

Report for Congress

Received through the CRS Web

Iraq: Oil-For-Food Program, International Sanctions, and Illicit Trade

Updated September 26, 2002

Kenneth Katzman
Specialist in Middle East Affairs
Foreign Affairs, Defense, and Trade Division

Iraq: Oil-For-Food Program, International Sanctions, and Illicit Trade

Summary

The “oil-for-food” program is the centerpiece of the long-standing U.N. Security Council effort to alleviate human suffering in Iraq while maintaining key elements of the Gulf war-related sanctions regime. In order to ensure that Iraq remains contained and that only humanitarian needs are served by the program, U.N. Security Council resolutions have mandated substantial controls on Iraqi oil exports and humanitarian imports. All Iraqi oil revenues earned under the program are held in a U.N.-controlled escrow account and cannot be accessed by the Iraqi government.

During the first five years of the program’s operations (1996-2001), there was a consensus among observers that the program had eased, but not eliminated, human suffering in Iraq. Concerns about the program’s difficulties prompted criticism of the United States; critics asserted that the U.S. strategy was to maintain sanctions on Iraq indefinitely as a means of weakening Saddam Husayn’s grip on power. At the same time, growing regional and international sympathy for the Iraqi people resulted in a pronounced relaxation of regional enforcement — or even open defiance — of the Iraq sanctions. The United States argued that continued sanctions were critical to preventing Iraq from acquiring equipment that could be used to reconstitute banned weapons of mass destruction (WMD) programs.

Seeking to improve international unity on containment of Iraq, the Bush Administration devised a “smart sanctions” plan that it said would speed the flow of civilian goods to Iraq and thereby improve living conditions for the Iraqi people. The U.S. plan offered to significantly ease restrictions on exportation of purely civilian goods to Iraq in exchange for greater international and regional cooperation to prevent any arms or weapons-related technology from reaching Iraq. The U.S. plan also sought to prevent the Iraqi government from receiving the proceeds of illicit oil sales to Iraq’s neighbors. The U.S. proposals appeared to move away from post-Gulf war linkages between sanctions easing and full Iraqi cooperation with U.N. inspections of Iraq’s WMD capabilities.

In reaction to the U.S. plan, France, Russia, and China, which are permanent members of the U.N. Security Council, pressed instead for a much broader easing of sanctions on Iraq. Regional governments refused to agree to any changes that would restrict their trade with Iraq, illicit or otherwise. After a few rounds of negotiations on the U.S. plan, the Security Council adopted (Security Council Resolution 1409, May 14, 2002) the portion of the U.S. plan that facilitates civilian exports to Iraq. Regional resistance scuttled the aspects of the plan that would have curbed Iraq’s illicit trade with its neighbors.

Contents

Background and Structure of the	
Oil-For-Food Program	1
Program Operations	2
Changes Outlined in Resolution 1284	4
Benefits of the Program	5
Food	8
Health and Sanitation	8
Education	8
Continuing Debate Over Sanctions	9
The “Smart Sanctions” Plan	9
Other Sources of Humanitarian Aid	11
Illicit Trade	12
Jordan	13
Iran/Persian Gulf	13
Syria/Military Technology Exports to Iraq	13
Turkey	14
Oil Sales Surcharges	14
Oil Exploration Contracts	15
Flights to Iraq	15
Appendix: Overview of U.S. Regulations Governing	
U.S. Participation in the Oil-for-Food Program	17

Iraq: Oil-For-Food Program, International Sanctions, and Illicit Trade

Background and Structure of the Oil-For-Food Program

The “oil-for-food” program reflects a longstanding U.N. Security Council effort to alleviate human suffering in Iraq while pressing Iraq to comply with all relevant U.N. Security Council resolutions.¹ The program represents a temporary and limited exception to the comprehensive international trade embargo imposed on Iraq by U.N. Security Council Resolution 661 (August 9, 1990) as a consequence of its invasion of Kuwait. U.N. Security Council Resolution 687 (April 3, 1991) provided for the international embargo on Iraq’s exportation of oil² to end once Iraq had fully complied with U.N. efforts to end its weapons of mass destruction (WMD) programs. The WMD inspections began in April 1991 but proceeded more slowly than expected, and an end to sanctions did not appear to be in sight by April 1991. Without oil export revenues, Iraq was unable to import sufficient quantities of food and medical supplies, and, according to virtually all accepted indicators (infant and child mortality, caloric intake, and other indicators), living conditions deteriorated sharply during 1991-1995.

The first version of an oil-for-food plan would have allowed Iraq to export \$1.6 billion in oil every six months. It was adopted by the Council in 1991 in Resolutions 706 (August 15, 1991) and 712 (an implementing plan adopted September 19, 1991), but Iraq rejected it as too limited in scope and an infringement on Iraq’s sovereignty. There was little movement on the issue during 1991-95, despite dramatic declines in Iraq’s living standards. On April 15, 1995, the Council adopted Resolution 986, which took into account one of Iraq’s concerns by allowing the export of \$2 billion in oil every six months. Iraq and the United Nations signed a memorandum of understanding on the program on May 20, 1996 (document number S/1996/356) and, after several more months of negotiations on details, the first Iraqi oil exports began on December 10, 1996. After the first year of the program, the Secretary General determined that the program was not meeting the food and medical needs of the Iraqi people, and Resolution 1153 (February 20, 1998) raised the oil export ceiling to \$5.256 billion per 6-month phase. In an effort to provide Iraq an incentive to cooperate with a new program of U.N. weapons of mass destruction (WMD) inspections, the U.N. Security Council, in Resolution 1284 (December 17, 1999),

¹For a further discussion of Security Council resolutions and requirements on Iraq, see CRS Issue Brief IB92117, *Iraq: Compliance, Sanctions, and U.S. Policy*.

²That embargo was imposed by U.N. Security Council Resolution 661 of August 6, 1990.

abolished the export limit. This resolution had a number of additional provisions and implications for the oil-for-food program, as discussed below.

Program Operations

In order to ensure that only humanitarian objectives are served by the program, the oil-for-food program places substantial controls on Iraqi oil exports and humanitarian imports. Iraq's state-owned oil marketing company (State Oil Marketing Organization, SOMO) negotiates with international oil companies to sell Iraqi oil. Oil purchase contracts are reviewed by a panel of oil contract overseers reporting to the U.N. Sanctions Committee,³ which administers the implementation of sanctions on Iraq. The oil overseers review Iraq's pricing proposals monthly. Iraq is only allowed to export oil under the program, not any other products.

The oil sold is exported through an Iraq-Turkey pipeline and from Iraq's terminals in the Persian Gulf. According to Resolution 986, "the larger share" of oil exports must run through the Turkish route. The proceeds from these sales are deposited directly, by the oil purchasers, into a U.N.-monitored escrow account held at the New York branch of France's Banque Nationale de Paris (BNP). Iraq's oil exports are monitored at the point of exportation by personnel from Saybolt Nederland BV, an energy services firm working under contract to the program.

In each six-month phase of the program, Iraq purchases goods and services directly from supplier firms, in accordance with an agreed distribution plan allocating anticipated revenues among categories of goods to be purchased in that phase. Prior to the major amendment to the program approved in May 2002, which is discussed later, the Sanctions Committee reviewed and had authority to approve contracts for the export of goods to Iraq. The Committee operates by consensus. Any Sanctions Committee member could place a "hold" on a contract for goods to be imported by Iraq, and the United States often placed holds on exports of dual use items (civilian items that could have military applications). In deciding whether or not to place a hold on a contract, the U.S. representative on the Sanctions Committee consulted with agencies of the U.S. government to determine whether Iraq could use the requested items for military purposes.

Under the new procedures adopted in Security Council Resolution 1409 (May 14, 2002) and placed into effect in July 2002, the U.N. weapons inspection unit (UNMOVIC, U.N. Monitoring, Verification, and Inspection Commission) reviews export contracts to ensure that they contain no items on a designated list of dual use items known as the Goods Review List (GRL).⁴ If so, the Sanctions Committee then decides whether or not to approve that portion of the contract containing the GRL items in question.

³The Sanctions Committee, set up by Resolution 661, consists of representatives of the member states on the U.N. Security Council.

⁴The Goods Review List is contained in U.N. document S/2002/515 of May 3, 2002. It can be found online at the U.N. oil-for-food program website, [<http://www.un.org/depts/oip>].

Under U.S. regulations written for the program, U.S. firms can buy Iraqi oil and sell goods to Iraq, including oil industry spare parts and equipment. Over the past few years, purchases of Iraqi oil by U.S. firms have ranged between one-third to nearly one-half of Iraq's normal export volume of about 2.1 million barrels per day. (See appendix for an overview of U.S. regulations governing U.S. firms' participation in the program.)

Once a contract is approved, BNP uses the funds deposited in the escrow account to pay letters of credit for the purchased goods. The arriving supplies are monitored at their point of entry into Iraq by about 50 personnel from the Swiss firm Cotecna⁵ at four approved border crossings — Umm Qasr on the Persian Gulf; Trebil on the Iraqi-Jordanian border; Walid on the Iraqi-Syrian border; and Zakho on the Iraqi-Turkish border. In Baghdad-controlled Iraq, the Iraqi government distributes imports to the population through a government rationing system, and distribution is monitored by about 158 U.N. workers from the World Food Program, the Food and Agriculture Organization, the World Health Organization, and UNICEF. The U.N. personnel visit ration centers, marketplaces, warehouses, and other installations to ensure that distribution is equitable and accords with the targeted allocation plans submitted by Iraq for each six month phase. In Kurdish-controlled Iraq, about 65 U.N. workers, accompanied by about 130 U.N. security guards, perform the distribution function. Some goods bound for the Kurdish-controlled areas are combined with Baghdad's purchases in order to obtain more favorable prices in bulk.

Under Security Council Resolution 1051 (March 27, 1996), exports to Iraq of dual use items are supposed to be monitored by U.N. weapons inspectors at their point of entry and site of end use in Iraq. This import monitoring mechanism was altered after the previous inspection regime (U.N. Special Commission, UNSCOM) left Iraq in December 1998 just prior to the U.S./British airstrike campaign against Iraq (Operation Desert Fox, December 16-19). Security Council Resolution 1284 (December 17, 1999) replaced UNSCOM with UNMOVIC, but Iraq has not allowed UNMOVIC into Iraq. In the absence of inspectors inside Iraq, end use monitoring is performed by some of the 158 U.N. employees who monitor the distribution of civilian goods coming into Iraq. However, these monitors are not trained weapons inspectors, and this has caused the United States and Britain to closely scrutinize, and to place many holds on, exports of dual use items to Iraq.

The oil-for-food program attempts to help Iraq meet its international obligations and ensure equitable distribution of imports to the Iraqi people. The revenues from Iraq's oil sales are distributed as follows:

- ! 25% is transferred to a U.N. Compensation Commission (UNCC) to pay reparations to victims of Iraq's invasion of Kuwait. As provided for in Security Council Resolution 1284 (see below), the deduction percentage fell to 25% from its previous level of 30% at the commencement of phase nine of the oil-for-food program (December 6, 2000).

⁵Cotecna replaced Lloyd's Register as point-of-entry monitoring contractor on February 1, 1999.

- ! 59% is used to purchase humanitarian items for Baghdad-controlled Iraq. This account was increased from its previous level of 53% when the reparations deduction was reduced in December 2000.
- ! 13% is used to purchase supplies in the three Kurdish-inhabited provinces of northern Iraq.
- ! 3%, the remaining amount, pays for U.N. costs to administer the oil-for-food program, as well as UNMOVIC's operating costs.

Changes Outlined in Resolution 1284. U.N. Security Council Resolution 1284, adopted December 17, 1999,⁶ was intended in part to improve the provision of relief for the Iraqi people and to offer Iraq an incentive to readmit U.N. weapons inspectors. The following highlights key provisions of it and related decisions:

- ! As noted previously, Resolution 1284 eliminated the limit on the amount of oil Iraq could export, in order to enable Iraq to generate more revenues for humanitarian purchases. All proceeds from the oil sales must still be deposited in the U.N.-supervised escrow account.
- ! Resolution 1284 began the process, continued in subsequent oil-for-food program rollover resolutions, of easing restrictions on the flow of civilian goods to Iraq. The resolution directed the Sanctions Committee to draw up lists of items, in several categories, that would no longer be subject to Sanctions Committee review, and therefore would not be vulnerable to "holds." The accelerated approval procedures for foodstuffs and educational goods began on March 1, 2000, and continued with pharmaceuticals, medical supplies, medical equipment, and agricultural equipment (March 29, 2000). Subsequent oil-for-food rollover resolutions made eligible for the new procedures water treatment and sanitation supplies (August 11, 2000) goods for the housing sector (February 26, 2001) and electricity supplies (May 24, 2001).
- ! Resolution 1284 laid the groundwork for foreign investment to explore for and produce oil in Iraq, although the resolution made this investment contingent on full Iraqi cooperation with UNMOVIC. Since late 2000, the Sanctions Committee has approved drilling in existing fields by two Russian firms (Tatneft and Slavneft) and a Turkish firm (Turkish Petroleum Company), but exploration of new fields is not permitted.
- ! Resolution 1284 created incentives for Iraq to cooperate with UNMOVIC by "express[ing] the intention," if Iraq is deemed to have "cooperated in all respects" with UNMOVIC, to suspend export and import sanctions for 120 days, renewable by Security Council. The Resolution implies that the Security Council would have to vote to implement the sanctions suspension. Under the resolution, UNMOVIC would use its first 60-day period inside Iraq setting a

⁶For full text of Resolution 1284, see [<http://www.un.org/Docs/scrses/1999/99sc1284.htm>].

new baseline for inspections and developing a work-plan for what remains to be done in order to be able to certify that Iraq is free of WMD. If sanctions were suspended, Iraq would once again be allowed to control its own revenues, although subject to strict but unspecified financial controls, according to the resolution. Arms exports to Iraq would still be banned and exports of dual use items would still be subject to scrutiny by the Sanctions Committee.

- ! Resolution 1284 also made some oil industry spare parts eligible for a streamlined approval process — contracts for such equipment are scrutinized by the same Sanctions Committee panel of oil overseers that review Iraq's oil sales contracts, without requiring full Sanctions Committee review. U.N. Security Council Resolution 1293 (March 31, 2000) increased to \$600 million, from \$300 million, the value of oil industry spare parts that Iraq could import per oil-for-food phase. This decision was taken in response to recommendations by the U.N. Secretary General that improving the humanitarian situation was contingent on the rehabilitation of Iraq's ability to export its oil.

Benefits of the Program

There is a consensus among U.N. officials and outside observers that the oil for food program has eased substantially, but not eliminated, human suffering in Iraq. The program, as well as some economic liberalization measures and illicit activity outside the program (discussed below), enabled Iraq to achieve 15% economic growth during 2000, according to the CIA's "World Factbook: 2001."

Few observers question that the program has made vast amounts of funds available for the purchase of food, medicine, and essential civilian goods. Table 1, supplied by the United Nations' Office of the Iraq Program, shows that higher oil prices, coupled with program modifications, have enabled Iraq to generate substantial revenues to fund imports. At times since the program began operations in December 1996, Iraq has generated more oil revenue than it did before the U.N. embargo was imposed in 1990 (about \$12.5 billion in *total* exports was generated in 1988), although substantial deductions are taken to pay the cost of implementing the program and for reparations payments. During 2000 (phases seven and eight), Iraq generated a total of about \$17 billion in oil revenues.

From inception until September 6, 2002, the program has generated over \$56 billion in revenues. During that same period of time, contracts for exports to Iraq of civilian goods worth \$37 billion have been approved, with goods worth \$24.3 billion having been delivered.

As noted in the table below, Iraq's sales of oil have run significantly below capacity since early 2001. The decrease is largely a result of disputes between Iraq and the United Nations over the formula for pricing Iraq's oil. Some members of the Sanctions Committee have sought to complicate Iraq's ability to impose surcharges on its oil buyer — such surcharges of about 30 - 50 cents per barrel constitute illicit revenue and are prohibited. In September 2001, to reduce Iraq's surcharging ability, the pricing formula was changed to "retroactive pricing," in which the oil is priced

after sale. This has significantly reduced Iraq's oil sales by about 25%, although the United Nations has noted a rebound to previous levels (about 2 million barrels per day) in September 2002. Iraq has sometimes unilaterally interrupted the sale of oil to protest Security Council policy or to challenge the United States and its allies. For example, Iraq suspended its oil sales for the month of April 2002 in protest against Israel's military incursion into the West Bank.

Table 1. Revenue Generated by Oil-For-Food Program
(through September 6, 2002)

Phase Number (each phase is six months)	Volume Sold (millions of barrels)	Value of Export (\$billion)	Average Price per Barrel (\$)
One December 10, 1996 - June 7, 1997 (\$2 billion export ceiling) ^a	120	2.15	17.92
Two June 8, 1997 - December 4, 1997	127	2.125	16.73
Three December 5, 1997 - May 29, 1998	182	2.085	11.46
Four May 30, 1998 - November 25, 1998 (Export ceiling raised to \$5.2 billion by Resolution 1153)	308	3.027	9.83
Five November 26, 1998 - May 24, 1999	360.8	3.947	10.94
Six May 26, 1999 - December 11, 1999	389.6	7.402	19.00
Seven December 12, 1999 - June 8, 2000 (Export ceiling lifted permanently by Resolution 1284)	343.4	8.302	24.13
Eight June 9, 2000 - December 5, 2000	375.7	9.564	25.50
Nine December 6, 2000 - July 3, 2001	293	5.638	19.24
Ten July 4, 2001 - November 30, 2001	300.2	5.35	17.82
Eleven December 1, 2001 - May 29, 2002	225.9	4.589	20.31
Twelve (a/o September 6, 2002) May 30, 2002 - November 25, 2002	91.7	2.233	24.35
Totals/Averages	3,117.3	56.412	18.10

Source: U.N. Office of the Iraq Programme.
[<http://www.un.org/Depts/oip/latest/basicfigures.html>].

a. Applicable U.N. Security Council resolutions allow Iraq to generate revenue, over and above the ceilings, to pay the costs of transit fees for exporting oil through Turkey, which explains why some figures might exceed stated ceilings.

The following represent the major accomplishments of the program in improving the living standards of the Iraqi people.

Food. In his November 19, 2001 report on the program, U.N. Secretary General Kofi Annan notes that, in Baghdad-controlled Iraq, the Iraqi government is now importing and distributing food sufficient to maintain about 90% of the U.N. target caloric intake of 2,463 kilocalories per person per day. The full ration was achieved only during December 2000. The report notes that few families can buy additional food, although the prices of foodstuffs in Iraq have remained relatively stable. A report by oil-for-food program head Benon Sevan, submitted September 25, 2002, said that “the steady pace of supply for most of the food basket continued.” The Secretary General’s report does not identify any food problems for the three Kurdish provinces, which is consistent with press reports that food has become relatively abundant there, sometimes to the detriment of local agricultural production.

Health and Sanitation. The Secretary General’s November 2001 report said that the increased distribution of health supplies and production and import of drugs have improved health services for patients, particularly in the areas of infectious diseases and heart disorders. The report also noted improvement in the diagnostic and other equipment in use in Iraq’s hospitals. In the related area of water and sanitation, the Secretary General’s report said that there has been some recent improvement because of the arrival of vehicles and purification chemicals and equipment to increase the production of potable water. Benon Sevan’s September 25, 2002 report said that U.N. observers were finding an overall decrease in the incidence of diseases such as cholera, measles, and meningitis.

In mid-1999, UNICEF released its first country wide survey of infant and maternal mortality in Iraq since 1991. The survey took a number of precautions to ensure that the survey results would not be altered or modified and UNICEF is confident that the survey information is accurate. It showed that infant mortality in the southern and central sections of Iraq (under the control of the Iraqi government) rose from 47.1 deaths per thousand live births during 1984-1989 to 107.9 deaths per thousand during 1994-1999. The under five-year-old mortality rate rose from 56 to 130.6 per thousand live births in the same time period. According to the report, this increase in mortality resulted in about 500,000 more deaths among children under five than would have been the case if child mortality trends noted prior to 1990 (imposition of sanctions) had continued. In the northern part of Iraq (currently under the protection of the international community) the mortality rate has declined over the same period: infant mortality dropped from 63.9 per thousand live births in 1984-1989 to 58.7 in 1994-1999 and under five-year-old mortality dropped from 80.2 per thousand live births to 71.8 per thousand.

Education. The Secretary General’s November 2001 report identifies significant shortages of materials and equipment throughout the education sector. According to an earlier report (September 8, 2000), Iraq’s literacy rate (53.7% of adults and 70.7% of the youth) “has remained fixed for a number of years.”

Continuing Debate Over Sanctions

Even though most observers agree that the oil-for-food program has improved living conditions in Iraq substantially, debates have continued over how to improve the effectiveness of the program and over whether and how to ease international sanctions on Iraq. The United States and Britain have tended to place most of the blame for the program's shortcomings on Iraq, alleging that the Iraqi regime disregards the needs of its people. U.N. administrators of the program criticize Iraq on similar grounds, but they also attributed program deficiencies to U.S. and British policy, which they allege slows or halts the flow of infrastructure equipment that is required to realize the program's benefits.

The issue of contract holds on infrastructure equipment has been one of the most contentious that the United Nations has faced. Past U.N. reports on the program claim that infrastructure equipment, such as trucks, communications gear, forklifts, electricity, and water treatment equipment, are crucial to the timely distribution and proper storage and functioning of foodstuffs and medical products. At the time of the adoption in May 2002 of aspects of the "smart sanctions" plan discussed below, the United States had placed almost \$5 billion of goods on hold.

In response to international criticism of the holds, the United States asserted that 90% of all contracts were approved and that the holds had minimal impact. The United States maintained that all contracts needed to be scrutinized to ensure that no equipment would be used to rebuild WMD programs, especially because U.N. weapons inspectors are not in Iraq to monitor dual use exports that are shipped there. U.S. officials say they want to ensure that no contract is being awarded solely to encourage political support for Iraq from parent governments and that all contracts submitted for review must provide required technical specifications.

U.N. reports discuss the impact of the holds on the humanitarian situation, but some also cite Iraq for often failing to follow U.N. procurement recommendations and for failing to efficiently distribute program imports, particularly medicine and medical equipment. The Secretary General's May 18, 2001 report criticizes Iraq for failing to submit purchase applications for health, education, and water treatment supplies, as well as energy equipment for phase nine. U.N. reports do not accuse Iraq of purposely diverting imports from the program to the military or regime supporters, although some U.S. reports, such as a February 28, 1998 State Department fact sheet, say Iraq has diverted other food stocks to these elements. The November 2001 report was somewhat less critical of Iraqi procurement practices than were past reports.

Some of the fault appears to lie with factors outside the control of any particular party. The Secretary General's September 8, 2000 report attributes the decline of the health sector, in part, to the departure from Iraq of foreign and Iraqi health professionals.

The "Smart Sanctions" Plan. With no permanent end to international sanctions in sight due to the lack of U.N. weapons inspections, the debate over further modifications to the oil-for-food program has remained the centerpiece of a broader debate over Iraq sanctions. This debate intensified in May and June 2001

when the five permanent members of the U.N. Security Council attempted to incorporate into an oil-for-food rollover a U.S. plan to implement “smart sanctions” on Iraq. The smart sanctions plan represented an effort, articulated primarily by Secretary of State Colin Powell at the beginning of the Bush Administration, to rebuild a consensus to contain Iraq. The U.S. plan centered on a trade-off in which restrictions on the flow of civilian goods to Iraq would be greatly eased and, in return, Iraq’s illicit trade with its neighbors would be brought under the oil-for-food program and its monitoring and control mechanisms. The next effect, according to the concept, would be to target sanctions only on limiting Iraq’s strategic capabilities, and not on its civilian economy.

The smart sanctions plan was intended to defuse criticism by several governments, including permanent members of the U.N. Security Council France, Russia, and China, that the United States is using international sanctions to promote the overthrow of the Iraqi government or to punish Iraq indefinitely for the invasion of Kuwait. These governments appear to believe that no amount of Iraqi cooperation with the United Nations will be sufficient to persuade the United States to lift sanctions on Iraq, and they and other governments have moved unilaterally to skirt or erode the sanctions regime.

Differences between the permanent members over how to implement these measures prevented immediate agreement on the U.S. plan. With phase nine of the oil-for-food program set to expire on June 4, 2001, the permanent five members of the Security Council began discussions on the U.S. smart sanctions plan, but no agreement was reached, and the oil-for-food program was extended with no changes. With the September 11, 2001 attacks and the war in Afghanistan bringing the United States politically closer to Russia and, to a lesser extent, China, the Security Council reached agreement to adopt some elements of the U.S. plan, as provided for in Security Council Resolution 1409 (May 14, 2002). The following discusses the debate that led to Resolution 1409, and compares what was agreed to in the resolution versus what had been sought in the original U.S. smart sanctions proposals.

- ! **List of Restricted Items.** A major point of dispute was the criteria for placing items on a list of goods that would continue to need Sanctions Committee review (the Goods Review List). Russia and France initially maintained that the proposed list, which included such goods as high performance computers, optical sensing technology, drilling equipment, aircraft spare parts, and marine sensing gear,⁷ was too extensive, and would have the net effect of hindering the rebuilding of Iraq’s civilian infrastructure. However, France and China ultimately agreed to the compromise list, and this aspect of the U.S. plan was incorporated into Resolution 1409.
- ! **Border Controls.** Border control provisions, a central element of the original U.S. smart sanctions plan, were not included in Resolution 1409, largely because of strong opposition by Iraq’s neighbors to controls on illicit trade

⁷A May 24, 2001 draft of the list of goods that would still be subject to review is at [<http://www.cam.ac.uk/societies/casi/info/annex010524.html>].

with Iraq. Iraq's neighbors maintained that enhanced border controls would harm their economies. Early drafts of what later became Resolution 1409 called on the U.N. Secretary General to consult with Iraq's neighbors to formulate a plan for them to buy up to 150,000 barrels per day of oil from Iraq, with the proceeds to be held in escrow. The early drafts also called for the United Nations to enhance its border monitoring procedures to ensure that no contraband goods reach Iraq. None of these provisions, nor any variations of them, were contained in Resolution 1409.

- ! **Flights.** Early draft resolutions of the smart sanctions plan attempted to gain some control over international civilian flights to Iraq by requiring that their cargo be inspected at designated airports outside Iraq. The draft proposals would have permitted Jordan to return six Iraqi Airways passenger aircraft grounded in Amman since the Gulf war, and Tunisia to return four planes there. These provisions were not contained in Resolution 1409.
- ! **Foreign Investment/Energy Exploration.** Early drafts of the smart sanctions resolution "expresse[d] an intention" to permit foreign companies to provide services in Iraq. Some diplomats interpreted this as implicitly including energy exploration services, although most observers believed that such permission would need to be explicit. Permanent Security Council members Russia, France, and China have pressed for investment in Iraq's energy sector, and companies from these countries have reached agreement with Iraq to develop several oil fields if and when the prohibition on foreign exploration is lifted. No provision along these lines was included in Resolution 1409.
- ! **Oil Sales Surcharges.** The early smart sanctions proposals attempted to address the reported practice of Iraq's surcharges of about 30 - 50 cents per barrel of oil, which goes into the coffers of Iraq's government. The drafts stipulate that a list of companies authorized to do business with Iraq be drawn up, a list which it is widely understood would include only large, well-known international oil firms that would not pay Iraq these surcharges. This provision was not incorporated into Resolution 1409, but the Sanctions Committee subsequently addressed the issue separately by adopting the "retroactive pricing" mechanism. The surcharging issue is discussed further below in the section on illicit trade.

Other Sources of Humanitarian Aid

UNICEF, the World Food Program (WFP) the U.N. Development Program (UNDP), the European Community (ECHO), the International Committee of the Red Cross (ICRC), governments, and private relief organizations such as Catholic Relief Services and Save the Children continue to provide additional relief to supplement the oil-for-food program. UNICEF, ECHO, and WFP focus their humanitarian aid on the South and Central part of the country rather than on the economically better off Kurdish north.

It is impossible to determine precisely the total amounts of bilateral and multilateral aid by all donors. However, the U.N. Secretary-General's recent reports and statements have suggested that these aid sources are declining, possibly because

donors believe the oil-for-food program is satisfying Iraq's needs. Secretary General Annan has called for increased international assistance to Iraq, and Resolution 1284 "encourages" countries and international organizations to provide supplementary humanitarian aid and educational materials to Iraq. After Baghdad's incursion into the Kurdish north in late August 1996, the United States virtually ended its assistance program for northern Iraq, which had been about \$45 million per year. The incursion caused all American-based humanitarian relief organizations in northern Iraq to leave in fear of Iraqi reprisals against them.

There is no single source for information on humanitarian assistance to Iraq. A recent report of the Organization for Economic Cooperation and Development (OECD), which provides donor information for the years 1994 through 1998, indicates that Iraq received a total of \$76.36 million in bilateral assistance in 1998.⁸ This does not include any funds provided by U.N. agencies but does include grants by the European Commission (ECHO). A Washington-based official of the European Commission said in June 2001 that the European Union has given over \$200 million in aid to Iraq since 1991.

Illicit Trade

In order to generate funds that it can use without restriction, Iraq has conducted illicit oil dealings with its neighbors and other countries. It has generated additional funds by imposing surcharges on oil buyers. The primary concern of U.S. officials is that Iraq is reportedly using these revenues to buy prohibited military and WMD technology. U.S. officials have also accused Iraq of squandering the illicit revenues on projects and items that do not improve living standards for average Iraqis. On February 29, 2000, the Clinton Administration accused the Iraqi government of using its resources to build nine lavish palaces (valued at about \$2 billion) and to import non-essential items such as cigarettes and liquor.⁹

There are no authoritative figures for the value of illicit trade with Iraq. However, the most widely cited estimates come from a study, released in May 2002, by the General Accounting Office (GAO).¹⁰ According to the GAO study, Iraq earned \$6.6 billion in illicit revenue from oil smuggling and surcharges during 1997-2001. Of that total, GAO estimates \$4.3 billion was from illicit oil sales and \$2.3 was from surcharges on oil and commissions from its contracts to buy civilian goods (kickbacks). The study estimates that during 2001, Iraq earned \$1.5 billion from illicit oil sales through Jordan, Syria, Turkey, and the Persian Gulf; and about \$700 million from surcharges and contract kickbacks.

⁸Geographical Distribution of Financial Flows to Aid Recipients. Disbursements, Commitments, Country Indicators. 1994-1998. OECD. 2000.

⁹Alcohol is classified as a food, so the imports are technically legal under the international sanctions regime in place since Iraq's August 2, 1990 invasion of Kuwait.

¹⁰ GAO-02-625. Weapons of Mass Destruction: U.N. Confronts Significant Challenges in Implementing Sanctions Against Iraq. General Accounting Office, May 2002.

Additional details on Iraq's illicit dealings are discussed below.

Jordan. Since the Gulf war, Jordan has notified the Security Council that it imports Iraqi oil (between 70,000 - 100,000 barrels per day as of March 2002, according to the GAO study) at below-market prices. The oil is in exchange for civilian goods and write-downs of Iraq's debt to Jordan. The United States supports the Sanctions Committee decision to "take note of" the Jordanian purchases, neither approving them nor deeming them a violation. The Administration has routinely waived unilateral sanctions on Jordan that could be imposed because of this trade.¹¹ In October 2000, Jordan cancelled an agreement with Lloyd's Registry, in force since 1993, for the firm to inspect Iraq-bound cargo in Jordan's port of Aqaba. This inspection agreement covered goods other than those imported under the oil-for-food program; goods imported under the program are monitored at all points of entry, including the Iraq-Jordanian border.

Iran/Persian Gulf. The GAO study estimates that Iraq was exporting illicitly about 30,000 - 40,000 barrels per day through the Persian Gulf in March 2002. This exportation is apparently conducted with cooperation from Iran. Of the funds generated through this export channel, about one-half go to Iraq, one-quarter go to smugglers and middlemen, and one-quarter go to Iran's Revolutionary Guard for "protection fees" to allow the shipments to hug its coast and avoid capture. Many believe that exports through the Gulf were higher during 1998-2000, but they have fallen because Iraq is diverting oil to the Syrian route, where there are fewer middlemen to pay. In early November 2000, Iraq openly admitted it is using its Gulf ports for contraband imports by announcing it would import 30,000 Toyota automobiles "from Qatar and the United Arab Emirates."¹² Neither of these Gulf states have land borders with Iraq and both of them have called for the easing of Iraq sanctions.

Syria/Military Technology Exports to Iraq. In late 2000, according to several press reports, Iraq began exporting oil through an Iraq-Syria pipeline, closed since 1982 but now repaired. According to the GAO study, Iraq exported 180,000 - 250,000 barrels per day through this route in March 2002. This exportation is reputedly under a bilateral agreement with Syria under which Syria refines the Iraqi oil for domestic use, and pays Iraq about half the world market price for oil, freeing up extra Syrian oil for export. Resolution 1284 states the Security Council's "intention" to allow new oil export routes, such as this line, and the U.S. and British position is to oppose the reopening of this line unless it is brought under the oil-for-food program and its monitoring and control mechanisms.

There is growing concern that Syria is becoming a major transit point for prohibited imports by Iraq of military equipment and technology that could be used for WMD. In July 2002, a respected Israeli military expert reported that Syria had served as a transit point for Iraq's importation of Russian-made engines for combat aircraft (sold by Ukraine) and tanks (sold by Bulgaria and Belarus), and Czech-made

¹¹Every fiscal year since 1994, Congress has included a provision in foreign aid appropriations cutting U.S. aid to countries that violated the Iraq embargo.

¹²"Iraq to Import 30,000 Toyota Vehicles." *Dow Jones Newswire*, November 1, 2000.

anti-aircraft cannons (sold by the Czech Republic).¹³ According to the same article, Syria also passed on prohibited equipment to Iraq sold by Hungary and Serbia.

In late September 2002, both Ukraine and Belarus denied providing weapons systems or dual use technology to Iraq. However, in late September 2002, the Bush Administration initiated what it called a “temporary pause” in U.S. assistance to Ukraine (about \$55 million held up) because of allegations that Ukraine has provided the “Kolchuga” early warning radar system to Iraq. In February 2001, the United States struck an air defense network that was being upgraded with the help of a Chinese firm, according to press accounts, although it is not known how the fiber optic equipment reached Iraq.

Turkey. According to the GAO study, Iraq exported the equivalent of 40,000 - 80,000 barrels per day of oil through Turkey in March 2002. The exportation is in the form of 450 Turkish trucks per day carrying Iraqi oil products (not crude oil) through the Iraqi Kurdish areas into Turkey in spare fuel tanks. The Turkish government taxes and regulates the illicit imports. As in the case of Jordan, the U.S. Administration has routinely waived the imposition of U.S. sanctions on Turkey for permitting this illicit trade.

Oil Sales Surcharges. As noted above, the GAO study estimates that Iraq earned over \$700 million in 2001 from oil sales surcharges and kickbacks on purchases of goods. The GAO study obtains that estimate by assuming that Iraq obtained a surcharge of 35 cents on each barrel of oil sold under the oil-for-food program. The GAO estimated the “kickback” percentage for Iraq at 5 percent of the value of each purchase contract.

As noted above, the Sanctions Committee moved to curb Iraq’s ability to surcharge on oil sales by adopting a “retroactive pricing” formula. The United Nations said in late September 2002 that Iraq, in part due to the pricing formula, had ended its surcharging practice and that Iraq’s oil sales were rebounding.

Prior to adopting retroactive pricing in September 2001, the Sanctions Committee had evaluated a number of alternative methods. One proposal, not adopted, was to price Iraq’s oil every ten days or every fifteen days rather than monthly. Another idea, not adopted, was to limit Iraq’s oil buyers to major international oil firms, rather than smaller oil traders that were willing to pay Iraq the surcharge. A press report in March 2001 (Reuters, March 8, 2001) listed companies that were purchasing Iraqi oil; many are small companies from countries that seek to do business with Iraq or are sympathetic to easing sanctions on Iraq. U.S. majors are said to buy some Iraqi oil shipments from these small traders.

The list included: Italtel (Italy); Mastek, and Quantum Holdings (Malaysia); Zarubezhneftegas, Mashinoimport, Slavneft, Sidanco, and Rosneftimpex (Russia); Fenar (Lichtenstein); Emir Oil, Coastal Oil Derivatives, and Benzol (United Arab Emirates); Nafta Petroleum, and KTG Kentford Globe (Cyprus); Glencore, and Lokia Sari (Switzerland); Al Hoda (Jordan); Belmetalenergo (Belarus); Samasu (Sudan);

¹³ Schiff, Ze’ev. Syria Buys Arms for Iraq. *Ha’aretz*, July 15, 2002.

Erdem (Turkey); African Petroleum (Namibia); Shaheer Trading (Yemen); Aredio (France); Commercial Home (Ukraine); Awad Ammora (Syria); Montega (South Africa); Afro Eastern (Ireland); and Bulf Drilling (Romania).

Oil Exploration Contracts. There are no public allegations that any international oil companies have begun new oil exploration investments in contravention of existing U.N. resolutions. However, a number of companies have signed exploration deals that would go into effect if and when the ban on oil exploration is lifted. Much of the focus of U.S. officials has been on oil exploration deals by Russian firms. In general, Russia seeks to obtain repayment of Iraq's \$7 billion in debt to Moscow, and possibly to earn funds selling arms to Iraq if such sanctions are eventually lifted. In August 2002, it was reported that Russia and Iraq will soon sign a \$40 billion economic cooperation agreement, although it is not clear that any of the planned cooperation would violate oil-for-food or other sanctions guidelines. France has long had substantial economic interests in Iraq as well. Some of the presumptive contracts for oil exploration in Iraq include the following:¹⁴

- ! Al Ahdab field — China National Oil Company (China)
- ! Nassiriya field — Agip (Italy) and Repsol (Spain)
- ! West Qurna — Lukoil (Russia)
- ! Majnoon — Total Fina Elf (France)
- ! Nahr Umar — Total Fina Elf (France)
- ! Tuba — ONGC (India) and Sonatrach (Algeria)
- ! Ratawi — Royal Dutch Shell (Britain and the Netherlands)
- ! Block 8 — ONGC (India)

Flights to Iraq. Since September 2000, Iraq may have conducted an unknown amount of additional illicit trade aid from flights to and from Iraq. These flights began as relief flights carrying humanitarian aid, intended to challenge the U.S. and British interpretation of U.N. Security Council Resolution 670 (September 25, 1990). Resolution 670 requires the banning of flights to or from Iraq that are carrying any "cargo to or from Iraq or Kuwait other than food in humanitarian circumstances, subject to authorization by the Council ..." or the Sanctions Committee. Prior to September 2000, the U.S. interpretation prevailed that all flights to Iraq require Sanctions Committee authorization prior to takeoff. France, Russia, and other governments, although not opposed in principle to inspecting cargo bound for Iraq, argue that passengers are not "cargo" and that the U.S. interpretation that Resolution 670 restricts all flights to Iraq is not correct.

The cargo on these flights has not been subjected to any U.N. monitoring to ensure that the cargo comports with oil-for-food guidelines. Since September 2000, regular charter flights have begun between Iraq and Syria and Iraq and Jordan. The United States criticized those governments that allow the flights to proceed without approval, but no U.S. or U.N. measures have been taken against the flights or against Jordan or Syria.

¹⁴Morgan, Dan and David Ottaway. In Iraqi War Scenario, Oil Is Key Issue. *Washington Post*, September 15, 2002.

One donation to Iraq in November 2000 drew strong U.S. criticism and a sanction. A member of the royal family of Qatar presented Saddam Husayn with a Boeing 747 jumbo jet as a “gift.” The Qatari, Hamad bin Ali bin Jabr Al Thani, heads the Gulf Falcon air services company, which gave him access to the aircraft. On November 24, 2000, the Clinton Administration announced that exports and reexports of many U.S. goods would need specific Commerce Department approval for sale to Mr. Al Thani or his businesses. U.S. officials said that sanctions were imposed to ensure that U.S. goods would not be improperly diverted to Iraq.

Appendix: Overview of U.S. Regulations Governing U.S. Participation in the Oil-for-Food Program¹⁵

The Iraqi Sanctions Regulations implement Executive Orders No. 12722 (August 2, 1990) and 12724 (August 9, 1990), issued after Iraq's August 2, 1990 invasion of Kuwait. The executive orders imposed a ban on U.S. trade with and investment in Iraq, and froze Iraq's assets in the United States. The Iraq Sanctions Act of 1990 (Section 586 of P.L. 101-513, signed November 5, 1990) reinforces those executive orders. The August 9 executive order amended the August 2 executive order to align U.S. sanctions with U.N. Security Council Resolution 661 (August 6, 1990), in keeping with the United Nations Participation Act (22 U.S.C. 287c). That resolution imposed a comprehensive embargo on all Iraqi imports and exports.

In the aftermath of Iraq's invasion, Iraq was again placed on the U.S. list of state sponsors of terrorism under Section 6(j) of the Export Administration Act (P.L. 96-72). Iraq had been removed from the list in 1982. Countries on the terrorism list are barred from receiving U.S. foreign assistance, votes in favor of international loans, and sales of munitions list items (arms and related equipment and services). Exports of dual use items (items that can have military applications) are subject to strict licensing procedures.

U.S. regulations governing trade with Iraq have since been modified to allow for U.S. participation in the oil-for-food program. Key provisions of the U.S. sanctions include the following:

U.S. firms may apply to the Office of Foreign Assets Control (OFAC) of the Treasury Department for specific licenses for the following activities under the oil-for-food program:

- ! “the sale and exportation to Iraq of medicines, health supplies, foodstuffs, and materials and supplies for essential civilian needs.” The goods can be sold, subject to a license, to the government of Iraq or to a U.N. entity distributing aid under the program.
- ! “the purchase and exportation from Iraq of Iraqi-origin petroleum and petroleum products;”
- ! “the trading, importation, exportation or other dealings in or related to Iraq-origin petroleum and petroleum products outside Iraq; and”
- ! “the sale and exportation to Iraq of parts and equipment that are essential for the safe operation of the Kirkuk-Yumurtalik (Iraq-Turkey) pipeline system in Iraq.”

¹⁵Source: Iraq: What You Need to Know About the U.S. Embargo. An Overview of the Iraqi Sanctions Regulations – Title 31, Part 575 of the U.S. Code of Federal Regulations. U.S. Department of the Treasury, Office of Foreign Assets Control, [<http://www.treas.gov/ofac/>].

In addition:

- ! The regulations “generally” prohibit “the performance of contracts in support of industrial, commercial, public utility, or governmental projects” in Iraq. U.S. persons may not provide financing or consulting services to a foreign country company where those services would benefit such projects in Iraq. U.S. persons may not provide consulting services or goods, in connection with Iraqi projects, to foreign subsidiaries of U.S. corporations, although foreign subsidiaries themselves are not subject to U.S. regulations.
- ! All transfers of funds by U.S. persons to the government of Iraq or to persons in Iraq, are prohibited, as are “all commitments or transfers of credit, financial transactions, or contracts.”
- ! All transportation-related services, or the use by U.S. persons of vehicles, ships or aircraft registered in Iraq, are prohibited. Travel-related transactions by U.S. persons are also prohibited, with the exception of travel related to journalism, or U.S. government or United Nations business.