

**BEFORE THE HOUSE INTERNATIONAL RELATIONS COMMITTEE  
SUBCOMMITTEE ON OVERSIGHT AND INVESTIGATIONS  
APRIL 28, 2005**

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**STATEMENT OF EVERETT SCHENK,  
CHIEF EXECUTIVE OFFICER,  
BNP PARIBAS – NORTH AMERICA**

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Chairman Rohrabacher, Congressman Delahunt, Members of the Committee, my name is Everett Schenk. Since May 2000, I have served as CEO of North American Corporate and Investment Banking Operations for BNP Paribas. With me today are Patricia Herbert, the head of Banking Operations for the Bank's New York branch; William Vassallo, a Director of Corporate Banking Operations for the New York branch; and Harold Lehmann, who prior to October 2001 supervised the Bank's processing of Oil-For-Food Program letters of credit.

BNP Paribas has over 10,000 employees in the United States. In my capacity as CEO, and since 2000, I have been responsible, among other things, for overseeing the New York branch of the Bank, which has provided certain banking services to the United Nations in connection with the Oil-For-Food Program pursuant to a Banking Services Agreement with the UN.

By way of background, the Oil-For-Food Program was created through a unanimous resolution of the Security Council of the United Nations ("UN") with the principal objective of alleviating the suffering of the Iraqi people by providing

humanitarian goods to Iraq under contracts approved by the so-called "661 Committee" or "Sanctions Committee" of the UN Security Council. To that end, the 661 Committee authorized specified contractors to furnish approved goods to Iraq. Once a contract had been authorized by the 661 Committee, the UN directed its bank – the New York branch of Banque Nationale de Paris and later BNP Paribas – to issue a letter of credit naming the contractor as the beneficiary, thereby providing assurance that the beneficiary would receive payment under the contract upon delivery of the approved goods to Iraq and presentation of the required documents.

Although the Program was expected to be short-lived, it was renewed on twelve separate occasions, each for a six month period, and lasted for some six and one-half years. In the 1999-2000 time-frame, the Program underwent explosive growth due to the decision of the 661 Committee to greatly expand the goods that were permitted to be delivered under the Program. With this decision, the sheer volume of the letters of credit that the Bank was required to issue and process skyrocketed. The processing of these letters of credit became a much more complicated and challenging task, not only because of this increase in volume, but also because the transactions themselves were considerably more complex due to the wide range of the goods that were being approved under the Program by the 661 Committee, and the greatly increased geographical diversity of the approved suppliers.

From the Program's inception, it was contemplated that humanitarian letter of credit beneficiaries might well need financing in connection with their UN-approved

transactions. Beneficiaries therefore were permitted under the Oil-For-Food Program to assign proceeds under their letters of credit to secure bank financing to obtain the required items. An assignment of proceeds is a traditional means of securing such financing, and commonly takes various forms. These include an assignment to a bank to obtain a direct cash loan from which the beneficiary can pay its supplier; or an assignment to a bank making funds available to the supplier; or an assignment to the supplier providing financing to the beneficiary in the form of goods supplied on open account.

When I appeared before the full Committee last November, questions were raised about a humanitarian letter of credit that had been issued to a UN-approved beneficiary named Al Riyadh International Flowers Company, where it appeared that several payments had been made at the request of the beneficiary to an entity named East Star Trading Company. Having had no advance notice from the Committee that it was interested in those payments, the Bank had not had time to fully prepare to address the issue on that occasion.

Since then, however, and in response to the Committee's inquiries in these regards, the Bank has been engaged in a comprehensive review of the approximately 54,000 payments that were made pursuant to humanitarian letters of credit issued under the Program, utilizing a systematic approach that so far has required the expenditure of approximately 8,000 man-hours. As a result of that process, which is ongoing, we have considerably more information today than we did in November about payments that were

made to certain persons other than the letter of credit beneficiaries. As you know, we have shared that information with the Committee in the form of an Interim Report that was prepared specifically for the Committee's use in anticipation of this hearing.

I would like to return in a minute to the subject of East Star. But before I do, let me say at the outset that nothing in our investigation to date has led us to believe that any letter of credit proceeds that were assigned or paid to anyone other than a bank making loans directly to beneficiaries were causally related to any corruption which may have occurred in the Oil-For-Food Program.

Further, let me say that we have found that in the course of processing assignments and payments, some mistakes were made. Although mistakes are perhaps inevitable in the context of a Program that required the processing of approximately 54,000 payments under approximately 20,000 letters of credit and 32,000 amendments involving an estimated 5 million pages of documents, they still should not have occurred. We certainly appreciate the Committee's concerns regarding the handling of the humanitarian letter of credit transactions, and hope that the Committee will find our testimony helpful in addressing the issues that were raised at the last hearing.

To return then to the subject of East Star. We understand that East Star is an affiliate of a large international export group called Pacific Inter-Link that was incorporated in Malaysia in 1988. Pacific Inter-Link exports a wide array of foodstuffs, pharmaceuticals, building materials and other consumer products from the Far East to the

Middle East, Africa and Europe. Pacific Inter-Link and seven of its affiliates were awarded numerous UN-approved humanitarian supply contracts in almost every phase of the Oil-For-Food Program, totaling approximately \$270 million in value. East Star was a supplier of goods to Al Riyadh and a number of other humanitarian letter of credit beneficiaries under the Program.

We understand that these beneficiaries typically assigned a substantial portion of the proceeds they were entitled to receive under their letters of credit to a financing facility that a major international banking institution had extended to East Star. That financing facility enabled East Star to carry out its supply obligations to the beneficiaries. For those unfamiliar with trade finance practices, a financing facility is a common arrangement under which a bank extends a revolving line of credit to a borrower through an account that permits the borrower to draw a specified maximum loan amount. Ordinarily, as funds are deposited back into the account to repay the loan, an equal amount can be borrowed again. So when letter of credit proceeds were paid into the account at that major bank, we understand that those payments would have served in the first instance to repay that bank for the loans it had made to finance the underlying UN-approved humanitarian goods transactions, rather than to pay East Star for the goods themselves.

I will say more in a moment about how such payments comported with the procedures that the Bank had put in place for processing assignments of proceeds and payments under Oil-For-Food Program humanitarian letters of credit. But I want to

emphasize, as I noted earlier, that financing arrangements such as these are commonplace in the world of trade finance and are entirely legal and integral to the free flow of goods in the global marketplace.

The Bank's review identified comparable financing arrangements involving other suppliers to beneficiaries of humanitarian letters of credit under the Oil-For-Food Program, including in particular a financing facility maintained at another large international bank by another major supplier of goods named Al Douh Jordanian Establishment. Significantly, a number of Al Douh affiliates were UN-approved suppliers of approximately \$88 million worth of goods under UN-approved humanitarian supply contracts throughout the various phases of the Program. As with East Star, letter of credit beneficiaries assigned proceeds to the financing facility maintained by Al Douh, which in the first instance would have been available to repay the bank for financing it provided for the underlying UN-approved humanitarian goods transactions rather than to pay Al Douh for the goods themselves.

As I already have indicated, the review that the Bank has undertaken is ongoing, and we expect to provide this Committee with a final report of our findings when it has been completed. But to date, there has been no indication that any so-called "third party payment" has served as a means to corrupt the Oil-For-Food Program.

That is not to say, however, that these payments, while totally consistent with normal trade finance practice, were also consistent with the procedures the Bank had

put in place for processing letters of credit under the Program. As I remarked at the outset, financing is integral to the movement of goods contemplated by the humanitarian side of the Program, and assignments of letter of credit proceeds are the logical means to assist in securing such financing, regardless of the form the financing might take.

The Banking Services Agreement contains an ambiguous provision that seems to speak to this issue as follows:

The Central Bank of Iraq will forward to the Bank requests from the appropriate Iraqi Government entities to open irrevocable, non-transferable, non-assignable (except to the supplier's bank for the repayment of financing for the purchase of the humanitarian supplies) [letters of credit] for the account of the Iraqi purchaser in favour of the supplier.

While it is clear that this provision was intended to exclude assignments of proceeds to anyone other than a bank providing financing for the underlying UN-approved humanitarian goods transaction, it is far from clear whether it was meant to further limit assignments only to a bank providing such financing directly to the beneficiary, and to foreclose such financing if it was provided by a bank through the beneficiary's supplier. In any event, as its operational procedures evolved, the New York branch of BNP and then BNP Paribas took a conservative approach in deciding that assignments of proceeds as a general matter should be limited to banks providing financing directly to letter of credit beneficiaries.

As I said earlier, our review has identified some instances, reflected in our Interim Report, in which assignments or payments were made to persons other than beneficiaries or banks making direct loans to them, contrary to the Bank's procedures. Based upon the review we have conducted to date, the Bank has determined that in some, but by no means all, of those instances, the information that was available to the letter of credit processing personnel at the time would have indicated the possibility that the assignments or payments were being made to financing facilities extended by banks to suppliers, rather than to the beneficiaries themselves. The Bank has determined that, in these instances, the processing of those assignments or payments constituted avoidable errors.

Although the Bank did take steps over the course of the Program to enhance management and strengthen and reinforce its policies and procedures for processing letters of credit under the Program, we believe, with the benefit of hindsight, that still more should have been done. In particular, better training of the numerous temporary clerical employees that had to be hired on extremely short notice to deal with the sudden, sharp upsurge in the volume and complexity of humanitarian supply contracts to which I referred earlier, could have minimized the incidence of such payments. In addition, enhanced monitoring of the performance of those employees could have resulted in corrective actions being taken that further could have reduced the incidence of such mistakes.



Still, to evaluate these assignments and payments properly, we believe a number of observations are in order:

- I would begin by observing first, that the beneficiaries in the transactions involving assignments all made representations to BNP Paribas that they were assigning proceeds to banks that were providing them with financing for those transactions; and second, that the banks providing the financing in the transactions involving assignments that I described earlier confirmed this on a number of occasions.
  - In fact, the assignments of proceeds in the transactions I described earlier were in favor of banks; and we understand that the payments that were made under those assignments would have served in the first instance to repay the banks for the financing they made available for underlying UN-approved humanitarian goods transactions.
  - Moreover, the fact that the financing banks, which are large international institutions, evidently were comfortable stating on various occasions that they were providing financing for the transaction to the beneficiary, albeit through the supplier, underscores the fact that this distinction is at best one of form.

- It also is worth noting that any legal claims with respect to the proceeds that had been assigned in these circumstances would have belonged to the financing banks that were designated as the payees, and not to the suppliers to which the financing had been extended.
  
- Another point I would like to make is that assignments of the type I have described are legitimate commercial arrangements, quite apart from any limitations that may have existed under the procedures adopted by the Bank for processing humanitarian letters of credit under the Oil-For-Food Program.
  
- Furthermore, the Bank has not identified any instance where a letter of credit itself, along with its corresponding obligations, was transferred or assigned by a beneficiary to a third party in violation of the Banking Services Agreement.
  
- The Committee also should be aware that the Bank is in possession of a notice of arrival with respect to the goods that are the basis for each of the payments we are addressing here today.
  
- It is highly significant as well that the suppliers who were involved in the substantial majority of the dollar value of the transactions to which

I referred earlier were, either directly or through their affiliates, UN-approved beneficiaries under other humanitarian letters of credit worth hundreds of millions of dollars.

- Nor should we lose sight of the fact that where the proceeds of a letter of credit are paid directly to a beneficiary, the beneficiary is free to use some or all of those proceeds to repay any bank that provided financing for the transaction, whether the funds were advanced by that bank to the beneficiary or its supplier; or to pay its supplier directly; or to pay others.
- I would call the Committee's attention to the fact that, even today, none of the so-called "third parties" that have been identified appears on the United States Department of Treasury Office of Foreign Asset Control's List of Specially Designated Nationals.

Finally, and most importantly, I want to emphasize again that the Bank has seen no indication that any assignment of proceeds or payment to any so-called "third party" is causally linked to any corruption that may have occurred in connection with the Oil-For-Food Program.

In closing, I would reiterate that in order to be fully responsive to the Committee's inquiries, the Bank is continuing its review; and that it intends to provide

this Committee with a final report at the conclusion of that process, just as it did on an interim basis here, to assist the Committee further in its own assessment of this matter. My colleagues and I would be pleased to respond as best we can at this stage of the process to any questions the Committee may have. Thank you.