PRIVATIZATION AND CORRUPTION: THE WORLD BANK AND AZERBAIJAN

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EXECUTIVE SUMMARY

In April, 1995, the World Bank approved the Petroleum Technical Assistance Project (PTAP) to assist the Azeri government in restructuring the State Oil Company of the Azerbaijan Republic (SOCAR). Seven months later, the IMF approved a stand-by credit to underwrite an economic reform program for the country, designed to promote the privatization of state-owned enterprises. Because of its oil rights and its stake in the prospective trans-Caucasus pipeline, the investment world recognized SOCAR as the 'crown jewel' of potentially purchasable public firms in Azerbaijan.

At the World Bank in the mid 1990s, the debate about the effectiveness of the prevailing method of privatization in former Soviet republics, such as Azerbaijan, had become increasingly intense. On the one hand, Jeffrey Sachs promoted and defended the voucher-based method: from the government, adult citizens received vouchers they could exchange for shares in investment funds that bought public enterprises. Sachs claimed that vouchers represented a more equitable distribution of public assets than other approaches to privatization and that the newly-created investment funds helped to establish capital markets. On the other hand, Chief Economist Joseph Stiglitz argued that the voucher method left ownership in the hands of profit-seeking, poorly-regulated investment funds, which ultimately decapitalized public enterprises, leaving them in ruins. With the Russian economy on the verge of collapse, after protracted exposure to Sachs' method virtually deindustrialized the country, Stiglitz' arguments were gaining credence.

By 1996, Viktor Kožený, an international financial operator who had allegedly defrauded investors in the Czech Republic of nearly US$1 billion through the voucher privatization program there, had resurfaced in Azerbaijan. World Bank officials, either resident in the capital or traveling there on mission, feared that Kožený would exploit the vulnerabilities of the voucher privatization scheme in progress, just as he had manipulated the program in the Czech Republic.

At the same time, the World Bank's Country Manager was wary of senior Azeri officials at the State Property Committee (SPC), which administered the privatization program. The SPC was responsible for listing the enterprises to be sold and for managing the voucher distribution process, among other things. In addition, the lack of transparency in the relationship between the Azeri President's office and the management of SOCAR concerned the World Bank specialists as the privatization program evolved.

From Kožený's perspective, three problems of perception had to be resolved if he was to successfully produce a windfall in Azerbaijan equivalent to the one he had generated for himself in the Czech Republic. First, Kožený had to convince World Bank officials that the privatization scheme was credible and should continue, despite growing doubts about the voucher method. Secondly, he had to persuade Azeri officials and the World Bank that he should be allowed to participate and buy vouchers (and options to buy vouchers) despite his dubious reputation in international financial circles. Finally, he had to induce investors to believe that they could gain control of SOCAR by buying into his investment funds.

In the fall of 1997, when Kožený's Azeri operation was well underway, his collaborators in Baku discovered that World Bank staff members in Azerbaijan were warning pivotal government officials to avoid dealing with him. On October 31st, 1997, a Kožený employee in Azerbaijan sent a memo to Freddie Botur, a friend of World Bank President James Wolfensohn and an investor with Kožený. The memo outlined the support Kožený needed from the World Bank in order to legitimize his operations. Botur met with Wolfensohn and discussed the memo, which Botur gave to Wolfensohn. Then, on November 13th, 1997, the Vice Chairman of the SPC wrote Kožený and notified him that Bank staff had made negative comments about him. Again Kožený mobilized his contacts to approach Wolfensohn and neutralize the influence of lower-level staff members on the Azeri government and on the Bank, itself.

Sometime between November 15th and December 9th, 1997, Kožený met with Wolfensohn, apparently armed with information about embarrassing financial investments Wolfensohn had made in the past. Despite the fact that the Bank staff members had warned Azeri officials about Kožený, on December 9th, Wolfensohn wrote 'an acquittal' letter to him, informing him that they had not and that the matter was being investigated by the Vice President for Europe and Central Asia. The Vice President then wrote the SPC Vice-Chairman with the same message. In the meantime, an influential lobbyist working with the Kožený team wrote Kožený's attorney and informed him that the effort to move decision-making regarding Azerbaijan out of the hands of local World Bank representatives had been successful. According to the lobbyist, decisions about the Azeri privatization program would be made at senior levels in Washington and would not be influenced by the opinions of Bank officials in Baku.

Despite the risks inherent in the Azeri privatization program, the scheme proceeded until 1999. During that time, Wolfensohn met twice with Viktor Kožený and once with each senior SPC official, although the World Bank Country Manager in Baku had told him both men were corrupt. Only when investor Frederic Bourke exposed the fact that at least one major investor had been defrauded was the scheme halted. Ultimately, investors in Kožený's enterprises lost over US$200 million.

World Bank senior management, which had been warned by a number of different people about the SPC, Kožený, and SOCAR continued the voucher operation until Bourke exposed it. In 2000, the Bank project to restructure SOCAR, approved in 1995, was cancelled. Only half of the funds allocated had been disbursed, and the Implementation Completion Review written by the Bank revealed that efforts to promote a legal framework for private investment in the energy sector through legislative action were unsuccessful for lack of 'borrower ownership and capacity.' In simpler language, the report meant that the Azeri government had opposed transparency and accountability measures.

At the time that the fraud in Azerbaijan occurred, none of the World Bank officials in a position to anticipate corruption was able to expose it, given that the Bank President had helped to conceal it. Moreover, the documents obtained show that an internal World Bank memorandum and a letter written to Wolfensohn by the World Bank Country Manager about corruption in the SPC found their way into Kožený's files, strongly suggesting a link between Kožený and senior management at the Bank. The official secrecy of the World Bank and the immunities afforded it, however, make additional details of the relationship inaccessible. The documents that do expose Wolfensohn's role in the Kožený episode in Azerbaijan only became available because Kožený's files were obtainable through the discovery process in a criminal prosecution.

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Corruption is not just an issue of developing countries. There are corruptions and there are the corruptors. And many corruptors come from developed countries and many corruptors are clients of all of us. If we don't want the cancer of corruption to spread in the world we, ourselves, must stand up to it.

Address to the Bankers' Club
James D. Wolfensohn
President
The World Bank
February 3, 1997
London

Banking supervisors must determine that banks have adequate policies, practices and procedures in place, including strict "know-your-customer" rules that promote high ethical and professional standards in the financial sector and prevent the bank being used, intentionally or unintentionally, by criminal elements.

Core Principles For Effective Banking Supervision
Basel Committee on Banking Supervision
September 1997

* The Basel Committee was established by the central-bank Governors of the Group of Ten countries in 1974. The Committee formulates broad supervisory standards and recommends statements of best practice in the expectation that individual authorities will implement them.

I. Introduction

In 1999, a privatization scheme rumored to include the state-owned oil company in Azerbaijan, a former Soviet republic on the Caspian Sea, halted abruptly. An investor discovered that Omega Advisers, Inc., a hedge fund, and quite possibly he himself, had been defrauded by an international financial operator named Viktor Kožený.* Funds, supposedly invested to participate in the auctioning of state-owned enterprises, had not been deposited in the accounts of the Azeri government agency that managed the privatization program. At that point, well over US$ 80 million was missing, although in the end, over US$ 200 million was lost.

The scheme need not have advanced so far before it was stopped. The World Bank was providing technical assistance for its implementation and the specialists involved were aware, early on, that the sale of large state enterprises in Azerbaijan could be a swindle. These staff members, directly and indirectly, warned higher level officials at the Bank that the Azeri government agency in charge of privatization, the State Property Commission (SPC) was corrupt and that the State Oil Company of the Azerbaijan Republic (SOCAR), the asset investors sought to buy, would not be sold, despite the recurring semi-official tease that it would be. Three Bank staff members specifically warned Azeri officials to be wary of the suspect financier who had corrupted the privatization process in the Czech Republic a few years before. In addition, by 1997, a significant contingent of policy experts and economists at the Bank, including the Chief Economist himself, openly criticized the method proposed for privatization in Azerbaijan for its lack of transparency and its vulnerability to 'venal practices.'

Viktor Kožený, the financier in question, knew through his own operatives that Bank staff might expose him as well as corrupt Azeri government officials. To thwart their potential intervention in what promised to be a highly profitable venture, he enlisted

* Viktor Kožený is a Czech financier who holds Irish citizenship and resides in the Bahamas. Criminal charges have been brought against him in the United States and the Czech Republic for allegedly illegal activities involving privatization schemes in the Czech Republic and Azerbaijan. In 2003, the Manhattan District Attorney indicted Kožený for grand larceny, and a 411-page Czech indictment was filed against him five years later. Frederic Bourke Jr., an investor who exposed Kožený's attempt to exploit the financial vulnerabilities of the privatization process in Azerbaijan, voluntarily gave testimony for the prosecution to the New York grand jury that handed down that indictment.

Bourke is the one investor who exposed Kožený's corrupt Azeri scheme. Nevertheless, he is the investor who now faces criminal charges in a badly flawed federal prosecution. At his request, GAP is conducting a broad public interest investigation of the Azeri privatization program and Kožený's investment scheme. The GAP investigation includes independent analyses of the policies and activities of the United States government, the World Bank, and other governmental and corporate entities. This report is the first in a series produced by the investigation, and it focuses on the role of World Bank management and staff in Viktor Kožený's campaign to manipulate the Azeri privatization program.

Graham Wisner, a well-connected lobbyist at Patton, Boggs in Washington, D.C., and James Wolfensohn, President of the World Bank. These two men lent their reputations, connections, and, in Wolfensohn's case, his institution's support, to a fraud in the making perpetrated by a rogue financial speculator and apparently corrupt high-level government officials.

Because the World Bank enjoys sovereign immunities and is not subject to either national or international law, its President was free to facilitate Kožený's operations in Azerbaijan without fear of consequences. The role of the World Bank in the corruption of privatization in Azerbaijan has only been exposed because James Wolfensohn became involved with an international speculator who was himself subject to criminal prosecution.

II. Voucher Privatization and Azerbaijan

When the Cold War ended in 1990 and the republics of the former Soviet Union gained independence shortly thereafter, the World Bank had already developed the strategies it would implement in the region. During the 1980s, a package of policies that came to be known as the "Washington Consensus" had been applied throughout the developing world by the Bank and the International Monetary Fund (IMF), and the processes of privatization and trade liberalization were far advanced. At the time, however, the allegations of widespread corruption that would come to be associated with both privatization, which facilitated the theft of national assets, and liberalization, which expedited the transfer of stolen wealth abroad, had not yet been well articulated.

After independence, the Republic of Azerbaijan joined the World Bank Group in phases: in 1992, Azerbaijan joined the International Bank for Reconstruction and Development (IBRD), which lends at market and near-market rates, and the Multilateral Investment Guarantee Agency (MIGA), which insures foreign direct investment. Three years later, the country also joined the International Development Association (IDA), which issues grants and lends at concessionary rates, and the International Finance Corporation (IFC), which lends directly to private firms. A limited Country Assistance Strategy (CAS) was presented to the Bank's Board of Directors in 1995 and a full CAS was discussed in 1996, but apparently never approved. As the first in a list of objectives, the pending CAS proposed: "[E]stablishing a policy and institutional framework conducive to efficient and equitable private sector led sustainable growth."[1]

The terms of the CAS were developed in response to the deplorable conditions in Azerbaijan at the time. In 1995, the Azeri economy and social structure were both critically damaged by the events of the previous five years. The country had been through the collapse of the Soviet Union, a series of coups, and a protracted conflict with Armenia that had displaced nearly 15 percent of the population. Poverty rates exceeded 60 percent and infrastructure and social services had disintegrated. Nonetheless,

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[1] Report No. 21459, Azerbaijan, Country Assistance Evaluation, World Bank, Washington, D.C., November 30, 2000, p. 3.

Azerbaijan attracted the attention of Western entrepreneurs because of the country's rights to Caspian oil deposits.

In 1995, World Bank work began in Azerbaijan. Early documents, without specifics, refer to the fact that political stability, fragile though it was, had been restored, and both presidential and parliamentary elections had been held.[2] In the first year of comprehensive Bank involvement, evaluators wrote that results in many areas were encouraging. Inflation, they said, had been brought under control, and privatization in agricultural land, industry and banking was proceeding. Nevertheless, the Bank's evaluators noted, that: "The pace of public sector governance reform and private sector development has been slow....Layers of regulations and corruption impose a high cost on new domestic and foreign investors, impeding investment and growth."[3] This observation was a gross distortion and understatement, considering what they knew, even at the time. As the Bank's program in Azerbaijan evolved, corruption continued to plague the public sector reform, largely due to political circumstances and to the abrupt transition from socialism to a capitalist market economy.

A. *Political Realities and the World Bank*

The Articles of Agreement of IDA prohibit the Bank from interfering in the political affairs of member countries,[4] a constraint that leads the Bank to maintain an official quasi-silence about the character of member governments. The provision has its purpose. Over the years, the Bank lent billions to the notoriously corrupt, such as Mobutu Sese Seko of Zaire, Anastasio Somoza of Nicaragua and Ferdinand Marcos of the Philippines, all important allies of the United States and Western Europe in the Cold War. Bank officials justified the practice by claiming that development projects were judged on their economic merits alone. Given the reputations of the loans' ultimate beneficiaries, Bank officials simply left aside the likelihood of larceny. As a result, the Bank's lending practices during the Cold War in developing nations in Asia, Africa and South America left many countries saddled with economically crippling levels of debt that, due to the incompetence and corruption of their leaders, they could never repay.

When lending began in Azerbaijan, however, it had become increasingly difficult to argue that the Bank considered economics alone in deciding what and who to underwrite. The Bank's own policies of privatization and trade liberalization had virtually erased any pretense that a meaningful boundary separated the economic from the political. To implement such policies, governments were required by loan conditionalities to approve regulatory legislation, alter their judicial systems and in some cases, amend their

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[2] Ibid., Annex, Memorandum To The Executive Directors And The President, November 30, 2000.
[3] Ibid. p. 2.
[4] Articles of Agreement, Article V, Section 6, Political Activity Prohibited: The Association and its officers shall not interfere in the political affairs of any member; nor shall they be influenced in their decisions by the political character of the member or members concerned. Only economic considerations shall be relevant to their decisions, and these considerations shall be weighed impartially in order to achieve the purposes stated in this Agreement.

constitutions.[5] Moreover, as the impact of the policies spread, the scope of corruption based on privileged political access to economic information in borrowing governments dramatically increased.

Nevertheless, Bank analysts maintained the position of non-intervention in political affairs when issuing formal statements and analyses. Documents prepared by the Bank described the political situation in Azerbaijan during the 1990s very briefly in accounts that were vague and understated, and which tended to end abruptly in 1995. Analyses beyond 1995 and factual descriptions of more recent events would reflect negatively on the sitting government. Institutional restrictions could be interpreted to mean that even technical documents lacked the license necessary to describe the scale and the impact of corruption because the political autocracy that ruled the country would be implicated.

The Country Assistance Evaluation (CAE) prepared by the Bank for Azerbaijan in 2000 tempered references to what impartial observers recognized as a corrupt and authoritarian political structure. In part, the CAE read:

> Azerbaijan had four governments between 1991 and 1993. After presidential elections in 1993, President Aliyev faced two coup attempts. Parliamentary elections in November 1995 restored political stability. Despite a political consensus for a market economy, reforms have often been delayed because of factional or personal interests.[6]

The account is a remarkable statement. It is true that, in November, 1995, Azerbaijan acquired a liberal constitution, providing for a presidency, a legislature with the on-paper power to approve the budget and impeach the president, and a judiciary with a certain limited independence. The CAE, however, was written in November, 2000 and read as if the political developments that occurred after 1995 had little or no impact on ensuing economic and financial realities. In this evaluation, the World Bank omitted mention of the fact that Heydar Aliyev himself took power through an armed insurrection that ousted a democratically elected President, Abulfez Elchibey, in 1993, before holding elections that were 'flawed.'

Prior to assuming the presidency, Aliyev had been a high-level KGB official and his résumé included a position on the Soviet Politburo under Leonid Brezhnev. Subsequently, he became First Deputy Prime Minister of the Soviet Union, responsible for transportation and social services, but was forced to resign in 1987 by Mikhail Gorbachev, in the face of corruption charges. One of Aliyev's first acts as the President of Azerbaijan was to negotiate, behind closed doors, a US$13 billion Production Sharing Agreement (PSA) with a consortium of oil companies known as the Azerbaijan

[5] Curiously, Bank staff members do not seem to interpret this kind of intervention as 'political.' For example, the Country Manager in Azerbaijan, as privatization moved ahead, told interviewers that the Bank's role in the program was limited and was mostly 'economic.' He then went on to say that the Bank assisted in drafting privatization laws and attempted to help the Azeris put a legal and administrative framework in place with which to manage oil. Drafting laws is typically seen as a political activity in any commonly understood sense of the term, but apparently not in the World Bank context.
[6] Report No. 21459, p. 1.

International Operating Company (AIOC) in what was called 'the deal of the century.'[7] When ratified, the PSA had the force of law, but Azeri regulations did not require that its particulars be disclosed to the public.

More meaningful assessments of the Azeri political economy noted that the government participated in the AIOC consortium through SOCAR, which was closely controlled by the President's office.[8] Through a network of informal and familial ties linking SOCAR to himself, Heydar Aliyev centralized control over Azerbaijan's single-most important export commodity. One analyst characterized the situation as an 'oil-politics dynamic:' "The mechanisms for controlling Azerbaijan's oil sector are tightly clustered around the president. As the politically-acceptable agent of the government, SOCAR has a near-monopoly on the management of the country's oil industry."[9]

This centralization of power could be exercised despite the fact that, after the elections in 1995, the Parliament had become responsible for approving PSAs proposed by SOCAR. In practice the legislature had little power of oversight. Opposition deputies acknowledged that PSAs were secretly negotiated and the quantity of "bonus payments" made to specific government officials was undisclosed. By 1995, the Aliyev government had consolidated power and was well-known for its secrecy with respect to oil dealings and its suppression of opposition political parties and trade unions.

In contrast to the Bank appraisals, more impartial and candid assessments portrayed the Aliyev government in Azerbaijan, about this time, as one of the most corrupt in the world.[10] Influence was based on an informal network of family connections that had acquired a veneer of constitutional government. Political institutions were closely linked to clan and family, with the executive firmly controlling the legislature. In addition, the president appointed the prime minister and cabinet members, who, for their part, typically were obliged to buy their jobs. Many ministers were related to the Aliyevs.[11]

As the Head of State, Heydar Aliyev enjoyed definitive influence over the decision-making that determined the scope of the privatization program in the country. In theory, Aliyev had to secure the approval of the Council of Ministers in order to initiate the privatization of SOCAR. In practice, however, many ministers were directly or indirectly dependent upon him for their respective positions, and their ability to oppose a

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[7] Participating companies include: BP, Unocal, LUKoil, Statoil, ExxonMobil, Pennzoil, ITOCHU, TPAO, Delta Hess and SOCAR.
[8] David Hoffman, "Oil and Development in Post-Soviet Azerbaijan," *National Bureau of Research Analysis*, Vol. 10, no. 3, August, 1999.
[9] Ibid. p. 16.
[10] *'Central Asia Survey'*, The Economist, Feb.7th 1998, pp. 3-18. See also Transparency International's Corruption Perception Index for 1999, which ranked Azerbaijan as one of the four most corrupt countries included in the scale, equal to Indonesia but slightly less corrupt than Nigeria and the Cameroon. Although the index did not include Azerbaijan until 1999, the ranking could be imputed to earlier years: the Head of State and the ruling party were unchanged since 1993.
[11] Well over twenty of Heydar Aliyev's relatives held influential positions in his government and in state owned enterprises. For the list and the positions, see Hurriyyat, Baku, in Azeri 18 Jul 02 p.7. See also "Azerbaijan: Turning Over a New Leaf?" ICG Europe Report N°156, 13 May 2004.

presidential initiative was tenuous. As a result, Aliyev was a valuable personal ally for foreign investors seeking to gain control of specific assets as the privatization program, developed with strong IMF and World Bank influence, moved forward.

B. *Voucher Privatization*

When the IMF promoted the privatization of the national assets of the former Soviet republics and the central European countries, the World Bank had already developed a menu of methods for transforming public to private ownership and control. Before privatization came to Azerbaijan, programs in the form of direct sales, management buyouts, public offerings, voucher privatizations, and lease or concession arrangements had been elaborated and carried out, primarily in Latin American countries during the 1980s.

For Eastern Europe, Russia and Central Asia, no method was more favored by the World Bank than voucher privatization. The economists gaining prominence at the time, primarily Jeffrey Sachs and the disciples around him, claimed that this method of auction and sale was preferable for transition economies. The method was justified using dense economic jargon about developing capital markets and sequencing market reforms. Because of the tradition of political silence at the Bank, no one admitted that the method appealed because it distanced the economy so drastically from the ownership prerogatives based on already existing socialist customs or de facto property rights.[12]

At the same time, experiences with privatization in Latin America had exposed the weaknesses in the method of outright sale of state assets because a lack of transparency resulted in the transfer of public assets to monopolistic private control at artificially reduced prices. Supporters of vouchers (the 'voucheristas') argued that the use of coupons for the purchase of state enterprises would: i) result in a more equitable distribution of public wealth, and ii) solve the problem of a lack of cash in a transition economy.

Using this procedure, all adult citizens were entitled to a voucher allowance, which they could exchange, either through sale or auction, for shares in state enterprises. The process also required the establishment of investment funds that pooled vouchers in order to acquire more concentrated shares of state enterprises. These funds issued shares in their own assets in exchange for the vouchers they bought from citizens. Ultimately, the investment funds were to be listed on newly created stock exchanges, inaugurating capital markets in formerly socialist countries.

In practice, the method was a dismal failure. The capital markets established were weak and volatile, and the value of the vouchers traded on them could be manipulated among a relatively small and privileged number of potential buyers. The Sachs economists then

[12] Management buyouts and employee ownership schemes, which represented a more incremental transfer of assets and left enterprises in the hands of those who knew how to run them, were disparaged for possibly endowing the *nomenklatura* with new privileges in the emerging capitalist system.

tried to deepen the markets by privatizing pension funds and forcing them into the financial fray. In the former Soviet republics, the result for working people was catastrophic. First, they lost their jobs as former state enterprises collapsed after privatization, and next they lost their pensions in the newly-created, poorly-regulated capital markets.

To be sure, the voucher scheme had its critics at the Bank. Experts argued that the process contained an inherent vulnerability. This method would pass control of productive enterprises from the state to financial interests seeking quick profits rather than to entrepreneurs intending to restructure and run the companies. When investment funds became the purchasers, those who controlled them tended to try to profit directly from the resale of existing assets and capacity. For a number of institutional reasons, the new owners lacked the incentive, capacity and expertise to develop the enterprises and actually operate them.[13] Privatization using vouchers necessitated the introduction of these investment funds, which, in a post-socialist setting, would undermine the growth of a capable industrial sector, transferring capital into an under-regulated, non-transparent financial sector. According to this view, a long-term consequence of voucher privatization with investment funds would be the decapitalization of functioning enterprises in favor of asset stripping by fund managers. Like the corporate raiders who struck troubled companies and bankrupted them in the 1980s around the world, the financiers who controlled investment funds and vouchers were well placed to enrich themselves through the manipulation of the privatization process and paper trades in the financial sector.[14]

The Czech Republic

Voucher privatization was employed in the Czech Republic, beginning with a first wave of public sales from October, 1991 to December, 1992, and continuing in a second wave from August, 1992 to November, 1994. To participate in the bidding, Czech citizens purchased a coupon booklet for the equivalent of US$35 and registered it with the government Participants could invest their vouchers in Investment Privatization Funds (IPFs), which would then bid for shares in a public enterprise on behalf of their shareholders. In the immediate aftermath, the process was widely judged a success because of the high proportion of state assets sold. At the time, however, even some supporters of voucher privatization expressed misgivings about the potential problems of unregulated ownership through investment funds.[15]

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[13] For the best critique of voucher privatization, see David Ellerman, "Voucher Privatization with Investment Funds: an Institutional Analysis," The World Bank, Washington, May, 1998.

[14] Voucher privatization, widely employed in Russia at the insistence of the IMF, the World Bank and the Sachs group, virtually destroyed the industrial capacity of the country. An industrial base that moved Russia from a feudal economy to the second most powerful industrial nation in approximately fifty years was all but destroyed by voucher privatization in fewer than ten.

[15] Josef C. Brada, "Privatization is Transition--Or is it?" *The Journal of Economic Perspectives*, Vol. 10, No. 2. (Spring, 1996), pp. 67-86.

These fears were well-founded. Over the course of the following two years it emerged that a single Czech financier, Viktor Kožený, had manipulated the assets of the sizable IPFs he had established and transferred their assets to his offshore corporations, beyond the reach of his investors. While establishing the Harvard Funds, as his IPFs were known, Kožený assembled a team of international lawyers and financiers to help with acquisitions and investments, which developed expertise in the steps necessary to corner the market on vouchers, manipulate their value and transfer the value of formerly state-owned enterprises abroad. On January 1, 1994, Kožený left Prague, never to return. He continued to control his Czech operations from abroad and by sometime in 1996 had 'tunneled' an alleged US$1 billion of his investors' assets into offshore entities over which he exercised control without accountability.

By late October, 1995, the Czech press was reporting on Kožený's links to the US entrepreneur Michael Dingman, and Czech authorities were investigating Kožený's Harvard Funds, as well as his transfer of assets to Dingman. One year later, an article sharply critical of Kožený appeared in Fortune magazine and deemed him the "Pirate of Prague," a moniker he has yet to lose.[16] Within three years of the two-step process that privatized Czech assets, the economy faltered and GDP growth turned negative. By 1997, the model privatization process had imploded and both political and financial crises hit the Czech Republic, occasioning a drastic cut in public expenditures. Much of the loss in capital markets was directly or indirectly attributable to the financial machinations of Kožený, through the Harvard Funds.

It became clear from the Czech case that the effect of poor corporate governance and the lack of mature regulations and effective enforcement in the capital markets meant that the investment funds established to concentrate ownership and prepare firms for the market economy gutted them instead. One of voucher privatization's strongest critics, David Ellerman, then at the World Bank, not only believed that voucher privatization with investment funds had been a mistake, but that it had been a predictable one, even in the absence of meaningful political analysis.[17] When Joseph Stiglitz became the Chief Economist at the Bank in 1996, he also took up the critique: he confronted Sachs and his voucher privatizers with the growing body of evidence from Russia and Eastern Europe of the negative impact of their theories.[18] In the targeted region, the institutional vulnerabilities of voucher privatization could prosper, and the political environment allowed a financial operator like Kožený access to privileged information and influence. The result, in Stiglitz' view, was ruinous for those who had sold their vouchers and for the industrial base in which they thought they had invested. Specifically referring to the Czech Republic, Stiglitz wrote:

> "The Czech Republic received accolades early on from the IMF and the World Bank for its rapid reforms; it later became apparent that it had created a capital market which did not raise money for new investment, but allowed a few smart

[16] Charles P. Wallace et al., "The Pirates of Prague," Fortune, December 23, 1996.
[17] Ellerman, "Voucher Privatization with Investment Funds."
[18] Joseph Stiglitz resigned from the World Bank in 2000, the year before he won the Nobel Prize in economic sciences.

money managers (more accurately, white collar criminals – if they did what they did in the Czech Republic in the United States, they would be behind bars) to walk off with millions of dollars of others' money. As a result of these and other mistakes in its transition, *relative to where it was in 1989,* the Republic has fallen behind – in spite of the huge advantages in its location and the high level of education of its populace [emphasis in original].[19]

The Republic of Azerbaijan

With an economic debacle in the Czech Republic on the horizon, as Viktor Kožený demonstrated the vulnerability of voucher privatization plans to corruption, the government of Azerbaijan adopted the same method to transform its command economy to a market-driven economic system. In 1995, the Azeri Parliament approved a privatization program proposed by the President. Over 70 percent of state enterprises (based on both value and employment figures) were to be transferred to private hands. After the initial wave of sales that focused on small enterprises, attention turned to the privatization of medium-size and large enterprises in 1997.

IDA and the Petroleum Technical Assistance Project

An early IDA loan that partially disbursed in Azerbaijan was the Petroleum Technical Assistance Project (PTAP). The Board of the Bank approved a credit of US$20.8 million on April 20, 1995. The implementing agency for the project was SOCAR, and it was to participate in establishing i) legal institutions for a market economy, and ii) infrastructure services for private sector development. These outcomes were to contribute to the broader development goal of creating a favorable climate for foreign investment in the energy sector.[20]

That same year, the Azeri government and the Bank's analysts had determined that capital for the refurbishment of existing oil fields and exploration of new ones would come from the private sector. Technical assistance (TA) provided through the PTAP was to create the institutional capacity necessary to manage anticipated private sector investment in the oil sector. According to the Memorandum of the President, written as a preface to the TA, the objectives of the exercise were to:

a) accelerate foreign private investment and financial participation in petroleum exploration and production by providing technical assistance to SOCAR;
b) strengthen petroleum subsector institutions through development of petroleum legislation, training, and improvement in information systems; and

[19] Joseph Stiglitz, *Globalization and its Discontents,* W.W. Norton, New York, pp. 185-186.
[20] Petroleum Technical Assistance Project, Project Performance Assessment Report, World Bank, Washington, April 27, 2006.

c) prepare investment projects in the petroleum subsector, through joint studies between SOCAR and foreign advisors.[21]

On November 30, 2000, the credit closed, however, and US$11.5 million in funding was cancelled. When the TA was assessed by the Bank after cancellation, the Implementation Completion Review (ICR) rated both the borrower's and the Bank's performance as 'satisfactory.' But when the project's performance was re-evaluated in 2006, a more independent team changed both the Bank's and the Borrower's rating to 'unsatisfactory.' This second evaluation team wrote, somewhat delicately, "[T]he significant policy conditions exceeded the limited capacity of the implementing agency and the government. As a result, the ability to achieve the project's main objective was substantially weakened."[22]

The evaluation's conclusions were telling: apparently, efforts to promote a legal framework for private investment through legislative action were unsuccessful for lack of 'borrower ownership and capacity.' In plainer language, the government of President Aliyev was not committed to such regulation and proved unwilling to allocate the resources necessary to implement it. In addition, the project's execution unit lacked the autonomy and authority to manage the finances allocated for its use. While describing a scenario in which a government passively rejected transparency and disclosure mechanisms in its energy sector development, the twenty-plus-page report did not include a single allusion to corruption. On the contrary, the Bank's diagnosis of the future prospects for private-sector led expansion in the petroleum sector was optimistic. Problems of 'governance' and public sector management were relegated to secondary consideration, if they were considered at all.

The Economic Reform Program

In November, 1995, the IMF approved a US$138 million stand-by credit to support Azerbaijan's 1995-96 economic reform program. Among the primary goals of the program were the achievement of rapid progress in privatization, and the initiation of the enterprise restructuring process.[23] The IMF announced that the distribution of vouchers for mass privatization of medium to large-scale enterprises would start by the end of March 1996.[24] In addition, Azeri authorities would develop a restructuring program that drew on the experience gained in the other former Soviet republics.

By this time, David Ellerman at the World Bank had already made the argument that voucher privatization, a part of the 'shock therapy' advocated by Jeffrey Sachs, did not

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[21] Technical Annex, Azerbaijan, Petroleum Technical Assistance Project, World Bank, Washington, D.C., March 28, 1995, p. 5.

[22] The ICR does not appear on the World Bank's website, but its conclusions are cited in the Project Performance Assessment Report, Azerbaijan Republic, Petroleum Technical Assistance Project (Credit 2708-Az). World Bank, April 27, 2006, p. ix.

[23] "IMF Approves Stand-by Credit and Second STF Drawing for Azerbaijan Republic," http://www.imf.org/external/np/sec/pr/1995/pr9558.htm.

[24] Distribution actually began in March, 1997 and originally the vouchers were to expire on August 15, 2000.

lead to the constructive restructuring of non-profitable state enterprises. The investment funds that ultimately controlled the vouchers did not control a large-enough share of the companies in which they invested to make it worthwhile for fund managers to devote their energies to the daunting task of restructuring. Instead, Ellerman wrote, these managers would 'tunnel' out the value of existing assets, leaving behind eviscerated shell companies.

Despite the arguments and the dismal example of the Czech privatization, the IMF and the Bank were set to run the same play again. Voucher booklets were distributed to Azeri adult citizens in 1997. Foreign investors who wished to participate in the program were obliged to buy options, in addition to the vouchers. Both were tradable but had no face value. Companies to be entered into the program were selected by the Office of the President, the Cabinet of Ministers, or the State Property Committee (SPC), but they were not named as the program began.

Not only was the play the same as it had been in the Czech Republic, but one of the key players was also involved again: Viktor Kožený. While Kožený's profits from his Czech experience had been substantial, Azerbaijan's program represented a considerably larger gain. As the program launched, news reports circulated speculating that SOCAR would be included among the enterprises to be sold. Although SOCAR was encumbered with debt, overmanned by staff, and saddled with dilapidated and deteriorating infrastructure, its assets still proved potentially attractive. In fact, potential investors in the privatization program and members of the SPC referred to SOCAR as the 'crown jewel' of Azerbaijan's state-owned enterprises. SOCAR held a 10 percent stake in the AIOC and would negotiate a 25 percent stake in the Baku-Tbilisi-Ceyhan (BTC) pipeline financed by the IFC at the Bank. In addition, any newly discovered reserves – not already committed under existing agreements – would belong to SOCAR. Estimates of potential returns for investors were in the billions of US dollars.

In 1996-97, then, the Azeri privatization program was approved and funded by the IMF, the political reforms required to give Azerbaijan a patina of democratic government had been implemented, and vouchers were to be printed and distributed. At the same time, Viktor Kožený's team of international lawyers and accountants, which had successfully manipulated the Czech privatization program, was still in place, and he had accumulated the capital necessary to begin acquiring vouchers and options in Azerbaijan.

III. The Kožený Operation in Azerbaijan and the World Bank

In October, 1997, circumstances converged to facilitate a Kožený operation in Azerbaijan that would be at least as profitable as the one he had executed in the Czech Republic. Standing between him and a windfall, however, were three problems of perception. Because Kožený relied on appearance and persuasion to attract investors, all of these issues were significant and documents show increasing preoccupation within his team in Baku. Before the Azeri privatization program developed much farther, Kožený had to convince:

- World Bank officials working on technical assistance in Azerbaijan that the privatization program was a credible one;
- High-level Azeri officials that he should be allowed to participate in the program as a buyer of vouchers and options despite his dubious record in the Czech Republic;
- Investors that the program would include the State Oil Company, SOCAR, the 'crown jewel' of state assets.

Kožený would solicit investments in his offshore companies, based on the likelihood that these companies could purchase enough options and vouchers to gain control of SOCAR,[25] when President Aliyev issued the decree privatizing it. He accumulated the physical vouchers in a vault in the "investment bank" that he had established in Baku, which he showed to investors from time to time.[26] He did not inform his investors, however, of the true price of the options and skimmed the considerable difference between what investors paid him per option and what he paid the SPC. Whether he kept all proceeds or, as is alleged in a US Government Indictment, split the difference with SPC officials or the Aliyevs, is still unknown.

The first perception problem – a credible privatization program – was paramount. In 1997, with the Russian economy on the verge of collapse, voucher privatization, as a scheme, was difficult to defend. Moreover, the SPC presided over the process, and the World Bank Country Manager in Azerbaijan believed the Chairman and the Vice Chairman to be corrupt.[27]

The second and third problems surfaced repeatedly in 1997 and 1998. Informed World Bank staff members informally disparaged the Azeri voucher program and observed that SOCAR would not be among the enterprises sold or auctioned by the state. If Kožený could not counter these impressions he could incur substantial losses. He had already created investment funds and started stockpiling vouchers and options in Azerbaijan, operating on the conviction that he could persuade potential shareholders in his investment funds of the likelihood of SOCAR's sale. In resolving his difficulties, Kožený and his legal team determined that a key ally would be James Wolfensohn, President of the World Bank. Because of the tarnished reputation of the Aliyev government, Kožený needed the Bank's vote of confidence in the privatization program

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[25] While SOCAR was to be the primary target of Kožený's investment companies, acquisition of other large state-owned Azeri enterprises was also contemplated. These other targets, however, such as Aztelecom, and Aznergo, were seen as providing less than half the return that SOCAR could generate (Report of Clayton Lewis to Leon Cooperman of Omega Advisers, March 22, 1998).
[26] Shafik Gabr, Proffer, February 7, 2002. "Gabr saw with Kožený the room in which Kožený's "coupons" were stored. The coupons were stored in boxes, which, in turn, were stacked "up to the ceiling". Gabr recalled this fact because he recalled thinking at the time, "Are these really coupons?" then looking into the boxes to check. Gabr did not recall separately reviewing documents that may have confirmed the size of Kožený's voucher holdings."
[27] Ayşe Güneş-Ayata, Ayca Ergun, Isıl Çelimli. *Black Sea Politics: Political Culture and Civil Society in an Unstable Region*, I. B. Tauris, 2005, p. 108

in order to make the voucher venture attractive to his investors. Given the visibility of the fraud in the Czech Republic, he also needed an unequivocal expression of confidence from a credible high-level Bank official to present to the Azeris. He also needed the Bank's good offices to present a convincing case for the privatization of SOCAR.

A. *The Campaign to Sanitize Kožený's Reputation*

Despite its inability to make political pronouncements, the Bank was the institution best-placed to assess the risks inherent in the Azeri privatization program and the reliability of an international investor like Viktor Kožený in the mid 1990s. The internal debate at the Bank about the integrity of voucher privatization as a method was intense, and after 1996, it involved Joseph Stiglitz, the Bank's Chief Economist who was increasingly outspoken in opposition to vouchers. Stiglitz' advisers called Jeffrey Sachs the P.T. Barnum of privatization, whose voucher scheme survived only because "there's a sucker born every minute." Many Bank staff members working on privatization in the former Soviet republics were also familiar with the history of the voucher fraud in the Czech Republic because the Bank had been deeply involved.

In the early 1990s, Czechoslovakia received a World Bank Structural Adjustment Loan (SAL). The SAL had been made in the amount of US$450 million in 1991, US$300 million of which was transferred to the Czech Republic when it split from the Slovak Republic. The reform program financed by the SAL was to effect a rapid transition to a market economy through the mass privatization of state owned enterprises, deregulation, and price and trade liberalization.

The Bank had also assessed the effectiveness of reforms implemented as a result of the policy advice and the funds made available through the SAL, although the reports issued by the Bank on the Czech voucher privatization program varied widely in the conclusions they drew.[28]

In addition, the Bank operates in geographic regions, where staff members are assigned to a set of contiguous countries and address development topics that use their expertise. Staff members with experience in voucher privatization assigned to the Europe and Central Asia Region (ECA), which includes both the Czech Republic and Azerbaijan, could be expected to work in both countries. In short, Bank staff members working on privatization in the Czech Republic would have been aware of problems inherent in the subsequent Azeri program. They might also be expected to recognize Kožený's role in the fraud that had disrupted the Czech transition and to detect his presence when he resurfaced only three years later in Baku.

Documentation shows that, in October, 1997, Kožený's reputation as "The Pirate of Prague" was circulating in Baku, and at that point, he had already begun the transactions necessary to become a major participant in the voucher program. He began establishing

[28] See "Investment Funds in Mass Privatization, Lessons from Russia and the Czech Republic," *Viewpoint,* World Bank Group, April, 1997. Also "Ownership and Corporate Governance – Evidence from the Czech Republic," *Viewpoint,* World Bank Group, May, 1997.

operations in Baku in May, 1997 and had accumulated nearly US$40 million in vouchers by September. The two major investment funds created for this purpose were Oily Rock Group Ltd., named for the outcropping of rock in the Caspian Sea that marked the location of major oil deposits, and Minaret Group Ltd. Through his operatives, Kožený was purchasing privatization vouchers and options using US currency flown by private or chartered jets into Azerbaijan.

According to correspondence and documents concerning this period, Kožený became alarmed when he was informed by his team in Baku that Bank staff members, either resident in Azerbaijan or traveling there for specific missions, believed that the privatization process would be fraudulent and that he, himself, was corrupt.[29]

Because one of the features of mass privatization that made it attractive to governments and to the Bank was the rapidity with which it could be implemented, this development disturbed Kožený immediately. If he were to profit from his growing stock of vouchers and options, then privatization had to proceed, and he had to ensure that he was a presentable participant in order to become a major beneficiary.[30]

At this point, Kožený mobilized his contacts and associates to conduct a campaign designed to launder his reputation and vouch for the Azeri privatization program using the President of the World Bank. Kožený would provide senior Azeri officials and SPC members with at least neutral, if not positive, information about himself from the highest levels of the Bank. Memos written by Kožený's colleagues show that this was an elaborate strategy. His allies felt that the Bank's Country Manager, Tevfik Yaprak, was especially hostile to Oily Rock and Minaret, as well as to the 'non-transparent' way in which the Azeris were privatizing and that therefore, Yaprak's opinions had to be censored. Interviews conducted recently suggest that the Bank staff members in question were unaware that a campaign was underway to silence them.

Christine Rastas, a Minaret employee, collected key intelligence in Baku and Washington, D.C. for the Kožený team about the opinions and likely actions of the Bank. She and others believed that they could be successful only if they managed to eliminate Yaprak from the communications between the Bank and the Azeri government regarding both Kožený and privatization. She wanted a positive assessment of the entire process from the Bank and feared that Yaprak would sabotage efforts to secure one. On October 31st, 1997, she wrote a briefing memorandum warning about the problem with Yaprak, and articulating a plan for addressing it:

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[29] Correspondence between Viktor Kožený and Christine Rastas, October 31, 1997. Also, correspondence between Viktor Kožený and Barat Nuriyev of the SPC, November 13, 1997. The World Bank staff members named were Joseph Saba, Tevfik Yaprak, and Igor Artemiev.

[30] Kožený was also under significant financial pressure to quickly 'turn' his investment. He had initially funded his investments in Azerbaijan with his privatization proceeds from the Czech Republic. However, at the start October, 1997, Kožený had just drawn down US$29,000,000 of a US$50,000,000 credit line from Russia's Alfa Bank. The credit facility was established to invest in Azerbaijan and included a structured option agreement that would allow Alfa Bank to assume much of Kožený's Azeri investment should it succeed. However, the facility also carried an 18% interest rate and was valid only to the end of 1997.

> The conclusion I've drawn from all of this is that we should not have too much trouble persuading the World Bank to issue a favorable statement about the performance of Azeri Privatization officials as long as we do not raise the ire of the local representative. Hence we have asked our local staff to keep their distance from him and not engage in any controversial discussions on the subject. On your side, if we are able to arrange some sort of meeting or assistance with your friend, I would recommend that you try to avoid any discussions that call for comment on or the involvement of the local representative. Our aim is to keep the discussion at high levels at the Bank and out of range of any local turf disputes.
>
> In addition to the efforts you are making to engage your friend on this issue, [Kožený attorney] Hans [Bodmer] in Zurich has also been pursuing additional contacts at high levels [of the World Bank] via a Washington Law firm. Unfortunately, the status and details of that effort are not yet available...
>
> In summary, we are looking for friendly relations between the highest levels of the World Bank and Azeri Privatization officials and maybe an official statement of endorsement to make the latter feel more comfortable. If we can also achieve good relations for ourselves in the process, we would be happy.[31]

Additional documentation shows that the 'friend' to be approached for a meeting or assistance was James Wolfensohn.

Among his associates and investors, Kožený relied first on Freddie Botur to provide him with privileged access to Wolfensohn. Botur, the recipient of the memo above from Rastas, was a fellow Czech émigré and the owner of Tennisport, a New York City landmark where Wolfensohn played. He had also invested US$100,000 in the Oily Rock Group and planned to invest more. The record shows that Botur met with Wolfensohn on October 31st, 1997, the same day he received the Rastas memo. The two men met for about one hour to go over the points raised in the Rastas memo, a copy of which Botur gave to Wolfensohn. At this point, Wolfensohn was fully apprised of the Kožený team's internal plans for manipulating Bank policy, plans and statements regarding Azeri privatization.[32] Using the Rastas memo, Botur apparently informed Wolfensohn about what Kožený needed from the World Bank.

A second contact who helped Kožený gain the access he needed at the Bank was Graham Wisner, a lobbyist for Patton Boggs in Washington, D.C. and the brother of then US Ambassador to Egypt, Frank Wisner. Through his brother, Graham Wisner knew Egyptian billionaire and Kožený co-investor Shafik Gabr, who knew the 'number two and number three' at the Bank. In the fall of 1997, Graham Wisner and Kožený worked together to separate Bank leadership from the news disparaging both the Azeri program

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[31] Memo from Christine Rastas to Freddie Botur, October 31, 1997.

[32] Fax from John Pulley, Kožený's bodyguard and assistant, to Hans Bodmer, November 1, 1997, relaying Kožený's message to Bodmer: "Mr. Botr provided him [Wolfensohn] with a copy of the memorandum written by Christine Rastas in Baku that outlines the problems."

and Kožený coming from the Bank's own Central Asia team. Correspondence from Graham Wisner to Kožený's Swiss attorney and currency courier, Hans Bodmer, on November 6, 1997 reads, "I have established excellent contacts at the World Bank who are directly monitoring the mission to Baku. The decisions and recommendations are to be made in Washington, D.C. and not in Baku by local reps." [33]

On November 13th, 1997, the communications and meetings designed to clear the way for Kožený as a major investor in the Azeri privatization program apparently hit a major obstacle: a letter from Barat Nuriyev, Deputy Chairman of the SPC in Azerbaijan, to Kožený himself. In part the letter read:

> I am sorry to have to write this letter to you but the State Property Committee is the organisation in Azerbaijan responsible for the process and consequences of privatisation.
>
> Two or three weeks ago, I was discussing the privatisation problems with Mr. Tevfik Yaprak, the World Bank's representative in Azerbaijan. During the conversation we touched on many issues of privatisation and to my surprise Mr. Yaprak mentioned your name in the most negative sense, claiming you to be the speculator and the person having problems with Interpol among other things. To be frank, at this time I thought this information was passed to Mr. Yaprak by the foreign investors who consider your group as a serious competitor, but 3 days ago I met the World Bank's representative from the mission Joseph Saba and Igor Armetiev and they, unfortunately, repeated the words said by Mr. Yaprak emphasising that you are wanted by Interpol and have a criminal record in the Czech Republic. Finally, they told us that your group is not a desirable company to participate in the privatisation in Azerbaijan.[34]

The letter went on to explain that the World Bank was an important partner in privatization for the Azeri government and that the opinion of its representatives could not be dismissed. Nuriyev asked Kožený to provide information establishing "....that the opinion of the World Bank representation is not factually correct."[35]

In light of ensuing events, this letter can be read in one of two ways. On the one hand, it might have been a subtle assertion of the SPC's potential power over Kožený. On the other the letter could have been a complex pretext used to approach Wolfensohn at the World Bank and solicit his direct support in silencing the Bank staff members. Documents and correspondence written in October show that Kožený and his attorneys were actively collaborating with high-level SPC officials in an international effort to rehabilitate his reputation.[36]

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[33] Correspondence between Graham Wisner and Hans Bodmer, November 6, 1997.

[34] Correspondence between Barat Nuriyev and Viktor Kožený, November 13, 1997.

[35] At the time, the opinion was, in fact, mistaken. Kožený was under investigation by Czech authorities in 1997, and had not been convicted of a crime.

[36] Correspondence between Viktor Kožený, Tom Farrell, Andre Wahrenberger, Hans Bodmer, Frank Chopin, Nadir Nasibov, Vaclav Klaus, Gerald McConnell, and Jiri Weigl (a Czech Minister and advisor to Vaclav Klaus), October, 1997.

The day Nuriyev wrote the letter, Kožený flew from Baku to Moscow to meet with Andre Wahrenberger, one of his attorneys, to consolidate a course of action that would counter the negative impact of cautionary remarks made by World Bank staff members in Baku. According to Wahrenberger, the allegations about Kožený were made in a meeting, and others who had been present were prepared to confirm the fact. As the result of consultations with Kožený in Moscow, Wahrenberger wrote to Kožený's US attorney, Frank Chopin, outlining a strategy for securing support from Wolfensohn. The plan laid out a series of potential courses of action, but the team ultimately decided that an audience with Wolfensohn for Kožený was the best option. Initial contact was to be personal and informal, with an official meeting later, as a follow up. In preparation for the first meeting Kožený was to arm himself with a list of questionable investments or financial transactions that Wolfensohn had made in the past. In addition, Kožený was to solicit assistance from Wolfensohn in silencing Bank staff members, including having Yaprak, Saba, and Artemiev quietly "removed," presumably from their assignments involving Azerbaijan.[37]

The Nuriyev letter occasioned a flurry of activity within the Kožený camp. Correspondence among Kožený, Bodmer, and Graham Wisner over the course of the following two weeks suggests that Wisner's contacts at the Bank were also used to influence opinion there about Kožený. More significantly, on the 25th of November Kožený began a trip that took him from London to Moscow, to London, to New York and back to London. When he arrived in New York, at 9:20 am on November 30th, 1997, Kožený had been in the air for approximately fourteen hours. He remained on the ground for four hours, and flew back to London on the Concorde at 1:45 p.m. Travel documents show that the four hours Kožený spent in New York on November 30th are the only time he spent in the United States between November 13th and mid December.

On December 9th, James Wolfensohn sent a letter to Viktor Kožený, addressed to his office for the Minaret Group in Baku, Azerbaijan. The letter read:

> Thank you for your visit and for bringing to my attention your concern regarding the letter addressed to you by Mr. Barat Nuriyev, Deputy Chairman of the State Property Committee of Azerbaijan, dated November 13th, 1997.
>
> I have asked Johannes Linn, the Vice President for the World Bank's Europe and Central Asia Region, to look into the facts underlying the case. He has established with the World Bank staff referred to in the letter that they did not make the statements to Mr. Nuriyev which were attributed to them in the letter. In particular, they did not state that it would be inappropriate for the Azerbaijan authorities to do business with you or that you were wanted by Interpol. They did advise Mr. Nuriyev that it is important for his agency to take the appropriate steps of due diligence in reviewing the records of potential investors with whom the

[37] Correspondence from Wahrenberger to Frank Chopin, November 14, 1997.

> agency considers to do business. Mr. Linn has written to Mr. Nuriyev to that effect. A copy of the letter is attached.[38]

Wolfensohn enclosed a copy of the letter written by Johannes Linn to Barat Nuriyev, which read, in part:

> I have discussed this matter with the staff concerned, Messrs. Yaprak, Saba and Artemiev, who informed me that they did not make such statements to you nor do we have any evidence to this effect.[39]

In light of Kožený's travel itinerary during this period, it appears that Wolfensohn met with him in New York on November 30th and that there the Bank's reservations about the integrity of Viktor Kožený as a major investor in the Azeri privatization process were resolved. Nine days later, Wolfensohn wrote the letter to Kožený assuring him that World Bank staff had not maligned him and that "the facts underlying the case" would be investigated by Johannes Linn. Interestingly, Kožený did not appear to be worried about the investigation by Linn. He was evidently confident that it would be conducted narrowly: Linn would determine only what the staff members involved did or did not say about him. Even a casual inquiry would have linked Kožený immediately with his questionable activities in Prague and substantiated that Nuriyev was justified in being uncertain about him. Kožený, however, seems convinced that this aspect of the incident would not be the focus of Linn's investigation.

World Bank Staff Members Respond

When interviewed on June 25th, 2008, about his role in the privatization episode in Azerbaijan, Johannes Linn said that he had never heard of Viktor Kožený, although he remembered that there had been problems with voucher privatization in the Czech Republic. Linn, now executive director of the Wolfensohn Center for Development in Washington, D.C., also said that the reservations, at the Bank, about privatization schemes would have been beneath Wolfensohn's 'radar screen' and that the particular concerns of an individual financier, such as Kožený, would not have been considered sufficiently important to engage the attention of the World Bank President.

Joseph Saba, one of the Bank staff members to whom Nuriyev attributed warnings about Kožený, denied, when interviewed on June 30th, 2008, that he had ever mentioned Kožený, or any other individual investor, by name to the Azeri SPC officials. He said that he had been worried only about the design of the privatization program; if the public perceived that auctions and vouchers were gimmicks or that privileged investors could corner the market on vouchers, the entire privatization exercise would be undermined. Saba mentioned particularly the problems that might ensue if the public should come to believe, for whatever reason, that foreign investors had enjoyed an unfair advantage in acquiring state assets. Saba was unaware that Nuriyev had written a letter to Kožený

[38] Correspondence between James Wolfensohn and Viktor Kožený, December 9, 1997.
[39] Correspondence between Johannes Linn and Barat Nuriyev, December 9, 1997.

about statements he, Saba, had made and did not know that Wolfensohn had been involved personally in the episode.

In contrast, Tevfik Yaprak, when interviewed in April, 2007, cited his own impressions about Kožený and his associates buying up vouchers in the belief that SOCAR would be privatized. He characterized these activities as a "frenzy," but said that his observations would have been oral or "back office reports" between Baku and Washington. Ironically, while Yaprak perceived these informal messages and exchanges to be harmless, these were precisely the kinds of communications that most preoccupied Christine Rastas at Minaret, Andre Wahrenberger, and Kožený himself.

Igor Artemiev, the other Bank official mentioned in the Nuriyev letter to Kožený would not be interviewed. In response to a written request for information, he replied, "I do not recall preparing any evaluations of the program and, if I was involved in writing documents, I certainly did not keep any copies…."[40]

Repeated calls to James Wolfensohn were not returned.

Kožený's Reputation Rehabilitated

Although both Rastas and Nuriyev reported that three Bank staff members had warned the Azeris and visiting investors about Kožený on different occasions, and Yaprak reported his own skepticism about the privatization scheme and about Kožený, Wolfensohn wrote the December '97 letter to Kožený denying these negative remarks had been made. With his written exoneration from Wolfensohn in hand, Kožený then undertook a concerted effort to enlist US investors in his voucher funds in Azerbaijan. On December 22, 1997, he threw an opulent Christmas party at his house in Aspen that netted an expanding circle of reputable supporters and allies, including Frederic Bourke, who was to denounce the operation as a fraud a year later. James Wolfensohn, referred to in Kožený's notes as a friend of fellow invitee Freddie Botur, was invited to the party, but he declined to attend.

The second meeting between Kožený and Wolfensohn took place as a formal encounter, in keeping with Wahrenberger's original plan. On March 10th, 1998, in Washington, the two men met again, apparently with Nadir Nasibov, the Chairman of the Azerbaijan SPC. Nasibov had made a speech earlier in the week at the Third Annual Conference "Investing in Russia and the CIS" in New York, attended by Kožený's investment team. In his speech to the conference, Nasibov promoted the likelihood of significant returns on investments in his country's energy sector and characterized the financial activity in the Caspian as "the last great oil rush of the twentieth century." Following the conference, Nasibov and Kožený met with Graham Wisner in Washington, the lobbyist who had successfully ensured that the headquarters mission to Baku the previous November would not allow local World Bank staff in Azerbaijan to make recommendations about the

[40] Correspondence with Paul Vaca, June 11, 2008.

privatization program. They then met with Wolfensohn, but the purpose of this meeting is unknown.[41]

B. *The Campaign for the Privatization of SOCAR*

Staff members of the World Bank who are well-positioned to understand the less transparent actions of their counterpart governments are the Country Managers and Resident Representatives. These officials are usually stationed in the borrowing country, typically for a period of years, they debrief Bank missions working on specific projects and meet regularly with high-level country officials both professionally and socially. At the outset of the privatization program in Azerbaijan, the then World Bank Representative Kutlay Ebiri was skeptical about the circulating rumor that SOCAR would appear on the list of state enterprises to be sold. Ebiri, stationed in Azerbaijan from 1996 until mid 1997, told interviewers that SOCAR "....[W]as feeding the President's family, the bagmen, the [President's] relatives....SOCAR was beyond any discussion of privatization."[42]

Ebiri's successor, Tevfik Yaprak, who had arrived in Baku in mid 1997 and who had alarmed Christine Rastas by his hostility to Kožený, was also outspoken about his belief that the Aliyevs would not allow SOCAR to be sold. In Yaprak's opinion, the entire program was corrupt, and the idea that the Aliyevs would include SOCAR on the list of enterprises to be sold was absurd. [43] When asked if he had ever believed that SOCAR would be privatized by President Aliyev, Yaprak told interviewers, "Who in their right mind would privatize their major stream of income?" He was quite adamant: he had never heard any senior official mention the intention to privatize SOCAR.[44] Yaprak also pointed out that, to his knowledge, the privatization of SOCAR had never been cited in MULKIYYET, the official publication of the privatization committee, where target enterprises were listed. In addition, he had told the US and the British ambassadors to Azerbaijan that the privatization of SOCAR would not occur. In an interview, Yaprak mentioned Azeri government officials who were concerned about the process and wished to reform it. In particular, he referred to Vahid Akhudov, who had been the head of the state police in Baku and who became the State Economic Policy Advisor to the President. According to Yaprak, Akhundov was vocal about his belief that the entire privatization program was a 'scam' and was 'hurting the country.' Finally, Yaprak told interviewers, "Vouchers were a joke." Privatization, such as it was, had become an inside deal. In reference to the vouchers, Yaprak said, "Politically influential people captured them."[45]

Yaprak's view, as well as Ebiri's, about SOCAR's prospects was shared by Joseph Saba, a World Bank Specialist who worked on the privatization program in 1997 and 1998, and

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[41] In a March 17th, 1998 conference call with Kožený, Bodmer, and others, Nasibov would note that World Bank officials did not like that he met with Wolfensohn.
[42] Interview with Kutlay Ebiri, World Bank Resident Representative, Baku, Azerbaijan, May 3, 2007.
[43] In an April 26th, 2007 interview, Yaprak called the Azeri privatization process "a total scam".
[44] Interview with Tevfik Yaprak, April 26, 2007.
[45] Ibid.

whom Barat Nuriyev had mentioned in connection with concerns about Kožený's integrity. According to Saba, SOCAR was not to be included in the program "in the early days." He did not believe that it was necessary to privatize a key asset, such as the state oil company. SOCAR should have been assessed and audited first to determine which parts of the company were functioning efficiently, and which were not, before any decision on privatization in the beginning of the program. Saba pointed out that, so far as he knew, such analyses had not been conducted at that point.

To profit from the privatization program, the Kožený team had to contest these opinions and foster the perception that SOCAR would be privatized. Once again, Wolfensohn was enlisted. Barat Nuriyev, the author of the letter to Kožený about warnings from Bank staff members, requested a meeting in Washington in late 1997 or early 1998. According to Kutlay Ebiri, Wolfensohn only met with Nuriyev because a close friend insisted that he do so. After the meeting, Ebiri concluded that Nuriyev's purpose in the meeting was to assure Wolfensohn that the privatization of major assets in Azerbaijan would soon occur.[46]

Then in March, 1998, Wolfensohn met with Kožený again, together with Nadir Nasibov, just after Nasibov pitched the Azeri privatization program to the investors' conference in New York. At the conference Nasibov told his audience:

> The top priority of the current period and coming years is to improve the quality of current pipeline of assets for medium-scale privatization and to prepare attractive large-scale SOEs (State Owned Enterprises) for corporatization and case-by-case privatization. In this respect, preliminary work has been done, initial legal and standard basis created, enterprises, which shall only be privatized upon a special decision of the President, selected (power, heat and gas suppliers, chemical and metallurgy enterprises, machine building, enterprises for wine, brandy, tobacco, tea and fish processing).[47]

While he did not mention SOCAR by name, his allusions to it earlier in the speech were noteworthy. He pointed out that five PSAs had been signed by President Aliyev between 1994 and 1997, including the 'deal of the century,' and that an additional four oil contracts worth approximately US$10 billion had been signed in Washington in August, 1997. He assured potential investors that the privatization program was legitimate and characterized it as "....incorporated within the framework of comprehensive reforms," including trade liberalization and a tolerant foreign investment climate. At the outset, he emphasized to his audience that investment opportunities in Azerbaijan were supported by the World Bank, through its Structural Adjustment Credit, as well as by the IMF. Finally, Nasibov explained the terms for foreign investors' participation in privatization through the purchase of options to buy vouchers. He mentioned that some twenty million options had already been sold and that investors could be certain of lucrative returns. The government, he said, would make available "....high grade quality assets for

[46] Interview with Kutlay Ebiri, May 3, 2007.
[47] "Investment Opportunities in Azerbaijan," presentation of Nadir Nasibov to the "Investment in Russia and the CIS" March 4, 1998.

privatization."[48] Because of Nasibov's focus, in his speech, on the profitable potential of investments in the oil sector, investors primed by Kožený would understand this last reference to be an allusion to SOCAR as an asset that would be sold.

By March, 1998, then, vouchers were distributed and being resold in Azerbaijan, Kožený was already attracting large scale investments from the US in his voucher and option ventures, Oily Rock and Minaret, and, with help from Wolfensohn, he had successfully established himself with the SPC in Azerbaijan as a reliable privatization participant. For his part, Wolfensohn had met with Barat Nuriyev and Nadir Nasibov, the Chairman and Deputy Chairman of the SPC, respectively, lending each of them a certain amount of respectability despite Yaprak's warnings, and with Kožený twice. He had also obliged the Bank's Vice President for ECA, Johannes Linn, to write on Kožený's behalf to Nuriyev acquitting Kožený of any implication of wrongdoing. At the same time, however, the drumbeat of criticism about the privatization program in Azerbaijan continued inside the Bank.

The investors' conference in New York and the March meeting with Wolfensohn took place in an environment of increasingly serious criticism. Although they could say nothing publicly, or even officially to internal decision-makers, Yaprak and others were concerned about the corrupt character of the government and the close relationship between the SPC and President Aliyev's office. Tevfik Yaprak apparently wrote a letter and made statements to the effect that the officials responsible for the process were corrupt and that the process itself had been subverted to support the financial interests of the Aliyevs and their cronies. According to the notes of one Kožený associate, the World Bank "Turk" sent a letter to Wolfensohn saying that the Chairman and Vice Chairman of the SPC were corrupt and that the Bank should sever relations with the SPC.[49] Given the sensitivity of the opinion expressed in the letter, it is not clear how Kožený's colleague would have known about it, unless Wolfensohn or someone close to him had relayed the information to the Kožený camp.

In response, the people working for Kožený were to obtain letters from clients and investors, such as Goldman Sachs, in support of the SPC and privatization.

Finally, acquiescing to an Azeri government request, Wolfensohn sent Bank staff members Gerhard Pohl, Vladomir Rudlovcak, and James Welch to Baku from September 14th through the 18th to meet with Azeri government officials and conduct an analysis of the privatization process.

The group submitted an "Aide Memoire" to Wolfensohn dated September 18th that enumerated certain difficulties with privatization in Azerbaijan, but cleared the way for continued Bank involvement despite the corruption. It did not recommend severing ties with the SPC. On the contrary, the memo set out the steps the Bank might take to improve the integrity of the process that were astonishingly naïve, under the circumstances. First the evaluators enumerated the problems with the process that were

[48] Ibid.

[49] Tom Farrell, calendar notes, May 9, 1998. The "Turk" was Tevfik Yaprak.

commonly cited in Baku and Washington: auction techniques were not secure, and the list of agencies and enterprises to be privatized was not transparent. The authors of the memo proposed that, henceforth, the Azeri government authorize and list the large firms for inclusion in the process, identify sources of financing for international advisors, and select privatization experts to assist the SPC. The memo also recommended that the Bank remain involved in the process through technical assistance loans for the sale of the largest enterprises or the provision of partial risk guarantees for investors. The memo made numerous, quite specific, references to SOCAR as a target of privatization, an inclusion that suggests that the evaluators did not consult in-country Bank staff members, in keeping with the maneuvering of Graham Wisner who had sought to isolate the local representatives. In describing the types of firms to be privatized, the memo referred to:

> [P]rofitable or potentially profitable companies, e.g. SOCAR, that would be attractive investment opportunities for voucher holders and strategic cash investors, and which will be sold to strategic buyers for cash and vouchers and to voucher-holders....

And further:

> For illustrative purposes, the privatization advisers may perhaps recommend to sell SOCAR as an integrated oil company with the present upstream and downstream assets, but may recommend to spin off the state's interests in other production sharing agreements into a separate ownership fund. Similarly, the recommendations would probably include transfer of regulatory and control functions of SOCAR to a ministry and the separate sale of some of the support businesses to strategic investors through commercial tenders.[50]

The fact that the aide memoire was found in Viktor Kožený's files indicates that Bank personnel were informally transmitting relevant internal information to him concerning the Bank's thinking about the commercial future of SOCAR.

IV. The Consequences for Investors

Leon Cooperman was Chairman and CEO of Goldman, Sachs Assets Management, when he left to develop his own US$ 3 billion hedge fund, Omega Advisers, in 1991. Seven years later, when Omega was facing dramatic losses as a result of Russia's pending default, Aaron Fleck, an acquaintance of Kožený's, called Cooperman, whom he knew from Goldman Sachs. Fleck pitched the Azeri privatization scheme to Cooperman, who delegated due diligence on the investment to his colleague Clayton Lewis.

After traveling to Azerbaijan and meeting with Kožený, Lewis reported to Cooperman that there was only a five percent chance that the investment could fail. According to Cooperman, Lewis had learned of the involvement of both the International Monetary Fund (IMF) and the World Bank in the privatization program and was encouraged by it:

[50] Azerbaijan Privatization Consultation Mission Aide Memoire, Baku, September 18, 1998.

> He also learned of the interests of the World Bank and the International Monetary fund in the privatization – both of these significant, reputable institutions worked with the Azeri government in designing its privatization program and encouraged the government to follow through on its privatization program. And it was my understanding that he and/or various members of his team spoke directly with representatives of the World Bank and IMF confirming their support for the privatization.[51]

Lewis' trip took place in March, 1998, well after Bank staff in Azerbaijan had been questioned by Johannes Linn about the negative comments they had made to an Azeri official about Kožený. Presumably, Bank staff members were unlikely, at this point, to reiterate their unfavorable opinions of the privatization program or of Kožený to anyone who might report back to either Linn or Wolfensohn.

In his account of Omega's investment, Cooperman emphasized "[O]ur primary concern was whether or not this was a real investment, whether the country was committed to privatization, and whether there was real value here for our investors."[52] These were precisely the concerns Bank staff had raised with Azeri officials, the US and UK ambassadors and visiting investors. Variously, the Country Manager and the former Resident Representative had characterized the vouchers as "a joke," the SPC as corrupt, and the scheme to privatize SOCAR as "a scam." In the spring of 1998, however, according to Omega Advisers, they were no longer alerting potential investors to problems with the Kožený endeavor.

On the strength of Lewis' recommendations and Cooperman's corresponding judgment, Omega committed US$182 million to the Azeri privatization through Viktor Kožený. In the end, Omega's investment, as well as the investments of numerous others, was lost.

V. Conclusion

By mid-1998, Kožený had accomplished his threefold mission. He had created the impression that he was a reliable participant in the voucher privatization scheme, that the SPC was a viable agency to execute the program and that SOCAR apparently would be sold, if not immediately then in the medium term.

More significantly, in late 1997 and 1998, he had achieved these objectives with what appears to be the ongoing support of James Wolfensohn, acting in his capacity as World Bank President. The Rastas memo expressing the Kožený team's fears about Tevfik Yaprak was given to Wolfensohn by his friend Freddie Botur on October 31st, 1997. The memo apprised Wolfensohn of Bank staff members' unflattering opinions of the Azeri privatization program, as well rumors that did not support Kožený's preferred view of the economic landscape. Through this memo, the President of the World Bank was

[51] Leon Cooperman, US Attorney Meeting, January 6, 2006.
[52] Ibid.

effectively briefed on the Kožený team's strategy and tactics regarding the Bank. Subsequently, Wolfensohn received, through Kožený, Nuriyev's letter questioning Kožený's integrity. Wolfensohn dealt with the information by meeting with Kožený and by transmitting a letter to him stating flatly that staff members at the Bank did not suggest to Azeri authorities that it was "inappropriate to do business" with him. Wolfensohn also gave Kožený a clear signal, with this letter, that the staff members in question had been silenced.

The chronicle of privatization in Azerbaijan, which ended in 1999 with the exposure by Frederic Bourke of Kožený's machinations, is a cautionary tale. As an institution, the World Bank was structured to detect corrupt operators like Kožený and to ensure that neither borrowing governments nor legitimate investors were defrauded by them. Over the years, mission specialists, the Resident Representative and the Country Manager of the Bank in Azerbaijan were aware of the dangers implicit in a collaboration between Heydar Aliyev and Viktor Kožený. After their initial statements, however general, Bank officials were apparently silenced, with the exception of Tevfik Yaprak, who was ignored.

All of them were overruled by a small group of powerful and influential men who, operating behind the scenes, could use men with better reputations than their own, such as Wolfensohn and Wisner, to present an investment "opportunity" that appeared to be credible although it involved "The Pirate of Prague." Any effort by Bank staff members to 'out' Kožený was, on the face of it, blocked by him through the World Bank President. James Wolfensohn's December 9th, 1997 letter was possibly the most effective maneuver used to establish Kožený's credibility. In his letter, Wolfensohn assured Kožený that the questions he raised concerning Bank staff members' remarks about him would be investigated by the Vice President of the ECA Region, Johannes Linn. Linn's investigation of staff members' comments in this context would have had a chilling effect on other Bank employees who might have otherwise been inclined to criticize either voucher privatization in Azerbaijan or Kožený. For Wolfensohn and Linn, evidently, the silencing of Bank staff members critical of corruption in Azerbaijan was the outcome desired. Corruption itself went un-remarked by either man. In the documents obtained in this case, Wolfensohn never raised any concerns about corrupt practices in privatizing Azeri enterprises, and the question of Kožený's infamous operations in the Czech Republic was not raised.

At the Bank's 1997 Annual Meeting, James Wolfensohn told his audience, "Last year, I highlighted the importance of tackling the cancer of corruption. Since then, we have issued new guidelines to staff for dealing with corruption — and for ensuring that our own processes meet the highest standards of transparency and propriety."[53] With statements such as these, Wolfensohn was on his way to becoming the first 'anti-

[53] James Wolfensohn, "The Challenge of Inclusion: 1997 Annual Meetings Address," September 23, 1997, http://web.worldbank.org/WBSITE/EXTERNAL/NEWS/0,,contentMDK:20040629~menuPK:34472~pagePK:34370~piPK:34424~theSitePK:4607,00.html

corruption' president of the World Bank. For ten years, he spoke to Third World governments on anti-corruption measures and transparency, and when he left the World Bank, he exited with accolades for finally drawing international attention to corruption as a cause of poverty.

The same year, however, that Wolfensohn first issued staff guidelines for addressing corruption, he became a 'front' for one of the most notorious of corrupt actors in the privatizing world of the former Soviet bloc countries. At the behest of friends, he lent his reputation and his institution's support to precisely the kind of fraud and theft that he so frequently denounced for its negative impact on development and its incalculable cost to the world's poor.

At the time this occurred, international organizations and financiers had experienced nearly twenty years of privatization around the world and nearly ten years of privatization in the former Soviet republics. The Sachs/Stiglitz debate on the use of vouchers had nearly run its course, and the facts supported Stiglitz: voucher privatization opened the door to fraudulent manipulation of capital markets, such as they were, and new, non-transparent and unregulated financial sectors. In 1998, the economy of Russia collapsed under the weight of a now worthless industrial sector, and the verdict was in.

Still, the Bank was poised for another round of voucher privatization in Azerbaijan. In that context, real-world experience and knowledge were buried in acronym-laden semi-public documents about 'fragile democracies' and 'factional interests.' A Bank specialist operating in Azerbaijan at the time recounted that he occupied himself with technicalities of program design and worried about the public perception of the voucher process. If Azeris believed that the auction and sale of state assets was fair, then the program was a success. If not, then it had failed, he said.

Similarly, Viktor Kožený was concerned about perception. If his investors perceived that he was legitimate, that the Azeri government was responsible, and that SOCAR would be sold, then the process was also a success for him, although arguably, not one of these things was true.

Neither Kožený nor Bank management seemed worried about what the privatization program really was: a fraud perpetrated on investors, taxpayers in donor countries, and the public in the borrowing country. SOCAR would not be sold because its off-the-books revenues supported the Aliyevs. Kožený defrauded his investors by selling them, in violation of contract, privatization options at a staggering (40x) mark-up over his own costs basis, in turn using the proceeds of this fraud to fund his own interests. And the conduct of the SPC officials was (and remains) highly suspect.

Nevertheless, a Bank bureaucrat described his mission in Azerbaijan as "ensuring that the process was carefully designed to minimize fraud," and he compared his aspirations for SOCAR management to the Norwegian state oil company. "There are many similarities," he said. Unfortunately, there are many differences, too. It makes little sense to worry about the design of a voucher program for privatization, building in safeguards against corruption, when, in reality, the head of state can decide from one day to the next which companies will be sold, and a rogue financier has a warehouse full of vouchers bought on the cheap with foreign cash. No program design is able to minimize that kind of fraud.

In late November or early December, 1997, Viktor Kožený confronted James Wolfensohn about derogatory remarks made by World Bank staffers concerning his financial operations. Kožený came to the meeting armed with potentially embarrassing revelations about Wolfensohn's past investments. He did not have allegations of wrongdoing, however, nor could his attorney's postulations about a potential defamation lawsuit on Kožený's behalf have materialized; the Bank had immunity from such lawsuits. Why, then, did Wolfensohn capitulate so readily, initiating an investigation into his employees' remarks and assuring the SPC that Bank staff had not maligned Kožený? The Country Manager cautioned Bank senior management about the frantic accumulation of vouchers in Azerbaijan at the time and warned ambassadors that the rumors of SOCAR's impending sale were false. He also wrote directly to Wolfensohn saying that the SPC itself had been corrupted that the Bank should eschew any relationship with it.

The opinions of the Country Manager were not in doubt. Kožený was already renowned as the "Pirate of Prague," and the Aliyev government was acknowledged as one of the most corrupt in the world. Still, the voucher program went forward, despite two years of internal warnings at the Bank, until a whistleblower exposed it in 1999. By that time, however, the damage was done. 'The loss to investors outside of Kožený's own core associates is estimated to be well over US$200 million, while the loss to the Azeri state and the public was inestimable.

VI. Epilogue

Privatization continues in Azerbaijan, and, when the validity of the vouchers was extended to January, 2010, the underlying vulnerability of the process to fraud remained unchanged. In 2003, the President approved a new SOCAR Charter, restructuring the enterprise, merging offshore and onshore oil and gas production, and authorizing specific offshore construction units for privatization. Between 2004 and 2006, the European Development Bank, in cooperation with the US Trade Development Agency, undertook an additional commercialization and restructuring project at SOCAR, and appointed a task force to advance the process.

On May 10, 2006, oil was first pumped from the Azeri-Chirag-Guneshli field into the new Baku-Tbilisi-Ceyhan pipeline. The inauguration ceremonies of the pipeline in Azerbaijan were held on May 25th, 2005, and the current President, Ilham Aliyev, the son of the previous president, presided. The IFC, the private sector lending arm of the World Bank, supported construction with an investment of up to US$125 million and provided up to US$125 million in additional funding through commercial syndication. By the date of the pipeline's inauguration, or thereabouts, filings in US Courts suggest that Viktor Kožený's primary investment vehicle had recovered much of its voucher holdings while he himself successfully fought extradition from the Bahamas.

To date, no steps have been taken to ensure that the fraud perpetrated in 1997-1998 involving Azeri vouchers, a rogue financier and the phantom privatization of SOCAR is not reprised. If, in fact, there are lessons learned, they seem to imply that whistleblowers will be silenced. At the World Bank, a whistleblower protection policy was finally approved after two years of negotiations, but it lacks effective enforcement mechanisms. Staff members finding themselves in opposition to the Bank President, should he seek to facilitate a questionable operation, would be ill-advised to try to avail themselves of the policy's purported protections.

Before another round of privatization begins, the member countries of the World Bank should reconsider the blanket immunities afforded senior managers there. Currently, documents raising serious questions about the actions of senior management at the Bank in the late 1990s came to light only because disreputable financial operators with whom they became involved were forced to reveal the documents in response to criminal prosecution. At this date, no staff member at an international financial institution is under any legal obligation to cooperate in any national investigation, so long as the matter being investigated can be related to official business, even peripherally. Senior managers at the World Bank, in particular, wield enormous discretionary authority over the disbursement of other people's money, for which they are not accountable. Because of their global reach, their authority over billions of dollars in capital, and their freedom from the constraints of regulations to which ordinary citizens are subject, World Bankers can become crucial facilitators of corruption, when they exploit the secrecy and immunity provided by the institution.