

# **Report on corruption in Azerbaijan oil industry**

## **prepared for EBRD & IFC investigation arms**

**COIWRP, Azerbaijan, October 2003**

### **I. About us**

The Committee of Oil Industry Workers' Rights Protection was established in 1996. The Committee protects human rights of employees in the oil sector of Azerbaijan, struggles against corruption and bribery, implements a public monitoring on the oil projects realized in Azerbaijan etc.

### **II. Corruption in Azerbaijan**

COIWRP has published explicit facts, concerning corruption existing in the Azeri oil sector, in the press many times since 1997. Our press announcements are devoted to the oil larceny, illegal tax reductions, corruption practices connected with construction works and supplies. These publications had attracted public attention to the corruption issue. But, unfortunately, the Azeri authorities that should deal with corruption do not attempt to take any measures over this issue. Specifically as a result of corruption, the rights of thousands of people have been violated. Corruption causes pollution of the Caspian Sea environment, dying of workers on drilling platforms, harsh working conditions and low wages. As a result of the corruption in oil industry, the biggest part of the oil incomes do not flow into the state budget; that causes the fiscal problems and budget deficit arises. Authorities use the financial hardships as an excuse for putting their hands on different expenditures from the State Oil Fund (SOFAZ) and receiving numerous credits from international financial institutions. And that means the violation of the human rights of millions of people.

**It is necessary to take into account that State Oil Company (SOCAR) is the central point of corruption in Azerbaijan. It operates with the oil incomes, which are the main part of the state budget, and it is directly controlled by Presidential Bureau, Heydar Aliyev and his family.**

**In following text we describe some from the last corruption cases in Azeri oil industry. These cases are directly connected with SOCAR, which is one of the shareholders (19%) in BTC Co., constructing new Baku-Tbilisi-Ceyhan / Erzurum oil and gas pipelines system in Caucasus. BTC Co. requires the loan in approximate amount 600 mil. USD for BTC pipeline project from EBRD and IFC. We are afraid of this loan, because this huge amount of money flowing in completely corrupted environment could only**

**support the corruption practices, worsen the human rights situation and cause next violations of the law.**

We are prepared to provide more detailed information on all below described cases.

At first, let us introduce the topic and explain in a few points the corruption mechanism in Azerbaijan oil industry.

**The basic corruption scheme is possible to explain by this way:**

1. Top managers of big company (in this case SOCAR) found (usually indirectly, through their relatives etc.) their own private enterprises.
2. SOCAR submits some orders to the subcontractor firms, which are owned by SOCAR managers or by their relatives.
3. The invoiced price of works is much higher than market price, usually more than two times. Very often no work is carried out (or the real work is in much lesser scope), although "in the papers" everything is OK.
4. SOCAR pays full contract price to subcontractor, then SOCAR manager (the real owner of subcontractor or its relative) gets back usually 50% of the sum for himself in cash, the rest of money keeps the subcontractor. As the result, budget of the State Oil Company and its subdivisions is under systematical larceny.

Important conjunctions:

- Corruption is most of all connected with construction works, reconstruction and repairing, because it is uneasy to check the real price of components and stock quality. In the same time it is possible to engage the huge range of various companies on construction sites and during reconstruction.
- Because corruption in Azerbaijan has vertical system, the officials always send (usually approximately 50%) of defrauded money to their bosses, they transfer substantial part of money to their bosses etc. At the top of structure stays SOCAR president, above SOCAR is Presidential Bureau.
- Substantial part of contracts and orders is realized without any written documents or agreements, payments are often realized in cash.
- If any national inspection organization (Ministry of Taxes, Prosecutor's Office, Police etc.) starts its investigations, it never clarifies the corruption case in full range. Mechanism is following:
  - Inspectors of Ministry of Taxes come to SOCAR following information of SOCAR employees, suspicion from corruption practice.
  - Inspectors of course know the real prices of all the goods and services in the country and can quite easily estimate the amount of defrauded money.

- Some not high officials are dismissed or arrested for corruption practice. High officials have to pay substantial part of estimated defraud to the inspection. Inspection transfers the respective amount to ministry's head officials, minister is controlled by Presidential Bureau.
- Because corruption series continues to higher and higher levels, inspection usually stops the investigation at the level of high officials of the company.
- If the speech goes about huge companies as SOCAR is, the amounts of defrauded money goes to hundreds millions of USD per year.

### **III. The concrete cases:**

Baku Factory of Deepwater Constructions (BFDC, subdivision of SOCAR, former named "Shelfprojectstroj" Governmental Company) rented a couple of construction grounds to BP Corporation, which is the main shareholder in BTC Co. It happened in 2001, when director of BFDC was Tahir Mammadov. The grounds serve as construction-installment area in the framework of the Azeri, Chirag and deepwater Guneshli (Stage 1) oil field exploitation project. ACG project is a part of Azerbaijan-Georgia-Turkey pipelines system, BTC Co. also requires the loan from EBRD & IFC directly for ACG oil fields development.

The profits from construction grounds rent should be spent on reconstruction of the factory, expansion of its production, new equipment purchasing as well as for creations of new jobs. (Because BFDC is a part of State Oil Company, not the private enterprise, it should follow the interest of the profit as well as the interest of public welfare). But management of BFDC plant decided to use the gained profits for other useless expenditures (especially minor reconstruction works, which are overpriced and exceed many times the market prices), embezzled the certain share of the money. The subcontractor companies provided the works for BFDC belong either to the SOCAR authorities or to BFDC management representatives.

Involved subcontractor companies of BFDC are following:

- Ildurum (Flash) Company, indirectly owned by Rafiq Aliyev of SOCAR
- AG Grade, indirectly owned by Rovnak Abdullayev of SOCAR

#### **A. Ground works in BFDC**

In February 2002, the ground works (to create wholly flat platforms construction grounds in the territory of BFDC) in the sum of 100.000 USD carried out by BFDC per order of AG Grade. There was probably no contract signed for those works and money was paid in cash. The materials and stock used for these

works were not expensive and didn't have a good quality. We suppose that the real value of the work was not higher than 20.000 USD. As the result, next 80.000 USD from total amount flowed into private pockets and the taxes from the contract remained unpaid.

**We enclose two complaints on this issue, which stayed without any answer:**

1. =19.03.2003 From Mr. Rajabov To: BDFC / Najafov  
Complaint on overpriced ground works on construction grounds.
2. =15.05.2003 From: Mr. Rajabov To: BDFC / Mr. Abdullayev  
Complaint on overpriced ground works on construction grounds.

### **B. Reconstruction of BFDC administrative building**

In 2002 – 2003, Ildurum Company carried out the repairs in BFDC – exchange of doors and windows in the factory office building. Each 1 m<sup>2</sup> of the door was produced for 630.000 AZM (126 USD) at the same time when the identical type of door costs not more then 200.000 AZM (40 USD) at the local market, each one screw was calculated for 8.000 AZM (1,7 USD). Calculation has done the same Ildurum Company, which carried out the reconstruction. Total volume of the contract was more then 1.500 m<sup>2</sup> of doors and windows. Because the calculation operates with exaggerated numbers, part of money flowing from SPC plant's account was embezzled.

**We enclose following documents to substantiate the claim:**

3. =20.08.2002 From: Mr. Rajabov To: BFDC / Mr. Ferejov  
Complaint on overpriced doors and windows exchange, some works were not done
4. =Nov.2002  
Particular calculation on doors and windows exchange
5. =Nov.2002  
Invoice for part of windows and doors exchange contract
6. =Mar.2003  
Invoice for part of reconstruction in BFDC factory
7. =Mar.2003  
Invoice for part of reconstruction in BFDC factory

8. =17.03.2003 From: Mr. Rajabov To: BFDC / Mr. Najafov  
Complaint on overpriced plastic doors and windows exchange.

### **C. Lifting cranes**

In May 2002, the port-type lifting crane in the sum of 3 bill. AZM / 600.000 USD was bought by BFDC from MorNeft Company (another part of SOCAR, lead by Agasef Aliyev) as new crane. Just after this purchase, capital repair of the crane started and is not completed till now, with up to now expenses in the sum approximately of 100.000 USD. According to our estimation, embezzlement in the sum of 200.000 USD has been made in connection with crane purchase and reconstruction.

BFDC management also rented to the above mentioned AG Grade Company 25 lifting cranes for 20 USD per hour in 2001. AG Grade then signed contracts to rent the same cranes with two sub-contractors of BP Azerbaijan – Bos-Shelf (co-founder from Azeri side is BFDC) and American Mac Dermott Caspian Contractors. The rent price was suddenly 80 USD per hour. It means, that BFDC, as the branch of SOCAR, loses 60 USD per each hour utilisation of each one from the construction cranes from 2001. Of course it was easily possible to sign the contract directly between BFDC and companies without any damage.

### **We enclose following documents to substantiate the claim:**

9. =18.01.2002 From: BFDC / Mr. Mammadov To: Mr. Rajabov  
Your suspicions were checked, we will take your proposals into account.

10. =03.03.2002 From: BFDC To: Mr. Rajabov  
All your complaints were already resolved.

11. =14.03.2002 From: SOCAR / Mr. Zeynalov To: Mr. Rajabov  
Bos-Shelf and Mac Dermott won the tender, their work is specialized and very good.

12. =05.08.2002 Form: Mr. Rajabov To: BFDC / Mr. Mammadov

Complaint on the cranes renting through mediator companies to foreign enterprises.

### **IV. Which other actions we have already taken regarding this report**

Because of above mentioned corruption practices even during investigations of corruption cases, we try to appeal directly to respective state bodies (Ministry of Taxes, Prosecutors etc.) just very rarely. We always publish all our investigations and informations about corruption practices in SOCAR and its subcontractors at

press conferences. We suppose it is a good way to inform all the state bodies dealing with corruption as well as the general public.

From 2001, we tried many times to resolve the above mentioned problems in direct communication with respective companies and SOCAR representatives. As the enclosed correspondence shows, we either didn't receive any answer or received the answer, which doesn't clarify the situation and doesn't contribute to any solution.

Our publications of informations about corruption usually causes dismissal of some not very important SOCAR officials, but no case was so far fully clarified and resolved. The real clarification of corruption cases is not in interests of any national state body.

### **Example – Ministry's investigation in 2003**

In January 2003, Ministry of Taxes started the investigation on corruption suspicion in SOCAR. As the result, two not high officials were arrested (Nizami Gafarov and Ismichan Yusifov), accused from bribery (Chapter 308 and 179 of State Code of Criminal Procedure, Defraud of state property in large scale). Inspection revealed 800 private companies involved in corruption scheme, then the investigation came to governmental level and was slowed down. The only result were structural changes in SOCAR, with no real impact on SOCAR transparency or proper utilization of public money and incomes from the oil exploitation.

### **Note about COIWRP members prepared this report**

Vidadi Rajabov was working in BFDC Company as the official responsible for production quality control in Department of main construction activities. In May 2002, he was dismissed because his fight against corruption in BFDC and was arrested for "hooliganism" and was liberate only in the frame of amnesty. He is a coordinator of COIWRP on corruption in subdivisions of SOCAR.

In 2002 – 2003 other two people were dismissed from SOCAR subdivisions because of their fight against corruption practices (Mirvari Gahramanli, COIWRP chairwoman and Alexander Stepanovitch Kazakhov). Also all relatives of these people working in administration were dismissed.

### **Concrete steps we already realized in the recent time on corruption cases:**

- Letters to SOCAR and BFDC (2001 – 2003)
- Press conference on corruption during BTC pipelines laying, November 2002
- Press conference, publishing all the above mentioned facts, 22 September 2003

- Approx. 10 – 20 interview on corruption issue published in 2002 in local press
- 6 interviews on corruption issue published in 2003 in local and international press

**V. Enclosures:**

- 12 letter copies mentioned in the text
- 5 letter copies connected indirectly with the issue
- COIWRP report on corruption in Azerbaijan oil industry, 2002
- COIWRP report on corruption in Azerbaijan oil industry, 2003