure was required by law, it would void 'gagging clauses' in licence agreements with some governments that prevent disclosure and would thus avoid the problem of companies being penalised for breach of contract. Disclosure of key financial data is required by law in every developed country, so why should it be different in Angola and other developing economies?

To that end, the **Publish What You Pay** coalition of more than 190 Northern and Southern NGOs is calling for legislation to require extractive companies to disclose their payments to all governments. This crucial first step would help citizens in resource-rich-but-poor countries to hold their governments to account over the management of revenues. In addition, by creating a level playing field through regulation, companies' reputational risks will be mitigated and they will be protected from the threat of having contracts cancelled by corrupt governments.

The last section of this report looks at the pressing need for international regulations and a systematic foreign policy approach to promoting revenue transparency. International stock markets and accounting standards should require oil, mining and gas companies to disclose their payments worldwide. A requirement for transparency about a country's resource income and expenditure should become a standard condition in all international financial assistance to all countries where such transparency does not exist. Transparency should also be a condition of resource-backed loans from private banks. Export credit agencies, which insure many major extractive investments, should also require disclosure of revenues.

The monitoring of revenues could be improved by amending the operational parameters of the World Bank and the IMF to mainstream revenue transparency across their lending and technical assistance portfolios, by making it a condition of all aid and loans, and national poverty reduction strategy consultations.

The public disclosure of revenues by extractive companies and governments in resource-dependent countries will not stop all corruption overnight. But without transparency, there can be no accountable government, and efforts to ensure that resource revenues are well spent are likely to fail, with the effect of deepening poverty, instability, conflict and state failure. It is time for companies and governments to come clean on the revenues generated by natural resource exploitation.

The price of opacity: one in four of Angola's oil dollars is unaccounted for, and one in four of its children dies in infancy.

Credit: J.B. Russell/Panos Pictures

Kazakhstan

Kazakhstan is a major Caspian Sea oil producer. Credit: A. Ustinenko/Patker/Still Pictures

Money unaccounted for: US$1.1 billion from the 'Kazakhgate' scandal and a massive presidential 'secret fund' in Switzerland.

Introduction

In early 1993, the newly independent Republic of Kazakhstan drew up two crucial agreements: its first national constitution and its first oil contract with an American company, Chevron (now ChevronTexaco). In the decade since, Kazakh President Nursultan Nazarbayev has tried to amend both to suit his personal ambition. Altering the constitution has not proven problematic for him – Nazarbayev now rules, essentially, by decree – but Chevron was less than pleased with his desire to rewrite the terms of the 40-year, US$20 billion deal that bought it a large share of the massive Tengiz oil field. The spat was resolved after the Bush administration stepped in to protect the interests of US oil companies.

Nazarbayev was wise to back down: this section details the 'Kazakhgate' scandal in which the President and others became enormously rich profiteering from the entry of multinational oil companies into Kazakhstan in the mid-1990s. This story, coupled with the demise of Kazakhstan's fledgling democracy, the deteriorating human rights situation of its citizens, revelations of a billion-dollar secret government account in Switzerland, and the largest foreign corruption case in US history that has resulted from Kazakhgate, make a compelling rationale for improved transparency and accountability from both corporations and host governments.

If companies had been obliged to publish their payments to the Kazakh government, it is unlikely that the system of kickbacks and offshore money laundering detailed below could have come into being. The lack of transparency during contract negotiations was so complete, in fact, that the Kazakhgate scandal was only uncovered as a result of a disastrous miscalculation by President Nazarbayev himself.

Kazakhgate

Kazakhstan, a former Soviet republic and geopolitical linchpin in central Asia, possesses some of the largest oil and gas reserves in the world.[1] Chevron's 1993 purchase of a half-share in Kazakhstan's massive Tengiz field made it an early entrant into Kazakhstan's post-Soviet economy. Containing some six billion barrels, Tengiz is believed to be the world's fifth largest deposit of crude oil.[2] One retired Chevron executive termed it 'a geologist's dream'.[3]

Once it became apparent how enormous the reserves were at Tengiz, other European and American companies became increasingly desperate to get involved. Yet by 1996, only one other company – Mobil (now ExxonMobil) – succeeded in purchasing a share. It seems that it did so without taking part in any formal bidding process.

How did they land the deal? Enter two American citizens who have since become subject to criminal proceedings in the US for their involvement in these deals: former Mobil executive J. Bryan Williams III and independent merchant banker James Giffen. Williams pleaded guilty in June 2003 to evading taxes on more than US$7 million in unreported income, including a US$2 million kickback he received in connection with Mobil's business in Kazakhstan.[4] 'I knew what I was doing was wrong and unlawful', Williams admitted.[5] Whilst he admitted to conspiring with others, Williams declined to disclose any names. Giffen's case, at the time of writing, has yet to go to trial. Meanwhile, international investigations into the role of other parties continue.

Plenty of oil, but little transparency.
Credit: John McDermott/Panos Pictures

Back in the mid-1990s Williams was a high-flying oil broker for Mobil, specializing in crude purchases on the spot market. Giffen, who was apparently president of the US-USSR Trade and Economic Council in the 1980s, had long-standing ties with the Kazakh leadership and became a special advisor to President Nazarbayev shortly after the latter took office in 1991. Giffen founded a private banking company, Mercator, headquartered in New York, which the Kazakh government subsequently hired to negotiate deals with foreign oil companies.

Giffen's indictment by a Grand Jury in New York alleges that he set up a scheme that 'defrauded the Government of Kazakhstan of funds to which it was entitled from oil transactions and defrauded the people of Kazakhstan of the right to the honest services of their elected and appointed officials'.[6] The alleged scheme was based around Nazarbayev and Kazakh Oil Minister Nurlan Balgimbayev demanding that the oil companies pay Mercator's fee on behalf of the Republic of Kazakhstan, an odd arrangement that, the indictments allege, helped Giffen to skim money from the deals and distribute largesse.

After Mercator helped Chevron buy into Tengiz in 1993, for example, it received a 'success fee' of US$0.75 for every barrel of oil that Chevron pumped there.[3] Given that it was the Republic of Kazakhstan that retained Giffen's services, it seems odd that Chevron should pay him such a bonus. Furthermore, there is a law in the United States called the Foreign Agents Registration Act that requires anyone who acts as an 'agent of a foreign principal'[7] to register with the Justice Department but, according to a detailed study of his activities in the *New Yorker* magazine, Giffen did not.[3] Neither Giffen nor Mercator are currently registered in the latest listings (for 2002).[8] In the mid-1990s, US Ambassador to Kazakhstan William Courtney reportedly urged Giffen to comply, though the New Yorker also reported that Giffen denied having the conversation with Courtney.[9] Courtney's successor also expressed misgivings about Giffen's failure to register.[3]

According to the US Grand Jury Indictment against Giffen, Mercator received roughly US$67 million in such success fees between 1995 and 2000.[10] During the same period, the indictment records that Giffen also caused approximately US$70 million, paid by oil companies into escrow accounts at Swiss banks for oil and gas rights in Kazkahstan, to be diverted into secret accounts under his control. Out of the success fees and the funds diverted by oil companies, the indictment alleges that Giffen made unlawful payments of more than US$78 million to two very senior officials of the Kazakh government dubbed 'KO-1' and 'KO-2'.

The indictment itself does not mention who these officials are but says that they had the power to influence substantially whether Mercator obtained and retained lucrative business with the Kazakh government. KO-1 is, in fact, then-oil minister Balgimbayev, whilst KO-2 is President Nazarbayev himself. Their identities have been confirmed by numerous observers and can be checked by cross-referencing the US indictments with mutual legal aid requests and Swiss court documents relating to the matter.

For example, the Grand Jury indictments specify that KO-1 was the owner of an account called Orchard Holdings into which money was diverted.[11] Swiss court filings obtained by Global Witness detail Balgimbayev's legal appeal against the freezing of assets in the Orchard account by a Swiss magistrate in June 2000. Balgimbayev is therefore identified as the owner of Orchard and hence KO-1. Similarly, the Giffen indictment alleges that the Semrek Foundation, which owned one of the recipient companies of diverted funds called Orel Capital, was secretly owned by 'KO-2 and his heirs'.[12] Swiss court documents state that Nazarbayev was the beneficiary owner of Semrek and, hence, KO-2.[13]

From Vaeko to Tengiz

Mobil's Williams appears to have negotiated with Giffen in order to secure access to Tengiz for the company, knowing that, as one US State Department official stated, he 'seemed to have a stranglehold on almost all oil and gas contracts'.[9] With Giffen's help, Mobil entered into two contracts related to Kazakhstan in July 1995.

The first of Mobil's contracts described above was a preliminary agreement with the Kazakh government that gave Mobil the right to negotiate a share in Tengiz, for which Mobil paid a US$5 million 'advance' to Mercator. The second deal was more complex: Mobil entered into an agreement to finance an 'assetless shell company' called Vaeko Europe in its purchase, transport, processing, and sale of condensate (a liquid form of natural gas) from Kazakhstan to a refinery in Orenburg across the Russian border.[14] According to the *New Yorker*, even Mobil's in-house lawyers would come to conclude that the Vaeko deal was intended to smooth the company's path into Tengiz and not a profitable venture in its own right.[3] The indictment against Giffen also describes the deal as 'an effort to induce Kazakhstan to close the deal in Tengiz'.[14]

As all pipelines from Kazakhstan went through Russia at the time, Russian influence on the Kazakh oil sector and its future projects was significant; and, as it turned out, the Russians needed help. An ageing refinery owned by the family of a former prime minister had been left without gas supplies by the collapse of the Soviet regime.[3]

Giffen recruited the aid of business colleague Friedhelm Eronat, who controlled Vaeko Europe.[15] The US indictments specified that the plan was to use Vaeko as a vehicle for cash that Williams would supply from Mobil to fund the transfer of condensate from the Kazakh gas field of Karachaganak to the refinery in Russia. The processed fuel would be returned, Mobil would receive a small fee from condensate sales and Vaeko would reap all remaining profits. The indictments describe this deal in its most basic terms as an unsecured loan to Vaeko for which Mobil assumed all risk and was entitled to no profit beyond the set fee from the sales.[16]

But Vaeko did not repay Mobil and the latter booked a loss of tens of millions of dollars.[17] Millions of dollars of Kazakh customs revenues also seems to have been lost on the deal as the processed material appears to have been sent on to Europe rather than being re-imported to Kazakhstan. A set of official Kazakh customs documents provided to Global Witness calculated the loss of revenue to the Kazakh government to be almost US$42 million.[18] That this state of affairs was allowed to continue suggests high-level sanction for the deal on the Kazakh side of the border.

Kazakh customs documents from 1996 identifying significant losses to the treasury from condensate exports.

Not everybody appears to have lost out, however. According to the US court indictments of Giffen and Williams, US$1.1 million was transferred from Vaeko's bank account into a secret Swiss account controlled by Giffen in March 1996. The latter subsequently wired US$1 million to the account of Balgimbayev's Orchard account. Subsequently, Balgimbayev allegedly used the money to purchase over US$180,000 worth of diamond jewellery and a spa vacation for his family.[19]

Back in Fairfax, Virginia, Mobil's financial analysts may have become concerned with the reported losses from the deal Williams had struck. When challenged, however, Williams assured his colleagues that Mobil President Lucio Noto had approved the deal and explained that 'the Russian mafia had got hold of the money.[3] Mobil's lawyers investigated and eventually concluded, according to one internal summary, that 'Mobil had long-term projects and interests – Tengiz – in mind when it entered this transaction'.[20]

The Kazakh government was certainly aware of Mobil's relationship with Vaeko. Global Witness has obtained a copy of Vaeko's contract with the government dated 17 February 1995, in which Balgimbayev approved the sale of five million tons of gas condensate to Mobil and its 'agent' Vaeko Europe.

Document signed by oil minister Balgimbayev that highlights a close working relationship between Vaeko and Mobil.

In the autumn of 1995, Lucio Noto flew Giffen, Nazarbayev and a few senior Mobil executives to the Bahamas via corporate jet to talk about Tengiz.[3] By 5 April 1996, however, negotiations had stalled. Williams was dispatched to restore goodwill and on 9 April 1996, Mobil was awarded a 25% share in Tengiz.[21]

In a report filed with the US Securities and Exchange Commission announcing the Tengiz purchase, Noto is quoted as saying that: 'Mobil is delighted to have obtained 25% of the Tengiz field given that there was a substantial amount of competition from other major companies'.[22] This comment about competition seems odd because, although other companies were clearly interested in getting into Tengiz, Global Witness sources have consistently highlighted the absence of any formal bidding procedures for the 25% stake.[23] A former Chevron executive told the *New Yorker* that Kazakhstan's willingness to let another American company buy into the field without competitive bidding was a surprise to industry insiders because European companies were also very interested in the stake.[3] This raises important questions about the basis on which Mobil was chosen.

The *New Yorker* reported that, at the meeting in the Bahamas, Nazarbayev made extraordinary requests, including a Gulfstream jet, tennis courts at his home, and satellite trucks for his daughter's television network.[3] Mobil apparently declined these demands, but nevertheless had to hurdle two other unusual requests before landing a stake in Tengiz: that Mobil directly pay Mercator's fees that were due from the Kazakh government, and that Mobil pay them on top of the asking price for the field.

Mobil over a barrel

According to the indictment of Williams, during the initial negotiations over Tengiz, the Kazakh officials insisted that Mobil pay the fees the Republic of Kazakhstan owed to Mercator for its services in brokering the deal. The Williams indictment states that: 'Mobil executives raised questions about the propriety of the arrangement and expressed concerns regarding whether [it] would violate the Foreign Corrupt Practices Act'. Williams vouched for Giffen, the indictment adds, and Mobil eventually agreed to pay the fee.[24]

The other key adjustment to Mobil's original position was that, contrary to their prior arrangement, Mobil would now pay Mercator's 5% fee – some US$51 million – *on top* of the purchase price. Given Nazarbayev's requests for an aeroplane and tennis courts, and given their previous concern over the legality of the fees, Mobil officials might reasonably have guessed there was a real risk of impropriety on the Kazakh side.

The Williams indictment put the value of Mobil's purchase at US$1.05 billion. Yet in its May 1996 filing with the US Securities and Exchange Commission, Mobil announced that it had acquired a 25% share of Tengiz for US$1.1 billion. This US$50 million difference is almost exactly the amount that Mercator was paid. It is hard not to conclude that Mobil therefore included its payment to Mercator, a fee that was not paid to the government of Kazakhstan, in the contract amount reported to the SEC. If this was the case, then it follows that Mobil was in effect treating the unusual payments to middlemen as just another cost of doing business in Kazakhstan. Requiring companies to disclose their net payments to national governments would, of course, have detected these unusual side-payments.

Between 3 August 1995 and 17 May 1996, Mobil wired a total of US$51 million into Mercator's account at Citibank in New York, inclusive of the US$5 million goodwill payment mentioned earlier.[25] The indictments describe how more than half of that money was immediately funnelled out of Mercator's account to the accounts controlled by various parties to the deal.

Some US$25 million passed through the account of a Swiss company called Nichem controlled by a person labelled in the indictments as 'Co-Conspirator One (CC-1)'. Information contained in legal assistance documents passed to Global Witness reveal that CC-1 is, in fact, Vaeko boss Friedhelm Eronat.[26] Nichem directed millions into the account of Hovelon Trading, a company based in the British Virgin Islands and controlled by Giffen with the help of an unidentified individual referred to in the indictment as 'Co-conspirator Two (CC-2)'. Hovelon then wired US$20.5 million to a Swiss account in the name of Orel Capital Ltd, a company beneficially owned by Nazarbayev and his heirs.[27] Nazarbayev spent this money on, amongst other things, some US$45,000 of fees for an exclusive Swiss boarding school for his daughter.[27]

According to the indictments, there were numerous similar transactions over a period of several years. Some US$2 million was deposited in the account of Alqi Holdings, an offshore company belonging to Mobil's Williams.[28] Other beneficiaries included Balgimbayev via his Orchard account, which received payments totalling more than US$10 million between August 1997 and April 1999.[29]

According to the indictment, the person who set up the bank accounts and managed money on behalf of Giffen and others was an employee of French bank Credit Agricole Indosuez (CAI), named as 'Co-conspirator Three (CC-3)'.[30] The *Wall Street Journal* quoted 'people familiar with the matter' as saying that CC-3 is Jean-Jacques Bovay, a senior manager at the Geneva branch of CAI who has since left the bank. The newspaper quoted its sources as alleging that Bovay was paid millions of dollars for his services. Bovay's lawyer declined to comment to the newspaper on this allegation.[31] An American request for legal assistance in investigating 'Kazakhgate' also identified Bovay's involvement in moving money for Mercator for 'Financial Advisory Services for the Republic of Kazakhstan'.[32]

Mobil and the middlemen

Giffen has subsequently been charged with wire fraud and/or violating the US Foreign Corrupt Practices Act for his role in the above transfers, save that to Williams' Alqi account, which was a payment between two private American citizens and therefore not proscribed by law. Williams is charged only with tax evasion on that money.[33] Giffen now faces up to 88 years in jail and fines of more than US$84 million.

Mobil has yet to face any charges, although the Justice Department is seeking extensive information over its transactions with Giffen and others.[34] Justice Department investigations have also widened to take in at least one other major oil company. ChevronTexaco was subpoenaed in April 2003 to appear in court in New York, and to hand over any documents relating to its dealings with President Nazarbayev, Balgimbayev, Giffen, Eronat, Bovay, and other individuals and companies.[35] The company has said all its payments to Kazakhstan were 'properly made' and complied with US and local laws.[36]

In June 2003, Williams changed his plea to guilty on the charges of tax evasion, acknowledging that he received payments from unidentified 'people, organisations and governments' with whom he did business on Mobil's behalf.[37] He did not say why he had been paid, nor did he disclose any connection between these payments and his business at Mobil.

It is difficult to believe that Williams was unaware that Giffen would distribute largesse to others given that he would receive a kickback from Mercator himself. At best, Williams was an employee willing to talk his company into making an irregular payment to a middleman on behalf of a foreign government, and he appears to have received a large reward for his ingenuity.

Mobil – ExxonMobil since the 1999 merger – claims that Giffen was 'an official representative of the Kazakh government and therefore a legitimate conduit for concessions payments'.[38] However, it remains unclear whether Giffen had registered as a representative of a foreign government and one might expect a company as prominent as Mobil to check that the middlemen with whom it does business are operating in compliance with the US Foreign Agents Registration Act before sending tens of millions of dollars into their accounts.

It is also hard to understand why Mobil did not take more vigorous action to oversee the activities of Mercator, Giffen and Williams given the outrageous demands alleged to have been made by Nazarbayev in his meeting with Noto. Assuming the innocence of everyone at Mobil, the company should nonetheless exercise better supervision of executives authorised to grant payments of tens of millions of dollars and to negotiate deals worth more than a billion dollars.

A written request from US investigators for assistance from the Swiss authorities, obtained by Global Witness, indicates that Mobil was concerned about a risk of impropriety by its employees and had some knowledge of CAI's Jean-Jacques Bovay.[39] According to the request, Mobil discovered that one of its employees had taken out an unauthorised loan of US$11 million from CAI and in April 1997 notified Banque Indosuez that Bovay was 'familiar with the circumstances surrounding the transaction'. Mobil repaid the loan and closed the CAI account.

The request goes on to note that in March 1998, Mobil contacted Yves Capian, the Chief of General Inspection at CAI, and advised him that it was 'conducting a confidential internal review of certain commercial activities that may have adversely affected Mobil'.[39] The areas under review included: '1) unauthorised payments to third parties; 2) possible diversion of funds to unidentifiable offshore entities; and 3) possible money laundering transactions'.

As all these three points featured in the indictments, it is hard therefore to avoid the conclusion that Mobil's probe may have concerned the Mercator case and Kazakhstan. Since no Mobil executive has been charged with these crimes, it can only be assumed that the investigation came up empty. Worryingly, Mobil once again began to do business with Kazakhstan through CAI only a month later (see next section). It may be only coincidence that about this time, according to the *New Yorker*, Williams quietly retired from Mobil at the age of 58.[3] He was subsequently appointed the US government's overseer of the UN's Iraqi Sanctions Committee.[40]

Same system, different companies?

Mobil was not the only oil company to play into the hands of Giffen, Nazarbayev, and Balgimbayev. In other transactions investigated by the US Justice Department, oil companies looking to secure exploration and production-sharing deals with the government of Kazakhstan made huge deposits into escrow accounts at CAI with the understanding that the bank would distribute the funds to pay the 'fees of certain advisors to Kazakhstan', including Mercator.[41] None of the oil companies involved have been charged for their role in these unusual procedures.

In early 1997, Amoco paid US$51 million into such an account, while Texaco was part of a consortium that wired US$17 million to CAI in November of 1997. In April 1998, a group of international companies including Mobil paid US$23 million of a US$175 million 'signature bonus' into a CAI escrow account at the direction of the Kazakh leadership. Later that year, at Balgimbayev's instruction, Phillips Petroleum directed US$30 million of a US$277 million purchase into another escrow account at CAI.

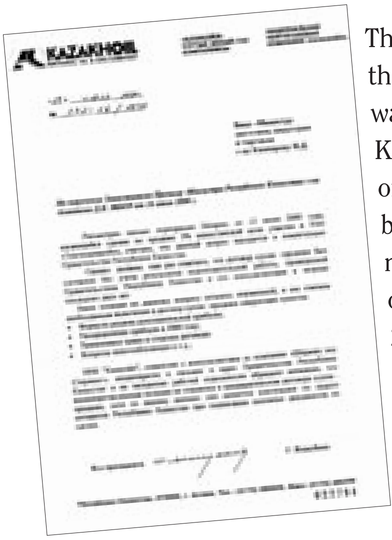
Amoco's money appears to have been siphoned away courtesy of what the indictment describes as a 'sham agreement' between a company affiliated with CAI and the Kazakh leadership, facilitated by Giffen.[42] In the other instances, Nazarbayev and Balgimbayev entered into an 'exclusive paying agency agreement' with CAI, which directed huge fees to the bank for the privilege of doing business there. Of Texaco's US$17 million, for example, over US$11.4 million was retained by CAI as a 'fee'.[43]

The Giffen indictment then describes how this fee was shunted to private beneficiaries: Nazarbayev's Orel received US$5 million, Balgimbayev's Orchard Holdings banked US$2.5 million and a private company called Condor – named as belonging to Giffen in his indictment – was sent some US$2 million.[44] As the Giffen indictment describes, a secret agreement 'disguised the fact that almost 90% of CAI's purported fee was being paid to Giffen and, through Giffen, to Kazakh officials and Giffen himself'.[44]

The indictment also names CC-3, who Global Witness believes to be Jean-Jacques Bovay, as being involved in 'a paper record making it appear that those funds would be used to pay Kazakhstan's consultants on the transaction and then diverted a large percentage of the funds in escrow through a series of secret Swiss accounts into secret accounts beneficially owned by senior Kazakh officials and Giffen himself'.[45] Swiss investigators have subsequently announced a probe into the role played by Bovay and whether he personally received any payments from the Kazakh transactions.[46]

None of the oil companies can be accused of directly knowing that the money they poured into escrow accounts would end up in the pockets of Kazakh officials, bank employees or James Giffen. However, it remains unclear what due diligence and risk mitigation took place, especially given the curious arrangement by which companies like Amoco and Mobil paid consultancy fees to Mercator on behalf of the government of Kazakhstan. The Williams indictment alleges that Mobil did this in spite of concerns about possible US Foreign Corrupt Practices violations when Williams, who benefited personally from the transactions, vouched for Giffen.[47] If Mobil had been obliged to disclose its payments to Mercator on behalf of the Kazakh government, it might have mitigated the risk of such conflicts of interest and protected its reputation more effectively.

It is also reasonable to ask why companies were content to deposit such huge sums owed to the government of Kazakhstan into various accounts held in Switzerland rather than with Kazakhstan's national bank or its official treasury accounts. It is striking that a mere month after Mobil wrote to the Chief of General Inspection at CAI advising him of its internal review of bank transactions and possible diversion of funds to unidentifiable offshore entities and money laundering transactions, the Giffen indictment reported that Mobil was part of a consortium that paid US$23 million of a signature bonus into an escrow account at the bank at the direction of Balgimbayev.[48] The indictment also alleged that US$11 million of that money was subsequently retained as a fee by CAI, of which US$10 million was siphoned off to Balgimbayev, Giffen and Nazarbayev.[48]


KAZAKHOIL

The lack of transparency in the brokering of oil deals was so extreme that Kazakh government officials were often blocked entirely from the negotiating process. In one letter dated 21 July 2000 and leaked to Global Witness, the acting president of state oil company Kazakhoil lamented that the sale of an additional 5% share of Tengiz to Chevron that year was closed 'without consideration of the preparatory work completed by the Government of the Republic of Kazakhstan and its consultants [including major US law firm Sherman and Sterling] during the last two years'.[49]

In the letter, the company president requests that the contract be changed to reflect 'key positions defending the interest of the Republic of Kazakhstan', which had been left out. One wonders whose interests, exactly, were defended in the contract as it was drawn up between Chevron and the Kazakh leadership.

How Nazarbayev 'shot himself in the ass'[50]

The system of money-laundering and bribes maintained by Nazarbayev, Balgimbayev, Giffen and others, as described by the indictments, appears to have been so extensive that investigating magistrates in Switzerland identified as suspicious between 50-60 accounts in at least four different banks. In 2000, Swiss officials froze the assets of several accounts that the US indictments would later describe as 'secret accounts beneficially-owned by senior Kazakh officials' including Nazarbayev and Balgimbayev.[51]

In fact, their transgressions only came to light because of a spectacular blunder on the part of Nazarbayev. Hoping to pillory Akezhan Kazhegeldin, a political opponent who was once prime minister, Nazarbayev asked Belgian bank officials to search for illegal assets in accounts that may have been held by Kazhegeldin.[52] The Belgian investigators found none, but they did uncover accounts benefiting other Kazakh officials. They referred the investigation to Swiss officials who subsequently notified the US Justice Department of James Giffen's involvement in the transfers to Kazakh officials. Kazhegeldin claims to have phoned Nazarbayev and taunted him for inadvertently revealing his own accounts with the words: 'you shot yourself in the ass!'.[50]

By 1999, the pressure was on and legal investigations had also begun in the US. In August, Nazarbayev transferred US$84 million out of his Orel account at CAI and into a new account at Banque Pictet, established as the official property of the Republic of Kazakhstan.[53] Shortly thereafter, Balgimbayev's wife and children moved out of the house in Massachusetts that had been bought by a front company owned by Balgimbayev and funded by oil money.[54] Investigators were uncovering a host of private benefits, including the matching 'his and hers' snowmobiles Giffen had sent Nazerbayev and his wife and the oil money that the President used to pay for his daughter's Swiss boarding school.[55]

President Nazarbayev isn't so open about his finances.

Credit: Despotovic Dusko/Corbis Sygma

Crackdown at home

The lavish lifestyle of those Kazakhs reported in the indictments contrasts sharply with the appalling intimidation and violence directed at those within the country who are trying to investigate Kazakhstan's missing money.

As investigations advanced in 1999, Nazarbayev created a Law on Confidential State Affairs placing 'disclosure or publication of information about the president and his family and their economic interests or investments into the realm of state secrets punishable by severe sanctions'.[56] He installed his daughter as head of the state television channel and signed a law requiring that all channels air at least half their broadcasts in the Kazakh language, a blow to commercial stations since half of their audience speaks Russian rather than Kazakh. Transmission of one news programme on Kazakhstan's NTV channel reporting a *New York Times* article about the secret Swiss accounts was pulled off the air in mid-sentence.[57]

A series of brutal attacks have also occurred on Kazakh journalists investigating Kazakhgate. On 6 May 2002, Irina Petrushova, chief editor of *Respublika*, an opposition newspaper that had written extensively about the scandal, was sent a funeral wreath with the script, 'Dear Irina Petroshova, from colleagues'. On 19 May, a headless dog was tied to their office window with a note attached by a screwdriver stabbed into the animal informing her that

The dead dog and burnt-out office were warnings to a journalist who wrote about the Kazakhgate scandal. The note says: "There won't be a next time."

'There won't be a next time'. Petrushova later found the dog's head on the doorstep of her home. On 22 May, the office was burnt to the ground.

Journalist Lira Baysetova, who lost an eye after being beaten by unknown assailants in 1997, published an interview with a Swiss official confirming that Switzerland had frozen the accounts of Nazarbayev and two former prime ministers in the opposition paper *Soldat* in 2002. The next day, her daughter went missing and the newspaper's offices were destroyed by fire. Three weeks later, she was informed that her daughter had been arrested for drug possession and a few weeks after that she was told that her daughter had died while in custody. International human rights groups have since voiced suspicions about the circumstances of the girl's death.[58]

On 28 October 2002, the night before flying to the US to give a series of talks about political conditions in Kazakhstan, freelance journalist Sergei Duvanov was arrested for allegedly raping a minor. He has lost two appeals, despite clear evidence of an egregious miscarriage of justice: an unpublished report by the Organisation for Security and Co-operation in Europe (OSCE), obtained by Global Witness, found 'serious procedural violations' and concluded that the investigation had not been full and objective, and the evidence presented in court was not sufficient to reach a conclusion.[59] Duvanov had previously been attacked by knife-wielding assailants outside his home.[60]

Today, there is no independent television station in Kazakhstan and little independent press. In the words of Irina Petrushova: 'without exception, every single independent journalist and editor who has published a report opposing the government has had criminal charges brought against him or her'.[61] The government also requires all news-related websites to register with the authorities. Another account states that although 'nobody officially dictates to journalists what they should write, and there is no ban on criticism ... everyone who takes that path knows what the consequences may be'.[62]

Nazarbayev was quick to defend himself politically as well. In June 2000, he got parliament to give him life-long immunity from prosecution. He also eliminated the presidency's term limits and its mandatory retirement age and granted himself the right to ban any political party.

In the summer of 2001, a month-long legal window was opened during which money could be repatriated from overseas accounts and deposited in Kazakh banks, with no taxes charged and no questions asked. The President's ability to make full use of this law himself may have been constrained by the fact that many of his overseas accounts had been frozen at the time. Another measure of protection, according to radio reports, was the 'scheduled destruction of all tax records between 1995 and 2000'.[63]

By 2002, Swiss and American officials were exchanging information and ten years of Mercator's files had been subpoenaed. Nazarbayev had his Washington lawyer address a letter to the US Justice Department, which stated, 'I am deeply concerned that foreign relations between the US and the Republic of Kazakhstan—an important ally in the war on terrorism with significant oil and gas reserves in an unstable geographic region—will deteriorate if prosecutors maintain their pursuit of the documents in Kazakhstan and continue to aggressively investigate Kazakh officials'.[64] It is no longer a secret that one of those 'Kazakh officials' was Nazarbayev himself.

The billion-dollar secret fund

The most startling revelation of the whole affair was yet to come. The pressure of the investigation, and the fact that Switzerland was becoming a perilous place for Kazakh officials' secret accounts, led to a stunning announcement in parliament in April 2002 by new Prime Minister Imangaly Tasmagambetov: he stated that in 1996, the Kazakh leadership had created a top-secret Swiss account, under Nazarbayev's direct control, to hold a US$1 billion payment made for an oil contract that year. Exactly which contract was not made clear but it is most likely to have been the other US$1 billion from the Mobil deal because of the timing.

Tasmagambetov went so far as to say the fund had saved Kazakhstan's independence: 'The head of state was left with no other choice except to take all responsibility upon himself. That was when the appropriate decree was signed on the secret fund as a reserve fund of the government in the event of economic crisis or a threat to the security of the country. I emphasize that the President acted exclusively in the interests of the country and within the framework of the laws of the Republic of Kazakhstan.'[65]

Tasmagambetov also distinguished between the secret fund and the foreign bank accounts allegedly belonging to Nazarbayev, saying that if such accounts exist, they were set up by other people to compromise the President's name.[65]

The account had supposedly been tapped twice, once for US$800 million to shore up pension funds and once to help stabilize the currency after the devaluation of the Russian rouble.[66] Tasmagambetov said the remaining amount would be transferred back into a new national fund within Kazakhstan.

However, budget transparency was so poor that it has been impossible to determine whether the 'secret fund' was in fact used as Tasmagambetov said it had been. The World Bank might wonder, for example, why Nazarbayev did not use the fund in 1999 (when it supposedly still contained US$200 million) rather than taking out a World Bank loan of US$300 million to finance pension reforms.[67]

To this day, Kazakhstan's rulers have never clearly identified where all this US$1 billion went, nor have they explained why the President himself unilaterally decided that he was the most appropriate person to control a huge slice of Kazakhstan's oil money out of sight of his parliament and his public, nor exactly how this unusual approach to money management fits within the framework of Kazakhstan's laws. The Kazakh Constitution, for example, requires in Article 54(2) that parliament 'approve the republican budget, the reports of the Government, and Estimation Committee about its implementation, and introduce changes into the budget'.

Tasmagambetov stated, by way of explanation, that 'in 1996, it would have been complicated for parliament to make this law about the National Fund themselves'.[68] Similarly, the Kazakh Deputy Minister of Information has gone on the record to argue that information about the secret account had not been shared with parliament because 'it would have elicited many questions'.[69]

So, many questions

One may admire the candour of a government that admits to hiding a billion dollars overseas in order to avoid questions from its parliament and people about what it is doing with public money. It is one of the main aims of the *Publish What You Pay* campaign not only to generate such questions but also to ensure, through revenue transparency, that they can be answered.

The US$200 million left in the secret fund was transferred back to Kazakhstan to form part of an official National Fund for oil and gas revenues that was created in August 2000. Other major deposits in the National Fund have included some US$660 million from the sale of a 5% share in the TengizChevroil consortium – which, as mentioned earlier, took place without any supervision – and some 10% of taxes paid by the nine largest oil companies and three largest mining companies operating in the country. The latest information available is that the National Fund now contains assets in excess of US$2 billion.[70]

Although day-to-day bookkeeping of the National Fund's assets rests with the National Bank of Kazakhstan, almost every line of control rests solely with Nazarbayev. He has the exclusive right to make and change the rules that govern the Fund as well as to authorize its expenditure. He also determines the Fund's supervisors.[1] While the

The Tengiz pipeline in Kazakhstan. Credit: A. Ustinenko/Patker/Still Pictures parliament receives reports about the Fund's activities, there are no rules specifying the content of these reports or the dates for their submission. More importantly, parliament has no authority to approve, reject, or amend these reports. No guidelines exist on what constitutes permissible expenditure and what limits exist on spending. Just as the Fund was created by presidential decree, so it can be scrapped at Nazerbayev's whim.

Outside the National Fund, the government's income and management of oil revenues is equally opaque. The chairman of Kazakhstan's national bank is on the record as saying that information about how much money remains in government accounts abroad is a 'state secret'.[71]

Kazakhstan's national oil and gas company, KazMunaiGaz, whose holdings include a 20% stake in the Tengiz oil field, is not subject to the accountability and reporting requirements expected of publicly traded companies or elected officials. It operates behind a veil of secrecy, with no public disclosure requirements.

Transfer pricing – the practice of transferring goods on paper to offshore accounts in order to elude taxes – is also rife. The tax havens of Bermuda and the British Virgin Islands were ranked in 2000 as Kazakhstan's second and third largest trading partners behind Russia, mostly receiving oil.[72] Such operations may cost the state an estimated US$1 billion per year of the US$4 billion tax income due to it.

Perhaps the biggest question that remains is: 'what went wrong?' The weekly paper *Argumenty i fakti Kazakhstan* touched on the irony of Kazakhstan's oil boom when it reported as an April Fool's joke that a new decree would divide the state's earnings from hydrocarbon development equally among Kazakhstan's adult population. 'This means that every citizen of the country who has come of age at the moment the decree is issued will receive, according to some calculations, $200,000 with monthly dividends on top!'[73]

The arithmetic may be questionable but the point is clear: ordinary Kazakhs have not seen the benefits to which they are entitled. Instead, some 40% of the population are classified as living in poverty and a quarter of the nation lives on less than US$4 a day.[74] Overall, the number of people in poverty has doubled since independence.

The rest of the world has a strong interest in doing business with Kazakhstan, as evidenced by the plans of international oil companies to invest at least US$37 billion in the country over the next 40 years.[75] But there is a strong need to establish clear ground rules for doing business in such environments. A government making the transition to a capitalist economy is under enormous pressure to create an economic environment that is both functional and fair, but it cannot succeed with either goal without the help of the massive international companies that create markets.

The American oil companies referenced in the Giffen and Williams indictments provided capital that was needed by Kazakhstan but they also consented to highly unusual payments to middlemen and deposited huge amounts of money into accounts at Swiss banks. Since Nazarbayev appears intent on eliminating the ability of his fellow citizens to investigate and expose corruption at the highest levels, the obligation of oil companies doing business with Kazakhstan to maintain strict ethical standards is all the more significant.

In this context, revenue transparency from multinational companies is a neat and efficient solution. If companies had been required to publish what they pay openly, then neither the Kazakhgate embezzlements nor the billion-dollar secret fund could have been kept secret. The fact that the commissions to Giffen and others were reported as a cost of doing business makes the case for systematic disclosure even clearer: Kazakh citizens and authorities, had they been aware of this information, would have had details about payments that oil companies thought they were making to the government that had not made it through to the Kazakh treasury. Mobil's reputation inside and outside of the country might not have suffered so much collateral damage from events if it had openly disclosed that information to Kazakhstan's people and to the relevant national authorities.

Given the Kazakh government's decision to deliberately destroy official tax records, it is now impossible for Kazakh citizens to know how much money should have gone into their treasury. This would not be the case if oil companies were required to publish details of their payments to the government. Similarly, brave Kazakh journalists would not have been killed, beaten up or judicially framed while attempting to uncover the dealings of a corrupt ruling elite. It is unacceptable that the world should find out what was paid – and into whose pockets the money went – only because Nazarbayev inadvertently laid bare his own finances while trying to eliminate a political rival. We cannot rely on the diminished judgment of the corrupt to enforce transparency and legality.

Congo Brazzaville

War in Brazzaville: the real price of Elf's African strategy? Credit: Le Segretain Pascal/Corbis Sygma

Money unaccounted for: currently, about US$250 million per year.[1]

The Republic of Congo (Congo Brazzaville) is one of several African states where oil wealth has left a legacy of corruption, poverty and conflict. This section looks at the way Congo's development has been stymied by the unaccountable management of oil revenues, beginning with the ugly history of French state oil company Elf Aquitaine.

A huge court case in France recently provided unprecedented details of Elf's opaque and anti-competitive 'African Strategy'.[2] The company systematically paid kickbacks, peddled influence and encouraged government indebtedness in order to maintain its control over the oil of several African countries. Elf's strategy institutionalised opacity and led to unaccountable government, massive debt and chronic instability.

Perhaps no country suffered more than Congo Brazzaville, the fourth-largest oil producer in sub-Saharan Africa.[3] Once one of the richest states in Africa, Congo now has the highest per capita debt in the world: according to the International Monetary Fund (IMF), Congo's external debt is US$6.4 billion or over twice the country's GDP, while the government itself puts total debt at US$11.5 billion.[4] One-third of government income goes to service oil-backed debt – that is, loans from private sources that are secured against future oil production. One World Bank report cites 'mismanagement of the country's rich natural resources' as the primary factor fuelling the violent conflict that has claimed thousands of lives in the country.[5]

Elf had an enormous amount at stake as the dominant oil company in Congo Brazzaville, where oil receipts today account for around 70% of the country's income and 90-95% of its exports.[6] Elf's proprietary interest in Congo Brazzaville led it not only to feed corruption, but also to meddle with elections, encourage massive indebtedness and, worst of all, to fund both sides in the 1997 civil war. Elf's successor, the private-sector TotalFinaElf (now Total), remains a major player in Congo: in 2002, it still accounted for around 70% of the country's oil production.[7] Transparency is still desperately needed in Congo, as this section will outline. Recent negotiations between the Congolese authorities and Total show that the tradition of secrecy surrounding oil income continues under the government of Denis Sassou-Nguesso, autocratic strongman turned elected president.

Many Congolese citizens are bitterly aware that oil has not benefited them, its owners, and a resurgent civil society has begun to demand more accountability. In 2002 Congolese church leaders wrote in an open letter to their president: 'The Congolese people do not know much about how much our country receives from this black gold, and even less about how the revenues are managed. What it does know is the price of oil is measured not in barrels or dollars, but in suffering, misery, successive wars, blood, displacement of people, exile, unemployment, late payment of salaries, non-payment of pensions.'[8]

Given its huge debts, Congo is understandably keen to join the IMF's Heavily Indebted Poor Countries Initiative (HIPC), which offers massive debt relief in return for policy reforms agreed with the IMF and the World Bank. However, its oil earnings continue to be managed unaccountably, especially the operations of the national oil company *Société Nationale des Pétroles du Congo*, undermining the promises on improved transparency that the government has made to the IMF and others. The Sassou-Nguesso government cannot be allowed simply to take the IMF's money and run.

The message of the Elf affair is clear: if the company had been obliged to disclose its financial relationship with the Congolese government, there is no way that its 'African Strategy' could have worked. At the same time, if the government had managed its oil income accountably, Congo might not be reeling economically, politically and socially from the crushing burden of debt and war.

Elf's legacy in Congo

The trial of 37 former senior executives of the now-defunct Elf, for 'misuse of company assets' to the tune of hundreds of millions of dollars, ended in Paris in mid-November 2003 with the conviction of 30 of the accused.[9] The 600-page indictment listed allegations of corrupt behaviour by top Elf officials including siphoning-off commissions into secret bank accounts, buying multi-million dollar properties and expensive jewellery and embezzling money for divorce and alimony fees.[10] The penalties handed down included fifteen prison sentences, seven suspended sentences and heavy fines. Loïk Le Floch-Prigent, former chief executive of Elf, was given a five-year sentence and a US$471,000 (€375,000) fine; Alfred Sirven, his right-hand man, was also sentenced to five years and fined US$1.25 million (€1 million); and André Tarallo, former Director for Africa and of Hydrocarbons was given four years and a US$2.5 million (€2 million) fine.[11]

But this is not just another corporate fraud scandal. The indictment alleged that the accused took advantage of the pre-existing 'Elf system',[12] whereby the company paid African decision-makers from offshore accounts to maintain its powerful market position in several countries. There was nothing illegal under French law about the largesse distributed by Elf at the time, and the Paris trial looked only at allegations of misuse of the company's own assets by individual employees.

Prosecuting judge Renaud Van Ruymbeke aimed to show that the Elf system was used as a '*pompe à finance*'[13] (cash cow) that effectively transferred revenues from public to private hands. To make this case, the prosecution provided extensive details about how offshore structures were set up to buy off African leaders, by diverting signature bonuses (one-off payments) and '*abonnements*' (money skimmed from oil sales) into personal accounts. These leaders were also encouraged to take out oil-backed loans that enriched 'the secret funds of Elf'.[14] In Congo, this created conditions of unaccountable government and direct indebtedness to the company that progressively secured Elf's hold on the country's politics.

The three top Elf executives who were convicted in the trial enjoyed particular influence in Congo. Loïk Le Floch-Prigent was Elf's chief executive between 1989 and 1993. Alfred Sirven held the catch-all title of *Directeur des Affaires Générales* (Director of General Affairs), and André Tarallo, known as 'Mr Africa', was a former president of Elf's subsidiary, Elf Congo. André Tarallo admits to acting as Elf's 'secret financier' until 1989, a role he testifies was then taken over by Sirven.[15] His role was to liaise with 'existing heads of state' whilst Sirven developed contacts with opposition leaders.[16] The secret payments and oil-backed loans began in the early 1970s but the company's

Convicted: Elf's Tarallo, Sirven and Le Floch-Prigent. Credit: AFP/Getty Images involvement in Congolese affairs reached its peak during the political upheaval of 1990-1992, when dictator Denis Sassou-Nguesso was replaced by the democratically-elected president Pascal Lissouba.[17]

The Elf System in Africa had three main components:

- **Bonus Payments**. These were the most basic element of the system. According to Tarallo's testimony, they usually ranged from US$1 to US$5 million but sometimes exceeded US$10 million.[18] Tarallo testified that two payments of US$10 and US$25 million for Congolese offshore permits were directed into accounts controlled by Lissouba,[19] and a bonus of US$4 million was paid to Congolese Minister of Oil Koukebene.[20] Jack Sigolet, in charge of finances for Elf's African subsidiaries from 1978-1985, was not among the accused.[21] He testified to several bonuses of sums ranging from US$3-5 million.[20] In addition, testimony in the indictment suggests that Sassou was rewarded for, for instance, providing Elf with an introduction to José Eduardo dos Santos, President of neighbouring Angola.[22] Elf's activities in Angola are examined in the next section of this report.

- ***Abonnements***. *Abonnements* – literally 'subscriptions' – are described in the indictment as ongoing payments tied to oil sales.[23] They were funded by the company's sales subsidiary Elf Trading under-invoicing the crude oil it bought from African subsidiaries by selling the oil with an average mark-up of US$0.20 per barrel and placing US$0.40 per barrel into Liechtenstein-based trusts in Elf's name. These trusts then transferred funds into offshore accounts held by Congolese leaders.[24] The indictment identifies several accounts, structured under a trust called 'Iserco', that it claims were used between 1989 and 1992 to transfer some US$64.8 million into the pockets of Congolese decision-makers.[25]

- **Oil-Backed Loans**. While bonus payments and *abonnements* rewarded decision-makers for favouring Elf, Le Floch-Prigent, has stated on the record that the aim of Elf's oil-backed loans was 'to balance the accounts of the producer states, to allow them generally to pay civil servants' salaries and avoid revolts'.[26] It could be argued, however, that the actual result was short-termism in the government's financial management and the collapse of the state's formal accounting structures, which were supplanted by a haywire system of offshore accounting.

  Jack Sigolet, Elf's financial wizard, claims the oil-backed loan system was 'conceived in such a way that the Africans were only aware of the official lending bank and were ignorant of the whole system which Elf rendered particularly and deliberately opaque'.[27] Loan money followed a circuitous route and behind the scenes the company was itself profiting directly from it.

  Sigolet testifies that Elf would set up a company, usually in Switzerland, and then either lend money to it at a low interest rate or guarantee a loan to it from another source. The Swiss-based company would then lend the money at a higher interest rate to a bank that would, in turn, lend it – at a much higher mark-up – to Congo.[28] Cash-rich Elf was able to borrow at low interest rates but Congo, in Sigolet's words, had to 'put up with' much higher rates because of its indebtedness.[29] It is hard to avoid the conclusion that Elf knowingly capitalised upon, and thus increased, Congo's indebtedness because it was profiting from the difference between these interest rates.

  A portion of each loan was held back as 'syndication rights', which amounted in practice to free cash for the company and its allies in the African state. On a two-year, US$100 million loan, these fees would be worth around US$3 million.[30] According to Sigolet: 'Generally, the amount that went to the authorities of the African state (head of state, minister for oil or of finance or advisor) could reach around US$700,000. They had offshore accounts to receive the money. The remaining US$2.3 million were transferred into an Elf-controlled account in Switzerland or Liechtenstein.'[30]

Elf found yet another way to make money off these loans through its 40% stake in the Banque Française Intercontinentale (FIBA). FIBA, 'at the crossroads'[31] of Elf's relations with African states, was the main vehicle for dispensing Elf's largesse. It was created in 1975 by Omar Bongo, president of Gabon and Sassou-Nguesso's son-in-law, with Elf's Jack Sigolet serving as its president until 1996.[32] Several African nations opened government accounts at the Paris branch of FIBA, into which royalties and taxes were paid. According to the indictment, key players also had personal accounts there, among them Bongo and Sassou-Nguesso.[33]

The Elf indictment states that when he came to power, Lissouba opened a personal account, the funds for which came partly from the Congolese Ministry of Finance account at FIBA, into which oil receipts were paid.[34] The testimony of FIBA's then-director, Pierre Houdray, records that he used funds in Lissouba's account to buy a multi-million dollar property in Paris for Lissouba. He also alleges that 'Mrs Lissouba made cash withdrawals which sometimes exceeded one million French francs (FF),' or hundreds of thousands of dollars.[34]

According to Sigolet, Congo's first oil-backed loan was arranged when Sassou-Nguesso took power in 1979 and demanded an immediate advance on future production in response to the sudden destabilisation of the world oil market.[35] Initially, Elf sought to ensure that the total sum of loans never went higher than around FF500 million (or US$117 million at the 1979 exchange rate).[36] By June 1994, however, this ceiling had doubled to FF1 billion, the repayment of which was rescheduled in exchange for granting Elf new oil concessions.[37]

Yet the loans created an extraordinary paradox: a system dreamed up as a way to pump quick infusions of cash into the country, in order to pay civil servants and preserve the peace, ended up indebting the nation and reducing the government's control of revenues to the extent that unrest was virtually assured. An unpublished 2001 IMF report concluded that 'rather than contributing to the welfare of the Congolese population, the proceeds from oil-collateralised borrowing may have been used to finance combat operations during the civil war'.[38]

Elf's system had two key elements. The first was that losses for the state were turned into private gains for the company, Elf officials, and the ruling elite of the country hosting its operations. The second was that the company created conditions of deliberate indebtedness though oil-backed lending, progressively securing its hold on the country's internal politics. Le Floch-Prigent's main defence in the Elf trial was to say that he inherited a system that was out of control and there was little he or anyone else could do to contain it.[39]

Elf and the Congolese civil war

In Congo and elsewhere, the Elf system appears to have been used to destabilise any perceived political threat to its interests.[40] According to Tarallo, Elf's official policy was always to support the existing government, which in this case was President Sassou-Nguesso. This situation was upset, however, by the democratisation of the Congo in the early 1990s.[41] Sassou-Nguesso gave way to a transitional government and the presidential elections of August 1992 were won by Lissouba.

According to Tarallo's testimony, Elf suspended the practice of paying *abonnements* during the political transition. But Pierre Fa, Elf's former Head of Audit, testifies that the company intervened to obstruct a planned IMF audit of the oil sector in 1991 so as to mask its practice of under-invoicing African subsidiaries. The company was also alleged to have a US$2.5 million slush-fund account called *Tomate* (Tomato) for the 1992 elections.[42] Sirven denies this last allegation, contending that the *Tomate* fund was meant instead to fund UNITA, the Angolan rebel army.[42] Even if true, this assertion hardly absolves the company of its part in increasing regional instability.

Lissouba asked Elf for a large loan in the run-up to legislative elections in mid-1993, chiefly to pay the salary arrears of Congo's civil servants. Le Floch-Prigent denied Lissouba's request for 'reasons of political stability of the Congo…considering that if M. Lissouba won an absolute majority [in the elections], there would be an ethnic war'.[43] Le Floch-Prigent's testimony states his belief that 'democracy in

Elf's office loomed large over the war in Congo.
Credit: Martin Adler/Panos Pictures

Congo is ethnic'; apparently meaning that he thought Congolese society would fragment along ethnic lines and that Sassou-Nguesso was the only leader capable of uniting it.[44]

Lissouba testified that after France's then-president François Mitterrand refused his request for help, the Congolese government was forced to raise cash by increasing oil taxes and royalties from 17% to 33% and by seeking an oil-backed loan of US$150 million from the US company Occidental Petroleum (Oxy).[45] The terms of the loan were disastrous for the Congolese, and demonstrative of the way such lending drains the state treasury: according to Le Floch-Prigent's testimony, Congo's share of oil production for the next 10 years was to be sold at the bargain price of US$3 a barrel.[46] With the help of the Oxy loan, Lissouba won the elections soon after.

The intervention by a US company into French oil territory appears to have been particularly threatening to Elf. According to his testimony, a furious Le Floch-Prigent even went so far as to advise the French government to hold up payment of the loan money through the French-controlled central bank, but his advice was ignored.[46]

According to Tarallo, Elf subsequently bought the Oxy loan in conjunction with Italian oil company Agip: if true, this suggests that the company was anxious to maintain its hold over the new government.[47] Tarallo also claims that Elf approved Lissouba's request for *abonnements* as one of the perks of his new office, although this claim is contested by Lissouba.[48] In April 1996, Tarallo alleges that Elf paid some 50 million Swiss francs into accounts held by Lissouba or his proxies.[49]

Although Tarallo is on record stating that Elf's official policy was always to support the leader in office,[50] and the company attempted to normalise relations with Lissouba,[51] the testimony of former Congolese Finance Minister Nguila Moungounga alleges that the company also financed several bids to return the former dictator Sassou-Nguesso to power.[52] The first was a coup attempt in January 1992 by the army chief of staff,[52] and the second was the 1993-1994 war sparked by opposition leader Bernard Kolelas and Sassou-Nguesso himself.[53] In 1996, Sassou-Nguesso renewed his claim to the presidency, and the resulting political tension put Elf in an awkward position.[54] Evidence in the indictment suggests that the company resolved the problem as it had in Angola, by supporting both sides of the developing conflict.

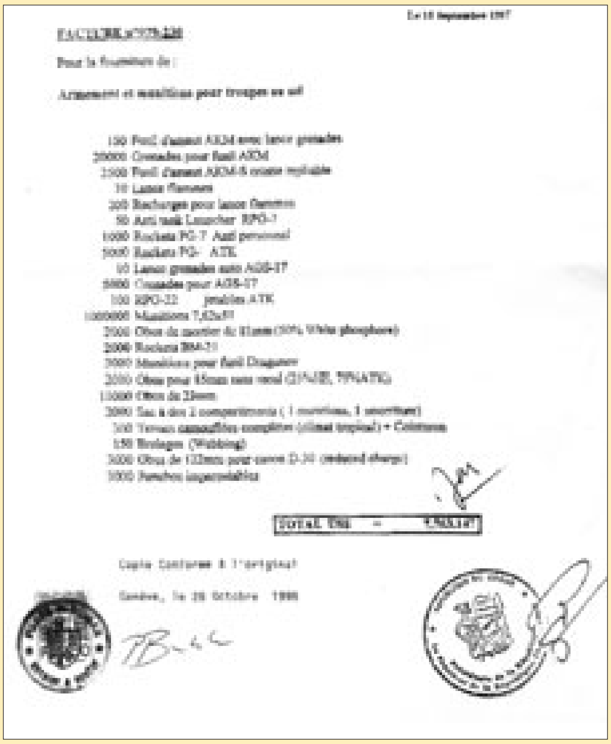
Arms for oil

As the civil war of 1997 loomed, the indictment suggests that Tarallo and his former Elf colleague Jack Sigolet

Oil for Arms

According to ex-president Lissouba's testimony in the Elf indictment, at the start of the 1997 Congolese civil war, Tarallo told him 'you need to have a war chest', and Tarallo and Sigolet subsequently introduced him to notorious Belgian arms trafficker and money launderer Jacques Monsieur.[72] Tarallo denies this: 'I do not know Jacques Monsieur … and I have never had anything to do, in any capacity, with any arms purchase or its financing'.[73]

Orders were placed with Monsieur for weapons such as helicopter gunships[74] totalling US$61.5 million and the payments were routed through the Paris branch of FIBA, partly owned by Elf.[75] The indictment records that the arms were 'paid for with oil': that is, with funds siphoned-off from Congo's oil revenues and paid into the FIBA account of the Congolese Ministry of Finance.[76] From May to September 1997, a total of around US$52 million (FF303 million) entered the account and between US$25 and US$30 million was paid out for arms.[77] In addition, Sigolet admits to making arrangements for a new oil-backed loan for US$50 million for Lissouba, routed through an offshore company called Darrow, although he claims the financing never happened.[78]


Pour la fourniture de :

Armement et munitions pour troupes au sol

Copie Conforme à l'original

Some of the arms supplied by Jacques Monsieur during the Congolese Civil War of 1997.


TO : MME MINARD
FROM : S. BOISACQ
DATE : 12/06/97
PAGES : 04 (incl.)

Attention Mr HOUDREY Directeur Général FIBA

DETAILS BANCAIRES / BANK DETAILS

FIRST NATIONAL BANK
Parktown branch
Johannesburg
R.S.A.
Nom du compte : SABLON TRADING cc
No du compte : 6000011886
Clearing No : 250455
Tel : 2711-4841843
Fax : 2711-6420119

US$ 1.800.000,00 (UN MILLION HUIT CENT MILLE DOLLARS US) A TRANSFERER AU COMPTE CI-DESSUS POUR LIVRAISON IMMEDIATE DE DEUX (2) MI 17 IV COMPLETS, AVEC EQUIPAGES.
LIVRAISON A BRAZZAVILLE COMPLETEE ENTRE SIX ET HUIT HEURES APRES RECEPTION DU PAIEMENT.
LES EQUIPAGES DES DEUX APPAREILS SONT MIS A VOTRE DISPOSITION, A NOS FRAIS, POUR UNE DUREE DE DEUX SEMAINES.
DETAILS TECHNIQUES CI-JOINT (PP 2 à 3).
LES CINQ (5) APPAREILS EN REFERENCE NOTRE FAX DU [illegible], TRANSMIS A MR [illegible] PEUVENT ETRE EQUIPES DE LA MEME MANIERE ET ETRE LIVRES, AVEC EQUIPAGES, A BRAZZAVILLE EN DEANS LES 24 HEURES APRES RECEPTION DU PAIEMENT.
COMPTE TENU DE LA LOGISTIQUE DE L'OPERATION UNE REPONSE RAPIDE DE VOTRE PART NOUS AGREERAIT.

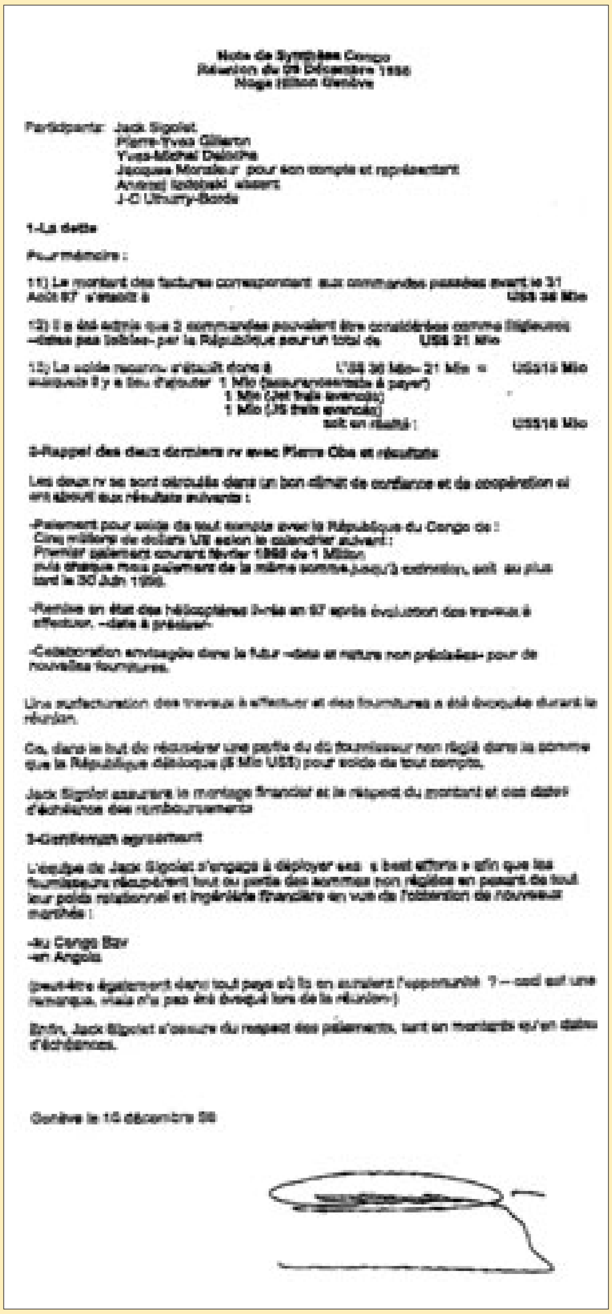
Payments for weapons, including helicopter gunships, went through Elf's bank FIBA.

Sigolet testifies in the indictment that when Sassou-Nguesso returned to power 'it was disagreeable for [him] to have to settle debts for the arms delivered to Mr Lissouba'.[79] In May 1998, according to newspaper reports, Monsieur delivered the last of Lissouba's weapons via Jet Finances Consultants.[80]

According to Belgian newspaper *Le Soir* and meeting notes obtained by Global Witness, Sigolet, acting on behalf of the Congolese government and now retired from Elf, held a meeting with Monsieur at the Noga Hilton in Geneva on 9 December 1998, along with several others including the CEO of Jet Consultants Finances.[81] At this meeting, the Sassou government agreed to repay the outstanding debt to the tune of 'US$5 million according to the following timetable: first instalment in February 1998 of US$1 million then payment of the same sum each month until liquidation of the debt, at the latest by June 30 1999'.[82]

The participants also discussed the possibility of getting money to Monsieur through 'over-invoicing for future repair work [on the helicopters Congo had bought] with the aim of recouping part of the money due to the supplier which has not been included in the sum unblocked by the Republic (US$5 million) in settlement of the account'. This future repair work appears not to have come to pass.[83]

By 2000, with US$1 million still to be repaid, Monsieur allegedly threatened to reveal both the weapons orders signed by Sigolet and the FIBA invoices[84] and to expose kickbacks to top executives on aircraft and insurance contracts paid through FIBA's subsidiary FIBAViat, as Sigolet alleges in the indictment.[85]


Note de Synthèse Congo
Réunion du 09 Décembre 1998
Noga Hilton Genève

Participants: Jack Sigolet
[illegible]
Jacques Monsieur pour son compte et représentant
[illegible]

1-La dette

Pour mémoire :

11) Le montant des factures correspondant aux commandes passées avant le 31 Août 97 s'élevait à US$ 36 Mio

12) Il a été admis que 2 commandes pouvaient être considérées comme litigieuses [illegible] par la République pour un total de US$ 21 Mio

13) Le solde reconnu s'élevait donc à US$ 36 Mio – 21 Mio = US$15 Mio
auxquels il y a lieu d'ajouter 1 Mio [illegible]
1 Mio [illegible]
1 Mio [illegible]
soit un résultat : US$18 Mio

2-Rappel des deux derniers rv avec Pierre Oba et résultats

Les deux rv se sont déroulés dans un bon climat de confiance et de coopération et ont abouti aux résultats suivants :

-Paiement pour solde de tout compte avec la République du Congo de :
Cinq millions de dollars US selon le calendrier suivant :
Premier paiement courant février 1998 de 1 Million
puis chaque mois paiement de la même somme jusqu'à extinction, soit au plus tard le 30 Juin 1999.

-Remise en état des hélicoptères livrés en 97 après évaluation des travaux à effectuer. –date à préciser-

-Collaboration envisagée dans le futur –date et nature non précisées- pour de nouvelles fournitures.

Une surfacturation des travaux à effectuer et des fournitures a été évoquée durant la réunion.

Ce, dans le but de récupérer une partie du dû fournisseur non réglé dans la somme que la République débloque (5 Mio US$) pour solde de tout compte.

Jack Sigolet assurera le montage financier et le respect du montant et des dates d'échéance des remboursements

3-Gentleman agreement

L'équipe de Jack Sigolet s'engage à déployer ses « best efforts » afin que les fournisseurs récupèrent tout ou partie des sommes non réglées en passant de tout leur poids relationnel et ingénierie financière en vue de l'obtention de nouveaux marchés :

-au Congo Bzv
-en Angola

(peut-être également dans tout pays où ils en auraient l'opportunité ? – ceci est une remarque, mais n'a pas été évoqué lors de la réunion-)

Enfin, Jack Sigolet s'assure du respect des paiements, tant en montants qu'en dates d'échéances.

Genève le 10 décembre 98

Sassou-Nguesso's government reluctantly settles debts to Jacques Monsieur left by the defeated Lissouba.

helped Lissouba to arrange arms purchases through the notorious Belgian arms-trafficker and money-launderer Jacques Monsieur (see box: 'Oil for Arms').[55] It records that the arms were 'paid for with oil': that is, with funds siphoned off from Congo's oil revenues and paid into the FIBA account of the Congolese Ministry of Finance.[56]

Some sources allege that Elf's involvement in weapons procurement in Congo went beyond introductions and financial facilitation. The French newspaper *Le Canard Enchaîné* reported in 1997 that Elf supply boats were used to transport Angolan troops supporting Sassou-Nguesso to Congo's oil town, Pointe-Noire.[57] Lissouba makes a similar assertion in the indictment, claiming that 'from 1994-1995 onwards, the arms used by Sassou's young people were transported in Elf barges. They came from Angola'.[58] *Le Monde* quotes allegations by French intelligence sources that Sassou's militia, the 'Cobras', were able to get arms 'thanks to the secret financing networks of oil companies'.[59] *Le Nouvel Observateur* claimed that Elf also employed public relations consultants to boost Sassou-Nguesso's image abroad and these consultants chartered a flight to take French journalists to visit Sassou-Nguesso's headquarters.[60]

Such allegations have recently resurfaced. In December 2003, *Le Monde* reported that continuing investigations into alleged bribes paid by Elf in Nigeria in the mid-1990s 'could revive the questions over the possible implication of the oil group in the Congolese civil war'.[61]

Sassou-Nguesso gained the decisive military advantage in 1997 due to support from the Angolan military, according to Tarallo's testimony.[62] Angolan president José Eduardo dos Santos may have had a number of motives for this intervention, not least his belief that Congo had become a launching pad for separatist guerrillas from the oil-rich Cabinda region of Angola, and that Congo aided diamond smuggling by the rebel UNITA movement.[63]

Angola appears to have been an Elf ally, too. According to Tarallo's evidence, Sassou-Nguesso introduced the company to President dos Santos and was duly rewarded.[64] Angola became the recipient of Elf bonuses, *abonnements* and oil-backed loans. *Le Nouvel Observateur* commented that Elf had 'very promising projects in Angola' and hoped that 'the war would have dispersed the final clouds troubling Franco-Angolan relations'.[60] Eye-witnesses report that Elf's offices and its fleet of four-wheel-drive vehicles were left untouched when Angolan soldiers pillaged the rest of the oil town of Pointe-Noire.[65]

On 15 October 1997 Lissouba fled Congo, leaving behind a capital city devastated by violence, with thousands of dead, widespread looting, systematic rape of women and hundreds of thousands of civilians displaced.[66] There were also reports of widespread summary executions of opponents following Sassou-Nguesso's victory.[67] Yet more fighting in 1998-1999 led to the destruction of many southern towns, including parts of Brazzaville, and displaced an estimated 800,000 civilians, one-third of the country's population.[68]

Sassou-Nguesso and several members of his government have now been indicted in the French courts for the execution and disappearance of 350 returning Congolese refugees in May 1999, and the investigating judges have issued an international arrest warrant for one of the accused, Army-Inspector General Norbert Dabira.[69]

When the war finished, Tarallo resumed his role as counsellor to Sassou-Nguesso.[70] According to his testimony, his real sympathy in the conflict had always lain with Sassou-Nguesso and his only reason for supporting Lissouba was 'to reinforce the interests of Elf', always his 'essential preoccupation'.[70]

Concerning Elf's overall role in the Congolese civil war, Le Floch-Prigent, asks in indictment: 'how did we get to the point, being the lead oil production company in Congo, of allowing a civil war to develop which transformed the capital city of Congo into a wasteland?'[71] If the details of who did what to whom are not entirely clear, one truth is unquestionable: if Elf had been obliged to publish its payments to the Congolese government in a transparent way, then the 'Elf system' could not have operated or spun out of control so that it engendered wholesale regional instability.

Sassou III: Business as usual?

Sassou-Nguesso returned to power in elections held in 2002 with almost 90% of the vote, by which time Elf had been privatised. Although these elections were given a seal of approval by EU observers, local human rights groups denounced them as rigged.[86] Sassou-Nguesso's main opponents, Lissouba and Kolelas, were excluded and a third contender pulled out hours before the poll alleging 'an electoral hold-up'.[87]

A merger in 2000 created TotalFinaElf (now Total) and presumably a chance for the new company to forge a new relationship with Congo. However, the new Total appears to be to paying for Elf's past actions. The Congolese government alleged that changes to Production Sharing Agreements and the sale of government shares in Elf Congo under Lissouba had short-changed Congo of its fair share of taxes and royalties and the government requested that Total reimburse Congo for lost revenues to the tune of US$500 million.[88] The president appeared to be playing hardball with Total, encouraging advances from US oil companies: Total's application for an extension on its Haute Mar concession was turned down and the concession was granted instead to an American company (Murphy Oil). Chevron was also made the operator of K Structure (shared between Congo and Angola) even though Total is the main shareholder in the block.[88]

Relations between the government and Total appear to have improved after an agreement was reached in July 2003. However, the terms of the agreement raise more questions than they answer. Newspapers say that, in return for the government renouncing all its demands, Total agreed to reschedule the US$197 million oil-backed debt owed to it by the government. Congo will now have until 2010 to repay, but the heavily-indebted country will end up paying US$280 million, almost US$100 million more.[89]

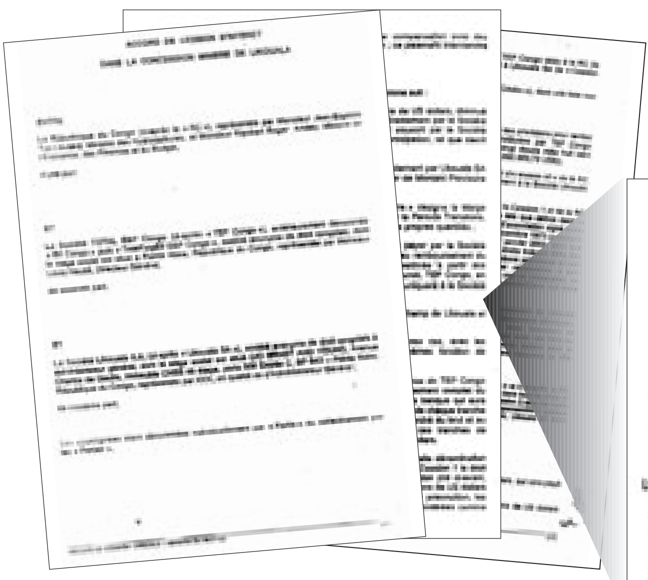
Moreover, in a bizarre deal smacking of yet more opacity, Total also agreed to give the government its share in the Likouala oil field to settle any outstanding disputes.[89] According to newspaper reports, the Likouala field has official reserves of 30 million barrels.[90] However, rather than turning its share over to the state oil company, the SNPC, one newspaper states that the government sold it on to a private company called 'Likouala SA' for around US$160 million.[89] *Africa Confidential* said that '[the shareholders] are thought to include trusted proxies of Sassou's … the company is essentially a commercial vehicle for sharing revenues from the Likouala oil field'.[91]

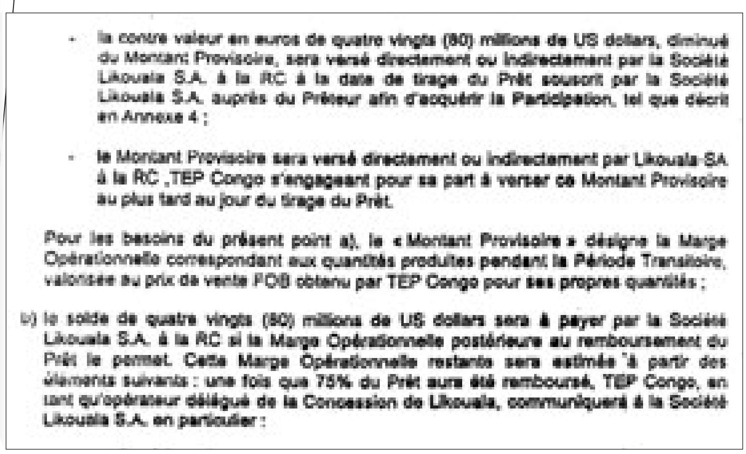
Global Witness has obtained a copy of the draft agreement and also reviewed a confidential memo on the agreement.[92] Both documents appear to confirm the press reports of a 'two stage' deal: the government will receive Total's 65% share in the Likouala field, valued at US$160 dollars, and then immediately transfer its share to a private Congolese-registered company, Likouala S.A. The company is described as having a 'single shareholder'. The agreement refers to an upfront payment of US$80 million by Likouala S.A. to the Congolese authorities. This money is to be raised by a loan from a bank or banks, with a further US$80 million payment to the government once the initial loan is paid off, the operational margin of the field permitting. Total is to remain the operator.

The memo states that the reason for this 'two stage' process is 'to allow Total to serve as a support for a financial operation linked to Likoula'. In a recent interview, Bruno Itoua, the Head of the SNPC, states that 'the government needed funds immediately and Total, for tax reasons, did not wish to pay out liquid assets'.[93]

Once again, there has been no public debate over this arrangement, nor is it clear who owns Likouala S.A., whether the initial payment of US$80 million has been made and if so, where it has ended up. A summary of the 2004 budget obtained by Global Witness does not appear to record this deal as revenue for either 2003 or 2004. Moreover, this operation seems to be, in effect, an oil-backed loan. As such, it would contravene the government's undertaking to the IMF in April 2003 to stop oil-backed lending.[94] There is also a question as to what the 65% stake in the Likouala field is actually worth. If 30 million barrels of oil can in fact be extracted from the field, then the value of the 65% stake may be significantly more than US$160 million.

Global Witness has asked Total for clarification of its relationship to Likouala S.A. but at the time of writing had not yet received a response. In the light of Total's participation in international initiatives to improve transparency in revenues from the oil sector such as the





- la contre valeur en euros de quatre vingts (80) millions de US dollars, diminué du Montant Provisoire, sera versé directement ou indirectement par la Société Likouala S.A. à la RC à la date de tirage du Prêt souscrit par la Société Likouala S.A. auprès du Prêteur afin d'acquérir la Participation, tel que décrit en Annexe 4 ;

- le Montant Provisoire sera versé directement ou indirectement par Likouala SA à la RC ,TEP Congo s'engageant pour sa part à verser ce Montant Provisoire au plus tard au jour du tirage du Prêt.

Pour les besoins du présent point a), le « Montant Provisoire » désigne la Marge Opérationnelle correspondant aux quantités produites pendant la Période Transitoire, valorisée au prix de vente FOB obtenu par TEP Congo pour ses propres quantités ;

b) le solde de quatre vingts (80) millions de US dollars sera à payer par la Société Likouala S.A. à la RC si la Marge Opérationnelle postérieure au remboursement du Prêt le permet. Cette Marge Opérationnelle restante sera estimée à partir des éléments suivants : une fois que 75% du Prêt aura été remboursé, TEP Congo, en tant qu'opérateur délégué de la Concession de Likouala, communiquera à la Société Likouala S.A. en particulier :

The Likouala deal: another oil-backed loan?

UK-led Extractive Industries Transparency Initiative, Global Witness believes Total should disclose details of its new arrangements with the Congolese government.

Finally, the memo includes another surprising provision: 'TEP [TotalFinaElf Exploration and Production] Congo will take care of the costs incurred and any possible financial penalties imposed [on the Republic of Congo] in favour of the Antoine Tabet group. A provision of US$70 million has been created for this purpose.'[95]

Antoine Tabet is a businessman currently involved in litigation with Congo over alleged non-payment for public works projects financed by oil-backed loans from Elf in the 1990s.[96] In January 2004, the French press reported that Tabet had been charged by Elf investigating judge Van Ruymbeke with 'aiding and abetting the misuse of credit' and 'benefiting from the misuse of credit' in collusion with the then-head of Elf Congo, Frédéric Isoard, in relation to the oil-backed loans.[97] Why would Total agree to pay one of Congo's creditors on the government's behalf, a creditor who, moreover, is now alleged to have misappropriated funds from Elf loans? As with the Likouala deal, this appears to raise serious questions about Total's commitment to avoiding the opaque and tortuous arrangements that characterised Elf's relationship with the Congolese government.

Sassou-Nguesso, Congo's military strongman, has reinvented himself as a democrat.
Credit: Robert Patrick/Corbis Sygma

Meanwhile, the citizens of Congo are still saddled with enormous oil-backed debts. According to an unpublished 2001 IMF report on Congo, oil-backed loans are 'the most expensive and inflexible part of the Congo's external debt'.[98] In recent years 'one-fourth to one-third of Government oil revenue' has been automatically transferred to offshore accounts held by creditors.[99] The World Bank representative in Congo confirmed to Global Witness that the country's current oil-backed debt is owed to Total and Agip.[100] Figures for this debt in 2003 placed it at between US$250-400 million, before the rescheduling of the Total debt in September 2003.[101]

Sassou-Nguesso's second regime has seen a concentration of power in the hands of the presidency, and he increasingly rules by decree.[102] Congolese finances remain inscrutable, oil-backed debts from the civil war remain a massive drain on state solvency – the IMF reported in 2001 that short-term debt stood at 186% of GDP[103] – and offshore arrangements of oil-backed financing have continued (see below), providing Sassou with a huge unaccountable revenue stream. This unaccountability extends to other areas: Amnesty International has condemned the 'climate of impunity' that continues to exist in the country over widespread human rights abuses.[104]

Payments by companies like Total remain totally opaque. The first signs of ordinary Congolese citizens' disquiet over this situation emerged in June 2002 when prominent church leaders appealed to oil companies and the government to open their books, and for a public audit of state oil company SNPC.[105] Although Sassou-Nguesso dismissed this appeal as a 'provocation',[106] debate has not been dampened by the government's unfavourable response. In February 2003 in Paris, over 20 Congolese and international civil society groups reiterated the critical importance of revenue transparency for Congo's development and, in September, Congolese organisations formed a *Publish What You Pay* platform.[107] To date, civil society has received no official response to its concerns from its government.

Meanwhile, large amounts of oil money are apparently not reflected in the national budget. From 1999-2002, the IMF has estimated that government accounts underreported the amount of oil revenues received by US$248 million.[108]

Where that money went remains unclear, but in its most recent report the IMF characterised the overall performance of the government in meeting IMF targets under the reform programme as 'disappointing'.[109]

The World Bank, in an interview with Global Witness, has since stated that there are no longer any off-budget operations by the government, that all oil monies are now accounted for by the Treasury, and that the 2003 budget produced under new Finance Minister Roger Rigobert Andely gives the correct figures for oil receipts and oil debt.[110] The IMF's representative, Norbert Toe, while lamenting 'slight overspending' by the government in the last trimester of 2002, also congratulated Andely on progress made in 'cleaning up' the management of state finances.[111]

Nevertheless, figures for oil revenues and budget documents passed to Global Witness still appear to contain significant discrepancies and there still appear to be major revenue streams that are not recorded in the budget (see below).[112] Indeed, the government itself admitted in April 2003 that there had been 'major slippages' in its fiscal performance, rooted in 'off-budget and advance payments practices, the organization of elections and the lack of strict controls'.[94]

It is impossible to double-check the figures given for oil revenue paid to the government as they are not disclosed by the companies. Nevertheless, oil industry sources in Congo have told Global Witness that the total figure for net oil receipts by the government (after deductions for debt payments) is around 33-35% of total sales.[65] Sassou-Nguesso confirmed this estimate in a February 2003 interview: 'Out of CFA 100 francs, Congo receives an estimated CFA 30 francs, roughly speaking…these CFA 30 francs are always presented to Parliament each year'[105]. Similarly, Itoua confirms that 'in principle' the Congo receives a third of total sales, although he states that Congo in fact receives less than it should, around 26-28% as opposed to, say, the 40% Angola receives.[113]

Industry sources interviewed by Global Witness conservatively estimate Congolese production to be around 270,000 barrels per day (bpd),[114] which means, at a conservative price of US$25 per barrel, annual sales of US$2.5 billion. The government should therefore receive about US$800 million in revenue. The figure given for 2003 revenues in the 2004 budget is US$650 million (CFA 342,600 billion francs), a figure that seems particularly low given that oil prices have reached historic highs. More curious given the scale of oil operations in Congo is the fact that for 2003 a figure of zero revenues was returned for taxes and signature bonuses in the budget.[111]

Top: Total's headquarters in Pointe Noire, Congo.
Bottom: Total facility near Pointe Noire.

Do Total, Agip, Chevron and the other companies not pay taxes? According to an expert source, this is indeed the case. If so, it goes against IMF standard tax policy, which states that '[m]ining and petroleum projects should be subject to the income tax like other activities in the economy'.[115] Moreover, in April 2003, it was reported that the government had granted two new concessions to Murphy Oil.[116] Were no signature bonuses paid on this contract?

Another form of oil revenue not featured in the 2003 budget is the '*Provision Pour Investissement Diversifié*' (PID). According to Congolese civil society and oil industry sources, since January 1996 oil companies have paid 1% of total profit oil (the oil left after costs have been paid) to the government to invest directly in projects to develop the Congolese economy.[117] It appears that, until 2000, PID income was kept completely off the balance sheet.[117] In the 2002 budget, the estimated figure for the PID is given as around US$11 million (CFA 6.6 billion francs).[112] In the budget for 2003, the PID does not feature at all, only to reappear in the 2004 budget, where a figure of US$15 million (CFA 7.7 billion francs) is recorded. Sources in the Congo have told Global Witness that the reason it did not figure in the 2003 budget was because Finance Minister

TABLEAU RECAPITULATIF DU PROJET DU BUDGET DE L'ETAT, EXERCICE 2004

LIBELLE	Prévisions 2002	Exécution [illegible]	Prévisions 2003 (1)	Exécution [illegible]	Projection à fin décembre(*)	PREVISIONS 2 004	Variation [illegible]	%
I BUDGET DE FONCTIONNEMENT								
I.1 Recettes hors Dons								
A. Recettes non Pétrolières								
Impôts et taxes intérieurs :	135,000	122,103	151,500	96,200	133,300	150,700	-0,800	-0,53
Droits et taxes de Douanes	52,000	34,787	55,000	31,200	45,800	50,600	-4,400	-8,00
Taxe Spéciale sur les Hydrocarbures(TSH)	12,000	10,031			0,000		0,000	
Recettes de Services & de portefeuille	6,500	2,827	7,500	4,136	4,800	8,700	1,200	16,00
Sous-total A	205,500	169,748	214,000	131,536	183,900	210,000	-4,000	-1,87
B - Recettes Pétrolières								
Redevance Pétrolière	136,508	71,782	134,748	123,974	148,821	153,530	18,782	13,94
Profil-Oil	161,455	120,353	162,625	149,622	179,488	180,713	18,088	11,12
Bonus Pétroliers	0,000	3,710	0,000	0,000		4,000	4,000	
Yanga/Sendi (15%)						7,981	7,981	
Excess Oil						31,803	31,803	
Produits de vente des Cargaisons	55,000	333,521	75,000	69,004	82,777	0,000	-75,000	-100,00
Autres revenus pétroliers (frais de formation)				0,000		0,700	0,700	
Sous-total B	352,963	529,368	372,373	342,600	411,086	378,727	6,354	1,71
C - Ressources de transferts	0,750		1,750	1,000	1,750	0,150	-1,600	-91,43
dont: contribution SNPC			1,000	0,000	0,000	0,000	-1,000	
TOTAL RESSOURCES PROPRES (A + B+C)	559,213	699,116	588,123	475,136	596,736	588,877	0,754	0,13
D - Ressources à rechercher (en Capital)	33,550	-40,882	170,603	-22,535	156,550	227,863	57,260	33,56
TOTAL RECETTES	592,763	658,234	758,726	452,601	753,286	816,740	58,014	7,65
I.2 Dépenses de Fonctionnement								
a)-Dépenses courantes, hors Dette								
Personnel	120,000	120,395	120,000	90,500	121,200	124,500	4,500	3,75
Matériel	63,055	78,403	50,075	37,400	50,000	51,775	1,700	3,39
Charges Communes	78,895	73,362	42,800	31,163	42,800	47,700	4,900	11,45
Transferts hors Contribution	70,050	54,543	78,125	120,137	144,200	133,550	55,425	70,94
dont : Collectivités locales	12,600	4,937	16,000	8,907	10,500	16,000	0,000	0,00
Filière carburant				8,100	12,500	7,000	7,000	
SNPC :				35,800	38,000	14,000	14,000	
- frais commerciaux				3,600	5,000	6,000	6,000	
- compte d'avance				32,200	33,000	8,000	8,000	
CORAF			5,000	16,000	16,000	8,000	3,000	60,00
SOCOTRAM			1,400	1,700	3,100	5,000	3,600	257,14
Interets/decouverts Banques locales	5,000	8,886	9,000	10,800	14,000	14,800	5,800	64,44
Contribution à l'Investissement	132,000	198,432	88,988	69,947	100,286	121,802	32,814	36,87
Sous-total a.-	469,000	534,021	388,988	359,947	472,486	494,127	105,139	27,03
* - Solde Primaire	90,213	165,095	199,135	115,189	124,250	94,750	-104,385	-52,42
b).- Service de la Dette	123,763	124,213	369,738	92,654	280,800	322,613	-47,125	-12,75
Sous-total-b.-	123,763	124,213	369,738	92,654	280,800	322,613	-47,125	-12,75
TOTAL DEPENSES	592,763	658,234	758,726	452,601	753,286	816,740	58,014	7,65
II - INVESTISSEMENT								
A- Moyens librement affectables (Ressources pro								
Contribution du Budget de Fonctionnement	132,000	198,432	88,988	69,947	100,286	121,802	32,814	36,87
dont Prélèvements pétroliers	0,000		28,035	0,000	0,000	0,000	-28,035	-100,00
PID	6,648	6,194	6,989	7,253	7,714	6,873	-0,116	-1,66
Produits de la privatisation	10,800		4,418	2,100	4,400	1,900	-2,518	-56,99
PL 480	1,000		0,000	0,000	0,000	0,000	0,000	
Sous-total A	150,448	204,626	100,395	79,300	112,400	130,575	30,180	30,06
B- Emprunts Etat	36,588	19,639	37,401	3,700	9,900	38,500	1,099	2,94
C- Dons	27,477	3,666	20,738	8,600	10,600	18,000	-2,738	-13,20
TOTAL INVESTISSEMENT	214,513	227,931	158,534	91,600	132,900	187,075	28,541	18,00
III- BUDGET GENERAL DE L'ETAT								
Fonctionnement net	460,763	459,802	669,738	382,654	653,000	694,938	25,200	3,76
Investissement	214,513	227,931	158,534	91,600	132,900	187,075	28,541	18,00
TOTAL BUDGET GENERAL	675,276	687,733	828,272	474,254	785,900	882,013	53,741	6,49
IV- IMPASSE BUDGETAIRE	97,615	-17,577	228,742	-10,235	177,050	284,363	55,621	24,32

PIB au prix du marché : 2145,5 milliards dont pétrolier : 1043,9 milliards (48,66%), hors pétrole : 1101,6 millards (51,34%)

(*) : Estimation à fin décembre 2003

Ressources en capital = Total Dépenses - Total Ressources Propres

Solde Primaire = Total Ressources Propres - Total Dépenses de fonctionnement hors Service de la Dette

Hypothèse pétrolière 2004 : Production = 12,147 soit 89,2 millions bbl; 1bbl brent =25,6$; brut congolais : 24$; 1$= 580 FCFA

Revenus pétroliers/PIB	20,8	18,0
Revenus pétroliers/PIB pétroliers	43,0	36,9
Solde Primaire/PIB	6,2	4,4
Solde hors recettes pétrolières/PIB	-14,3	-13,2
Revenus hors pétrole/PIB hors pétrole	17,9	19,1
Salaires/PIB	6,0	5,8
Investissement/PIB	6,6	8,7

The 2004 budget raises questions about transparency.

Andely had blocked its use out of his concern over past lack of transparency and accountability.[118] So where is the money going now, and what happened to the PID funds in the six years from 1996-2002?

The lesson is simple: unless there is more transparency in the oil sector, including the publication of the SNPC's independently audited accounts, there is no way the budget figures for oil receipts can be verified.

The absurdity of the current situation was highlighted early this year when, in an unprecedented move, MPs were asked to approve legislation reducing the government's share of revenue from Total. In the words of an opposition spokesman, oil has always been 'a family affair'[119] in Congo, so many MPs and political commentators were mystified as to why the Assembly was even being consulted.[120] How could they approve such changes without having the full picture about current revenues and arrangements on which to base their decision?

Société Nationale des Pétroles du Congo

Not only are the arrangements the government makes with foreign oil companies in Congo opaque, but the state oil company *Société Nationale des Pétroles du Congo* (SNPC) also appears to be managed without any transparency.

According to SNPC chief executive Bruno Itoua, the company was set up in 1998 to defend the interests of the Congolese state against the predatory behaviour of oil companies, by developing a national capacity for exploration and selling.[121] Yet according to the IMF, 'none of the SNPC's after-tax income (US$43 million in 2001) has been transferred to the budget', causing a loss to the treasury of 'potentially significant sources of income'.[122] Even the notoriously untransparent Angolan state oil company Sonangol, upon which SNPC has been explicitly modelled,[123] has managed to transfer some money back to the Angolan budget. This appears to mean that Congolese citizens, in whose name SNPC was set up, are seeing none of the benefits. So, despite the reason behind its creation, ironically it would seem that SNPC has become another black hole in Congo's budget.

The company was created with the help of a World Bank economic recovery credit[124] yet, according to a company insider, it has operated to date outside the fiscal oversight of both the Ministry of Hydrocarbons and the Ministry of Finance, although Itoua shares a very close relationship with Sassou-Nguesso.[125] When questioned over the company's opacity, Itoua's bizarre response was to state that, 'the reason transparency wasn't defined legally [when SNPC was established] as a specific mission was because that would have been a recognition that there had previously been a lack of transparency [in former state oil company HydroCongo]'.[126]

In July 2001, the Congolese government agreed to an IMF Staff Monitored Programme (SMP) as a prerequisite to any future economic restructuring or debt relief programmes,[127] and the World Bank subsequently gave US$5 million to improve transparency with priority given to the oil sector.[128] Under the SMP, the government agreed to three things: a 'Convention' clarifying the relationship between the company and the state; an audit of the SNPC's accounts, followed by an audit of the entire oil sector; and an end to the practice of oil-backed loans. The government's compliance with any of these requirements is highly questionable.

The Convention

The Convention, finalised on 30 June 2001, determined that the SNPC should transfer the proceeds of all sales into a treasury account, less a remuneration of 1.69%, within a specified time period.[129] Yet SNPC still apparently believes itself to be a purely commercial entity with operational and financial autonomy, and has unsuccessfully sought to argue so in court against debt collection actions targeting its assets on the grounds that it is an emanation of the state.[130] SNPC and the government are in clear contravention of the Convention because SNPC's earnings are not being transferred back to the treasury. According to the IMF, one explanation for this is that SNPC's business operations are financed by its earnings, and that the company is trying to expand into oil trading, and even into non-oil sectors, even

Congo's oil company, SNPC, doesn't pass its profits back to the state.

though the IMF itself noted that this 'seems to run counter to the SNPC's stated mandate' and recommended it limit 'the scope of its activities to the upstream sector'.[131] Does this mean Congolese citizens are foregoing revenues to help fund off-budget business operations by SNPC?

The Audit

Publication of the World Bank-funded audit remains long overdue. Due to be completed by mid-July 2003, the Congolese government and the World Bank did not even agree the terms of reference or the choice of auditor (KPMG) until March 2003.[132]

Disagreements over the terms of reference appeared to be ongoing. Itoua stated publicly: 'I think that the KPMG team is headed by a young man who is perhaps not very experienced, who perhaps has not read correctly his schedule of conditions'.[133] A copy of KPMG's summary of its first mission obtained by Global Witness confirmed that there had in fact been a breakdown in relations between the government and the audit team over issues such as Itoua's contention that the audit should only cover SNPC's books since the June 2001 Convention (thereby keeping three years of figures from the light of day) and the existence of 'special accounts and their use'.[134]

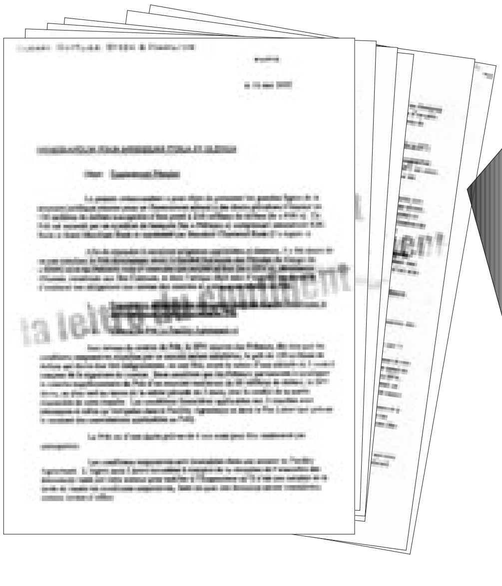
The auditors, meanwhile, complained of a lack of full and prompt access to information 'in contradiction of the terms of the audit contract'.[134] Most significantly, they were denied access to SNPC's bank accounts: 'Mr Itoua … raised the fact that the SNPC's bank accounts contain transactions relative to operations carried out in the name of the state; so in consequence SNPC would need an official letter from the Ministry of Finance authorising him to allow KPMG access to the bank statements'.[134] There is an apparent contradiction here: SNPC claims that it is financially and operationally autonomous from the state when in dispute with creditors, yet seems to be claiming financial interdependence with the state when in dispute with World Bank-appointed auditors.

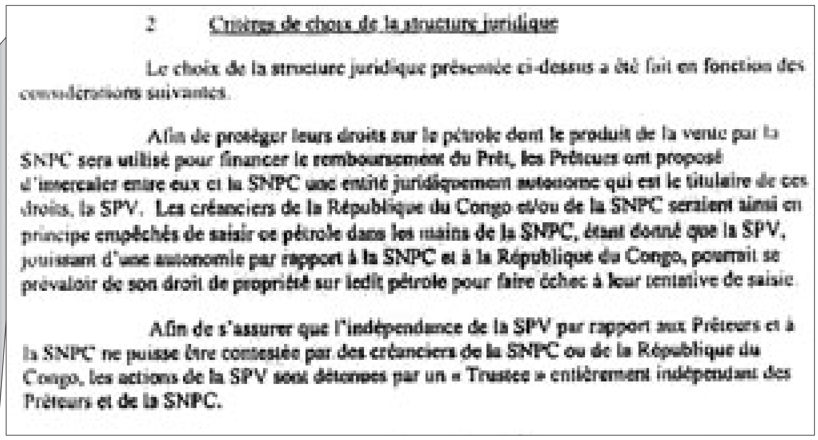
In June 2003, one newspaper reported that the audit had been briefly suspended by the Congolese government, because the government said the auditor's interest in the way that SNPC markets oil (through its London subsidiary, SNPC UK, headed by Sassou-Nguesso's son, Christel-Denis) was not within its terms of reference.[135] According to the IMF, the audit was finalised in July 2003 but it has still not been published, despite a commitment by the government to do so.[94] Global Witness and Congolese civil society groups have made several attempts to obtain a copy of the audit, but to no avail: when asked about the publication date, a representative for SNPC's London office said that he had never heard of the audit.[136]

No More Oil-Backed Loans

Congo has already mortgaged a substantial amount of its future oil extraction for ready cash. According to the IMF, from 1995-2000, some 75% of the government's borrowing was oil-backed.[137] The government promised to stop this practice in 2001 and repeated the promise in its 3 May 2002 and 11 April 2003 Letters of Intent to the IMF.[138]

Nevertheless, the SNPC continued to borrow against oil revenues in 2002, contracting a US$233 million loan from the French bank *Société Générale* and a US$210 million loan with a consortium comprised of Standard Chartered, Rand Merchant Bank, and KBC, while also renegotiating an earlier US$250 million loan with *Société Générale*.[139] The US$210 million loan was subsequently blocked in the Caymans by creditors of the government.[140] This is not all: Global Witness has obtained documents suggesting that two further loans of US$70 million and US$80 million were negotiated with BNP Paribas in July and September 2002 respectively.[141] The IMF underlined that SNPC's 'heavy collaterized borrowing undertaken in 2002 [which it





2 Critères de choix de la structure juridique

Le choix de la structure juridique présentée ci-dessus a été fait en fonction des considérations suivantes.

Afin de protéger leurs droits sur le pétrole dont le produit de la vente par la SNPC sera utilisé pour financer le remboursement du Prêt, les Prêteurs ont proposé d'intercaler entre eux et la SNPC une entité juridiquement autonome qui est le titulaire de ces droits, la SPV. Les créanciers de la République du Congo et/ou de la SNPC seraient ainsi en principe empêchés de saisir ce pétrole dans les mains de la SNPC, étant donné que la SPV, jouissant d'une autonomie par rapport à la SNPC et à la République du Congo, pourrait se prévaloir de son droit de propriété sur ledit pétrole pour faire échec à leur tentative de saisie.

Afin de s'assurer que l'indépendance de la SPV par rapport aux Prêteurs et à la SNPC ne puisse être contestée par des créanciers de la SNPC ou de la République du Congo, les actions de la SPV sont détenues par un « Trustee » entièrement indépendant des Prêteurs et de la SNPC.

SNPC planned to route a US$210 million oil-backed loan offshore to avoid creditors but the deal did not go through.

estimated at US$300 million] breached the authorities' commitment under the previous staff-monitored program'.[131]

A bill dated 23 May 2002 from SNPC's Paris lawyers Cleary Gottlieb to Bruno Itoua, leaked and subsequently published, states that the US$210 million loan referred to above was to be managed by a Special Purpose Vehicle (SPV) or 'legally autonomous entity' set up in the Cayman Islands.[142] An SPV is an offshore company created for a specific purpose which, as anyone who followed the collapse of Enron will know, can sometimes be an extremely complex and obscure way of structuring a business. Another leaked memo to Itoua also published explicitly states that: '[t]he creditors of the Republic of Congo and/or the SNPC will thus be in principle prevented from seizing this oil from the SNPC, given that the SPV, which will be autonomous in relation to the SNPC and the Republic of Congo, would be able to assert its right of ownership over the said oil'.[143] In this case, the SPV mechanism was never implemented due to pressure from creditors.[144] But the question remains of why any government would condone the use of such complex vehicles that make it all the more difficult to account for the use of government funds.

There have also been news reports that a loan for a dam project in Congo was guaranteed by the SNPC.[145] Newspapers say that the deal, worth US$280 million, was agreed between the government and Chinese SEMEC group in March 2003,[146] with 85% financed by the Export-Import Bank of China, and 15% by the Congolese government.[147] The Chinese share of the project will be collateralized by Congo's oil; yet another form of oil-backed financing.[145]

Finally, as discussed above, a major provision of the government's settlement of its long-running dispute with Total appears to be a new oil-backed loan of up to US$160 million.

It might be expected that the government would be happy to encourage compliance by SNPC and others with the IMF's work as a prerequisite for massive debt relief. But given the resistance to disclosure via an audit, continued oil-backed lending and the flouting of the stipulation in the Convention that the SNPC return its profits to the state, it is hard to not to conclude that avoiding scrutiny of SNPC's operations is more important to the government than debt relief. Although the IMF 2003 report welcomed some progress by the new government in trying to centralise oil revenue through the treasury, it noted that transparency in the SNPC 'remains problematic'.[148] In October 2003, the IMF suspended negotiations with the Congolese government because of the government's failure to fulfil its commitments under the IMF programme.[149]

The main reason for the suspension was that the government failed to hit its target budget surplus by over US$100 million (CFA 57 billion francs).[149] This surplus is defined in relation to oil prices: the target was set for an average oil price of US$22 whereas in reality the average price was nearer US$28.[150] According to the head of the IMF team, the reason the government did not meet its target despite bumper oil prices was that there had been 'at the level of the SNPC, the retention of oil revenues due to the State; the non-transmission on time of part of the revenues to the Public Treasury; and the use of revenues outside the terms of the budget'.[149]

In effect, according to a source in Congo, the government's oil income was down US$78 million (CFA 42 billion francs) on projections. This was largely because the government made large transfers totalling around US$44 million (CFA 24 billion francs) to the state-owned refinery CORAF, a subsidiary of SNPC, while SNPC failed to transfer a further US$11 million (CFA 6 billion francs) to the Treasury.[151] According to *Africa Energy Intelligence*, 'CORAF is surviving at present on major subsidies from the government … even though the refinery appears on paper to enjoy considerable perks: it makes a lot of money on the sale of gasoline [and receives] other financial advantages which amount to US$20 million per year'.[152] In this case, why is the government continuing to transfer such large subsidies to CORAF?

In addition, according to the head of the IMF team, the government broke its commitments to the IMF by choosing to 'pay off internal arrears, expenses that were not planned for in the state budget for 2003'.[149] The government paid off debts on large infrastructure projects,[153] rather than using the surplus, as agreed, to reduce Congo's external debt and pay overdue salaries and pensions to public sector workers.[138,149] Presenting the budget for 2004 to Congo's parliament recently, the Finance Minister referred to a deficit of over US$540 million (CFA 284 billion francs): a 'hard core' of external debt which went unserviced in 2003.[154] This 'hard core' must include oil-backed loans. If so, then the government effectively rescheduled its oil-backed debt in 2003, once more reneging on its commitment to the IMF not to contract more oil-backed debt, and with the country presumably paying heavily in the process.

At the time of writing, newspapers say that the IMF and the Congolese authorities have agreed a new programme of measures that must be implemented before further discussions on debt relief can take place, including 'transparency in the management of oil' and 'no more oil-backed lending'.[155]

Trawling for profits: Socotram

One Congolese paper sees Socotram this way.

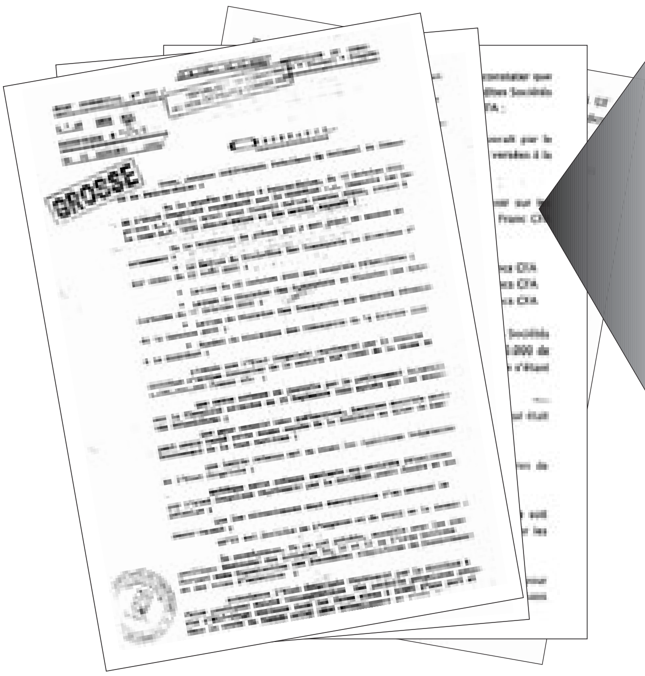
As if these problems were not enough, Global Witness has uncovered another, partially state-owned company that appears to be operating, with the apparent awareness of oil companies, in a completely opaque fashion.

In October 2000, sources including senior oil industry executives and a former MP and ex-Elf employee said that the TotalFinaElf tanker Astro Léon was seized by the Congolese authorities at the terminal of Djeno near Pointe-Noire.[156] Legal documents from the case obtained by Global Witness show that, along with the tanker and its Agip cargo, oil belonging to Total at the terminal was also impounded.[157] The seizures were to enforce a fine of US$9.7 million (CFA 5 million francs) imposed in a dispute between the government and the companies over payment of an export tax to a private company called *Société Congolaise de Transports Maritimes* (Socotram), representing the Congolese state. The government disputed the companies' deduction of around US$8 million from taxes due in September 2000 'to reimburse the maritime tax that they had paid to Socotram'.[158]

Company insiders claim that subsequently a secret settlement was struck between the Congolese authorities and oil companies: the companies would pay the tax but continue to book the payments to the costs claimed upfront from any oil production. Increasing the portion of this 'cost oil' of course reduces the amount paid in profit oil to the Congolese state.[65]

The incident raises several disturbing questions. Firstly, why would the companies reimburse themselves for the payment of the export tax to Socotram unless they questioned its validity? And why would the government allow export taxes to be transferred from the public purse into the pockets of a private shipping company in the first place?

Socotram was originally founded in 1990 as a national shipping company, which gave it the right to collect 40% of the country's shipping taxes on exports and imports as its fee. The state owned only a 45% share in Socotram, and at the time the majority 55% share was in the hands of



Que grande a été la surprise de l'Etat Congolais de constater que pour la fiscalité attendue le 20 Septembre 2000, lesdites Sociétés ont prélevé la somme de 4.086.000.000 de Francs CFA ;

Que selon lesdites Sociétés, cette retenue s'expliquerait par le remboursement de la taxe maritime qu'elles auraient versées à la SOCOTRAM ;

Que par ailleurs, ces Sociétés se proposent de retenir sur les ressources de l'Etat la somme de 4.249.000.000 de Franc CFA par prélèvement successif de la manière suivante :

- Octobre 2000 .... 1.501.000.000 de Francs CFA
- Novembre 2000 .... 2.028.000.000 de Francs CFA
- Décembre 2000 .... 720.000.000 de Francs CFA

Que déjà pour la fiscalité du mois de mai 2000, lesdites Sociétés avaient fait une retenue de la somme de plus 3.000.000.000 de Francs CFA qu'elles avaient dus remboursées par la suite s'étant rendu compte de l'illégalitéde ladite retenue ;

Que présentement, la retenue opérée au titre de l'impôt qui était attendu le 20 Septembre 2000 est infondée et injustifiée ;

Que ladite retenue met en cause les équilibres budgétaires de l'Etat Congolais ;

Qu'il y a donc urgence à ce qu'une mesure conservatoire soit prise pour garantir le rembarsement de ladite somme par les Sociétés sus indiquées ;

Que toutes les démarches entreprises par l'Etat Congolais pour obtenir le remboursement de cette somme sont restées sans réponses positives des Société Pétrolières ;

The government and oil companies in dispute over export taxes to Socotram.

SAGA, a transport and handling company headed by French businessman and close associate of Sassou-Nguesso, Pierre Aim.[159] However, according to an academic source, in 1991 Socotram was 'reorganised' because SAGA lacked sufficient financial resources to invest in the company, and Elf became an additional investor.[160] In 1996, SAGA was taken over by the French Bolloré group but Aim stayed on as an advisor to the company.[161]

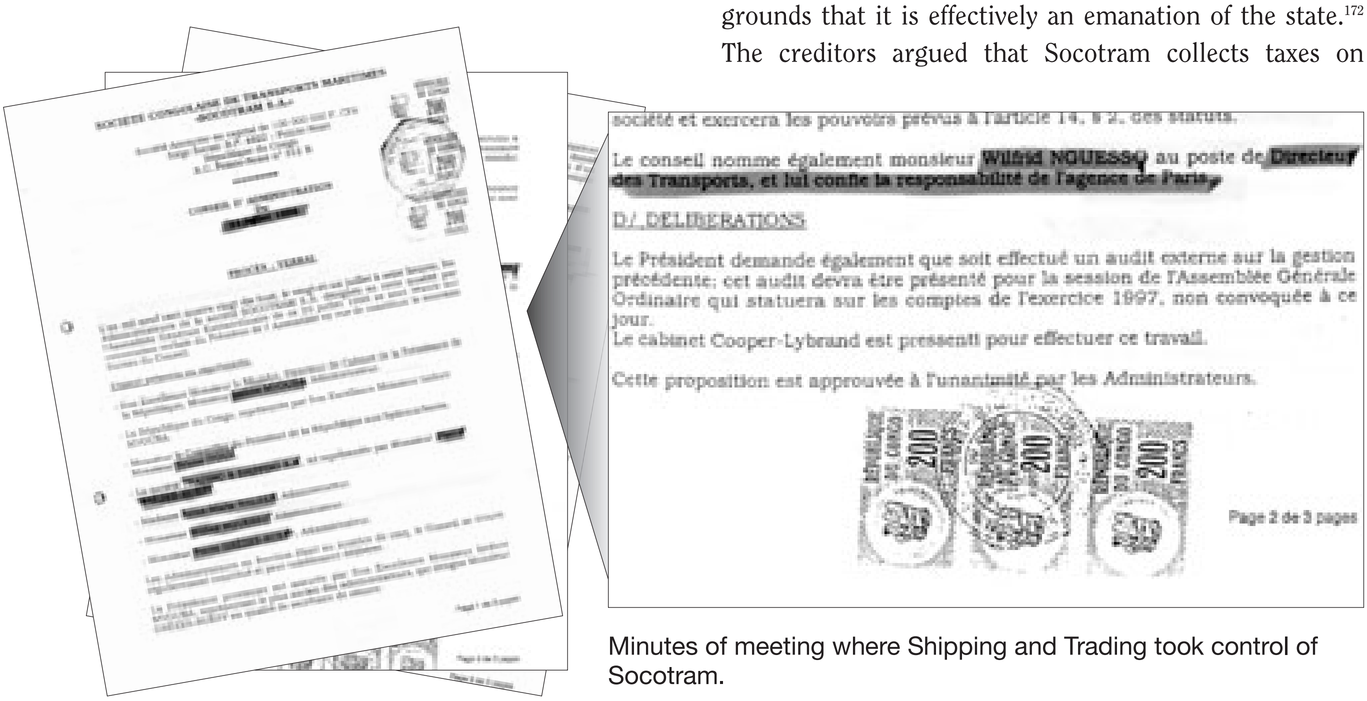
According to newspaper reports, Aim was arrested in Rome on an international warrant for 'abuse of company assets' relating to another of his businesses while travelling with a Sassou-Nguesso delegation in June 2002.[162] He was subsequently released and returned to France where, in October 2003, he was questioned by the authorities. The case is still pending.[163] However, the majority ownership of Socotram had changed long before, according to minutes of a board meeting held in July 1998.[164]

After Sassou's return to power, new decrees issued in January 1998 reaffirmed Socotram's right to collect 40% of the 'shipping taxes' on all oil, timber and other goods transiting through Congolese waters.[165] The minutes of the July 1998 board meeting now identified a new company, Shipping and Trading, as the majority shareholder. No clarification was given as to why SAGA and Elf had been replaced as shareholders.[166] New board members included the Congolese Chief of Staff of the Presidency, Isodore Mvouba, and current SNPC boss Bruno Itoua. Wilfrid Nguesso was named as a representative for Shipping & Trading and nominated Transport Director: Wilfrid Nguesso is the President's nephew.[164/167] No address or place of registration is given in the minutes for Shipping and Trading. However, according to one source, Shipping and Trading operates out of Liechtenstein.[168]

Socotram's mandate grants it royalties of US$2 per ton of oil, of which US$0.60 per ton is to be paid in commission to the Congolese General Directorate of Maritime Shipping (DIGEMAR). If Congo's oil production is an estimated 270,000 bpd, Socotram should receive around US$26 million in revenue per year on oil exports (the company is allowed to charge even more for exports such as timber).[169] The commission paid to DIGEMAR should amount to around US$7.4 million annually. Whilst DIGEMAR is supposed to transfer this money to the Congolese Treasury, newspaper reports say that no accounting lines for Socotram have appeared in the state budget since 1999, when around US$350,000 (CFA 200 million francs) in commission to DIGEMAR was recorded.[170] This is despite the fact that oil companies are on record in the court papers relating to the *Astro Léon* case as paying *at least* US$8 million to Socotram in 2000.

Furthermore, while the 2003 budget does not mention either any revenues from, or transfers to, Socotram, the 2004 budget records that a 'subsidy' to Socotram of US$5.7 million (CFA 3,100 billion francs) was, in fact, paid in 2003, and estimated a payment of US$9.3 million (CFA 5,000 billion francs) in 2004 (see table on p.28).[171] What does this payment represent and why was it not recorded in the 2003 budget?

So where has the money gone? Like the SNPC, Socotram was targeted by frustrated creditors Walker International Holdings and the Connecticut Bank of Commerce, on the grounds that it is effectively an emanation of the state.[172] The creditors argued that Socotram collects taxes on



société et exercera les pouvoirs prévus à l'article 14, § 2, des statuts.

Le conseil nomme également monsieur Wilfrid NGUESSO au poste de Directeur des Transports, et lui confie la responsabilité de l'agence de Paris.

D/. DELIBERATIONS

Le Président demande également que soit effectué un audit externe sur la gestion précédente; cet audit devra être présenté pour la session de l'Assemblée Générale Ordinaire qui statuera sur les comptes de l'exercice 1997, non convoquée à ce jour.
Le cabinet Cooper-Lybrand est pressenti pour effectuer ce travail.

Cette proposition est approuvée à l'unanimité par les Administrateurs.

Page 2 de 3 pages

Minutes of meeting where Shipping and Trading took control of Socotram.

behalf of the Congolese state, that Shipping & Trading is a shadow company registered in Liechtenstein and in reality owned by Wilfred Nguesso, and that Congolese authorities have complete control over the company's operations and revenues.[173] In this case, the court ruled against the creditors, identifying Socotram as a private entity.[172] The matter is currently on appeal.

Thus it appears from the judgement that the revenues from state taxes are going directly into a private entity. Socotram's lawyers stated that Trading and Shipping was the 'transferee of shares' previously owned by SAGA and Elf Congo, and was a company 'in which French private interests are the majority shareholders'.[172] Global Witness has asked Total to clarify whether they still hold any interest in Socotram and, if not, when the transfer of shares to Trading and Shipping was made. At the time of writing, Total had not yet responded.

According to newspaper reports, the category of tax being collected by Socotram is normally imposed by a national shipping entity and its purpose is to finance a national shipping fleet or port facilities.[174] Moreover, standard practice for this kind of tax is that it should go through the Treasury.[175] However, where a country does not have a national shipping line, as is the case in Congo, the World Scale Organisation, which monitors maritime freighting charges, integrates the tax as a 'port tax', that is, an import/export tax.[170] Socotram's lawyers in the debt collection action also argued that its share of shipping taxes was granted by Congo as the equivalent of a state subsidy to help the country establish its own shipping fleet. They stated that although the company's activity is at present limited to freighting, it expects to acquire its own shipping fleet.[172]

According to one Congolese expert commentator, Socotram is in fact modelled on Sonatram, Gabon's national shipping line, which also has hardly any actual shipping capacity.[170,176] In January 1995 the French company Delmas, a subsidiary of the Bolloré group, acquired the Sonatram fleet and in 1997, the Gabonese authorities passed a law authorising shipping taxes on oil and mining products.[177] As with Socotram, since Gabon did not have a national fleet, these taxes amounted to export taxes. The European Union's economic assistance programme advised the Gabonese government that such taxes should be used solely for port and shipping development and that it considered the move to impose export taxes on oil harmful to the country's development; a similar suggestion was also advanced by the World Bank.[178] Under pressure, the Gabonese authorities annulled the law in February 2000.[170,176]

Nonetheless, Socotram is still in business in Congo. Its methods of operation and the fact that no revenues from the company are recorded in the budget raise serious questions about Congo's oil governance. In effect, oil companies appear to be participating in the transfer of state money into private hands for unclear purposes. If the companies were obliged to publish all payments made to the state, as envisaged by the *Publish What You Pay* campaign, then their role in relation to Socotram's revenue gathering would be clarified, and any potential reputational risk averted.

The end of the Elf affair?

The legacy of Elf's four decades of interventions in Congo has been endemic instability, massive oil-backed debt, unaccountable government and a stubborn tradition of opacity in the management of oil revenues, particularly by the SNPC. Since the early 1990s, struggle for control of oil revenues in Congo has gone hand-in-hand with armed struggle for control of the state,[179] leaving in its wake a brutalised population and ever-deepening poverty. The civil strife continues today. According to Amnesty International's 2002 report, hundreds of unarmed civilians were killed and at least 50,000 people were affected by the ongoing conflict in the Pool region of Congo and in Brazzaville.[180]

In September 2003, Congolese church and civil society organisations reiterated the earlier calls for transparency over Congo's oil money, describing it as the key to the country's progress and development.[181] A new Congolese *Publish What You Pay* coalition has specifically called on all the main actors – the Congolese government, the international community, and the oil companies – to play their part. To this end, oil companies should publish what they pay to the government, and the government should lift the gagging clauses in oil contracts, publish its oil revenues, and pass an oil revenue management law promoting clear and accountable management of the country's oil income.[182] The coalition also wants good governance and fiscal transparency to be placed at the heart of any poverty reduction strategy agreed with donors. To that end, the coalition has called on international donors not to grant the Congolese government any new money until it had fulfilled its current promises to reform and requested that, thereafter, lending be tied to specific indicators of the transparent management of Congo's oil wealth.[183]

Will these actors respond to civil society's new desire to hold their government to account over the management of their oil? Given Congo's democratic deficit, strong support for their efforts at the international level is essential. The Elf system could not possibly have operated if there had been mandatory full disclosure by oil companies, as demanded by Congolese civil society and the *Publish What You Pay* campaign. Similarly, if companies were obliged to disclose their payments to the state, Socotram's confusion of the boundaries between public and private revenues, and the cost inflation process by oil companies could not have occurred. Oil companies must now accept responsibility for their role in Congo's conflict-ridden past and present, and prove that they can be a positive force for development by engaging in dialogue with civil society and openly publishing the payments they make for Congo's oil.

Equally, the government must publicly disclose information about its management of oil money, including SNPC's audit, and provide details on tax exemptions to companies and their duration. A situation where the national oil company transfers none of its profits to the national treasury cries out for reform.

The IMF and World Bank programme to improve transparency in the oil sector, as a prerequisite for allowing Congo to escape from its crushing debts, is an important step towards improving Congo's oil governance. The IMF has highlighted that there remains an urgent need for 'routine, rigorous verification of oil sector revenues',[184] and stated that any future agreement on debt relief 'would depend critically upon sustained progress in the implementation of … transparency and accountability in the oil sector'.[185] Yet the SNPC and the government are clearly still not cooperating fully with the reform programme, as the IMF itself acknowledged by suspending temporarily its negotiations with the Congolese government. Interestingly, the IMF has also recently recognised that mandatory disclosure by companies as advocated by the *Publish What You Pay* campaign would be an important step in achieving transparency in Congo.[186]

The IMF's firm stand so far is commendable. But during meetings in Paris last year between multilateral and bilateral donors and the Congolese government, the World Bank and other donors instead congratulated the government on its progress in improving economic governance.[187] According to a World Bank statement, the donors also agreed on the need 'to ensure the country's quick access to debt relief'.[188] This undermines the IMF's position.

The head of the IMF team recently commented that 'Congo has, in fact, benefited from nine previous programmes which have not achieved the proposed objectives'.[189] Given this poor record, the IMF, the World Bank and others must make absolutely clear to the Congolese government that entry to the HIPC initiative is conditional on the implementation of fiscal transparency and good governance, with a particular focus on making SNPC accountable. Such conditionality should also be extended to any further multilateral and bilateral aid to the country.

In the words of one international agency source observing the Congo oil audit process, there is a real danger that once the government is granted access to debt relief, transparency reforms will simply be abandoned.[190] Indeed, the French government has gone so far as to promise to champion Congo in upcoming negotiations on debt relief with the IMF and the EU, stating that France was 'very strongly committed' to pleading the Congolese government's case.[191]

France has a particular responsibility to help improve management of oil money in Congo both because of its historical support for the Elf system and its recent commitments to revenue transparency through the G8 Declaration on Fighting Corruption and Improving Transparency and its participation in the UK government's Extractive Industries Transparency Initiative.[192] In June 2003, France's representative at the EITI stated that his government stood fully behind the initiative and was prepared to enter into a dialogue with states and companies to make headway on this issue. In the light of these commitments, France should as a first step encourage the Congolese government to begin piloting disclosure of its oil revenues through the EITI, and to respond to civil society's concerns about where the oil money is going with concrete measures such as publication of the audit.

To date, there has been no meaningful consultation by the government with the civil society groups supporting greater transparency over the management of Congo's oil revenues. The IMF, recognising the 'keen interest in oil sector policy matters in the Congo', has recommended that the government should engage more systematically with civil society, ensuring 'the broadest participation possible' in the elaboration of its poverty reduction strategy.[193] Yet only recently, the government adopted a draft strategy for reducing poverty without even agreeing it with the IMF or civil society.[155, 194]

Congo remains a test case for the commitment of the international community to achieving real change on revenue transparency. Together with disclosure by oil companies, a strong stand by donors and the international financial institutions could, not before time, push Congo towards reform and solvency.

Angola

Dos Santos won't answer the questions that matter.
Credit: Joao Silva/Corbis Sygma

Money unaccounted for: almost US$1.7 billion per year from 1997-2001.

Wealth for the few, poverty for the many

Nowhere are the devastating effects of revenue misappropriation and state corruption more starkly illustrated than in Angola, where one in four children will not live to see the age of five. One in four is also the ratio of money that disappears from the state budget each year. The two figures are related: while most Angolans suffer devastating poverty, oil income has enabled some top officials of the ruling *Movimento Popular de Libertação de Angola* (MPLA) to become very, very rich. As one Angolan journalist puts it: 'the workers' party has become the millionaires' party'.[1]

Global Witness highlighted the wholesale looting of state revenues in Angola in two earlier reports, *A Crude Awakening* (December 1999) and *All the Presidents' Men* (March 2002). Mechanisms of money misappropriation have included offshore money laundering, over-priced military procurement and a deliberately opaque method of running up debts against future oil production. This section updates and expands on our earlier reports and underlines that, at a time when Angola is on an international publicity drive to improve its image, little has really changed.

All the Presidents' Men drew attention to the 'Angolagate' scandal, showing the way that Angola's ruling elite profited from the brutal civil war between the MPLA and the rebel *União Nacional para a Independência Total de Angola* (UNITA). Members of this presidential elite (known as the *Futungo* after President dos Santos' seaside stronghold) worked with associates in France and elsewhere to skim huge sums from the government's military procurement process.[2] These arms deals, and the kickbacks that went with them, were paid for with oil revenues.

It became clear that the persistent lack of disclosure of basic payments to the Angolan state by international oil companies meant that, by default, they were complicit in the looting of state resources in Angola. It was with Angola in mind that Global Witness and others first launched a call for extractive industries to publish their payments to governments so that ordinary citizens, who own Angola's oil under the country's constitution, could find out where their revenues were going. Without such transparency, there can be no accountable management of Angola's oil wealth.

The death of sociopathic UNITA boss Jonas Savimbi in early 2002 meant the end of Angola's civil war.[3] However, Angola's citizens have yet to see any real peace dividend. Instability is rife and military operations continue in the oil enclave of Cabinda. There is now is a major concern that the mechanisms of embezzlement entrenched during the war will simply be redirected towards profiteering from the country's reconstruction. Although the government has gestured towards joining the international community and invited the International Monetary Fund (IMF) to assist with poverty reduction and economic growth, national elections remain on hold, the *Futungo* continues to borrow against future oil revenues, and the country's oil income remains completely non-transparent.

The *Futungo* undoubtedly find any external scrutiny of their actions unsettling; however, mismanagement and misappropriation of oil money appear to have led to a cash crisis so serious that the government is desperately in need of re-financing from the international community. In a reflection of this external pressure for transparency, the government has recently published on its website a heavily edited summary of a tracking exercise for Angola's oil revenues by accounting firm KPMG, called an 'Oil Diagnostic'.[4] For the first time, this report affords the public some insight into the dire state of Angola's oil accounts, including the meltdown of the government's 'Petroleum Account' that was specifically established to improve revenue tracking.

The government has also allowed the IMF to publish the results of its 2003 Article IV consultation exercise, which describes the IMF's surveillance activities in Angola and provides an overall summary of the country's macroeconomic situation.

While the publication of both reports is a necessary first step towards transparency, they stop far short of providing all the information that would allow thorough public scrutiny of the *Futungo*'s bookkeeping practices. Indeed, the government is currently holding back the publication of other more detailed and forthright reports, including the IMF's 2001 and 2002 Article IV reports and staff commentaries.

Having obtained these documents, Global Witness is able to shed light on exactly what the Angolan leadership was hoping to hide. The 2001 and 2002 reports paint a damning picture of the government's fiscal impropriety and its deliberate obscurantism, in contrast to the published 2003 report, which contains no such commentary (see section: 'The reports they don't want you to read'). Figures from the 2002 report imply that an average of US$1.7 billion has gone missing each year from 1997-2001 from the Angolan treasury. Meanwhile, the international community has struggled to raise the US$200 million required to feed the one million Angolans dependent on aid.

A million Angolans depend on food aid.

Angola's elite has responded to calls for improved transparency by claiming that decades of civil war have left the country without the capacity for transparent government. Accountability and democratic debate are, apparently, a luxury. But the very same incapacitated government has recently begun to use opaque 'Special Purpose Vehicles' in tax havens to service new oil-backed loans. Banking records belonging to the Angolan state oil company Sonangol, revealed by the International Consortium of Investigative Journalists, show its adeptness in using complex offshore structures to move money around and to pay overseas business partners. The records also show that almost none of Sonangol's income touches Angolan soil despite national laws requiring oil money to be managed through the central bank. This ability to manage such sophisticated mechanisms demonstrates that it is not financial expertise that the *Futungistas* lack, but the political will to reform.

This section also covers Angola's dodgy debt renegotiations, missing multi-million dollar signature bonuses, and under-the-table payments made by former French state oil company Elf Aquitaine, details of which have been provided by the recent trial of more than 30 senior former company employees in Paris. Elf paid money to Angolan officials on both sides of the war, helping to fuel decades of bloody conflict that destabilised the whole region.

In each of the cases detailed below, major financial improprieties and accounting fraud would have been detected if oil companies and the government had been obliged to disclose details of their financial transactions. Unless the international community acts systematically to ensure that oil income is managed transparently, then the opacity surrounding oil money in countries like Angola will continue to result in massive public losses for private gain and the grinding poverty of ordinary Angolans will continue.

Elf and Angola

The Congo Brazzaville section of this report revealed how French state oil company, Elf Aquitaine (recently taken over by TotalFina and now re-branded as 'Total') developed its presence across Africa through a web of influence-peddling, kickbacks and opaque offshore banking. The same cast of characters and the same system operated, with similarly devastating results, in Angola.

French prosecutors in Paris filed a 600-page indictment charging 37 former Elf executives with 'misuse of company assets' in March 2003.[5] The indictment detailed how Elf acted as a *'pompe à finance'*[6] (or 'cash cow'), setting up a highly opaque system of financing to pump company money into Swiss bank accounts to pay off African leaders and other key decision makers.[7] There was nothing illegal under French law about the largesse distributed by Elf at the time. The Paris trial looked only at allegations that this system was subsequently abused by Elf executives to embezzle money for their personal use, thereby defrauding the French government of millions of francs between 1989 and 1993.[8]

The trial ended in Paris in mid-November 2003 with the conviction of 30 of the accused and penalties including prison sentences and heavy fines.[9] To make its case, the prosecution provided extensive details about a series of offshore structures and a deliberately opaque way of doing business instituted by the company executives to distribute largesse to leaders across Africa[10] and to allow the company to manipulate national and international politics to its advantage. This so-called 'Elf System'[11] used oil-backed loans to mortgage countries' future revenues for ready cash, and the payment of off-the-books bonuses and 'subscriptions' to officials in several African countries. Angola, where Elf won its first contract in 1978, was one of these countries and, like Congo Brazzaville, saw the system spiral out of control.[12]

Jack Sigolet, who was not charged with any offences, was the Elf executive in charge of arranging oil-backed financing for African leaders. He testified that the loan system was conceived 'in such a way that the Africans were only aware of the official lending bank and were ignorant of the whole system which Elf rendered particularly and deliberately opaque'.[13] According to his testimony, Sigolet arranged several oil-backed loans for the Angolan government during the civil war: for US$50-100 million in 1990; US$200 million in 1992; US$50 million in 1994; and further loans for unspecified amounts from which the company benefited handsomely.[14]

The indictment describes how, although the company's official policy was to support the existing government,[15] Elf sought to maintain its influence on events by bankrolling both sides,[16] assigning different men to handle each faction: André Tarallo to the MPLA and Alfred Sirven to UNITA.[17]

The testimony by Yves Verwaerde, a former member of the European parliament and a supporter of UNITA, describes how Savimbi 'reproached Elf for having gone beyond its economic role and played the role of a political agent. He accused Elf of having financed military operations, in particular helicopters, used by the government against UNITA'.[18] As a result, Savimbi 'threatened to blow up Elf's oil facilities in retaliation'.[18]

But UNITA were also on Elf's payroll. The indictment records that between US$16-20 million was paid to UNITA from accounts controlled by Sirven during the run-up to the 1992 elections, after the Bicesse Accord ceasefire the previous year.[19] According to the indictment, Elf and UNITA reached a secret agreement in August 1992, one month before the elections, which would give Elf a leading role in the country if the rebel group should win power.[20] According to one witness, the aim of the payments was 'to finance [UNITA's] election campaign'[21] but, given that UNITA was in fact re-arming even as it campaigned for election, there can be no guarantee that the money was not spent on military materiel. In the event, UNITA lost the election and fighting broke out again.

By funding both sides in the conflict, Elf probably helped to prolong Angola's four-decade-long civil war. The war cost some 1.5 million lives and displaced 4.5 million people.[22] The only reason that this iniquity has come to light is because the French judiciary sought to investigate the misappropriation of millions of francs of public revenues by company officials via the 'Elf system'.[23] The tragedy of the current situation in Angola is that ordinary Angolans are denied the same right to reclaim lost assets in their country because of the continuing lack of transparency in its oil business.

Angolagate revisited

Previous Global Witness reports have sought to highlight the way that the Angola's civil war provided a cover for the full-scale looting of the country's oil money by national and international business and political elites, typified by the Angolagate 'arms-to-Angola' scandal that broke in France at the end of 2000.[2]

Angolagate is the story of how a legitimate exercise in self-defence by the MPLA government against UNITA turned into a conspiracy to rob the country of its oil money through over-priced military procurement, kickbacks and the mortgaging of future oil reserves for ready cash in the form of oil-backed loans. Recently, details of the scandal have been further verified by the public testimony of Jean-Bernard Curial, formerly in charge of Southern Africa for the French Socialist Party, charged with 'complicity in the misuse of company assets'; 'complicity in the abuse of trust'; and 'illegal arms trafficking'.[24] The Angolagate case is still pending. The scandal not only provides a disturbing insight into Angola's oil mismanagement in time of war, but also raises major concerns that the system exists in a modified form today.

May 1991 saw the signing of the Bicesse Peace Accords, which were taken by many as a sign that the country's post-independence civil war was finally at an end. Whilst the government forces demobilised in (mostly) good faith, UNITA did not. When the MPLA won the 1992 elections, Savimbi refused to accept defeat and resumed hostilities. In the meantime, the collapse of the Soviet Union had cost the Angolan government its greatest financial and military supporter. UNITA was able to seize and hold large cities for the first time, capturing five of the eighteen provincial capitals in one the most brutal stages of the war.[25]

Losing ground to UNITA, Angolan President dos Santos turned to sympathisers in the French establishment for help in the war effort. In April 1993, he approached Jean-Bernard Curial, who at that time headed a humanitarian aid company called Stired, which purchased food and medicines for Angola and Mozambique on behalf of various French ministries.[24]

Although France had various economic and political interests in Angola, not least its oil investments, the French government was divided in its allegiances. Mitterrand's centre-left presidency was cohabitating with the centre-right administration of Edouard Balladur and the defence ministry, which would have been the obvious avenue for military assistance to the Angolan government, was controlled by staunch UNITA supporter François Leotard.

According to Curial, Mitterrand's son Jean-Christophe, ex-advisor for African affairs to the French presidency, stepped into the breach and introduced Curial to businessman Pierre Falcone.[24,26] Falcone worked as a key advisor to a security export company, Sofremi, which was controlled at the time by the French interior ministry under Charles Pasqua.[27] Falcone also owned a set of private logistics and procurement companies, under the umbrella organisation Brenco International.[28]

Pierre Falcone

Arkadi Gaidamak

Falcone then worked with Russian émigré and businessman Arkadi Gaidamak (also spelt 'Gaydamac').[29] In a telephone conversation with Global Witness, Gaidamak claimed that he and Falcone travelled to Angola where they were provided with Angolan diplomatic passports, after which they operated as *de facto* Angolan officials.[30] During this conversation and earlier in press reports, Gaidamak claimed that the purpose of their cooperation related only to the provision of oil-backed loans for Angola and strenuously denied that they had been involved in the supply of weapons. In a later conversation with Global Witness, however, Gaidamak admitted that arms had in fact been supplied but justified this arrangement on the grounds that these deals had been arranged with a legitimate government.[29]

The scars of Angola's war.

According to *Le Monde*, Curial's testimony to Judge Philippe Courroye, chief investigator of the Angolagate affair, states that the first contract to supply materiel to the Angolan government was signed in November 1993 and provided some US$47 million worth of mostly Russian arms to Angola. In April 1994, it was amended to cover a total of US$463 million worth of materiel.[24] Curial was in charge of supplying humanitarian aid and equipment such as uniforms at that time. Curial testified that he chose to distance himself from these operations in 1995 after he began to see them as '*une gigantesque escroquerie* [a gigantic fraud]'.[24]

The Angolan government did not have the money to pay for the arms directly, so a system of high-interest loans against future oil production was devised: those arranging the provision of materiel would be paid an initial sum up-front; they would deposit this money and send for the weapons; and an oil-backed loan would then be raised from French banks and disbursed out of Paris to cover the remaining costs and fees.[30] Gaidamak has previously confirmed to Global Witness that he and Falcone were 'made signatories' on accounts that they set up with Banque Paribas for the process of generating oil-backed loans and that they acted for the government.[31] This suggests that Gaidamak and Falcone had control over the funds obtained from the loans, which were, in effect, a significant part of the Angolan state budget, located and disbursed entirely extra-territorially from Angola itself. And it is here that the supervision and accountability of those involved in the procurement process may have begun to falter.

Curial alleges in his testimony that this offshore procurement process outside the national budget became a 'huge money-making machine' for Falcone, Gaidamak and Angolan leaders.[24] However, commissions and kickbacks were not illegal under French law at the time.

Official interest in the Angolagate deals began with a French Financial Brigade investigation into possible tax evasion on the 1993 and 1994 arms contracts. The Financial Brigade subsequently removed some 50,000 documents from premises connected to Falcone and Gaidamak in early 1996 and filed a request to Brenco for over US$220 million in taxes in 1998 – the largest request for back-taxes in French history.[32]

A raid on the apartment of Falcone's secretary during that investigation recovered 26 diskettes that contained numerous details of payments to people connected to Brenco and its operations. The disks recorded payments by Brenco to major figures in the French political establishment, but it is the size of commissions to a number of prominent Angolans that is most remarkable. *Le Monde* reported that, according to the investigators, Angolan ambassador without portfolio in Paris, Elisio de Figueiredo, received US$18 million in commissions for his part in the deals.[33] Given that he was acting on behalf of the Angolan government at the time, why this massive personal payment? As revelations of his activities mounted, de Figueiredo left Paris. He has since returned and is currently serving as 'Plenipotentiary Ambassador'.[34] According to French newspapers, he has been called for questioning on several occasions by the French Financial Brigade investigators but has never responded to their requests. He has not been charged.[35]

In his testimony to investigators, Curial alleged that Falcone and Gaidamak made US$300 million from the April 1994 deal, equivalent to 65% of the asking price in the contract and that part of this sum was then passed on to Angolan officials.[24] If true, this claim confirms the earlier concerns about their commissions, and kickbacks to others, expressed in *All the Presidents' Men*.[2]

According to Curial's testimony, kickbacks were so common that Elf finance executive Jack Sigolet had come to refer to Angolan officials by the percentage of their cut. For example, José Leitão de Costa, Secretary to the Council of Ministers, was known as 'Mr Thirty Percent' and de Figueiredo as 'Mr Twenty Percent'.[24]

Curial also admitted to making money himself from the procurement process.[24] In his testimony, he described how some US$3.6 million passed through an account in Brussels under his control between 1993 and 1996. After keeping part of this money for himself, he passed the rest on to Angolan officials and twice delivered cash payments of FF200,000 (around US$40,000) to de Figueiredo during 1994-1995.[24]

In December 2000, Falcone was arrested and charged with 'illegal arms trading, fiscal fraud, misuse of company assets, abuse of trust and influence peddling'.[36] He was jailed in Paris and subsequently released on the highest bail in French legal history. French weekly magazine *Le Nouvel Observateur* alleged that the bail money was to be paid back by Angolan state oil company Sonangol as a gesture of solidarity.[37] In June 2001, Falcone released a letter through his US spokesman, Jason Rose, in which he protested his innocence of the charge of arms trading, which he said 'is totally false! The accusation is as destructive and unjust as the charge of witchcraft was in the Middle Ages. Legally, nothing stands up to close scrutiny. What then, am I accused of morally? Of making a lot of money? Most certainly. And I have.'[38] In January 2001, an international arrest warrant was issued for Arkadi Gaidamak, who had refused to appear for questioning before Judge Courroye. In an interview with *Le Monde*, Gaidamak stated that he would be prepared to meet Judge Courroye but only if 'he ensures I am going to be treated correctly. For the moment this is not the case'.[39]

Falcone confirmed payments to figures such as Elisio de Figueiredo but argued that they were 'in order to facilitate things and not to buy people'. He went on to clarify: 'In other words, it is not corruption, but it is *within the operational logic* over there in Angola [emphasis added]'.[33]

Global Witness has highlighted other arms deals funded by loans in 1995-96 and the operations of other companies within Falcone's Brenco group in Angola. One such company, *Companhia Angolana de Distribuição Alimentar* (CADA), reportedly secured a US$720-million contract in 1999 giving it a five-year monopoly over food supplies to the Angolan army, the *Forças Armadas de Angola*.[40] Sources in the food industry describe how the company was then routinely allowed to escape the import auditing procedures to which other companies were subjected.[41]

The Portuguese daily *Público* stated that, according to its sources, the CADA contract was pushed through without any form of public tender, and that the contracting of CADA was part of a process whereby control over resources and supplies was brought directly under the control of the Presidency.[42]

Although the war is now over, opaque procurement deals persist. A recent case spotlighted Peru's sale of six Tucano aircraft to Angola for US$4.8 million in October 2001.[43] This led to criminal charges being filed in Lima against 30 senior Peruvian officers by a state prosecutor for 'alleged crimes of collusion to the detriment of the state, public faith and omission of functions … when they reached agreements to favour third parties to the detriment of the Peruvian treasury'.[44] The media reported the prosecutor as estimating that the treasury 'had failed to receive $2 million for the sale'.[45]

According to press reports, the deal went through an intermediary in the Virgin Islands called Trade Air Corporation.[46] This violated internal Peruvian airforce procedures principally because 'the authorization was for a direct sale to the Angolan government'.[44, 47] Trade Air's role was officially confirmed by the Angolan Chief of Staff, General Pedro de Morais Neto, who stated that the company was 'obviously' paid a commission for its services.[47]

One Peruvian Air Force spokesperson commented to Peruvian daily *El Comercio* that because the deal involved 'directly or indirectly three presidents, three ministers, five commanders-in-chief, five chiefs of staff, five heads of procurement, five operational commands and four teams of experts, "this makes it impossible that there was any concerted criminal operation"'.[48] It seems, however, that questions over pricing, alleged commissions and the use of opaque intermediary companies continue to surface in relation to Angola's procurement process.

Turning debt into money

Given the track record of profiteering from the war effort, a major concern is that the reconstruction effort may also be vulnerable to the same practices. Nowhere is this

A Sonangol refinery in Luanda, Angola.

danger clearer than with Angola's attempts to restructure its debts. Coupled with the marked absence of any peace dividend for ordinary Angolans, this concern provides a compelling rationale for insisting on transparent management of Angola's oil money.

Angola is heavily indebted. At the end of 2001, the country owed about US$9.6 billion to foreign creditors, or 129% of its average annual export income. Of this debt, US$4.8 billion (ie. half) is in arrears.[49] As with arms procurement, the restructuring of the country's debts appears to have been exploited to covertly move more of the nation's wealth through opaque offshore accounts.

A case in point is Angola's Russian debt. By 1996, the Russian debt stood at US$5.5 billion. In November that year, agreement was reached to reduce this debt by 70%, leaving an outstanding US$1.5 billion in the form of 31 promissory notes to be paid off between 2001 and 2016. This sum later increased to US$1.9 billion because of accrued interest.[50] Falcone and Gaidamak appear to have worked directly on rescheduling the Russian debt from 1996 onwards, using an intermediate company called Abalone Investment Limited.[50] A Russian billionaire banker called Vitali Malkin, who reportedly had close ties to ex-premier Boris Yeltsin, was also a shareholder in Abalone.[51]

Falcone is quoted in *Le Monde* as saying that that he and Gaidamak 'were trying to obtain an agreement to abandon 70% of the Angolan debt vis-à-vis Russia, and the re-scheduling of payments for 30% of the debt over 20 years'.[52] Falcone said his payment for these services was 'less than US$15 million'.[52] Gaidamak is quoted by Israeli paper *Yedi'ot Aharonot* as saying, 'as a matter of fact, I even supervised the relations between Russia and Angola, looking after the interests of both parties'.[53] He denied that there had been any misappropriation of funds to *Le Monde*, explaining that he and his partners in Abalone had made US$50 million in three years in a 'classic trading operation, extremely favourable for us'.[54]

In February 2002,[55] a Geneva-based investigation into the possible involvement of Pierre Falcone in 'money laundering, support for a criminal organisation' and 'corruption of foreign public officials' resulted in money in Switzerland and the remaining half of the Russian promissory notes being frozen.[56] Swiss newspaper *Le Temps* stated that one of the reasons for the investigation was that 'instead of being deposited in favour of the Russian state, in theory the owner of this debt, the bulk of this amount was deposited into the accounts of high-ranking officials of the two countries'.[55] The Swiss investigation is still pending. Neither Gaydamak nor Malkin have been charged.

Global Witness has obtained a list of transactions through Abalone's account (No. CO-101436) at a Geneva branch of UBS bank between 16 June 1997 and 17 June 2000 which confirms newspaper reports that US$774 million was paid to the company between 1996 and 2000.[57] The document shows the account flooding with money from Sonangol and then almost immediately draining out. Very few of the transfers listed appear to have gone to the Russian government: of a total US$773.9 million paid in by Sonangol, only US$161.9 million was passed on to the Russian finance ministry.[58]

The rest of the listed transfers went to Falcone, Gaidamak, Malkin, Angolan officials and a series of obscure offshore companies. Falcone and his Brenco group of companies are recorded as receiving US$88 million directly (US$57.7 million to Falcone himself). Gaidamak is recorded as receiving US$60.5 million, Malkin US$48.8 million, and US$3 million is recorded as being sent to Angolan cabinet secretary José Leitão da Costa e Silva. *Le Monde* also reported that some US$4 million from Abalone was transferred to another Angolan official in two US$2 million transactions, although Global Witness is not able to confirm this report on the basis of the document in its possession.[56]

The transaction records raise a host of interesting questions, including the identity of the beneficial owners of company accounts that received payments from Abalone, such as Bastwick Trading and Malagas Financial Ltd in Amsterdam, AB Petroleum in Luzern, Loke Trade in Fribourg, Technopromexport in Moscow, Antalla Ltd and Nordson Financial Ltd in Nicosia, Penworth Ltd in Geneva, Dynatron Ltd and Candelbrum Ltd in Luxembourg. There is no indication from the document as to what role, if any, these companies played in the debt rescheduling deal: their presence confirms no more and no less than that they received the specified payments from the Abalone account.

The transactions also include some US$41.9 million being paid to an account (No. 25785; reference 'Lisbonne') at the Banque Indosuez Luxembourg (now Credit Agricole Indosuez). *Le Monde* states that 'according to Judge Devaud [the Swiss Prosecutor], more than 40 million dollars, transferred between 3 October 1997 and 15 January 1998 from the Abalone account at the UBS in Geneva to an account opened at the Credit Agricole Indosuez in Luxembourg was 'in all likelihood' destined for Mr de Figueiredo and dos Santos'.[56] An internal memorandum reviewed by Global Witness, dated 22 June 1999 from UBS's Legal and Compliance Department, describes how the Russian debt repayment agreement was to work after the bank agreed 'to act as 'escrow agent' for the deal at the request of Glencore UK Ltd' [the subsidiary of the private Swiss oil trader Glencore International] in April 1997. According to the memo:

> 'Glencore UK Ltd. is to obtain loans for future Angolan oil sales from commercial banks [….] The proceeds of these oil-backed loans is transferred by Glencore UK Ltd into our accounts for use by Sonangol, the Angolan state oil export company, so that it can finance the repurchase of these [debt] obligations. Sonangol then transfers through our bank to the buyer, Abalone Investements [sic] Limited, its remuneration for its role as determining intermediary in this operation to buy back the Angolan debt and the price fixed by the Russian Finance Ministry for the repurchase of its obligations. Then, UBS will transfer the amount corresponding to the cost of these obligations to Unicombank. In return and simultaneously, Abalone Investments Ltd receives from the UBS the obligations purchased and their repayment certificates, and returns them to Sonangol on behalf of Angola which can cancel them and thus progressively erase its debt to Russia.'[59]

According to the memo, Glencore International confirmed in writing to the bank that it would pay the 'escrow fees' for the account, and that it would reimburse all costs and fees of third parties that may not have been settled in advance by Abalone Investments Ltd.[59] The arrangement to pay the account fees appears to be confirmed by two payments by Glencore into the UBS account.[58]

This is a highly unusual state of affairs, in which the Angolan government is using a opaque private third party (Abalone) as an intermediary in the repayment of its sovereign debt to Russia. Moreover, it raises the question of why a private oil trader would pay the account fees on behalf of Abalone.

The deal also raises the question of what UBS understood about the parties to the transaction as the bank holding Abalone's account, particularly in the light of the subsequent investigations. Another internal memorandum from UBS' Legal and Compliance Department dated 6 September 1999, titled 'Abalone Investment Co', raised 'the question of reputational risk' to the bank in the light of the proposed changes 'desired by the MOF [Russian Ministry of Finance] and Abalone'.[60]

The principal change reviewed in the 6 September memo was that Angola's debt obligations would not be covered

Transactions through the account of Abalone Investments Ltd, UBS, Geneva. Companies' presence on this list indicates no more than that they received a payment from Abalone.

'by the transfer of a sum of US$ but by delivery to the MOF of securities representing Russia's debt to its creditors in the London Club (PRINs [Principal notes]/IANs [Interest Accrual Notes]), securities which are valued on the stock market'.[60] The other change to the arrangement discussed in the memo is that the Russian Ministry of Finance account was to be managed not by Unicombank but by another Russian bank, SBERINVEST, due to the former at the time 'having had its banking licence withdrawn and now being in administration'.[60] The memo outlines the bank's concerns about these changes as 'UBS will have no way of controlling whether the price for the [Angolan] State Obligations and Repayment Certificates has been paid in advance by Abalone because this verification falls within the framework of the agreement between Abalone and SBERINVEST to which UBS SA is not party'.[60] The memo also highlights that,

> '…this transaction is in relation to two countries that have become more sensitive and unstable, Russia and Angola, and any possible mention of one of the

representatives of one or other of the parties such as Abalone, SBERINVEST or the MOF [Russian Ministry of Finance] in a newspaper article, even if a posteriori this is judged to be unfounded or indeed libellous, would not prevent, in the first instance, a Swiss or particularly Genevan judge taking an interest in the people mentioned'.[60]

Finally, 'the most delicate point' according to UBS is that there was 'no official confirmation from the MOF and the Russian government' authorising this change to the form of payment for the debt and the new agreement '[did] not bear any official MOF seal and the signature of its representative is not certified'.[60]

A fax from Abalone Investments Ltd to UBS, dated 22 September 1999, appears to show that UBS' role in the agreement was subsequently terminated on the initiative of SBERINVEST.[61] However, the Abalone account records also appear to show that the UBS account CO-101436 continued to operate until at least July 2000. This implies that UBS did not immediately act on the internal risks that it identified in the memo. But in all events it appears that, as Swiss newspaper *Le Temps* put it, 'the internal compliance department of UBS expressed serious doubts about the legality of the transaction'.[62]

Le Monde reported that several bank accounts in Luxembourg also received transfers related to the Russian debt repayment and that French magistrates received information from Tracfin, the anti-money laundering service of the French Foreign Ministry, that Falcone had opened accounts for three Panamanian-registered companies at the Banque Internationale de Luxembourg (BIL). The paper also stated that '[a]ccording to Tracfin, the 'economic beneficiaries' of these accounts were Mr Falcone himself, Mr de Figueiredo and the Angolan President José Eduardo dos Santos himself.[54] A later article reported that 'when questioned on this point [by the French judiciary], Mr Falcone "strongly den[ied] Tracfin's assertion"'.[56]

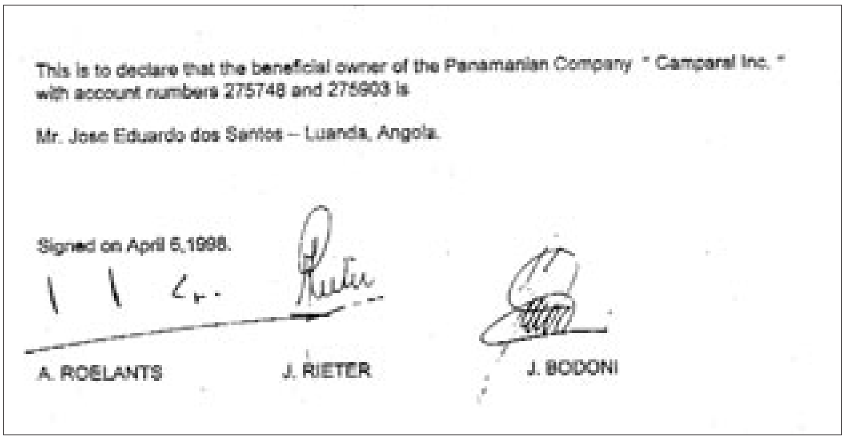
French weekly *Le Canard Enchaîné* subsequently reported in December 2003 that the French judiciary confirmed President dos Santos as the beneficiary of the US$37.11 million deposited in one of the BIL accounts. The newspaper reproduced a document on BIL-headed notepaper signed on 6 April 1998 by three of the bank's representatives confirming that 'the beneficial owner of the Panamanian Company 'Camparal Inc' with account numbers 275748 and 275903 is a 'Mr José Eduardo dos Santos – Luanda, Angola'.[63]

Documents relating to the French investigation seen by Global Witness state that the beneficiaries of the other two accounts, Dramal and Tutoral, were Pierre Falcone and Mr de Figueireido respectively. Dramal contained around US$1.8 million and Tutoral around US$7.3 million.

These documents also reveal a complex chain of transfers in August-October 1997 via accounts belonging to Falcone's Brenco Trading Limited (BTL) at the Banque de Gestion Edmond de Rothschild which ended with the Panamian companies at the BIL. The transfers, totalling around US$98 million, originated from bank accounts in Geneva, including US$48 million from the Abalone UBS account set up for the Russian debt buy-back.[64]

This points to the highly unusual situation where the president of a sovereign state collects a multi-million dollar payment from the restructuring of his country's national debt.

Le Temps reported that the Dramal, Tutoral and Camporal accounts were subsequently transferred to three accounts at the Discount Bank in the Cayman Islands in 1999.[65] According to *Le Temps*, a Swiss banker questioned by Judge Devaud also testified that the accounts were effectively managed from Geneva and that US$56 million in one of the accounts is 'the fortune of the president of Angola, José Eduardo Dos Santos'.[65] *Le Temps* itself described the contents of the alleged presidential account as 'public assets' transferred to an offshore company owned by Falcone, by way of payments for Falcone's services to the Angolan state.[65] According to *Le Monde*, the same investigation has also shown that 'Elisio de Figueiredo … received some US$18.8 million in an account opened in the Cayman Islands'.[33, 54]


This is to declare that the beneficial owner of the Panamanian Company " Camparal Inc. " with account numbers 275748 and 275903 is

Mr. Jose Eduardo dos Santos – Luanda, Angola.

Signed on April 6,1998.

A. ROELANTS J. RIETER J. BODONI

Three bankers testify that a Mr José Eduardo dos Santos is the beneficial owner of a bank account containing US$37 million in Luxembourg.

According to press reports and other sources, the outstanding half of the Russian debt repayment, around US$700 million held in the form of promissory notes, remained frozen in Switzerland until October 2003, as a result of these revelations, when they were unblocked and released to the Russian government.[66] *Africa Confidential* also reported that 'Russia told the Paris Club it had roughly US$700 mn. of fresh claims on Angola, which had last year told the IMF that all such debts had been cleared'.

Slum in Luanda: wherever the money goes from Angola's many loans, it isn't here. Credit: Jeremy Horner/Panels Pictures

Le Temps said that, according to a 'senior representative of the Federal Foreign Affairs Department,' a deal was agreed between the Swiss and Angolan governments in April 2003, to repatriate to Angola the contents of all the Swiss accounts frozen during investigations into the debt restructuring, where they are to be used for development purposes under the supervision of a commission including Swiss representatives.[65,68] However, there appears to be no *public* information about how much Angolan state money is blocked, when it will be returned or exactly how it will be managed. Moreover, according to *Le Temps*, 'Angola does not want to include the accounts at Discount Bank [in the Caymans] in the agreement, since this would mean admitting that they were its property'.[65] At the time of writing, it is reported that the Swiss request to block the funds now in the Caymans has been rejected and their current whereabouts is unknown.[69]

The IMF has also questioned the Angolan government about these highly unusual debt deals. According to a document passed to Global Witness, the IMF states that '[i]n early 2002, the [Angolan] authorities explained that the intermediary [Abalone] helped facilitate the sale of arms to Angola and that a total of US$1.5 billion had already been paid to this company. The company had, in turn, bought the entire debt from Russia at an unspecified price.'[70]

This statement by the Angolan government to the IMF about military procurement raises additional questions as to what Abalone was up to. However, when questioned further, Angolan officials 'were not able to give details of these loans because it would infringe on their national sovereignty'.[70] In the face of such worrying levels of secrecy over external borrowing and the direct links with the arms trade, the IMF recommended that future borrowing be fully documented, approved by the National Assembly and the information made available to the public. Unfortunately, the Angolan government declined such advice because it 'felt that such a level of transparency vis-à-vis parliament and civil society would be too intrusive on government affairs'.[70] Perhaps the disclosure of such details would highlight that the ruling elite were also benefiting directly from these deals?

Predatory Portugal

In November 2002, press reports alleged that the Angolan government had negotiated a no-questions-asked deal to pay off its US$2.2 billion debt to Portugal.[71] According to one Portuguese newspaper, the debt was largely inherited from UNITA, though the government had agreed to honour it in the April 2002 Memorandum of Understanding which underpins the ceasefire.[72]

Contacts close to the deal have told Global Witness that Portugal subsequently received a formal reprimand from the Paris Club (the global forum for restructuring government-to-government debt which Portugal had applied to join) for its negotiations with Angola.

A summary of discussions by Paris Club members held on 11 December 2002 obtained by Global Witness states that: 'Portugal signed a bilateral agreement with Angola on November 27. The total amount involved is [US]$1 billion of which [US]$730 million will be restructured over 30 years, including a 5-year grace period, at 1.75%. The remaining [US]$270 million will be refinanced by a Portuguese bank and collateralized with future oil receipts'.[73]

The deal was controversial for two reasons. Firstly, it went 'against the solidarity principles of the Paris Club':[74] that is, it violated the Paris Club principle that all negotiations should be uniform so that all creditors receive equal treatment. Secondly, '[s]everal creditors voiced concerns about the increasing share of Angola's external debt that is collateralized and noted that this will complicate any future restructuring in the Paris Club'.[74] *Africa Confidential* also reported that the Paris Club members and the IMF were 'furious' because they regarded the deal as 'undermining IMF pressure for reform'.[67]

An ex-official of the Portuguese Finance Ministry commented to Global Witness that he believed the new agreement was prompted more by the urgent need to address Portugal's public deficit to keep it within the limit imposed by the European Stability Pact, than by anything to do with forgiving Angolan debt.[74,75] It appears that the Angolan government agreed to an immediate one-off payment of US$270 million in return for some debt forgiveness and for favourable terms for repaying the rest.

A representative of the Portuguese Embassy in London told Global Witness that, as of December 2003, the agreement was not finalised.[76] Nevertheless, the message of deficient governance is clear: at a time when Angola faces a critical humanitarian situation, its government appears willing to borrow massive sums at high rates of interest in order to service its debts to Portugal, while the latter seeks a quick-fix for its EU Stability Pact obligations.

Massive new offshore loans

Not long after the Portuguese deal first surfaced in January 2003, the Angolan government arranged a massive new oil-backed loan from foreign banks, routed through the Cayman Islands, which this time generated more than US$1 billion. The oil-backed loan was arranged by BNP Paribas, Société Générale, Natexis Banques Populaires and Banque Belgolaise and is Angola's largest so far.[77]

The loan appears to be serviced through an opaque structure based in an offshore tax haven called a Special Purpose Vehicle (SPV), the assets of which will be the proceeds of Angolan oil production.[78] As mentioned in the Congo section of this report, an SPV is an offshore company set up for one specific purpose. But as the spectacular collapse of Enron has illustrated, SPVs can also be structures of Byzantine complexity that can be used to obscure assets or losses. Given the huge sums that have already gone missing from the government's accounts, the use of such a complex and un-transparent structure to service a loan of this size is clearly grounds for great concern.

The IMF has not commented publicly on such arrangements, but senior IMF officials privately disapprove of such means of financing because there are far more responsible ways of servicing the country's debts.[79] The IMF itself offers far better terms for long-term loans than international banks, yet Angola has routinely opted for short-term, high-interest loans from private lenders.

Indeed, such private loans form the backbone of Angolan finances. Global Witness revealed that the government raised US$3.55 billion in oil-backed loans between September 2000 and October 2001, US$3.05 billion of which was raised in 2001 alone – the same year the Angolan government agreed with the IMF to limit its new borrowing to US$269 million.[2] Amongst other things, the IMF requires fiscal transparency from borrowers seeking preferential loans. Far from opening its books and therefore getting a better deal for the country, it appears that the *Futungo* is instead devising ever more complicated means of raising money.

The IMF has been involved in two surveillance operations on the Angolan government's accounts, in January-June 2001 and in April-December 2002. These Staff Monitored Programmes, are the first step in negotiating any loan agreement and involve a basic financial audit of government accounts. The government also agreed to an audit of Angola's central bank and an 'Oil Diagnostic' revenue-tracking exercise, which is intended to reconcile income from the oil sector with government receipts. However, there was no clear commitment to make the results public and the work has suffered numerous delays and tortuous renegotiations of terms of reference.

To its credit, the government has finally published a heavily edited summary of the oil revenue-tracking exercise as a concession to the IMF. Similarly, after refusing to allow publication of several of the IMF's Article IV Consultation reports, Angola has finally allowed a summary report for 2003 to be made publicly available. However, the report omits discussion of the huge financial discrepancies identified in earlier reports.

These reports and their accompanying staff commentaries have been passed to Global Witness. These documents, along with the summary of the Oil Diagnostic, record a picture of appalling fiscal laxity, with about quarter of the government's income completely unaccounted for and/or lost and subsequently recorded *post hoc* as spent.[80]

The reports they don't want you to read

The IMF's 2002 consultation report provides the most explicit summary of the government's opaque accounting methods. It states that:

> '[F]requent dialogue with the authorities and significant technical assistance in recent years has yielded little progress in the key areas of governance and fiscal transparency. There is virtually no public information on fiscal and external public borrowing, the state-owned oil company manages the country's oil-related receipts through a web of opaque offshore accounts, the central bank and other public companies suffer from poor internal controls and large operational deficits, and the weakness of basic economic data hampers the design and monitoring of a macroeconomic program. It would be very difficult for Angola to formulate a meaningful poverty reduction strategy without addressing these and other transparency and governance-related problems.'[81]

Government performance overall was deemed 'unsatisfactory'.[82]

The 2002 report points at two major streams of unaccountable revenue expenditure. It writes that 'during the last five years, extrabudgetary expenditures and residual unexplained discrepancies in the fiscal accounts have averaged 11% and 12% of GDP per year, respectively'.[82] To save any confusion over what these categories represent, the report clarifies that 'even though these outlays have been recorded ex-post as expenditures, their precise nature remains to be fully identified'.[83] In effect, this indicates that a startling average of 23% of Angola's GDP each year appears to be spent off-the-books (see table: Angola's Unaccounted-for Money 1997-2001). This is an average of about US$1.7 billion per year. In 1999, the government's missing money was a gigantic US$2.4 billion, almost 40% of the country's GDP.

Even worse, a breakdown of government expenditure shows that this missing money, when added to the country's expenditure on defence and internal security, may account for more than half of the government's total outgoings (see table: Skewed Priorities). In 1999, Angola's unaccounted-for money is some ten times greater than total social spending.

Money unaccounted for in Angola 1997-2001*

Year/Category	1997	1998	1999	2000	2001 (est.)
Total expenditure	4,966	2,760	5,028	5,380	4,669
Extra-budgetary 'ex-post expenditure' (US$ millions)	980	566	1,290	1,062	205
Extra-budgetary 'ex-post expenditure' (% GDP)	12.8	8.8	21.2	12.0	1.6
Discrepancies and unexplained gaps (US$ millions)	1,775	134	1,132	415	907
Discrepancies and unexplained gaps (% GDP)	23.1	2.1	18.6	4.7	9.6
Total money unaccounted for (US$ millions)	2,755	700	2,422	1,477	1,112
Total money unaccounted for (% GDP)	35.9	10.9	39.8	16.7	11.2

*Global Witness table. Source 2002 IMF Article IV Report

Skewed priorities: a comparison of social spending versus the budget's black holes*

Budget line (% GDP)	1997	1998	1999	2000	2001 (est.)
Defence and internal security	8.3	14.5	25.8	9.0	6
Unclassifiable	8.2	5.2	20.7	25.7	1.8
Discrepancy	23.1	23.1	18.6	4.7	9.6
Sub-total	39.6	42.8	65.1	39.4	17.4
Education	3.8	2.6	1.5	1.9	2.9
Health	2.0	1.4	1.2	2.0	2.3
Social security, welfare, housing	1.4	0.9	1.2	5.5	2.5
Sub-total of social expenditure	7.2	4.9	3.9	9.4	7.7
Ratio of unaccounted-for money and unclassified expenses to social expenditure	4.3:1	5.8:1	10.1:1	2.7:1	1.5:1

*Global Witness table. Source 2002 IMF Article IV Report

The 2002 Article IV report adds that: 'Sonangol … assumed some time ago complete control of foreign currency receipts from the oil sector and stopped channelling them through the central bank as mandated by law. These receipts now go through bank accounts of subsidiaries or through escrow accounts to service oil-guaranteed loans. These difficulties are exacerbated by the continuous arrears of Sonangol on payments of taxes and oil bonuses to the Treasury'.[84]

There is no direct comment on the issue of missing money in the 2003 IMF report. But the report does not mention that there has been any improvement in accounting for missing revenues and one table contains a line for 'unexplained discrepancies' in government accounts. These amount to US$1.19 billion in 1999, US$407 million the following year, US$540 million in 2001 and US$347 million in 2002.

These figures correspond with a slight downward revision to the 'residual unexplained discrepancies' category of missing money highlighted by the IMF in 2002. Interestingly, the 'ex-post expenditure' category has vanished and is simply being reported as part of government outgoings. (One assumes that the IMF would have commented if the *Futungo* had suddenly found receipts for these missing billions.[85]) The report does provide some updated figures for estimated income (and a helpful breakdown of Angola's complicated oil money regime) but, again, refrains from commenting how much of this reported income actually reached the government's coffers.

The KPMG's Oil Diagnostic summary is also vague on the overall amount of missing money, which is surprising given that its *raison d'être* was to track oil money into the government's accounts. Even taking into account the bizarre caveat in the report's first line that 'this Report shall not be seen as suitable to be used beyond the government, IMF and World Bank', the Diagnostic describes an accounting nightmare.[86] One of the 'central, fundamental and indispensable aspects' of which is that the government and the central bank, the *Banco Nacional de Angola* (BNA), have allowed private and state companies and public entities to do business and keep accounts in both the national currency, the kwanza, and US dollars, with no reconciliation of variations between the two currencies.[87] This is despite the fact that Angola is a hyperinflationary economy.

One key event highlighted by the Diagnostic is the collapse of the government's Petroleum Account at the BNA in 2001. This was because the account contained insufficient funds to service cash calls (liquidity demands) and government debt obligations placed on it. According to the Diagnostic:

'Even though the Petroleum Account was established [in 1995] to improve the control and the management of the oil revenues, no significant regular reconciliation procedures were established between the Ministry of Finance, Sonangol and the BNA to approve the balance of the Petroleum Account on a monthly basis. No regular closing procedures are applied to determine the range of the validity dates of the sales balances and related petroleum account transactions (that is payment of taxes) involving the Ministry of Finance, the BNA and Sonangol, which led to permanent discrepancies.'[87]


Angola's central bank: where the oil money isn't.

It remains unclear why, given the huge amount of money the oil industry provides to the country, the government's account collapsed for lack of money, or how, in the wake of this collapse, the government is now managing its oil accounts.

Moreover, the quality of financial information provided to the Diagnostic team was clearly extremely poor. The consultants complain that they 'could perform a very elementary and limited analysis' of Sonangol's upstream and downstream activities and that 'no auditor could voice an opinion' on the company's accounts 'giving or not a true and just picture' of its finances.[88] The Diagnostic team identified that Sonangol has 'a large number of active bank accounts' and that the 'internal controls' on these accounts are 'weak' with 'a considerable number of errors and differences to be documented, reconciled and confirmed'.[89] In addition, several foreign accounts held in Sonangol's name, such as at Lloyds in London, did not appear on its books.[90] Sonangol's outgoings are similarly opaque – one of its subsidiaries is recorded as booking US$7.5 million in expenses for 'the Houston project', unsupported by any external documentation.[90]

Similarly, the BNA 'has not installed adequate control procedures to safeguard the bank's fixed assets against loss or misuse'. The report also reveals that 'some of the bank's accounts have not been reconciled, that there are accounts for which the bank has never received bank statements, that some accounts were frozen and taken to court and that no provisions were taken about them [….] There is also a large number of reconciliation articles and no proof that these were or are being investigated to solve them'.[91] The Diagnostic also notes that the bank has a 'big' workforce, of which a 'large number does not have sufficient or useful qualifications'.[90]

Sidelining the signature bonuses

A July 2002 investigation by the International Consortium of Investigative Journalists (ICIJ) into the destination of one signature bonus paid by Marathon Oil revealed yet another example of the unaccountable operating environment in which oil-related business is conducted in Angola. The tortuous offshore routes used to bank signature bonuses paid by oil companies – and the possibility that large sums may never have reached the national treasury at all – are a perfect illustration of the complete lack of transparency in the payment and receipt of oil monies in the country.

The ICIJ tracked a US$13.7 million payment from Marathon into a Sonangol account in Jersey, a British offshore tax haven, in July 2000. The same day 'Sonangol transferred an identical sum of money out of Jersey to another Sonangol account in an unknown location'.[91] During the summer of 2000, large amounts of money were transferred from Jersey accounts to a variety of destinations. US$7.2 million went to international construction companies; US$2.4 million went to a security firm guarding diamond mines and oil-storage facilities; US$2.2 million went to a private bank, *Banco Africano de Investimentos* (BAI), in which Sonangol is a 17.5% shareholder; and US$5.5 million to a Liechtenstein-based firm that provides catering and other services to the oil industry in Angola.[92] When ICIJ asked one lawyer specialising in international fraud the reason why Sonangol would open accounts in Jersey instead of London or Paris, he replied that 'the incentive for keeping money in a place like Jersey can only be secrecy, but a parastatal company should be anything but secret. When companies ask me about red flags signifying when a payment is suspicious, I say, "when they want a large amount of money sent to an offshore account".'[93]

The IMF's 2002 Article IV report also mentions unaccounted-for signature bonuses, highlighting the direct control exercised by the Presidency and Sonangol over this income.[94] According to the IMF, funds from the most recent bonuses paid for Block 34, an ultra-deepwater block auctioned in October 2001 (and owned by Norsk Hydro, Shell and ConocoPhillips) had not reached the National Treasury one year later. 'The delay in effecting this transfer could not be explained, except by the fact these funds are outside the control of the treasury', it concluded.[95]

The report says that the Angolan authorities reported some US$285 million in payments for this concession to the IMF. However, it states that this figure was 'lower than the payments for the treasury of about US$400 million (not including additional payments of nearly US$100 million to Sonangol's Social Fund and other funds) reported to the staff by the oil companies for the same concession. The authorities stated that they could not provide any supporting documentation on these payments because of confidentiality agreements with the oil companies.'[95] Clearly, if oil companies were obliged to publish what they pay, such disturbing discrepancies of hundreds of millions of dollars could be resolved.

One year later, the IMF's 2003 Article IV report had eventually tracked down a large portion (about US$289 million) of these signature bonuses. After deduction of some US$49 million in charges by oil companies for services and debt charges to Sonangol, the balance was placed into one of the government's 'official' offshore accounts.[96] However, the report does not comment on the discrepancy between the figures reported in 2002 that, even taking into account the further US$49 million deduction, would still amount to around US$70 million, nor on the whereabouts of this missing balance.

Lack of capacity or lack of application?

The response of the *Futungo* to any call for improved transparency is that, emerging from so many years of war, the country lacks the capacity to account for all of its present and past transactions. They also claim national sovereignty concerns. These explanations are profoundly unconvincing. A government and state oil company that handle billions of dollars through complex offshore arrangements, including the use of Special Purpose Vehicles and foreign tax havens, can certainly manage a simple balance sheet. Similarly, a government cannot claim the defence of sovereignty over its actions if it has abrogated its responsibility to provide services to its citizens.

Documents passed to Global Witness from those close to the regime show that the government already collects some data on the reporting of oil income, and that these figures are posted within the Ministry of Petroleum. In 2001, as first reported in *All the Presidents' Men*, revenues of some US$3.8 billion were reported by the Ministry of Petroleum from oil companies operating in the country.[2] A first step towards transparency would be for the government to make these figures public by, for example, adding them to the basic information about the oil sector on the new Ministry of Finance website.

The country's unwillingness to let the IMF publish the results of its 2001 and 2002 Article IV Consultations does not indicate that Angola feels helpless to effect transparency, but rather than it does not want information about oil money in the public domain.

The government has also directly threatened oil companies that have wanted to disclose payments in the past. In February 2001, when BP said it would release summary data on its payments to the government, the company was threatened with termination of its contract by Sonangol, on the grounds that BP would be violating a confidentiality clause in its operating licence (see box in penultimate section: The Dangers of Voluntarism - BP in Angola).

The retaliation experienced by BP illustrates the need for the home states of oil companies to enact regulations which require the public disclosure of company payments to the governments of countries where they operate. Angolan oil contracts have a clause that waives confidentiality for all information 'to the extent required by any applicable law, regulation or rule (including, without limitation, any regulation or rule of any regulatory agency, securities commission or securities exchange on which the securities of such Party or of any of such Party's affiliates are listed)'. Had BP and its competitors been required by stock market regulators or accounting standards to publish their payments, then the company could have done so without jeopardising its competitive position in Angola or exposing itself to retaliation from those with vested interests in non-disclosure. Disclosure required by law would be depoliticised and would come to be regarded as part of normal business procedures.

The Angolan government recently attended the launch of the UK-led Extractive Industry Transparency Initiative (EITI) in London. Sonangol boss Manuel Vincente said that the state oil company would publish its accounts for 2003 but, in a clear rebuff to the EITI, the Angolan deputy finance minister claimed 'observer status' for his country rather than committing to full participation.[97]

Two days later, Angolan Deputy Prime Minister Aguinaldo Jaime announced in a speech to the oil industry in London that 'for the first time in Angola's history, the budget will encompass all revenue and that will send to the donor community the signal that the Angolan government is committed to a fully transparent way of managing the budget'. As Jaime himself commented: 'In the past, we had off-budget transactions, so the budget lacked credibility'.[98]

This seemed a relatively clear and unambiguous commitment to improving the transparency of the government's finances, but there is no clear timeline attached. Also, will this budget be made publicly available? Will such information cover all the government's and the company's offshore accounts and will they be audited by a reputable accounting firm? What sort of accounts will Sonangol submit, especially in view of the fact that the KPMG Diagnostic team could not find a single auditor willing to vouch for the accuracy of the company's books?

This announcement would seem a step in the right direction but, given the haemorrhage of oil revenues in the past, Angola must give credibility to its pledges of disclosure by fully participating in the EITI process and promoting double-disclosure book-keeping of the country's oil money, whereby the net payments of companies are reconciled with the receipts reported by the government.

As in Congo Brazzaville, there is a real danger that unless clear and effective methods for tracking revenue are installed, then the Angolan government will abandon any transparency reforms as soon as it is given the green light for new IMF funding.

It is telling of the lack of any the real commitment to reform that despite expressions of repeated concern about off-budget loans by the IMF, no sooner was the 2003 consultation published than Sonangol was reported as trying to tap a syndicate led by Japan's Nissho Iwai for a new US$500 million loan to fund its own upstream investments.[99]

Another recent event that plants a doubt about the sincerity of the *Futungo*'s reform efforts is the appointment of Falcone as Angola's Ambassador to UNESCO in September 2003. Press reports suggest that the appointment could secure him full diplomatic status and immunity from prosecution in France.[100] A formal statement from Luanda explicitly linked the UNESCO appointment to Falcone's past role as a *de facto* 'state agent' carrying out 'missions related to the supply of national defence' after the resumption of fighting with UNITA in 1992, adding that '[t]he Angolan government, by appointing Mr Pierre Falcone as Angolan state agent, does not intend to obstruct the [sic] French justice but […] to ensure that the personal and functional immunities were reacquired by those who acted on our behalf and mandate'.[101] At the time of writing, an international arrest warrant had been issued by the French authorities for Falcone, who has left France. According to *Le Monde*, while Falcone's lawyers stated that 'their client enjoys "total diplomatic immunity"', the investigating judges believe that Falcone's diplomatic immunity 'extends "solely to acts carried out" in the context of his UNESCO position'.[102]

Peace dividends?

Despite Angola's wealth of natural resources, it remains one of the poorest countries in the world, ranked 161 out of 173 countries in the UN's Human Development Index, some 36 places below its Gross National Product per capita ranking, indicating great potential for increased spending on development and social well-being.[103] Although the April 2002 ceasefire agreement brought an end to the country's brutal war, the humanitarian situation remains dire: poverty, squalor and chaos are still features of everyday life and the country's basic infrastructure remains fragmented.[104]

Over a million Angolans rely on the UN's World Food Programme (WFP) for their survival. Even more rely on the UN's transportation facilities to distribute basic items such as tools and seeds, as well as materials to build hospitals, schools and other amenities so that 'normal life' can begin again.[105]

The UN's mid-year review of the situation in the country in 2003 reported that 'overall levels of vulnerability remain some of the highest in the world and there has been virtually no improvement in social indicators [though it also mentions that international assistance has helped tackle acute malnutrition and vaccinations]… in addition, hundreds of thousands of people remain in acute distress in tens of locations where mine infestation, poor road conditions and broken bridges limit access'.[106] The report also notes that 'an estimated 70 percent of returnees have resettled without any form of assistance from the local authorities or humanitarian organisations to areas where the preconditions specified in the Norms of Resettlement of Displaced Persons [specifying the basic standard of assistance] are not yet in place'.[107]

Many thousands of ex-UNITA soldiers and their dependants remain hungry, unemployed and homeless (some reports put the figure at over 100,000). In addition, the demobilisation process has not been properly audited and many ex-UNITA combatants still have their weapons.[107] One prominent Angola commentator, Justin Pearce, writing in South Africa's *Mail & Guardian*, also noted that 'the provision of "resettlement kits" – farming tools, seeds and other essentials of life – to UNITA's men was held up for six months after the contract to do this was awarded to a company owned by a close associate of President José Eduardo dos Santos'. According to Pearce, one UN official 'insisted that there are plenty of people inside the government who want to get things done. Unfortunately, those are not the same people who have the cash at their disposal to do so, since funds get tied up at the level of the Presidency'.[1]

A further problem is that stability in the oil-rich enclave of Cabinda is deteriorating due to fighting between government troops and separatist rebels linked to the *Frente de Libertação do Enclave de Cabinda* (FLEC). A few months after the establishment of the UNITA ceasefire in Angola, some 40,000 troops were mobilised in the province and reports of killings, disappearances, arbitrary detention, torture, rape and looting are widespread.[108] In June 2003, the Angolan army even moved into neighbouring Congo Brazzaville in search of separatist fighters,[109] accompanied by ongoing allegations of widespread human rights abuses and kidnapping by the Angolan army on Congolese territory.[110]

Although Cabinda receives 20% of the resources allotted for Angola's 18 provinces, many Cabindans feel that the *Futungo* do not have their interests at heart. One Cabindan who is also an oil company employee stated: 'Look at Angola … it leads the world in the number of amputees, its leaders are corrupt, it has no money, it's heavily mined – why would we want to stay with them?

Angola doesn't have an argument for Cabinda, that's why they must use force.'[111]

These events have disturbing implications for oil companies operating in the country. Insurgent groups regard oil companies as legitimate targets of war and the situation may have been exacerbated by recent reports from human rights groups that the Angolan military is using company premises for the detention and interrogation of suspected FLEC supporters.[112] Foreign oil company employees are already forced to live in a secure compound outside the main town and travel around by helicopter.[113] In the past, the instability caused by Angola's civil war spread to Cabinda. It is now conceivable that the reverse could happen, with Cabinda's conflict threatening Angola's hard-won peace, particularly if there are continuing problems with the decommissioning of UNITA troops.

The situation in Cabinda also shows clearly that the *Futungo* may remain trapped in a wartime 'siege mentality' in which press censorship and authoritarian government are the norm: dozens of independent journalists are currently imprisoned for daring to criticize the government and independent newspaper *Angolense* received a barrage of threats when it published a 'rich-list' of Angolans in January 2003.[114] Top of the list of those with more than US$50 million in assets was President dos Santos, with an estimated personal fortune of 'several hundreds of millions of dollars'.[115] When Catholic radio station *Radio Ecclesia* broadcast the list a month later, Vaal Neto, the Communications Minister, accused the station of 'antenna terrorism'.[116]

So far, the Angolan government has earmarked some US$60 million for humanitarian assistance. This is a positive first step, but pales in the light of the missing billions from the state budget and the millions in aid provided by the UN, the World Bank, and bilateral donors. If the Futungo managed the country's money more accountably, it seems clear that the government could provide for its own people: that it chooses not do so is a strong signal to the international community that the country's troubles are far from over. Instead, around a quarter of Angola's GDP per year appears to be haemorrhaging from the state's coffers.

Had oil companies been required to publish what they pay to the Angolan government, Angola's missing oil money would have come to light sooner, as would the need for a more joined-up approach to domestic capacity-building and accountability by the international community. Unless these are now implemented, Angola's oil money threatens to remain as out of reach for the Angolan people as the oil platforms themselves.

The war may be over, but its costs are all too visible.

Equatorial Guinea

Welcome to Equatorial Guinea. Credit: Gervasio Sánchez/Heraldo de Aragón

Money unaccounted for: perhaps as much as US$500 million. There seems to be little in the way of a formal accounting system for revenues and it appears that much of the country's oil money is being held overseas and out-of-sight. The International Monetary Fund (IMF) reported that 'recorded fiscal surpluses in 2000-01 exceeded the increase in government bank balances by US$170 million', a discrepancy of about 10% of GDP.[1]

Time of the fat cows

The regime of President-for-life Teodoro Obiang Nguema Mbasogo, who executed his brutal uncle Mathias Obiang to gain power in 1979, has been tarnished with allegations of corruption, cronyism, brutal political repression, routine human rights violations and drug trafficking.[2] Some academics have even described the country as one of the few 'criminal states' in Africa, involving 'the use for private purposes of the legitimate organs of state violence by those in authority, and the function of such violence as an instrument in the service of their strategies of accumulation of wealth'.[3]

This would seem a dangerous environment in which to do business. As one leading Spanish newspaper commented in the early 1990s: 'Only someone suicidal would set up a business in Equatorial Guinea today, unless it was a funeral parlour.'[4] At that time, the country was almost completely isolated from the international community – outside its starring role in Fredrick Forsyth's thriller of mercenary warfare in Africa, *The Dogs of War*[5] – and the economy was stagnant.

Since then, a remarkable offshore oil boom has occurred. Production is now about 300,000 barrels per day and rising and foreign, predominantly US, investment has been pouring into the country.[6]

In 2002, President Obiang – also known as '*El Jefe*' (meaning 'The Boss') – prophesied a period of unprecedented prosperity for his people: 'Like the Scriptures say when the Pharaoh of Egypt had a dream of lean cows and fat cows, we have passed the time of lean cows that represent hunger, and we are now in the time of fat cows which is prosperity.'[7]

Equatorial Guinea's state radio says Obiang's actions can't be questioned becuase 'he is in permanent contact with the Almighty.'[43] Credit: International COVER.

On paper, the country has seen the fastest GDP growth in the world, put at over 60% in 2001[8] and oil activity has accounted for 86% of the country's GDP from 2000 to 2002.[9] The World Bank estimates that Equatorial Guinea's annual oil revenues have increased from about US$3 million in 1993 to over US$210 million in 2000 and may reach US$700 million in 2003.[6] The Bank also reports that 'there has been no impact on the country's dismal social indicators'.[10]

In 2000, a Special Rapporteur to the UN Commission on Human Rights reported that '80 per cent of national income is in the hands of 5 per cent of the population'.[11] In 2001, he stated that '[t]he exceptional economic boom which followed the discovery of major oilfields in the mid-1990s has not led to any improvement in the economic, social and cultural rights of the population, more than 65% of which lives in conditions of extreme poverty'.[12] Overall, the Rapporteur viewed the situation in the country as having seen no improvement since 1979, 'despite the recommendations which the Commission has made year after year to the Government of Equatorial Guinea'.[12]

A September 2003 report by the US Energy Information Agency likewise states that 'despite rapid growth in real GDP, there is strong evidence of government misappropriation of oil revenues, in particular, for lavish personal expenditures. Furthermore, the failure of the government to inject oil revenues into the country's economy, especially to fund much-needed improvements in the country's infrastructure, has meant little improvement in the economic and social welfare of most Equatoguineans.'[13] The IMF concurred in December 2003 that 'the country's [Human Development Index] ranking has actually deteriorated during [the past few years], indicating that other nations were more effective in improving the living conditions of their citizens while often dedicating fewer budgetary resources to this task'.[14]

Dramatic allegations have recently surfaced that may explain the huge discrepancy between the country's oil income and its continuing poverty. Information published in the *LA Times* in January 2003 suggests that a massive US$300-500 million of the country's oil money is parked in a bank account in Washington DC under Obiang's control.[15] Documents revealed below highlight a close working relationship between the President, his family and those managing Equatorial Guinea's oil money in organising extravagant real-estate purchases for the former in the US.

El Jefe himself told a foreign journalist in November 2003 that there was 'no poverty' in the country and that 'the first problem is the people's cultural level. The people are used to living in a very different way, which you people think is poverty. In [Equatorial] Guinea, what we have is shortages.'[16]

One of these shortages appears to be the almost complete absence of transparency about Equatorial Guinea's oil money, although the country's constitution stipulates that oil revenues should be entered in the annual budget, which should then be approved by parliament.[17]

Documents from the World Bank and other sources (discussed below) routinely highlight the dire state of the country's oil accounting. Obiang himself has gone on the record on a number of occasions to state that Equatorial Guinea's oil resources are a 'state secret'.[18] More recent comments from government officials deny any secrecy *per se*, and allege that Equatorial Guinea would like to become a test case for the UK Government's Extractive Industry Transparency Initiative (EITI).[19] Clear information about Equatorial Guinea's oil income has not yet entered the public domain, nor is it clear how the country intends to follow up its interest in the EITI.

Given the serious nature of the allegations of regime involvement in crime and human rights violations – including testimony from ex-regime insiders that allege its involvement in drug trafficking (see below) – multinational companies could risk significant reputational damage just by doing business in Equatorial Guinea. This damage could be even worse if it turns out that oil companies are paying money directly into extra-territorial accounts outside of parliamentary scrutiny without asking any questions. Transparency over payments to the state should be a minimum condition if companies are to avoid being seen as complicit with the alleged excesses of the regime.

The critical period of opportunity for turning the country's oil windfall into developmental gains, and avoiding the instability often associated with misuse of oil wealth, is short. At the current rate of exploitation, the country's oil income will probably last about between one and two decades.[20] The balance of evidence so far suggests that the country's one chance to kick-start its development is in very real danger of being squandered, and that insecurity and infighting loom large in the country's future.

Equatorial Guinea's offshore oil money

Equatorial Guinea's oil money may not be driving the country's development because much of it may not even be in the country.

A January 2003 *LA Times* article reported that a massive US$300-500 million of Equatorial Guinea's oil revenues have been placed in an account at the Dupont Circle branch of Riggs Bank in Washington, DC. The article states: 'Several sources familiar with the account said it was controlled exclusively by Obiang and its balance has ranged from $300 million to $500 million during the last two years'.[15] The article also claims that ExxonMobil and Amerada Hess pay money directly into the account and although such payments were not illegal, they are frowned on by international financial institutions and anti-corruption groups. The two companies declined to comment to the paper on this claim. If true, these claims imply that a major portion of the country's oil revenues is being held offshore and out of sight of the country's citizens.

A pattern of opaque offshore financial management was also suggested by John Bennett, ex-US Ambassador to Equatorial Guinea, in a TV interview in November 2003. He alleged that the income to the country had been some US$1.5-2 billion dollars over the last decade and that members of the ruling elite were 'putting it offshore'.[21]

The *LA Times* names Simon Kareri as the account manager at Riggs and describes him as a senior international banking manager who provides private banking services for individuals with a minimum of US$1 million to invest.[15] The article notes that Kareri previously came to the attention of the press by providing private banking services for Malian businessman Foutanga Dit Babani Sissoko, who

Riggs Bank: is this where the oil money goes?

faced a civil suit from Dubai Islamic Bank for misappropriating almost US$250 million. Some of that money was subsequently recovered in a default judgment.

The article relates that: 'Kareri opened a Riggs account for Sissoko in 1997, when Sissoko was under house arrest in Miami after having pleaded guilty to attempting to bribe a US customs agent. Sissoko wanted to conceal his control over the account, ran millions of dollars through it and regularly had a representative stuff large withdrawals into a suitcase or his pockets. Kareri told Dubai Islamic lawyers in a deposition that he was suspicious of Sissoko but did not report his concerns to his superiors or the Treasury Department.'[15]

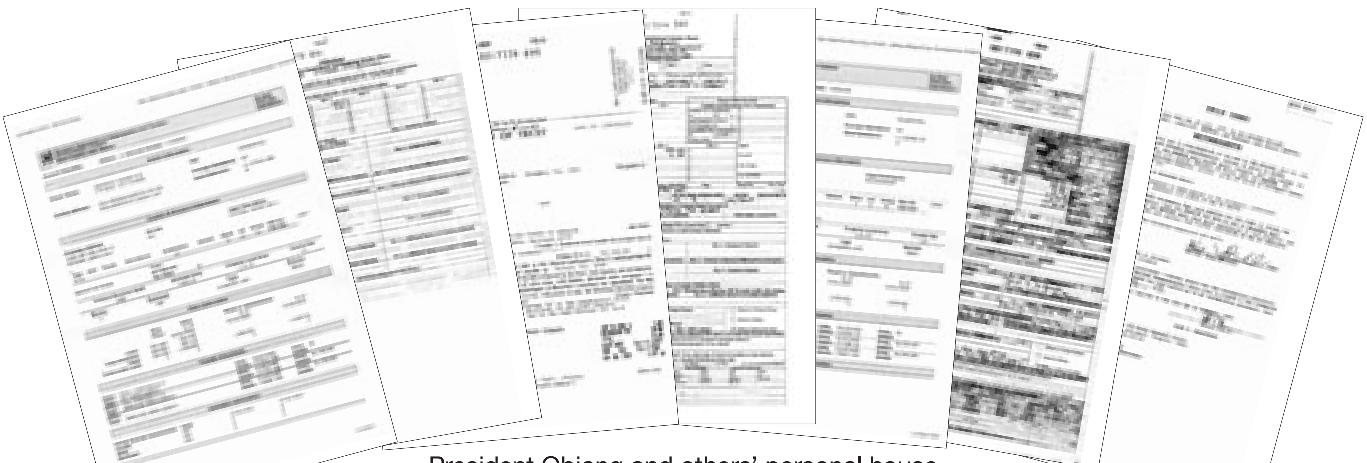
Global Witness recently discussed the information about the Riggs account with the Equatoguinean ministers of the Treasury, and Departments of Justice and Energy.[22] The ministers confirmed the existence of the Riggs account and stated that it was an official Treasury account. Initially, they declined to confirm or deny whether Obiang alone had control over the account but assured Global Witness that whoever had signatory power had been duly approved by the government. In a later conversation, two of the ministers described the President as the 'first auditor' of the country and said that he personally checks the revenues the Treasury receives.[22]

Comments by Obiang during two TV interviews in November 2003 appear to confirm that the President is in sole control of oil money. In one interview, in the context of questions on this issue, Obiang said: 'I am the one who arranges things in this country because in Africa there are a lot of problems of corruption, the diversion of money. If there is corruption, diversion of funds, then I'm responsible. That's why I'm a hundred percent sure of all the revenue because the one who signs is me.'[16] In a second interview he further clarified: 'I find myself forced to personally assume full responsibility as Sole National Paymaster General – even though many people are against this – in order to exercise the necessary control, since as President of the Republic, the Constitution holds me responsible for the proper functioning of all State institutions'.[21] The IMF has previously recommended that this supervisory role be carried out by the Minister of Finance.[23]

Article 10 of an oil production contract shown to Global Witness by the ministers states that all oil receipts are to be deposited directly in the country's Treasury. However, they explained that oil receipts were routinely parked offshore for two main reasons. First, the Treasury building itself is not secure, as it is not equipped with modern security systems and lacks a safe. Second, as payments made by oil companies are in US dollars, the government would lose money on commission charges if they were to be deposited into the Equatoguinean branch of an international bank and changed into local currency. Furthermore, there would be a time lag between the deposit of the cheque and the crediting of the account. [21]

These explanations beg the obvious question: why is not possible for the government to hold a foreign currency account with the Bank of Central African States (BEAC), where it already has a treasury account? Indeed, the IMF has been calling on the government since 1999 to transfer 'all payments by the oil companies' to the treasury account it holds at BEAC[23] and to 'fully disclose government bank accounts abroad'.[24]

It seems natural to ask whether oil companies have investigated with due diligence that the accounts they are paying into do, in fact, belong to the Treasury. The Kazakhstan section of this report noted that Mobil wrote to a Swiss bank in March 1998 to get details of account transactions to pursue an internal investigation into questioned payments. Did ExxonMobil carry out advance checks on the Riggs account?



President Obiang and others' personal house purchases in 1999 and 2000, c/o Simon Kareri, Riggs Bank, Washington DC. Kareri is said to have managed the government's finances too.

Meanwhile, Obiang himself has purchased two luxurious houses in Maryland through transactions facilitated by Kareri. In late 1999, Obiang appears to have paid US$2.6 million in cash for a mansion in the exclusive DC suburb of Potomac, Maryland. The house has ten bathrooms, seven fireplaces and an indoor pool.[15] The following year, another Maryland house was bought in the name of Obiang's wife Constancia Mangue Nsue for a more modest US$1.15 million. It was later transferred into the names of Constancia and Obiang. Constancia took out a US$747,500 mortgage from Riggs for this purchase, which was paid off nine months later. Tax filings and contact details for both purchases are given as: Simon P. Kareri, Riggs Bank NA, 1913 Massachusetts Avenue, NW Washington DC 20036.[25]

Mansions bought by Obiang and family near Washington DC in 1999 and 2000, with the help of a Riggs Bank employee.

Kareri is also reported to have helped Obiang's brother Armengol Ondo Nguema to buy a townhouse in Virginia worth about US$350,000 in 2000.[15] Armengol, head of the Equatorial Guinea's notorious security forces, is one of the most influential and feared members of the ruling elite. Sources including the US State Department have confirmed allegations of his forces' involvement in grave human rights violations.[26]

The *LA Times* says Kareri sent a reference letter to the real-estate agent in which he described Armengol as 'a valued customer of Riggs Bank'. This endorsement is in striking contrast to a State Department report, published in 1999, which relates reports that five prisoners were beaten to death in prison by security forces under the direction of Armengol. The report stated: 'Police reportedly urinated on prisoners, kicked them in the ribs, sliced their ears with knives, and smeared oil over their naked bodies in order to attract stinging ants. The President and senior government officials acknowledged that the security forces had committed excesses, but attributed them to rogue elements. However, according to credible reports, this torture was approved at the highest levels of the Government and was directed personally by the chief of presidential security, Armengol Ondo Nguema … [who] allegedly taunted prisoners by describing the suffering that they were about to endure.'[27]

Global Witness has not yet had a response from Kareri or Riggs bank about these issues. When Global Witness asked the Equatoguinean ministers about the Obiang family's house purchases and the sources of payment, they said the President was independently wealthy through a number of private business ventures. According to the ministers, one of these ventures was leasing or selling the 'Abayac' villa complex between the airport and Malabo to ExxonMobil.[19] This complex has since become the base for ExxonMobil's operations in Equatorial Guinea.

The Equatoguinean ministers also said that information about oil revenues and their management was freely available but could only be provided in-country. They invited Global Witness to come to Equatorial Guinea to access this information. However, during a second meeting with Global Witness, the ministers became distressed when asked for clarification of various points. One minister stated that he was not prepared to continue the discussion and, accusing Global Witness of being terrorists and racists, he walked out, precipitating the end of the meeting.

Obiang's brother Armengol: real estate investor and alleged torturer.
Credit: CBS 60 Minutes

'A breakdown in fiscal discipline and transparency'

The historical background in Equatorial Guinea is one of very weak disclosure. Successive World Bank and IMF reports suggest that: there is little or no effective system of government accounting; that oil companies lend the government money at very high rates of interest, for undisclosed purposes; that a substantial amount of the country's revenues are held offshore; and that the government has spurned offers of technical assistance in renegotiating key oil contracts.

A 1999 report by the IMF records a 'breakdown in fiscal discipline and transparency' since the development of major oil fields in 1992 and 1996.[30] It also notes that 'serious weaknesses remain in budgetary procedures and governance, budgetary control of expenditure commitment is lacking, and persistent extra-budgetary spending hampers the integrity of the annual budget exercise and effective policy design and implementation'.[31]

A summary of the IMF's follow-up consultation with the government in 2001 – the latter did not allow the full report to be published – stresses a 'lack of control over government financial operations'.[24] It states: 'there is no fiscal control over the payments due from, and paid by, the oil companies. Government oil revenue is paid into treasury accounts held abroad. Moreover, large extra-budgetary expenditures have been financed since 1996 through advances on oil revenue, and the oil companies have been withholding government oil revenue at source to repay these advances.'[24]

The most recent IMF report on Equatorial Guinea (December 2003) reiterated that '[f]or a long period, the authorities' response to persistently poor economic management … and serious governance issues was inadequate, and insufficient provision of economic information has seriously impaired the staff's ability to perform effective surveillance'.[9]

The IMF noted some limited progress 'in enhancing the transparency of oil-related transactions, and other aspects of managing the oil sector', in particular claiming that 'the use of advance payments has been discontinued'.[32]

This report should not paint an unduly negative picture of the dialogue: after all, government representatives were at least prepared initially to sit down and talk about the issue. It is unclear though whether the invitation to visit Equatorial Guinea and the commitment by the government to open its oil books still stands.

At the inaugural meeting of the UK government's Extractive Industry Transparency Initiative, the Equatoguinean government claimed it was moving towards transparency and welcomed the opportunity presented by the initiative. Cristobal Menana Elá, Minister of Mines and Energy, stated: 'After an exhaustive analysis of the principles and actions of this initiative, we observed that the principles of such an initiative fit perfectly and is in conjunction with our Government Policy [….] In conclusion, there are the avenues that our Government believes we can transmit information related to natural extractive resources in a transparent manner while respecting contractual clauses'.[28]

It is to be hoped that the government will now elaborate its plans to implement the EITI and will clarify the issues surrounding the Riggs account. An IMF report in 2003 also explicitly called on the government 'to follow through on their intentions to become a pilot case under the Extractive Industries Transparency Initiative'.[29]

Nevertheless the IMF noted that 'discrepancies in earlier years still need to be clarified' and referred to 'persistently weak budgetary discipline'.[33] The report stated that 'in 2001, the increase in government deposits fell short of the recorded fiscal surplus by 10% of GDP. Overall by end-2001, the accumulated recorded fiscal surpluses in 2000-01 exceeded the increase in government bank balances by US$170 million.'[34] This would suggest that a substantial amount of Equatorial Guinea's oil money is currently outside of official government accounts.

The IMF underscored 'the urgency of developing a medium-term strategy aimed at transforming Equatorial Guinea's oil wealth into sustained development. This should include further improvements in governance and transparency; [and] the development of a transparent framework for saving and managing part of the country's oil wealth.'[35]

An ex-advisor to the government confirmed the government's woeful oversight of its oil money to Global Witness saying that the budget 'means nothing – it's just a piece of paper. The reality is completely different.'[36] The advisor also said that offers of technical assistance from the World Bank had been rejected on a number of occasions. This situation seems even more extraordinary given that the government has signed contracts with oil companies in the past on much worse terms than those secured by other African oil producers (see later).

The claim that the government turned down offers of help is backed up by information from the Bank's own Operations Evaluations Division.[37] A 2002 report states that, despite offers of direct assistance and the existence of an in-country capacity building project, the government chose to negotiate the two main oil contracts, for the Alba field in 1990 and Zafiro field in 1992 without any outside help. The Zafiro deal took place without the Bank even knowing, even though it was meant to be collaborating with the government at the time.[38] The Bank interpreted this event as 'a lack of commitment to the fundamental objectives of the project, and a preference for immediate cash over long-term financial optimisation (giving priority to negotiating advances on future oil revenues)'.[39]

The World Bank report also states categorically that 'no data on the breakdown of oil revenues is available'.[40] It also condemns the government's 'unwillingness to share critical contractual information and overall tendency toward secrecy' and the fact that it 'defaulted and is still in default on its obligation under the project to account for oil revenues through the budget'.[41]

'Dictatorial Guinea'

The questions about the government's handling of oil revenues are far from theoretical, given that these revenues help to empower a political regime that has been characterised by reports of extreme brutality towards its own people and accusations of involvement in drug trafficking. The evidence below suggests that the nickname bestowed by a French newspaper, 'Dictatorial Guinea', is an apt one.[42]

There is a palpable climate of fear and impunity in country. Recently, state radio – the only source of news for most citizens – has stated that because of President Obiang's permanent contact with God: 'he can decide to kill without anyone calling him to account and without going to hell because it is God himself'.[43]

There have not been any free, fair and transparent elections in Equatorial Guinea since independence in 1968, the US State Department reported in 2000.[44] Obiang received over 97% of the vote in the 2002 presidential elections after opposition leaders pulled out *en masse*, in a ballot described by the State Department as 'marred by extensive fraud and intimidation'.[45] Perhaps the opposition were still smarting from an ugly event that June: a mass trial of over 140 opponents of the regime accused of an attempted *coup d'état*. The trial was denounced by Amnesty International, which said it considered those convicted to be 'prisoners of conscience'.[46]

The regime may not stop there to silence dissent. The State Department notes, for example, that the government has tried to neutralise exiled opposition groups by kidnappings in other countries.[44]

A 2002 US State Department reports confirms that the government's human rights record remains poor, with security forces cited as carrying out torture, beatings and other abuses against prisoners and suspects which sometimes led to deaths. Prison conditions are harsh and there are deaths in custody from torture, abuse and lack of medical care.[47]

Major concerns have also been raised about the ill-treatment of women and ethnic minorities.[48] Eyewitnesses have reported that after a demonstration by minority groups in January 1998, soldiers and civilians from the Fang ruling tribe patrolled the streets of Malabo beating up members of the Bubi ethnic minority and raping women. Some of the women had forks thrust in their vaginas and were told, 'from now on, that's your husband'.[49]

A report to the UN Commission on Human Rights noted in 2001 that, 'there continues to be no sustained rule of

Equatorial Guinea's opposition, en route to trial in 2002. Credit: Gervasio Sánchez/Heraldo de Aragón

law in Equatorial Guinea: rather, power is concentrated in the hands of the executive, which leads to continued arbitrary detention and torture'. The report went on to say that 'the situation could be improved with a modicum of political will' on the part of the international community and added that multinational corporations exploiting the country's wealth also have a role to play in achieving positive change.[50]

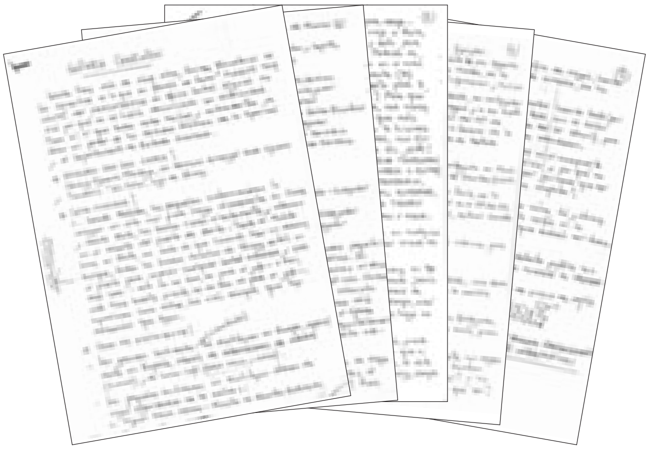
An October 2003 report by the International Bar Association (IBA) on the country's legal system states that 'the laws in Equatorial Guinea are either i) not written and thus never properly or consistently used; ii) the laws are inconsistent with the constitution; iii) the laws are outdated, and iv) they are ad hoc'.[51] Overall, the IBA concluded that '[t]he people of Equatorial Guinea have almost no access to legal protection or many of the basic human rights …. Political control is concentrated within a small elite which hold the executive and judicial powers, without effective separation. Corruption is endemic, and torture is in common use by the police'.[52] In the light of the country's new-found oil wealth, the IBA 'urge[s] those in power to use some of the new oil revenues to bring justice and rights to the people of Equatorial Guinea' and appeals for 'international investors … to hold [the country's leaders] to account'.[52]

As if these issues were not disturbing enough, there are allegations that the regime is linked to drug trafficking. In 1994, the respected Paris-based *Observatoire Géopolitique des Drogues* (OGD) went so far as to classify Equatorial Guinea as a 'drug trafficking state', meaning that the OGD believed there to be direct government involvement in the drug trade.[53]

There have been intermittent reports from the late 1980s onwards of about ten members of the ruling elite being caught with large quantities of drugs whilst travelling on diplomatic passports.[54] In addition, two former regime insiders have made serious and explicit allegations about Equatorial Guinea's role in the drug trade.

The former Equatoguinean Minister of Information, Santos Pascual Bikomo Nanguande, made a written statement to a judge in Spain, where he is serving a nine-year prison term for entering the country with over 14 kg of heroin from Pakistan in 1997,[55] in which he alleged that Equatorial Guinea was a '*plaque tournante*' (a revolving door) in a narcotics trafficking network that was based around its foreign missions and use of its diplomatic bag to transport drugs.[56] He also named senior regime figures who, he said, headed and ran the trafficking network.

Another regime insider, Joaquín María Alogo de Ondo Edu, was arrested as investigations into Bikomo's activities widened in 1997, but was later released. In September 1998, however, his body turned up in



Bikomo's letter to a Spanish judge in 1997 in which he alleges his country is a revolving door in an international narcotics trafficking network.

Medellín, Colombia.[57] Shortly before his death, Alogo wrote a confession, subsequently passed to Global Witness, in which he claimed that his luxury house in Madrid was used as a base for drug trafficking, document forgery and trafficking in Equatoguinean passports.[58] Alogo also described how he set up a lucrative passport trafficking business out of Hong Kong in the run-up of the British colony's transition to Chinese rule and claimed a knowledge of extensive offshore banking and money-laundering operations involving banks in Paris, Cameroon and Switzerland.[59] Interestingly, he also wrote that oil money was involved in these offshore banking operations.

The Equatorial Guinean embassy in Madrid condemned articles in the Spanish press linking the regime to drug trafficking as 'tendentious, unfounded, insulting and sensationalist'.[60] At the time of going to press, the government has not responded to enquiries on this topic by Global Witness.

Alogo's confession written a few days before his death in Medellín, Colombia in 1998.

There is evidence, however, that members of the Equatorial Guinean government were associated with some controversial figures in the 1990s such as Victor Guy Llansol, of whom the *Dictionnaire Geopolitique de Drogues* says that the US Drug Enforcement Agency (DEA) 'affirms (he) was working for the Medellín Cartel'.[61]

Foreign expatriates and government officials in Equatorial Guinea told Global Witness that Llansol began spending time in the country in the early 1990s and was placed in charge of telecommunications for the president.[62,63] He arrived with sophisticated electronic equipment that was, to say the least, disproportionate to the nation's rudimentary communications, where people are listed by their first names in the phonebook.[62,63,64] Some sources suggest that Llansol also became a senior financial advisor to the government.[62,63] Foreign diplomats resident in Equatorial Guinea, including the then-US Ambassador, also say that Llansol was known to the DEA, which opened a file on him, and that he appeared to be involved in money laundering.[62,64]

Global Witness has also obtained a copy of a letter to President Obiang in January 1993 from a Venezuelan company which offered him a loan to 'fund development' against future 'agro-industrial and mining revenues'.[65] According to the Spanish newspaper *El Mundo*, the guarantor of the loan was a Panama-based company whose treasurer was Llansol.[66] *El Mundo*, which names Llansol as Llanse, reported that the company later lent Equatorial Guinea some US$1.5 billion.[63] Global Witness does not have any independent confirmation that this loan was actually completed. If it had been, its value would be roughly four times the country's GDP, which raises the obvious question as to where such money went.

Global Witness has seen offers of zero or low interest loans from around the same time, linked to conditions such as the granting of diplomatic passports, which raise interesting questions about other financial links formed by regime members. [61]

More generally, there are serious outstanding allegations of institutionalised impropriety and serial human rights abuses. They warrant a serious response through a comprehensive and transparent investigation by the Equatorial Guinean Government and, where appropriate, by officials of other jurisdictions. There is also a clear lesson for international companies operating in the country: transparency and due diligence over their payments to the government are vital if they are to mitigate the reputational risk of association with the regime's alleged excesses and iniquities.

Is Big Oil profiting from the regime?

One possible attraction for oil companies of an environment as risky as Equatorial Guinea is its unusually high profitability. According to the IMF, the government's share of oil profits is very small by international standards. The Fund's 1999 report said that the first contracts 'guaranteed an inordinately high 30% rate of return for oil operators and offered exceptionally favourable cost recovery conditions'.[67] The IMF said that while the government take for sub-Saharan African countries ranges from 45-90%, the initial government take in Equatorial Guinea was estimated at only around 15-40% and probably at the lower end of that range.[68]

One ex-government advisor described the way that oil contracts with the regime have taken advantage of the country's lack of capacity, its notoriety and the business inexperience of its elite. The ex-advisor put the government's share of the profits from the first concessions granted in the country at a trifling 10%, even lower than the IMF's range of estimates. The Economist Intelligence Unit offers a third and still lower estimate, at about 5%.[8,36]

The ex-advisor explained that the government's share increased after 1999 when the World Bank pointed out how bad a deal it was getting. Earnings are now somewhere between 15-25% of the profits.[36] Yet the World Bank states that the revised contracts on the Alba field are 'still too favourable to producers'[69] while the IMF records that the new contract system 'continues to bestow the oil companies with, by far, the most generous tax and profit-sharing provisions in the region'.[70] Transparency would clearly help redress this situation: if oil companies were obliged to publish their payments to the state here and in other countries, it would be obvious that Equatorial Guinea is getting a poor deal for its oil wealth. Of course, this might be one of the major reasons why international companies object to individual company disclosure.

The IMF also reports that the Equatoguinean authorities have little or no capacity 'to effectively monitor oil costs and to systematically evaluate company budget submissions'.[70] This renders the regime reliant on the oil companies' own accounting systems and analyses of operating costs to ensure they receive the correct revenues, which makes it possible for contracting companies to move costs around and use transfer pricing to minimise tax liabilities. The Angolan state oil company Sonangol, in contrast, is notorious for its diligence in assessing the operating and infrastructure costs of international oil companies.

Oil companies have also taken advantage of the regime's 'preference for immediate cash over long-term financial optimisation'[39] by loaning money for what the IMF calls 'unrecorded extra-budgetary spending'[70] at non-concessional rates. This meant providing up-front loans at high interest and then deducting this money at source from oil payments, although recent evidence suggests that such practices may have ended.[35] It was as if the regime was living off high interest credit cards provided by oil companies, with accountability made impossible because there were no government records of who owed what. One source suggested that large sums of money were spent in this way on infrastructure for the Central African leaders' summit in Malabo in 2002.[36]

President Obiang claims there is "no poverty" in Equatorial Guinea. The evidence says otherwise. Credit: Channel Four News

Sources familiar with Equatorial Guinea's oil accounts state that 2001 World Bank audits of both oil company operations and payments to the government uncovered sizeable discrepancies between payments due, and payments made by, companies operating in the country. In one case, one of the country's main operators had to make a 'corrective' payment of around US$53 million.[71] The 2003 IMF report also noted that US$88 million (some 3% of estimated GDP) has since been reclaimed by the government from audits covering 1996-2001.[72]

Questions about the nature of the relationship between the regime and oil companies are further underlined by a fax apparently sent to Mobil's Abayak headquarters on 25 August 1999 by the Minister of Mines and Energy, Cristobal Menana Elá Nchama, requesting funds 'according to the usual procedure' for a forthcoming presidential trip to Canada and New York.[73] The fax was first leaked to Spanish newspaper *El País*.[74] Shortly thereafter, the Equatorial Guinean government denied that Mobil ever paid President Obiang's travel expenses.[75] They explained that the trip was actually a medical check-up at a famous US clinic, which would suggest a personal rather than a public trip. Despite this official denial, it is necessary to ask why the minister made the request for funds in the first place and what the usual procedures are for oil companies requested to cover the funding of personal or public trips by senior officials.[73]

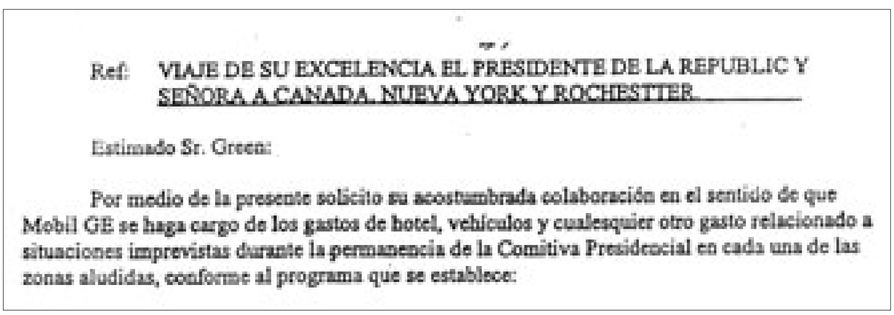
The US State Department and *El País* also report that, prior to 1999, oil companies employed local workers exclusively through the 'Agency for Promotion and Employment of Equatorial Guinea', known as APEGESA. According to both sources, the agency retained two-thirds of employees' salaries as a fee, screened out potential employees considered 'unfriendly' to the ruling political party, and fired several who signed a petition complaining about ill-treatment.[76] One newspaper recently explained that, 'any Equato-guineans that want to work for foreign multinationals have to go through the employment agencies run by Obiang's brothers, Armengol and Mba Nguema: for example, MSS, Multi Service System, and SENAVI, Servicio Nacional de Vigilancia'.[77]

By 1999, the government was making large repayments of its borrowings from oil companies by allowing them to deduct the money at source from oil revenues. It was reported in November 2003 that the regime was also close to completing negotiations for a $400 million oil-backed loan arranged by Deutsche Bank and four other banks on behalf of the newly formed state oil company, GEPetrol, which sought the money to buy a 20% stake in a liquefied natural gas project led by Marathon.[78] Given the unhappy precedent of oil-backed loans in Angola and Congo Brazzaville, this will render government finances even more obscure. The IMF recently warned that '[the authorities] should be aware that operations of state-owned oil companies have often led to transparency and control problems'[79] and advised that 'any expansion of GEPetrol's activities should proceed cautiously, with due attention paid to related transparency and governance issues', highlighting the need for 'a more detailed framework for the firm's supervision […] including proper internal and external controls, corporate governance, and reporting procedures'.[80]

Troubling questions on transparency

It is clear that the government of Equatorial Guinea will not be able to put to rest the allegations of unaccountable management and conflicts of interest over oil money until it declares and manages its revenues openly and transparently. As in Kazakhstan, revenue disclosure by companies would immediately identify whether the government's oil revenues are currently being parked outside the country. Such disclosure is made doubly important by the apparent lack of any coherent accounting for oil revenues in the country.

The *status quo* poses uncomfortable questions for oil companies and their investors. Consider the Riggs account. Payments into a treasury account overseas are not illegal, but US accounting rules – and more recently, the Patriot Act – call for close scrutiny of 'high risk' accounts such as those set up by foreign political leaders or their families.[81] Any US banking activity by the regime or its members would seem to be high risk, calling for increased scrutiny under the Act, given: a) Obiang's admitted personal control over the state's money and the possible conflict of interest with his role as first auditor of state income; b) the reputation of Obiang's brother Armengol as a torturer and allegations of grave human rights abuses by the government; and c) allegations of oil companies making loans for undisclosed purposes.



Ref: VIAJE DE SU EXCELENCIA EL PRESIDENTE DE LA REPUBLIC Y SEÑORA A CANADA, NUEVA YORK Y ROCHESTTER.

Estimado Sr. Green:

Por medio de la presente solicito su acostumbrada colaboración en el sentido de que Mobil GE se haga cargo de los gastos de hotel, vehículos y cualesquier otro gasto relacionado a situaciones imprevistas durante la permanencia de la Comitiva Presidencial en cada una de las zonas aludidas, conforme al programa que se establece:

Letter apparently from Equatorial Guinean government in 1999 requesting funds from Exxon 'according to the usual procedure' for a forthcoming presidential trip to Canada and New York.

Unless they take steps to mitigate associated risks by being fully transparent, oil companies working in the country might be seen as complicit in the misuse of state assets, with the knock-on effect on their reputation and share value. Reputational damage and loss of social licence to operate is increasingly worrying for investors in the oil, gas and mining sectors, as evidenced by the recent expression of concern by fund managers with control over US$6.9 trillion worth of assets.[82] There is a conflict of interest between the short-termism of current management of many oil companies operating in Equatorial Guinea, which have played along with an opaque and brutal regime in order to reap quick profits, and the interest of long-term shareholders who may pay the price of complicity in the future. Shareholders should not be complacent about the possibility that their oil company is making payments to a government whose soldiers may rape women with forks.

Despite his lengthy absences from Equatorial Guinea, Teodorín is the newly appointed Minister of Infrastructure whose talent and family resources have also earned him a place in the Los Angeles rap scene through his Beverly Hills music and publishing venture TNO Entertainment. As he himself explained: 'I am young and I like music a lot…Rap, funk… I am very close friends with the Jackson family, especially with Jeremy Jackson…next 25 September [2001], we are going to launch our first rap record. I haven't spent much, only half a million dollars'.[86]

The Riggs account also offers a coded message to the wider international community. Insiders suggest that the account's overseas location may reflect Obiang's desire to put the money beyond the reach of those around him, in part because of his increasing unease about the intense competition between various members of the ruling elite including his first son Teodorín and his cousin General Augustin Ndong Ona to succeed him as president. At the time of going to press, various sources report that a new wave of repression has begun in the country, focusing on General Ndong Ona, his family members and close associates.[83] One interpretation of this situation is that 'Equatorial Guinea's long-awaited power transition … with President Teodoro Obiang Nguema's oldest son, Teodoro, likely eliminating rivals in a final move before seizing the reins'.[84]

Given that Equatorial Guinea lies in a part of Africa where oil wealth is commonly linked to coups and civil wars, there is a risk of future insecurity that could well interrupt foreign access to its oil. Thus, the international community needs to push for transparency as part of a wider effort to put the country's political system on a stable and sustainable footing.

Based on our discussion with Equatoguinean ministers in February 2003, there are two points on which Global Witness and the government may agree. Firstly, any attempt to improve transparency should be global rather than singling out Equatorial Guinea.[22] Revenue transparency is a global governance problem that requires a global solution. Secondly, the ministers called for capacity-building assistance.[22] Such assistance is vital because there is minimal capacity in Equatorial Guinea at the moment. However, given that the absence of financial transparency in the country may be convenient for the regime, future assistance must be conditional on the transparent and accountable declaration and management of the country's oil money.

The absurdity of the current situation in Equatorial Guinea is epitomised in the almost perfect contradiction served up by an ExxonMobil spokeswoman in response to the Riggs account allegations. She protested: 'I don't know where our payments are made … we have very high business standards and ethical standards'.[85] It is impossible to have it both ways: oil companies and foreign governments must act now to avoid further complicity in the dispossession and penury of the Equatoguinean people.

Nauru

The ravaged remains of Nauru's topside. Credit: Sinartus Sosrodjojo/JiwaFoto Agency

Money unaccounted for: The entire Nauru Phosphate Royalties Trust worth more than US$1.4 billion.

A cautionary tale

While Kazakhstan, Congo Brazzaville, Angola, and Equatorial Guinea are faced with the immediate challenges of responsible resource extraction and fiscal accountability, the tiny island nation of Nauru – the world's smallest republic – has reached the twilight years of its catastrophic century-long engagement with the phosphate mining industry which provided virtually all the government's income.

Nauru has been a tax haven since 1972, although it made little effort to promote itself as such until it came to the world's attention as the 'launderer of choice' for the assets of the former Soviet Union. A Nauruan company is subject to almost no taxes, does not have to file a company report and does not have to identify its owners.[1] Having an economically-critical extractive sector develop in such an opaque management climate has led to a governance disaster. The island's story is included in this report as a bleak warning to other governments and the wider international community of the dangers of getting resource management wrong and ignoring failure.

For a brief period in the 1980s, Nauru had the highest per capita income in the world: now the island's resources have been plundered, there is no stable government, and the country is in terminal economic decline. Indeed, Nauru may 'voluntarily' cease to exist in the none-too-distant future as its population moves to a different island because the government is now insolvent and the island is virtually uninhabitable. This would make it the ultimate failed state.

Phosphate is the opiate of the masses

There is an old Nauruan saying that 'tomorrow will take care of itself'. Prior to the first phosphate mining operations of 1906, the sentiment might have proven correct; Nauruans had thrived on their island, halfway between Hawaii and Australia in the South Pacific, for more than a hundred generations.[2] But the discovery that Nauru possessed huge stores of rock phosphate – a valuable fertiliser formed by sea creatures, trapped in the coral as the island rose from the sea and enhanced by millennia of bird droppings – was to end the island's splendid isolation.

Phosphate mining effectively cannibalises the structure of the island itself: the topsoil has to be stripped off leaving behind a moonscape of 15-metre high, knife-edged coral pinnacles on which nothing will grow. The bleached coral wasteland that results heats up in the sun and drives away rainclouds and moisture. Some 80-90% of Nauru's total area of eight square miles has now been 'consumed' in this manner. Inhabitants cling to a small strip of vegetation on the beach around the island's ring road. This kind of mining could only have been in the interest of the people living on the island if the money was reinvested to compensate for the ecological damage caused. This did not happen.

Ordinary Nauruans had little say in phosphate extraction when it began under German colonial rule at the turn of the 20th century, and the occupiers notably failed to reimburse the islanders for the devastation of their land. In 1906, Germany sold the right to mine Nauru's phosphate to the British and Australian Pacific Phosphate Company in exchange for a cash payment to the German government, shares in the company and royalty payments for every ton exported. Nauruans were not involved in the negotiations but were paid a small 'gratuity' for each ton of rock removed. After the First World War, Australia, New Zealand, and the United Kingdom took over as trustees of the island and assumed the rights and assets of the Pacific Phosphate Company. The three powers then signed the Nauru Island Agreement of 1919, which entitled them to Nauru's phosphate at the cost of production. The British Phosphate Commissioners (BPC) controlled the mines and the nation was administered by Australia.[3]

Following a brief but brutal Japanese invasion during the Second World War, the BPC went so far as to suggest that the entire population of the island should simply move: with their numbers drastically reduced by the war and their land consumed by mining, it was suggested that they might be better off resettling on Australia's Curtis Island.[2] The Nauruans refused and the BPC resumed its mining operations.

In 1948, reported revenues from mining were some AU$745,000, of which a mere 2% went to Nauruans directly or into trust funds. Another 1% was charged for the costs of administering the island. When information on exactly how much money was being made from phosphate mining became publicly available, Nauruans began to push for a greater share of revenues – a small victory for the idea of revenue transparency. By 1966, Nauru's inhabitants were granted 22% of mining revenues and an additional 14% was earmarked for the island's administration. The islanders were still not yet receiving the full price of the phosphate on the world market, however. The BPC was selling phosphate onwards to trading companies at the bargain price of 10 shillings per ton compared to a world price of about 30 shillings per ton,[4] so Nauru's phosphate wealth was being sold off on the cheap.

By the time Nauru finally gained independence in 1968, mining had already destroyed more than a third of the island's area. Although dispossessed for decades, each Nauruan woman, man and child was suddenly worth about AU$500,000.[4] In the wake of independence, Nauruans turned against foreign control of their phosphate industry and set up a government-owned business called the Nauru Phosphate Company (NPC) to continue extraction. Profits were to be split three ways: annual royalty payments to landowners; investments in real estate and other holdings through the government-managed Nauru Phosphate Royalties Trust; and payments to a rehabilitation fund to tackle the estimated 20-year, US$210 million project of rehabilitating mined-out land.[5] All of these funds were maintained and distributed through the Bank of Nauru.

Nauru also enacted corporation and trust laws as early as 1972 to make itself attractive as an offshore financial centre, although it never widely advertised its status as a tax haven. Under the framework established by Nauru's Companies Act, the International Companies Act and the Banking, Insurance, Stamp Duties and Trust Companies Act in the early 1990s, companies are granted an extraordinary set of privileges.

Offshore companies are not charged personal or corporate income taxes, capital gains tax, withholding taxes, or any sales taxes or employment taxes. They also operate under conditions of full anonymity such that, 'the details of neither the directors, nor the owners are available in the public company register since these details need not even be reported to the authorities of Nauru'. Although all companies are required by law to keep accounts, so-called international and exempt (i.e. offshore) companies did not have to file them.[1]

This tax-free, reporting-free environment was set up partly because the revenues from the phosphate business meant that Nauru never had to develop a broad income base, although it also meant that the phosphate income itself was free of any coordinated scrutiny. As the NPC was actually doing business in-country, it was technically subject to slightly more stringent reporting requirements than offshore companies. In reality, neither oversight nor the framework for oversight were ever developed.

Virtually all of the Trust's assets were invested in dozens of Nauruan offshore holding companies that, under Nauru's laws, were subject to almost no reporting. For example, a property in Honolulu, Hawaii was bought by the Nauru Phosphate Royalty Honolulu Corporation (NRPH), which was a subsidiary of the Trust, to be developed by the Nauru Phosphate Royalty Development Corporation, itself a subsidiary of the NRPH. Such a plethora of agencies, often operating under reporting-

Phosphate mining has driven Nauru's economy for decades, but now the money is running out.

Credit: Sinartus Sosrodjojo/JiwaFoto Agency

exempt status, made bookkeeping and asset tracking almost impossible.

Government ministers themselves often had overlapping and conflicting roles. President Rene Harris, for example, was chairman of the NPC and managed a failing shipping venture funded by the Corporation's money called the Nauru Pacific Line.[6]

Although the Nauruan Constitution mandates that an annual budget be presented to Parliament in each fiscal year, various government entities failed to publish their accounts for years. The Republic of Nauru Finance Corporation, which was responsible for annual payments to landowners, did not table a budget for eight years in the 1990s.[7] As of September 2001, *Pacific Islands Magazine* noted, the Bank of Nauru and the NPC had not filed reports for any year since 1995.[8] The Asian Development Bank's 2002-2003 Outlook for Nauru states: 'there is a need to improve transparency. The true debt position of the government and its instrumentality, the net worth of the Nauru Phosphate Royalties Trust (NPRT), and the reasons for the substantial decline in its value are not fully known'.[8]

The cumulative effect of years of opaque accounting and secretive transactions makes it virtually impossible to determine the country's real economic situation with any degree of accuracy; the government itself probably has little idea. The *Sydney Morning Herald* reported, 'Nauru's leaders either remain secretive on the net value of foreign assets, or they really do not know, because there are a plethora of government agencies and no national accounts are kept'.[9]

For one brief moment, Nauru had the highest reported per capita income in the world.[4] Estimated assets reached a high in 1991: by one estimate, that year the world's smallest independent republic held assets worth AU$2.1 billion, or almost about US$1.4 billion.[10] If the money had been invested sensibly, each of Nauru's 8,000 citizens would be worth many millions of dollars today.[4]

A common joke at the time was that 'Nauru' stood for 'No Action Unless Really Urgent'.[3] A direct result of this attitude was a total failure to hold the government accountable for the management of revenues. Flush with money and with severely diminished oversight, the government spent lavishly, failed to produce budgets, invested poorly, and in many cases squandered wealth in unworthy business ventures. The *Sydney Morning Herald* described as 'legendary' the 'stories of excess and waste' and 'investment white elephants'.[10]

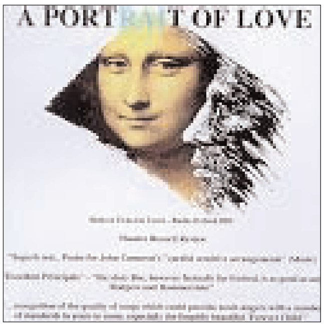
Somebody call my broker

The great tide of money resulted in a weak work ethic amongst Nauruans – a problem compounded by the fact that the dirty work of mining itself was done mainly by poorly paid immigrants from nearby islands and China – that would ultimately undermine the development of a varied and self-sustaining private economy. The great majority of Nauruans were employed by government-owned entities, such as the NPC; as recently as 2001, the government employed 95% of working Nauruans.[11]

Islanders themselves paid no taxes and enjoyed free health care, electricity, housing, and education. Citizens too ill to be treated on the island would be flown to Australia for free care. In addition, if a student wanted to attend college overseas, the government would foot the bill. As land was lost to the mines, Nauruans imported more and more of their food and developed a sweet tooth. Even though there was only one road on the island, cars outnumbered people.[12] The combination of processed foods and cars caused the Nauruans to develop the highest rates of obesity and diabetes in the world. Life expectancy dropped to 56 years, among the lowest in the South Pacific.[13]

Nauru's leaders lived the high life and became notorious for their gambling habits in the casinos of Melbourne and one senior official was famous for collecting Cadillacs. *The Visionary*, a sporadic political publication that is Nauru's only national news-sheet, accused President Rene Harris of running up a tab of over AU$1.5 million with the Bank of Nauru that would take 25 years to repay on his salary.[14] Questioned by an Australian Broadcasting Corporation journalist on allegations that whilst in charge of the NPC, he had accrued personal bills worth AU$230,000 for various luxury items, lavish holidays, and a property in Melbourne, Harris responded that he was not aware of 'misappropriating that amount of money' and then said he had repaid the money, although he also declined to provide any proof of the latter assertion.[15]

Among Nauru's bad business investments was its own airline, Air Nauru: despite its remote location halfway between Hawaii and Australia, Nauru's leaders envisioned the island as a travel hub. Air Nauru ran up multi-million dollar losses for years.[4,12] Nauru also launched a shipping line that failed, as did a phosphate refinery plant in India. Perhaps the most striking folly was the government's US$2.9 million underwriting of a musical production on the London stage in June 1993 called 'Leonardo: A Portrait of Love'.[16] The show was panned by critics, one of whom remarked that it was 'six months to Christmas and the first turkey has arrived' and closed after only four weeks.



Several of Nauru's financial consultants and investment partners have been indicted on charges of embezzlement and fraud:[17] one set of investors even convinced the Nauruan leadership to spend almost US$30 million on a bogus bond issue.

By 1996, the Trust was worth half of its estimated 1991 value. The government continued to spend, borrowing from future mining royalties, even though by definition there would be no future for mining.

The Trust's money was also used to buy properties all around the world, including a skyscraper in Melbourne, hotels in Fiji, and a development complex in Hawaii, all of which might have been solid investments had the government not borrowed against an expected rise in the value of the properties.[8]

These debts would prove the most painful of all. When a worldwide depression in phosphate prices caused a slump in income, the government borrowed from the Trust to pay landowners' annual fees. Meanwhile, the Bank of Nauru, the NPC, and other national entities also drew upon the same trust, such that in 2001, Nauru had to write off hundreds of millions of dollars of loans drawn on the Trust.[18] Strapped for cash, Nauru turned to outside lenders and continued to mortgage the remains of its future phosphate revenues.[19] By 2002, the island's budget deficit was US$15 million, or about a quarter of its gross domestic product. External debts were much higher, due to loan refinancing and the mortgaging of property assets around the world.

Nauru's wealth fuelled a spending spree on investments like this building in Melbourne, Australia.

The Asian Development Bank summarised the situation as follows: 'successive governments have financed the fiscal deficits in an unplanned and largely non-transparent manner, borrowing directly from NPRT (the Trust), and employing the government-owned Republic of Nauru Finance Corporation (RONFIN) as an on-lending agency that borrowed from NPRT and used NPRT assets as collateral for external commercial borrowing. The financing of the budget deficits and debt servicing created a liquidity crisis in 1996 that has continued and intensified in subsequent years. As liquid funds in NPRT and government corporations such as NPC have been depleted, government has relied on extending its overdraft with the Bank of Nauru (BON). The issuing of BON cheques has drained the bank of its reserve holdings of currency (the Australian dollar), leaving it unable to effect international transfers or meet depositors' withdrawal demands. BON has been insolvent for two years, financial intermediation has broken down, and confidence in the payments system has disappeared. The NPRT assets that were to secure sustainable consumption levels for an almost totally import-dependent society have been substantially run down'.[19]

The economic naiveté of the Nauruans was matched by political volatility. The island's tiny government, an 18-member parliament including the president and his cabinet, was frequently dissolved and/or in disarray. Universal suffrage did not translate into truly competitive elections. In 2001, *Pacific Islands Magazine* wrote that 'election to Parliament has been the preserve of by-now veteran politicians assured of votes of automatic loyalty from members of big extended families...Governments are formed by dominant personalities able to persuade fellow Parliamentarians assured of a cabinet post to elect them as president.'[20]

In their grappling for power, members of Parliament made frequent use of a Nauruan law that allows a vote of no confidence: Nauru has had ten changes of government since 1996. This constantly changing administration has made it all but impossible to maintain any long-term strategy for management of phosphate revenues. By August 2001, the Bank of Nauru was insolvent;[9] when landowners went to the bank in December of that year to collect their annual royalty checks, the money wasn't there. Air Nauru's fleet dwindled to one jet, usually grounded for want of fuel and repairs. When the lone phone line to the island went down after a flood in early 2003, it took two months before someone was sent out from Australia to repair it. Shipments of diesel fuel and fresh water were repeatedly held up for lack of payment and the government stopped paying its employees.

A comprehensive plan for financial reform was devised in 1999 through National Economic Summit proceedings, in partnership with the Asian Development Bank (ADB); but the government did not make public the recommendations, and few if any were implemented.[9] A particularly bleak 2002-2003 Outlook Report from the ADB says that Nauru is in 'long-term economic decline', and calls its financial sector 'essentially non-operational'.[9]

The NPRT and the Rehabilitation Fund have been frittered away; the country is subject to lawsuits in China and Japan for nonpayment of debts. Nauru's myriad offshore companies have begun a firesale of their assets and properties worldwide. And, as a coup de grace, recoverable phosphate is set to run out this year.

Desperate measures

Nauru has made many last-ditch efforts to make money, each more problematic than the last. In the summer of 2001, it agreed to become part of Australia's ominous-sounding 'Pacific Solution', accepting an AU$20 million aid package in return for taking in hundreds of Iraqi and Afghan asylum-seekers who had tried and failed to reach Australia. The refugees were established in camps built upon the mined-out coral. Despite protests from Nauruans, particularly following the September 11 terrorist attacks, about 300 asylum seekers remain.[21]

Nauru's record on immigration issues might be considered controversial, given that the island has a propensity to sell passports to anyone willing to pay for them. Nauru hired agents to sell passports in Hong Kong and Macao; citizenship and a passport in the name of one's choice could be purchased for as little as US$10,000.[22] In 2003, the US Government released details of the arrest of six alleged terrorists, including two Al Qaeda operatives, who were caught travelling in Southeast Asia on Nauruan passports.[23]

The government-run Nauruan Agency Corporation (NAC) allows banks to register on the island for as little as US$50,000.[24] A reporter who visited the island in 2000 discovered that the NAC is housed in a shack near the beach: he met no-one there but a bemused cleaning lady, and few other Nauruans appeared to know that it even existed.[25] But by September 2001, some 400 entities had used this service; all of them were registered to the same post office box.

Financial transactions can be completed online and, like its offshore companies and investment trusts, Nauru does not require banks registered there to file records with the authorities.[26] Russian businessmen appear to have made particularly good use of this service: in 1999, Viktor Melnikov, deputy chairman of Russia's central bank, told the Washington Post that some US$70 billion was transferred from Russian financial institutions into the accounts of Nauruan banks the year before.[27] Melnikov explained that more than 90% of that money then returned to Russia; 'that is to say our economic entities use this method to transfer their assets, hiding them … and later when they need these funds for their work here, they bring them in as credits. They effectively evade taxes in this way.'[28]

Nauru was also in the first wave of states sanctioned as a 'non-cooperative country or territory' by the OECD Financial Action Task Force (in 2000) for these problems.[28] In March 2003, then-president Bernard Dowiyogo travelled to Washington to discuss money laundering and passport trafficking. Whilst there, Dowiyogo suffered a diabetes-related heart attack. He signed a presidential order from his hospital bed to shut down offshore banks and died shortly afterwards, victim of a condition that plagues 50% of his fellow Nauruans. At age 57, he had already outlived the average life expectancy of his people.

After two more changes of government and a period of hung parliament, Rene Harris is now back at the helm, although he is also crippled by diabetes and survives due to monthly kidney dialysis in Melbourne. Under sustained international pressure, Nauru announced in June 2003 that it had closed down its offshore banking sector, suspending the licences of 139 banks.[29] The island was later removed from the OECD's list of countries considered uncooperative in the fight against tax evasion.[30]

Nauru's President Rene Harris

Nauru's offshore banking business is finally coming to an end; the island itself may be going the same way.

Up, up and away

Nauru has no arable land left and islanders cling to the shoreline as the miners dig up the last of the phosphate. Rainfall is decreasing as the phosphate moonscape heats up and drives clouds away. Fresh water and the majority of the island's food must now be imported. There seem to be few ways that Nauru can remain self-sufficient: one ambitious scheme, put forth by Australian businessmen, would transform the entire state into a casino. The plan would essentially outsource Nauru's government to the Australians, who would be granted an exclusive 10-year license to attract investment, issue banking licenses, maintain a shipping register, oversee casino operations, and regulate travel documents, in exchange for 50% of the profits and government titles.[31]

The other idea for survival is one that was first proposed by the British Phosphate Commission after the Second World War: the entire population of Nauru could simply move. Curtis Island is still available. This time it might be an offer that the Nauruans cannot refuse. The island's low-lying land is increasingly threatened by rising waters attributed to climate change and there is no money for remedial action. With or without its beleaguered citizens, Nauru may be fated to quietly vanish from the map.

For Nauru's people, the cupboard looks bare. Credit: Sinartus Sosrodjojo/JiwaFoto Agency

Paradise lost

Nauru's sorry tale provides a dramatic example of the curse of sudden wealth and the 'paradox of plenty'. A resource industry developed in a tax haven where zero disclosure was required. The initial bonanza reinforced a lack of oversight and accountability in state institutions and progressively led to the breakdown of a functioning and accountable state.

Taken advantage of by foreign phosphate companies, and colonising nations, for decades, the native Nauruans were eager to claim their own rewards. But having been occupied since their introduction to the modern world, the Nauruans were poorly prepared to manage their resources and their future. Australia and other countries benefited from cheap phosphate, but did little to help educate the Nauruans. Sporadic interventions by the Asian Development Bank failed to turn the tide and the island's main bilateral partner, Australia, has seemed more interested recently in using Nauru as a dumping-ground for asylum-seekers than in promoting accountable government.

The international community has based its model of energy security on the premise that failed or failing states can be left largely to their own devices as long as the resources keep flowing out, with little or no attention paid to the impact of revenues from these resources on weak state structures. The obvious lesson from Nauru is that the model does not work: initial problems with accountability and oversight are left to become fatal flaws in a state's whole architecture.

Nauru's resource management disaster demonstrates that the international community must systematically engage failed and failing states on the revenue transparency issue. It also shows that although transparency on the part of international companies is a key to the open and accountable management of revenues by states, it is not the whole solution in itself. The next section of this report looks at ways for the international community to enact a systematic and worldwide approach to revenue transparency.

Making companies and governments transparent

Oil, gas and mining companies make a number of different payments of resource revenues to government. These include:

- Royalty payments, often denominated as a percentage value of production;
- Bonus payments on signing a contract, on the location of commercial mineral deposits or on reaching certain production levels;
- Corporate income tax, paid on income after permitted deductions for operating, exploration and interest costs and depreciation of assets;
- Other taxes including withholding tax on dividend payments, excise tax, customs duties, sales/value-added tax and property tax.

Although complicated, these arrangements are not unfathomable. A few simple reporting rules could capture most company and government interactions. Much of the work on deciding who should report what and when has already been done under the auspices of the UK government's Extractive Industry Transparency Initiative.

However, most contracts signed by oil, mining and gas companies with host governments have a gagging clause in them that prevents disclosure of information without government approval. Permission is unlikely to be forthcoming when it is most necessary, as BP found out to its cost in Angola. The company made a public declaration that it would publish its payments to the Angolan government and almost immediately received a letter threatening contract termination for violating the confidentiality clause of its extraction agreement (see box: 'The Dangers of Voluntarism').

Confidentiality clauses are less of an obstacle to disclosure than they seem, however, because they typically include broad exemptions for information that is required by law. Article 33(2) of the standard Deep Water Production Sharing Agreement in Angola, for example, states that: 'either Party may, without such approval [i.e. the approval of the national government or the state oil company], disclose such information … to the extent required by any applicable law, regulation or rule (including, without limitation, any regulation or rule of any regulatory agency, securities commission or securities exchange on which the securities of such Party or of any of such Party's affiliates are listed)'.

The logic of the *Publish What You Pay* campaign is clear, therefore. If stock market listing requirements and company financial reporting standards included an obligation for extractive industry companies to disclose their revenue payments to governments, then any specific gagging clauses would be voided in respect to their payments to that particular government.

There is an argument that listing-based disclosure requirements will not work because they do not cover unlisted companies, whether private or state-owned. In practice, however, most of the biggest players in the extractive industries are either listed on stock exchanges or likely to list in future. At a global level, listed resource extraction companies compete mainly with each other. If all these bigger players are captured by disclosure requirements, there will be no significant loss of competitiveness.

Unlike the voluntary disclosure advocated by some parties, disclosure imposed by regulators would take the political heat out of the relationship between resource extraction companies and the countries where they do business. Disclosure would simply become a standard operating procedure that a company would implement without further discussion, rather than a statement of principle or a political judgement on a particular host government.

The exact form of regulation and the type of companies affected by it will depend, of course, on the country in which the regulation or rule is passed. This step is neither unprecedented, burdensome nor difficult to implement because:

- Resource extraction companies are routinely subjected to disclosure requirements above and beyond most other businesses because the size and quality of their reserves and other such data have a direct effect on their financial worth;
- There is minimal associated reporting burden. Companies must already know what they pay to every national government for internal accounting purposes and for group financial reports;
- Under anti-bribery legislation in most OECD countries, stock market regulators already police a 'books and records' provision that requires companies to keep adequate details of their dealings with other entities and prohibits 'off-the-books' accounting. Disclosure of payments made by individual companies to foreign governments is a logical extension of this requirement and is consistent with the spirit and intent of existing provisions.

Revenue disclosure is also in the enlightened self-interest of company management, shareholders and the international community. Investment managers who control some US$6.9 trillion (€5.5 trillion, £3.8 trillion) of funds have recently spelt this point out very clearly in a joint statement first issued in May 2003 (see below).[1]

The *Publish What You Pay* coalition has highlighted numerous ways to promote revenue transparency in the extractive industries. These include:

- Non-legislative adjustments to accounting requirements and stock market listing rules enacted by regulators in the wake of recent accounting scandals;
- A future international financial reporting standard for the extractive industries, developed by the International Accounting Standards Board;
- Legislative adjustments to existing anti-bribery ‘books and records’ provisions enforced by national securities and financial regulators;
- Work on harmonised European company reporting standards, such as the EU Directive on Transparency Obligations of Publicly-Traded Companies, which is currently before the EU Parliament.

There is no shortage of appropriate vehicles to achieve revenue transparency. It is political will that is currently lacking.

The Dangers of Voluntarism – BP in Angola

The retaliation experienced by BP when it announced that it would disclose its revenue payments in Angola is an object lesson in why leaving companies to become transparent voluntarily will rarely achieve meaningful disclosure.

In a February 2001 letter to Global Witness, BP-Amoco Group Managing Director Richard Olver stated that the company would publish total net production by block, its net payments to state oil company Sonangol, and total taxes and levies to the Angolan government.

This announcement brought a dramatic response from Sonangol boss Manuel Vincente, in the form of an immoderately-worded letter that was copied to all the other oil companies operating in the country as an implied threat.

The letter, subsequently leaked to Global Witness, recorded Sonangol’s ‘great surprise, and some disbelief’ that BP was ‘disclosing information about oil-related activities in Angola, some of which have a strict confidential character … thereby seriously violating the conditions of legal contracts signed with Sonangol’. Such activities were deemed ‘sufficient reason to apply … contract termination’.

The letter accused BP of deciding to adopt transparency because it has ‘been under pressure by organised groups that use available means in an orchestrated campaign against some Angolan institutions by calling for “pseudo-transparency” of legitimate government actions’. This statement is somewhat confusing: if government actions are legitimate, why be afraid of transparency?

The Angolan threat appeared to have had the desired effect. BP has subsequently sought to highlight that information about its payments to the Angolan government are contained in its UK tax filings for BP Exploration (Angola) Ltd, a UK registered subsidiary of the company, and has argued that by doing so, it has fulfilled its promise. But BP Exploration (Angola)’s filings are hardly the complete set of information promised in Olver’s declaration. They do not provide any information about the financial dealings of other BP Amoco subsidiaries operating in the country (such as Amoco’s interest in Block 18 which is registered in the Netherlands), nor would BP Angola’s books disclose whether there were payments to the Angolan government made direct by its parent company.

BP’s experience makes it clear that oil companies operating in countries like Angola are in a difficult position. There is little benefit to international oil, mining and gas companies in having their legitimate payments to governments misappropriated, but if they try to publish relevant information, they face retaliation from vested interests in the government and being undermined by less scrupulous companies. A regulatory solution that would create a level playing field for all companies and implement good practice across competing companies is therefore necessary if transparency is to happen where it is most needed.

Why transparency is a corporate governance and energy security priority

Revenue disclosure will allow company managers to protect their corporate reputations and ensure they are not facing unfair competition from unscrupulous rivals or inadvertently destabilising the environment in which they operate. It will also benefit investors and the international community more broadly.

There is little value to companies in having their legitimate payments to governments misappropriated and squandered, since this only leads to social divisiveness and instability which may eventually threaten their operations. As Shell and Chevron have experienced in Nigeria, the long-term reputational damage from dealings with a corrupt regime can be huge. Poverty, ethnic unrest and resentment against oil companies boiled over in the Delta region in March 2003 and the ensuing turmoil slashed Nigeria's output by more than 750,000 barrels per day – a loss of one-third of the total production of sub-Saharan Africa's biggest oil producer.[2] Because of the unrest, some oil tankers loading in Nigeria have been required to take out war risk insurance.[3]

More generally, the perception that producer governments are less than accountable to their own people in the management of natural resources can also be a catalyst for unrest. A case in point is the recent upheaval in Bolivia, where a political confrontation over natural gas exports led to violent protests and the toppling of President Gonzalo Sánchez de Lozada.[4]

Policies to require revenue transparency are also in the interests of investors and the international community more broadly. As Enron and similar scandals have demonstrated, a company that manages its finances in a non-transparent way poses a clear risk to the interests of its investors. The Kazakh and the Congolese case studies showed American and French companies using non-transparent means to win future gains that are turning out to be highly insecure: indeed, some of the contracts are so opaque that they are subject to continual renegotiation. Investors need to be reassured that companies are not winning business with methods that could be counter-productive in the long term.

This point is very clearly highlighted in a recent statement by 57 major North American, European and South African investment houses which manage some US$6.9 trillion in funds and hold significant stakes in all the main international oil companies. They state: 'legitimate, but undisclosed, payments to governments may be accused of contributing to the conditions under which corruption can thrive. This is a significant business risk, making companies vulnerable to accusations of complicity in corrupt behaviour, impairing their local and global "licence to operate", rendering them vulnerable to local conflict and insecurity, and possibly compromising their long-term commercial prospects in these markets.'[1]

Newmont Mining's experience in Indonesia provides a good example of the positive impacts of disclosure on a company's operational environment. The company began publishing details of its payments to the Indonesian government in local newspapers in 1999 in response to concerns over where that money was going. The company now puts out quarterly adverts stating the amount and

'Extractive revenue management and transparency are really the heart of the matter: the problems and opportunities they present are at the nexus of security of supply for the US; accountable government and sustainable development for the people of the oil-producing countries; and sustainable investment for the companies.

Opaque and inequitable revenue distribution is usually due to a combination of raw political calculation, gross corruption, and sheer mismanagement. The squandering of public revenue skews patterns of investment and further enriches elites; it corrupts governance and erodes the rule of law; it exacerbates regional conflicts and threatens national unity; it deprives local communities of their right to development and condemns them to poverty. Companies' bottom lines may not be affected in any one year, but the cumulative squandering of revenues takes its toll: it challenges their social license to operate; endangers their local operations; and threatens their global reputations. It does so by stoking tensions between oil-producing communities and the companies operating amidst or in close proximity to them. It puts companies in the unwanted position of acting as *de facto* surrogate governments, due both to the default of the real government authorities and to the sometimes violent demands of the local communities. And it can make the companies appear complicit in human rights abuses committed by security forces called in to quell … unrest.'

March 2003 Statement to Carnegie Endowment for International Peace by Bennett Freeman, ex-US Deputy Assistant Secretary of State for Democracy, Human Rights and Labor.

nature of its payments to the government as well as specifying to whom the payment was directed and the bank account numbers where payments were made. Although there is controversy about certain other aspects of Newmont's operations in Indonesia, company executives describe the disclosure of payments as one of the most important things they have done in the country to improve their relationship with local stakeholders, not least because it highlighted the government's responsibility for service provision to local stakeholders.[5]

There are other business benefits to greater transparency. Investment analysts may need information on company payments to a state so as to calculate the in-country costs of doing business, to work out the profitability of investments and to identify company subsidiaries in particular countries that are under-performing. The higher the level of disclosure, the better investors will be able to safeguard their own interests.

More broadly, the instability triggered by mismanagement of oil revenues can pose a major threat to energy security. It also threatens the prospects for transparent and accountable government, the promotion of which should be a foreign policy priority for energy importers like the US. Countries in Africa that are not transparent about their revenues currently supply about 15% of American oil imports, a figure that the US National Intelligence Council expects to rise to 25% by 2015.[6] Production from the potentially unstable Caspian region is expected to double in the next decade: though this production may be more important to European energy security than the US, any future disruption of supply would have a knock-on effect on world oil prices.

As a recent report by the US African Oil Policy Initiative Group argues, 'the US should not be partnering with unpopular, undemocratic regimes. On the contrary, proper foreign policy would bolster American values with our allies and encourage democratic development. One way to achieve this is to engage with energy-producing countries in a way that fosters and encourages the development of a middle class, rather than allowing petro-dollars to flow into the hands of a small number of corrupt leaders and their associates … African oil is not an end, but a means: a means to both greater American energy security and more rapid African economic development.'[7] Revenue transparency is essential to achieve these objectives, which should also be a priority for other industrialised countries.

Lack of transparency imposes a further cost on the international community. The illicit diversion of oil and gas revenue causes serious shortfalls in state budgets which can only be made up, if at all, by grants and loans from abroad. This imposes a heavy and unnecessary burden on international humanitarian agencies, economic assistance agencies and official lenders, nearly all of whom receive funding from the North. This money should be used for more positive purposes than filling in the gaps caused by the misappropriation of oil and gas revenues by corrupt officials.

Aftermath of a riot; oil fuels violent conflict in Nigeria's Delta region. Credit: AFP/Getty Images

Publish What You Earn: Requiring host government transparency

Some contractual arrangements between companies and host governments – mostly oil and gas contracts since the mid-1980s – may also involve the government receiving an income from so-called 'Production Sharing Agreements' that is independent of company payments (see box: 'Resource Extraction Regimes').

Achieving a complete picture of government income from resources will therefore require governments to reveal their revenue streams from both state-owned companies and production sharing arrangements. This information, added to data from companies about what they have paid, will create a form of double-disclosure book-keeping that will enable the citizens of resource-rich-but-poor countries to track the movement of revenues into the national budget.

Mechanisms to promote transparency of a host government's own share of profit oil and gas are less direct than those applied to international companies. In addition to high-level diplomatic pressure, there are a number of other levers available to the international community. Taken together and delivered in a systematic manner, these policies will capture the government's own revenue stream from resource extraction in many non-transparent countries. Again, it is not policy ideas that are lacking, but their coordinated and effective delivery. These include:

- **Getting it right from the start**
  Resource-rich developing countries should be targeted with more effective capacity-building assistance before extraction begins, so as to promote best practice in contracting and revenue management from the start. This role could by played by bilateral donors, or by multilateral agencies like the World Bank.

- **Attaching conditionality to development assistance**
  There is a basic efficiency argument for making development assistance to non-transparent resource-rich countries, for other than humanitarian purposes, dependent on the public declaration of their income streams (see box: 'Transparency is a Corporate Governance and Energy Security Priority'). Currently, donor money that is desperately needed elsewhere is being used to cover for the failure of states to provide for their own citizens, because the government's own money has been embezzled. If this problem is not going to be endlessly exacerbated, revenue transparency must be required for future funding programmes (see box: 'Conditional Development Assistance from Donor Governments and International Financial Institutions').

- **Supporting reformers in government**
  Capacity-building assistance to governments in non-transparent countries should be targeted at domestic constituencies for reform, such as finance ministries trying to promote centralised accounting and budgeting.

- **Investing in civil society**
  Improved disclosure by multinational companies should be complemented with actions that strengthen the capacity of local civil society to call governments to account over the way revenues are managed and spent.

- **Requiring transparency through export credit agencies**
  Export credit agencies (ECAs) are public bodies that provide government-backed loans, guarantees, and insurance to corporations from their home country that seek to do business overseas. Oil field development involves major infrastructure projects often in partnerships with national oil companies like Sonangol in Angola, and the huge sums involved are often a reason for all the partners to seek ECA support.

  If the ECAs made revenue transparency a criterion for all future export credit financing agreements in all the countries where they operate, then state oil companies would be required to publish their accounts. If this does not happen, then taxpayers in the North will be unwittingly subsidising the disempowerment of civil society in the South by helping to fund oil industry development without appropriate accountability and transparency. By extension, this will worsen the burden on Northern taxpayers as development assistance is needed to pick up the burden of state failure in the South.

- **Requiring disclosure of resource-backed loans from banks**
  In addition to payments made directly to the state by companies in the extractive industries, there is a clear need to require the disclosure of loans secured against future resource revenues, especially oil revenues. Banks may favour such loans because they earn high interest rates and are secured against future resource extraction, but the banks risk making

Resource Extraction Regimes

There are two main forms of resource extraction agreement, concessionary and contractual.

A **concessionary system** is an agreement between the company and a host government that gives the former the right to explore for, develop, produce, transport, and market a commodity within a fixed area for a specific amount of time. The production and sale of that commodity from the concession is then subject to rentals, royalties, bonuses and taxes. The company holds title to the resources produced.

Most mining contracts and many old oil and gas contracts are concessionary, often taking the form of 'joint ventures' in which companies take a percentage of an operating licence, pay proportionate development and operational costs and, after paying taxes and royalties, receive any profits in proportion to their shareholding. In these cases, requiring companies to disclose their payments to a government would provide a clear picture of a government's income from these types of concessions.

Contractual systems cover most oil and gas contracts since the mid-1980s. In these arrangements, a host government retains ownership of its hydrocarbon or mineral reserves and an extractive company makes a deal with the host government whereby it bears all exploration costs and risks and development and production costs in return for a stipulated share of the production resulting from this effort.

These arrangements most commonly take the form of **Production Sharing Agreements** (PSAs). In the oil industry, where such arrangements are most important, contracting companies recoup their costs upfront from a share of the oil extracted, called the 'cost oil'. After payment of taxes and other duties, the remaining oil, called 'profit oil', is divided between the private-sector partners and the state company according to their equity stakes in the block. The theoretical advantage of a PSA over a joint venture is that the government gets its own share of the oil which it can control and sell independently of the multinational companies.

PSAs are less transparent than concessionary agreements because the breakdown of income is more complicated as the government receives a share of the profits independently from the direct payments (e.g. signature bonuses, royalties and taxes) made by oil companies. Such arrangements are promoted by institutions like the World Bank regardless of their governance implications. Income from direct oil trading by a government is usually about 20-30% of the total revenues from oil extraction, though this can rise to 70% in the case of mature oil producers, for example in the Middle East.

Some oil companies have used examples from oil developments in the Middle East to argue that requiring disclosure by multinational companies alone would leave a substantial portion of government revenues off the books. This is a matter of concern, and it is one of the reasons that organisations like Global Witness and its *Publish What You Pay* partners do not only seek disclosure by multinationals but are also calling for host government transparency. However, company disclosure is a crucial part of the equation for a number of reasons:

- *Payments by companies comprise the majority of revenues to governments at the start of field development.* Most fields in the countries in this report are currently in the field development phase. In this early phase the government's profit share is smaller because most of the revenues are taken by companies to recoup their up-front investment costs. Thus, the government's direct take, as opposed to payments from the oil companies, is necessarily lower. To take one example, calculations commissioned by BP and Statoil in Angola, for a joint development intended to start in late 2002, show that oil company tax payments constitute 68% of the government's oil income from the concession during the first nine years of production.[8]
- *Mortgaging of government revenues means most ready cash is from company payments.* Most of the non-transparent governments mentioned in this report are probably receiving most of their income through taxes and royalty payments from companies. This is because governments have often mortgaged their share of future profits in exchange for money upfront, which is then used by ruling elites for purposes unknown. The next three to five years of the Angolan government's production, for example, may well be tied up servicing the hefty interest payments on its several billion dollars worth of oil-backed loans.
- *Requiring disclosure by law protects multinational companies, so there is no reason not to provide that information.* Companies often claim that they are not surrogate governments: Global Witness agrees that companies can only do so much. It is not up to them to worry about whether their information provides a complete picture of government finances; all that a company should be concerned about is whether adequate regulations exist to require disclosure that protects it from gagging clauses in its Production Sharing Agreement. It is not up to companies to call a government to account for the way it manages its money, nor should they tell that government how to spend that money.
- *Company payment information provides a first point of leverage for civil society.* Even if all the information on government income is not available, local civil society can at least begin the process of tracking those payments declared by companies into the national budget. This, in turn, will put pressure on the government to declare its own income directly.

themselves complicit with the misappropriation of state funds unless provisions are in place to check that loans are being properly used and to ensure that the borrowing government's fiscal management is transparent. Banks should therefore disclose all resource-backed loans and require that the borrowers agree to be audited in a transparent fashion, as a condition of receiving the loan. In cases where a state oil company was the recipient of an oil-backed loan, the audit would need to reveal not only its receipt of the money but subsequent transfers of money to the government.

At best, the provision of recent oil-backed loans may have undermined the work of multilateral institutions like the International Monetary Fund (IMF) in countries like Angola by providing governments with funds which are not subject to the strict conditions of IMF loans. At worst, oil-backed loans to such countries may provide a whole system of parallel financing, outside of public scrutiny, which supports the shadow state and provides opportunities for cash to be diverted into private pockets.

Such information is not being made routinely available to civil society, in whose name such debts are arranged. As with oil revenues, ordinary citizens cannot know whether such loans are appropriate and are therefore unable to hold their government to account over the use of credit facilities.

The voluntary Wolfsberg Principles, created by 11 leading banks and the anti-corruption NGO Transparency International, seek to deny the use of banking services for 'criminal purposes'. Each signatory bank will 'endeavour to accept only those clients whose source of wealth and funds can be reasonably established to be legitimate'.[9] This could easily and effectively be extended to cover disclosure of resource-backed loans. At the moment, several Wolfsberg signatories, including ABN Amro, Citibank and Société Générale, lend money to Angola for purposes unknown. More broadly, the issue of loan disclosure needs to be factored into future 'know-your-customer' requirements by banks.

G8 and the UK Extractive Industry Transparency Initiative (EITI)

The declaration of the G8 countries following their meeting in Evian on 1-3 June 2003 supports an intensified approach to revenue transparency. The G8 members made a commitment to:

- Encourage governments and both private and state-owned companies to disclose their revenue flows and payments;
- Work with participating governments to achieve high standards of transparent public revenue management, including the processes for awarding contracts and concessions;
- Provide capacity-building support where this is needed;
- Encourage the IMF and World Bank to give necessary technical support.

The most significant follow-up so far has been the UK's Extractive Industry Transparency Initiative (EITI). UK Prime Minister Tony Blair deserves significant praise for his leadership in bringing together representatives of industry, civil society and government to discuss the topic and to launch a framework for enhanced revenue disclosure and oversight in June 2003.

At that meeting, a broad set of principles was agreed that 'underline the importance of transparency by governments and companies in the extractive industries', 'the principle and practice of accountability by government to all citizens for the stewardship of revenue streams and public expenditure' and the need for double-disclosure book-keeping to reconcile company figures with government accounts.[17]

Credit: Sven Torfinn/Panos Pictures

Conditional Development Assistance from Donor Governments and International Financial Institutions

The donor community already accepts the principle that it should promote good governance in recipient countries; the use of conditionality to promote transparency is a consistent and logical extension of this principle. For example, the US government's International Anti-Corruption and Good Governance Act, passed in 2000, amended the existing Foreign Assistance Act to add 'the promotion of good governance through combating corruption and improving transparency and accountability' to the list of major US foreign policy goals. The Bush Administration's Millennium Challenge Account initiative also placed good governance at the core of its fund disbursement criteria.

As for the European Union, its Cotonou Agreement with African, Caribbean and Pacific recipients of development assistance also recognises that fighting corruption is a fundamental element of future development assistance. Article 9(3) notes that good governance is the 'transparent and accountable management of human, natural, economic and financial resources for the purposes of equitable and sustainable development … Good governance … constitute[s] a fundamental element of this Agreement'.

Revenue transparency is perhaps the most basic measurable criterion of good governance in developing countries whose income is almost entirely reliant on resource extraction.

The World Bank and the IMF have a particularly important role to play in promoting revenue transparency because of their technical expertise and central role in macroeconomic restructuring. So far, their engagement has been sporadic and piecemeal.

The World Bank not only disburses development assistance directly but is also involved in direct investment in the extractive sector through the International Finance Corporation (IFC), a Bank subsidiary which partners with private investors. An internal evaluation of the World Bank's performance in January 2003 highlights the failure of its current approach. It states that due to the 'links between poverty and poor governance … increased EI [Extractive Industry] investment is likely to lead to bad development outcomes *for many if not most of the Bank's clients* [original emphasis]'.[10] The report calls for 'a fundamental reorientation of the Bank's work … away from prioritizing the attraction of new investment and toward capacity building and technical assistance focused on strengthening the government's capacity to maximize the benefits and minimize the risks of existing EI investment'.[11]

The World Bank could achieve this policy reorientation by mainstreaming a requirement for revenue transparency across all its engagements with countries where extractive industries are significant. In return for Bank technical assistance and structural adjustment loans for the oil, gas and mining sectors, or for macro-economic purposes, governments should be obliged to mandate the disclosure of receipts from oil and mining by state agencies and the disclosure of all such payments to the state by extractive companies. The IFC and the Multilateral Investment Guarantee Agency (MIGA), a Bank unit which guarantees investment against political risks, should also require that all companies receiving their support should publish their payments to states.

Multiple reports by the World Bank's own consultative bodies are now calling on it to show leadership on revenue transparency. The Extractive Industries Review (EIR), a two-year multi-stakeholder consultation by the Bank that completed its final report at the end of 2003, states that 'the WBG [World Bank Group] should vigorously pursue transparency at country and company level in all the resource-rich countries it works with. The WBG should partner with, for instance, the Extractive Industries Transparency Initiative and Publish What You Pay to promote revenue transparency in its client countries and should use its power as a convenor to vigorously support existing efforts to build common action against corruption. WBG requirements need to be in line with these initiatives.'[12] A July 2003 report of the World Bank's own Operations Evaluation Department entitled 'Extractive Industries and Sustainable Development' made very similar suggestions.[13]

So far, however, conditionality for revenue transparency by the World Bank has been patchy and inconsistent. Although the World Bank made disclosure and auditing of revenues from the Chad-Cameroon oil pipeline a condition for its support for the project, it failed to apply such conditionality to the signature bonuses paid by participating companies. In addition, the World Bank's showpiece disclosure agreement with the Chad government comes up for renegotiation at the same time as the first significant revenues will be flowing back from the pipeline. Similarly, although an independent panel was set up to oversee the disbursement of revenues, the panel currently lacks the capacity to fulfil its mandate.[14]

Similarly, a 2002 World Bank and IMF Review of their National Poverty Reduction Strategies concluded that transparency within countries and international development partnerships is critical if efforts to reduce poverty are to succeed.[15] Despite this, both the IMF's Oil Diagnostic revenue tracking exercise with the Angolan government has not led to any results being published. Nor despite a commitment from the government, has the IMF/World Bank audit of oil revenues in Congo Brazzaville.[16]

A further problem, highlighted by Global Witness discussions with World Bank officials during 2003, is that some of the latter currently appear to favour 'aggregated disclosure' by extractive companies. This model envisages that companies operating in a given country would not individually publish their payments to the state, but give the data to a third party (such as the World Bank itself) which would then publish the total for all companies as an aggregated figure.

There is no inherent problem with a third party auditing revenue data from companies and state agencies after they has been published, so that any inconsistencies can be reconciled, as long as the process done out in the open. But if the data from companies are aggregated in secret and then only published as a single total figure, the result would be a watered-down form of transparency which will lack credibility because civil society is obliged to trust the word of the aggregator rather than being able to assess the data for itself. Any third parties involved in collating or checking the data should be supporting the efforts of civil society to monitor the flow of revenues, not substituting for them.

It is not clear why the World Bank might want to endorse this form of 'aggregated disclosure', which falls short of the principle adopted in the industrialised countries, where key information is disclosed by individual companies. It is not clear on whom the duty of aggregation would fall, and aggregated disclosure would negate one of the biggest benefits of revenue transparency for the extractive industries themselves, which is that individual companies can demonstrate that they are making a contribution to society by pointing to their revenue and tax payments.

The only obvious beneficiaries of aggregation would be oil and mining companies, who would therefore be relieved of the need to reveal the contract terms they have struck with different countries, which may vary considerably, or global tax minimisation arrangements which may be legal but controversial.

The generally piecemeal and unsystematic approach of the World Bank and IMF to date would seem to undermine the IMF's efforts to promote a code of good practice on fiscal transparency more widely amongst its members. Unless donor governments and the international financial institutions commit themselves to mainstreaming a requirement for revenue transparency across all their lending, development and technical assistance programmes, they will inevitably fail to address the underlying reasons for poverty and macroeconomic mismanagement in resource-rich-but-poor countries. Instead, they will simply perpetuate a vicious circle of using the money of Northern taxpayers to cover up some of the symptoms.

The Chad-Cameroon pipeline: a first step towards transparency, but flaws remain. Credit: AFP/Getty Images

The Initiative has categorised the main revenue streams from resource extraction and developed the necessary templates for data collection. It has also shown that reporting such flows is neither burdensome nor difficult and identified a number of pilot countries willing to begin the process of transparent reporting. The list of possible pilot countries currently includes Ghana, Georgia, Azerbaijan, Trinidad and Tobago and Timor Leste (East Timor). Nigeria is planning a transparency initiative which draws on elements of the EITI while tiny Sao Tome and Principe, where oil exploration is about to begin, is at the early stages of an EITI-inspired transparency project.

The UK government's follow-up strategy in the six months following the June EITI meetings has been erratic. For example, Timor Leste has not been secured as a pilot country for transparency even though Prime Minister Mari Alkatiri himself attended the EITI meeting for the whole day. The country that has promised the boldest action on transparency, Nigeria, has actually gone some way beyond the cautious approach adopted to the EITI, and these changes are being driven by the Nigerian government itself, with input from the World Bank, rather by than the UK.

There are a number of problems that threaten to undermine EITI's effectiveness.

Problem number 1. Lack of outreach and under-resourcing

The primary responsibility for implementing the EITI until now has lain with the UK Department for International Development (DFID), but early signs indicated that despite EITI's status as a DFID priority, the Initiative was given neither the political support nor the resources it needed. The head of the DFID team working on EITI left after the inaugural conference in June 2003 and was not replaced until December: until recently, the DFID team had only two full-time staff. This weak start has not gone unnoticed in countries like the US, where there has been scepticism about EITI, and in countries like Angola where transparency problems are greatest.

In a positive recent development, the extractive industries team at DFID was bolstered to six full-time officials, with others providing input, and the team has begun working with pilot countries. DFID's capacity to run the EITI on its own remains limited however: although the endorsement of the World Bank for EITI in late 2003 offers the prospect of greater resources, there is still clearly a need for significant improvements in capacity and communications. There is growing frustration from parts of industry and the investment community that are sympathetic to transparency, as well as from civil society, about the lack of progress to date.

Problem number 2. EITI is a purely voluntary process

The second flaw in the EITI approach (and that taken by the G8) is that they have emphasised a purely voluntary approach to publication of information. Companies have agreed to publish their figures if and when a host government gives them permission. The problem with this approach is that the necessary commitment to openness will simply not materialise where political and business elites have a vested interest in maintaining their cash supply. This means that the Initiative will not work in those countries where transparency is most needed! (See box: 'The Dangers of Voluntarism'). Indeed, experience of voluntary audit arrangements in Angola and Congo Brazzaville demonstrate that this approach to publication is not viable.

Problem number 3. No individual company disclosure

Insidious ideas, such as 'aggregated disclosure' of payments from more than one company, have also crept into the proposed standards. As noted earlier, this means that companies will not commit themselves to an individual declaration of their revenue streams but will pool their data with other companies to release an aggregate national figure. Whilst it is important to protect commercially confidential information, the commitment to publish only highly

Credit: Robert Grossman/Africaphotos.com aggregated data, rather than with company-by-company detail, runs counter to the philosophy of transparency underlying the initiative. As individual company disclosure is the accepted standard in every developed country, this approach also threatens to engineer a deliberate discrepancy in corporate behaviour between North and South. Additionally, one of the central benefits of disclosure, which is that a company improves its social licence to operate by indicating the contribution it makes to government finances, is lost.

The adoption of aggregation, like voluntary disclosure, appears to reflect pressure on DFID by parts of the oil industry, notably in the US. It is not clear why some companies favour this approach: one possible reason is that aggregated disclosure would conceal the various legal but controversial methods that Big Oil uses to minimise its tax payment obligations. The Equatorial Guinea section of this report noted the potential for companies to use complex accounting to minimise their payments to countries which desperately need the money. The Equatoguinean government's almost complete lack of capacity to monitor the oil industry resulted in significant underpayments that were only corrected when the World Bank intervened. Such events are a clear argument for the need to maximise transparency from individual companies.

Problem number 4. Ambiguous drafting

References to 'respect for contracts' in the EITI and 'contract sanctity' in the G8 resolution may be abused. The extreme secrecy clauses built into many contracts between companies and states could be used to block complete disclosure and lead to both sides claiming to have complied with the principles of the initiative whilst actually disclosing only small proportions of total revenues.

Part of the reason for such dubious wording is that ExxonMobil and other US companies claimed that if the EITI established any clear international standard over extractive revenue management then they might be sued for non-perfomance under an arcane piece of US legislation called the 'Alien Tort Claims Act' (ACTA). The Act was written in 1789 but has more recently been used to seek damages in US courts for possible corporate complicity in human rights abuses that violate the 'law of nations'. Since the EITI will not be part of the law of nations, but a voluntary initiative that is predicated on permission to disclose being granted by host governments, it seems disingenuous to cite this law as the basis for possible liability.[18] However, the fact that companies feel so exposed because they may sign a set of principles but not be allowed to disclose by a particular government is itself a clear argument for regulations to require disclosure to all national governments.

Buy-in on transparency?

In the wake of the EITI's launch, there has been significant progress towards transparency in three countries, Nigeria, Ghana and Iraq.

President Obasanjo of **Nigeria** pledged on 7 November 2003 that his country would openly publish all its revenues from the oil industry and would require oil companies operating in the country to individually disclose their payments. This welcome step, coming from a country long dogged by massive oil-related corruption, will be extremely positive when put into practice. Obasanjo explicitly stated his support for the EITI principles, while noting that the reporting templates developed by the EITI would need to be adapted to Nigerian conditions, and he also endorsed the model of disclosure supported by the Publish What You Pay NGO coalition. It is particularly significant as an example to other countries that Nigeria has committed itself to go beyond the problematic 'aggregated disclosure' model currently favoured by the EITI to the much more effective, comprehensive and transparent model of individual company disclosure.[19]

The Minerals Commission in **Ghana** provided, for the first time, detailed information on production data, government revenues and company receipts from its mining sector in September 2003 to national newspapers. This action is clearly a step in the right direction, although companies have not been required to publish what their payments directly, nor has civil society been fully involved in the process. However, current indications are that further movement towards transparency has become bogged down, for reasons that are unclear. Ghana should be given credit for what it has done so far, and its status as the first mover in the EITI process should be recognised, while being encouraged to move further.

Iraq is in an anomalous position following the US-led invasion in mid-2003, in that it is jointly governed by the American-controlled Coalition Provisional Authority (CPA) and a council of Iraqi leaders. The US legislature approved an Appropriations Bill for Iraq and Afghanistan in late 2003 which, amongst other things, provided almost $19 billion for spending on Iraq's development. An important provision in this Bill, which became law in November 2003, requires that the CPA report monthly on the volume of Iraqi oil production, the value of revenue derived from it and the use of such revenue. These data have to be published on the CPA's website in Arabic and English. But although some data on public revenues and spending are now on the website, the CPA does not yet appear to have complied with this specific requirement of the law.

This measure is clearly in the interests of the CPA, as well as the Iraqi people, since it should help (if properly implemented) to forestall the widespread suspicion in Iraq that the US military presence is intended to control the country's oil. Iraq is in a state of political transition which is intended to lead in the near future to an all-Iraqi, democratically elected government. It is to be hoped that the provisions on revenue transparency mandated for the CPA will also be adopted by a future Iraqi government. Given the misuse of oil revenues in the past to support the murderous dictatorship of Saddam Hussein, there is a clear and pressing need for revenue transparency in Iraq, as part of a system of accountable government.

Unsurprisingly, all the countries featured in the case studies of this report have been absent from meaningful participation in the EITI. Angola even invented the bizarre category of 'observer' for itself. But endorsing the EITI will not be enough in itself: a country like Angola, with a long record of oil-related corruption, should not be allowed to sign up to the Initiative unless it makes a meaningful commitment to open its books. There is a risk that endorsing EITI could simply become a figleaf for countries or companies who actually want to deflect pressure for real change.

The US, which could play a central role in EITI, has, at best, remained ambivalent towards it and, at worst, has tried to sideline the Initiative into much larger and more diffuse pieces of work. In the end, it appears that the US decided it was better to water down the initiative from the inside, and sent a series of minor State Department functionaries to the EITI meetings to issue lukewarm endorsements. Do US diplomats fear that the Bush Administration's paramount foreign-policy objective of energy security might be hindered by too much focus on good governance and accountable use of oil and mining revenues? If so, this would be a remarkably short-sighted and unimaginative approach to the transparency issue, since the ultimate guarantors of a secure energy supply are stable and well-governed producing states.

More recently, Secretary of State Colin Powell has made forthright statements about the need for transparency in the extractive industries. He stated in February 2004, to a question about corruption and US companies in Nigeria: 'We don't want to see any of our countries (sic) cheated by a country in which they're investing. And we don't want to see any of our companies take advantage of a government of a country in which they are invested or located. We want to see no corruption and total transparency, not only for the government, but for our companies as well.'[20] The US now needs to act on this principle and act on the EITI.

Overall, the EITI is a move forwards on the issue of transparency in that the principle of disclosure was clearly recognised by all the participants, but there now needs to be much more rigorous and effective action towards implementing its principles by participating governments and companies. The UK government, as the driving force behind EITI, has a particular responsibility to push for change. Its current reliance on voluntary disclosure alone is not sufficient to promote transparency in those countries where it is most desperately needed. A voluntary approach to transparency would not be universally adopted, and does not address the magnitude of the problem given that the missing money involved may literally mean life or death for the poor and vulnerable in some countries. The EITI therefore needs to reopen the debate on mandatory measures to promote transparency.

Citizens of countries like Equatorial Guinea are still waiting for prosperity.

Credit: Channel Four News

Conclusion:
Towards a joined-up approach to revenue transparency

The goal of revenue transparency is fully consistent with the international objectives of accountable government, corruption prevention and democratic debate about issues of resource management. Businesses will benefit too. Requiring transparency would have the effect of protecting companies from allegations of complicity with corrupt governmental practices and of providing a level playing field for competitors. Finally, revenue transparency is a vital first step towards alleviating the crushing poverty of the ordinary citizens in many resource-rich developing countries.

Transparency is in the best interests of almost everyone concerned – citizens, companies, donor governments and the wider international community – except a corrupt elite grown fat from the systematic misappropriation of state assets.

The ordinary citizens of resource-rich countries are the real owners of those resources and yet they lack even basic information to call their governments to account over the management of resource revenues. Multinational businesses do not benefit from having to compete on the size of kickbacks rather than technical merit, nor do they gain when their legitimate payments to governments end up funding social division. But, if they try to do anything about it on their own, they face retaliation from vested interests and the threat of having their operations assigned to less scrupulous competitors, as BP discovered to its cost in Angola. Meanwhile, Northern taxpayers currently subsidise the failure of resource-rich states in the South to provide properly for their own citizens. The international community faces instability and an unsustainable operating environment that threatens security of resource flows.

It is the intransigence of the corrupt few that makes the current purely voluntary approach of the EITI, while a good first step, an insufficient basis for real change where that change is most needed.

Revenue transparency is not an unwarranted imposition of the North on the South. Article 1 of UN General Assembly Resolution No. 1803, 'Permanent Sovereignty Over Natural Resources', states very clearly that 'the right of peoples and nations to permanent sovereignty over their natural wealth and resources must be exercised in the interest of *their national development* and of *the well-being of the State concerned*' [emphasis added]. People cannot have sovereignty over their resources if they are not privy to the deals made to exploit those resources. Assisting the transparency of revenues through promoting a strategy of double-disclosure bookkeeping is in keeping with the spirit and intent of this resolution.

If anything, companies are cynical in their use of opaque accounts in the developing world when they play by different rules in the North, where disclosure in the marketplace has been legislated for decades. The landmark 1933 US Securities Act was designed to help the market recover from the lack of transparency and accountability that had helped create the conditions of the 1920s stock market bubble and the subsequent Great Depression. Legal scholar and future Supreme Court Justice Felix Frankfurter identified the power of public scrutiny to this end: 'The Securities Act is strong insofar as publicity is potent; it is weak insofar as publicity is not enough…The existence of bonuses, excessive commissions and salaries, of preferential lists and the like, may all be open secrets among the knowing, but the knowing are few. There is a shrinking quality to such transactions; to force the knowledge of them into the open is largely to restrain their happening. Many practices safely pursued in private lose their justification in public.'

Requiring revenue transparency from multinational resource extraction companies is a logical extension of existing policy instruments such as anti-corruption 'books and records' rules, stockmarket listing requirements, and national and international accountancy standards.

Finally, transparency is a necessary condition of good governance, and should be recognised as such by international finance institutions when they allocate taxpayers' money. Aid disbursement and investment in extractive industry projects should take place only within a coherent policy framework that makes such investments consistent with poverty reduction and development goals.

It is time for national governments to come clean on their income from natural resources and for the international community to require revenue transparency from those extracting resource revenues. Transparency will not eliminate corruption overnight in resource-rich-but-poor countries but, without it, we do not stand a chance.

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Oil installations in Equatorial Guinea. Credit: Robert Grossman/Africaphotos.com global witness

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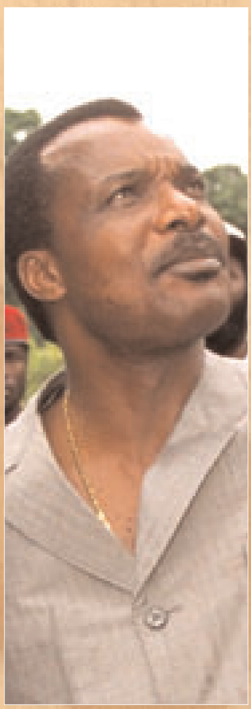
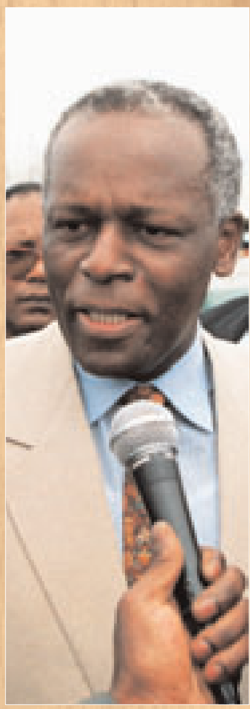
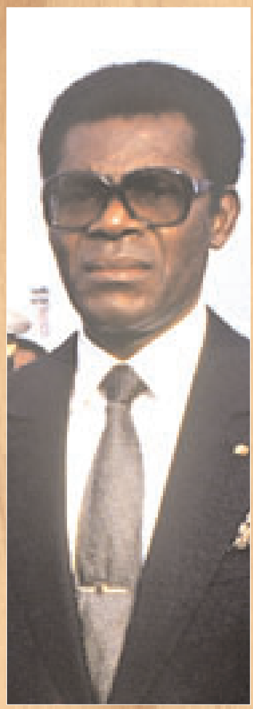


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