‘Commodities – Switzerland’s most dangerous business’ paints a searing and detailed picture of one of globalisation’s biggest winners, a powerful industry whose dealings often take it into dangerous areas. In the last decade Switzerland has emerged as one of the world’s dominant trading hubs for commodities, handling from 15 to 25 per cent of world trade. All the world’s largest trading houses operate partly or mainly out of this seemingly peaceful and innocent country. But while these powerful companies experience an unprecedented boom, the population of many resource-rich developing countries remain mired in poverty. This book tackles the question of why?

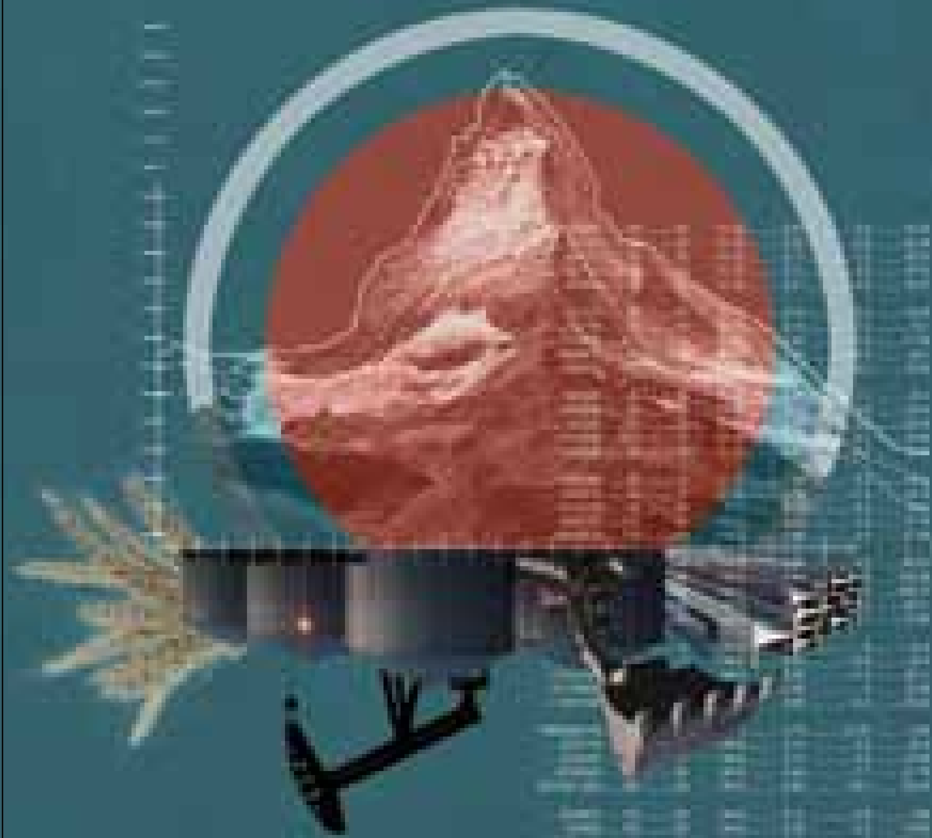
By means of research and reportage, Berne Declaration (BD) digs down to uncover the historical roots of Switzerland‘s role as a trading hub, scrutinises scandalous business practices and their political contexts, goes down a copper mine in Zambia, and exposes the leading Swiss companies and players in this discreet industry. The book reveals how commodity deals are financed and how taxes are avoided, provides insights into the social and environmental consequences for producing countries, and suggests how greater justice can be achieved in a business which is worth billions and upon which we all depend.

COMMODITIES

SWITZERLAND’S MOST DANGEROUS BUSINESS

BERNE DECLARATION (ED.)

Preface by Karin Lissakers, The Revenue Watch Institute



BD
Berne Declaration
Déclaration de Berne
Erklärung von Bern

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EDITORS BERNE DECLARATION
TRANSLATION FROM GERMAN HE TRANSLATIONS, LEICESTER
www.HETranslation.co.uk
REVIEW SIMON PARKER, ZURICH
BOOK DESIGN & TYPESETTING DANIELA TRUNK, ZUG
2012, ZURICH

THIS BOOK IS ALSO AVAILABLE IN PRINT IN GERMAN AND FRENCH

GERMAN VERSION

TITLE **ROHSTOFF – DAS GEFÄHRLICHSTE GESCHÄFT DER SCHWEIZ**

PUBLISHED BY SALIS VERLAG AG, ZURICH
www.salisverlag.com
EDITING OLIVER CLASSEN, ZURICH
PATRICK SCHÄR, BASEL
PROOFREADING INA SERIF, FREIBURG IM BREISGAU
BOOK DESIGN & TYPESETTING DANIELA TRUNK, ZUG

ISBN 978-3-905801-50-7
ISBN 978-3-905801-51-4 (E-BOOK)
2011, ZURICH

FRENCH VERSION

TITLE **SWISS TRADING SA. LA SUISSE, LE NÉGOCE ET LA MALÉDICTION DES MATIÈRES PREMIÈRES**

PUBLISHED BY EDITION D'EN BAS, LAUSANNE
www.enbas.ch

ISBN 978-2-8290-0413-1
2011, LAUSANNE

ACKNOWLEDGEMENTS //

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Berne Declaration (BD) is an independent non-governmental organization formed to combat the root causes of poverty by promoting more equitable and sustainable relations between Switzerland and the developing world. We are committed to global justice and address issues of trade policy, commodity production and trade, the politics of food, finance and fair trade. As part of a worldwide network of human rights groups, environmental and development organizations, the BD promotes a more equitable and humane route to global development.
To this end, we carry out investigative research, run public campaigns to raise awareness and undertake successful advocacy work in Switzerland and on the international stage. Founded in 1968, Berne Declaration (BD) today has a staff of 22 in its Zurich and Lausanne offices, and boasts a membership of 22'000 individuals, who finance over 80 per cent the organization.

www.evb.ch/en

THANKS

A generous bequest enabled Berne Declaration (BD) to publish this book.

Berne Declaration (BD) would like to thank its colleagues at Revenue Watch (RWI), in particular Karin Lissakers and Alexandra Gillies, for their generous support for this English edition.
www.revenuewatch.org

Finally, the publishers would like to thank Getty Images and Keystone for their kind cooperation.

CONTENTS //

PREFACE //

COMMODITY HUB SWITZERLAND: CRUCIAL FOR MORE TRANSPARENCY

Karin Lissakers
President, Revenue Watch Institute

'Commodities: Switzerland's Most Dangerous Business' by Berne Declaration (BD) sheds light on the role of Swiss companies in the natural resource sector and commodity trading in particular, areas which have hitherto escaped close scrutiny and understanding.

Aside from a few high profile scandals such as the Iraq Oil-for-Food prosecutions, traders have largely operated under the radar with limited external understanding of their business practices. However, this appears to be changing, thanks in part to the public listing of Glencore, rising commodity prices, and penetrating research such as this book.

'Commodities' sheds light on several aspects of this vast, powerful and global business. Firstly it provides a primer on how commodity trading works. The early chapters situate trading within the broader natural resource sector and global economy, and trace the emergence of Switzerland as the hub of trader activity. It explains the relationship between paper and physical trading, and breaks down the stages through which deals are made. Such explanations are difficult to glean from trade publications and press reports, and will be valuable to audiences not steeped in industry affairs. What stands out from this review is the size of the transactions in question and the scale of Swiss involvement. For example, Swiss companies conduct 35 per cent of global oil trading; Glencore alone trades volumes that top 25 per cent of total world trade in several minerals, including zinc, copper, lead and thermal coal; and Geneva-based companies sell up to 50 per cent of Kazakh and 75 per cent of Russian oil.

Second, the book illustrates the influential role played by Swiss companies in many resource rich countries. The companies discussed in the book – Glencore, Gunvor, Trafigura, Vitol and others – engage in high value deals that directly impact the economic prospects of many nations. The book provides snapshots of the activities of Swiss companies in countries including Zambia, Democratic Republic of Congo, Equatorial Guinea, Kazakhstan and Uzbekistan. The authors describe how some trading companies exhibit higher thresholds for political risk than many of the larger upstream companies. With their access to financing and logistical prowess, traders can offer valuable services to such countries by helping their raw materials reach the global market. However, it also means that Swiss traders are operating in environments that exhibit the weak governance associated with the 'resource curse'. Weak institutions and limited state accountability characterize these scenarios, and render non-transparent transactions more susceptible to manipulation than in other kinds of environments.

Along these lines, a third objective fulfilled by the book is to flag several governance risks associated with trading. The book takes a first step towards this goal by offering several cautionary tales of instances where trading activities appear to have contributed to harmful outcomes for producing countries. In some cases, the accounts describe close relations between companies and political elites, such as those of Glencore and Gunvor in Russia. In others, they illustrate the high political risk threshold that underlies business decisions such as Glencore's potential takeover of ENRC, a mining company whose Kazakh and Congolese

operations have attracted controversy in the past. Still others, such as Trafigura's offload of toxic materials in Cote d'Ivoire, suggest how weak regulatory environments can sometimes offer attractive business opportunities. These anecdotes provide data points which are not yet connected, but they certainly make a strong case for further study.

Finally, the authors call for greater transparency. By the time this recommendation is made, the reader is well convinced that the activities of trading companies – be they Swiss or otherwise – would benefit from greater oversight and accountability. Their size alone legitimizes this recommendation. Furthermore, these companies often engage in high value transactions with governments or state-owned companies. In such cases, they are buying access to public resources, and the sale proceeds enter government budgets. For example, *Energy Intelligence* reported in 2011 that Swiss traders Vitol, Trafigura and Glencore received contracts to lift a combined 240,000 barrels per day from the Nigerian government. At current prices, the sale of this much crude would generate over 10.5 billion US dollar in annual revenues. The conduct of these high value sales is of great public importance, and deserves transparent treatment.

Transparency is one of the few available mechanisms for monitoring the sale of public assets. For most oil producers in particular, transactions with traders are essential as this is how they monetize their very large in-kind revenues. Around 70 per cent of Nigeria's oil revenues come from the sale of the government's share of oil (over 1 million barrels per day) to various off-takers, mostly traders. Unless the price, volume, date, and other information about these sales are known, the public cannot assess whether it is getting a good deal for its resources. Along with these basic transparency requirements, further measures would be needed to discourage tax evasion – a costly practice that is discussed in chapter 14. Regulatory weakness puts developing countries at particular risk of these abuses, resulting in the loss of sorely needed public revenues.

The movement to promote transparency and good governance in the natural resource sector has made important advances over the last decade. This campaign is motivated in part by the recognition that resources can play a crucial role in development. Far greater than foreign aid in size, resource revenues can provide the financing needed to build infrastructure and expand social services in many of the world's neediest countries. This only happens when producing countries receive a fair deal in the extraction and sale of the resources, and spend the revenues in ways that benefit the public.

Transparency can help achieve these outcomes. But often transparency is needed most where it is least likely to emerge. Some home governments are helping to advance this objective. As described in chapter 18, the 2010 US Wall Street Reform Act (the 'Dodd-Frank Act') requires all US listed extractive sector companies to publish how much they pay to foreign governments, and to report this information for each individual project. The European Commission has made a similar proposal currently under consideration by EU member states. However, even if these efforts move forward successfully, a number of companies, including several profiled in this book, will be excluded because they are based in other such as Switzerland.

This book sheds light on a segment of the natural resource sector that has important implications for many producing countries. It should help to build the case for why greater openness in commodity trading offers potential benefits to citizens in resource rich countries worldwide.

WELCOME //

Commodities are the lifeblood in the veins of the global economy and are of commensurate strategic importance. No wonder, then, that increasingly scarce natural resources have become an ever-growing political issue in recent years.

01 //

WELCOME TO SWITZERLAND, THE COMMODITY CAROUSEL: 'WARNING: RISK OF DIZZINESS!'

Geneva, Grand Hotel Kempinski, end of March 2011. While the world stares spellbound at the slow-motion reactor catastrophe at the Fukushima nuclear power plant, the commodity business meets for its annual rendezvous, the 'Trading Forum', on the shores of beautiful Lake Geneva. In his talk, oil trader and Mercuria co-owner Daniel Jaeggi responds to this burning issue and reflects on what a global nuclear phase-out might well yield for him and the others present. Although only five per cent of the world's energy comes from nuclear power, that nevertheless corresponds to 610 million tonnes of oil annually, or 15 per cent of global output. "I just leave you with that," Jaeggi closes with a smile.

Where others see only disaster, the commodity trader sees an 'opportunity', his chance for new, large and, above all, profitable business. Successful 'opportunity hunters' have transformed Switzerland into a centre for commodity traders and made it a world leader, and all in just a few decades. As one of the very few top traders who is actually Swiss, Jaeggi is also the exception that proves the rule. In almost all cases it has been non-Swiss – managers as well as companies – who have made this small, landlocked country into the largest global commodity hub.

Yet this amazing success story is based on something deep-rooted in the Swiss character, namely political opportunism. Consistently standing on the sidelines, looking away and claiming not to know, even refusing to join the UN until 2002, are all actions which have been defended under the cloak of 'neutrality.' These have brought Swiss-based companies a large number of questionable but all the more lucrative business opportunities. The rise of the commodity trading centres of Zug and Geneva was also facilitated by their exceedingly moderate tax regimes and a societal tendency towards a great deal of confidentiality and little regulation and control. In short, Switzerland as a commodity hub, although by no means planned, is much more than mere coincidence.

The commodity market in Switzerland is large – astronomically large. And it has grown explosively: between 1998 and 2010, net receipts in this sector increased fifteen-fold. According to the trade newspaper *Handelszeitung,* the twelve largest companies in Switzerland include five commodity businesses (according to research by Berne Declaration (BD), there are in fact seven). Despite its significance and hazardous nature, virtually nothing is known about this secretive business, which in 2008 contributed roughly as much to the country's GDP as the traditional mechanical engineering sector. And in this regard, even the initial flotation of industry leader Glencore in May 2011, billed as a "watershed moment for the entire commodities industry" *(Financial Times),* will probably not change anything. This book is therefore a pioneer work and attempts to capture the swiftly-turning Swiss commodity carousel within a single book.

Commodities are the lifeblood of the global economy and are of commensurate strategic importance. No wonder, then, that increasingly scarce natural resources have become an ever-growing political issue in recent years. The key terms in this drama are oil price boom, food crisis, evictions, population displacement, security of supply, price speculation, CO_2 emissions, land grabs and conflicts over the Arctic. Given such a diversity of topics already, there are some the next 400 pages do not cover. For example, the commodities that are consumed by industry and private individuals within Switzerland itself. In comparison with the transit trade – the business of the Swiss commodity sector – in which the goods never arrive in Switzerland at all, domestic consumption is entirely insignificant. It's not about famous brands such as Nestlé, Shell or Starbucks, either. They are involved in commodity trading, but are primarily major customers of the real traders and are therefore not included. In addition, the controversial question of how a country today ensures politically that it obtains all the raw materials that its economy and people need is also not answered here.

The subject of this book is rather all Swiss companies, including the 'corporate immigrants' with their central operations in Switzerland, that are active in either commodity trading (Mercuria, for example), the extraction of raw materials (Xstrata, for example) or both (Glencore, for example). We have analysed all the main commodity groups: energy sources (especially crude oil and its derivatives), ores and metals, and agricultural products ('soft commodities'). The world's largest independent oil trader Vitol operates out of Geneva, Glencore in Zug is the dominant commodity colossus, with its main focus on ores and metals, and the four most important agricultural trading firms all have prominent trading offices in Switzerland.

Our focus is necessarily on such industry leaders. Due to limited space, the niche players, who are encountered mainly around Lake Geneva, but occasionally also in other cantons, are mentioned only in passing. To really bring light into the darkness of the 'black box' of commodity trading, we examine its wider contexts and general business practices across the companies. From its historical origins, and continuing via the complex tax tricks and speculative instruments to some specific places of action (and consequences), we show everything that is important for an understanding of this multi-layered commercial sector.

What has motivated us to undertake this research project is a fundamental contradiction. It might be a development-policy truism but this makes it no less pressing: resource-rich countries are and often remain very poor – not despite, but precisely because of their natural resources. A prime example of this 'resource curse' is the Congo, while Zambia is another and we report from both countries. Nevertheless, this book is not a chronicle of the global scandals of the Swiss commodity traders. Why not? Because our main interest is in the other side – our side – of this 'accursed' equation. Here, the same commodities are making some trading businesses and their owners rich beyond measure. The managers of Glencore roughly tripled their wealth at a stroke by bringing their company to the stock exchange in 2011. The widespread poverty of entire countries and the wealth of some top traders are directly linked. This book demonstrates how this is the case.

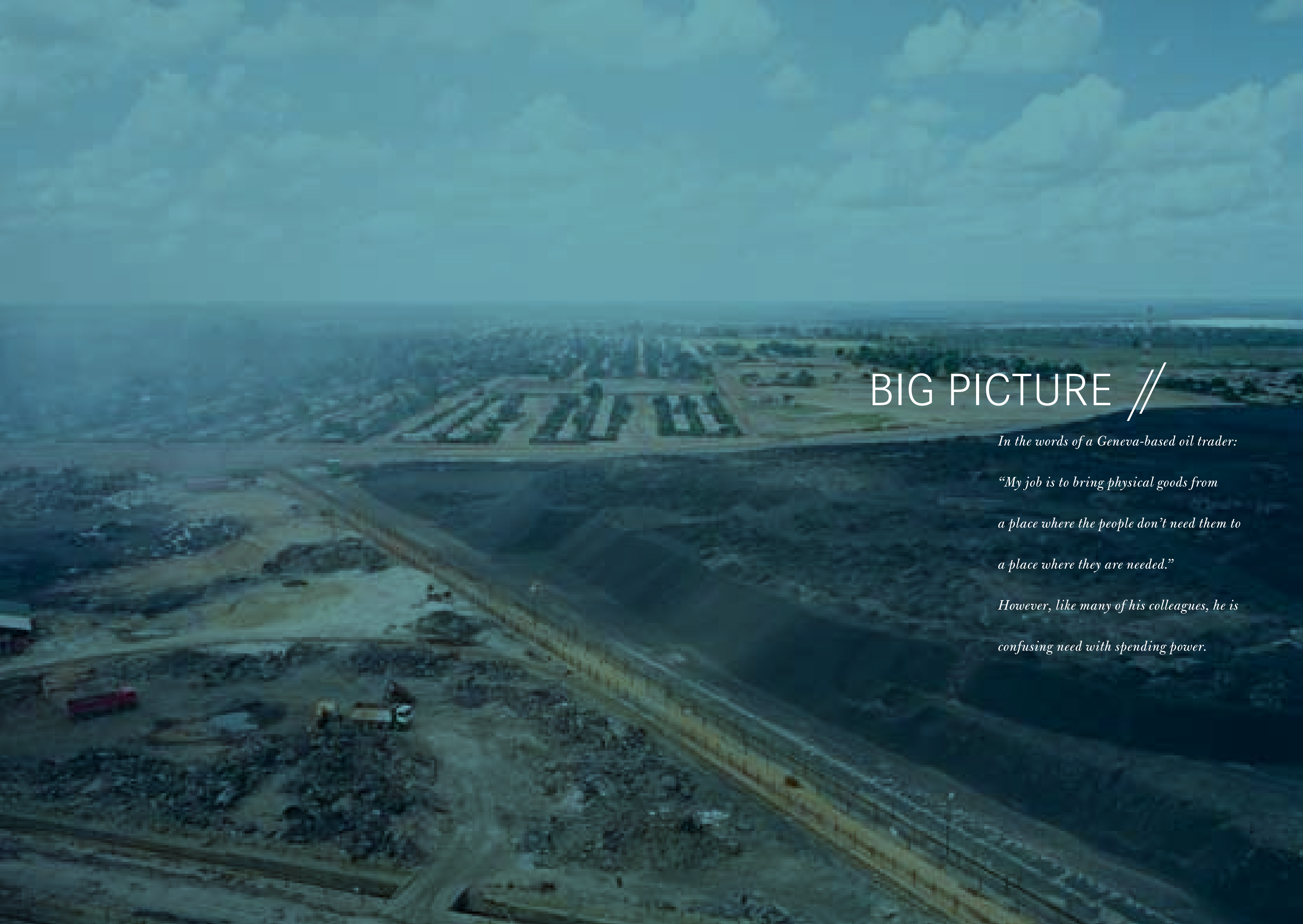
On the whole, the commodites business as practised in Switzerland today is dangerous for all countries in the southern hemisphere that are blessed with natural resources but at the same time suffer from weak or corrupt governments. This is particularly the case for those men, women and children who live in the dirt and dust of the mines and production facilities. Mining, crude-oil production and large-scale industrial farming harm the living conditions of millions of people by using land and polluting water supplies and the air.

But the trading companies' business model, which frequently exploits grey areas, is also dangerous for Switzerland. Corruption, aggressive tax avoidance, speculation mania and human-rights violations pose enormous risks for reputations and, as in the case of bank secrecy, constitute the country's "next exposed flank" *(Tages-Anzeiger)*. Switzerland is not only a tax haven, but also lacks transparency and regulation – and it attracts commodity trading as a dunghill attracts flies. The commodity businesses between Lake Zug and Lake Geneva still enjoy free rein, but some countries such as Bolivia are defending themselves and demanding fairer commodity prices, the United States is imposing a duty of transparency on the commodity business, and the EU wants to reduce foodstuffs speculation. In other words, the world will not simply a spectator at this so-called 'locational advantage' swindle forever.

"Improved accountability and control [of the commodity business] could potentially change living conditions, economies and political systems around the world," says the investors' guru George Soros.

While Eva Joly, the MEP and courageous campaigner against white-collar crime, is convinced that in 20 years' time humanity will classify the current distribution of wealth in the commodity business in much the same way that we regard slavery today. We therefore share the motto of U.S. Federal Judge Louis Brandeis who acted against corruption and bank power 100 years ago and knew even then that "sunlight is the best disinfectant". So if this book lets some sunlight into the Swiss commodity hub, it will have achieved its goal.

PS: Since the German edition of this book went to press, Glencore and Xstrata have announced their intention to merge. If this goes through, the ensuing company will be the fourth largest mining company and at the same time the most profitable commodity trading company in the world. Naturally, it will be headquartered in Zug.



BIG PICTURE //

In the words of a Geneva-based oil trader:

“My job is to bring physical goods from a place where the people don’t need them to a place where they are needed.”

However, like many of his colleagues, he is confusing need with spending power.

02 //

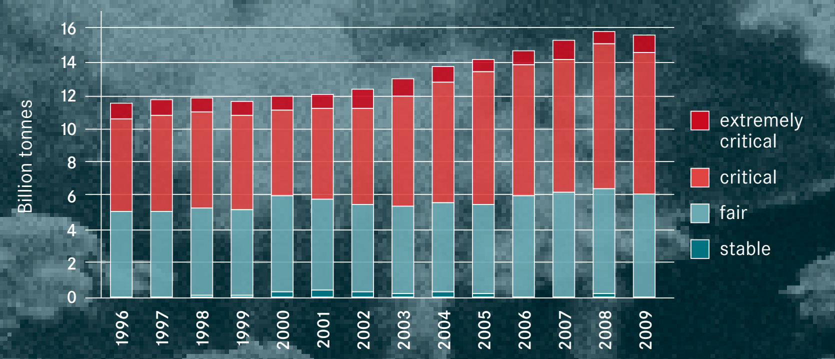
THE NATURE AND IMPORTANCE OF COMMODITIES IN WORLD TRADE

We cannot function without raw materials. The natural resources of our planet are the material basis of our economies and societies: they fuel prosperity and growth. We are consuming more and more, and so our need for natural resources is ever increasing. More raw materials have been consumed since World War II than in the entire history of mankind.[1]

These fuels of our civilisation often come from developing countries: 59 per cent of metals and ores (as much as 71 per cent of copper), 63 per cent of coal and 64 per cent of oil.[2] Increasingly, they come from politically unstable countries, as shown in FIG. 1. These are states which have no effective environmental or social legislation and are often shaped by war and conflict. The lives and health of the people who live around the mines, quarries and production facilities are thus exposed to great danger.

FIG. 1

ORIGINS OF RAW MATERIALS IN TERMS OF POLITICAL STABILITY



Source: BMWFJ 2011

TYPES OF COMMODITIES AT A GLANCE: WHAT ARE THEY, WHAT ARE THEY FOR AND WHAT DO THEY COST?

So that they can be exchanged easily, heavily traded raw materials are standardised in size and quality, after which they are referred to as 'commodities'. Commodities are usually divided into three categories. Energy commodities, ores and metals (also known as 'mineral commodities'), and agricultural goods ('soft commodities'). Energy commodities are a relatively simple category, comprising mainly crude oil and oil products, natural gas and coal. Mineral commodities are much more diverse, dominated by the metal commodities such as iron, non-ferrous metals such as zinc, and precious metals. Finally, there is the agricultural sector, including a wealth of foodstuffs such as grains, ingredients for drinks (e.g. coffee and cocoa), versatile

TAB. 1

THE UNIVERSE OF THE MOST IMPORTANT COMMODITIES

Non-renewable commodities			**Renewable commodities**
Energy commodities	Mineral commodities		Agricultural commodities
	Metal commodities	Non-metal mineral commodities	
Crude oil and oil products	Non-ferrous metals: e.g. aluminium (alumina), lead, cobalt, copper, nickel, zinc, tin, rare earths	Gemstones	Grains: e. g. wheat, maize, rice
Natural gas	Iron	Industrial minerals: e. g. salt, gypsum, phosphate	Vegetable fats
Coal (bituminous coal, lignite)	Precious metals: e. g. gold, silver, platinum, palladium		Coffee, cocoa, sugar
	Radioactive metals: e. g. uranium		Cotton

Source: Compiled by authors

materials such as sugar and oil, and fibres for textile production TAB. 1. In the trade the term 'commodities' is used rather loosely. On all the markets there are materials which, strictly speaking, are already intermediate products. As far as metals are concerned, aggregates (ores, e.g. bauxite) and the intermediate products obtained from them (alumina) and lastly the pure products (aluminium) are all traded as 'commodities'. Besides iron, the metals which are especially important

TAB. 2

MAJOR INDUSTRIAL METALS AND THEIR USE

	Properties/use	Main countries of origin	Main consu-ming countries
Aluminium	Most common metallic element in the earth's crust, light, and robust. Used in vehicles (air, road, rail), in construction, for consumer goods and packaging	China, Russia, Canada, Australia	China, USA, Japan, Germany
Cobalt	Used as a steel alloy, in heat-resistant paints and pigments, for paints and varnishes, as a catalyst, in batteries and as a trace element in steel alloys in medicine and farming	Democratic Republic of Congo, Zambia, Australia, Canada	China, USA, Japan, Germany
Copper	Good conductor of electricity, used in cables, electric coils and connectors, also in coins	Chile, USA, Peru, Australia	China, USA, Germany, Japan
Nickel	Hard yet malleable, used in stainless steel production	Russia, Canada, Indonesia, Australia	China, Japan, USA, Germany
Zinc	Low melting point, used to prevent iron and steel products from corroding and in casting moulds in heavy industry	China, Australia, Peru, USA	China, USA, Japan, Germany
Tin	Soft and light to process, used in the electronics indus-try and for coatings in cans of tinned food	China, Indonesia, Peru, Bolivia	China, USA, Japan, Germany

Source: Compiled by authors

to industry (industrial metals) include many non-ferrous metals. TAB. 2. Since Switzerland does not play a major role in the trade in rare earths, which are central to the electronics industry, these are ignored here.

Be it cotton or lead, all these very different commodities have one thing in common: since the turn of the century they have shot up in price. This fact alone explains why commodities are such a relevant and controversial issue today. Although prices dipped sharply in 2008 following the financial crisis, metals and agricultural goods have long since surpassed their previous highs FIG. 2.

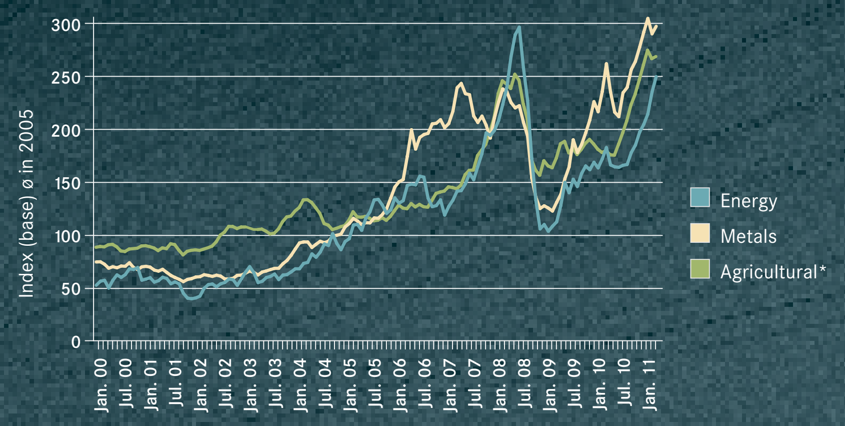
COMMODITY TRADING: A LUCRATIVE NECESSITY

Whereas some parts of the earth are rich in mineral deposits, others are almost entirely dependent on imports. A good example illustrating just how much the distribution of raw materials and their consumption differ worldwide is oil. In 2010 every human being in the world consumed five barrels of oil on average FIG. 3. Whereas the Middle East can produce 43 barrels per person per year, thereby generating huge surpluses, in Asia merely one barrel per capita is extracted from the ground at present. Trading redresses this global imbalance.

It is this function that gives commodity trading its public identity. Daniel Jaeggi, Vice-President and Head of Global Trading of Geneva-based oil trader Mercuria, puts it this way: “My job is to bring physical goods from a place where the people don’t need them to a place where they are needed.”[3] However, like many of his colleagues, he is confusing need with spending power. It can hardly be due to a lack of need that in Africa only one out of the (modest) four barrels of oil produced per capita is actually consumed there, and the rest have to be sold. By way of comparison: the average person in North America consumes all of the 14 barrels produced there and then imports eight more from other regions (among them Africa).

FIG. 2

PRICE FLUCTUATIONS BY COMMODITY GROUPS 2000 – 2011

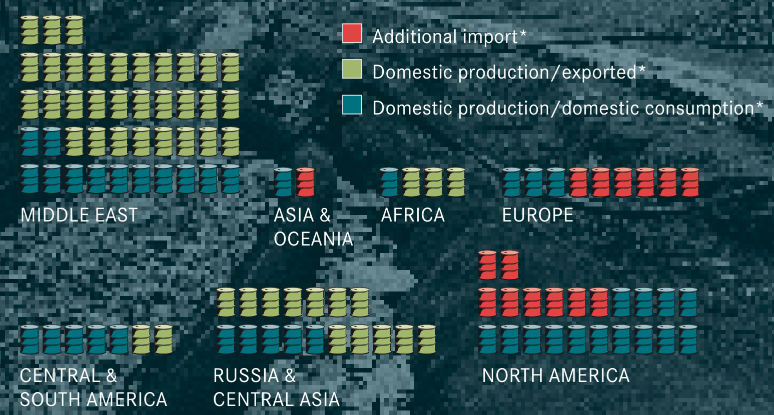


*Grains, vegetable oils, sugar, fruit, coffee, tea, cotton

Source: IMF Primary Commodity Prices

FIG. 3

OIL PRODUCTION AND CONSUMPTION PER CAPITA BY REGION IN 2010



*Per capita (barrel/year)

Source: UN DES; U.S. Energy Information Administration

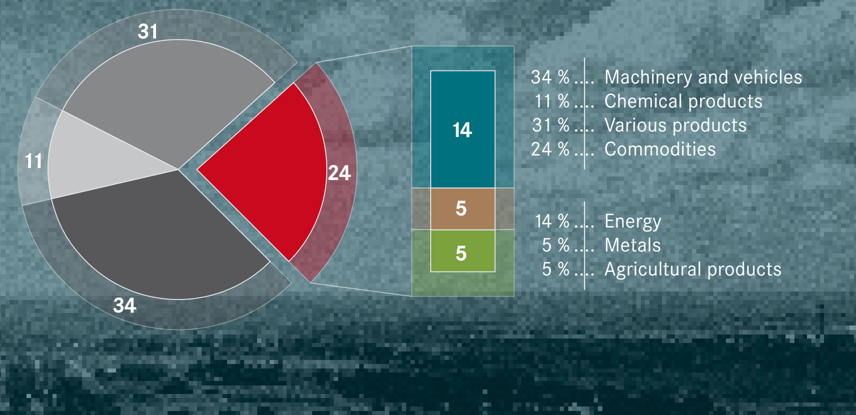
Although some of the raw materials are consumed directly in their countries of origin, that a sizeable share invariably reaches the global market is beyond question. Today, this process is dominated by 'commodity trading', where commodities make up around a quarter of the total world trade volume FIG. 4.

Of even greater significance than the value of commodities in world trade terms is their importance in weight. Commodities are obviously much cheaper per tonne than finished products. Since 80 to 90 per cent of world trade is seaborne, the statistics for international maritime cargo transport afford interesting insights.[4] About 70 per cent of the ships carry commodities. These carriers can include oil tankers and bulk vessels with metals, coal or wheat on board FIG. 5. In contrast, the variety of sea-going containers, which are mainly used to transport end products and symbolise global world trade, account for a mere 14 per cent of world trade in terms of weight. So when it comes to the transport of bulk materials, commodities trading actually accounts for roughly two-thirds of world trade.

'Oil is king': In terms of its value 'black gold' accounts for almost exactly half of all commodity exports. Taking oil, natural gas and coal together, the share of energy commodities in total commodity exports is just short of 60 per cent FIG. 6. The remainder are exports of mineral (20%) and agricultural commodities (20%).

FIG. 4

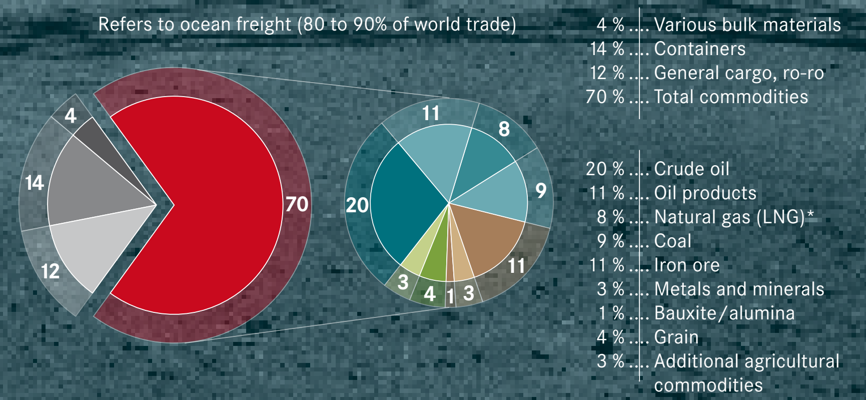
SHARE OF COMMODITY TRADING IN WORLD TRADE IN 2009 (MONETARY)



Source: Authors' illustration; UNCTAD 2010b (World trade exports)

FIG. 5

SHARE OF COMMODITY TRADING IN WORLD TRADE IN 2009 (WEIGHT)



*Includes an additional 0.46 million tonnes transported via pipelines (BP 2010)

Source: UNCTAD 2010a

FIG. 6

COMMODITY MARKET BY SHARE
(MONETARY SHARE IN WORLD EXPORTS)

*Includes fruit and vegetables, which are not standardised commodities

Source: Authors' illustration; UNCTAD 2010b

'LITTLE BIG SWITZERLAND' TOPS THE TABLE.

Given their global dominance it is hardly surprising that fossil fuels also monopolise the Swiss commodity trading hub. TAB. 3 gives an overview of the main commodities traded and those Swiss-based companies that conduct the majority of this trade, and in turn are covered in this book.

TAB. 3

MARKETS OF THE MAJOR SWISS COMMODITY COMPANIES

Company	Energy Commodities			Mineral Commodities			Agricultural Commodities		
	Oil	Natural gas	Coal	Copper	Alu	Iron	Grains	Vegetable fats	Sugar
Glencore	●	○	●	●	●	○	○	○	○
Trafigura	●		○	●	●	○			
Xstrata			●	●	○				
Vitol	●	○	○	○	○				
Mercuria	●	○	○						
Gunvor	●	○	○						
Litasco	●								
ADM							●	●	
Bunge							●		●
Cargill	○	○	○			○	●		●
Dreyfus	○	○	○	○			●	●	●

● Company's core business
○ Company's secondary business

Source: Compiled by authors; company publications

Important commodity trading hubs are located in Asia, Europe and North America FIG. 7. The trading hub of Amsterdam has Europe's largest port, Rotterdam, at its disposal, while Houston has huge oil refineries and storage facilities, Chicago and Hong Kong have important commodity exchanges. Switzerland, on the other hand, has nothing that would suggest this small, landlocked country was destined to become one of the main hubs of the commodity business, but this is what has happened. The Canton of Zug has traditionally been important but key players are also located in the Cantons of Zurich and Lucerne. Nevertheless, the most dynamic area at the moment is clearly Geneva, which leads the league of global commodity hubs.

FIG. 7

GLOBAL COMMODITY HUBS

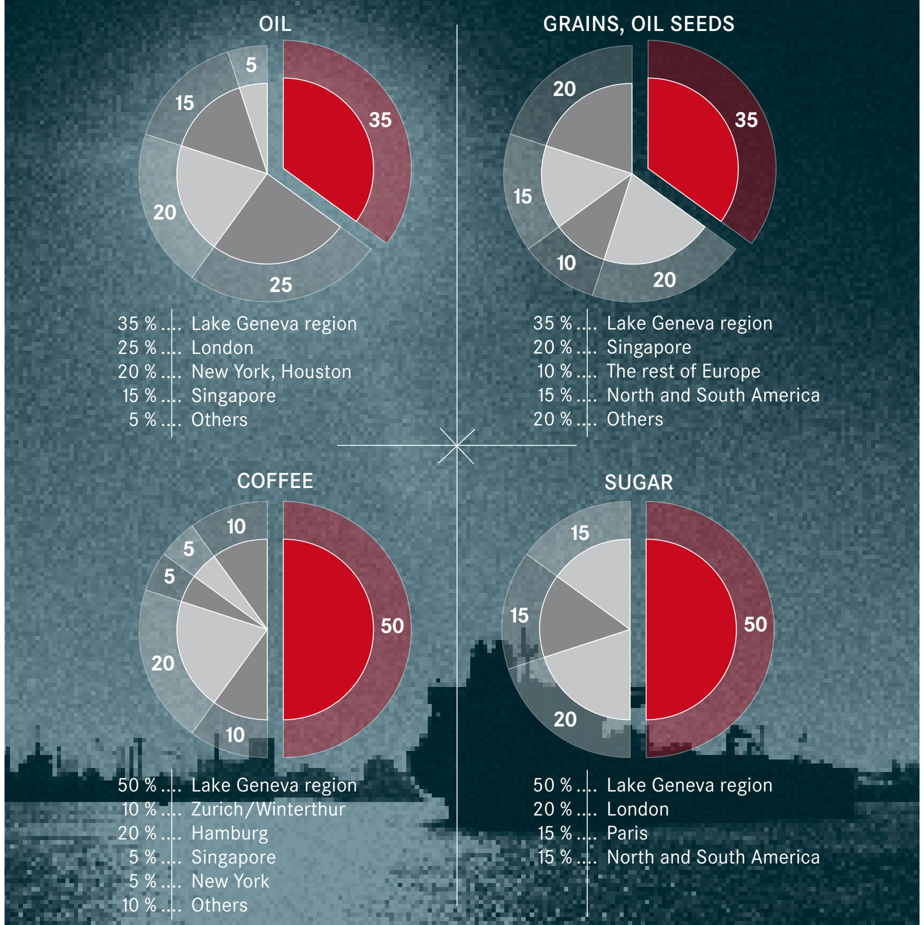
Source: Ernst & Young 2007

According to GTSA, the industry organisation Geneva Trading and Shipping Association CHAP. 11, Geneva has not only replaced London as the most important oil trading city, but in grain and coffee trading the industry heavyweights are also now located on the shores of Lake Geneva CHAP. 12. FIG. 8 illustrates the shares of trade transacted here.

To what extent these GTSA figures are for lobbying and location-marketing purposes or are based on sound data, is difficult to assess.

FIG. 8

MARKET SHARES OF THE GENEVA-BASED COMMODITY TRADERS



Source: GTSA[5]

The other commodity arenas, especially Zug, are not even included here. Particularly in the case of metals and coal, they provide significant market shares for Swiss traders.

SMART MODEL: 'TRANSIT TRADE' WITHOUT 'TRANSIT TRAFFIC'

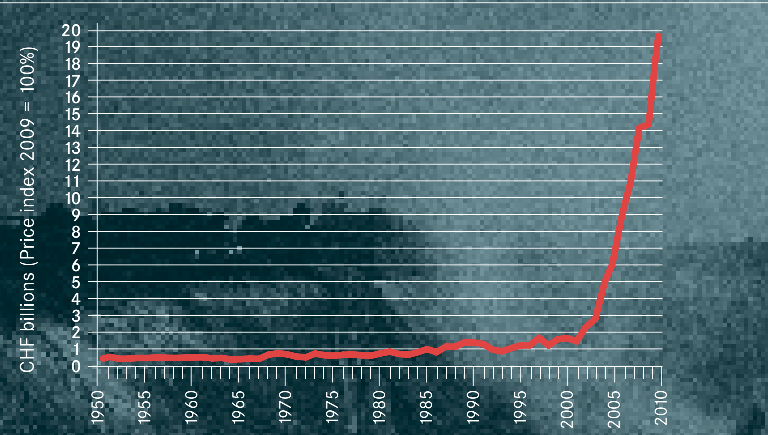
One thing is certain: the commodity trading handled by Switzerland far outstrips Swiss domestic consumption. For example, if the recorded annual trade volume of oil were to remain within its borders, national consumption would be covered for the next 75 years. Even if all the lorries on the Gotthard route were only transporting oil, only five per cent of the oil traded here in Switzerland could be brought over the Alps. But the logistical limits are of no concern to the Swiss commodity traders as they practice a very specific business model, so-called transit trade (also known as 'merchanting'). Contracts may be concluded, deliveries scheduled and ships chartered from Swiss offices, but the actual goods – except in the special case of gold CHAP. 9 – never touch Swiss soil. From an African mine, for example, the raw materials are dispatched via land and sea routes directly into a Chinese smelter.

In this way, the flow of goods conveniently eludes the official statistics of the Swiss Federal Customs Administration – one reason for the notorious lack of transparency in the business. Nevertheless, data can be retrieved by another route because the Swiss National Bank (SNB) measures the transit trade as an export of services. Transit trade is defined as all transactions in which Swiss companies buy goods abroad and then sell them directly and unaltered to customers abroad (so crude oil that is refined before it is sold on is not recorded). For the most part (94 per cent in 2009) Swiss transit trade is commodity trade.[6]

The SNB's data may not provide a complete and exact picture, but they do give a good approximation, which brings something astonishing to light. When illustrated in a graph, it is clear that Swiss transit trade since 1998 has shown a steep upward curve. The SNB puts this almost exponential increase down primarily to the influx of commodity trading companies. In addition, the already established businesses have grown massively. Previously ignored for the most part, these data verify the huge growth of the commodity trading business in Switzerland FIG. 9.

FIG. 9

GROWTH IN TRANSIT TRADE, 1950 TO 2010
(NET RECEIPTS*)

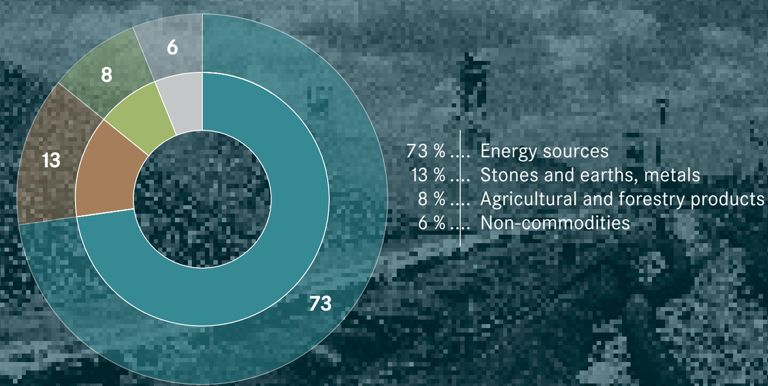


*Net receipts = gross receipts - gross expenditure

Source: SNB

FIG. 10

SHARES BY COMMODITY GROUP IN THE TRANSIT TRADE IN 2009
(GROSS RECEIPTS)



Source: SNB

The information provided by the Swiss National Bank also sheds light on the sectors in which these companies make their sales FIG. 10.[7] The energy sector is by far the strongest player. Its proportion in Switzerland is even slightly larger than in the whole of world trade.

Another word on economic relevance: in 2008 commodity trading contributed roughly the same amount to the gross domestic product (GDP) of Switzeland as the engineering industry, namely around two per cent. But the latter employed about 95,000 people, while the figure was probably not even a tenth of that in the commodity trading sector. Since then commodity trading has continued to increase and by 2010 was already contributing over three per cent to GDP. The business thus employs relatively few people, but in return per capita sales are all the higher. The reason for the latter is that this business has traditionally made relatively low gross margins of just a few per cent, achieving its high profits mainly through enormous volumes. This is reflected in the sales figures: for the whole industry in 2009 these were 480 billion Swiss francs just for transit trade.[8] To this has to be added the transactions not captured in the SNB statistics. In media reports for the Geneva region annual sales of 700 to 800 billion are quoted.[9] In terms of world trade in commodities, which is a colossal business of 3,000 billion Swiss francs, the companies operating in Switzerland have a share of at least 15 to 25 per cent already and the trend points towards a significant increase in this share.

INTERIM CONCLUSION

Mankind is consuming more and more resources, most of which are traded internationally as commodities. Just how much commodity trading dominates world trade is illustrated by the fact that one in four dollars now changes hands there. And two out of every three cargo ships now transport commodities. The revenues from this multi-billion business more than trebled in value between 1998 and 2009, driven by rising commodity prices.[10] In Switzerland the market increased as much as fifteen-fold during roughly the same period. Today the global arenas of this business are located around Switzerland’s Lake Geneva and Lake Zug – albeit behind closed doors.

A trader enjoys telling the story of the unfortunate long-distance truck drivers who painstakingly transported a tanker full of Kazakh oil through Afghanistan. When they set off oil prices were at the peak of the price hike.

COMMODITY TRADING //

By the time they reached their destination a week later the same barrels of oil were worth only half the amount and their journey was a financial disaster.

03 //

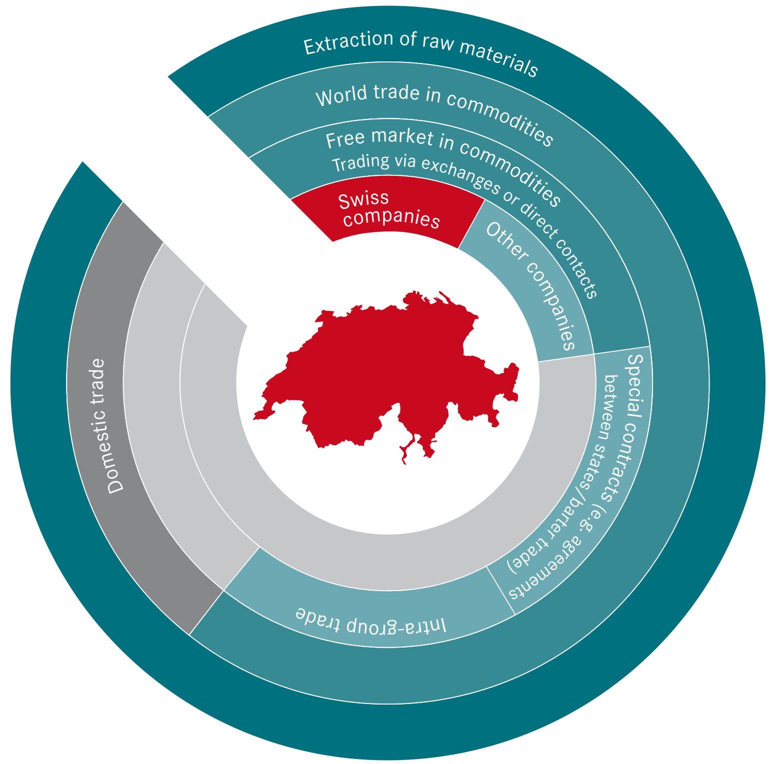
COMMODITY TRADING: TOOLS AND MECHANISMS

Commodity trading is a complex structure of interlocking processes and interconnected players and encompasses very different phenomena. A preliminary distinction can be made between domestic trade and world trade FIG. 1. Taking crude oil as an example, total world trade volume coresponds to just under half of global output. In contrast, for coal it equals only an eighth since China alone produces and consumes almost half. However, if Shell Nigeria delivers oil to Shell Switzerland for example, this counts as intra-group trade. According to expert estimates this type of trading is extremely important. Governments also negotiate many commodity deals between one another directly, although they do involve leading export companies if necessary. Such deals include so-called ‘barter trades’, based on an offsetting transaction or an exchange of goods, for example oil for cashew nuts or armaments. Essentially, this permits contracting parties to trade whatever they chose to.

Quantitatively far more important is the ‘free commodity market’. On this market commodities can reach their end users in industry in two ways: either they are sold on the commodity exchanges or they are ‘sold directly’ by a commodity trading company. This is the primary business sphere of the trading companies operating in Switzerland and therefore the focus of this book.

FIG. 1

OVERVIEW: TYPES OF COMMODITY TRADING AND FOCUS OF THE BOOK



Source: Authors’ illustration

Whatever route is used to bring commodities to their buyers and regardless of whether it concerns a cargo of coffee, copper or crude oil, physical commodity trading involves the transport of freight, usually by ship. Hence, the trading companies are invariably also logistics companies. Their core business involves buying a commodity, shipping it from A to B and selling it at a higher price in order to cover their business costs and make a profit.

Direct deals between commodity traders and industrial customers comprise either deals with long-term purchase agreements, the traditional type of commodity trading, or deals on the spot market. The term 'spot' comes from the phrase "on the spot". A spot market refers to all the sales which are made when prices are fluctuating rapidly and which have short delivery deadlines. According to Platts, a renowned data services provider on the commodity market, even today long-term deals outnumber spot deals by nine to one. Estimates for the oil market indicate a roughly 30 per cent share for the spot market. For natural gas, which is liquefied for sea transport, the figure is said to be 20 per cent of production volume.

BRENT CRUDE OIL AND CHICAGO PORK BELLIES: PHYSICAL EXCHANGE TRADING

Another part of commodity trading takes place on the exchanges. This is where major consumers and major producers buy, for example, wheat, crude oil or aluminium directly or via financial intermediaries at a price that is valid at the moment the transaction occurs at a certain reference site. The three major trading centres for crude oil are the NYMEX (New York Mercantile Exchange), the ICE Futures (Intercontinental Exchange) in London and the market in Singapore where the barrels (standard 159 litres barrels) from the region around Dubai are traded. Each marketplace focuses on its own particular type of oil. Thus so-called 'Texas Light Sweet' is bought and sold on the NYMEX. The

price of this standard type is set in Cushing, a small town in Oklahoma, where most of the large US oil companies (oil majors) operate huge, and in terms of energy policy strategic, oil storage facilities. Similarly, what is traditionally known as 'Brent' crude oil from the North Sea is traded on the ICE and 'Dubai Light' in Singapore. The main players in these markets are the American majors, all operating through their trading arms and subsidiaries.

Other global commodity exchanges are the LME (London Metal Exchange) for metals, or the London Bullion Market for gold and silver. As well as oil, metals are also traded on the NYMEX. Similarly, transactions in gas, coal and electricity also take place on the ICE. Agricultural products are traded on the EURONEXT in Europe. However, this sector is dominated by the Chicago Mercantile Exchange, which specialises in grain on the one hand, but is also the place where all kinds of goods, everything from concentrated orange juice to the legendary 'pork bellies', are traded.

HEDGING VS. SPECULATION: PAPER TRADING IN COMMODITIES

Over time these exchanges have developed into the material and monetary ventricles of the global circulatory system of commodities. Hence the spot prices originating there are still regarded as reference values although on today's commodity exchanges (or specialised derivatives exchanges) it is no longer physical trading but paper trading that dominates in terms of value. According to estimates some 10 to 15 times more 'paper barrels' than 'wet barrels' (physical oil) are traded on the oil market. And in 2006 nickel was bought and sold thirty times more often for paper money than for real money. The most important instruments of paper trading are shown in TAB. 1.

TAB. 1

INSTRUMENTS OF PAPER TRADING

Derivatives	Derivatives are 'derived' securities, whose price or value is determined by a 'base value', for example a share price, interest rate or even the price of a commodity. Derivatives can also be used to bet on the probability of a state becoming bankrupt or a company insolvent. Some derivatives are traded on the exchanges in standardised form and subject to certain rules. Others, so-called OTC (Over-The-Counter) derivatives, are exchanged directly between specialised trading parties. Not listed on an exchange, derivatives trading such as this is highly opaque.
Commodity Futures	Paper trading in commodities usually involves commodity futures – a sub-category of what are collectively known as derivatives. A futures contract is a security whose owner undertakes to sell goods of a specified quantity and quality at a later date to a customer who in turn undertakes to pay for the goods at a price fixed in advance (i.e. for a 'fixed' date). There are two types of futures: binding (the goods must be traded) and conditional (the goods can be traded on the fixed date).
Standardised Commodity Future	An exchange traded, binding futures contract. This type of contract is based on a real base value (e.g. concentrated orange juice), includes a specific, agreed volume (quantity) and quality of goods (frozen, concentrated juice of Florida oranges) and a fixed date and price. Yet, less than three per cent of the contracts agreed on the futures markets actually involves a delivery of the goods; the majority are 'settled', i.e. the difference between the initial futures price and the price actually valid on the future date is paid.
Commodity Forward	Similar to a future but not standardised and therefore not traded on an exchange; instead the contract is concluded directly between the two parties.
Traded Option	An exchange-traded, standardised contract. An option is the right to purchase e.g. concentrated orange juice at an agreed price on a given date. The owner of the option decides unilaterally whether to exercise the option or not. Here too, exercising an option usually. Here too, the vast majority do not trigger a physical delivery but are settled financially.
OTC Option	Not listed on an exchange, this type of option is concluded directly between two parties.

Source: Compiled by authors

Futures are indispensable instruments, which commodity traders use as safeguards against sharp price fluctuations. A trader from Vitol enjoys telling the story of the unfortunate long-distance truck drivers who painstakingly transported a tanker full of Kazakh oil through Afghanistan. They set off in 2008 when oil prices were at the peak of the price hike and the price of a barrel was 140 dollars. By the time they reached their destination a week later, the same barrels of oil were worth only half the amount and their journey was a financial disaster. If price fluctuations of such magnitude befall an entire super tanker shipment, it can mean bankruptcy for a smaller trading company. To minimise this risk, traders carry out 'hedge' transactions. 'Hedging' means literally encircling with a hedge (the term hedge funds has the same linguistic roots, but hedge funds are something quite different, namely unregulated investment funds). Hedging in order to safeguard prices means that a trader makes a futures deal to offset the actual transaction. The trader wins both ways, either on the real deal (for example if prices rise) or on the futures deal (if prices fall). In this way the trader is trying to keep the overall profit from both transactions within a certain range.

In the case of paper trading there are two groups of players, which differ from one another in principle. On the one hand, there are the buyers and sellers of physical commodities ('commercial actors'), whose main aim is to use hedging as a safeguard against price fluctuations. On the other, there are various financial players such as banks or hedge funds ('non-commercial actors'), who are only interested in the profits they can make by speculating on the commodity futures markets. In conceptual terms, the distinction between these two sets of market participants is clear and simple. In practice, however, a future used as a hedge is no different from a speculative future. What makes the difference is solely the motivation of the players. Worse still, the transition from safeguarding to speculating is fluid. For example, Glencore writes about oil deals being safeguarded by 'paper transactions', which might involve some speculation ('taking increasing exposures').[1] Be that as it may, one thing is certain: a major part of commodity futures trading is pure financial speculation. Nor is there any disputing the fact that in recent years the structure of the commodity markets has changed dramatically under the increased influence of the financial players. This transformation has sparked off a heated debate on the effect of speculation on the volatility of commodity prices CHAP.13.

WE CANNOT FUNCTION WITHOUT (GENEVA-BASED) BANKS: THE FINANCIERS IN COMMODITY TRADING

The most important 'commodity' the trading companies require for their transactions is the money to finance them. Operations such as these are capital-intensive in the extreme: a shipment of oil by tanker for example requires raising tens or even hundreds of millions of dollars. If the trading companies intend to finance their operations themselves, they need large funds of their own and a great deal of liquidity. The largest among them can obtain these funds on the capital market (issuing bonds), directly from the banks via credit lines or by issuing shares.

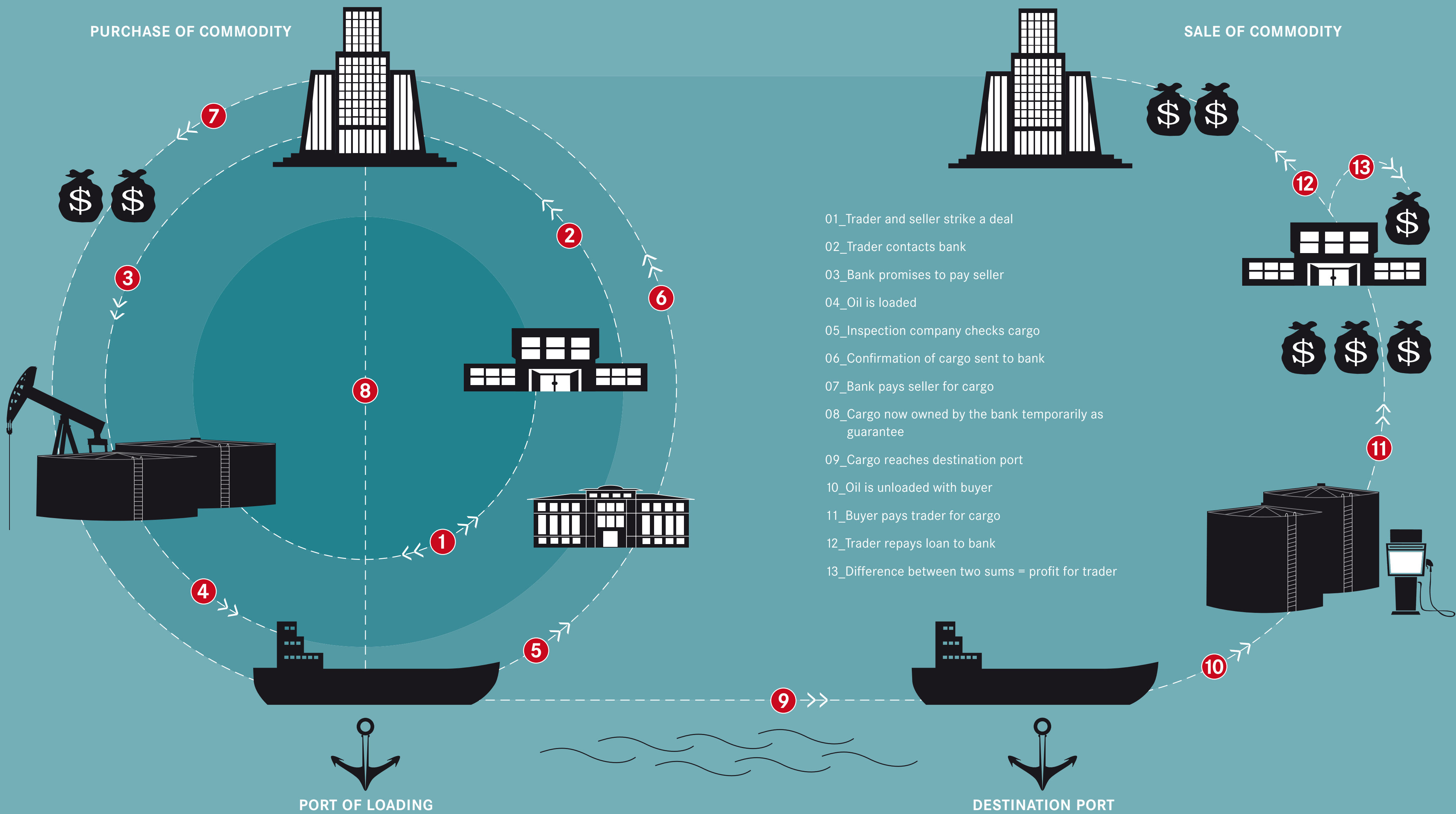
In certain cases commodity traders can conclude individual transactions through a third party. Financially strong buyers such as the six crude-oil multinationals can finance the operations themselves as customers. They do so by performing a role traditionally reserved for the banks, that is, by providing traders, who take on the role of middlemen, with credit lines. The traders then get the capital they require for the actual transactions, without having to provide bank guarantees (open accounts) – the standard scenario for deals with the oil majors.

However, in all other cases individual transactions require involving the banks. Generally, financial institutions grant these types of temporary loans in the form of documentary credits or letters of credit. A letter of credit is a type of bank credit granted to a trader in exchange for a lien against real goods FIG. 2. Normally, the quantity and quality of these goods are confirmed in the delivery or transport documents, which are usually issued by an inspection and certification company. The shipment acts as the bank's security – in effect, the bank becomes the temporary owner of the goods. On the due date of the transaction the trading company receives the money from the buyer, with which it repays the loan plus interest.

Designing and using financing instruments for commodity deals, above all transactions against letters of credit, has been a Geneva speciality for a long time CHAP. 4. It is expertise like this that enabled the trading region on the southern shores of Lake Geneva to develop in the first place. Meanwhile, the 'commodity trade finance' business continues to boom. At Crédit Agricole, for example, the number of employees working in this sector has doubled since 2005.[2] In 2009 the Geneva Cantonal Bank announced a healthy 7 per cent increase in its profits in this sector.[3] Yet such credit dealings are not without risk. For example, in December 2010 a Geneva bank syndicate under the direction of industry leader BNP Paribas lost 135 million dollars, which had been lent as credit to the Lausanne subsidiary of the Russian trading company RIAS. The banks believed they were guaranteed by several thousand tonnes of wheat in a depot in southern Russia, but this proved to be a fallacy.[4] Thus the certification confirming the quality and quantity of the goods, which is used as security in these types of transactions, is crucial. The fact that the world's leading inspection and certification company, SGS, has its headquarters in Geneva, gives this marketplace another decisive advantage.

FIG. 2

TRADE BY MEANS OF LETTERS OF CREDIT: PROCESSES AND PLAYERS ILLUSTRATED IN THE EXAMPLE OF AN OIL DEAL



Source: Authors' illustration

HISTORY //

Despite a UN embargo supplies of the 'black gold' to the pariah apartheid regime in South Africa continued. This posed no risk if it was done from Zug since Switzerland boycotted this UN boycott.

04 //

HOME OF THE TRADERS: SWITZERLAND'S RISE TO A COMMODITY TRADING HUB

The area now occupied by today's Switzerland has played an important role in internal European trade since the Middle Ages. In the slipstream of the colonial powers some of the Swiss trading houses rose to become important players in world trade in the 19th century. However, none of the traditional, great trading houses lived to see the 21st century and today there is hardly a trace of the historic trading houses left in Switzerland. Hence their legacy cannot offer a convincing explanation for Switzerland's rise to commodity trading centre.

It was really in the inter-war years that Switzerland's course was set for the success that came into its own after World War Two. Unashamedly attractive tax rules made some cantons irresistible to the new arrivals and migrant companies, which were crucial to Switzerland's development into the commodity trading hub it is today.

One of the first of these businesses that are still important today settled in Geneva in 1946. It was not a trading company, however, but one of the key service providers of the new sector. Founded in Rouen in France in 1878, SGS, which offers inspection, verification, testing and certification services, was given the job of monitoring the implementation of the Marshall Plan after World War Two. Having been spared the ravages of the war, Geneva in neutral Switzerland was the ideal location for this.[1]

In 1956 the first migrant company among the traders, and still a major player today, arrived in Geneva. Attracted by tailor-made tax concessions, the US grain trader, Cargill, opened its European branch there.

'REMOTE CONTROLLED': LOCATION PROMOTION ZUG-STYLE

Holding companies, i.e. companies that manage holdings in other companies, have been enjoying tax privileges in the rather rural Canton of Zug since 1924. These special rules were extended in the 1930 Tax Law and still apply in essentially the same form today CHAP. 14. The first draft of this law came from the pen of Zurich commercial lawyer, Eugen Keller-Huguenin, who played a crucial role in formulating tax law in the Canton of Zug in the interests of Zurich as a financial centre.[2] The new law granted tax privileges to not only holding companies but also domiciled companies, i.e. companies that do not conduct domestic operations. In actual fact, a 'domiciled company' was, and still is, merely a euphemism for a brass plate company, which was not permitted either to employ staff nor use office space in Zug. Finally there were also the mixed companies, a Swiss innovation first mentioned in 1930. Although these companies had to conduct most of their business abroad, they were allowed to operate in Switzerland as well.

Holding and domiciled companies were (and still are) exempt from the cantonal tax on profit; at that time they only paid a minimum rate of between 0.05 and 0.15 per cent on their capital. For the mixed companies it became normal administrative practice in the late 1950s to tax domestic profit (no more than 20 per cent of business transactions) at the standard rate, but only a quarter of the profit earned abroad was taxed at all – a cantonal rule, which benefited above all international trading companies also operating in Switzerland. Concerns about this financial policy, which were to prove more than justified later on, were raised in the very first debate in the Zug Cantonal Government. For example, the Catholic, conservative politician and later Federal Councillor, Philipp Etter, feared that "the enactment of the proposed law might attract companies to the Canton of Zug, which will bring the canton more trouble than joy".[3]

IN ZURICH'S WAKE AND OTHER BOOM CONDITIONS | Otto Henggeler, as Zug Finance Director from 1919 to 1946, had passionately pushed for tax privileges. But he did not live to see this strategy bring the hoped-for additional revenues to the canton because of the Great Depression, World War II and the post-war economic difficulties. But he did not live to see this strategy bring the hoped-for additional revenues to the canton. Not until the late 1950s did the number of incorporated companies in Zug begin to rise, and then the rise was rapid. Around that time, however, other Swiss cantons began to offer tax privileges similar to those in Zug, so even more incentives were needed to encourage the boom that was occurring. In this connection, Zug's proximity to Zurich, both geographically and because of Zurich's active pursuit of its own interests in the formulation of the Zug tax laws, played a central role. In the late 1950s and early 1960s it was mainly commercial lawyers from Zurich's Bahnhofstrasse who recommended the Zug location to their international clients. In addition, Zurich bankers also opted for the neighbouring canton on the grounds that a shell company in Zug was the ideal vehicle for tax evasion by private individuals.

Added to this was the fact that the standard practice of the tax authorities was extremely helpful to the companies. A politically decreed 'tax truce' was deliberately cultivated and further concessions were not ruled out for attractive potential clients. This was perfectly managed by a network of law offices and fiduciary services agencies, which were able to process the formalities in a particularly efficient and 'client-oriented' manner. Hans Straub for instance, the Zug Finance Director of the boom years, sat on 82 (!) boards of directors and continued to manage his private law practice in his official office at the same time. His ministerial secretary said later, "At that time the state and private sectors were one and the same thing. I handled business incorporation, documents, work permits and everything else connected with them."[4]

After World War II Switzerland was highly attractive for trading companies for another reason; it was one of the few countries whose currency was freely convertible. This meant that an unlimited amount of Swiss francs could be exchanged for other currencies. Moreover, the import and export of capital was not subject to any restrictions or government controls whatsoever, an exception at the time.

FIRST NEW ARRIVALS: THE METAL MEN ARRIVE | Among the first key new arrivals to the shores of Lake Zug was Philipp Brothers in 1956, then the world's largest trading company for minerals and metals. Philipp Brothers is of paramount importance to the emergence of Switzerland as a commodity hub because their arrival marks the beginning of trading in 'hard' commodities – metals and ores. The traditional houses had only traded in 'soft commodities', i.e. agricultural commodities. With oil, which Philipp Brothers added to their portfolio in the 1970s and which soon played a pivotal role, they brought together all the commodities that are still important for Switzerland as a commodity trading centre to this day. Despite the epoch-making significance of Philipp Brothers for the most recent economic history of the country, the only book ever written about this company is not available in any Swiss library. This cloak of silence over Philipp Brothers is all the more astonishing when one considers the media interest that their most famous trader, Marc Rich, has attracted for decades.

Philipp Brothers goes back to two German brothers who began trading metals in Hamburg in 1901 and quickly expanded to London and the USA, where New York became the company headquarters. Just how much importance was attributed to the Zug subsidiary can be seen from the fact that Sigmund Jesselson managed the office. His younger brother, Ludwig, was one of the two principal shareholders in the business, then still Chief Financial Officer, shortly afterwards CEO and later Chairman of the Board.[5] The shrewd banker, Sigmund Jesselson, was the right man to get the very best out of the new location both financially and as regards tax: "[H]is strength was in tax, legal and financial matters; it was he who made sure that everything was correctly done, legally and accounting-wise." The Zug subsidiary, slated to become the European headquarters, was soon handling a considerable part of the global business.[6]

Many commodity traders, who became successful when working independently, learned their trade at Philipp Brothers (later Phibro, after various mergers). The best known is Marc Rich and his partner, Pincus Green, with Green always greatly overshadowed by Rich. Philipp Brothers had already done many of the things in Zug, which Rich, Green and their company later repeated. For example, they brought the right people on board: Hans Hürlimann, a member of the Zug Cantonal Government and later Federal Councillor, was a director of Philipp Brothers, and the Zug Federal Attorney, Rudolf Mosimann, became a director of Marc Rich + Co. AG. When Rich was indicted in the USA, Mosimann had to resign – but as a federal attorney, note, not as a director of the company.

'RIGHT PLACE, RIGHT TIME': MARC RICH AND THE REBIRTH OF THE OIL TRADE

Marc Rich, American of a German-Jewish refugee family, began working for Philipp Brothers in New York in 1954, after giving up his marketing studies. Like all beginners, he started in the transport department but very soon worked his way up. In 1967, the then 32-year old Rich was appointed manager of the Madrid branch of Philipp Brothers. Although the managers of the foreign subsidiaries were known as the 'prodigal sons' inside the company, according to A. Craig Copetas, Rich's first biographer, the job had one enormous advantage: direct access to the European nerve centre of Philipp Brothers in Zug, Switzerland.[7]

Following on from his successes in the emerging oil trade, Rich wanted more than his annual salary of 100,000 dollars. In 1974 he demanded for himself and Pincus Green a bonus of 500,000 dollars each.[8] When this was refused, he left the company and, together with Green and other former colleagues, set up a company in Zug, Marc Rich + Co. AG. Born in Brooklyn in 1934, Pincus Green never became anywhere near such a public personality as Rich, yet, without him, the company they ran together would never have been a success. Green was a transport and finance specialist with decades of experience and had retained highly exclusive contacts from his time as a chrome and copper trader at Philipp Brothers.[9]

At the time, it was a nasty, bitter parting. Indeed, Rich's new company succeeded in poaching staff and therefore customer contacts and business from Phibro. As early as the mid-1980s, shortly before Phibro's departure from Zug, the legendary Swiss journalist, Niklaus Meienberg, recorded how someone who was employed at Phibro at the time described the atmosphere. Apparently relations between Phibro and Marc Rich were more than strained: every Phibro employee had to sign a declaration to the effect that he/she would not have any personal or business dealings with Marc Rich's people.[10]

AN END TO THE OMNIPOTENCE OF THE SEVEN SISTERS

In the 1970s the oil market underwent a dramatic transformation. The abundance of the black gold that had fuelled the post-war boom came to an end. Now it was no longer the customer who was king, but the supplier. The West's consumption rose from 19 million barrels (just under 159 litres) a day in 1960 to more than 44 million barrels a day in 1972.[11] At the same time the US was no longer producing an oil surplus, but became a large oil importer itself. The effects soon became apparent – and they were dramatic.

In the Yom Kippur War between Egypt, Syria and Israel late in 1973 the Arab producing countries primed their 'oil weapon'. They strangled production and imposed an embargo on supplies to the United States and Great Britain. It was not the first time oil had been used to apply pressure. The Arab states had already attempted the same thing during the Suez Crisis in 1956 and in the Six-Day War in 1967. At the time the Americans simply fired up the pumps and produced more oil. But by 1973 these 'surplus reserves' were no longer available. The industrialised countries experienced the first oil shock with prices rising by leaps and bounds, and supply shortages.

Even before this the producing countries had begun to increase their share of the oil revenues. After the fall of the monarchy in Libya a young colonel named Muammar al-Gaddafi called for an increase in the 'posted price', that is, the price the oil companies (who at that time also owned the oil in the ground) paid the producing countries. Other countries followed suit and OPEC likewise decided to increase the price of oil. The 'posted price' rose from 1.80 dollars per barrel in 1971 to 11.65 dollars by December 1973. In the end, it was the deployment of the 'oil weapon' that led to the biggest price hikes: at the beginning of October 1973 the price had stood at 5.12 dollars but passed the 11 dollar mark by December of the same year.

Price was not the only bone of contention between the oil-producing countries and the oil multinationals, at the time still dominated by Anglo-American oil companies: Jersey (Exxon), Socony-Vacuum (Mobil), Standard of California (Chevron), Texaco, Gulf, Royal Dutch/Shell and British Petroleum, together known as the 'seven sisters'. In the early 1970s the producing countries ended the system of concessions CHAP. 17 and nationalised the oilfields. This marked the end of the domination of the 'seven sisters'. Until then it was they who had owned not only all the oil reserves discovered in their concession areas, but also the production plants, pipelines and tanker fleets, as well as the refineries and networks of petrol stations.

Now it was the turn of the producing countries to become the pivotal players in the oil trade. In 1973 the OPEC countries were still marketing a mere eight per cent of their production themselves; by 1979 it was 42 per cent. The significance of the spot market also began to increase dramatically CHAP. 3. This market had been a marginal phenomenon for a long time, a market on which refineries might sell their surplus production. In 1979 only eight per cent of oil was traded on the spot market. By 1982, following the second oil shock, over 50 per cent of the international trade in crude oil was conducted via the spot market or at prices based on this.

A year later the New York Mercantile Exchange, the world's largest stock exchange, introduced trading in oil futures contracts. These enabled speculation in 'paper oil', in other words, securities based on the price of oil. The transformation of the oil markets was complete. [12]

PROFITEERS OF THE OIL CRISIS AND SPOT MARKET | It was during these turbulent times that the oil traders entered the world stage, as Daniel Yergin describes in *The Prize,* his epic tale of the age of oil, for which he was awarded the Pulitzer Prize. Oil traders became all-important and upset the market even further during these volatile, unregulated and chaotic times. The collapse of the virtual monopoly of the integrated oil multinationals gave the traders vast room to manoeuvre. The state-controlled oil companies in the OPEC countries, which by then owned a growing share of total production, did not have any distribution channels of their own. They sold their oil on to the large oil companies, independent refineries or to the traders, who in turn sold it on to smaller oil companies and independent refineries. The traders made their best deals when they succeeded in procuring cheap 'contract oil' via long-term contracts and selling it at much higher, short-lived yet extremely lucrative, spot prices. According to Yergin, all a trader had to do to secure a contract "was to pay a ridiculously small commission to the right people".[13]

BRIBES, CRIMINAL CONNECTIONS AND HUSH MONEY | Marc Rich + Co. AG profited from direct contacts within the innermost circles of power of the Shah of Persia, which Pincus Green had established at Philipp Brothers. Not only Iran, but also Nigeria, itself notoriously corrupt even in the 1970s, were Rich's main suppliers. In a largely uncritical biography by Daniel Ammann, Rich himself does not deny having paid bribes.[14] Here too, Switzerland offered a brazen advantage: 'commission payments', i.e. bribes, could still be paid into Swiss bank accounts, numbered, anonymous, and secret accounts. In addition, up until 1 January 2001, bribing foreign officials was totally legal in Switzerland, and not only was it legal, but the money used for this could even be deducted from taxable profit as 'allowable business expenditure'.[15]

The most lucrative deals could be made when oil bought cheap via long-term contracts could be sold when the spot price shot up. This was the case during the second oil shock between 1979 and 1980 when Iranian oil, a substantial share of the global supply, almost completely disappeared from the market temporarily in the chaos following the fall of the Shah and in the Iran-Iraq War. However, this was followed by the Latin American debt crisis, a worldwide recession and then another long phase of low oil prices. During this time the spot price was usually below contractually agreed prices.

Yet, even then Marc Rich + Co. AG was able to make a great deal of money by conducting the type of transactions the other giants in the industry would not touch. For example, the company supplied the pariah apartheid regime in defiance of the UN oil embargo. South Africa paid eight dollars more than the spot price just to get at the 'black gold' it needed to survive during the boycott. Even this trade did not pose a risk if it was done out of Zug since Switzerland was not a member of the UN and placed commercial interests above the consensus of the world community. Given his close business connections to the South African apartheid regime, Rich was in the best company among the Swiss banking and commercial elite. Rich's friendly biographer, Ammann, describes the dealings with South Africa as his "most important and most profitable" business: Rich admits to having made a profit of two billion dollars from this alone. How crucial a factor Switzerland as a location was for the business with South African became apparent when Phibro moved from Zug to London in 1985. They had to leave their South African operations behind and they were handed over entirely to Newco, set up in Zug by former Phibro people .

Even war could prove good for business: Rich admits to having been for a long period of time the sole trading representative for Angola, whose population had been suffering under a bloody civil war and a proxy war waged by the great powers since 1975. He also held a stake in the state-run oil company, Sonangol, until 1983.[16] As had been the case already at Philipp Brothers, the top managers at Marc Rich + Co. AG were linked directly to the success of the business as shareholders. This was a much better way of ensuring the degree of secrecy that was essential in a business driven by corruption, nepotism and greed, than by using simple confidentiality agreements.

TAX AVOIDANCE, PARDON AND PATRICIDE | Marc Rich + Co. AG was legally headquartered in Zug and the tax privileges it enjoyed there were vital for its commercial success. However, during the first years of its exponential growth, Marc Rich and his management team resided in the luxury New York offices of its US subsidiary, Marc Rich International. In September 1983 Rich, Green and their company were indicted in the United States. The charge sheet listed 51 crimes in total, including tax evasion to the tune of at least 48 million dollars, and organised crime. If found guilty, the sentence would amount to 325 years in prison.

One aspect of the charges proved fatal for Rich's image in the United States: trading with the enemy. The employees at Marc Rich + Co. AG had not left Iran after the fall of the Shah, and the Ayatollah's regime continued to do business with Rich. Even after the United States had imposed an embargo against Iran and while US citizens were still being held hostage in the American embassy, his company continued to buy and sell Iranian oil.

After the indictment Rich and Green fled to Switzerland, as safe a haven for tax refugees as it was for the proceeds of tax avoidance. Just a year later the two companies Marc Rich + Co. AG and Marc Rich International confessed to tax evasion in the United States and paid a settlement and fines, which together totalled 200 million dollars. However, the charges against the main perpetrators, Marc Rich and Pincus Green, remained.[17]

Switzerland refused to give the United States any legal assistance, either by extraditing Rich and Green or by handing over the requested documents to the US authorities. Now wanted men, the two company leaders took advantage of the fact that tax evasion does not constitute a criminal offence in Switzerland. Both tax offences and sanctions breaches are explicitly omitted from the Swiss Act on International Mutual Assistance in Criminal Matters of 1981: 'A request shall not be granted if the subject of the proceeding is an offence which appears to be aimed at reducing fiscal duties or taxes or which violates regulations concerning currency, trade or economic policy.'[18]

Since Rich and Green never appeared before a US court, they were never charged. On his website (under 'corrections in the media') Rich carefully documents all the counter-arguments to articles in which he is described as a 'convicted' tax criminal. With the help of a former legal advisor to Bill Clinton (monthly salary 55,000 dollars), the favourable testimonies from prominent figures (from the former Mayor of Zurich, Josef Estermann, to Shimon Peres), the efforts of his ex-wife (who is one of the major donors to the democratic party) and having gained immediate access to the President by circumventing the usual route, Rich and Green were pardoned by President Bill Clinton on his final day in office.[19]

However, by that time Rich had already lost his importance as both a real, dominating personality and as a symbolic figure in the commodity trading centre Switzerland. Just as his departure from Philipp Brothers was viewed as 'patricide', it was now Rich's turn to suffer a similar fate. In 1993 he was ousted by the top managers in his company, which was rechristened Glencore CHAP. 7.

At the start of this dispute Claude Dauphin, one of those in charge of the oil business, and Eric de Turckheim, along with four more top managers had left Rich's company and founded Trafigura in Lucerne in 1993 CHAP. 7. People who had learned their trade at Phibro or under Marc Rich led many other smaller commodity trading companies, located predominantly in Zug. Most of these have since been liquidated or survive only as niche companies. Advances in technology proved fatal to the small and medium-sized trading companies."The Internet injected a great deal of transparency into the metals trade and transparency has always meant falling margins," said the President of Newco, Phibro's successor in 2001.[20] Only two years later Newco also went into liquidation and was officially deleted from the commercial registry in 2010.

LETTERS OF CREDIT & CO: NO BANKS, NO COMMODITY TRADING

Marc Rich's success story would not have been possible were banks not willing to advance him the money for his trade deals. When it was set up, Marc Rich + Co. AG had capital stock worth only a little over one million Swiss francs. Unlike a listed company, a privately owned business such as the one belonging to Rich, cannot obtain additional capital by issuing shares for investments and acquisitions. Consequently, it depended on borrowed capital, first and foremost from bank loans. Without the active support of one or more financial service providers, traders cannot move the vast sums that are customary and necessary in the commodity business. The primary financial instruments employed are lines of credit and commercial loans known as letters of credit.

A line of credit allows a company to draw down a limited sum of money. The company must pay a small basic fee for this facility, regardless of whether the credit limit is exhausted or not. In the 1970s the banks were lending sums between twice and five times the estimated value of the businesses borrowing the money. Even at the start of his own business Rich's line of credit, according to his biographer Copetas, was approximately 50 million dollars.[21] This demonstrated a remarkable degree of faith by the banks in a business that was no more than a handful of traders, some telephones in a four-room Zug apartment and a single telex machine that stood in the bathroom out of a lack of space. In contrast, the contacts, which Rich, Green and his partners took with them from Phibro were highly lucrative. This fact was not lost on the banks.

Specialised credit instruments were developed for the trading business, known as 'letters of credit' CHAP. 3. According to Trafigura co-founder, Eric de Turckheim, it was thanks to this system that companies with just a fraction of capital were able to carry out operations costing several million dollars.[22] Unlike classic loans, the number and size of these letters of credit are not based on a customer's financial circumstances and soundness, but merely on the plausibility and profitability of a planned specific transaction or a series of consecutive transactions. For example, a bank loans money for a shipment of wheat or oil, which passes into the bank's possession as collateral while they are shipped from the supplier to the customer. Once the goods are delivered, the partner banks release the payment for the shipment. The trader receives the money, which is then used to pay back the loan and any interest payments to the bank. This enables traders with no capital of their own to make hefty profits. The banks for their part need to acquire a great deal of expertise about shipping logistics, insurance and the quality of the goods they are financing to make decisions on such loans:. They are assisted by specialist inspection and verification companies, such as Cotecna or SGS.

ZUG HAS ITS KING, GENEVA ITS POPE.

A banking expert completely unknown outside the industry perfected this system of financing. As far back as the early 1970s Christian Weyer, a Frenchman by birth, discovered the potential of trade finance when working for the Banque de Paris et des Pays-Bas (Paribas, known as BNP Paribas today) in Geneva. According to the newspaper *Le Temps* Geneva's position as the world's leading centre for the sector now defined as 'commodity trade finance' can actually be attributed to Weyer. He is called the 'pape du négoce' (pope of trade). For the prominent figures in the Swiss commodity business apparently only superlatives fit – and the king's throne had already been given to Rich.[23]

At the start of his career Rich relied heavily on both Paribas and the American bank, Bankers Trust. "They liked the business. They opened letters of credit whenever and wherever we needed them," Rich told his favourite biographer.[24] In his one and only interview Weyer himself recalls another important business partner: "One of our first customers was a neighbour of the bank. He was a coal trader and we began to finance his team. Today they are Vitol, one of the giants of the oil trade."[25]

In 2007 the Geneva branch of BNP Paribas had a market share of 40 per cent and employed 370 staff in commodity trade finance. In second place with 15 per cent was Crédit Agricole (120 employees), which was also French and located very close to its great rival on the banks of the Rhone. Third place is now held by Credit Suisse (250 employees), which started in this business in 1989.

TRADING CENTRE GENEVA: SERVICE CENTRE AND OIL MECCA

Not only the banks, but also many more companies are located in Geneva; together with the commodity traders and specialised financial institutions, they make up the 'commodity trading industry cluster'. Specialised insurance companies, consulting firms, security, logistics and haulage companies and the world's largest inspection and verification company , SGS, all profit from commodity trading in Geneva.[26]

As expected in the second-most important UN city, it was Geneva's internationality that fuelled the commodity trade, closely bound up as this was with the political interests of all manner of countries. The communist Soviet Union, for example, became a leading importer of commodities in the 1970s. At the time the Russian consulate in Geneva acted as the main procurement agency for this giant state. With the end of the Cold War the former Soviet Union was de-industrialised and, thanks to the oil fields that were opened up in Siberia and Central Asia, the former Soviet Union soon became a leading producer of commodities. Since the turn of the century Russian and Kazakh oil has contributed to Geneva's status as the world's leading oil-trading centre CHAP. 11.

The most recent and exciting development of Switzerland as a commodity hub is only just beginning; it has been discovered by China. The Chinese state-controlled oil company, Sinopec, the seventh-largest company in the world,[27] took the first step when it acquired Geneva-based Addax Petroleum from Jean-Claude Gandur for 7.8 billion Swiss francs in 2009.[28] Addax operates principally as an oil producer in Nigeria and Iraqi Kurdistan. The involvement of Gandur brings full circle the process that started with the arrival of Philipp Brothers in Zug back in the 1950s. Gandur worked for Phibro as an oil trader between 1976 and 1984 and was therefore one of Marc Rich's successors.

INTERIM CONCLUSION: WHY SWITZERLAND?

It is possible to argue that three forces explain Switzerland's rise to a commodity hub:

- The country's lack of UN membership and an economic and socio-political context that would not impose commercial constraints at any price, even when there was consensus throughout the world, as in the case of the boycott against the apartheid regime.
- A robust financial centre with both large domestic and foreign banks and the free movement of capital associated with this.
- Special tax rules, which attracted trading companies in particular and allowed domestic and foreign commodity traders to optimise their tax payments.

The crucial year for the boom in the industry we see continuing to this day was 1956 when the first heavyweights, Philipp Brothers and Cargill, moved to Zug and Geneva respectively. From about the mid-1970s onwards the commodity cluster created its own dynamic: Well-established commodity traders attracted new commodity traders and the service providers on which the business depended. Referring to these dynamics, an oil trader in Zug puts it like this: "It's like a snowball. Once you've created a small ball it just gets bigger and bigger."

ZUG //

Around 26,000 people and almost as many companies are currently registered in this boom town. Most of the buildings under construction are for corporate entities even though many of them need no more than a letterbox.

Glencore, Baar – 2011

05 //

CENTRAL SWISS IDYLL: APPOINTMENT IN RICH COUNTRY

When the leading Anglo-Saxon media report on Glencore, they often include its geographical location, for example, "based in the unassuming Swiss town of Baar, next to Zug and near Zurich."[1] But what traces, if any, do the commodity traders leave behind them in Zug and the surrounding area? And just how visible is the industry leader founded by Marc Rich? A flying visit by public transport.

Zug, the Porsche paradise and canton with the highest concentration of cars in the whole of Switzerland, can be reached comfortably by train. Once an hour and directly from Zurich airport. On a train with noticeably more than its fair share of first-class carriages, most of which are occupied even on a dull April morning, the journey takes less than three-quarters of an hour. The Swiss Federal Railway's exceptional service to Zurich's gateway to the world is definitely an additional locational advantage of Zug, and is no doubt due to the mobile manager caste that often cultivates closer relationships with London, Singapore

or Buenos Aires than with its own business address and tax domicile. Commercially, the direct connection is doubly attractive: it saves on the horrendous multi-storey car park charges as it gains valuable work time, preferably spent on a Blackberry. Since the trains are equipped with laptop charging facilities and designated 'quiet' wagons.

"Yeah, coal went straight up. But watch out, the markets are going nuts, it's gonna be a wild ride today. And forget lunch, they served splendid breakfast on the plane." You had to listen very closely indeed to be able to note down even snippets of the words spoken by the elegantly yet unobtrusively dressed man in his mid-thirties sitting diagonally opposite you in the compartment. He spoke hastily yet authoritatively in a rasping voice and in a dialect that was almost impossible to place. Australia perhaps or more likely South Africa? At any rate the man was in his element, but lowered his voice the moment he suspected others of listening in on his conversation. So the reporter put down his pencil and, after the Zimmerberg tunnel in Thalwil, his gaze wandered first to Lake Zurich, glistening through the strands of mist, next, after the Albis underpass, to the pastures and woodland slipping past, which announced the train's arrival in 'Zugerland'.

AS MANY COMPANIES AS THERE ARE PEOPLE – MORE OF AN INCENTIVE THAN AN ATTRACTION

The train glided through the industrial belt, past plain commercial buildings and cool glass façades and into the canton's capital where it was greeted by many building cranes – a sign of the massive investments. Around 26,000 people and almost as many companies are currently registered in the boom town. Buildings are being constructed all around the train station situated at some distance from the old town and the lake, most of them for corporate entities, despite the fact many of these need no more than a letterbox. In a 1984 account of its development from a poor, agricultural Central Swiss canton to an attractive yet anonymous business location, Zug was described as a mushrooming, amorphous, rampant town with an incongruously dressed-up old town planted like a Disneyland right in the middle of the new buildings that had shot up out of the ground like weeds.[2] Worries about the town's evident loss of identity and the increasingly acute pressure on space prompted even the Swiss daily *Neue Zürcher Zeitung,* known for its support of economic liberalism, to ask whether the limits of growth were now visible in Zug.[3]

If you exit the oversized station and head towards the 'Metalli', a former metal goods factory converted into a large shopping mall, less than 50 yards further on you will find yourself standing in front of the largest visible legacy of the man whom many people here and abroad still regard as the commodity trader par excellence, Marc Rich. In contrast, Zug's inhabitants saw this man as their own JR Ewing and in the 1980s rechristened the company headquarters, the 'Dallas-Building' after the legendary US TV series portaying the most unscrupulous TV oil magnet of all time. Dating from the same time is the saying by the former mayor of Zug, Walter Hegglin, that what was good for Marc Rich was also good for Zug. At the time still an architectural landmark for the respectable, unassuming provincial town, the glass cube only suggestive of transparency is today flanked by a whole row of equally tall but less conspicuous office complexes. Since the 'rebranding' of the Marc Rich + Co. AG into Glencore and its relocation to a nearby industrial area, the Zug Cantonal Bank now occupies the building at 37 Baarerstrasse.

REFUGE FOR THE 'REFUGEE OF THE CENTURY'.

Anyone from this famous, even notorious, address wishing to enter the glass courtyard had merely to cross an inconspicuous car park. Previously this restaurant with its circular bar (including the penthouse opposite) also belonged to the local Rich business empire. Rich himself used to have lunch regularly in these same rooms in an atmosphere reminiscent of charming, prim 1950s tea rooms, sometimes with, sometimes without, his bodyguards. A favourite story concerns an episode when a journalist went up to the table that was permanently reserved for the 'refugee of the century' (*Washington Post*) and, politely yet firmly, requested an interview with the latter. Rich fled to the toilet, climbed out of the window and hurried back to his high-security office wing. The jittery ex-tycoon sold his unofficial canteen along with the company in 1993 and has been living in even more tranquil Meggen on the shores of Lake Lucerne ever since.

My local guide Josef Lang, a progressive politician and long-term Rich critic, tells me that until the glass courtyard was converted into today's Pier 41 dance club you could meet anyone and everyone in Zug at this bar, occasionally even administrative staff associated with the commodity traders. The traders themselves hardly ever meet in public and if they do, they prefer to meet in either the Almodo bar or the elegant Mantra Lounge on the other side of the railway line. On this rainy April day the impeccably dressed chauffeur Viktor was sitting sipping his second Espresso, recounting that he had already picked up a few Russian traders in Geneva early that morning and was about to drive them straight on to Zurich airport, describing them as very pleasant people who laughed a lot and gave good tips. Admittedly, he had had to wait half a day outside a villa in Oberägeri the day before, which was no fun even in an armoured Mercedes S-class. Things seemed to be moving faster that day: his mobile rang and in less than ten seconds later Viktor was en route to his exclusive clients.

A DRIVE IN A DASH OF THE COMPANY'S COLOURS

The reporter too finished his coffee and strolled to the other side of Baarerstrasse. There on the north-western Metalli corner stood a purple minibus with the engine running and sliding door open, on a parking space discreetly marked 'private', although it was clearly hoping for passengers. As I walked past my eyes were drawn to the right front mud

Glencore, company shuttle bus – 2011

flap where, below the logo of the Zugerland Verkehrsbetriebe (ZVB, Zug Public Transport Organization), Glencore's logo was emblazoned. An enquiry to the driver, who was not wearing a uniform, extracted the following reply: this mobile dash of colour in the midst of the greyness of Zug was a shuttle service to the company headquarters situated about a kilometre away. We were informed by the jovial driver in his late forties, on the payroll of the ZVB, that the only people eligible to travel with the minibus were the employees and visitors of the large import/export business, adding that the ZVB had chosen the colour but the vehicle belonged to Glencore. We discreetly mentioned our scheduled meeting at the Fontana restaurant at the Glencore headquarters and the driver first frowned but then gestured for us to get in.

Before the largely empty minibus turned off into Industriestrasse on its round trip, we noticed the sophisticated mirror façade of the Hotel City Garden, which looks like a recently landed UFO for those dressed in pinstripes, located on the edge of a residential neighbourhood. Continuing, the road led right through what is commonly known as the 'Zug oilfield', past an unattractive mixture of workshops, small businesses and blocks of flats. Occasionally the names of unfamiliar refinery, pipeline and petrol station businesses flashed past and after the next right-hand bend a white cube appeared with two large company signs (Shell Switzerland and Glencore) and many small other ones. It was only when the eye-catching minibus had passed through the unobtrusive entrance that it became clear: these were the premises of the largest commodity corporation in the world.

BUSINESS LUNCH IN GLENCORE'S CANTEEN

Before the two security guards posted in front of the unassuming main entrance received the new arrivals, I slipped through the passenger door onto the public pavement and walked round the building complex that Glencore has rented from the Schweizerische Unfallversicherungsanstalt

(Swiss National Accident Insurance Organization). Just before noon not a sound emerged from the building, and not a movement was visible behind the blinds. “Glencore is looked on as the guys screaming into telephones, but it’s more the dull old business of logistics. Glencore trading floors are more like DHL offices than Goldman Sachs.”[4] The white hulk sandwiched between industrial neighbourhood and farmland could just as easily be housing a biotech or telecom company. On the other hand you would never suspect that this secretive command centre of an economic world power had a rear entrance accessible to the public, let alone that behind it could be found a restaurant frequented by the local community, but belonging to Glencore.

Naturally, I had reserved a table and was very politely placed next to a wall decoration by the Fontana restaurant Chef de Service. The decoration turned out to be a, concealed door to Glencore’s offices. The solid-looking interior and the majority of the casually dressed guests were in sharp contrast to the luxury ‘rolling stock’ on the company car park we had just crossed. My host told me reassuringly that fast cars with large engines were just as much a part of Zug as the sunsets over the harbour or traditional cherry gateau and went on to recommend the fillets of ‘Rötel’, a particularly delicious type of fish from Lake Zug, fried in butter. Meanwhile three elegantly dressed, smooth-shaven young Glencore employees had taken their seats at the neighbouring table. Despite the spring-like temperatures the conversation, conducted simultaneously in English, Russian and German, revolved around Christmas: to be more precise, around the ‘awesome performance’ by Simple Minds at the corporate Christmas event for 500 managers, and to be even more precise, around the 3,000 dollars that one of the three had won for having bet correctly on the top act. Apparently, in previous years Pink, Sting and Bryan Adams had been flown in for the same event. So gala gossip as opposed to company secrets are the talk even of top traders at lunchtimes. The reporter found such banality in big business somehow reassuring, and called for the bill.

"Nafuti Nafuti", the song most played in the last two years in Zambia, is about love – needless to say, eternal love. As soon as it rings out, hardly anyone stays in their seats.

ZAMBIA //

One simply has to dance. Yet the men continue to drink silently, with reddened eyes and a fixed gaze.

06 //

“THIS IS BAGHDAD, JUST WITHOUT WAR.”

In 2009 and again in 2010, the French film journalist Alice Odiot travelled to the Zambian copper mine of Mopani, which is operated by a subsidiary of Glencore, to research the social and environmental consequences of the mining operations. An extraordinary report about taxation lies, sulphur poisoning and Zambian civil courage.

Christopher plays billiards. The table stands in the middle of the pub, the Social Club. In Zambia, anyone who doesn't play billiards well is regarded as suspicious. Christopher lines up his shot accurately and ignores the loud music that fills the room. In Kankoyo, a district in the mining town of Mufulira, people like to listen to loud music. “Nafuti Nafuti”, the song most played in the last two years in Zambia, is about love – needless to say, eternal love. As soon as it rings out, hardly anyone stays in their seats. One simply has to dance. Yet the men continue to drink silently, with reddened eyes and a fixed gaze. Christopher has not drunk anything and with his cue he takes a few more shots. He is happy and self-confident. Even if it takes five years – he is sure that his side will win.

We met Christopher Nkatha for the first time in June 2009. Christopher is a miner. He worked for Mopani Copper Mines plc (MCM), the mining company which exploits the copper deposits in Mufulira. The mining area extends over 19,000 hectares in the heart of the Copperbelt industrial region. Mufulira is situated only a few kilometres from the border with the Democratic Republic of the Congo. It is the last town in the north of Zambia that is accessible via the single, damaged asphalt road leading from the capital, Lusaka, to the neighbouring country.

Here, the Mopani mine operators have built the largest copper smelter in Africa FIG. 1, P. 110 . It is one of the most profitable mining locations in the country. Copper is a strategic metal; no industry, no technology can do without it. Gaining access to copper is like winning a battle, and it means power. Some commodity traders had grasped this fact before the price of the red gold shot skywards and the privatisation of the Zambian mining sector was a bonanza for them. As the owners of the source of the commodity, they have the power to dispose of the deposits. Never before have copper prices been so high – more than 10,000 dollars per tonne in 2011, and all the great powers are eager to secure continuity of supply. Zambia, relatively liberal and with a population of 13 million, but almost 18 times the size of Switzlerand, has one of the largest copper deposits in the world. This country in southern Africa should be swimming in profits but instead it is one of the world's poorest countries, and the reasons are not war or dictatorship. Today, 68 per cent of its population live below subsistence level and 10 million Zambian men and women face the threat of malnutrition.

Photographs in this chapter are by Audrey Gallet and Meinrad Schade. They show the Mopani mine and daily life in Mufulira. Further pictures from the series are found throughout the book.

WORLD BANK, IMF AND EIB IN THE TWILIGHT

Not one of the 12 multinational companies that extract the copper in the country is in Zambian hands. The country's mining sector was privatised at the end of the 1990s and the World Bank likes to describe this privatisation process – one of the fastest in the world – as the most successful in southern Africa. The state-owned Zambia Consolidated Copper Mines (ZCCM) was split up under the strict supervision of the World Bank and the International Monetary Fund (IMF). Among the licenses that were owned by ZCCM, one was for the Mopani copper mine in Mufulira, which at the time was the mine with the greatest strategic importance because it contained facilities for processing copper concentrates into export-ready copper plates.

MCM, the company operating the Mopani mine, received financing from the European Development Fund (EDF), which provides loans to projects for sustainable development in Africa. The mining company received a loan amounting to 48 million euros. The executives of the European Investment Bank (EIB), the EU agency that leads the 'Loans' section of the EDF, told us, "From the environmental point of view, this project is a model." Thanks to the purchase of a new smelter that can capture the sulphur dioxide that is released by the processing of the copper minerals, environmental pollution should be reduced and the skies should again be blue.

The poisonous sulphur dioxide gas would now be converted in a kind of huge shower, the 'desulphurisation plant', and 'fed back to the production process'. Any waste materials would therefore be recycled in this way. In accordance with the Cotonou Agreement, which states that 'the reduction of poverty and the promotion of sustainable development' is at the heart of European-African cooperation, the EIB loan was granted to 'a company under Zambian law' – in this case Mopani Copper Mine (MCM).

COPPER POLITICS AND A KING-SIZE BED

We arrive in Zambia in June 2009. The presidential elections are approaching and the effects of copper mining on the land and the people are among the crucial issues of the election campaign. The Patriotic Front is the strongest opposition party and holds a majority in the Copperbelt mining districts. Almost every day it highlights the consequences of the mining in the only independent newspaper *The Post*. We give no detailed information about the purpose of our trip and obtain filming permits for Zambia. But after a few at the mine word about our presence had got out and we are stopped by the mine's security service and taken to the police station. Clearly, it is not customary to approach the mine with a camera. We are told that we need to apologise to Mr Muulwa, the Chief Superintendent for the Mufulira District. Furious, he phones the regional Governor. Then he hangs up, calms down again and decides to show us his city.

We are led into a department store with imports from South Africa and find ourselves beside a brand new, pink king-size bed. "Of course, Mufulira has plenty of everything," our host assures us. The mine brings the city everything it needs; work and taxes. Mr Muulwa mentions no numbers, but seems very convinced. In the evening he accompanies us to a bar, and the next morning he signs a letter that authorises us to roam his city with camera and microphone. Without prompting, he points out that the tap water here is safe to drink. "It is very good, and we have no problems at all with it," he adds. Now, armed with the authorisation to film, we leave the city centre in the company of Mr Chileshe, an unemployed miner.

Because a rental cross-country vehicle costs 2500 dollars a month, we opt for a small, blue Toyota. We continue along to the mine site. A few children climb onto the pipelines at the foot of the barbed wire fences that surround the site. In white paint are the words 'Do not run on the pipelines, do not sit on them!' The pipes contain a liquid mixture from the copper mining operation. Slag heaps in the form of large artificial hills, piled up from the sediments from the mine, obscure the view of the production facilities in some places. Armed guards are standing atop these small, black mountains. A sign points the way to the entrance to the mine where trucks emerge, loaded with copper plates that are visible under the cover of their trailers, or hauling a silver-coloured tank with a warning in embossed lettering that announces, 'Caution - Acid!'

METAL IN THE MOUTH, MOURNING FOR A BABY

Mr Chileshe takes us to Kankoyo, the Mufulira district that borders directly on the mine site and has 40,000 inhabitants. There are no guards in view here, and the barbed wire has disappeared. At the roadside, a few children play with their kites, which consist of plastic bags nailed to two branches, or they scramble at the foot of the slag heaps from where they pick up pebbles and throw them at each other. Is it possible that these innocent pebbles might contain copper or cobalt particles? The further we make our way along the dusty, bumpy road, the more of the mine complex becomes visible. Bluish, white and black smoke rises up from an incredible jumble of gigantic tubes, pipes and funnels. Our microphones catch the continuous din from the mine. Night and day we hear this uniform loud noise during the entire month of our stay.

For the last half an hour, or since we arrived here, I have had a strange, slightly sweet taste in my mouth. Then it changes, as if I had just eaten the tip of a pencil. It tastes metallic and unpleasant. I breathe through my nose and my lungs contract. I feel a burning in my windpipe.

Mr Chileshe had put his arm in front of his face and is now protecting himself with his jacket sleeve. He smiles, slightly embarrassed. "That is the Centa", he tells us. This is the name that the residents of Kankoyo have given the poisonous gas that streams out from the installations. Sulphur dioxide. You cannot suppress the cough; in fact, the more you cough and then inhale to get some air again, the more it hurts your chest. Our only desire is to escape. Never before have I breathed in air like this. "We have never got used to it either," Mr Chileshe tells us as we enter the

small courtyard in front of Christopher's house. Cracked walls form two rooms under a tin roof eaten away by rust. All the roofs in the district are in this condition. All are marked by the acid rain. In contact with water, sulphur dioxide turns into sulphuric acid. Rainfall is therefore a real threat here, because it makes the soil infertile. Everywhere just dust, making it impossible to grow a vegetable garden or anything else.

Christopher invites us in and introduces us to his family. He has seven children and a wife who is also there. It would take us almost a year before we discovered her real name because everyone calls her "Mother of Junior", who is Christopher's eldest son. He is twelve years old and Cleopatra, his eldest daughter, is 17. She wears a wide, sleeveless T-shirt and pregnancy stretch marks are clearly visible on her skin. However, she just buried her baby two weeks ago. The child lived for only a few months and she has yet to fully comprehend what has happened. She has nightmares. "My baby didn't die of a childhood disease." She says the plant still spews out sulphur dioxide, despite the desulphurisation systems.

Christopher became a grandfather for the first time. Because his daughter was still so young, he was not pleased about it at first, but nevertheless he wanted to provide for the new-born under his own roof. "The baby wasn't doing well, it was short of breath. We brought the baby to the health centre immediately. But there is no doctor there, and the nurses were on strike. And then you smell this air. Just imagine what it does to a baby. You can't be sure of seeing a child growing up here if it hasn't reached the age of one and a half yet." Since the privatisation of health care, medical treatment is not free, the coffers of the Centre are empty and the doctors have gone away. For the treatment of respiratory diseases that have been caused by sulphur dioxide, the nurses have only Paracetamol. The child died in the poorly equipped State hospital, says Christopher. The heat is stifling, Cleopatra looks at her textbook; she would like to go back to school. Beside her sits Mary, a relative of Christopher. He has taken her in too, because her husband is not very helpful, and she is pregnant. Another, even younger girl called "Mother of Margaret", also lives here in Christopher's house with her baby. The

nine square metre living room serves as a bedroom for the girls. In the evening, they spread out the sofa cushions on the ground and lie close to each other with the baby. Christopher and his wife sleep next door with the youngest children. With his income, Christopher feeds 12 people.

AGENCY WORK AND MASS LAYOFFS

We did not meet any women who work in the mine. Their main activity is to sell pastries and some vegetables at the roadside. But a nurse tells us in confidence that clandestine prostitution is inflicting devastating damage here, particularly since the mass layoffs at the mine. When the husband loses his job, the family is left with nothing. Mopani operates two hospitals, which have a good reputation and are open to employees. Why didn't Christopher take the ill baby there? "That is very expensive! I would have had to pay a fortune, because I was an agency worker. You have to be an employee of the mine, and I never was." Half of the Mopani workforce are agency workers. Christopher has laboured for six different employment agencies since 1997. The last time, the agency Pro-Sec got him a job as a foreman. He supervised a 40-man team digging tunnels 1,000 metres underground. "The air there is dangerous, a mixture of gas and dust," explains Christopher, a statement confirmed by investigations in 2008 that reported 'that the inadequate control of silicon dust in these mines can increase the risk of malignant diseases in many miners.'[1] Christopher's goal: an advance of eight metres per day, "otherwise I would have made losses for the company that employs me, which Mopani pays by the metre tunnelled." Agency workers from Pro-Sec are paid only half as much as that of their full-time colleagues – for the same work.[2] At the time Christopher earned 1.2 million Kwacha per month (approximately 272 US dollars). However, the quarterly school fees for a 15-year old child are 450,000 Kwacha, the rent for a house in Kankoyo 300 000 Kwacha.

Between December 2008 and June 2009 there were layoffs of some 3,000 miners at the Mopani mine. The agency workers were first to be affected Christopher received his layoff notice on the 5th of December 2008. One month later he received no more payments; half a year later he had not received even half of his severance pay. To feed his family, Christopher bought two shavers and opened a small hairdressing salon next to his home. But there are no customers in his neighbourhood. Junior helps him and cuts his buddies' hair. One of them tries to admire his new haircut in a shard of mirror. Christopher takes us a few steps further to a canvas hut, where the older boys sleep on a bed frame with broken springs. "I had to borrow money. To repay it, I sold the bed, our two mattresses and my radio. I don't know what to do next. It's worse for my children – that hurts me. I can't borrow any more money for the school." Under these conditions, it is difficult to explain that we want to film his everyday life in order to understand what is happening here. Still, Christopher agrees immediately though, his wife would like to know whether we will pay them for it.

The next day, we set up our camera. 'Mother of Junior' fetches water from a source a few dozen metres away from the house. She fills a plastic canister at a hose that protrudes out of the Earth. Then she freezes a part of this water. Christopher laughs when he sees our inquiring eyes. "That kills the small bugs, but when there's acid in it ... it stays in." Soon it will be meal time and 'Mother of Junior' wants to go to buy vegetables. According to the World Trade Organisation, the price of staple foods in Zambia soared by over 20 per cent in December 2008. Her husband cannot give her any money, and advises her to add a bit of salt to the Nshima, a kind of maize porridge common here, to give it some flavour. Advice like this can be annoying and she flies off the handle, shouting, "How long is it going to take you to repair this bench? Go and find some work; we have nothing more! We have nothing, nothing, absolutely nothing more!" Mary agrees with her. Christopher puts the hammer down. "And where do you think I'll find something? No one in the district has any work, so who is going to give me any?" She yelled once more and then went back into her kitchen. Christopher carried on pottering about.

In the Kankoyo district, four out of five families have no regular income. Here, you work either in the local brewery, where the Chipolopolo is brewed that the miners drink, or in the factory that manufactures the explosive that is used to drive the tunnels. Or you work in the mine.

SCHOOL OR ELECTRICITY?

Two days later, Christopher handed his wife two invoices. “We have to pay 360,000 Kwacha for the school for Loveliness and 530,000 for Junior. And the next electricity bill is due in three days.” Looking at the ceiling, the mother remains poker faced. “What should we do? What is most important? If I don’t have any more electricity, it’s all over with the hairdressing salon. So, school or electricity?”. “The children,” she sighs. A few days later the family are sitting in the courtyard having dinner. The soup was made on a charcoal fire because the stove cannot be used. Two voices are heard in the dark. “Were you there when they switched off the electricity?” Someone lights a candle. The Director sent Eunice, the elder sister, home this afternoon. “She said to me that I would bring dirt in.” She does not go to school the next day, nor in the days following. She is 16 and her school fees are even higher than those of her brothers and sisters.

Christopher’s life is now hell. Rage rises up in him. While he can’t pay his electric bill, the mining industry, which consumes most of the electricity generated in the country, is granted preferential rates, just one of the advantages that this sector enjoys. Furious, Christopher roams the district with us. “Do you see these houses?” There are about 50 of them. “When the mine was still in State hands, 50 full-time miners came from these 50 houses. Now, about five people in this row of houses have a job.” He enters the social club. It is 11 o’clock in the morning and many customers are already completely drunk on the Chipolopolo. A woman dances all by herself in the middle of the room. She does not notice us. A few teenagers sit around idly, and men stagger through the pub brawling.

Christopher takes in the whole pub with a sweep of his arm. “Who here has a job? No one… “ Someone cuts him off, “And you, what do you do, sir? You’re just as much of a slacker as us.” Christopher replies, “Yes, I’m unemployed, because Mopani says it’s not making any profits ...” A man plants himself in front of the camera. He has clearly consumed a lot of alcohol today. He goes down on his knees and stares clumsily into the lens. “Stop the Centa, stop the sulphur dioxide!” Young women loiter, waiting for any unemployed man who is slightly less poor than them to disappear together into the ruins that surround the district. In the bar, mine guard threatens Christopher, who is slowly attracting attention. “You! Watch out. You’ll be arrested and locked up.” Before the bar was opened, there was a social centre here, hence the bar’s name. When the mine was run by the State, there were also training opportunities for women. And next door there was a shop where the miners were issued with food in exchange for vouchers. There were community centres like this everywhere in the Copperbelt industrial region. Many of Zambia’s best footballers and graduates came from here.

THE PLAGUE OF PRIVATISATION

For many years, Zambia was the model of progress for Africa. But public debt has turned the country into an exporter of commodities. Trying desperately to earn dollars to be able to pay its creditors, Zambia has squandered its riches.

It is 1964 Zambia has just gained independence. It nationalises its mines, generates profits and enables its population to have access to education and health care. In 1975 its gross domestic product is at the level of Portugal. Then raw-material prices fall as a result of the oil crisis, without the young national economy having had the time to diversify. Its export-based revenues melt away. Following the advice of the IMF and World Bank, Zambia accepts loans. Then the second catastrophe comes at the beginning of the 1980s. The US Central Bank increases interest rates brutally to attract capital and Europe is not far behind.

So Zambia has to make interest payments that increase three-fold from one day to the next. In July 1989, creditors demand the immediate repayment of the debt if the structural adjustment programmes from the World Bank and the IMF are not implemented. As a consequence, in 1991 the civil service is broken up and school and hospital services become subject to a charge. And in 2000 the mines are sold off at rock bottom prices. Seven years later, Edith Nawakwi, Zambia’s former finance minister and the one responsible for the privatisation policy at that time, said, “the World Bank and the IMF showed us plans indicating that Mufulira’s resources would be exhausted in five years. But by privatisation we could reduce our debt burden. For us this was a beautiful carrot, rather like when a dying man has a pack of medicine waved under his nose. We had no other choice but to comply.”[3] Contrary to all the predictions made by the IMF and World Bank, from 2004 copper prices soar again. But for Zambia this surge comes too late, as almost none of the country’s natural resources belong to it any longer.

OF PROFITS AND CONSCIENCE

Savior Mwambwa sits behind a stack of files. We are in a pleasant district of Lusaka, the capital of Zambia. “If we believe what they say, they never make a profit, but constantly lose money. And they lay people off without us being able to say anything against it, blaming the crisis ... the mining industry uses layoffs as a means of applying pressure on the government. And it works; our new tax law, which would have provided significant government revenues, was dropped.” The learned economist Savior is an activist. He directs the Centre for Trade and Development Policy, a Zambian NGO which denounces capital flight in Africa. He is convinced that Zambia could finance its development if, among other things, the commodity businesses would pay their dues to their host country.

After years of secrecy, the privatisation contracts concluded between the Government of Zambia and the mining companies were published in 2007 – by Savior. “This agreement assigns a minimum of social and environmental responsibility and taxation liabilities to the mining companies. The result is that the Government and people are robbed of the money they need so badly.” Page 7 of the document that Savior produces shows a four-year plan for job cuts. The tax provisions are listed in Chapter 8; one hundred per cent depreciation, no tax deduction at source whatsoever, relief from import duties for machinery. Royalties, a form of taxation CHAP. 17, are specified at 0.6 per cent, which is the lowest rate in the world. The term of the contract, concluded in the year 2000, is 20 years.

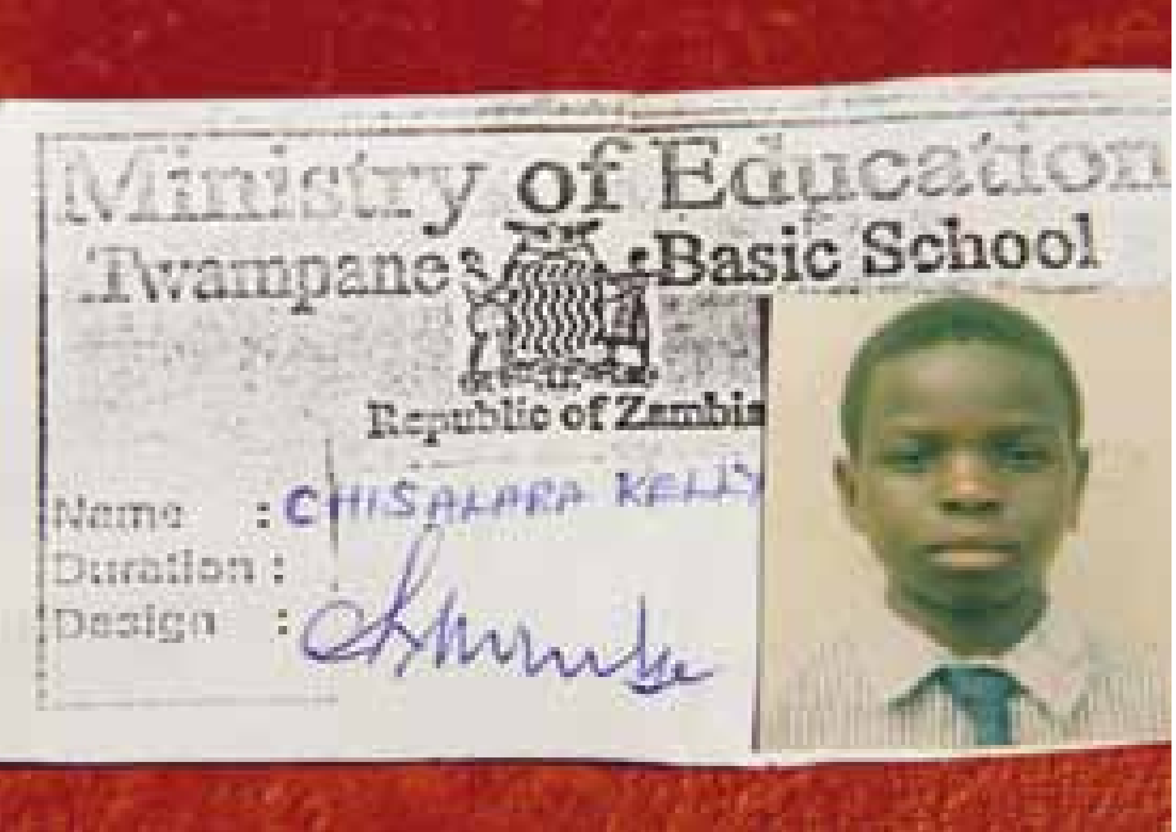
At that time, the IMF and World Bank advised Zambia as a matter of urgency to conclude such agreements in order to attract investors into the country. The operation of the mines by multinational companies was going to solve all problems. When the contracts became public, thanks to Savior, they caused a scandal. For the first time, Zambians understood the causes of their poverty. In April 2008 the Government cancelled the previous contracts with the mining companies and introduced a new tax on the basis of the increased copper prices – the ‘windfall tax’. This brought Zambia new revenues of 415 million dollars. In comparison, the budget for education and health care in Zambia in 2004 amounted to 293 million dollars. Following the temporary collapse of copper prices as a result of the financial crisis and the threat of further mass layoffs, in April 2009 the Zambian Government withdrew the ‘windfall tax’ and introduced new tax measures that, in some respects, were again advantageous for the multinationals.

From Savior, we also learn that more than half all Zambian copper is exported to Switzerland. The country buys eight times more Zambian copper than China and is thus the world's largest consumer of copper. There is a simple explanation. Mopani belongs to Glencore FIG. 4, P. 274, one of the world's largest commodity businesses, based in Baar in central Switzerland CHAP. 7. "Companies like Glencore," according to Savior, "book their profits in affiliates located specifically for that purpose in tax havens. And they sell on the copper within the business. You never know at what price, but in the process the mines evidently make losses. They have the best lawyers and the best accountants in the world. They do whatever they want." Until the start of 2009, Zambia had only two tax inspectors who were responsible for checking the financial statements of the mines. At Zambia's request, an audit was conducted by independent accounting firms during 2009 with the intention of revealing Glencore's subsidiary's financial machinations through which it sought to avoid taxation CHAP. 14. The publication of this report led to the launching of a collective complaint by several NGOs – among them the Berne Declaration (BD) – for breach of the OECD guidelines for multinational enterprises. The complaint was filed at the national OECD contact points in Switzerland and Canada in April 2011.

We ask Wisdom Nhekairo, one of the directors of the Ministry of Finance, how much Mopani has actually paid. "The status of this mining company hampers the taxation of its profits," is the answer. Of the twelve multinational corporations operating in Zambia, only one reported profits in its 2009 tax return . The Zambian state scarcely profits at all from the copper extracted in the country. According to MEP Eva Joly, whereas in 2006 Norway was able to retain 70 per cent of the value of its oil exports, in the same year Zambia kept only a paltry 2 per cent of the value of copper exports.[4]

In a nice hotel in Copperbelt Province, by chance we meet Dimitri, a Glencore consultant. "The management of Glencore are intelligent people. When they invest, it has to pay dividends. Zambia is, of course, a very good investment object." For Glencore, he is training a ten-man team of Kazakh engineers in a new production method developed by Mopani. In his room, Dimitri irons his shirt and with bare torso he explains that "acid is injected into the deposit, the acid penetrates it and leaches out the metals. The mixture is stored in reservoirs and then pumped to the surface. The copper is then extracted by means of hydrolysis." In effect, with this leaching process large quantities of sulphuric acid are being injected directly into the lower soil layers of Mufulira every day. The method is normally used in uranium mining – due to the radioactivity. This way, the miners do not come into contact with the raw material; the acid takes over their work. This leaching technique causes devastating environmental damage, but it is profitable; the copper can be produced more rapidly and with far fewer workers. Had not been possible to use the acid method at Mopani, the European Investment Bank would not have provided any loans. Thus, the objective of this 'aid programme' was obviously to increase the profitability of the smelter, to sell the surplus, and to lower production costs – and all this with the money that was intended for development projects that reduce the environmental impacts of extracting and refining.

Underneath the deposits into which hundreds of litres of sulphuric acid are injected every day lays the drinking water aquifer of the municipal company Mulonga Water. There is a system of pumps that should prevent acid from infiltrating there. Nevertheless, on 2nd January 2008 more than 800 people were poisoned by this drinking water. One of them was Junior, Christopher's eldest son. He still remembers it very clearly. "When I went to the hospital, there were lots of people there. They were all complaining of feeling unwell. I was afraid I was going to die."



A year later we are here again. This time we travelled to the mine with an activist from a French NGO who, together with Savior, denounces Glencore's machinations in Zambia.[5] Savior was looking for a spokesperson for the victims of the mass poisoning. In Kankoyo, Christopher was his most important ally. Savior gave him some advice for setting up an association. In his empty hairdressing salon, Christopher gathers unemployed miners, young people, housewives and mothers; in Kankoyo a real resistance movement was formed for the first time. In the whole Copperbelt mining area, something has changed. Miners demonstrate against the precarious jobs and the massive recourse to temporary agency work.

We take part in the first public meeting of 'Green and Justice', the organisation founded by Christopher. It takes place one Saturday in August 2010 in the courtyard of the Church of Kankoyo. The police have given permission for the meeting; Christopher has the signed approval in his pocket. As Chairman of the association, Christopher knows that guards from the mine may also be there. "With Green and Justice, we want to speak for those who have no voice, and condemn what is happening here in our community." Then Savior rises to his feet. "Mopani claims that it doesn't make any profits, and it therefore pays no taxes. Can you believe that?" People sitting on wooden benches under a tree shake their heads shyly. "If they really weren't making any profits, they would have gone away a long time ago, yes?" Loud approval. Savior now raises his voice. "That means they are lying and fiddling their accounts. So Mopani takes our copper, pollutes our environment, and pays no taxes. We can sue them. That is possible, but takes time ..." A man stands up and agrees. "We need to do something. This is Baghdad, just without war."

No one in Mufulira received compensation for the poisoning that made Christopher's son, and hundreds of others, ill. Mopani paid a fine of about one hundred dollars at the local office of the Environment Ministry and carried on production with sulphuric acid. The members

of Green and Justice find the worker who was on duty on the day of the accident. Mr Chileshe takes us to him. John was dismissed for 'negligence'. "The negligence is Mopani's. At this spot, 520 metres underground, there should have been three pumps." According to John, however, only one was in operation, and it broke down on 31st December 2007. For that reason, the acid could no longer be pumped back to the surface on the 1st and 2nd of January. John was arrested by the police at Mopani's insistence, but none of the charges could be upheld. Since then he has been freed, but is unemployed, and his children forced to leave school long ago.

The members of Green and Justice collect statements in the whole district. They get every witness to sign a consent form so that he or she can be represented by a lawyer. All report roughly the same experience; on that morning, they had the feeling of having swallowed razor blades. Vomiting, severe diarrhoea – some did not recover completely until several weeks had passed. Those who visited health centres were advised by the nurses to drink milk and go home.

Charles Mwandila is concerned about the production method using acid. The groundwater had already been contaminated as early as 2004 and 2005. In the offices of the Chief Executive of the Mufulira community, in front of our eyes he waves a water analysis that documents the events of January 2, 2008. "They talk about 'emissions', but in reality it is poisoning," he says angrily. Since 2000, Mopani has not complied with the standards in force in Zambia for the release of sulphur dioxide into the atmosphere. The Glencore subsidiary does not intend to take measures to fix the problem until 2014 or 2015. Charles shows one of the few air analyses that are available to him. In July 2009, the sulphur dioxide content was 72 times higher than the standard. The arsenic emissions also exceed the statutory limits by a factor of 16. This arsenic/sulphur dioxide mixture is highly carcinogenic. A young employee of the municipality tells us, "I don't want to lose my position. I have tried several times to determine the composition of the material flowing through the pipelines, but Mopani never replied. These process wastes are fed into a settling basin …"

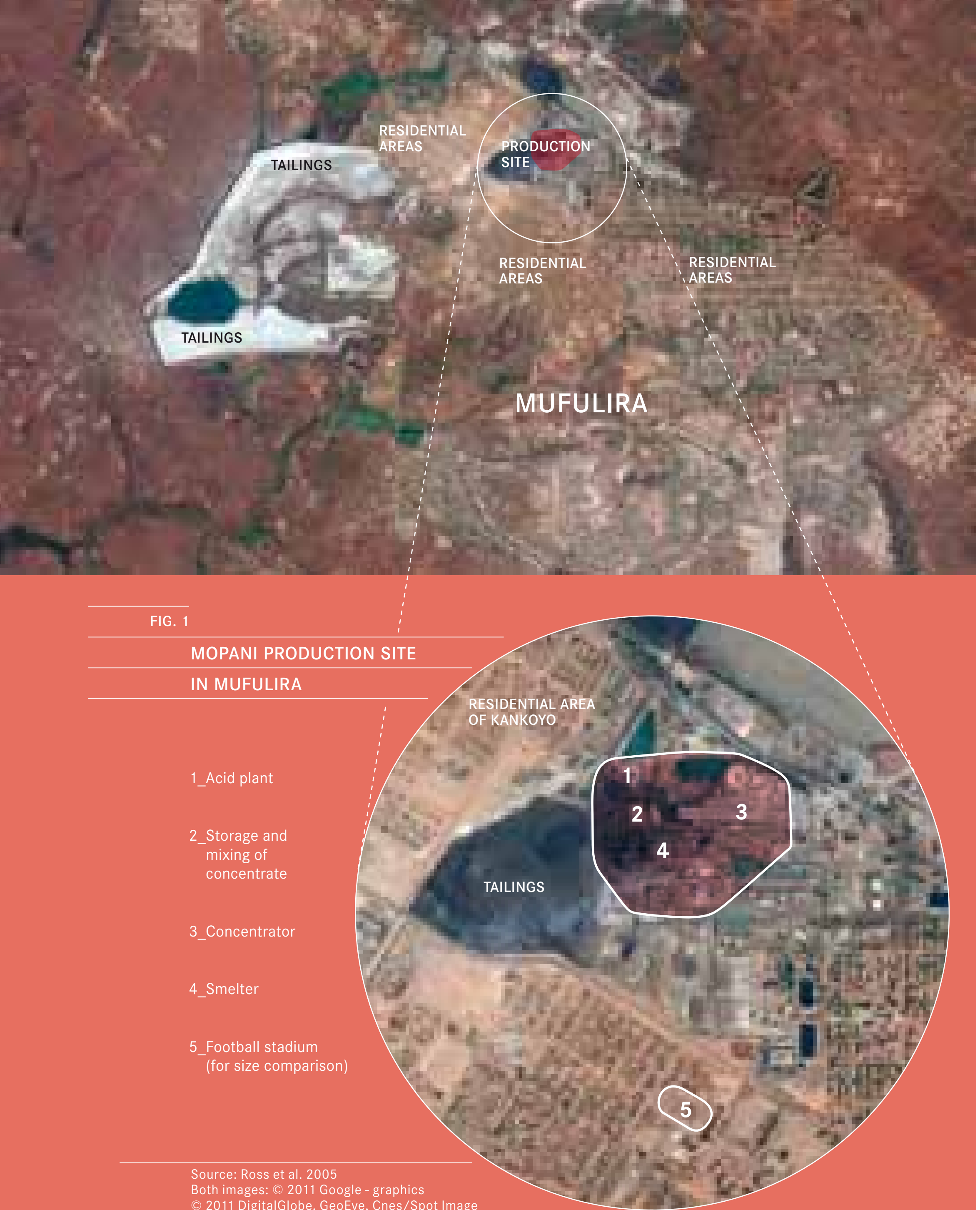


FIG. 1

MOPANI PRODUCTION SITE IN MUFULIRA

Source: Ross et al. 2005
Both images: © 2011 Google - graphics
© 2011 DigitalGlobe, GeoEye, Cnes/Spot Image

LICENCE TO POISON LAND AND PEOPLE

To get to settling basin No. 11, you have to leave Kankoyo. We follow the pipelines; because of their susceptibility to corrosion, they are laid above ground. A sign reads, “Danger zone. Entry prohibited.” We drive along a sand dune that is more than two kilometres long. The small grains are blown about by the August wind. These are the process wastes from the mine. They come directly out of the pipeline and dry in the air. Mr Pepino, a member of Green and Justice, explains “in these pipes and therefore all around are the process wastes from Mopani, a mixture of chemicals, water and sand. From the mine until they get here, they don’t pass through a single filter.” A bit further down, there is a tributary of the Butondo. Mr Pepino confirmed that the chemicals pour into it during the rainy season. A few kilometres from here, the tributary opens out into the magnificent Kafue. This is the country’s most important water reservoir, and it supplies a nature reserve before flowing into the Zambezi River. In June 2007, Mopani was accused of having polluted the Luanshimbo stream. The investigating authorities were not given access to the mine to determine which plant was the cause of the incident. To the inspectors, Mopani stated that one month earlier it had received the licence allowing it to run its waste water into the stream.

By the end of August 2010, Green and Justice had collected 97 witness statements. The members learned how to handle the camera and computer that Saviour obtained for them. They are confident. Savior has come back to keep them informed under the tree by the Church of Kankoyo. It will be a lengthy and complicated trial, but the victims in southern Africa are not going to put up with things any longer.

We are back in Christopher’s small living room. A few glasses are drained and Mr Chileshe dances the rumba. Cleo is doing better now. She would like to be a nurse. And ‘Mother of Junior’ is friendly; I see her laughing for the first time. Eventually, she tells us her first name: Maevis. Only Christopher leaves the party. When he is happy, he allows himself a game of billiards.

GLENCORE //

"No adequate comparable company or peer group can be defined as competing directly with Glencore," a company's bond-issue prospectus proudly claims.

Glencore, Baar - 2011

07 //

BIG, BIGGER, GLENCORE: DISCREET COMMODITY GIANT AT THE CROSSROADS

Glencore is an artificial name, a creation of the modern PR machine. But by 1857 the word had already found its way into literary history through the pen of the Irish writer Charles J. Lever. His novel *The Fortunes of Glencore* begins against the monumental backdrop of the rugged coast of Ireland: "Where that singularly beautiful inlet of the sea known in the West of Ireland as the Killeries, after narrowing to a mere strait, expands into a bay, stands the ruin of the ancient Castle of Glencore."

Glencore, the second-largest Swiss company by sales after Vitol, although located in the far more prosaic setting of the Zug industrial belt CHAP.5, is in fact the exact opposite of a ruin. Born in 1974 in central Switzerland, the company was renamed Glencore, its current brand name, in 1994 and has stealthily, quietly and discreetly flourished here, becoming a global corporation.

THE RICH RICH INHERITANCE: POWER STRUGGLES AND DIVORCE BATTLES

The story of the change of name and owner began in June 1992, when Marc Rich surprised everyone by suddenly sacking his closest colleague, Willy Strothotte. Unlike Rich, the German was not an oil trader but a 'metal man', having come from ICC Metals in 1978 to complement Rich. From then on Strothotte was the undisputed second in command of the company. Two versions of the reason behind his sacking continue to circulate.

The first: Strothotte wanted to counter the rumours of the company's horrendous losses and the gossip surrounding Rich's divorce battle by cautiously engaging in more open public communications and was gagged by Rich. Despite this, Strothotte went ahead and gave a lecture about the effect of the fall of the Berlin Wall on the business operations of Marc Rich + Co. AG. The Swiss financial magazine *Bilanz* quoted a former top manager that used to be a member of the management of various Marc Rich subsidiaries who said "this was a declaration of war against Rich," and the next day Strothotte was gone.[1]

The second: from the end of 1990 onwards Ravenswood Aluminium Corporation (RAC), a company belonging to Marc Rich + Co. AG, was involved in a bitter labour battle in the USA. The protesters and the United Steelworkers union managed to get as far as the company's headquarters in Zug and in front of the cameras of the US TV networks *ABC* and *NBC*. Later, in the final round of negotiations the workforce delegates demanded that all those sacked be reinstated. Taken by surprise at this 'all or none' demand, the Ravenswood Director looked at the clock and said, "I'll call Strothotte in Zug," who accepted the strikers' conditions. On receiving the news shortly afterwards, RAC Co-Director and Rich protégé, Jean Loyer reacted just as swiftly and dialled a Zug phone number. "Strothotte was dismissed that same day."[2]

Like the noisy departure of Marc Rich and Pincus Green from Philipp Brothers CHAP.4 this separation was by no means a peaceful one either. Rich had his ex-partner's office demolished and a seating area with plants installed in its place. Strothotte's dismissal is a key episode in the power struggle between Rich and his top managers, which Rich was nevertheless to lose in the end. Founded in 1987 the Marc Rich + Co. Holding AG was jointly owned by Rich and the other founding partners. This holding company in turn owned 75 per cent of Marc Rich + Co. AG. The remaining 25 per cent belonged to the top management of the latter. This constellation ended with the departure of co-founders Pincus Green and Alec Hackel. Now owned solely by Rich, the holding company had a 51 per cent stake in Marc Rich + Co., with management and the employees owning the remaining 49 per cent.

Not only did Rich make negative headlines as a tax fugitive, he also appeared in the gossip columns. Having stood by and watched an affair for two years, by April 1992 Denise Rich had had enough. What ensued was a divorce battle in which the glamorous US singer demanded what she was entitled to under Swiss law, namely half of the fortune accumulated during the marriage, or about 750 million Swiss francs. If not before then from this moment onwards the name Marc Rich was a reputational risk. Just one month after Strothotte's dismissal Claude Dauphin, the manager of the oil business in London, left Marc Rich + Co. AG. Just as Rich had done at Philipp Brothers, Dauphin in his turn poached key employees to help him found a rival company, Trafigura CHAP. 10, CHAP. 11.[3]

Things became much, much worse when, in July 1992, some Rich traders tried to manipulate the zinc market. They embarked on a secret mission to buy a million tonnes of zinc, corresponding to about 20 per cent of world production or two-thirds of the zinc sold on the London Metal Exchange. Their intention was to create an artificial shortage in supplies of zinc to drive up prices. Although the traders succeeded at first, they were unable to keep prices high until the futures they had bought in parallel earned the extra profit they had sought. In the end, the speculation backfired on the manipulators who in turn incurred losses of 172 million dollars.[4] It appeared that Rich, the oil man, who had authorised these dubious practices, did not understand enough about the metals trade.

These developments following Strothotte's departure led to further resignations and ultimately to open mutiny among those who stayed. In March 1993 Rich capitulated under pressure from his rebellious workforce and recalled the ousted Willy Strothotte. The latter accepted, but only on one condition: Rich must withdraw from the business. As a first step the managers and senior employees took over 75 per cent of Marc Rich + Co. AG. The profits they earned enabled the new owners of the company to increase their stake more rapidly than originally anticipated. By November 1994 Rich had sold the last of his shares, which had netted him 600 million dollars in total. The company was then rebranded as Glencore, which, according to Strothotte, stands for Global Energy Commodities and Resources.[5]

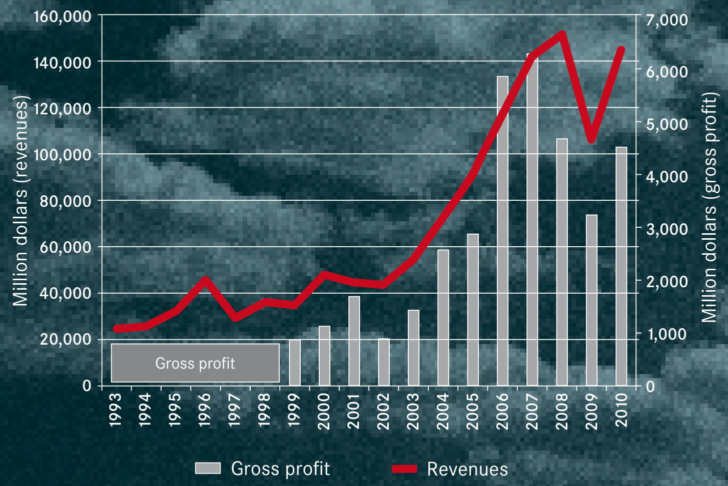
BIG IS BEAUTIFUL: A COMPANY BECOMES A COLOSSUS

Following the radical break with its founder, the company in Zug began to grow dramatically. The revenues that amounted to 25 billion dollars in 1993 have since increased almost six-fold, topping 145 billion dollars in 2010. In recent years Glencore has consistently been among the world's 20-40 companies with the largest revenues.[6] Moreover, until its Initial Public Offering (IPO), i.e., stock exchange flotation in 2011, the commodity giant was one of the largest companies in private ownership. Glencore supplies industry rather than shops and consumers and values discretion above all else, which explains why the company has only been known to industry experts until now.

Glencore's customers are other companies such as steel producer Arcelor Mittal, electronics manufacturer Sony and even commodity producers such as Shell und BP. Roughly 2,700 employees in offices distributed throughout more than 40 countries propel huge quantities of materials around the globe. Much of the business is simply logistics. Once a trader has wrapped up a deal, it's the turn of the 'foot soldiers'. More than half the staff in the commodity departments are what is known as Traffic Staff. As in a forwarding agent's office they are the people who decide which route aluminium from Brazil or copper from the Congo will take to its destination, which lorry is to carry it to which port and which of the several hundred cargo ships the company uses should dock there. According to estimates neither the US army, Walmart nor any other organisation transports larger volumes around the world.[7]

FIG. 1

GLENCORE'S REVENUES AND GROSS PROFIT BETWEEN 1993 AND 2010



Source: 1999–2010: Glencore's share-issue prospectuses and annual reports; 1993–1998: Media reports

Only those who deal in large quantities and have considerable expert knowledge of logistics, financial technology and the law can earn fat profits from the narrow margins in commodity trading. FIG. 1 illustrates how well Glencore has mastered this art form.

Alongside rising revenues the company's gross profits have also increased enormously. According to Deutsche Bank, Glencore could expect to experience a further growth boost in 2011, the year of its flotation. The same forecasts predict that by 2013 Glencore's gross profit will have doubled to reach more than ten billion dollars. In this case, revenues would rise from 145 billion in 2010 to 193 billion, followed by a slight drop due to exhausted mines.[8]

TAB. 1

GLENCORE'S MARKET POWER (BASED ON 2010)

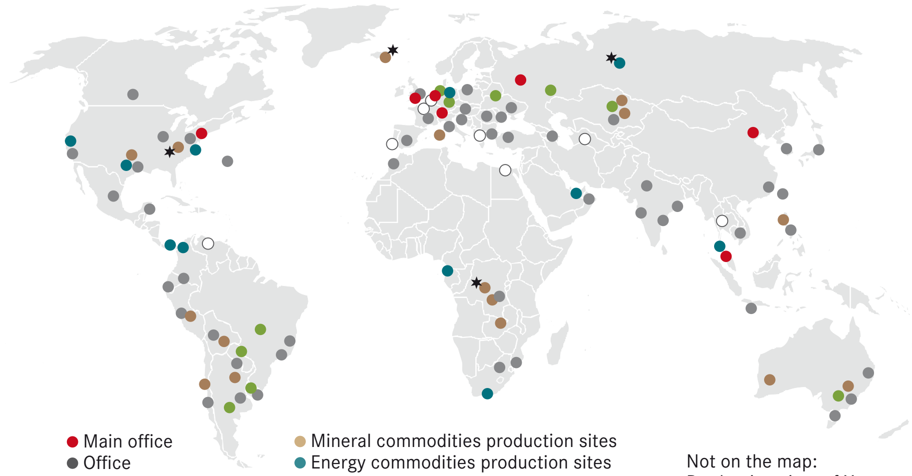
	Commodity	Million tonnes	Share on the free commodity market
Metals	Iron	9,3	1%
	Aluminium	3,9	22%
	Zinc	1,7	60%
	Ferro-chrome (for manufacturing stainless steel)	1,5	16%
	Copper	1,4	50%
	Lead	0,3	45%
	Nickel	0,2	14%
	Cobalt	0,018	23%
Energy	Coal (thermal)	196	28%
	Oil	125	5%*
Agricultural products	Grains	19	9%
	Vegetable oil and oil seeds	8	4%

**Volume traded on the free commodity market unknown, this figure represents share of total world trade according to UNCTAD 2010*

Source: Glencore's share-issue prospectuses and annual reports; UNCTAD 2010

FIG. 2

GLOBAL CORPORATION GLENCORE



● Main office
● Office
○ Independent office
● Mineral commodities production sites
● Energy commodities production sites
● Agricultural commodities production sites
✶ Minority interest

Not on the map:
Production sites of Xstrata and UC Rusal

Source: Glencore IPO prospectus; Glencore Factsheet 2011; Deutsche Bank 2011; www.chemoil.com

TAB. 2

GROUPS, DEPARTMENTS AND EMPLOYEES

Business groups	Departments	Employees in trading	Employees in production
Metals und ores	Alumina, aluminium	520 (250 in Baar)	43,000
	Zinc, copper, lead		
	Ferroalloys, nickel, cobalt		
Energy products	Crude oil, oil products	640	470
	Coal, coke	160	4,130
Agricultural products	Grains, oil seeds, biodiesel, sugar	950	7,200
Remainder		500	
Total		2,770	54,800

Source: Glencore IPO prospectus

Because of the relatively low margins in this industry, revenues from commodity trading indicate little about a company's financial health, but they are all the more relevant as an indicator of a company's economic impact. Together with market shares, they demonstrate a company's power. Were Glencore to go on strike, many a factory, industrial firm or coal-fired power station would simply cease to function. In 2010 for example, on average one tenth of the raw material in every single aluminium product sold worldwide originally came from the commodity giant in Zug. Taking into account that only part of world production ever actually reaches the free commodity market CHAP. 3, its market share totals in real terms in 22 per cent TAB. 1. Similarly, as much as a quarter of the cobalt produced in the world flows through Glencore channels.

Given market shares of up to 50 per cent, the company can be said to all but control the markets in question. If Glencore were to reduce its trading operations or put part of its own production into storage, the price of such a commodity would inevitably rise.

As the epitome of a global player Glencore operates on all five continents and is represented in over 40 countries FIG. 2. "[Glencore's] knowledge of the flow of commodities around the world is truly frightening," a business partner was quoted as saying in *Reuters* on 25 February 2011. The same lack of humility is evident in a Glencore bond issue prospectus: "[N]o adequate comparable company or peer group can be defined as competing directly with Glencore."[9]

YOUNG BOSSES, OLD WARHORSES AND GOVERNANCE PROBLEMS

Widespread yet close-knit, the Glencore network comprises many subsidiaries located anywhere from Bermuda via Luxembourg to Switzerland. There are 14 subsidiaries in Switzerland alone, as well as the parent company, Glencore International AG, which since its flotation has been restructured yet again under a shell company ('ultimate parent company') registered in Jersey. Within this structure, which is made up of three business units (metals, energy, agricultural commodities) and further sub-divided into six departments, work a total of 57,570 employees TAB. 2.

Each of these departments oversees the trade, production and even the financing and logistics of its relevant commodities. The specialists in the respective markets play such a pivotal role that the department managers are also members of the senior management. Glencore believes wholeheartedly in careers made within the company. Those who later become managers are usually hired young and remain loyal for a long time: nobody more so than Ivan Glasenberg whose career has shot up the fastest at Glencore. Originally a South African, and a Swiss citizen since 2010, Glasenberg has been living in Rüschlikon on the shores of Lake Zurich for many years, having been hired by Marc Rich at the tender age of 27 as a coal trader in apartheid South Africa. Glasenberg, who was already the company's top coal trader by the time he was 34, became the controller of Glencore's destiny as its CEO at the age of 45. The average member of the current top echelon is male (currently 100 per cent), joined the company at 30 and rose to the rank of top manager by the time he was 39. Christian Wolfensberger, one of the few Swiss nationals to make it to the very top and who studied at the University of St. Gallen, joined Glencore at the age of 23 and was promoted onto the Management Committee at 34.

The flotation in 2011 put pressure on Glencore to hire more external staff in order to improve governance, that is, the systems that control professional conduct and the proper management of transactions. Recent additions to the Management Committee are a Chief Risk Officer and a lawyer responsible for compliance with statutory provisions. The fact that the Board of Directors was headed by a CEO with many years of experience, namely Willy Strothotte, may have been typical for Glencore but it was not in line with international good practice. Thus the search for a competent external successor represented a break with tradition, and resulted in a media fiasco. On the day that the IPO was officially announced the *BBC* broadcast a report referring to former BP boss Lord Browne as the new Chairman of Glencore, whereupon Browne surprised everyone by withdrawing shortly afterwards citing "disagreement about governance issues".[10] The following scenario shows that Browne's concerns were not unfounded: at the time of the flotation it was revealed that Glencore employees would be answerable to the courts in Brussels in 2011 for bribing an EU agriculture official. The official had had, among other things, phone bills amounting to almost 20,000 euros and holidays in a luxury hotel near Saint-Tropez paid for him.[11]

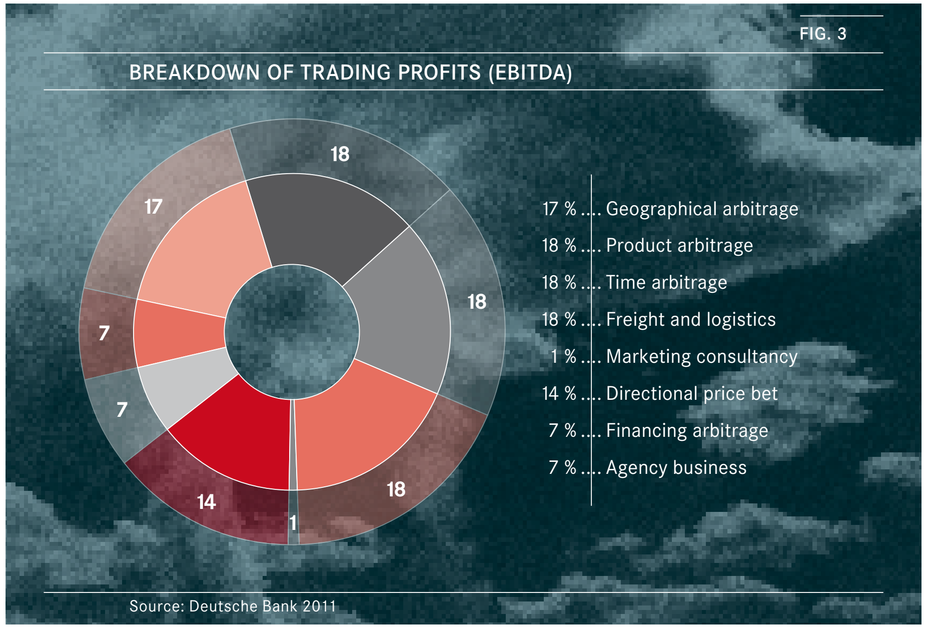
Into the breach stepped the colourful character of British-born Simon Murray. A former French Foreign legionary in Algeria, adventurer at the South Pole, and manager in Hong Kong, the 71-year old will in future be a regular visitor to Glencore in Baar as its chief inspector and representative. Murray has already broken with the core values of the company's culture to date, discretion and restraint. In his first interview after his new role was announced he ranted openly about African refugees, the big banks and, in particular, women in managerial positions. "Why tell everybody you've got to have X number of women in the boardroom? Women are quite as intelligent as men. They have a tendency not to be so involved quite often and they're not so ambitious in business as men because they've better things to do. Quite often they like bringing up their children and all sorts of other things," he pontificated.[12]

Almost-Chairman Lord Browne is not the only one who appears to be worried about the governance style of the industry leader. On 31 May 2011 the European Investment Bank (EIB) announced that it was investigating charges concerning Glencore's Mopani Copper Mine CHAP. 6, CHAP. 14 and would no longer agree to fund Glencore's projects: "[D]ue to serious concerns about Glencore's governance which have been brought to light recently and which go far beyond the Mopani investment, the President of the EIB has instructed the services to decline any further financing request from this company or one of its subsidiaries."[13]

TRICKS OF THE TRADE: PROFITS FROM ARBITRAGE (AND SPECULATION)

Besides its sheer size, two further factors contribute to Glencore's market power: its wide-ranging portfolio and rapid transformation from pure trader to trading producer. Even within its three sectors, metals, energy and agricultural products, Glencore is enormously diversified. This Swiss 'commodity supermarket' offers industrial firms the same advantages as high street supermarkets offer consumers: a full range from a single source. This unique selling point raises Glencore, on the one hand, above the trading departments of major producers such as BP (oil) and BHP Billiton (mining). On the other, Glencore rises above traders with a narrower range of commodities, such as Louis Dreyfus, Bunge and Cargill (agricultural) and Vitol (oil).

Glencore's core competencies in trading include the ability to anticipate and exploit price fluctuations. The more marked this volatility, the larger the potential margins. Rapid price changes – such as those triggered by the reactor accident in Fukushima and the revolutions in the Arab world in 2011 – create historic opportunities. But even without such dramatic events, traders find ways of using price differences (arbitrage) with regard to location, product and time to their advantage. What strategies does Glencore employ to achieve its trading profits? According to Deutsche Bank arbitrage on the basis of location, product and time contributes in roughly equal amounts to total profits, and the company profits as much from its global logistics network FIG. 3. Intriguingly, a detail from the analysis reveals that a business practice which all the major trading companies strongly deny using, namely price speculation ('directional price betting') CHAP. 13, generated 14 per cent of Glencore's profits, some 330 million dollars, in 2010.



VERTICAL INTEGRATION: FROM SIMPLE TRADER TO TRADING PRODUCER

The third growth factor after size and diversification is Glencore's entry into the extraction and processing of raw materials. The policy of vertical integration, investing heavily in the company's own mines and smelters, was begun by Strothotte and expanded by Glasenberg. By 2011 Glencore had come a long way from being simply a trading company; increasingly, it began controlling the first link in the value-added chain as a producer. As long ago as the late 1980s Strothotte, then manager of the metals sector, was already making initial investments in an aluminium smelter and a zinc and lead mine in Peru. In 1997 he stated in public that in future companies that only traded commodities would be relegated to the role of niche players.[14] Four years later he explained, "We have

TAB. 3

RELATIVE MARGINS FOR TRADE AND PRODUCTION (ADJUSTED EBITDA)

Department	Trade		Production	
	2010	2009	2010	2009
Metals	3.7%	1.8%	25.5%	19.7%
Energy products	0.5%	1.6%	23.9%	28.9%
Agricultural products	8%	4.5%	4.9%	4.4%

Source: Glencore annual report 2010

decided to operate on a more industrial scale [that is, in mines]. This way we will have a secure flow of raw materials in the long term."[15] The main reason for this strategy lay in the fact that consolidation among customers was putting increasing pressure on margins. Traders were facing fewer and fewer, but larger and larger customers.

By 2001 Strothotte was reporting that Glencore's industrial investments were having a positive effect on earnings. For the financial year 2010 the company published figures that showed, for the first time, the difference between the margins for trading and production TAB. 3.

The profit margins for producing metals and fuels are far higher than those for simply trading them. At the same time, each side of the business can act as a buffer for the other. In times of crisis production suffers from low commodity prices whereas traders can exploit these price fluctuations, and lower commodity prices reduce the need for capital in trading, which in turn frees up capital for acquisitions. Hence Glencore is always there, ready and waiting, when an attractive mine somewhere gets into financial difficulties and becomes an easy target.

It did not escape Deutsche Bank's notice that Glencore can strike like lightning if necessary, even "in regions which the other mining companies may not always want to operate in". The analysts conclude that "this opportunistic approach has in a sense has [...sic...] created most of Glencore's value." In fact, in terms of value, in 2011 fully 70 per cent of Glencore's production facilities were located in extremely corrupt and/or conflict-torn countries, such as the Democratic Republic of the Congo, Colombia, Kazakhstan or Equatorial Guinea.[16]

SOVIET RUINS AND ALLIANCES WITH THE RUSSKIS IN THE WILD EAST

The first surge in Glencore's vertical integration was focused on the former USSR. This is the region from where the company procures a major part of its goods. Glencore was quick to aggressively pursue its interests in the transition of the Eastern Bloc countries to a market economy, and to do so successfully. The times were chaotic and many mines, refineries and processing plants in the former Soviet mining industry, which could no longer sell their products to the dilapidated, state-owned mixed concerns, were being flogged off to private investors for a song. The caste of oligarchs that was developing at the time needed access to western markets and western finance. This Glencore could offer and it secured exclusive partnerships with the most important commodity companies and their managers in the former Soviet Union in return. It is to these eastern tycoons that the company in Zug owes not only the productive and cost-effective procurement channels it enjoys today, but also a dense network of contacts with direct influence in the former Soviet Union.

MARC RICH: OLIGARCH COACH AND FOREIGN EXCHANGE EARNER

This strategic marriage of convenience was able to build on the groundwork done by Marc Rich and his men, who had maintained good contacts with those responsible for Soviet commodity trading at the end of the 1970s. For example, negotiations by Phibro and later Rich had enabled the USSR to buy large quantities of copper in Pinochet's Chile, which it was officially boycotting at the time.[17] For his part, Rich helped the then state monopoly, Soyusneftexport, to sell oil to South Africa. In each case payments were made in the hard western currencies so valuable to the rulers of Soviet Russia. Just how important Marc Rich was to the Kremlin was apparent in August 1983 when the influential Russian daily newspaper *Isvestiya* defended on its front page (otherwise always reserved for strictly internal Soviet topics) the commodity trader, who had by then fled to Zug, in a leader entitled Open Repression.[18]

Then came the fall of the Wall. "It was a time of complete confusion. There were so many administrative controls, and there were just as many special privileges,"[19] commented Vladimir Lopukhin, Russian Minister of Oil and Energy between 1991 and 1992. Still under state control, the production companies were in acute financial difficulty and often bought access to western markets by offering to sell their raw materials at throwaway prices. According to one trader it was possible to strike a good oil deal by paying for a refinery manager to have his teeth seen to in London.[20] In this environment Rich set up four joint ventures with small Russian oil refineries which gave their managers, whom he made CEOs, unlimited export opportunities for their products. In return, he secured Russian black gold at far below the market price.

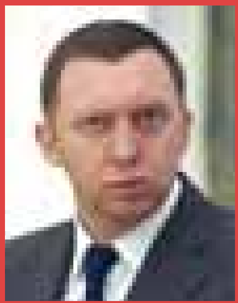
According to *Businessweek,* Rich quickly became the most powerful trader in the CIS countries. He was "a coach and sort of a godfather for several of the oligarchs," says economics professor Vladimir Kvint.[21] An executive of the International Bank for Reconstruction and Development put it more precisely, "Marc Rich is one of the grand designers of the scheme known as 'using offshore cash', whom the Russian commodity magnates let themselves be led by in the years between 1985 and 1992. Rich taught them how to avoid state interference in the sale of their oil."[22] After Rich's departure, Glencore, whose Russian subsidiaries fill two storeys of the International Trade Centre in Moscow, inherited these alliances. Let us take a closer look at the main ones.

UNITED COMPANY RUSAL: GLENCORE'S SUBSIDIARY AND PARTNER IN THIS MARRIAGE OF CONVENIENCE

One of the main links between Glencore and the oligarchs lies in the aluminium sector. At the start of 2010 Glencore had an 8.6 per cent stake in UC Rusal via Amokenga Holdings Limited in Bermuda.[23] With a market share of 12 per cent, Rusal is the world's largest aluminium producer. In 2010 the company employed about 75,000 people and achieved revenues of 10.98 billion dollars, with handsome profits of 2.87 billion dollars.[24] It owns or operates 8 bauxite mines, 16 aluminium smelters and 13 aluminium refineries in Russia, Ukraine, Sweden, Ireland, Australia, Jamaica, Italy, Guinea and Nigeria, also additional mines (syenite, fluorite, quartzite and bituminous coal), and various factories located in China and Russia. According to estimates, Rusal can probably meet half of Europe's demand for aluminium and 10 per cent of China's, near which its Siberian plants are situated.[25] 31 per cent of this gigantic production volume is sold by none other than Glencore.[26]

The aluminium company Rusal is to some extent both Glencore's 'spouse' (in the sense of partner) and 'daughter' (as in subsidiary). Following the collapse of the USSR, the privatisation of the aluminium combines and the consolidation of this sector reached its zenith with the merger between the old Rusal of Oleg Deripaska, the SUAL of Viktor Vekselberg and Glencore's aluminium sector. The world's largest aluminium producer that resulted from this three-way partnership was now owned by Deripaska (64.5%), Vekselberg (21.5%) and Glencore (14%).

GLENCORE'S TRIO OF OLIGARCHS:



Oleg Deripaska – the aluminium king

- Founder, CEO and principal shareholder of Rusal
- Estimated assets in 2010: 10.7 billion dollars *(Forbes)*
- Son-in-law of the head of presidential administration under Boris Yeltsin. Regarded as a key supporter of Vladimir Putin

Viktor Vekselberg – the Swiss industry oligarch

- Chairman of the Rusal Board of Directors
- Estimated assets in 2010: 11.2 billion dollars *(Forbes)*
- Founder and principal shareholder of the Renova Group founded in 1990, which holds large stakes in Oerlikon and Sulzer
- Interests in oligarch Mikhail Fridman's Alfa Group within the AAR Consortium (Alfa-Access-Renova). Like BP, AAR holds a 47.5 per cent in TNK-BP, Russia's third-largest oil company.

Mikhail Prokhorov – the nickel godfather

- Third shareholder in Rusal and founder of ONEXIM, one of the major private equity funds in Russia
- Estimated assets in 2010: 13.4 billion dollars *(Forbes)*
- Former partner of oligarch Vladimir Potanin, owner of Norilsk, the world's largest nickel producer

The threesome was then joined by a third oligarch and fourth Rusal stakeholder, Mikhail Prokhorov in 2008 P. 130.

Company founder Oleg Deripaska likes to present himself as a self-made man. Shortly after the fall of the Wall, having started to invest profits from a small metals trading company in the shares of the Sayanogorsk Aluminium Smelter in Siberia, he became its Director in 1994, aged 26.[27] Just four years later he controlled 76 per cent of private aluminium production in Russia, thereby laying the foundation stone for Rusal – and no-one could say exactly whether he was modelling his career on that of Rockefeller or Al Capone. Sometimes he is even portrayed as one of the men who brought Vladimir Putin to power.[28]

The Russian Viktor Vekselberg, a resident in Zug and second principal shareholder of Rusal, is no stranger to many people due to his large investments in OC Oerlikon and Sulzer, two jewels in the Swiss industrial crown. Less well known, however, is the fact that from 2011 onwards Everest, the holding company through which Vekselberg's Renova acquired the aforesaid holdings, has been managed by the very same Vladimir Kusnetsov who in 1983 as *Isvestiya* correspondent defended Marc Rich against attacks from American opponents in the article mentioned above.

Indeed, it was Mikhail Prokhorov who, until 2007, co-controlled the nickel company MMC Norilsk Nickel. After the split with his partner, Vladimir Potanin, he brought his shares into Rusal, which enabled the aluminium giant, and therefore indirectly Glencore, to control 25 per cent of Norilsk.

NICKEL GIANT NORILSK: COMPETITIVE WORLD MARKET LEADER WITH TIES TO SWITZERLAND

Norilsk is named after a former Siberian gulag town which today has a population of about 200,000. The company's main mine is situated just outside the town. Its global market share of 20.5 per cent for nickel and

48.6 per cent for palladium makes Norilsk the largest single producer of both these metals. Norilsk also mines platinum, copper, cobalt, silver and gold. The company, which is listed on the Moscow stock exchange and operates in Russia, Australia, Botswana, Finland, the USA and South Africa, earned revenues of 15 billion dollars in 2009.[29]

The story of Norilsk resembles that of Rusal. Although the company was privatised after the fall of the Wall, a third remained in the hands of the Russian state at first. In 1996 ONEXIM, owned by Mikhail Prokhorov and Vladimir Potanin, took control of Norilsk. At the beginning of 2008 Rusal bought some of Norilsk's assets from Prokhorov for an estimated 9-14 billion dollars. Yet, what looks like an alliance between the aluminium company and the nickel company conceals a deep-seated rivalry between two competing clans, with each fighting to gain overall control of Norilsk. In this battle Glencore is on the side of Deripaska.

Headquartered in Moscow, Norilsk has subsidiaries in Switzerland since the 1990s. It was in Geneva that Potanin and Prokhorov opened Switzerland's first Russian bank, Rosbank. By the end of 2010 the nickel giant also operated four Swiss subsidiaries and employed about 30 people. Three of the subsidiaries, Norilsk Nickel Holding SA, Norilsk Nickel International Finance (Cyprus) Ltd. and Norilsk Nickel Services SA, appear to be merely shell companies for tax avoidance purposes. Two of these companies are managed by a firm owned by Adriano Imfeld, who represented the canton of Obwalden on the Swiss National Council between 2001 and 2007, and was a committed supporter of his canton's 'attractive' tax policy.

GLENCORE'S GOLD MINE KAZZINC: DUBIOUS PARTNERSHIPS

The third, until now the most well hidden, alliance between Glencore and the Russian commodity oligarchy concerns the gold and zinc business. One thing is certain: Glencore International AG owns 50.7 per cent of the diversified company, Kazzinc, based in Oskemen, Kazakhstan. The owners of the remaining shares are not known. Created in 1997 out of the merger of eastern Kazakhstan's three main, formerly state-controlled, mines the company has a workforce of 22,000 employees distributed between eight sites, at which zinc, lead, copper and, in particular, gold are mined.

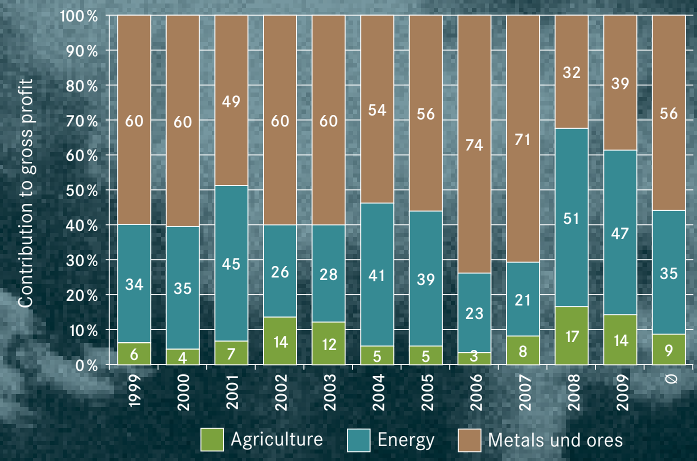
The ninth-largest country in the world is also one of its most important mining regions. More than 70 of the elements in the periodic table are extracted in the Central Asian mines of Kazakhstan. Led by the iron hand of Nursultan Nasarbayev since 1991, the country's regime does not have a reputation for either respecting human rights or integrity in business. The Nasarbayev clan, whose fortune was earned from bribes received from foreign oil concessionaries was confiscated by Switzerland towards the end of 1990s CHAP. 15.2, controls all the principal economic spheres of the country.

Almost nothing is known about the business relations Glencore is inevitably obliged to maintain with the entourage of this leader: 'inevitably' because the company in Zug can only tap the country's resources with Nasarbayev's consent, as in the case of Kazzinc's gold mine. Here, 40 per cent of the main mine Vasilkovskoye was still state-owned in 2003.[30] Moreover, harassment from the Nasarbayev clan had twice forced other international gold mining companies to stop exploiting the mine, which was then sold to the controversial businessman Grigori Loutchansky.[31] *Time* magazine has said that Loutchansky is "considered by many to be the most pernicious unindicted criminal in the world".[32] It is quite conceivable that the subsequent takeover of the mine by Glencore served to disguise dubious investments – for the benefit of all concerned. Today Vasilkovskoye is by no means the smallest nugget in the portfolio of Glencore who announced Kazzinc's stock market flotation in August 2010. However, the move was postponed, perhaps because other shareholders in the mine are even more publicity-shy than Glencore.

FIG. 4

GLENCORE'S GROSS-PROFIT CONTRIBUTIONS BY SECTOR

1999 TO 2009



Source: Glencore's annual reports and share-issue prospectuses

METALS CASH COW: WHERE GLENCORE MAKES ITS PROFITS

But let us leave Glencore's wild east and move on to analyze its overall revenue sources. How much each one of the three sectors (metal, energy, agricultural products) contributes to Glencore's overall profit varies from year to year and depends on the situation on the individual markets. Usually, the most profitable sector is metals. In years such as 2008, with record-high oil prices and crises in the metals-processing industry, the consistently strong energy business can occasionally take the lead. The agricultural sector is invariably beaten into third place FIG. 4.

TAB. 4

CONTRIBUTIONS OF BUSINESS AREAS TO PROFIT (EBIT)

(AVERAGE FOR 2009/2010)

	Trade	Production	Total
Metals	22%	18%	40%
Energy products	19%	8%	27%
Agricultural products	11%	1%	12%
Corporate and others	-5%	26%	21%
Total	**47%**	**53%**	**100%**

Source: Glencore annual report 2010

Glencore's 2010 annual report also contains a breakdown of the three sectors by trade and production for the first time TAB. 4. Given its paltry share, agricultural production contributes not more than a few pennies to the company coffers. The fact that behind this amount lie resources that include 280,000 hectares of farmland, the equivalent of all the farmland in Switzerland (excluding pastures), further demonstrates the size of this giant. However, both trade and production in the metals sector is a major business area for Glencore, as is trade in energy products. Each of these generates roughly 20 per cent of the company's profits.

On the production side the profits from the 34 per cent stake in Xstrata are also listed under Corporate and Others. These alone make up around a quarter of the profits. For its part, the mining company Xstrata generates about 70 per cent of its profit from metals and about 30 per cent from coal for power stations. This makes the production of the metals and energy at Glencore even more important. In a nutshell, mining is the key cash cow.

Financially, Glencore is just one long success story. In 1993/1994 Marc Rich sold his 51 per cent of the business empire for 600 million dollars, less than two decades later, in May 2011, when the company landed on the stock exchange its total worth was fifty times greater (60 billion dollars).[33] Parallel to that, the annual net profit of 260 million dollars (1992) rose to almost fifteen times that amount, 3.8 billion dollars (2010).

LOANS AND DEBTS: GENEROUS BANKS AND CS LIAISON

Glencore was an limited company even before its flotation. Yet, until May 2011 all its shares were owned by its 500 managers and key staff. Therefore, Glencore was unable to raise capital by issuing new shares in order to purchase mines or to expand its logistics operations. Quite the reverse was the case, if managers left the company, capital went with them. This explains Glencore's high level of debt, which at the end of 2010 totalled more than 30 billion dollars.[34]

Glencore had already begun issuing bonds in 2002 and by 2010 about a third of its debt capital had come from bondholders. A bank credit line of 10 billion dollars is the company's most important source of finance. A total of 97 banks, including 42 new banks, were involved in financing Glencore's credit line in 2010.[35] The Swiss members of the syndicate are UBS, Credit Suisse and the cantonal banks of Zurich, Geneva and Vaud.[36] In recent years Glencore has used as up to two-thirds of its line of credit. Letters of credit and bank guarantees are also important for financing specific Glencore transactions. By the end of 2010 this transactional debt amounted to 8.956 billion dollars.[37]

Furthermore Glencore not only depends on bank loans, but also functions as a bank itself. In 2010 the company's loans totalled more than three billion dollars. The largest loan went to the Russian oil company, OAO Russneft (two billion dollars), another went to the Indonesian coal mine PT Bakrie & Brothers Tbk (200 million dollars). In both cases the interest rate was a hefty nine per cent. Glencore also uses its role as a bank to win advantageous purchase contracts. In 2004 Glencore loaned Volcan, Peru's second-largest zinc mine, 40 million dollars, for which the former received purchasing rights lasting until 2010.[38] These types of contracts and the Glencore loans are often the first strategic steps taken towards the eventual acquisition of a mining company.

For a long time now Glencore has had a special relationship with Credit Suisse (CS). It was CS that helped Glencore to retain its proportion of shares when Xstrata's capital was considerably increased CHAP. 8. Together with Citi and Morgan Stanley, CS was one of the three leading banks participating in Glencore's initial public offering. Besides their strategic alliance, between 2006 and 2011 CS and Glencore also maintained an operative one. The commodity giant passed on insider knowledge which the bank then used to design structured products and derivatives CHAP. 13. The offspring of this fruitful relationship included Over-the-counter derivatives that have fallen into disrepute since the financial crisis due to their lack of transparency.[39] In 2008 CS employed 130 staff worldwide in the commodity sector. In January 2011 the then head of the commodity department left Credit Suisse. Shortly afterwards CS and Glencore announced that the alliance had been replaced by a "multi-year licensing and consulting agreement".[40]

AFTER THE FLOTATION: DAWN OF A NEW ERA OR BUSINESS AS USUAL?

As always, Marc Rich has a very definite opinion about the advantages of retaining private ownership of a commodity company: "It's much more practical to be a company that is not listed on the stock exchange. You don't have to give out any information. […] Discretion is a significant success factor in this business. We preferred to keep our lips tightly sealed. It benefited the business. It also suited our business partners."[41] After many years of rumours the launch on the stock exchange did eventually take place in May 2011, first in London then in the following week in Hong Kong. The two main reasons for this step, which marked the end of an era in the company's history, were to reduce debt and increase the company's 'war chest' for potential take-overs.

Compared to other giants in the industry, Glencore is deeply in debt and received no more than a miserable BBB- credit rating before the IPO. Were it to be further downgraded by the ratings agencies, insurance companies and pension funds would no longer be allowed to hold Glencore bonds. In addition, the financial management of Glencore is still bruised from the last quarter of 2008 when, after the collapse of Lehman Brothers, the banks completely stopped making loans. The market for short-term securities came to a standstill as well and there was an investment strike all over the world. The interest rates for what are known as 'credit default swaps', a type of insurance which protects investors against default, rose to stratospheric heights at the end of 2008. Had this situation persisted, Glencore's financial reserves would soon have been exhausted. Glencore's intention has been to use part of the capital raised with the IPO to reduce the credit line and clear debts.

Although Glencore has so far had sufficient capital to purchase mines, production facilities and holdings, the prices of these assets have positively rocketed in the wake of the commodity boom. A coal mine that could still be bought for 100 million dollars in 1980, cost two billion by 2010.[42] According to its IPO prospectus, Glencore intends to invest part of the capital raised with the IPO in the following major projects: well over two billion dollars are earmarked for increasing its stake in Kazzinc, five billion dollars in total for other projects, including expanding the mining operations at Mopani (Zambia), Prodeco (Colombia) and for oil production in West Africa (in particular, Equatorial Guinea).[43] The stock market flotation means additional shares can be issued at any time in order to enable large purchases or mergers. As Glasenberg put it just before the IPO (and in his first ever interview): "We will get firepower and we can buy assets when opportunities present themselves in areas and sizes that we could not do before."[44]

One of the projects under discussion has been a takeover of the Kazakh mining company, ENRC. The company, which is listed on the London Stock Exchange and has a trading department in Kloten, Switzerland, had a market value of 21 billion dollars in 2011. ENRC not only operates in its home country in Central Asia, but also mainly in the DRC. According to the London commodity expert Michael Rawlinson, the risks ENRC poses in terms of corruption and damage to a company's reputation preclude it ever becoming a partner to one of the large mining companies. "I don't think any other firm would dare to look at them, but Glencore would. They know how to deal with Congo, they know how to deal with oligarchs and they already operate in Kazakhstan. So, there's a perfect example of how they'll do stuff that other people won't."[45] Louis Dreyfus Commodities CHAP. 12 was also seen as a potential merger candidate for Glasenberg. One thing which the financial press was always agreed on, however, is that the dream merger would be one with Xstrata. "We believe there is good value in the two companies being together," confirmed the Glencore CEO.[46] Xstrata strong man, Mick Davis, is on record as having said that having the two companies listed independently of one another on the stock exchange as "unsustainable in the long term".[47]

In the end, the 'long term' lasted no more than 9 months; in February 2012 both companies announced their intention to merge. Glencore and Xstrata have until October 2012 to gain the approval of 83.5 per cent of Xstrata shareholders. Formally, three quarters of Xstrata shareholders have to approve the offer, but because Glencore cannot execute its voting rights on their 34 per cent Xstrata holding, this means that in fact only 16.5 per cent of the remaining Xstrata Shareholders can block the merger. Glencore and Xstrata must also convince competition and anti-trust authorities around the world that the new company will not be too dominant in the marketplace. This might be difficult because, following the merger, every third shipload of thermal coal that crosses the seas will be sold by Glencore Xstrata plc. The new colossal company will likewise be the top global producer of zinc and lead.

To find another merger with comparable characteristics, the *Financial Times* had to go all the way back to 1907, when Royal Dutch and Shell joined forces. Superficially, it appears that Xstrata will dominate the new

TAB. 5

THE VALUE OF THE GLENCORE EMPLOYEE SHARES (IN BILLION DOLLARS)

	Growth	Existing stock
2004	n.a.	4.647
2005	1.795	6.442
2006	4.485	10.927
2007	4.744	15.671
2008	-0.266	15.405
2009	1.281	16.686
2010	2.927	19.613

Source: Glencore annual reports

company. Davis will be CEO and Glasenberg his Deputy and the Chair of the Board will remain John Bond. Furthermore, most of the existing Xstrata heads of department will continue to perform the same function in the new company. However, in reality Glencore will call the shots because its management will continue to hold at least 45 per cent, almost a controlling stake, in the new company.

ENABLING STAFF DEPARTURES AND FACILITATING PAY-OFFS

Departing managers who have shares in privately owned companies have to be paid off. For this reason privately owned limited companies tend to be family businesses, in which leaving the business is rather like leaving your family. At Glencore it would have been fatal if members of top management leaving the company could have taken all of their shares at once with them. This is why in 2002 Glencore set up a highly unusual structure for its shareholders. Departing managers became creditors of Glencore and their shares were only paid off gradually. A portion even remained with the company in Zug, to be released only in the event of a stock market flotation (which is why former employees also had an interest in the IPO). Despite this rather clever trick departures cost Glencore a great deal of money: 993 million dollars in 2009, 504 million the following year. Since the flotation former employees will be able to sell their shares on the stock exchange without Glencore losing any money.

PROFITEERS AND INVESTORS: DID GLASENBERG INHERIT SHARES FROM STROTHOTTE?

By the end of 2010 the value of the employees' shares in Glencore was nearly 20 billion dollars. Their rapid growth is illustrated in TAB. 5. Despite the high wages and bonuses Glencore pays, ambitious employees had only one aim in mind: to work their way up to becoming members of the group of shareholders. This was where the big money could be made: before the stock market flotation the shareholders distributed the company's profits amongst themselves.

With the IPO about 900 million new shares were offered on the London and Hong Kong stock exchanges at an issue price of 530 pence (8.6 dollars), which poured 7.9 billion dollars into Glencore's tills. Twelve cornerstone investors had promised to buy shares worth 3.1 billion dollars. These included Credit Suisse (175 million dollars), UBS and Swiss private bank Pictet (100 million dollars each), the Chinese mining company Zijin Mining (100 million dollars) and heading the list an Abu Dhabi sovereign wealth fund (850 million dollars).[48] In addition, 240 million employees' shares worth 2.1 billion dollars were brought to the market and the earnings used to clear tax debts. The remaining pre-IPO shares were converted into shares in the new ultimate parent company, Glencore plc., registered in Jersey. Because the stock market flotation almost tripled the total value of the shares, it was the existing shareholders who made a big killing. The managers with shares continue

TAB. 6

WHO OWNS HOW MUCH OF GLENCORE?

	Before the IPO (2010)		After the IPO (May 2011)	
	Percentage	Million dollars	Percentage	Million dollars*
Willy Strothotte	7–10[49]	1,372.9–1,961.3	?	?
Ivan Glasenberg	2–3[50]	392.2–588.4	15.8	9,310
Daniel Maté Badenes	?	?	6	3,570
Aristotelis Mistakidis	?	?	6	3,520
Tor Peterson	?	?	5.3	3,130
Alex Beards	?	?	4.6	2,750
Steve Kalmin	?	?	1.2	605
Top 6	?	?	38.9	22,885
Top 12	30[51]	5,883.9	?	?
65 people Key management	57.5[52]	11,277.5	?	?

**Net asset values: depending on the price of Glencore shares when they are sold, this can be much more or much less*

Source: Compiled by the author und Glencore IPO prospectus

to control 83.1 per cent of the company after the flotation. An overview of the shares of a few key people, which contains many question marks, is illustrated in TAB. 6.

So the person who reaped the largest reward by far from the flotation was Ivan Glasenberg. Glencore's executive boss has merely a fraction fewer shares than all the new shareholders put together (16.9%), and the value of his shares is higher than that of all the new money the company received. Glasenberg became Switzerland's sixth-richest man virtually overnight (just behind Viktor Vekselberg). By way of comparison: Glasenberg's share package is worth more than half Zambia's gross domestic product (15.7 billion dollars) or the value produced yearly by 6.2 million Zambians. Daniel Francisco Maté Badenes is now the fourth-richest Spaniard and Aristotelis Mistakidis the second-richest Greek. Equally impressive, and at the same time equally disturbing, is the fact that the six top managers, whose shares make up over three per cent and must therefore be declared under British stock exchange legislation, own much more now after the IPO than all the 500 shareholders owned before this move.

If the information in the press is correct regarding who held what stakes in the company before the flotation, two important questions then arise: a) Why did Glasenberg's stake expand in the way it did?, and b) what became of what was then the majority stake owned by Willy Strothotte? It could be that Glasenberg has acquired some or all of Strothotte's shares. Although this would explain his increased stock, it would not shed light on how Glasenberg financed this coup.

Even if the IPO proved so lucrative for the top managers personally, it may not have been an immediate success. As a result of a lack of interest among investors – and because after merely a month the value of Glencore shares was almost ten per cent below the issue price – Morgan Stanley, the bank responsible, decided not to make use of an over-allotment option (a further 117 million shares).

MORE OF THE SAME? CONSOLIDATED FIGURES IN THE ENVIRONMENT DOGHOUSE

There is a great deal of speculation about what the effects of the IPO will turn out to be on the culture and business practices of Glencore. Clearly the company must now hold general meetings and publish annual reports and will therefore be more in the public eye. In reality, it was already possible to learn a great deal about the company from the bond offering prospectuses, as well as from the annual reports that have been published for years. Although these only went to investors and banks until the IPO, they could easily be tracked down. Still, the new

Glencore will not be substantially more transparent as publicly-listed companies need only show consolidated figures; the numbers for the many subsidiaries will be added together. These aggregated numbers give no information about transactions between the subsidiaries, which can be used for tax avoidance for instance CHAP. 14.

Trading companies, such as Noble and Bunge, have already undergone a stock market flotation without the move having had any noticeable effects on their business conduct. The U.S. investment banks Goldman Sachs and Morgan Stanley have acted no less aggressively following their flotations. No wonder, then, that Glasenberg cannot see changes occurring at his company, "We are not going to change the way we operate. Any talk that going public will hinder us is not true. It will not affect us at all."[53] Glencore may have found that certain investors will not tolerate anything and everything (e.g. US pension funds sold off Glencore bonds when it became known that the company was involved in Sudan), nonetheless, the dubious reputation of Rich's wealthy heirs did not deter banks and other investors from buying Glencore shares.

As regards the environment for example, Glencore is going to have to do much more to emerge from the London Stock Exchange doghouse, in which notorious companies such as Vedanta Resources or ENRC from Kazakhstan reside. Today the annual report notes succinctly under the heading Environmental Contingencies, "Glencore is unaware of any material environmental incidents at its locations"[54] – by 'material' it means 'financially relevant'. Even its colleagues in the industry see things differently. In 2010 Anthony Lipmann, former Managing Director of the UK company Lipmann Walton & Co. that trades in cobalt and other metals, complained in an open letter to Glasenberg that the sulphur emissions from the Mopani mine were 30 to 70 times higher than the limit value set by the Environmental Council of Zambia and the WHO CHAP. 6. During a visit to the site he had seen the consequences for himself: "[B]leached earth, the reduced crops, the corrosive effects of acid rain on roofs, paint and lungs."[55]

A very rudimentary sustainability report was issued by Glencore in the fall of 2011. Also the formation of the committee for Environment,

Health and Safety on the new Glencore board is a step, albeit in the wrong direction, since it includes ex-BP boss Tony Hayward, ousted after the oil spill in the Gulf of Mexico.

PROFESSIONAL PR = MORE TRANSPARENCY?

Whereas other global corporations employ whole departments to respond to questions from the media, to compile sustainability reports and manage their reputations, until now Glencore has seen company communications as something it could afford to neglect. Symptomatic detail: until spring 2011 the company website did not even contain the rubric News. While it is true that selected figures of business performance were published periodically, in fact glencore.com acted merely as a virtual business card and not as a public communication channel. As late as 2011 the company maintained the view that "Glencore is a private company and our communications policy with the media reflects this status."[56]

Among media professionals the statements made by Lotti Grenacher, Human Resources Director at the headquarters in Baar, who, in addition to this role, made valiant efforts to act as press spokesperson, are almost legendary. But it was always the boss himself who grabbed the phone when things began to get out of hand. At the beginning of 2008 Glencore received the Public Eye Award that the Berne Declaration (BD) and other NGOs present every year for particularly irresponsible business practices. The specific reason was the company's treatment of both its workers and water resources in Colombian coal mines. Annoyed at so much "unqualified and unjustified criticism," Glasenberg personally phoned the NGO coordinator at once and aired his annoyance. Since this did nothing to curb media reaction to this award of shame, Glencore then hired highly paid image consultants from London a month later who took just 24 hours to provide a *Spiegel* reporter with over 100 pages of 'evidence' of Glencore's social and environmental commitment in Colombia.[57]

INTERIM CONCLUSION

Companies which only trade commodities and therefore adopt the business model that Marc Rich + Co. AG practised successfully for a long time are a dying breed. In times of increasingly narrow margins it takes huge volumes to make real money out of trading. At the same time their industrial customers, who are also larger, wish to procure everything from the same 'commodity supermarket'. Consequently, the once-blooming trading landscape around Zug, which is dotted with small businesses, has largely withered. Not only does Glencore have the critical mass to dominate the trade, increasingly the industry leader has also pursued vertical integration and gone 'upstream' to the sources, i.e. to the metallic mines and oil wells. Today, the world's largest trader is also a very large mining company, and if the announced merger goes through, Xstrata Glencore plc will be the fourth largest in the world.

The stock market flotation is not a cleansing, from which will emerge a more transparent, more environmentally and socially compatible industry leader. On the contrary, Glencore will have more funds on hand to invest and than will become all the more dangerous as it continues to follow its strategy of investing heavily in conflict zones and zones with weak governance. Deutsche Bank estimates that the company's net profit will more than double to reach ten billion dollars. It is the Prodeco coal mine in Colombia, the Kazzinc zinc business empire in Kazakhstan, Katanga mine in the DRC and new oilfields off the coast of Equatorial Guinea that will turn out to be the real gold mines. This means that Glencore's key growth driver is located in regions where the risk of human rights violations and environmental damage is particularly high. If the colossus in Zug is to behave more responsibly in future, this will only be in response to enormous pressure from civil society and the threat posed by statutory regulations and ethical investors.

The stock market flotation has made a handful of men immeasurably rich. The nearly 23 billion dollars that the top six figures at Glencore have collected make investment bankers and hedge fund managers look like beginners. Little wonder the company's managers are increasingly seen by the public as no more than profiteers. If the six Glencore bosses were a country and their wealth its gross domestic product, they would be in 94th place in the world GDP ranking. Below these individuals, and all poorer than them, would be 96 real countries. Yet, it is precisely their soil that is the source of the managers' wealth.

More or less friendly takeovers and mergers,

successful and failed stock market

flotations, fines for environmental abuses,

XSTRATA //

future mega-mergers,

and sweet sounding music ...

Xstrata, Zug - 2011

08 //

MINING MADE IN SWITZERLAND: XSTRATA IN THE 'SUPER CYCLE'

In addition to the industry leader, Glencore, another mining great power has settled in the canton of Zug: Xstrata. After a merry-go-round of friendly and hostile takeovers and mergers, all that remains worldwide is a handful of global mega groups. As expected, either they originate in countries rich in raw materials or they have a colonial past, such as the world's number 2, BHP Billiton, a union of the Australian BHP (founded in 1885) and Billiton, whose shareholders first joined forces in The Hague in 1860, and which extracted tin, lead and bauxite in the Dutch colonial empire in Southeast Asia. The same is true of the mining companies Rio Tinto (Great Britain/Australia, 1873), Vale (Brazil, 1942) and Anglo American (Great Britain/South Africa, 1917). The exception among the top five is Xstrata, a company domiciled in Zug and listed on the London and Zurich exchanges. Xstrata neither originates in a resource-rich country nor has a colonial past and is much younger than its global competitors TAB. 1.

TAB. 1

THE FIVE MINING GIANTS

Company	2010 revenues in millions of dollars
Rio Tinto	56,576
BHP Billiton	52,798*
Vale	45,293
Xstrata	30,499
Anglo American	27,960

**For the year June 2009 to June 2010*

Source: Company websites and annual and quarterly reports

As long ago as 2001 Xstrata CEO Mick Davis predicted the phenomenon known as the Commodity Super Cycle, which has long since become commonplace in the industry: if supplies are limited in the short term, the massive raw material and energy consumption of the emerging economies would drive prices up. Xstrata bought mines and swallowed up mining companies at a frantic pace. Within a decade the company had risen from the ranks of SMEs (small and medium-sized enterprises) to become one of the hundred most valuable companies in the world. By 2011 Xstrata was the sixth-largest Swiss company listed on the stock exchange, after Glencore, Nestlé, Novartis, Roche and ABB.

The main shareholder in the Xstrata shareholder-value machine is Glencore, which owns around 34 per cent of the Xstrata shares through the Dutch shell company Finges Investment B.B. Until May 2011 the Zug twins shared the chairmanship of Willy Strothotte, and Glencore CEO Ivan Glasenberg also sat on the Xstrata board. Davis, however, distanced himself symbolically from Glencore prior to its flotation. In May 2011 Strothotte was replaced by Sir John Bond, who had chaired the board of the British bank HSBC with and telecom operator Vodafone. He is currently also on the boards of shipping logistics company Moller-Maersk and the Chinese property company Shui On Land.

Essentially, Xstrata comprises five production departments or businesses (plus the much smaller department Xstrata Technology Services). TAB. 2 gives an overview of their rankings and other key data.

TAB. 2

XSTRATA'S COMMODITIES

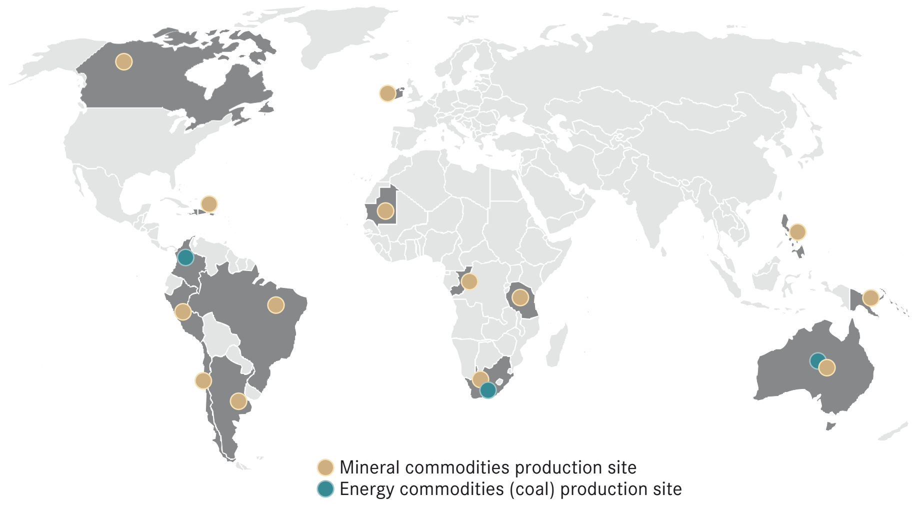
Business	Revenues in millions of dollars (share of group total)	Profits in millions of dollars (share of overall profit*)	Employees	Head-quarters
Xstrata Copper (copper)	14,004 (46%)	3,820 (49%)	11,483	Brisbane (Australia)
Xstrata Coal (coal)	7,788 (26%)	2,216 (28%)	10,473	Sydney (Australia)
Xstrata Zinc (zinc)	3,922 (13%)	917 (12%)	4,645	Madrid (Spain)
Xstrata Nickel	2,738 (9%)	503 (6%)	3,340	Toronto (Canada)
Xstrata Alloys(alloying metals, e.g. ferrochrome, vanadium)	1,894 (6%)	353 (5%)	8,337	Rustenburg (South Africa)

*Excluding unallocated expenditures

Sources: Xstrata annual report 2010, company websites

FIG. 1

THE XSTRATA WORLD



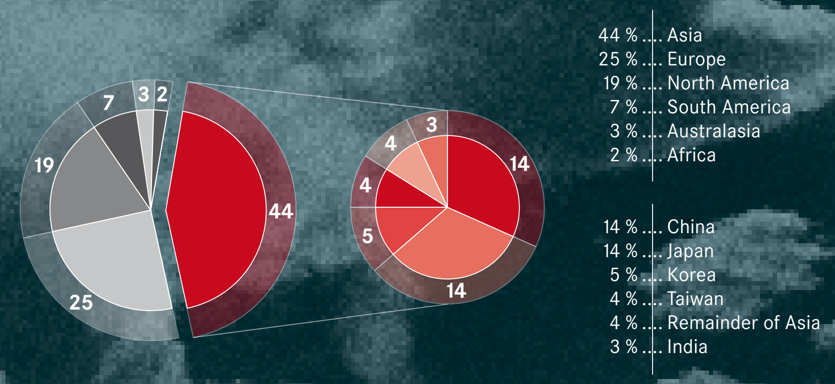
Source: Xstrata annual report 2010

Xstrata is a globalised company, whose principal mines and production facilities are situated in Latin America, Australia and Africa. The geographical origin of Xstrata's production and importance of the individual regions are illustrated in FIG. 1.

No less diverse than Xstrata's regions of origin are its major markets, dominated by those in Asia – surprisingly, Japan is still as important as China. FIG. 2.

FIG. 2

REVENUES ACCORDING TO TARGET REGION



Source: Xstrata annual report 2010

FROM CAPITAL RAISER TO MINING ARM: SÜDELEKTRA GOES XSTRATA

Xstrata's roots date back to another era when Swiss companies and investors dreamed about global expansion and went about promoting it. In November 1926 the Südamerikanische Elektrizitätsgesellschaft was founded in Zurich, a finance company that invested in the production and distribution of electricity in Latin America. The first credit from Südelektra, as the company soon became known, went to Lima Light, Power & Tramways. In 1929 the sub-continent also suffered under the Great Depression. The collapse of the Latin American currencies caused share prices to plummet. Although they rose for a short while in the 1950s, it was not long before the era of private electricity providers came to an end in Latin America. In Peru, where Südelektra still did a great deal of business, the military regime eventually nationalised all the electricity companies. Although Südelektra continued to exist officially, the holding company started to focus on the stocks and bonds of the largest Swiss businesses instead of on global expansion.

In 1990 the private bank PBZ sold its majority holding of 53 per cent in Südelektra to Marc Rich + Co. AG. Shortly afterwards this bank was taken over by the Schweizerische Bankgesellschaft (Union Bank of Switzerland, now UBS). The acquisition of the listed Südelektra gave the privately owned Marc Rich + Co. AG access to the Swiss capital market. It did so in a decidedly deft and discreet way, namely without going public and therefore disclosing its accounts.

The moment it became absorbed into Rich's empire, the company began to diversify beyond trading and increased its shares in mines and production sites (for aluminium for example). Despite high profits and generous banks, the meagre amount of available capital at Marc Rich + Co. AG had hitherto prevented the commodity trader from giving free rein to his growth fantasies. Südelektra, however, could be used as a vehicle to finance new interests and acquisitions via the capital market, through the sale of new shares. Südelektra enabled Rich, by then not exactly 'persona grata' everywhere in Switzerland, to strengthen his connections to the Swiss business establishment. The Südelektra board included people like Reto Dominiconi, who had been Nestlé's Chief Financial Officer, and the industrialist, Thomas Schmidheiny (Holcim).

In 1992 Südelektra acquired an interest in the Argentinian oil and gas reserves "Santa Cruz I". Two years later the company took over the South African ferrochrome producer, Chromecorp Technology. Südelektra then acquired the Chilean forestry company, Florestal del Sur, the largest exporter of wood chips for the Japanese cellulose industry in the mid 1990s, from Marc Rich + Co. AG. In 1999 the out-dated name disappeared and Südelektra became Xstrata, yet another diversified commodity company with a definite cornerstone: 82 per cent of its revenues came from the production of the metals ferrochrome and vanadium, which are used in the manufacture of stainless steel, the remaining 18 per cent was spread over forestry products, aluminium and fossil fuels.[1]

ZUG TWINS: ONE SUCCESSFUL AND ONE FAILED STOCK MARKET LAUNCH

Its exponential growth into today's Xstrata began with a failed initial public offering by Glencore. In September 2001 Glencore was in the final days of a road show, in other words, a presentation for potential investors for the initital public offering in Australia of its twelve coal mines there (which together formed a group called Enex). However, the panic reigning on the capital markets following the September 11 terrorist attacks caused the IPO that had been planned for 17 September to be cancelled. Mick Davis, who was appointed Xstrata CEO, suggested to Glencore that they should sell these coal mines to Xstrata together with the ones in South Africa.[2]

In order to finance these acquisitions, Xstrata made an initial public offering in London. Out of a total 168.6 million newly-issued shares Glencore received 68.6 million as part-payment for the Australian and South African coal mines. Altogether, the public offering earned 1.47 billion pounds (3.46 billion Swiss francs).[3] The former Swiss Xstrata officially merged with the London-listed Xstrata plc, although its shares were still traded not only in London but also in Zurich.[4] The market capitalisation of Xstrata increased more than twentyfold following its low point in 2003, to reach an all-time high in the spring of 2008.

THE FEAST: 'SWEETHEART' GLENCORE SHARES A TABLE FOR TWO

Xstrata is insatiable. Between its flotation 2002 and December 2010 the group amassed no less than 63 subsidiaries, 21 joint ventures, 8 finance or holding companies and 6 majority holdings.[5] The estimated 35 billion dollars or more needed to finance these takeovers came mainly from the issuing of new shares. Two of the most important acquisitions were that of MIM Holdings in 2003, which doubled the group's size in one fell swoop and of the Canadian Falconbridge for the tidy sum of 18.8 billion dollars in 2006.[6]

Such breakneck speed in the fast lane was not without consequences for Glencore. To maintain its holding in Xstrata, Glencore, who was in fact the parent company, also had to exercise its rights to new shares for the capital increases, i.e. to buy newly issued shares. However, Glencore was either unable or unwilling to incur additional debts as a result of the MIM mega deal. Consequently, Credit Suisse First Boston, the former investment branch of CS, made a temporary acquisition of Glencore's tranche of newly issued Xstrata shares for 1.1 billion dollars in total, which resulted in the bank owning 24 per cent of Xstrata.[7] At the end of 2006 Glencore bought the entire share portfolio back. Similarly, in the crisis year of 2009 Glencore lacked sufficient financial resources to keep its proportion of Xstrata's shares when Xstrata issued new shares again. This time the solution lay in a so-called 'sweetheart deal':[8] Xstrata bought the Prodeco coal mine in Colombia from Glencore for 2 billion dollars, in order that Glencore could buy it back for 2.25 billion dollars a year later. The manoeuvre, however, included a bitter pill for Xstrata: in that very year, 2009, the mine, which had been the subject of controversy for a long time, was called to account for having caused environmental pollution. Xstrata suffered not only negative headlines, it was also forced to pay 700,000 dollars in fines, as well as set up an environmental management system.

The potential 'mother of all mergers' has yet to take place. When commodity prices peaked temporarily in 2008, Xstrata rejected a takeover bid worth 85 billion dollars from its Brazilian rival, Vale. The reason was again Glencore: Vale was unwilling to agree to the extension of the exclusive purchase agreements demanded by the principal shareholder.[9]

An suggestion from Mick Davis about a merger that would create a 'mining super major', which was sent to the address of the board of Anglo American in June 2009, but was promptly rejected by Anglo American. However, in February 2012 Xstrata announced its intention to merge with Glencore, so a mining super major will emerge after all.

After a decade of exponential growth it was time to consolidate. Although the intention is to focus primarily on 'organic growth' in the coming years, at the time of writing investment is set to continue For example, 14 billion dollars will be channelled into expanding the production of coal, copper and nickel. A further 14 projects are already in preparation, costing 7.5 billion dollars in total. The company is expanding via both the 'greenfield' route, that is, by constructing new mines, processing facilities, rail links and port facilities, and the 'brownfield' one, in other words, through the development of existing mines by increasing their production and lengthening their service lives. As regards demand for its products, Xstrata has no worries. According to Davis when he presented the figures for 2010, the current boom could only be compared to the industrialisation of the USA or the recovery after the Second World War.[10] In short, an end to the Super Cycle is not in sight.

'LEAN MANAGEMENT': 50 PEOPLE EARNING BILLIONS

By the end of 2009 Xstrata employed 70,747 people worldwide: 38,561 directly and 32,186 indirectly via subcontractors.[11] Since 2004 these employees have been generating billions in profits TAB. 3.

Yet, just 50 employees work in the company's headquarters in Zug and its registered office in London. By way of comparison: Anglo American, which is of a similar size, has 1,000 employees under contract performing these functions. It is possible that the reason for such exceptionally slim structures is simply the fact that many key functions are carried out in the different businesses (for example Xstrata Coal). Growth was achieved through the acquisition of companies that were already large; whose headquarters then became the headquarters of an Xstrata business.

Staff savings also arise from the close partnership with Glencore, which means that Xstrata needs a relatively small trading department. In 2010 Glencore bought commodities worth 9,319 billion dollars from Xstrata; on top of this came payments for processing and refining, totalling around 301 million dollars. However, Glencore not only buys from Xstrata, it also markets a considerable share of the latter's products.

TAB. 3

EARNINGS BEFORE INTEREST AND TAXES (EBIT; IN MILLIONS OF DOLLARS)

2002	264.1
2003	545.9
2004	1,497.2
2005	3,932
2006	8,419
2007	8,792
2008	7,249
2009	1,871 (or 4,313 before exceptional items of 2,442, which include the acquisition of the Prodeco mines)
2010	7,669

Source: Xstrata annual reports

Exclusive purchase or marketing contracts for each of the commodities exist between the two 'Siamese' twins. These contracts are either short-term (e.g. copper), for 20 years (coal) or even for an indefinite period (evergreen), but can all be cancelled. In the case of alloys for example, Glencore receives a fixed fee of 3.5 per cent on top of the achieved sales price. If Xstrata finds buyers paying higher prices, Xstrata itself can sell the products. Even in that case, however, Glencore receives a 3.5 per cent payment.[12]

The third reason for such lean management at Xstrata is the company philosophy of the all-powerful CEO Mick Davis. The latter allows his key colleagues plenty of room of manoeuvre when making decisions – in order to increase shareholder value: "If you create an environment where people are free to act and are not burdened by responsibility, they will unlock untold value. We were radical in not having someone at the centre passing comments on how the operations should be run. I am the last person who should be telling a coalminer how to dig up coal."[13]

A journalist who visited the company headquarters in 2004 found it almost surreal: "Apparently, if you were not careful, you could easily miss the entrance to the office building at no. 2 Bahnhofstrasse in Zug, in its idyllic setting amidst shopping arcades, with a boutique on the right and a wide-fronted cafeteria on the left. A pillar with an intercom and a camera stood in front of the locked, revolving door. 'Zweiter Stock' (second floor) squawked a voice from the loudspeaker. Xstrata occupied just one floor. Ordinary offices painted in rather showy colours; separated from the corridor by a wall made almost entirely of glass, the meeting room looked intimidating. It seemed absurd that merely twelve people worked there. Hardly a sound could be heard, just a quiet telephone conversation a little way off and some signs of life in reception where a secretary was working in almost complete silence."[14]

GLASENBERG'S NEIGHBOUR: MICK DAVIS FORMS A GLOBAL GROUP

Whether shopping sprees, radical decentralisation or slimmed down headquarters, Xstrata's structures and strategies bear the unmistakeable stamp of CEO Mick Davis. The English Times sums up the 'Davisian philosophy' as follows:

- The value of momentum: Keep doing things, even if they initially fail.

- The value of opportunism: Seize chances rather than looking for a strategic fit.

- The value of value: Focus on shareholder return by linking the remuneration of staff to performance wherever possible.[15] Davis speaks enthusiastically about how he has made more of his staff millionaires than the entire global mining industry.[16]

Michael Lawrence Davis was born in Port Elizabeth in South Africa in 1958. He grew up in the same Jewish neighbourhood as Glencore CEO and Xstrata board member, Ivan Glasenberg. Davis studied at the Theodor Herzl High School in Port Elizabeth and Rhodes University, where he graduated in Accounting in 1979. Between 1986 and 1994 he worked for the South African state-controlled electricity company Eskom, becoming Finance Director in 1988, at the tender age of 29. Here he helped to reduce the number of employees by half and prepare the company for privatisation. During Davis' time at Eskom he played a crucial role in the success of Xstrata's predecessor, Südelektra. Chromecorp Technology (CCT), founded in 1987 and taken over by Südelektra in 1994, had long-term electricity supply contracts. Energy is the key cost factor in ferrochrome production and CCT obtained electricity from Eskom at 50 per cent below even the lowest industrial tariff in the mid-1990s.[17]

Having been passed over in the appointment of the Eskom CEO, Davis moved to the South African mining and company conglomerate, Gencor. The launch of the mining divisions of Gencor and Billiton as Billiton plc on the London stock exchange in 1997 thrust the CFO Davis into the international league of top managers. The listing of Billiton also marked the comeback of the London stock exchange as the centre of mining finance. Before Billiton's arrival on the scene, Rio Tinto had been the only notable mining company on the banks of the Thames. Davis was a driving force behind the merger between BHP and Billiton, which created the second largest mining group in the world at the time.

Yet his personal ambition to head the new group was again thwarted.[18] His departure to the then unknown Swiss niche player Xstrata surprised many; what he has made out of it since will no doubt have surprised even more.

GREEN SHAREHOLDERS GOLDEN BOY DESPITE 'GREENFIELD' PROJECTS

"Xstrata's objective is to create value for its shareholders in a sustainable manner, minimising our environmental impact, working in collaboration with communities and other groups and prioritising the health and safety of our workforce over production or profits:"[19] On the subject of sustainability Mick Davis' words often sound like those of a company leader who must take into consideration the increased environmental awareness and social conscience of the customers. Yet, it is not direct consumers that buy from Xstrata, since only insiders know about the brand, and an environmentally and socially cavalier mining company would have nothing to fear politically in Switzerland anyway. Why, then, the sweet sounding music?

One of the most fundamental differences between Glencore and Xstrata lies in their methods of communicating the environmental impact and human rights problems of their operations. It is primarily this difference that reflects the cultural contrast between Glencore, until recently a privately owned company, and the listed Xstrata. Xstrata's shareholders include many institutional investors, among them pension funds. A scandal posing a threat to reputations could quickly prompt those with high ethical standards to jump ship.

Xstrata has therefore been making efforts to minimise this risk for a long time now. Since 2004 the company has published an annual Sustainability Report, in which its planned objectives in terms of health and safety, climate change, biodiversity and water management are formulated, and information on their attainment set out in a four-point scale. In addition, a percentage of the profits is donated for social projects in the local communities. Mick Davis is one of 18 mining CEOs who have joined forces in the International Council on Mining and Metals (ICMM). This initiative sees itself as "a change agent […] related to our members' social and environmental responsibilities where collaboration makes sense". Davis leads the ICMM working group for climate change.

However, the sustainability report gets a great greenwashing at Xstrata too. According to its sustainability report, the group "is committed to implementing" the Voluntary Principles on Security and Human Rights. Unlike many other voluntary agreements, such as the Global Compact, this set of principles actually has some teeth. If applied consistently, they can have tangible effects on how companies can work together with local private security firms, police and the military. But in contrast to other main players in the business, such as Anglo American, BHP Billiton or Rio Tinto, Xstrata is not a "participant" to these principles. Xstrata's 'adherence' to these human rights principles is therefore meaningless.

Despite this, Xstrata has achieved its aim with regards to its intended target group of investors of a green persuasion: the company topped the Dow Jones Sustainability Index for mining in 2010 for the fourth year in succession. Nonetheless, even a mining sector leader cannot reduce the massive land and water use that mining necessarily entails if it believes in maximising its profits at the same time. Moreover, the accelerated development of 'greenfield operations', that is, new mines, processing and transport facilities, automatically creates further potential for conflict. At the time of writing for example, the current iron ore projects are being carried out in desperately poor countries such as Mauretania and Congo-Brazzaville. In turn, the Tampakan exploration in the Philippines has already been the target of guerrilla attacks and in 2009 unidentified persons killed a critic of mining in the region. What is more, in order to keep the cost of copper production down in Las Bambas, Peru, the intention is to pump the copper concentrate into existing processing facilities via a pipeline 215 kilometres in length, which will further increase what is anyway considerable water consumption in opencast mining.[20]

Even the expansion of existing mines causes problems. A local environmental organisation in the Hunter Valley in Australia has lodged an appeal against the doubling in coal production at the Ulan coal mine.[21] The global environmental network, Friends of the Earth International, has challenged the planned construction of the opencast mine, Wandoan, in Queensland because the coal extracted there will contribute to global warming.

INTERIM CONCLUSION

Switzerland is home to not only the largest global commodity trader (Glencore), but also the fourth-largest mining group in the world (Xstrata) despite the fact that the country has neither a raw materials base nor any pretensions to power left over from a colonial past. Xstrata stands out in the mining industry due to its multi-layered connections to Glencore. A whiff of adhesion contracts hangs over the relationship between the Zug twins and it is never clear whether the principal shareholder is pulling a fast one on its 'mining partner' or not. Not even 'Mr Xstrata' in the person of Mick Davis can solve this historically evolved dilemma.

Xstrata is swimming ahead of the sustainability tide in the waters of the financial markets. However, 'clean' mining is definitely not what the Sustainability Leader is engaged in, and its efforts to do business in a more environment-friendly way continually come up against the limitations imposed by the bottom line. Moreover, Xstrata's production is not 'fair' and therein lies another contradiction that is much more difficult to resolve in today's world: regardless of philanthropic social projects, there remains a glaring discrepancy between profits totalling billions, salaried millionaires and the scandalous poverty that exists all around the production sites that generate this very wealth .

... 20 tonnes of mine spoils for each single wedding ring ...

GOLD //

Switzerland shines not only as a gold hub, but

also with confidentiality, opaqueness and secretiveness.

Talk is silver, silence is golden.

09 //

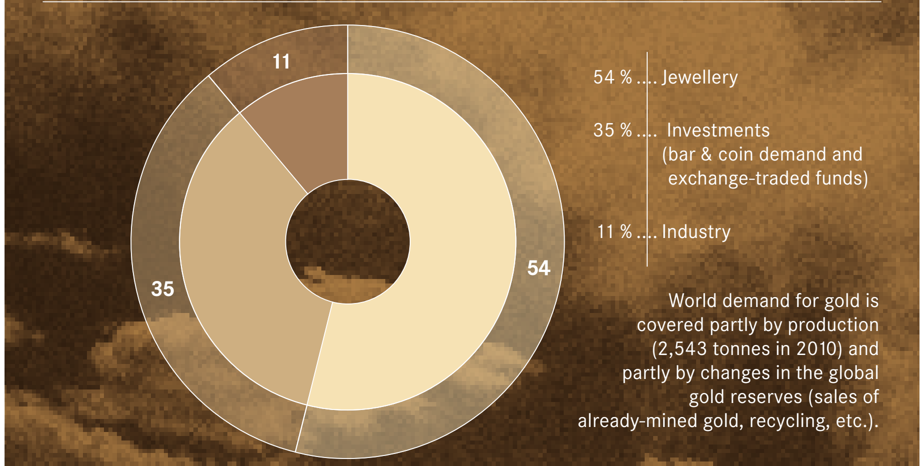
SWISS GOLDFINGER: FRIGHTINGLY BEAUTIFUL CONFLICT METAL

A large part of the global acquisitions and sales of gold is carried out from Switzerland. Until the end of the 1990s, the undisputed trading centre was the Zurich Gold Pool, established by the Swiss Credit Institution (now Credit Suisse), the Swiss Bank Corporation and the Union Bank of Switzerland in 1968. In second place was London. Since then however, numerous other financial centres, especially Dubai, have broken Zurich's long-standing dominance and the gold trade has become internationalised. Nevertheless, according to the World Gold Council (WGC), the umbrella organisation for the gold industry, still more than a third of global gold production is sold on the banks of the river Limmat in Zurich.[1] Thus, Switzerland is still the world's largest marketplace. In contrast to the other commodities passing through the Swiss carousel, the 'mother of all precious metals' actually comes into Switzerland physically for processing.

One can only speculate about the exact amount of gold imported and exported by Switzerland. According to the trade statistics published by the Federal Customs Administration, 2,306 tonnes of raw gold with a value of 70.1 billion Swiss francs passed through Federal customs in 2010.[2] To this has to be added gold dust and gold in the form of coins and fashioned items. In total, imports of 2,405 tonnes, or two-thirds of the annual global demand for gold of 3,812 tonnes FIG. 1, are booked by Switzerland. This figure does not include the substantial flows of gold that are trans-shipped and sometimes stored in the 13 Swiss duty-free warehouses, for example by discreet companies such as the Geneva-based Swiss Precious Metals.

FIG. 1

WORLD DEMAND FOR GOLD 2010*



*Aggregated demand of 3,812 tonnes, with a corresponding value of 155 billion dollars

Source: www.gold.org[3]

SOUTH AFRICA AND THE OSTRICH POLICY

Customs statistics remain opaque in another area: in contrast to the import/export data on other goods, and despite numerous parliamentary initiatives, the federal authorities do not publish any figures on the countries of origin of the gold coming into Switzerland. The leading role of the big Swiss banks in the international gold trade – and with it the almost paranoid secretiveness of this business – has its origins in the trade in gold mined in South Africa during the 1970s and 1980s. Its sale was crucial to the survival of the apartheid regime and generated huge profits. Today we know that up to 80 per cent of South African gold production passed through Switzerland – in an enterprising violation of the UN political-economic embargo.[4] It should therefore not come as a surprise that, to this day, the profiteers from those past deals still show no desire for transparency. But it seems strange that the Federal Council is perpetuating this secretiveness surrounding the gold business, and it raises the suspicion that this sector is still not managing its activities in a responsible manner. For example, 72 per cent of all material from the world's seventh largest goldmine, run by the corrupt Nazarbayev clan CHAP. 15.2, was exported to Switzerland. The *BBC* arrived at this estimate in 2005, based on information from the Kazakh Agency for Statistics, which was slightly more 'talkative' than its Swiss counterpart.[5]

CHILD LABOUR, WAR GOLD AND OTHER SINS

On the other hand, Peruvian statistics show that, until recently, gold accounted for 99 per cent of Swiss purchases of goods in this Andean country. This small, landlocked European nation thus moved up to be Peru's third-largest trading partner behind the USA and China. In global gold production, Peru is in sixth place. Apart from the fact that the yellow metal is mined there under devastating environmental and social conditions (for each wedding ring, 20 tonnes of mine spoil is produced), Peruvian gold is regularly criticised because of the not insignificant part it plays in money laundering and drug trafficking.[6]

Or Africa. An investigation by Human Rights Watch in 2005 highlighted Switzerland's key role in the marketing of the gold that comes from deposits in the Democratic Republic of the Congo. In violation of one of the embargos imposed by the United Nations Security Council, 70 per cent of this coveted commodity is allegedly landed in Switzerland, probably in the duty-free warehouses.[7] In August 2008, two journalists uncovered the winding paths along which Mali's gold, 96 per cent of that exported, mined overwhelmingly by children in medieval conditions, made its way to the smelters of Raffinerie Valcambi SA near Chiasso.[8] In 2011 a Human Rights Watch Report showed that between January 2009 and Mai 2011, 60 per cent of Mali's gold was exported to Swiss companies, including Decafin SA in Geneva.[9]

Responding to a question from National Councillor Josef Lang regarding the purchase of Congolese gold by Swiss companies – purchases since confirmed by a UN report – the Federal Council said in 2006 that it only knew of "special cases" and declined to give the names of the companies concerned "for reasons of data protection".[10] Even after being reminded of provisions designed to combat money laundering through gold trading, the government was content to state that the regulation for the control of precious metals did not impose a requirement on anyone to check whether the precious metal was of legal origin. Another fact concealed was that certain businesses among the Swiss gold refineries are not subject to the Money Laundering Act, which at that time had already been in force for nine years.

THREE REFINERIES AS CENTRES OF THE SWISS GOLD BUSINESS

According to the prestigious London Bullion Market Association, five of the eleven most important European gold refineries are located in Switzerland, where the production and sale of monetary gold are not liable to value added tax. The combined capacity of these refineries is a proud 40 per cent of global gold production.[11] Three of them have belonged for a long time to the three large banks (mentioned above), which financed the purchase of the gold that was originally melted down in their facilities and then formed into bars.

Valcambi SA, referred to above, was a subsidiary of Credit Suisse until 2003, but today is controlled by Newmont Mining, the world's largest gold production company.

Metalor Technologies SA, based in Neuchâtel, was established in the 19th century. As a key supplier to the watch industry, a sector with a large demand for gold, it belonged to the Swiss Bank Corporation from 1918 until 1998. Metalor is now in the hands of the French investment company Astorg. Under the name Métaux Précieux SA, Metalor processed the Central Bank of Zaire's yellow metal during the time of dictator Mobutu Sese Seko. The company is said to have handled Saddam Hussein's Iraqi gold.[12] The 2005 report by Human Rights Watch referred to above documents how the Neuchâtel company bought 'dirty' gold in Uganda that originated in the Congo, which at that time was at war. Metalor claimed to have no knowledge of its origin – despite the many alarming articles that were appearing in the press at the time. The company first denied everything and, then responded later, but not until 2005 did it cease its business with Uganda.

Argor Heraeus, in 1999 still 75 per cent owned by UBS and whose Board of Directors includes the former Federal Councillor Adolf Ogi, processes 400 tonnes of gold annually. According to the UN Group of Experts on the Democratic Republic of the Congo, some of this total includes bloodstained Congo gold, a fact persistently denied by the company.[13]

Even less is known about 'Produits artistiques et métaux précieux'. This Chiasso-based branch of MKS Finance, a business founded in 1979 by Lebanese businessman Mahmoud Shakarchi, is also said to process 300 to 400 tonnes of gold annually. Half of this is 'old material' i.e. old jewellery, imports of which from Vietnam have risen by leaps and bounds in the last two years.

And as far as the refinery Cendres+Métaux SA in Biel/Bienne is concerned, not even 'guesstimates' about its smelting capacity are circulating.

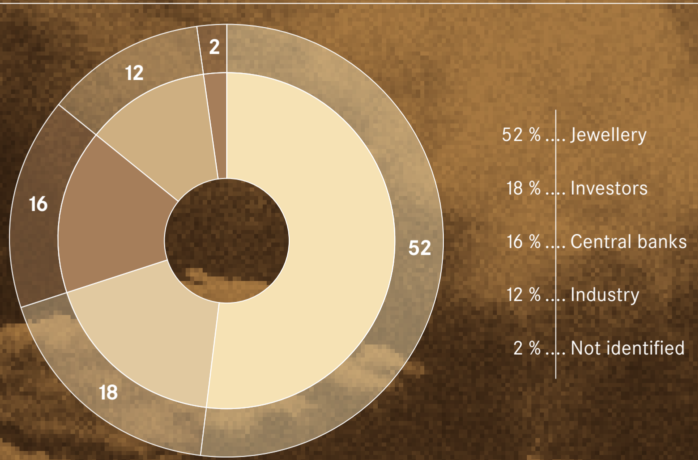
STORAGE AND LOGISTICS: THE FINANCIAL CENTRE ALSO BENEFITS

None of the leading gold production companies are domiciled in Switzerland. To make up for that, the three largest players in the industry are actively supported by the two big banks, UBS and CS. Between them, AngloGold Ashanti, Newmont Mining and Barrick Gold wrest 600 tonnes of gold annually from the ground, which corresponds to approximately a quarter of total world output. On the other hand, there are indirect investments by Swiss businesses in gold production companies; in 2011 Glencore, for example, held 50.7 per cent of the shares in Kazzinc CHAP. 7, a mining conglomerate that also operates the largest gold mine in Kazakhstan. The holding company Addax&Oryx, operating out of Geneva, has shares in the Canadian firm Axmin, which mines gold in Senegal and Sierra Leone.

While cautious in the production sector, the Swiss financial centre is, decisive in the transport and storage of this most important of all precious metals via companies that specialise in this field. The logistics and storage of the gold bars are costly and highly complex aspects of the gold trade and are mainly handled by SIX SIS, a subsidiary of the company that admisters the Swiss stock exchange. Since it opened in Olten in 1992, this company has operated the largest strongroom in Europe. For example, Bank Julius Bär holds the real value of its investment fund Physical Gold there. In October 2009 this amounted to some 65.35 tonnes of gold. As a comparison, HSBC in Manhattan holds 130 tonnes in its vaults, roughly equal to half of all the gold stored in the New York metropolitan area.

FIG. 2

DISTRIBUTION OF GLOBAL GOLD RESERVES AT THE END OF 2009*



*165,600 tonnes with a corresponding value of CHF 6,955 billion

Source: www.gold.org[14]

Last but not least, it is generally known that the banks offer shares in funds that are backed by physical deposits of gold. In times of currency uncertainties these are very popular investment opportunities that the banks turn into ever more important instruments in the gold market. Attracted by the spectacular 'bull market prices' of this precious metal, which rose from 260 dollars an ounce in April 2001 to more than 1,500 dollars in April 2011, the investment community invested massively in gold bullion. The result was that at the end of 2010 the respective funds

had a value equivalent to 2,167 tonnes of gold, or 7.1 per cent of world gold reserves FIG. 2 held by investors. And Swiss financial institutions are right at the front of the crowd. According to industry rumours, the Zurich Cantonal Bank, with an inventory of 184 tonnes in mid-October 2010, had the third-largest gold fund in the world, followed closely by Julius Bär. In October 2009, the gold held by just these two banks was 12.3 per cent of the total physical gold holdings of all the world's funds.

“We will make it happen ...”

ON THE HIGH SEAS //

Bargain-hunting by hook or crook – using dubious material and frighteningly ingenious and unconventional methods.

10 //

'CRUDE' BUSINESS IDEA: TRAFIGURA'S WASTE ODYSSEY

In 2005 Trafigura's oil traders developed a 'crude' business model. Sellable petrol was to be produced from the worst quality naphtha at a fantastically low cost – all thanks to an experimental refining process. Despite all the technical and legal obstacles the company implemented this plan. Undeterred, 'supertanker Trafigura' maintained its course towards disaster. The journal of an odyssey.

+++ Abidjan +++ Ivory Coast +++ 20 August 2006 +++

On 20 August 2006 the penetrating smell of rotten eggs assailed the nostrils of the people living in Abidjan, the economic centre of the Ivory Coast. Since early that morning around a dozen tanker lorries had been busy emptying the waste water chambers (slops tanks) of the oil tanker, 'Probo Koala', and dumping the waste in open landfills, many of them situated near or right in the middle of residential areas. It is here that adults and children collect and sort rubbish for a living. They were the first to complain of problems with their breathing and vision, diarrhoea and burns. The situation soon became serious with tens of thousands affected. In the end, 33 improvised health centres were set up to provide free examinations and treatment. Then riots broke out, which soon led to the resignation of the transitional government. In his 2009 report UN Special Rapporteur on the effects of toxic waste exports, Okechukwu Ibeanu, refers to official estimates of 15 deaths, 69 hospital admissions and 108,000 clinical consultations. He also mentions that there "seems to be strong prima facie evidence" for believing that the deaths and health-related harm reported were related to the 'Probo Koala's' waste.[1]

But what has all this got to do with secretive commodity trader Trafigura and its branches in Lucerne and Geneva? What we know for certain is that the 'Probo Koala' was chartered by Trafigura, the waste belonged to Trafigura and it was Trafigura that contracted the 'waste management company' in the Ivory Coast. "Trafigura is saddened by the deaths and illnesses in the Ivory Coast," the company announced.[2] Beyond that, the Swiss-Dutch company has consistently denied any responsibility whatsoever. "Trafigura vigorously denies any wrongdoing in relation to Ivory Coast," stated a lawyer on behalf of the company to Norwegian television.[3] This defensive strategy includes two crucial points: 1. Trafigura bears no responsibility for the behaviour of the waste management company it contracted and 2. the waste had no toxic effects whatsoever on human health.

News of the story spread beyond the Ivory Coast and around the world. Now, several years later, many connections have become clearer, but some key questions still remain unanswered. Trafigura continues to do less than nothing to clarify the situation. In response to unwelcome criticism the company prefers to sue for defamation according to British libel laws, a particularly powerful weapon. 'Libel Law' is feared by media professionals and NGOs all over the world since the legal costs alone can mean financial ruin – even with immaculate sources and impeccable research. In October 2009 Trafigura caused an uproar in the UK with a raft of relevant injunctions against the *Guardian*. The bone of contention was known as the 2006 'Minton Report', which had warned Trafigura of the grave dangers threatening the health of those affected only a few weeks after the event. Trafigura had the publication of the leaked expert report banned and, furthermore, prevented the newspaper from reporting about this ban. The *Guardian* even had to remain silent about the incident when the MP Paul Farrelly asked a question about it in Parliament.[4] But this time Trafigura had gone too far. Prominent judges[5] and politicians, such as the then Deputy Prime Minister, Nick Clegg, voiced their disapproval in public.[6] A few days later, the otherwise reticent Trafigura released a video message in which the company gave its assurance that it had at no time intended to prevent a parliamentary report on the incident.[7]

Trafigura usually negotiates settlements with its legal opponents before the matter goes to court. With surprising results: having sharply criticised the company at first, the world-famous *BBC* and even the British lawyers acting for the victims finally accepted Trafigura's self-justifying mantra that, "[T]he slops could at worst have caused a range of short term low level flu like symptoms and anxiety."[8] So, the waste is supposed to have produced no more than a few flu-like symptoms in the end. Why then had Trafigura not laid all the facts on the table a long time ago and instead hidden behind an army of expensive PR consultants and top lawyers? To understand the reasons, it is worth taking a trip to the margins of the oil business.

THE SULPHUR PROBLEM

The story begins in the Gulf of Mexico where, just a little inland, lies the small Mexican town of Cadereyta Jiménez. Life here is dominated by the nearby refinery, Ing. Héctor R. Lara Sosa. It belongs to the state-controlled oil company, PEMEX, which is adept at filling the state and party coffers alike. PEMEX is renowned on the crude oil market, a market

increasingly caught between the devil and the deep blue sea. On the one hand, the growing scarcity and inaccessibility of the reserves mean the oil being produced contains more and more sulphur; on the other, the market is hungry for products that are as sulphur-free as possible. After the war the rapid rise in sulphur emissions caused acid rain, prompting headlines about forest dieback early in the eighties. Then, stricter environmental regulations on oil products reversed the global trend in sulphur emissions. It was not just environmental organisations which demanded fuels that were as sulphur-free as possible, but also the automotive industry because these fuels do less damage to engines and, at the same time, are required for modern catalytic converters. The sulphur content of crude oil can vary enormously. Whereas so-called 'sweet' varieties are low in sulphur and less viscous, 'sour' oils are thick and sulphurous. Desulphurising them is technically difficult and expensive. As a result they cost rather less to buy than sweet crude oils. The more the price of oil rises, the greater this price advantage and the more it pays off to refine sour varieties, although this is more expensive.

At this point PEMEX decided to exploit the price advantage further, by processing an even sourer crude oil mixture in Cadereyta. From late 2002 the proportion of viscous Mexican Maya Crude, one of the crude oils with the highest sulphur content, was increased from 30 to 53 per cent of the crude oil mixture. This modification proved lucrative since the price spike during the next few years (including a historic high of 140 dollars in July 2008) vastly increased the financial benefits of using sour crude oil. According to estimates, the new crude oil mixture enabled the refinery in Cadereyta to save far more than 100 million dollars between 2003 and 2005 alone. Yet, it was decided not to expand the desulphurising facilities, "mainly due to budget reasons," said a PEMEX lawyer to the US environmental authorities in 2006.[9] Shortly afterwards an attempt was made to treat the remaining extremely sulphurous residues in the overburdened facilities, but PEMEX quickly abandoned the experiment and stored the residues (also referred to as ‹coker naphtha›) in its tanks instead. However, within 30 months these storage facilities were full to capacity. How could the material be disposed of? In the summer of 2005

PEMEX entrusted its trading division, PMI, with the task of finding a buyer for these inferior goods.

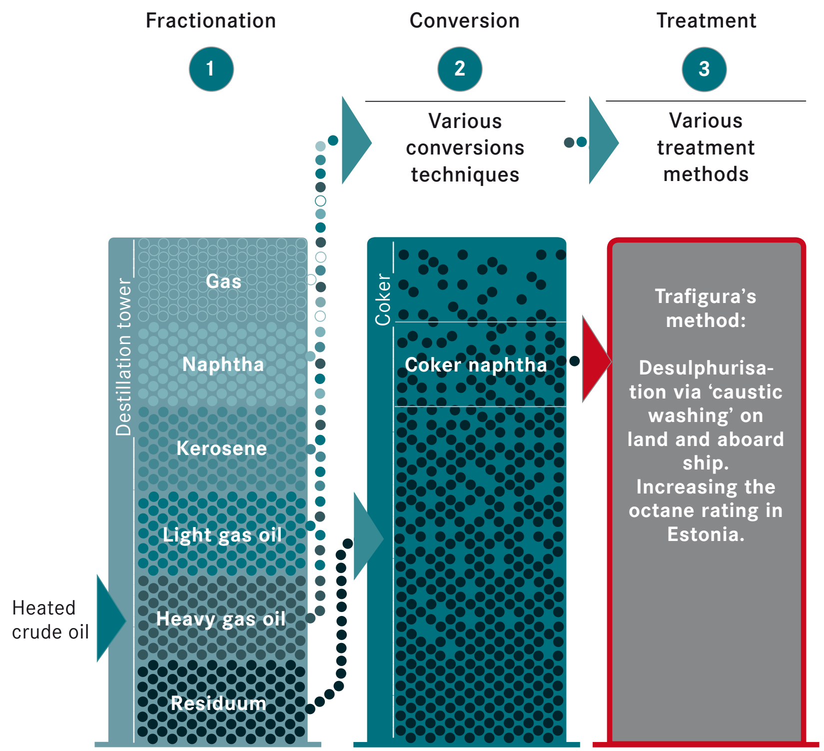
OPPORTUNITY IS THE MOTHER OF INVENTION: A 'CRUDE' BUSINESS IDEA

London, Christmas 2005. After days of hoping for a white Christmas, a few damp flakes fell at last on 27 December. Yet, the mood was anything but merry in Trafigura's prestigious offices just a stone's throw away from Hyde Park. It's 3:15pm and the fuel team has just received an email from a colleague in Houston. The subject line reads "More high sulphur from PMI,"[10] which means PMI is asking for a bid for its coker naphtha. During the next few hours twelve emails cross the Atlantic. It soon becomes clear: "This is as cheap as anyone can imagine and should make serious dollars."[11] But by what process can marketable petroleum be produced from the coker naphtha on offer?

The process comprises three steps; fractionation, conversion and treatment and should really be carried out by a refinery FIG. 1. But in this case only the first two steps were conducted by the Cadereyta refinery owned by PEMEX. During fractionation the crude oil is heated in a distillation column, whereby it separates into different grades of declining quality. At the top are the 'light' gases, followed by naphtha, kerosene, domestic fuel oil, heavy oil and residues. In a second step the constituents of the heavy products are again converted into lighter and heavier grades. A possible method for removing particularly cheap, sticky, viscous oil slurry is to use a coker, a unit that works at temperatures of around 500 °C. One of these machines was installed in Cadereyta in 2002. Different grades of oil are also formed in the coker and the second lightest is also called naphtha. However, this type of 'coker' naphtha is far inferior to naphtha that has been produced directly. This means the third and final step, treating this intermediate product, is all the more important.

FIG. 1

SIMPLIFIED ILLUSTRATION OF THE REFINING PROCESS AND OF TRAFIGURA'S METHOD



Light and heavy constituents separateinto different fractions according to their boiling point. Thick, sticky residues remain, forming a sediment.

Some of the heavy fractions can be converted into lighter constituents by means of conversion. The fractionated 'residues' can be heated even more, e.g. in a coker, and again separated into different fractions.

Any unwanted materials in the fractions (e.g. sulphur) are then reduced. With petrol, the octane rating is increased as well.

Source: U.S. OSHA Technical Manual 2003; NRK Focus: Dirty Cargo 2008; various other sources

This involves removing sulphur and other impurities and increasing the octane rating so that the product ignites more easily. However, this type of treatment is expensive.

Meanwhile, back in Trafigura's London office, a colleague, who asks for more time to test the product,[12] is confronted with the rhetorical question: "Do we want PMI to show these barrels elsewhere?"[13] No, of course they shouldn't wait until the competition gets wind of the bargain buy.[14] Some of the team members discuss the cheap treatment method, 'caustic washing'. This involves adding chemicals to bind with some of the sulphur content. Today Trafigura describes this treatment method as a "common and legal process, carried out around the world."[15] However, on this December evening in 2005 the team had misgivings. The plan to carry out the process in Texas, i.e. close to the source, was quickly rejected for legal reasons.[16] At 19:11 Trafigura trader James McNicol sent a message requesting a list of places where caustic washing was (still) actually allowed.[17] Just 20 minutes later Trafigura man Naeem Ahmed responded with the following message: "We have already spoken to all the main storage companies, US, Singapore and European terminals no longer allow the use of caustic soda washes since local environmental agencies do not allow disposal of the toxic caustic after treatment."[18] In other words, the controversial method was no longer allowed in many places for environmental reasons so the search concentrated on finding a waste management company willing to accept the process waste. By late that evening the list was uninspiring: a specialist company in Rotterdam (expensive, transport across EU borders not allowed) and one in the United Arab Emirates that "disposes the slurry in Fujairah (not sure if in a legal way!)."[19] Further clarification was planned. Shortly before midnight Claude Dauphin, one of the six top managers at Trafigura at the time, was put in the picture by a member of the trader team: "We will make it happen. PMI showing us more barrels Super Cheap now."[20] The very next morning McNicol replied: "Claude owns a waste disposal company and wants us to be creative."[21] The situation called for unconventional solutions, so it seems.

WEST AFRICA AND TEST CASE TUNISIA

By the end of that winter Trafigura's new coker naphtha business was starting up. Allegedly the company had signed a one-year contract to purchase the dubious Mexican material that was nowhere near to being usable petrol. Inside the company it was appropriately referred to as 'PMI crap'[22] and 'PMI shit'[23]. This material was a far cry from standard naphtha due to its sulphur content, among other things TAB. 1. A staggering 99.4 per cent of the sulphur would have to have been removed to meet the European limit values at the time – a sheer impossibility, given the cheap process planned.

But Trafigura had plans other than reducing the sulphur content to EU levels. The priority was not to eliminate the sulphur, but to convert it into less foul-smelling compounds. Trafigura saw this as crucial in view of the target market. In 2006 West Africa was Trafigura's key market CHAP. 11 and was at the same stage as Europe had been at the start of the 1980s with regards to sulphur regulations. What this meant in concrete terms was that African petrol often contained 100 times more sulphur than the European limit values stipulated. Those in the oil industry refer to the products manufactured for regions such as this as, "products adapted to the needs of the local market."[24] In other words, the fuels that are delivered are as dirty as they are allowed to be. The London traders expected earn some seven million dollars in profit per shipload from Mexico, which were due to arrive once a month.

After the initial tests in the United Arab Emirates Trafigura at last found a partner in Tunisia for its coker naphtha project. A business called Tankmed would make its tanks available for the chemical experiment. The first attempt went smoothly but by the second delivery massive problems had arisen. On 9 March 2006 a penetrating smell pervaded the vicinity of the tanks, becoming unbearable by 13 March.[25] The Tunisian authorities were alerted and by 22 March the pressure was so great that Trafigura trader, Naeem Ahmed, asked the White Consultant Group located in Dubai for help:

TAB. 1

COMPARISON OF SULPHUR CONTENT*

Crude oils with highest sulphur content	40,000
Crude oils with lowest sulphur content	100
Crude oil mixture from the Cadereyta re!nery before the end of 2002	22,800
Crude oil mixture from the Cadereyta re!nery after the end of 2002	26,500
Cadereyta coker naphtha (untreated)	8,000
Standard naphtha	50–1,000
Limit value for petrol in Togo in 2006	2,500
Limit value for petrol in the EU in 2006	50
Limit value for petrol in the EU from 2009	10

**Approximate figures in ppm – parts per million*

Source: Trafigura 2009b Appendix 2; Holland + Knight 2006[26]; ARA 2008; UNEP 2009

"Hi Steve

Hop[e] you are well. Any possibility Dave Foster taking a trip immediately to La Skhira/Tunisia to perform a PR Exercise to reassure guys about Odour during a recent caustic wash operation at the terminal?"[27]

David Foster hurried to the scene, investigated the incident and sent his report to Trafigura for checking. Trafigura did not see transparency towards the Tunisians as important, which explains why London replied that the key but critical section in which the probable cause of the smell was named should be omitted in the final version.[28] The consultant did as he was told and concentrated on other aspects.[29] However, the Tunisians became suspicious enough to end their involvement in April 2006.[30]

'DE-STINKING' THE WORLD'S FIRST OFFSHORE REFINERY

The loss of the Tunisian tanks left the traders in dire straits. The purchase contract obliged them to accept the regular shiploads coming in but the lack of processing facilities then prevented them from being shipped out. One employee warned that they urgently needed a plan if they were not all to 'suffocate' from the coker naphtha.[31] Just as PEMEX in Mexico beforehand, it was now Trafigura's turn to be left with huge quantities of unusable material.

It was at this point that another idea that had already been floated during that Christmas holiday period was given another airing: "Alternatively find a chemical carrier and treat cargo on vessel outside the US (but will still need to find a company that will take the waste)."[32] Treatment would no longer to take place in a refinery on land (with all those annoying regulations and controls), but would be moved to the open sea on board a tanker. The resulting waste was to be left to a waste management company to deal with. A suitable vessel was soon found. It was the 'Probo Koala', an old, blue tanker which its owner, a Greek shipping company, did not think so precious as to mind the highly corrosive liquids circulating around it. This type of 'washing cycle' was performed in its tanks for the first time off the coast of Malta in April.[33]

However, what exactly did happen during this remarkably cheap, hence quasi-magical transformation of highly sulphurous refinery residues into valuable naphtha? Trafigura's main problem was that most of the sulphur was in an exceptionally evil-smelling form. Referred to as mercaptans, such materials are the most foul-smelling there are[34] and for safety reasons are sometimes mixed in tiny amounts with gas products to make the latter detectable. Higher doses produce an extremely penetrating smell of rotten eggs which, in increasing concentrations, can cause respiratory problems. Solving this problem did not entail removing the mercaptans, but converting them into less foul-smelling sulphur compounds. In addition, a smaller amount of the sulphur sank to the bottom of the tanks together with the additives. What was left was highly sulphurous sediment. 'Cleaned' in this way, the naphtha swimming around at the top of the tanks was still highly sulphurous. Eventually it was delivered to Paldiski in Estonia where the octane rating was increased. Afterwards it was sold in West Africa as standard petrol.

And so it was that in the case of the 'Probo Koala' a new method of industrial production came to be invented, namely 'offshore refining'. Tucked away in isolated corners of the world's oceans, out of reach of possible inspections, there reigned almost complete commercial freedom. Trafigura set out to exploit it. The crucial problem that hung over the whole business like a sword of Damocles remained insoluble: what to do with the resulting process waste, this sediment full of sulphur and caustic soda?

SEARCHING FOR CHEAP WAYS OF DISPOSING 'SLOPS'

Trafigura's floating refinery anchored off Malta, then off Gibraltar in order to be able to process the coker naphtha in peace. Other vessels brought further loads of coker naphtha. Later Trafigura stressed that the 'Probo Koala' was used for "normal maritime gasoline trade operations," yet it was surely strange that such a standard process should nearly ruin the ship due to toxic deposits at the bottom of the tanks.[35] Moreover, early in the summer of 2006 the process waste began to accumulate on board: a load of round 25,000 cubic metres of coker naphtha produces about 150 cubic metres of waste. Conveniently, every tanker that cleans its storage tanks with water is fitted with special tanks for oily dirty water ('slops'). This has been required since 1983 according to the International Convention for the Prevention of Pollution from Ships (MARPOL) and Trafigura was therefore misusing these tanks because it was storing its process waste in them. MARPOL also requires its member states to ensure there are disposal facilities for 'slops' in every port. Here Trafigura sensed a cheap disposal solution and so began labelling its process waste as 'slops' even though they bore no relation to tank-washing water. However, the ports of Malta, Augusta (Sicily) and Gibraltar were not taken in by Trafigura's trick and turned away the waste FIG. 2.

Now flying a Panamanian flag, the ship set sail once more, this time on course for Amsterdam. At the same time Trafigura secured a quote from a private 'slops disposal company' there for "Gasoline Slops (Majority is Water, Gasoline, Caustic Soda)".[36] The business, Amsterdam Port Services (APS), was quoting around 30 euros per cubic metre.[37] On the evening of the 2 July, the long low barge, MAIN VII, slipped alongside the 'Probo Koala', hugging the high side of the ship. The suction pipe is laid quickly and emptying begins. APS employees soon become suspicious of the penetrating offensive smell. Having collected the waste they return to their berth, lock the tank chambers and send a sample to the laboratory for analysis. The next morning all previous attempts discretion turned to nothing: alerted by those in neighbouring berths on account of the strong smell, the fire brigade and police arrived on the scene. The environmental authorities were also notified, this time by an anonymous fax.[38] Then, based on the findings of its own analysis, APS concluded that its own facilities could not cope with this material. The company contacted their client and raised its the price it was charging to 1,000 euros per cubic metre in view of the laboratory findings.[39] Trafigura was outraged: "The removal company wanted to increase the price without providing any justification," it commented in its annual report 2006 only targeted at investors and not the general public.

The bill for the unloaded 250 cubic metres was going to come to over quarter of a million euros. Too dear for Trafigura, who demanded the return of all its waste. APS also wanted to get rid of it as quickly as possible, but the environmental authorities blocked the return, pointing out it required an export permit for hazardous waste. In the end, the environmental authorities gave in to pressure from APS, concluding that importing the waste had not yet been legally confirmed and therefore exporting it did not have to be approved either. The Dutch police tried to intervene once again, but in vain: The waste was pumped back onto the 'Probo Koala' and following this interlude in Amsterdam, the ship resumed its voyage to Estonia, took another load on board there and shipped it back to Lagos, Nigeria. Still on board: 528 cubic metres of waste that was to be disposed of at the "next convenient opportunity."[40]

'CIRCUMNAVIGATING' THE WASTE PROBLEM BETWEEN AMSTERDAM AND ABIDJAN

Attempts to dispose of the waste were also made in Lagos, but the company commissioned to do this could not cope with this waste either and Trafigura feared legal problems. To 'circumnavigate' the problems in Nigeria, Trafigura man Jorge Marrero then checked to see if a Nigerian barge could not take the waste aboard off the coast of Togo or in international waters. A colleague instructed Marrero via email to call the boss, but the latter was also against an operation in Nigerian waters so the new plan was: "We go to Lome [Togo], charter a barge and bring it back to Nigeria for Daddo [shipping agent] under a different name."[41] But the plan was never implemented. Afterwards Trafigura explained to the *BBC,* that this suggestion "most certainly" did not come from Trafigura's top manager Claude Dauphin and such plans had never been seriously considered.[42]

Ivory Coast on 17 August: at 13:46 'Captain Kablan', a manager in the local branch of Trafigura subsidiary, Puma Energy, received a detailed email from London. It was openly looking for a way of disposing of 528 cubic metres of 'chemical slops'. According to the *BBC's* investigations, at 14:00 Captain Kablan grabbed the phone and called WAIBS, the local shipping agent working for Trafigura. London had notified WAIBS at the same time as Puma about the 'Probo Koala', albeit with less precise details as to the composition of the 'slops'. Captain Kablan asked WAIBS for the phone number of the only large waste management company at the port. This was called ITE, but its employees would not be back from their lunch break for another 30 minutes, which is why the shipping agent gave him the number of another waste management business – a brand new one that had only had a licence for a month. The Compagnie

Tommy was delighted with such a large order. Handwritten in broken English, its quote promised "a good job" the very next day and disposal of the waste for between 30 and 35 dollars per cubic metre at a site called 'Akwedo' that was suitable for all types of chemicals. 'Akwedo' is the town's landfill. On the morning of 19 August 2006 the 'Probo Koala' berthed at Petroci quay in the port of Abidjan. Shortly afterwards tanker lorries arrived and the disaster was set in motion. [43]

EMU INSTEAD OF KOALA: THE SEQUEL IN NORWAY

Even before the world press reported on the scandal, the police had already been in touch with Trafigura man Naeem Ahmed: the Dutch water authorities required evidence of the proper disposal of the waste returned on board in Amsterdam.[44] According to Greenpeace Trafigura had requested a new invoice, quoting much higher prices, from the waste management business, Compagnie Tommy. Then came one headline hot on the heels of another: "Ivory Coast government resigns over pollution scandal" (Agence France Press), "Die Odyssee der 'Probo Koala'" *(Der Spiegel),* "Trafigura: affréteur au rabais" *(Libération),* "Global Sludge Ends in Tragedy for Ivory Coast" *(New York Times).* The toxic tanker and its hirer Trafigura were on everyone's lips.

Instead of pulling the emergency cord at last, on 22 September the company sent another request for disposing of the waste. The recipient this time was a small business called Vest Tank, located in the Norwegian fjords. Trafigura enquired about the price for "disposal of some chemical waste – a by-product of a Merox type washing operation."[45] Having received samples, the Norwegians agreed to accept the waste. The 'Probo Emu', which had since taken over from its sister ship as a floating refinery in the Mediterranean, weighed anchor. In response to some critical enquiries from a neighbouring Norwegian waste management company, Trafigura assured the latter: "'Probo Emu' has been involved in entirely normal operations and has not […] been linked with any events in West

Africa.”[46] In actual fact the ‘Probo Emu’ had not been in Africa, but its function was the same as that of the ‘Probo Koala’: ‘offshore caustic washing’. Similarly, Trafigura confirmed elsewhere that the waste on board the ‘Probo Emu’ was identical to that unloaded in Abidjan.[47] At the beginning of October Vest Tank not only unloaded the first shipment without further ado, it also carried out ‘caustic washes’ on more shiploads from Trafigura at its facilities. Successors to the Tunisians in La Skhira had been found at last!

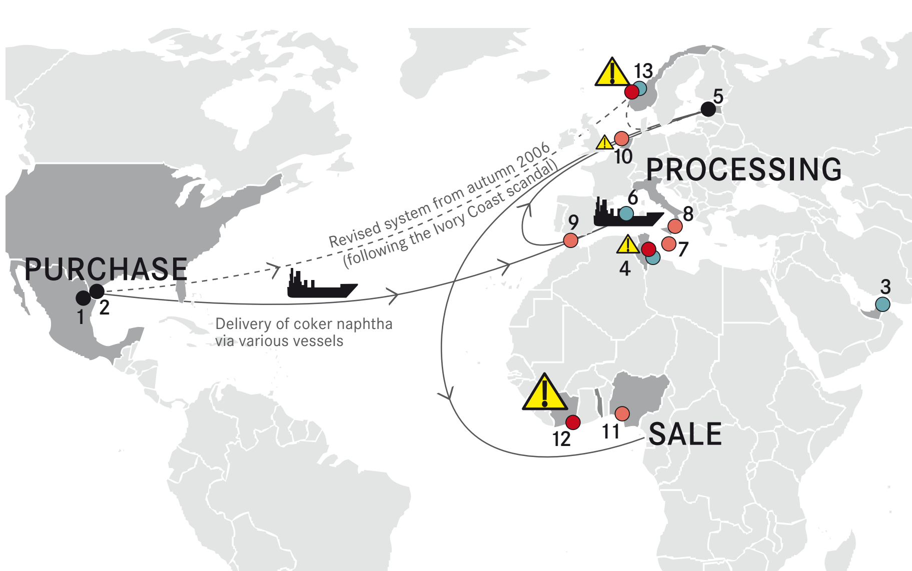
Eight vessels in total visited the small Norwegian port of Sløvåg between October 2006 and April 2007, bringing Vest Tank a shipload of waste and six loads of coker naphtha for treatment. By May, however, the two main tanks T3 and T4 could not take any more shiploads as the waste already there had to be disposed of first. The residues on the floor of the tanks were to be dissolved and the highly alkaline waste neutralised at the same time. After experimenting in a mini test facility, Vest Tank decided to add acid to the residues and implemented this plan on the afternoon of 23 May 2007. At 10 o’clock the following morning an enormous explosion shattered the stillness. Thick black smoke rose up above the area. Huge flames shot out of T3, soon after T4 also exploded. The tanker lorries parked next to the huge tanks looked like tiny matchstick heads, as they too caught fire one after another.[48]

Fortunately, Norway’s worst chemical disaster occurred in a sparsely populated region. Yet the inhabitants of the surrounding community, Gulen, had to cope with the same health problems as their fellow victims in the Ivory Coast: burning airways, watery eyes and difficulty breathing. Even months after the disaster, the people were overcome by nausea as soon as they smelt a strong odour. Had a fire had not broken out after the explosion, the effects could have been even more dramatic. In that case a deadly cloud of sulphur would have been the result according to Jon Songstad, Emeritus Professor of Chemistry at the University of Bergen.[49]

The irony of this story: on the day before the explosion a company called Alexela had bought the stricken Vest Tank plant. Alexela also owns the tank facilities in Paldiski, Estonia, where Trafigura’s vessels docked

FIG. 2

TRAFIGURA’S ‘COKER NAPHTHA BUSINESS’:
A GLOBAL BUSINESS FRAUGHT WITH ACCIDENTS AND DISASTERS



- Refining process (caustic washing)
- Failed attempt at disposal
- Disposal of process waste
- Dangerous event

1_Cadereyta (Mexiko), PEMEX refinery
2_Brownsville (USA), port of loading
3_Fujairah (United Arab Emirates)
4_La Skhira (Tunisia)
5_Paldiski (Estonia), increase in octane rating
6_Probo Koala and Probo Emu
(at anchor in the Mediterranean)
7_Malta
8_Augusta (Italy)
9_Gibraltar
10_Amsterdam (Netherlands)
11_Lagos (Nigeria)
12_Abidjan (Ivory Coast)
13_Sløvåg (Norway)

Source: Author’s illustration

so that the octane rating of the coker naphtha could be increased. One of the shareholders in Alexela, by the way, is Trafigura, which owned 39.9 per cent in 2007.[50]

SETTLE AND CONCEAL: LEGAL AFTERMATH

The highly sulphurous refinery waste affected the health of tens of thousands of people in the Ivory Coast, in Norway and in Tunisia, actually exposing some of them to fatal risks. Accordingly, in June 2010 the public prosecutor in Amsterdam with responsibility for this matter concluded, "Trafigura has let its own interests prevail above health and the environment ... Other choices could have been made but haste, speed and money have prevailed."[51] There remained the issue of the legal consequences of this scandal.

IVORY COAST | Three weeks after the events there, Claude Dauphin and Trafigura's regional manager for West Africa journeyed into the lion's den, straight to Abidjan. What was intended to be a 'humanitarian mission' ended for the Trafigura managers in five months in custody in the central jail. After some tough wrangling, the government of Ivory Coast (gross domestic product in 2006: 17 billion dollars) reached an agreement with the global company (revenues in 2006: 44 billion dollars) in February 2007. This included a payment of 198 million dollars and a declaration absolving Trafigura from all responsibility and legal liability for the disaster. Both sides agreed to refrain from any civil action. Soon thereafter, the judicial authorities also terminated all criminal proceedings against Trafigura's employees. Only Trafigura's business partners in Ivory Coast received prison sentences lasting many years.[52]

UNITED KINGDOM | The immediate victims of the toxic waste scandal turned to London and launched what became one of the largest class actions in British legal history on behalf of 29,614 claimants from Ivory Coast. Again, a settlement was reached in 2009, according to which 30 million pounds sterling were paid out to the victims. The process by which 1,000 pounds sterling on average was paid to each victim has been slow and was still ongoing in 2011. The argument over responsibility for the legal costs, which could in the end greatly exceed the amount awarded as compensation, was still in full swing in the autumn of 2011.

The class action entailed a group of twenty experts, ten from each side, examining the case thoroughly. The experts representing the victims finally accepted that they were not able to achieve the civil standard of proof required before a court as to a connection between the waste and serious injuries. But Trafigura quickly turned the conclusion 'no provable connection' into 'provable non-connection': "More than 20 independent experts established after long, careful and extremely detailed research that the slops [...] could not have caused the alleged deaths and serious injuries."[53] Moreover Trafigura seems to ignore the fact that fatality claims were not subject of the class action at all since they were explicitly excluded by the victims' lawyers soon after Trafigura reached a settlement with the Ivory Coast government in February 2007 and the government took steps to compensate families of deceased persons.[54]

The experts' reports are still under lock and key at the time of writing. What is undisputed is the chemical fact that the harmful impact of the waste was limited as long as it remained unchanged on board ships and in tanks. As soon as acid was added to neutralise it (as in Tunisia or Norway), the sulphur dissolved – with disastrous results. Trafigura maintains that no large quantities of acids came into contact with the waste in the landfills in Abidjan.[55] In other words, the magnitude of danger depended on the environmental conditions: clearly though the waste was potentially highly toxic.

NORWAY | Here Trafigura escaped the law enforcement authorities via a legal loophole since only the import of waste from other countries is regulated, but not that of waste from industrial processes on board a ship. However, the operations manager and the chairman of the board of Trafigura's partner, Vest Tank, were each sentenced to one and a half years in prison for environmental crimes. In May 2011 the appeal court upheld the verdict for the managing director.

NETHERLANDS | To date only Dutch courts have assessed this case. However, the application by Greenpeace Netherlands to have the criminal investigation extended to cover the events in the Ivory Coast was rejected in April 2011.[56] But in June 2010 the Court of first instance reached an explosive verdict on the events in Amsterdam harbour: in its view Trafigura had illegally exported waste into a developing country and concealed the hazardous nature of the waste. The court stated in its verdict that, contrary to Trafigura's account of events, the waste did not come from normal shipping operations but from a chemical process that had been carried out on board a ship for the first time, and the resulting waste was clearly hazardous to health. The court therefore imposed a fine of one million euros. However, Trafigura was acquitted of document fraud. Trafigura trader Naeem Ahmed was found guilty of concealing hazards, but also acquitted of document fraud. He received a six-month suspended jail sentence and was fined 25,000 euros. The captain of the 'Probo Koala' was given a conditional sentence of five months for the same crime and found guilty of document fraud because he had given false information about the waste in the cargo declaration for the port authorities. The court did not regard the fact that he was authorised to act for Trafigura as proven.[57] Trafigura and the public prosecutor both appealed the verdict against the company, but in December of 2011 the Amsterdam Court of Appeal fully confirmed it.[58]

Trafigura's top manager Claude Dauphin was initially included in the case but managed to be excluded from the proceedings in 2008. A witness claimed before the court, that Dauphin was busy at that time with moving his office from London to Geneva.[59] This decision was challenged by the public prosecutor and taken all the way to Netherland's High Court, and in January 2012 the Amsterdam Court of Appeal cleared the way for a possible prosecution of Dauphin, the most senior Trafigura employee involved.[60]

INTERIM CONCLUSION

Since the Marc Rich era, the rules in the commodity business, inasmuch as they exist at all, have been there for traders to evade as skilfully as possible. Because these companies are highly mobile, there are ever more, ever faster opportunities to clinch spectacular deals all over the world. Trafigura pushed this opportunism to the extremes, first by seeking out countries where regulation is weak and then by moving its refinery processes out into the open seas. Disposing of waste should, in the world of Trafigura cost as little as possible or even be a source of profit. So it was that in Norway in January 2007, a Trafigura vessel loaded a cargo of waste on board, mixed it with a consignment of quality petrol already aboard, and sold the mixture.[61]

It is virtually impossible to prosecute multi-national companies under criminal law for this kind of behaviour. What is more, there is scarcely any chance of prosecuting even such blatant wrongdoing as this in developing countries with weak governments, let alone on the high seas. The domestic judicial authorities there hardly have the means or the political support to combat a commodity giant. In addition, developed countries are still very reluctant to prosecute beyond their national borders CHAP. 19. There is usually no shortage of countries involved, as the Dutch public prosecutor's office shows in the example of the 'Probo Koala': "The company that charted the ship is Swiss, with a managing company in the Netherlands. The cargo of the ship was owned by the

English subsidiary of the company. The ship itself is owned by a Greek company and is registered in Panama."[62]

Impenetrable company structures and complex contractual relationships not only make prosecutions more difficult, they also make it easier for judicial authorities to pass the buck to the courts of other countries. Consequently, an action against Trafigura directors with French passports was rejected in France on the grounds that they no longer had close connections with France and Trafigura had its offices located elsewhere. On the other hand, in the country in which the company was officially domiciled, the Netherlands, Trafigura argued before the court that it did not actually operate there at all. The operative offices, it claimed, were in England and Switzerland.[63] As far it is publicly known, the Swiss judicial authorities have done nothing yet.

GENEVA //

Geneva, the oil Mecca – Dynamic and discreet, Geneva's development into a global oil Mecca has been brought about by the influx and founding of many new opaque companies.

11 //

GENEVA, THE OIL MECCA: THE ‘JET D’EAU’ GUSHES BLACK GOLD

One out of every three litres of oil sold on the global market is traded in Switzerland. The five largest oil companies in Geneva alone have a global market share of around 28 per cent TAB. 1. Glencore controls a further five per cent out of central Switzerland. These figures are confirmed by the Geneva Trading and Shipping Association (GTSA), which claims a world market share of 35 per cent for Geneva-based trading houses. The companies operating from the shores of Lake Geneva can be divided into two groups. The first, exemplified by Vitol and Trafigura, includes the traditional oil traders. The second group, whose chief exponents are currently Gunvor, Mercuria and Litasco, comprises younger companies that have grown in leaps and bounds in recent years, not least by selling oil from Russia and its neighbouring countries. According to the industry organisation, the Geneva Trading and Shipping Association (GTSA), the Geneva companies trade 50 per cent of Kazakh oil and as much as 75 per cent of Russian oil. In addition to the five Geneva giants,

TAB. 1

THE FIVE LARGEST INDEPENDENT OIL TRADERS IN FIGURES

		2004	2005	2006	2007	2008	2009	2010
Vitol	Revenues (billion dollars)	62	82	116	145	191	143	195
	Pro«t (million dollars)				1,111	1,368	2,284	
	Oil volumes (million tonnes/year): Crude oil and oil products					200	250	274
	Volumes of all energy commodities (million tonnes/year): Crude oil, oil products, natural gas, coal	200	201	229	266	291	316	394
Trafigura	Revenues (billion dollars)	18	28	44	51	73	47	79
	share of energy division	13	23	34	38	58	35	56
	Profit (million dollars)	153	296	511	453	440	837	690
	Oil volumes (million tonnes/year): Crude oil and oil products					75	100	124
Gunvor	Revenues (billion dollars)	5		30	43	78*	46	59
	Profit (million dollars)					292	289	68
	Volumes of all energy commodities (million tonnes/year): Crude oil, oil products, small quantities of natural gas and coal			60	83		93	104
Litasco	Revenues (billion dollars)				53	68	52	
	Profit (million dollars)		246	224	198	227		
	Oil volumes (million tonnes/year): Crude oil and oil products		80	83	99	96	115	125
	share via the Geneva trading department					82		
Mercuria	Revenues (billion dollars)	6			31	47	35	50
	Profit (million dollars)					244	454	
	Volumes of all energy commodities (million tonnes/year): Crude oil, oil products, small quantities of natural gas and coal		40	50	60	81	90	117
Total trading volume of oil for the five largest independent traders in Geneva (in million tonnes)								744
Oil market volume (measurement based on worldwide maritime transport volumes)								2,640
Market share of the five largest independent oil traders in Geneva**								28%

**Period between July 2007 and December 2008   **Multiple trading may have distorted this figure (e.g. transfer of ownership of an oil delivery within the same country)*

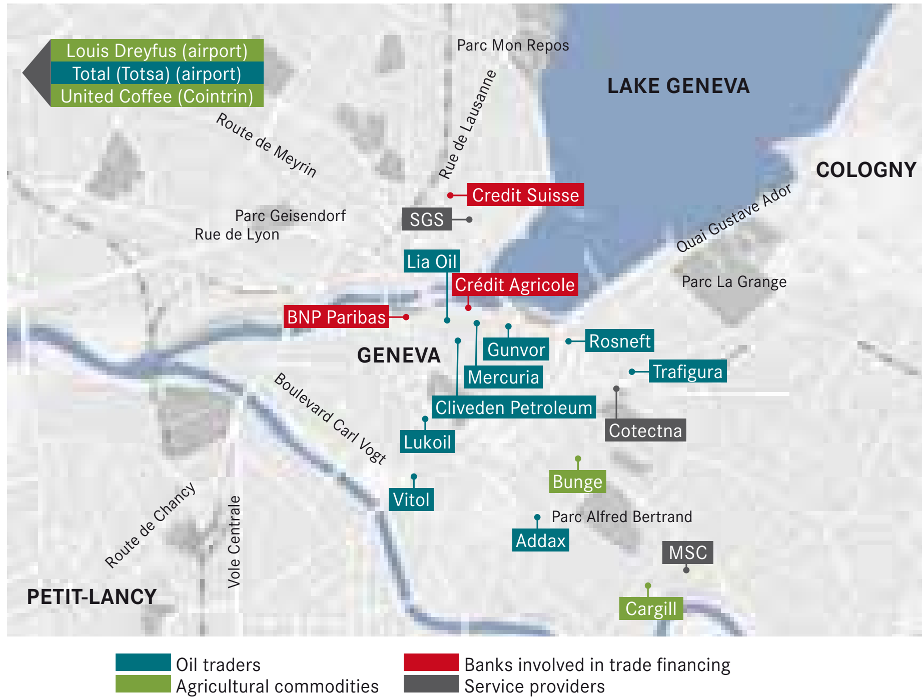
Sources: annual reports, company publications, media reports, world trade volumes: UNCTAD 2010 a number of smaller companies involved in trading, exploration, logistics and financial services also benefit from the current oil boom in Geneva.

Geneva's development into the dominant global oil hub is a recent development. After the oil crisis in 1973, supplier countries cancelled the contracts that had for decades bound them to the major US oil companies and took production into their own hands. Since then, crude oil has increasingly been sold via independent companies functioning as middlemen between producing countries and refineries. In Geneva these new major players were able to draw on the enormous funds they needed for this type of business from banks such as Paribas or, later, Crédit Agricole and the Dutch ING, which specialise in commercial loans. By the mid-1980s, Geneva bankers, who had learned their trade at Paribas, were already financing the sale of Soviet oil. During the same period, the oil company Elf also relocated its sales division to Lake Geneva, thereby enhancing the attractiveness of the city of Calvin as an oil trading centre. Elf, the French major player, wanted to profit from the traditional advantages of a prime location, which had already brought many a commodity trader to Switzerland and persuaded it to stay: low taxation, little regulation and easy access to finance for trading transactions. In addition, the company intended to circumvent the strict regulations for payment transactions which were in force in France at the time.

Elf and the other oil majors Shell, BP, Texaco, Mobil and Total are at the same time the suppliers, customers and competitors of independent wholesalers such as Vitol, Trafigura, Gunvor and Mercuria (Litasco, the number five, depends wholly on the Russian oil company Lukoil). This also applies to the third group of major players in the global oil market, the state-controlled oil companies. Vitol and Co. are not publicly-listed and operate almost entirely under the radar of Swiss politicians, the judiciary and the public. Their major shareholders and employees – both functions are often carried out by the same people – have amassed enormous fortunes, of which their princely mansions on the south shore of Lake Geneva convey only a vague impression.

FIG. 1

NEIGHBOURS AND COMPETITORS: GENEVA THE OIL HOTSPOT



Source: Author's illustration

THE VITOL STORY: METEORIC RISE TO THE LARGEST COMPANY IN SWITZERLAND.

The most important Geneva-based trading company for oil is Vitol, which has its headquarters on the shores of Lake Geneva. Founded by Jacques Detiger and Henk Vietor in 1966, the company established itself in Geneva as early as 1972, i.e. even before Elf, and today sells 5.5 million barrels of oil a day. This is the equivalent of 274 million tonnes a year and meets six per cent of global oil demand, or in other words, the yearly consumption of Germany, France and Italy combined. Vitol has subsidiaries in London, Houston, Moscow, Rotterdam and Singapore and describes itself as "the largest independent oil trader in the world."[1] The exponential growth of its revenues – 1998: 16 billion dollars, 2010: 195 billion dollars – has made Vitol the largest trading company located in Switzerland today, outstripping even Glencore. In contrast to its highly diversified rival in Baar, Vitol's business is based almost exclusively on trading crude oil and its physical derivatives (2008: 76%) and natural gas (12%). Only 12 per cent of its revenues are generated from chemicals, coal, metals and CO_2 emissions trading.[2]

The owners of the highly secretive parent company, Vitol Holding BV which is not listed on the stock exchange, are its senior managers, around 200 individuals in total. The Chief Executive Officer is the Scottish economist Ian Taylor. Having started at Shell, Taylor has worked for Vitol for over 25 years, and saw no reason to change this company structure in 2010.[3] Vitol has a complex, rambling organisational and legal structure of interconnected holding companies. The Geneva-based oil trading company, Vitol SA, which has also traded natural gas and electricity since August 2010, employs only 170 of the 1,578 employees worldwide (as of 2009), but is nonetheless responsible for financing all the group's commercial transactions. It is wholly owned by Vitol Holding Sàrl (Société à Responsabilité Limitée [private limited company]) in Geneva, whose sole owner in turn is Vitol Holding BV located in Rotterdam. For its part, the latter is owned by Vitol Holding II SA based in Luxembourg, whose shares the aforementioned 200 top managers split between themselves, just as they do the billions in profits which Vitol regularly generates.

GAINING MARKET ADVANTAGE FROM HUGE WAREHOUSES AND FAT COMMISSIONS

Its rambling structure makes it virtually impossible to identify the company's headquarters CHAP.14. It is this that enables its owners to create the ideal combination of the different, yet for corporate activities crucial, financial, legal and tax provisions of the diverse national jurisdictions in which the group operates. Hence Vitol succeeded in securing a highly advantageous tax rate of 19.6 per cent on its profits in 2009 (compared with standard corporation tax rates between 25.5 and 28 per cent in the Netherlands and the United Kingdom). In the previous year the rate had been even lower at an unbelievable 7.5 per cent.[4]

But what is the secret of Vitol's success? If you believe the business reports, it is primarily due to strategic advantages, in particular the company's enormous transport and storage capacities, measuring up to four million cubic metres in total. It is these that enable Vitol to exploit the high volatility of the prices of black gold to its best advantage: Crude oil bought cheaply is stored in Fujairah (United Arab Emirates), Zhuhai (China), Zárate (Argentina), Ventspils (Latvia), Lagos (Nigeria), New York or Rotterdam, where the company possesses huge tanking installations, until the price is high enough for Vitol to make fat profits. Another success factor cited by Vitol itself is the convenient location of its NARL refinery in Newfoundland (Canada). NARL lies on the main sea routes between North America and Europe and is therefore closer to West Africa than the refineries around the Persian Gulf. The fact that fully-loaded super tankers can anchor offshore at the NARL terminal enables Vitol to supply the key consumer markets for oil products quickly and relatively cheaply. Its main customers in 2004 also included the distribution companies of BP, Shell, Exxon, TotalFina and Chevron.[5]

However, there are other reasons why Vitol's business is booming. In 2010 a contract with the Nigerian oil company NNPC was revealed which had allowed Vitol to stock up with oil at 'competitive' prices, that is, prices lower than the current market value, in return for commission payments to representatives of the authorities.[6] This agreement was negotiated via a front company called Calson Bermuda Ltd., of which Vitol and NNPC each own 49 and 51 per cent respectively. According to Vitol, Calson was its main supplier in 2003, providing 17.6 per cent of its oil for around three billion dollars.[7]

REFUELLING IN AFRICA AND AT THE AIRPORT

Vitol was also involved in a case of corruption surrounding the head of the mineral oil company, SNPC, in the Republic of Congo (Congo-Brazzaville), who acted as special advisor to the country's president, Denis Sassou-Nguesso.[8] The company also pleaded guilty of involvement in the Oil for Food scandal before an American court in 2007 CHAP. 15.4. Those responsible at the time confessed to having paid bribes totalling around 13 million dollars to Saddam Hussein's regime between June 2001 and September 2002 in return for oil contracts in Iraq. What is more, they admitted giving false statements to the UN investigators. In September 2009 James Woolsey, the former head of the CIA, again pointed the finger at Vitol and accused the company of spearheading the procurement of petroleum and other products refined in Iran.[9] However, Vitol was unwilling to curtail the business until the summer of 2010 and only did so then when it realised its future access to the American markets was under threat. It is hard to believe Ian Taylor's assurance in 2010 that there was no room for shady deals in the oil trade.[10]

Like all trading companies, Vitol is also involved in trading derivatives, meaning it buys and sells crude futures contracts in order to protect itself against price fluctuations. This minimises the particularly high risks due to Vitol's sheer magnitude, which are associated with the transport and queue time of fully loaded tankers CHAP. 13. The oil giant follows yet another trend in the industry: optimising its value-added chain. In February 2011 Vitol acquired almost all of Shell's downstream operations (i.e. processing, storage and end sales), including its petrol stations and aviation and marine fuels divisions, in 14 African countries

for 945.3 million Swiss francs. Shell, where Ian Taylor had begun his career, retains a 20 per cent share in this venture which is Vitol's first strategic move towards establishing its own distribution and sales network. Moreover, the famous shell symbol remains emblazoned on all the products. The remaining shares in this joint venture are shared equally between Vitol and Helios Investment, a fund that presents itself as one of the "few independent private equity companies to be founded and managed by Africans."[11]

THE TRAFIGURA HYBRID: AN OIL COMPANY FOLLOWING IN GLENCORE'S FOOTSTEPS

Vitol's competitor, Trafigura, has long since had a weakness for African petrol stations. Although the company's reputation among the African public has been thoroughly tarnished by the toxic waste scandal in Ivory Coast CHAP. 10, millions of Africans still fill up their motorbikes and cars at Puma Energy pumps, no doubt oblivious to the fact that 81.3 per cent of the company is owned by Trafigura and the Puma branch in Abidjan was directly involved in the events at the time.

Just what is Trafigura putting into the petrol tanks of its African customers via this direct channel, a channel which is growing larger by the day? In the autumn of 2010 the state agreed to allow Trafigura to start supplying a third of Nigeria's imported fuel. Although Nigeria produces more crude oil than any other African country, and the crude oil is of the very highest quality, the country lacks the refineries to process it. At this point Trafigura stepped in, beginning to supply about 50,000 barrels of its fuel a day, for which it received 60,000 barrels of the finest Nigerian crude oil in return.[12] At the same time the company acquired BP's network of petrol stations in Zambia, Namibia and other countries for 296 million dollars.[13] The macabre background to this transaction? BP urgently needed cash to pay compensation claims related to the oil disaster in the Gulf of Mexico. Thus, Trafigura succeeded in doing the same with BP as Vitol had done with Shell. With traders such as Trafigura and Vitol now selling petrol directly to consumers, industry analysts are warning of the risks posed by an oligopoly of dubious firms and the possible "compromises on [fuel] quality" that could be the result.[14]

A SWISS GOLDMINE UNDER A DUTCH ROOF

Trafigura's distribution and storage department, which includes Puma, generates just three per cent of the firm's revenues and is therefore just a small part of the group as a whole. Over seventy per cent of Trafigura's revenues, and therefore its main function, concern the oil trade, in which it does not sell to consumers but to refineries and other oil companies. Here again Africa is the major market (21-29 per cent between 2006 and 2010).[15] Besides the two activities referred to, Trafigura also trades metals, some of which are extracted directly in its own mines. As regards the latter, the company invests heavily in Peru, Spain and the Democratic Republic of Congo CHAP. 15.1. Unlike the other 'pure' oil trading companies in Geneva, Trafigura is also a metals and mining company and more like Glencore in this respect. Put simply, the formula is: Glencore's oil business plus half their non-ferrous metals department and you've just about got a Trafigura TAB. 2.

Like Glencore, Trafigura is a product of the 'Marc Rich School'. Founded by former Rich traders, Claude Dauphin, Eric de Turckheim[16] and Graham Sharp in 1993,[17] the company has grown exponentially: for example, its reported net profit has increased twentyfold in the last ten years FIG. 2.

Environmental and human rights problems are not normally mentioned in the company reports of commodity traders, since they are regarded as having few cost implications and therefore are not viewed as being 'material'. However, the worst scandals have indeed caused considerable financial fallout at Trafigura FIG. 2.

TAB. 2

THE THREE LARGEST SWISS COMMODITY TRADING COMPANIES

COMPARISON (2010)

		Vitol		Glencore		Trafigura	
		Revenues (billion dollars)	Quantity	Revenues (billion dollars)	Quantity	Revenues (billion dollars)	Quantity
Energy	Oil	160	5.5 million barrels/ day	90	2.5 million barrels/ day	58*	2.5 million barrels/ day
	Natural gas	14	20 billion m^3		(not active		(not active
	Coal	total 21	substan-tial		100.9 million tonnes	21	in progress
Metals	non-ferrous			45	approx. 20 million tonnes		approx. 10 million tonnes
	ferrous		(not active)		approx. 9 million tonnes		in progress
Agricultural products				10			(not active)
Total		195		145		79	

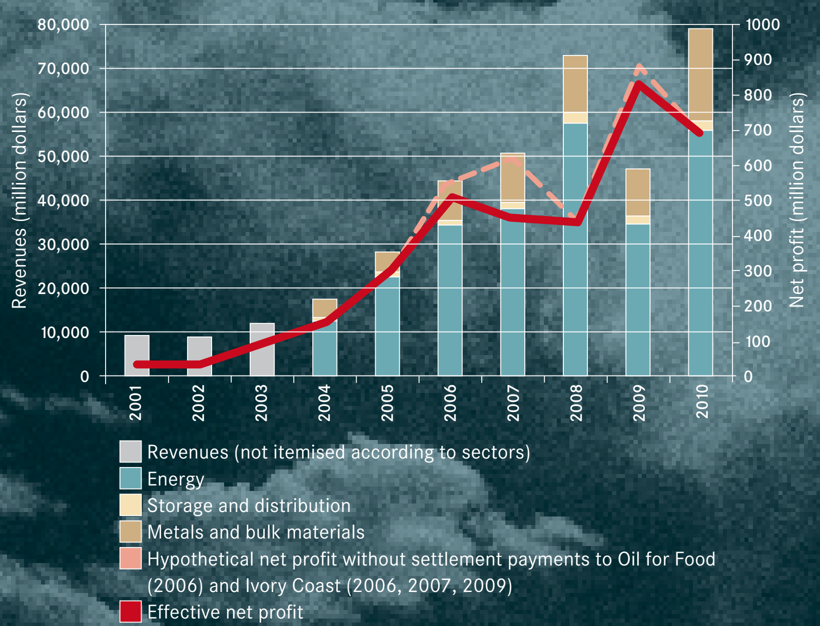
Incl. 2.2 billion for storage and distribution of both oil (Puma Energy) and storage of metals and coal (Impala)

Source: Company websites[18]; Glencore annual report 2010; Trafigura annual report 2010

Trafigura is a prototypical multi-national group: it did not grow up in one country and then expand, but was conceived, established and registered in several countries at the same time. The fact that Trafigura itself does not declare its nationality may be for tactical reasons, but it also shows that artificial constructs of this type no longer think in

FIG. 2

TRAFIGURA'S REVENUES AND NET PROFIT BETWEEN 2001 AND 2010



Source: Trafigura annual reports

national categories. No wonder that Trafigura is at times regarded as a Dutch company, sometimes as a Swiss or often as a Swiss-Dutch company by the media and authorities. In fact, there is some truth in all of these versions, depending on the nature of the question and the viewpoint of the questioner. The holding company is an offshore shell company situated in Curaçao CHAP. 14, P. 285, but the parent company, Trafigura Beheer BV, is officially registered in Amsterdam. Only 30 out of the 2,592 employees working for the company worldwide actually worked in Amsterdam in 2010.[19] On the other hand, both the key trading subsidiaries and the principle tax residence[20] are in Switzerland, in Lucerne and Geneva. Lucerne has been one of its main locations since the company's beginnings. In 2005 the official internal view was: "Trafigura is headquartered in Lucerne, Switzerland, but it is truly an international group."[21]

Today Lucerne is still the headquarters of Trafigura's metal trade and a Trafigura manager mentioned that about 200 people worked there all the time.[22] However, in the past oil trading and the administration of the company had been performed in London. The expansion of the subsidiary in Geneva in 2011 led to dramatic changes in this arrangement: London shrank by two-thirds to just 100 (mainly administrative) employees and the number of those working at the branch on the shores of Lake Geneva rose to 300. Since then Geneva has been the centre of Trafigura's oil trade. This is where its newly developed risk-management team is located, whose responsibilities include 'incident management.'[23] If successors to the 'crude' business model of 2006 CHAP. 10 were to be found anywhere, those responsible for it would now be in Geneva.

THE GUNVOR PUZZLE: HIGH FLIER WITH LINKS TO THE KREMLIN?

Gunvor is the third-largest oil trader on the southern shores of Lake Geneva. From their offices at 14 Quai Général Guisan its employees have a wonderful view of the 'Jet d'eau' (water fountain) near the marina. Gunvor is said to have sold 104 million tonnes of crude oil and oil based products to its major customers BP, Shell and Exxon in 2010. According to the company, revenues totalled 46 billion dollars and its profits 289 million dollars in 2009.[24] Today the company is thought to employ 400 staff, about 100 of them in Geneva. The company was founded in 1997 by the Swede Torbjorn Tornqvist, a former BP trader, whose fortune is estimated to be worth between 1.5 and 2 billion Swiss francs,[25] and the Russian, Gennady Timchenko, who now has Finnish citizenship. Within just a few years Gunvor succeeded in becoming the largest buyer and seller of Russian oil and therefore one of the largest oil traders in the world after Vitol, Glencore and Trafigura.

This meteoric rise occurred following the controversial break-up of Yukos, the mineral oil empire owned by the oligarch, Mikhail Khodorkovsky, at the hands of the Putin government in 2003. It was out of the ruins of Yukos that the Kremlin built the huge state-controlled company, Rosneft. By 2006 Gunvor was to all intents and purposes Rosneft's sales company and Rosneft the second-largest Russian oil producer after Lukoil.[26] Furthermore, Gunvor was said to be a major customer of Gazprom Neft, the sales agency of the Russian state-owned company Gazprom.[27]

The fact that a small trading company in Geneva could mutate into such a giant, selling a substantial part of state-owned Russian energy resources on the global markets, arouses the suspicion that Gunvor enjoys political support. This suspicion is fuelled by the relationship between Timchenko and Vladimir Putin. According to a press report in 2008[28] the two men have known each other since the early 1990s when Putin was still Deputy Mayor of Saint Petersburg. It was at that time that Timchenko took over a refinery 150 kilometres southwest of the former Leningrad. Like Igor Sechin (Chairman of the Rosneft Board of Directors), Alexey Miller (Gazprom's boss) and Dmitry Medvedev (Russian President), Timchenko was a regular visitor to the town hall in the city of Peter the Great. In any event, his relationship with Councillor Putin was close enough to allow them to found a judo club together, whose honorary chairman later became the head of state and finally prime minister. Timchenko's spokesperson does not seek to deny that his boss and Putin "have met occasionally, without necessarily being close friends."[29]

PUTIN RUMOURS AND YUKOS AFTERMATH

Gunvor vehemently contests that the success of its business is based on privileges granted by the Russian state authorities. Timchenko insists publicly that Gunvor is an "efficient" oil trader that owes its growth entirely to perfect service, attractive prices and outstanding reliability.[30] The fact is, however, that the identity of one of Gunvor's owners remains unknown at the time of writing. Besides Timchenko und Tornqvist, who between them own 95 per cent of the group at the time of writing, there is said to be another Gunvor stake belonging to a third shareholder, which in the past was worth up to 12 per cent. This unknown third person is rumoured to be Putin – a rumour which even the highly respected *Financial Times* circulated. A diplomatic dispatch published by WikiLeaks[31] revealed that the US ambassador in Moscow also found the suspicion worth reporting.

Gunvor has consistently denied this, maintaining that "Putin has not, nor has ever, owned anything beneficial or in any way in Gunvor."[32] The fact is: anyone wishing to shed light on the situation as regards the company's ownership encounters a highly opaque, rambling structure of holding companies. Gunvor's Geneva-based subsidiary is a branch of Gunvor International BV, a holding company registered in the Netherlands. This is wholly owned by Clearwater Advisors Corp., headquartered in the British Virgin Islands, via Gunvor Cyprus Holding Ltd. in Cyprus.[33] The Russian newspaper, *Novaya Gazeta,* has tried to find out just who is hiding behind this complex system of cross-shareholdings in front companies registered in Switzerland, Finland, Sweden, France, Luxembourg and on the Virgin Islands and behind Clearwater and the companies linked to it, in which Timchenko, whose fortune was estimated to be worth between 1.9 and 4 billion dollars in 2010,[34] or his wife, also owns shares.[35] Just the fact that the newspaper had published two diagrams, illustrating the extent of this labyrinth, prompted Timchenko's legal advisors to threaten *Novaya Gazeta* with legal proceedings.[36]

BNP Paribas, Geneva – 2011

One reason why Gunvor reacts so aggressively to reports on its relations with Rosneft and the Russian state authorities in general is presumably the legal action initiated against Rosneft, first in Russia, then in the Netherlands, the USA and England, by Yukos Capital. This Luxembourg finance company belonged to the dismantled business empire of Khodorkovsky. Yukos Capital filed a suit in the Manhattan district court in September 2009 claiming that "Gunvor is not simply Rosneft's agent, but functions as a subsidiary of Rosneft."[37] Accordingly, Yukos Capital claimed Gunvor should be included in the list of assets to be confiscated and used in compensation for losses suffered as a result of the dismantling of Yukos. The various proceedings are still in progress at the time of writing.

According to an extract from the company's register, dated 19 January 2011, Rosneft opened its own branch at 65 Rue du Rhône in Geneva.[38] Although the new branch was still just an address with neither staff nor offices in April 2011, it can hardly have been chance that the first official foreign location of the Russian oil giant was right outside Gunvor's front door. Gunvor has consistently pursued a diversification strategy in recent years, aiming to increase its productivity in Russia, to concentrate on operations outside the mineral oil industry and to secure more sources of supply outside the former Soviet Union. Its takeover of 76.9 per cent of Stroytransgaz, the second-largest Russian pipeline and plant construction firm, enabled Gunvor to buy more oil and natural gas concessions in Russia. In addition, Gunvor was able to acquire some of the largest coal reserves in Siberia. In one of his rare interviews Timchenko said in 2009 that, from then on, half of his oil would come from outside Russia's sphere of influence, especially from Indonesia, Algeria, Thailand and Ecuador.[39]

LITASCO: LUKOIL'S SALES ARM

Gunvor cannot swallow all the Russian oil on its own: in its wake come other traders selling considerable quantities of the black gold from the former Soviet Union via Geneva. First is the Lukoil International Trading and Supply Company (Litasco), a wholly-owned subsidiary of Lukoil, Russia's largest privately held crude-oil producer. Litasco sells most of Lukoil's products out of 9 Rue du Conseil-Général, Geneva, where it has had its headquarters since the year 2000. Gati Al-Jebouri, half Bulgarian, half Iraqi, was Litasco's boss from 2006 until 2010 when he was put in charge of Lukoil's oilfields in Iraq. According to Al-Jebouri, Litasco generated revenues totalling 67.5 billion dollars and profits of 227 million dollars in 2008.[40] In 2009 the Geneva-based trading company employed 415 staff, 206 of them in Geneva.[41] It is impossible to find out much more about Litasco via official channels. The company is rated number 2 after Total on the French oil market and supplies all the petrol stations owned by Lukoil in the USA according to its 2007 annual report. In addition, Litasco owns Eiger Shipping, a shipping company based in Geneva. Its former boss, Valery Golovushkin, is now President and Chief Executive of Socar Trading in Geneva. The business has excellent connections with the clan of the Azerbaijani president, Ilham Aliev, and sells the crude oil from state-owned producers in that country.

MERCURIA: GENEVA TRADE MESSENGER BETWEEN RUSSIA AND CHINA

Mercuria is the third Geneva-based company that lives off the West's appetite for Russian crude oil. Founded in 2004, the company is the Swiss trading arm of the J&S Group, which was operated by two immigrant Polish traders from 1993 onwards. The company has its headquarters in Larnaca, Cyprus, and first supplied Germany and Central Europe with Russian and Belarusian crude oil processed in two Polish refineries.[42] Later the J&S Group transferred its business to Mercuria, whose shareholders they then remained. The operative management of Mercuria is in the hands of Marco Dunand and Daniel Jaeggi, who split 30 per cent of the shares between them. Together with Glencore manager Christian Wolfensberger, they are among the few Swiss nationals who are top managers in the commodity business. The other employees own the remaining Mercuria shares – common practice in the industry.[43]

Mercuria's rise was even faster than that of Gunvor, so fast in fact that even Dunand seems "surprised"[44] at the firm's success. In just six years revenues shot up from six billion dollars (2004) to 50 billion dollars (2010). After trading for only five years, by the end of 2009 the company was the fifth-largest oil trader in the world, selling 90 million tonnes of crude oil and oil products in 2009. Mercuria has 25 offices all over the world and in March 2011 employed 850 staff (200 of them in Geneva).[45] In 2009 the company showed a profit of 454 million dollars and in 2011 confirmed that the taxes on its profits were 70 million dollars a year on average, the equivalent of a tax rate of around 15 per cent.[46]

Like Gunvor, Mercuria also started by selling Russian crude oil, which is said to have accounted for 40 per cent of its supplies in 2008.[47] And like Gunvor, Mercuria is also seeking to increase its product range by means of acquisitions in Nigeria, Canada, Kazakhstan and the Middle East. Further diversification involves the natural gas, coal and biodiesel industries. However, the enormous success of the trading messenger (Mercury = Roman messenger of the gods) is no doubt related to its ever-increasing deliveries to the huge Chinese market.[48] In addition, Mercuria is intensively involved in trading futures contracts, also known as 'paper barrels' CHAP.13. According to Dunand this virtual business accounted for about half of Mercuria's operations in 2007 when oil prices shot up astronomically.[49] Whether such a huge volume was merely intended as security or whether the company was indulging in speculation, remains open to suspicion, a suspicion refuted by Dunand's partner Jaeggi who states that their job was not to speculate, not even to have an opinion about price developments in the future. Functioning derivatives markets

Rosneft, Geneva – 2011

and futures are required as security and not as investment tools, according to Jaeggi.[50]

STRATEGIC CLUSTER OR PLAIN NEPOTISM?

Karl Marx referred to the proletariat “in itself” and the proletariat “for itself”, distinguishing between the objective existence of the proletariat and its subjective class consciousness. Similarly, there is no doubt about the existence of the Swiss commodity industry “in itself”. Yet is this at the same time “for itself”? Does it act collectively to pursue its own interests? Not surprisingly, the organisations that provide an answer to this question are to be found in Geneva.

‘Post tenebras lux’ (from darkness to light) is the official seal of the Republic and Canton of Geneva. In fact, since 2006 the major commodity players based in Geneva have demonstrated increased, albeit in homeopathic doses, transparency by means of the Geneva Trading and Shipping Association. Along with a similar organisation in the canton of Ticino, the Lugano Commodity Trading Association (LCTA), the GTSA is the only organisation throughout Switzerland which represents the commodity industry to the outside world. Its members are from the following sectors: trade, finance, logistics, product testing and related services. There is, of course, no official list of members. Older organisations such as the Propeller Club of the maritime logistics companies or the Geneva Petroleum Club have become more insignificant. Informal networks are much more important than formal ones: younger traders meet at the Geneva Club once a month, a sports bar where the trading companies take turns to sponsor the evenings and their employees regale one another with entertaining anecdotes about their day-to-day working lives according to Tom Cutler, a Geneva-based freight specialist. He says the senior traders prefer to spend their free time with their families in their luxury homes on the lakeside.

Minimal though it is, even the transparency of the GTSA is continually at odds with the notorious discretion of the industry, making lobbying, the actual aim of the organisation, much more difficult. Therefore GTSA General Secretary Geert Descheemaeker squirmed a little when he stated, "By the nature of our business, trading and shipping companies have little need to be known to the public at large. However, like any other Geneva residents, we do need representation. We have created GTSA because we feel it natural that a sector this important to Geneva (and to Switzerland as a whole) should be recognized and should have a voice to explain its point of view and concerns."[51]

Descheemaeker's rhetorical balancing act (between 'no need to be known' and 'a sector this important (…) should be recoginzed' is also reflected in the internal bulletins of the GTSA. Apparently, when a study was undertaken in 2009 in order to make government representatives fully aware of the importance of the industry to the Swiss economy, the GTSA found it extremely difficult to extract the necessary information from its members. In some desperation the organisation wrote, "Unfortunately, while your participation is primordial for the feasibility of the study, the response *rate is still poor.* GTSA guarantees that all individual data will be kept strictly confidential. *We really count on your participation.*"[52] When an enquiry was made to the GTSA office, an employee was utterly amazed that anyone outside the association was even aware of its existence. It was merely a matter of hours before the GTSA bulletin in question disappeared from the website of a law firm where it had earlier appeared. The industry lobby uses the newsletter to provide its paying members with useful and important information from the world of trade. For example, the aforementioned law firm reported on the threat of prosecution against Total in France due to the oil spill from its tanker Erika, in which it posed the anxious question, "Could legal entities be subject to criminal sanctions in Switzerland as well?"

SYMBOLIC IMAGE POLISHING BY MEANS OF A UNIVERSITY COURSE …

Since 2008 the lobby's work has included an MA course at the University of Geneva in which the GTSA is involved. The students must first be accepted by the university and then recruited by one of the participating companies. Naturally, the list of the companies involved is confidential. Interest in this programme among students is limited, but their potential new employers are backing out anyway. Although there was a respectable number of applicants, 250, in the second academic year (2009), only 48 were accepted and of these only 18 were actually recruited and therefore awarded a place. Once again the GTSA was forced to appeal to its members, who believe in internal training, "We really count on your participation to keep this programme going. We need to have at least 20 students next year if we want to be sure to maintain this programme. Geneva being such a trading hub, it would be a shame to loose the opportunity to academically train motivated local talent."[53]

The timing of the GTSA's birth was not just a matter of chance. In October 2005 the Volcker report on the Oil for Food scandal was published CHAP. 15.4, in which various Geneva-based champions of the industry were heavily involved. The GTSA birth also came soon after the EU Commission for Economic and Financial Affairs had launched its first salvo against the cantonal tax regimes that secure tax concessions for the commodity companies. Since then the GTSA has grown steadily from 27 members in the autumn of 2006 to more than 60 in just four years. Various observers in Geneva have however since come to the conclusion that the main aim of the GTSA is to monitor the commodity financing business and protect the market position of BNP Paribas. It was therefore anything but chance that most of the GTSA's publications were prepared by BNP Paribas staff – after all, the GTSA President is a manager at BNP. His name is Jacques-Olivier Thomann and he does not respond to written enquiries.

Vitol, Geneva – 2011

… AND VIGOROUS LOBBYING NATIONWIDE AND IN THE CANTONS

One of the more subtle games the GTSA plays to represent its members interests is by publishing industry statistics and strategically releasing information as ways of stressing the importance of the commodity business to Geneva and Switzerland. Another is by being seen to be promoting talented young people. However, the members' association can get tough too if necessary. For example, a statement from the GTSA Bulletin comments that, "Following the recent attacks from the EU on the auxiliary status of trading companies, the Bureau of GTSA has been received by Mr. Pierre-François Unger, State Councillor in charge of the Department of Regional Affairs, Economy and Health (DARES) and Mr. David Hiler, State Councillor in charge of the Department of Finance to express the concerns of our members. At this meeting it became clear that the Authorities are well aware of the economical importance of our sector and of its contribution to the GDP. They also well understand the importance of a stable fiscal regime. The Geneva cantonal authorities are closely coordinating with Berne and other cantons and in particular Vaud to express a common standpoint vis a vis the EU."[54] This example of lobbying, in which above all the 'mobile nature' of the commodity business was stressed, bore political fruit. A few months later Geneva's Green (!) Minister of Finance, David Hiler, stated that the Geneva authorities were determined to ensure that the various foreign companies stayed in Geneva and would undertake measures necessary for this, in particular adjusting the cantonal taxes within the framework of negotiations between Switzerland and the EU.[55]

In Berne too the GTSA has got its foot in the crucial door: "GTSA has a very good relationship with the Federal Minister of Economy, who regularly participates in our meetings and consults GTSA on the situation of Swiss-based traders. The Association, with the help of experts from our member companies, is working with the SECO [State Secretariat for Economic Affairs] towards eliminating possible trade barriers that affect the activities of Swiss traders."[56] Not only were the

Gunvor, Geneva – 2011

Geneva State Councillor, Pierre-François Unger, and the Mayor, Rémy Pagani, present at the annual Commodity Dinner in 2009, but also former SECO Secretary of State, Jean-Daniel Gerber. In the summer of 2007 the entire Swiss Federal Council, led by the former Geneva Finance Minister, Micheline Calmy-Rey, visited Mercuria during its 'office outing' and toured its premises. "We thank the Swiss government," wrote the Mercuria owners in a press release about the visit, "for creating and preserving an economic, political and legal environment which allows companies like ours to develop and contribute to the common good." Even the Federal Department of Finance lobbies for the commodity business: In March 2011 Switzerland and the GTSA sought to organise a joint workshop for the G20 and invite the private sector to take part. The subject: The risks of "counterproductive or disruptive regulation." The background: The efforts of the G20 to curb speculation in commodities, especially in foodstuffs.

Thanks to WikiLeaks we now know that even Swiss diplomats are working to further the interests of the commodity companies. In 2005 the Swiss ambassador to Peru took part in a meeting of high-ranking embassy staff and foreign mining companies that sought to address the issue of local opposition to mining projects. A manager of the Antamina mine, (in which Xstrata acquired a third a year later) had demanded that the diplomats intervene at the Ministry of Education to support the relocation of local teaching staff critical of the mining industry. In addition, he was to persuade the Catholic Church to remove hostile bishops. It was decided that a core group, made up of diplomats from the USA, Canada, Great Britain, South Africa and Switzerland, would have talks with the Peruvian government, the church and the party leaders.[57]

INTERIM CONCLUSION

During the last ten years the influx and founding of many opaque companies functioning primarily as sellers of oil and gas from the former Soviet Union have enabled the equally dynamic and discreet development of the commodity trading centre Geneva into the global oil Mecca. Besides the typical advantages of the Swiss location, the key factors behind this were the long-standing close relationships, formed in the 1980s between middlemen located in the cosmopolitan city on the shores of Lake Geneva and Soviet oil producers.

The close ties between former ex-Soviet oil billions and those who wielded political power there ensured that the trading companies in Geneva, whose primary role was to deal in Russian oil, developed into some of the most opaque, secretive representatives of Swiss commerce. This meteoric rise of companies that were still completely unheard of ten years ago and the feverish founding of similar firms at the time demonstrates that not only prices are highly volatile in the commodity business. The unpredictability of markets explains the current clear trend towards diversification which is observable in the oil Mecca Geneva.

A symptom of the increased importance of the oil traders within this sector and their growing need for political representation of their interests is the GTSA. The main function of the Geneva lobby organisation is to protect the cantonal and federal privileges enjoyed by the industry, for example in tax affairs. The announcement of the Geneva tax reform with its continuing favourable tariffs for the traders illustrates just how successful the GTSA has been.

AGRICULTURAL TRADE //

Export bans for wheat during or after devastating periods of drought usually lead to huge increases in global prices. A situation from which the commodity giants know how to profit, and starving populations are left to pick up the bill.

12 //

SOFT COMMODITIES: THE BLOOMING AFTER-HARVEST BUSINESS

Towards the end of the summer of 1850, the 17-year old Léopold Louis-Dreyfus drove a cartload of wheat from the family farm in Alsace over the border and sold it in Basel. The very next year he bought wheat from neighbouring farms and again made the twelve-mile journey to the trading centre at the Rheinknie, where the borders of Switzerland, France and Germany meet. He was one of the first people to notice that in the Swiss Central Plateau grain farming was being replaced by livestock and dairy farming. He further predicted that with the emerging railway network, Switzerland would become increasingly dependent on grain imports, given that the price of grain from Eastern Europe, Russia and later the USA was far lower than the price in Switzerland.

Dreyfus' grain trade flourished: only a few years after his first cross-border grain transactions he moved his activities to the more internationally oriented market in Berne. He began to buy corn from Hungary, Romania and other East European countries to satisfy the rapidly rising demand in the industrial centres of Western Europe. Since his native Alsace was ceded to Germany after the Franco-Prussian War, Dreyfus left Switzerland in 1875 and moved his business to Paris. There he laid the foundations of a company that is today one of the world's leading traders in agricultural commodities. Paris remains the location of the Louis Dreyfus Group's headquarters, although the company, now operating globally, has again been using Switzerland as its trading centre since 2006.

Much has happened at Dreyfus since the firm's beginnings. It is still one of the leaders in the grain trade and is currently the world's number one for rice. Today, the French family business has developed into a highly diversified company that operates all along the supply chain. The Dreyfus Group is a market leader in the cocoa, coffee, cotton, sugar and oilseed trades. It also trades in freight capacities, owns silos and port facilities and has started to process agricultural products on a large scale. Louis Dreyfus is a major producer of orange juice and owns its own orange plantations in Brazil. Furthermore, today's company trades not only in agricultural commodities but also in metals, electricity and financial products, as well as operating in the oil and natural gas business. This expansion of its range of commodities and penetration into upstream and downstream areas is a trend that can also be observed in other traditional agricultural traders who, like Louis Dreyfus, conduct the majority of their trading operations out of Switzerland.

ABCD: A 'GANG OF FOUR' TURNS SWITZERLAND INTO A GLOBAL AGRICULTURAL TRADING CENTRE

In the trade in agricultural commodities, a leading quartet comprising Louis Dreyfus and three other companies sets the tone globally. Often referred to as the exclusive ABCD club, this 'Gang of Four' is made up of Archer Daniels Midland, Bunge, Cargill and Dreyfus. Whereas Archer Daniels Midland – ADM for short – and Bunge are listed on the stock exchange, Cargill and Louis Dreyfus are still largely family-owned. Together, the four trading giants generated revenues of around 290 billion dollars in 2010 and, with more than 100 billion dollars, Cargill is the undisputed first among equals TAB. 1. According to the Boston Consulting Group, the four companies controlled about three-quarters of the global grain and oilseed trade in 2003.[1] More recent figures are not available, but there is no doubt that the 'Gang of Four' continues to dominate the trade in agricultural commodities. This can be deduced from the fact that Switzerland remains the world's most important trading hub for grain and oilseeds and the number one in Europe for sugar and cotton.

A AS IN ARCHER DANIELS MIDLAND | The two main divisions of the US agricultural giant, agricultural services (especially trading) and agricultural commodity processing, each contributed 46 per cent to its revenues in 2010. ADM has over 330 grain silos and can rely on an extensive transport network of ocean-going vessels, barges and semi-trailers, and also around 25,000 railway wagons. With 240 of its own facilities, the company is also one of the largest processors of soya beans, corn, wheat and cocoa in the world. It manufactures animal foodstuffs, industrial products and agrofuels on a large scale, as well as precursors for the food industry. ADM has established its European office in Rolle in the canton of Vaud, Switzerland. From its base on the shores of Lake Geneva ADM's subsidiary, ADM International Sàrl, manages 44 businesses in ten countries. However, the Swiss branch mainly operates as a trading centre and is responsible for financing and marketing.

TAB. 1

ABCD CLUB PROFILE

	Revenues 2010 (billion dollars)	Profit 2010 (billion dollars)	Employees		Traded products		Operates in (number of countries
			Total	Switzerland	Agricultural products	other	
ADM	61.7	1.93	29,000	160	Grains Oilseeds Corn Cocoa	Ethanol Biodiesel	60
Bunge	45.7	2.35	25,000	250[2]	Grains Oilseeds Corn Sugar	Fertilisers Ethanol Emissions certificates	30
Cargill	107.9	2.60	131,000	900	Grains Oilseeds Corn Sugar Cotton Cocoa	Electricity Oil Natural gas Coal Emissions certificates Freight capacities	66
Dreyfus	74.3	1.21	34,000	250[2]	Grains Oilseeds Corn Citrus fruits Cotton Coffee Cocoa Sugar	Ethanol Metals Freight capacities Electricity	53

Source: annual reports; company websites

B AS IN BUNGE | The soya trade in Brazil, where the company is the leading processor of leguminous vegetables, is as important to Bunge as the U.S. corn trade is to ADM. Founded in Amsterdam in 1818 and listed on the New York Stock Exchange, the company started to trade in sugar as well in 2006 and nowadays processes large quantities of sugar cane into ethanol. Bunge's logistics network includes both global transport and storage capacities and entire port facilities in North and South America, Russia and Vietnam. After its profits fell by two-thirds in 2009, Bunge sold its fertiliser business in Brazil, including a phosphate mine, for 3.8 billion dollars to the Brazilian mining company Vale.

Bunge's European business, which contributes 30 per cent of the company's revenues, is managed from its base on the shores of Lake Geneva.[3] As with ADM, its global trading centre is located in Switzerland. Bunge SA is a wholly-owned subsidiary of the Koninklijke Bunge BV in Rotterdam, which in turn belongs to the parent company, Bunge Ltd. Moreover, the Swiss Bunge SA also has a subsidiary, Oleina SA, which is involved in the wholesale trade in edible oils and fats in Russia and the former Soviet republics. Two more Bunge companies are located at the same address in Geneva, Ecoinvest Carbon SA and the Emissions Holdings Sàrl. Both are involved in a more abstract, less palatable type of trade, namely dealing in CO_2 emissions certificates.

C AS IN CARGILL | Cargill is the private corporation with the highest revenues in the USA. But revenues are not the only area in which this company deals in superlatives: it is the largest agricultural trader, largest grain merchant, largest cocoa merchant and second-largest cotton merchant in the world. Its operations range from production and processing to sales to the food industry, but the cornerstone of the activities of the company that is 90 per cent owned by both the Cargill and MacMillan families is trading.

When Cargill pitched its tent in Geneva in 1956, the company concentrated initially on importing grain and oilseeds from North America into Europe. Now, more than half a century later, Cargill International SA is one of the ten largest companies in Switzerland and in 2009 generated even more revenues than the Swiss retailer with the largest sales volume, Migros.[4] After trading in grains and oilseeds, the Geneva branch moved into the sugar business and it now moves over eight million tonnes of sugar a year. This equals 20 per cent of the global trade volume. According to the Geneva Trading and Shipping Association (GTSA) as much as half of the global sugar trade passes through companies in Switzerland.

However, the 900 Cargill employees in Geneva also trade in freight capacities, oil products, coal, electricity and CO_2 emissions certificates. Its takeover of both Provimi Kliba, a milling industry specialist and animal feed producer, and Zurich-based grain processor Blattmann has enabled Cargill to penetrate higher value-added segments in Switzerland. Blattmann processes agricultural raw materials into glucose syrup, maltodextrin, polyols, hydrocolloids and modified starch, and also manufactures pharmaceutical products.

D AS IN DREYFUS | Today 51 per cent of the Louis Dreyfus Group belongs to the wife and children of the founder, Robert Louis-Dreyfus, who died in 2009; the remaining 49 per cent is held by other members of the Dreyfus family. In 2009 the company made a net profit of 550 million dollars in the commodity sector, the second highest result in its history. The decisive factor contributing towards this spectacular result was the rise in commodity prices.[5]

By diversifying and expanding into production and processing in line with the general trend in the sector, Louis Dreyfus is likewise attempting to counteract margin erosion in trading. However, this strategy requires a great deal of capital. The company will need yet more disposable funds from 2012 onwards when the remaining relatives will be able to demand payment of their shares from the widow and children of the deceased owner. This brings a merger with another giant already listed on the stock exchange closer although negotiations with Olam International (domiciled in Singapore) broke down early in 2011. The merger of the two competitors would have created the world's third-largest agricultural commodity trader after Cargill and ADM. Apparently the principal shareholder, Margarita Louis-Dreyfus, was against the merger. It appears the family members disagree on the future of the media-shy, 160-year old trading company,[6] which has not even had a press office up to now.

The Louis Dreyfus Group has an incredibly complex and opaque company structure, comprising just fewer than 70 subsidiaries all over the world. In addition, there are a further 50 subsidiaries in the American tax haven, Delaware, which do not appear in the annual reports. A glance into the tangled web of the company's network offers this (admittedly incomplete) picture: the parent company is the Louis Dreyfus SAS in Paris. The umbrella holding company is Louis Dreyfus Holding BV in Amsterdam. However, the parent company is not only owned by a Dutch holding company, but also owns its own Dutch holding company: Louis Dreyfus Holding Netherlands BV. The company may not have any employees, but it does have several subsidiaries, including Louis Dreyfus Energy Holding Suisse SA and Louis Dreyfus Commodities Holding BV. The latter is part of Louis Dreyfus Commodities BV in Rotterdam, which is in fact the parent company of six Swiss subsidiaries: Louis Dreyfus Commodities (LDC) Services Suisse SA, LDC Finance Suisse SA, LDC Freight Suisse SA, LDC IT Services Suisse SA, LDC Metals Suisse SA and LDC Suisse SA, a trader in agricultural commodities. All these companies operate out of the Swissair Centre near Geneva Airport. This address is also the home of the wholly-owned subsidiary of Louis Dreyfus Négoce SAS, Sungrain Holding SA, which has a capital of 65 million Swiss francs and just a single employee. The Louis Dreyfus SAS (note the difference) owns Louis Dreyfus Finanz AG based in Zurich, whose purpose, according to the companies register, is to 'carry out all types of financial transactions'. Moreover, the Swiss branch of London-based Louis Dreyfus Trading Limited has also rented an office at the Geneva Swissair Centre, which deals with all and sundry apart from Switzerland, a clue that it is purely a shell company.[7]

Dreyfus has made Geneva the centre of its trade in cotton, rice, grains, oilseeds and sugar. It is from here that the leading rice trading company ships its goods to the growing markets in West Africa. Millions of tonnes of grains and oilseeds are transported from North and South America and the region surrounding the Black Sea to Europe every year.[8] The French family business also conducts its energy business out of Switzerland. For example, Louis Dreyfus Energy Services LP (limited partnership), domiciled in Delaware, trades in natural gas and electricity in France, Germany and England via its branch in Lausanne. Even its international shipping business – for both internal and external use – is conducted via landlocked Switzerland.

E AS IN 'EIDGENOSSEN' (I.E. THE SWISS PEOPLE) | Be they traders in cocoa, coffee or grain, all the traditional Swiss trading companies had disappeared by the turn of the century, at least as independent companies. The one exception is the cotton trader Paul Reinhart AG CHAP. 4. Based in Winterthur the company is now managed by Thomas Paul and Paul Jürg Reinhart from the seventh generation of the family. They and their 60 employees generated revenues of 800 million Swiss francs in 2008.[9]

Turbulence on the cotton derivatives exchange prompted prices to rocket in spring 2008. This caused shortfalls in liquidity for traders like Reinhart, who were hedging their positions on the stock exchange. Consequently, the Swiss company was finally forced to declare its US and Australian subsidiaries bankrupt. Nonetheless, according to the International Cotton Advisory Committee, Paul Reinhart AG remains one of the top ten global traders of raw cotton thanks to an annual sales volume of over 200,000 tons.[10]

Nowadays, however, the sophisticated city of Geneva has totally eclipsed provincial Winterthur as the Swiss trading centre for the 'white gold'. The Trade Finance Corporation estimates that at present 20 per cent of global volume is handled in the region around Lake Geneva where not only the businesses of the world's three largest cotton traders, Louis Dreyfus, Cargill and Olam, are located but also those of other heavyweights such as ECOM Agroindustrial and Noble. Even Glencore has entered the flourishing trade in this natural fibre, and

2010 poached a trading team from Noble in the process.[11] Although agricultural commodities are merely a footnote in the portfolio of Zug-based Glencore, the company trades in grains and edible oils and fats, as well as owning farmland in Australia, Paraguay, Russia, Ukraine and Kazakhstan CHAP. 7. As is generally the case with commodity trading, good connections apparently do no harm here either.

FAT PROFITS FROM SPECULATING AT THE EXPENSE OF STARVING PEOPLE

In the summer of 2010 when Russia feared huge losses as a result of a devastating drought, the government issued a ban on exports upon which global wheat prices shot up by 15 per cent within two days – a disaster for hundreds of millions of people who were not earning enough to feed themselves and their families even before the price skyrocketed.

According to the English-language financial press, the managers of the Russian Glencore subsidiary, International Grain, had pressured the Kremlin to ban exports. The company's headquarters in Baar emphatically denied a tip-off to this effect from one of the employees of Glencore.[12] What sounded fairly unconvincing even then became downright unbelievable following the latest information from the banks that were preparing Glencore's initial public offering. According to this information, the commodity giant is supposed to have speculated on rising wheat prices that same early summer in 2010.[13]

It seems the Russian export ban and resulting price rises had indeed poured handsome profits into Glencore's tills as planned: its profits in the agricultural sector more than doubled 2010. It was the starving populations in the southern hemisphere who were left to pick up the bill though. For example, as the world's largest wheat importer, Egypt was paying 184 dollars per tonne at the start of July 2010. Merely a month later, following the export ban, the price had risen by more than 100 dollars.[14]

That Geneva is also the measure of all things in the grain trade is demonstrated by Global Grain, the annual conference which takes place there each year and to which about 1,000 traders made the pilgrimage in 2010. James Dunsterville of the Global Commodities Group, former grain trader and organiser of the important commodity conference, regards Geneva's tax model as its crucial advantage: "If a trading company in Argentina has to pay 30 per cent corporation tax, it will be inclined to relocate its headquarters to Geneva. Although the company will continue to export the wheat out of Buenos Aires to Cape Town for example, its profits will be worth far more in Geneva, thanks in part to single-figure tax rates." According to GTSA estimates, 35 per cent of the world's grain and oilseeds are traded through the hub on the shores of Lake Geneva. This amounts to around 75 million tonnes, the equivalent of three-quarters of Europe and the CIS' volume of trade.[15] The main explanation for the dominance of this location lies in the trading departments of the ABCD companies.

"THESE COMPANIES HAVE GONE INTO CRIMINALITY."

"These companies" refers to the four grain trading companies ADM, Bunge, Cargill and Dreyfus and the charge was levelled by someone who should know; namely, Ricardo Echegaray, the head of Argentina's revenue and customs service. The Argentinean authorities provisionally struck the 'ABCD club' off the national export register, accusing all four companies of large-scale tax evasion in relation to their trade in Argentinean grain. The talk is of several hundred million dollars and is based on Echegaray's extensive investigations. At the end of May 2011 the tax investigator accused the grain traders of having submitted false sales figures, reduced their taxable income by means of inflated costs, and then shifted profits into tax havens. In Cargill's case, Swiss subsidiaries were also said to have been used. Although those accused strongly deny any wrongdoing. Echegaray insists he has evidence to prove criminal activities on the part of the Gang of Four.[16]

Another major Swiss trader is Ameropa, which operates out of Binningen in the Canton of Basel Land (BL), Switzerland. Privately owned and publicity shy, the company owns a cobalt mine in the Congo and trades not only in fertilisers, metals and petrochemicals, but also moves about three million tonnes of grain a year. Designed by Herzog & de Meuron its Binningen headquarters were inaugurated in 2001. The highly transparent building – an aesthetic contrast to Ameropa's opaque business policy – has since become a place of pilgrimage for students of architecture.

IS SWITZERLAND A 'BEAN' REPUBLIC? HOT COFFEE AND COOL COCOA

The traditional Winterthur company Volcafe, is no longer Swiss owned and has become more transparent in return. However, its new owners, the English ED&F Man, continue to operate their coffee business out of Winterthur. When they merged Volcafe with their own coffee business in 2004, they created the world's largest green-coffee trader with revenues of 1.5 billion Swiss francs according to the Swiss Press Agency SDA. Today, Volcafe's estimated sales of about 12 million bags, each weighing 60 kilograms, put the company into second place just below the Neumann Group in Hamburg, which also trades in Switzerland via its Swiss branch, Bernhard Rothfos Intercafé.[17]

An estimated 75 per cent of the 100 million bags of green coffee that are traded worldwide are handled via Switzerland.[18] Traders from Sucafina, a company which specialises in the coffee trade and is located in Geneva, sell about 3 million bags of coffee a year. ECOM Agroindustrial Corporation Limited, located next door in Pully (Canton Vaud), sells close to 10 million bags yearly.[19] One can only imagine that the representatives from these companies and their counterparts, the purchasing managers of companies such as Nestlé, Starbucks, United Coffee and Kraft Foods, enjoyed the 1st Swiss Coffee Dinner and Dance held in 2010. Where? In Geneva, of course.

The Swiss marketplace remains as important as ever for the global cocoa trade too. Although the Zurich-based Barry Callebaut has only existed in its present form since the mid 1990s, it still processes an impressive 15 per cent of global cocoa production. It procures the coveted beans mainly for the internal production of intermediate products for the food industry. Just as vertically integrated, Cargill and ADM, the two other giants in the cocoa business, are still regarded as classic trading companies.[20] Launching into processing is held to be a way of making up for the shrinking trading margins in the cocoa business. Today, very few firms, such as ED&F Man, confine their activities to trading only.[21]

EXPANSION THE ASIAN WAY: OIL PLATFORMS AS PART OF THE PROGRAMME

The Noble Group in Hong Kong moved its coffee and cocoa trading business to Lausanne, Switzerland, as far back as ten years ago. Its revenues of 56.7 billion dollars make the group one of the top-grossing Asian commodity traders. The company covers the entire supply chain, from production to delivery, and has long traded in more than just agricultural commodities. Noble has invested heavily in holdings and takeovers and has spent 3.4 billion dollars since the turn of the century, adding around 30 assets to its portfolio.[22] Vertical integration has enabled the trading giant to extract added value at every level. In addition, the company continues to expand its product range and is often compared to Glencore as a result. Not surprisingly, there is now a branch in Lugano, Switzerland, trading in precious metals in addition to Noble Resources SA in Lausanne. The company owns yet another Swiss subsidiary that handles the charter business as well as several more companies, all located in Baar, which purchase and operate oil platforms. Incidentally, located just around the corner is Transocean, which became famous throughout the world after the oil disaster in the Gulf of Mexico in the spring of 2011 when BP filed a claim against it for 40 billion dollars as compensation for its damaged Deepwater Horizon platform.

The leading Japanese trading corporation, Mitsui & Co. Ltd, pursues a similarly aggressive strategy to that of Noble, owning over 700 subsidiaries, including some based in Switzerland. For example, having acquired a minority interest in the Zug-based grain trading company Multigrain AG in 2007, Mitsui then proceeded to take over the latter gradually during the following years. This move has enabled Mitsui to strengthen its position in Brazil since its Swiss subsidiary also owns the Brazilian Multigrain SA which trades and processes soya beans, cotton and corn, and also imports wheat into Brazil. Yet another subsidiary of the Zug-based branch of Mitsui is Xingu AG. This company owns 100,000 hectares of arable land in Brazil, which is the equivalent of more than a third of the total arable land in Switzerland. The land is used to cultivate not only soya, cotton and corn but also sugarcane for producing ethanol. The declared aim of the Japanese trading giant's latest Brazilian venture is not to enter into the business of agricultural production for its own sake, but to secure constant supplies for its activities along the whole of the supply chain.

INTERIM CONCLUSION

The traditional Swiss traders in agricultural commodities have either disappeared or been taken over by foreign companies. Modern communication technologies and the increased importance of electronic trading have caused trading margins to shrink continuously, with the result that the business model of pure trading companies now appears out-dated. In addition, the focus on trading only one or just a few agricultural products entails too great a concentration of risk in times of highly volatile markets.

The world's dominant agricultural companies, above all the ABCD 'Gang of Four', have moved their trading departments to the shores of Lake Zug or Lake Geneva. In this way they have made Switzerland the pivotal international trading hub for agricultural commodities. Advantageous conditions, including the presence of the major customers for coffee and cocoa, have acted like a magnet for trading companies and continue to do so to this day.

As with other commodities, there is also a noticeable trend towards merging previously separate functions in the manufacture of agricultural products. Trading companies are expanding into both producing and processing stems, beans and grains in order to add value at every stage. With traditional smallholder crops, such as coffee and cocoa, trading houses tend to eliminate the middlemen without entering directly into production themselves. With other agricultural goods, however, the trend is clearly towards the in-house production of agricultural raw materials and the associated acquisition of land by trading companies.

The cards have been dealt – the global poker game began a long time ago.

SPECULATION //

"We are industrialists, who make use of geographical, technical and temporal advantages that always exist in the physical markets," says Trafigura's Finance Director. This is at best a partial truth – the difference between financial and trading operators in the commodity business has long since become blurred.

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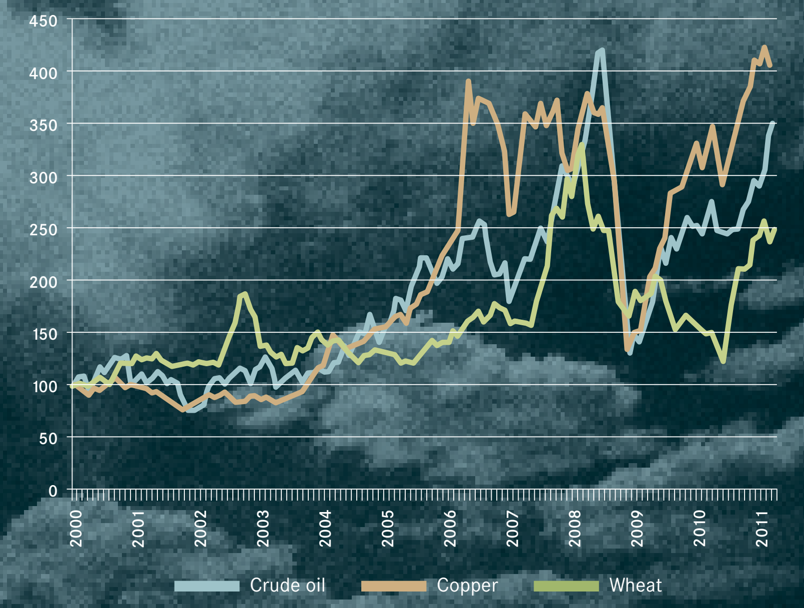
THE OTHER CASINO: HIGH-RISK SPECULATION

Since the start of the millennium, commodity prices in world markets have been highly volatile, i.e. they have undergone strong fluctuations. From June 2003 to June 2008, for example, the prices for oil and copper at a constant dollar exchange rate rose by factors of 3.8 and 4 respectively, and for wheat by a factor of 2.3. In the second half of 2008, prices fell massively. The same barrel of crude oil that cost 146 dollars in June 2008 could be bought for 40 dollars six months later. The next boom followed as early as 2009 FIG. 1. This enormous volatility of commodity prices presents great problems for both producers and consumers. For developing and emerging countries in particular, it has devastating consequences. For example, following merciless rises in the cost of staple foodstuffs, food riots broke out in 2007 and 2008 in Haiti, Cameroon and Egypt, as well as relatively economically advanced countries such as Mexico.[1]

FIG. 1

INDEXED MONTHLY PRICE MOVEMENT 2000 TO 2011*



*Base 100 = January 2000

Source: International Monetary Fund (IMF)

‘UNDERLYING’ VS. ‘FUNDAMENTALS’: WHO OR WHAT MAKES THE PRICES?

Such dramatic consequences of strongly fluctuating commodity prices led to a heated public debate about the mechanisms of price formation in that sector, and about the specific role of financial speculation. As mentioned in CHAP. 4, market operators attempt to protect themselves against price fluctuations through the use of future-dated contracts (‘Futures’), a process known as ‘hedging’. The resulting contracts can in turn also be traded. In fact, most transactions in the commodity markets take place in this virtual paper form, and fewer involve real, existing goods. In the case of oil, for example, it is estimated that the futures market is ten to fifteen times the size of the spot market.[2]

In the last 20 years, the commodity futures markets have changed profoundly. Through the deregulation and liberalisation of financial markets, they were gradually opened up to pension funds, hedge funds, investment banks and life insurance companies.[3] Increasingly, futures are no longer dominated by traditional operators such as the commodity traders who want to protect themselves against price fluctuations through 'hedging', but by speculators whose only aim is to try to maximise profits from this 'paper trade'. It was estimated that in 2008 less than one third of those involved in the futures market for foodstuffs were genuine traders in these commodities. In 1998 it had been 80 per cent.[4] The number of different commodity-based derivative securities has also increased and their trade outside the stock exchanges is commonplace. According to estimates by the Bank for International Settlements (BIS), the value of commodity derivatives contracts changing hands in this particularly non-transparent manner (OTC – 'over the counter') increased 14-fold globally from the end of the 1990s to June 2008, before dropping again as a result of the financial crisis.[5]

Opinions differ widely with regard to how these changes will affect the commodity futures market and commodity prices. For some, there is a close link between the price development of a derivative (for example, a wheat futures contract) and the 'underlying' (in this case, the price of wheat). Seen in this way, the cause of the price increase from 2003 to 2008 would be traceable back to the growing financial speculation with commodity futures contracts. For others, the prices in this sector, as in others, are still determined by developments in the real world ('Fundamentals') that influence supply and demand. With this in mind, the price boom would be mainly attributed to the global economic situation and especially to the massive increase in the consumption of commodities by emerging economies such as China. In the case of foodstuffs, therefore, the reasons would lie in the use of cereals for the production of agrofuels, and in production-related uncertainties (weather, crop quality and so on).[6] The UN Special Rapporteur on the Right to Food, Olivier de Schutter, notes that "speculation is not the main reason for rising or falling prices", but that it contributes to price volatility through the "destabilisation of markets", and he urges regulation in this regard.[7] And it seems that people are listening to him and to other critical voices. In any case, in the wake of the financial and economic crisis of 2008 in Europe and in the United States, various draft bills are being discussed, all aimed at better supervision of financial transactions in the commodity sector.

HEDGE FUNDS & CO.: WHO'S STANDING AT THE ROULETTE TABLE?

If we believe the commodity traders, who are trying very hard to sharply differentiate their activities from those of the pure speculators, there is no correlation between their profit and the price levels of commodities. Pierre Lorinet, Finance Director of Trafigura, thinks it will have "no effect on our performance, whether the price of oil goes up or down, because we are active in the trading of physical goods and not in financial engineering. We are industrialists who make use of geographical, technical and temporal advantages, which always exist in the physical markets."[8] This is at best a partial truth, because the difference between financial and trading operators in the commodity business has long since become blurred.

Derivatives dealers have played an ever more active role in the real commodity trading in recent years. American and British commercial banks such as Goldman Sachs, Morgan Stanley and Barclays Capital already have such large departments for physical trade that in 2003 Morgan Stanley, for example, was Vitol's seventh largest customer, coming immediately after the US oil majors.[9] A further example: the boss of JP Morgan Global Resources admitted that at the end of 2010 his bank had bought an amazing 122,222 tonnes of copper – a quantity that is equivalent to 50 per cent of the copper stocks traded on the London Metal Exchange.[10] UBS is also muscling in at the front. At the end of 2009 it was said to have had commodity inventories amounting to 16.2 billion dollars at its disposal. The value of this balance sheet asset had doubled within a year, putting UBS ahead of JP Morgan, Morgan Stanley and Goldman Sachs.[11]

Other companies, having so far only engaged in 'paper trading', have also recently begun to extend their operations to include trading in physical commodities. Anthony 'Chocfinger' Ward, manager of Hedge Fund Armajaro, caused a stir in 2010 when he bought and actually took physical delivery of 241,000 tonnes of cocoa, which corresponded to roughly 15 per cent of world reserves, and stored it in specially rented warehouses in the – eventually futile – hope that prices would rise.[12] Such coups are rare, but hedge funds are undoubtedly playing an increasingly important role in commodity speculation. According to industry estimates, the investment in such hedge funds amounted to 35 billion dollars in 2005, by 2008 it was already 70 billion, and at the end of 2010 it was 195 billion dollars.

TRADING BANKS, SPECULATING TRADERS AND INSIDER FUNDS

At the same time as derivatives traders have moved into physical trading, the physical trading companies have expanded their exchange activities beyond their own hedging needs. In 2009, a study by the American Securities and Exchange Commission showed how Vitol, during the price peak in July 2008, and by using an in-house hedge fund, held a full 11 per cent of all oil contracts on the New York commodity futures exchange (NYMEX). At that time, 81 per cent of all contracts on the NYMEX were held by financial institutions that speculated with the black gold either on their own account or on behalf of their customers.

On the 6th of June alone, Vitol bought contracts amounting to almost three times the daily oil consumption of the United States. On the same day, the price of oil rose by 11 dollars a barrel.[13]

The particularly close cooperation between Glencore and Credit Suisse CHAP. 7 is another variant of the rampant blurring of borders between commodity trading and financial speculation. The CS Funds launched in 2009, which are based on GAINS, are a concrete product of this cooperation. This abbreviation stands for 'Glencore Active Index Strategy' and denotes an index that traces the movement of commodity prices. Such indices enable investors or speculators to profit from price movements without actually having to buy the relevant values (in this case the commodities). GAINS represents the expectations of Glencore's 'Senior Traders' with respect to the price movement of 20 commodities. This index is therefore composed in alignment with their estimations. But: because Glencore does not publish any current information, CS customers do not find out how each index was composed until six weeks have elapsed. It clearly takes that long for exclusive insider knowledge in this sector to become out of date.

Since 2009, news agencies and stock market portals have been reporting at regular intervals that Credit Suisse and Glencore would soon jointly launch an aluminium fund backed by physical aluminium and traded on the stock exchange (ETF Fund). Glencore would be the perfect partner for this, and not just because of its own aluminium production. In contrast to competitors like Goldman Sachs and Morgan Stanley, Credit Suisse has no storage facilities of its own. As luck would have it, in 2010 Glencore bought a whole network of warehouses from the Italian logistics company Pacorini.

FROM BOOM TO BURST: TRAFIGURA TAKES IT TO THE MARGINS OF INSIDER TRADING

While Glencore gold-plates its insider knowledge via Credit Suisse, Dreyfus, like Vitol, uses it in the same way for an in-house hedge fund. Its global information and corporate network helps the in-house commodity group with earlier and more precise indications of market developments in agricultural goods. In mid-2008 – at the height of the financial crisis – Louis Dreyfus Investment Holdings BV (LDIH) was launched. Still in the same year, a LDIH subsidiary floated a 100 million dollar hedge fund. Managed from Geneva, the Alpha Fund invests mainly in options and futures contracts for cereals, oilseeds, sugar, coffee and cocoa. In just two years, the fund capital increased 20-fold to 2 billion dollars and from the beginning of 2011, no more new money was accepted from investors. Commodities inside knowledge pays off: in 2010 Dreyfus' Alpha Fund showed a return of 17.3 per cent, while the average yield of commodity funds in the same period was around 10 per cent.

Trafigura's diversification goes even further. The oil trader founded an asset management subsidiary, Galena Asset Management, which since 2011 has also operated from Geneva. Galena cooperates with several hedge funds and thereby exploits Trafigura's excellent market knowledge for investment in commodities. In addition, it manages six funds of its own with an investment volume of over 1.4 billion dollars. Although this direct exploitation of insider information is possibly actionable in the US, Trafigura sees no legal problems whatsoever. "Galena is subject to financial supervision by the UK FSA," says Trafigura's Managing Director Jeremy Weir, who is also the head of Galena. Galena Asset Management used to claim on its website "transparency, integrity and process underlie everything we do." And in case of doubt, good networking helps. It is certainly no accident that Lord Strathclyde, the leader of the Conservatives in the UK's House of Lords, sat on the Galena Board from 2005 to 2010.

The latest trend is the Galena Commodity Trade Finance Fund. With this fund, the circle is closed. Launched by the financial subsidiary of a commodity trading company that is itself financed by banks, the fund buys outstanding commodity trading credits from the (same) banks ('Pre-Export Finance, Structured Trade Finance'). This action relieves the balance sheets of the banks, so they in turn can give the commodity traders more credit, and so on. It seems almost as if Trafigura/Galena may have invented financial perpetual motion in the commodity sector. Of course, this only works until this bubble, too, bursts with a great 'Pop'.

THE FEWER REGULATIONS, THE MORE RISKS

In May 2011, the Swiss commercial lawyer Jean-Yves De Both noted that, "today, the trading companies operate quite unabashedly in a wide range of financial transactions, and entirely without authorisation or control by the financial regulator." In view of the increasingly more evident regulatory pressures in Europe and the US, "the commodity traders will have to decide quite soon whether they want to limit themselves to hedging transactions, or to operate under official supervision."[14] Cargill, for example, in a precautionary move has already complained to the US regulator, the Commodity Futures Trading Commission, that in the case of statutory regulations it would have to register as a 'Swap Dealer'. But this would reduce the profitability of the trading business because the company would have to put more of its own capital into the financial business.[15] De Both warns of the inaction of the Swiss authorities in this matter and says that it is "possible that companies registered here will enjoy their freedom a little longer."[16] One more reason for the commodity traders between Lake Geneva and Lake Zug to congratulate themselves on their Swiss headquarters.

TAX AVOIDANCE //

The ingenuity shown by the commodity companies when creating artificial complexity knows no bounds. The tax authorities are always two or three steps behind the accounting tricks. And in Switzerland they actually turn a blind eye deliberately.

14 //

'TRANSFER PRICING' & CO: TAX AVOIDANCE AS A BUSINESS PRINCIPLE

In the mid 1960s the Chief Financial Officer of the Standard Oil Company of New Jersey (later Exxon), Jack Bennet, was asked where the oil company made its profits: in production, refining, or the sale of petrol at garages. Bennet's answer? "The profits are made right here in the Treasurer's office,« he explained, »wherever I decide."[1] Thus the oil manager put today's defining characteristic not only of multinational commodity companies but also of multinational companies in general in a nutshell: they shift costs and therefore profits back and forth between their many subsidiaries in order to minimise their tax payments. Basically, this allows a company to book the highest possible costs in order to depress profits and therefore the tax on profits, or even to record a loss in order to avoid paying any tax at all. Even better is when the costs incurred by one subsidiary can appear as revenue on the books of another subsidiary of the same company located in a tax haven. By this method, profit is engineered to be highest in those subsidiaries based in tax havens and thus remain untaxed.

In fact it was the oil companies who nurtured the first flowering of this complicated game with internal transfer price adjustments known as 'transfer pricing'. For this to function the primary requirement is that there be jurisdictions in the world in which the statutory taxes are either low or non-existent. The chief financial officers discovered these in Panama and Liberia where their subsidiaries that owned the oil tankers were registered (a location which, incidentally, had the added advantage of lax health and safety standards). These subsidiaries bought crude oil cheaply from producing countries only to transport and then resell it at far higher prices to their own refineries in industrialised countries. As a result, the transport companies based in Panama and Liberia book the lion's share of the profit - tax free of course.

Today between 40 and 60 per cent of world trade is not carried out between different companies, but between subsidiaries of one and the same company group.[2] World trade, in this way conducted as internal trade, suffers from a certain irony as it is the very same multinationals that are loudest in lobbying for a free market economy. Yet in two-thirds of world trade, which these global players themselves control, anything but market prices apply. In the wake of worldwide competition for business locations the number of tax havens has dramatically increased. The international Tax Justice Network calculates that there are 70 jurisdictions which impose very low or no taxes at all on foreign businesses and provide special tax rules for certain company functions.

SERIOUS NUMBER GAMES: RELOCATING AND CONCEALING PROFITS

'Transfer pricing' can refer to the normal practice of setting prices for trading carried out between subsidiaries within a company group or to the manipulation of these prices. This practice is also labelled 'abusive transfer pricing' or 'transfer mispricing'. The aim of manipulating prices in this way is always to reduce revenues or inflate costs for tax purposes.

In addition, whereas a lower price is charged for exports, an inflated price is set for imports, e.g. of pre-products or machines. Both methods have the same aim: to reduce the taxable profit or even produce a loss. Evidence of this type of manipulation can be found in trading statistics. It was here that in 2008 a researcher discovered that cashew nuts had been exported from Nigeria to the USA at fifty cents per kilo when their real value was five dollars a kilo. Conversely, fibreglass cables, which actually cost six dollars, were imported into Nigeria for 1,372 dollars.[3] If a subsidiary in a tax haven acts as an intermediary in transactions such as these, most of the profit is recorded by the subsidiary and is therefore tax-exempt FIG. 1.

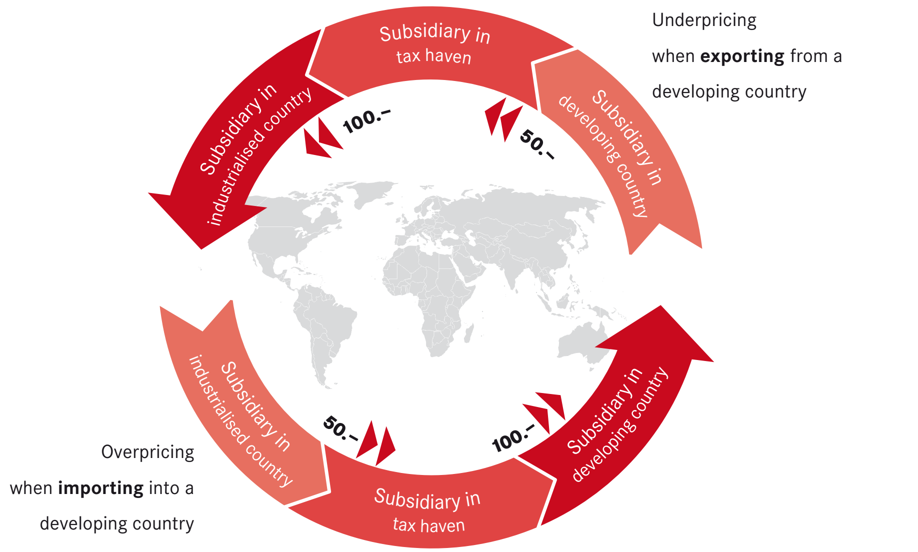
Profit shifting by manipulating prices in this simple way has become more difficult since many tax authorities have begun to require that market prices be charged for internal transactions (more on this below). However, today's companies have developed a raft of other possible methods to ensure their profits are allocated to tax havens.

Tax savings can be made by simply distributing company activities geographically. An expert report scrutinising companies paying remarkably low taxes summarised their behaviour as follows: "[These businesses] have a concentration of their more profitable functions in foreign jurisdictions where the average tax rate is lower and a concentration of their less profitable functions in jurisdictions where the average tax rate is higher."[4] TAB. 1 gives an overview of the main activities of profit shifting.

The term holding company refers to a parent company which has capital interests in legally independent subsidiaries. Together, the holding company and all its subsidiaries form the group. By establishing a holding company in a tax haven, the group can ensure that profits, which are allocated to the holding company or are returned by the subsidiaries, remain exempt from taxes. To make this possible, a political double taxation agreement (DBA) between the countries where the parent company and the subsidiaries are based is usually necessary. For example, these types of agreements ensure that dividends paid by the subsidiaries in their countries of

FIG. 1

MANIPULATING TRANSFER PRICING



Source: author's illustration

origin are not subject to withholding tax. This means that not all tax havens make suitable locations for holding companies, but only those with a dense network of such agreements. However, highly skilled tax optimisation involves not so much avoiding double taxation as achieving double tax exemption. Something all those working in the tax avoidance industry get very excited about is what is known as a 'double dip', i.e. the possibility of deducting interest payments twice, or succeeding in fabricating a tax-exempt dividend payment at a parent company out of a tax-deductible interest payment at a subsidiary by using an offshore finance company FIG. 2.[5]

TAB. 1

ACTIVITIES IN REGIONS WITH LOW OR NORMAL TAXATION LEVELS

	Low/no taxes	Normal Corporate taxes
Company structure	Holding company	Subsidiary
Financing	Granting loans, internal financing	Borrower internal debts
Patents	Owning patent rights	Using patent rights
Brand rights	Owning brand rights	Using brand rights
Leasing (e.g. machinery)	Lessor	Lessee
Management services	Provider of management services	User of management services
(Re-)insuring	Provider of internal insu-rance services	The insured

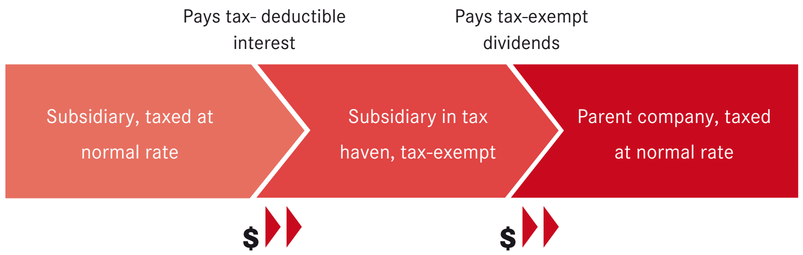
Source: compiled by the author

THIN SUBSIDIARIES AND FAT PARENT COMPANIES

The distribution of activities between tax havens and countries with normal tax rates illustrated above leads to a flow of money into those parts of a company located in tax havens. Internal financing involves a flow of interest payments; moreover, the debts of subsidiaries are usually tax deductible. ‘Starving’ the latter, referred to as ‘thin capitalisation’ in financial contexts, is one of the most effective methods companies employ to minimise taxes. It involves giving the subsidiaries very little capital of their own and assigning them large debts owed to the financial subsidiary of their parent company. An extreme example of this comes from Chile: when the Exxon Group sold the mining company, Disputada de las Condes, in 2002, it was revealed

FIG. 2

THE ‘DOUBLE DIP’: TWO FOR THE PRICE OF ONE



Source: author’s illustration

that the business had been reporting losses for 22 years and had never paid any taxes. It was so heavily in debt to an Exxon subsidiary in Bermuda as to remain officially bankrupt the whole time. Yet, strangely, the mining company still cost the buyers 1.3 billion dollars …[6]

Patents and brand rights involve paying licence fees. For example, the IKEA brand is owned by a Luxemburg holding company, which is owned by a Liechtenstein foundation. All the branches have to pay three per cent of their revenues for the use of the IKEA brand to the holding company in Luxemburg. As key value drivers in the industry most pharmaceutical patents also belong to subsidiaries in tax havens. Likewise, insurance and re-insurance entail paying premiums, leasing involves leasing rates and internal costing, as in management services, allows accountants’ imaginations to run riot. The US company WorldCom even succeeded in relocating its ‘management foresight’ to a subsidiary as an intangible asset. Unfortunately it didn’t do much good: WorldCom filed for bankruptcy in 2002 and CEO Bernhard Ebbers was sentenced to 25 years in prison.[7]

LEGAL? ILLEGAL? WHO CARES?

Tax optimisation by group structures is nearly always completely legal. It involves achieving the perfect combination of the different rules in various national jurisdictions and, frequently, aggressively exploiting any grey areas at the same time. This is why companies usually use many tax havens at once: the ideal location can nearly always be found for any activity. Sometimes what is needed is a combination of various tax havens. A popular combination is owning a holding company in Luxembourg and a finance company in Switzerland, known as a 'LUX/CH sandwich' in industry slang. It works the other way round too, as the example of Glencore further below illustrates. A method such as this makes it possible to reduce the total tax burden to two or three per cent of a company's profits, compared to standard tax rates of between 20 and 35 per cent. Moreover, interest payments by the borrowing subsidiaries are tax-deductible.[8]

Multinational companies have highly specialised and highly paid departments to plan their tax. As such, they are far superior to the tax authorities in most countries in terms of their expertise and manpower and as a result there is little cast-iron evidence on the specific tax-avoidance methods employed by companies, although these are standard practice. The most valuable evidence is that from whistleblowers or details of a company's internal affairs that become public knowledge in other ways, as in the examples below.

The legal systems and degree of tolerance operating in individual countries differ considerably. A powerful tax authority, such as the one in the USA, will only allow substantive offshore structures. For example, simply outsourcing patents to a shell company is not enough. For permission to be granted for patents to be held abroad, the American tax authorities insist that the research conducted in the USA earns compensation, paid by the subsidiary, and is therefore taxed in the USA. Nonetheless, some tax savings can still be achieved from the difference between these payments and the (higher) patent licence fees for using the outsourced patents.

At the other end of the spectrum are tax authorities, who turn a blind eye to this kind of corporate manipulating on principle (as in Switzerland), or are hopelessly out of their depth when faced with such deliberately contrived complexity (as in many developing countries). In such cases, simple shell companies without any offices or employees are often all that is needed to relocate profits, as the example below illustrates. It may be illegal but there is only a very slight risk of being exposed.

THE EXAMPLE OF VOLCAFE 'OFFSHORE INVOICING'

In 2004 documents were leaked to the Berne Declaration (BD) that revealed how the Winterthur-based coffee-trading company, Volcafe (since bought by ED&F Man), avoided paying taxes by using Cofina Limited (COF), a shell company in the tax haven Jersey. Volcafe sold coffee from subsidiaries in the producing countries to the parent company or large customers via Cofina: the subsidiaries sold the coffee to Cofina cheaply; Cofina sold it at a higher price to large customers or to the parent company in Winterthur. This is a classic case of transfer pricing by underpricing which permitted Cofina to record a tax-exempt profit of 24 million dollars in 1998 alone.

At the same time, Cofina was only a fiction; it was nothing more than the employees of a law firm on the British Channel Island of Jersey who were signing documents on behalf of Cofina. Cofina's operations were conducted by the employees of the individual companies in other countries who each had a second computer located in a warehouse instead of an office. In the event of a tax inspection, all they had to do was remove the cable connecting the two and Cofina could not be traced. And to keep things like that, Volcafe management stipulated precisely how the lucrative fiction 'COF' was to be maintained in their Instructions for Offshore Invoicing: "As COF will act as an independent [entity] in our group certain requirements in the flow of documents and a uniform appearance of COF is of great importance. [...] Please take care that all communication with the final buyer is made in the name of COF and mention clearly towards your customers that they receive all documents in the name of COF." Even small details were included: "You should program your fax machine in a way that your name does not appear on faxes dispatched in the name of COF. If it is cost wise justifiable you should install another fax machine for the dispatch of 'COF Faxes'." Evidently some customers became confused, but here too the manual had a ready-made simple solution: "Add a sticker with your address to all documents, which you dispatch in the name of COF and to which you expect an answer. This makes it easier for your business partners to send their mail to the right address." Soon after the Berne Declaration (BD) had made the Cofina construction public, Volcafe announced its liquidation in August 2004.

The example of Cofina also demonstrates how subsidiaries in tax havens can be used to award managers tax-free bonuses. Although the shell company had no employees, in 1998 Cofina paid out 2,188,193 dollars in wages. Incidentally, this is still standard practice in large companies today. For example, until recently UBS owned a business called Senior Executive Benefit Trust Limited in Jersey. Here too exposure worked wonders: having been uncovered by the Berne Declaration (BD), the bonus vehicle was dissolved at the end of 2009.

THE PITFALLS AND SNARES OF THE 'ARM'S LENGTH' PRINCIPLE

Even in an era of globalisation corporate taxation is one of the few functions of a state still organised at national level. The most important international organisation that deals with tax issues is the Organisation for Economic Co-operation and Development, a union of the industrialised countries. For decades the OECD has been trying to cope with the problem of 'transfer pricing' and the relocation of profits by employing a completely inappropriate method, namely the 'arms length principle'. In theory, companies should be paying the same prices for internally traded goods and services as they would pay were these to be sourced from third parties. In addition, the contracts between internal suppliers and service-users should meet the standards of contracts that are usually made between unrelated companies.

Although the books containing OECD advice on how to implement this high moral standard are growing ever thicker, the arm's length principle is having no effect. US senator Byron Dorgan poured scorn on the international rules currently governing internal pricing and tax policies: "It's the equivalent of asking the Internal Revenue Service to connect the ends of two different plates of spaghetti," Dorgan said.[9] The main weaknesses of current practice at a glance:

- Market prices exist for common, highly standardised products. But what is the market price for the precision machine part made by just one manufacturer?

- Similarly, it is virtually impossible to find an actual market price for intangible assets, such as patent licences, brand rights or management services.

- If two subsidiaries enter into a contract the stakeholders and decision-makers in both companies are the same people. It makes no sense for affiliated companies to enter into contracts such as those concluded by independent businesses anyway.

- Consequently companies can only optimise their taxes if each subsidiary is taxed separately as an independent unit. The fiction of independence conceals the fact that many of these constructs exist purely for the purpose of reducing the taxes paid by the holding company.

In short, the arm's length approach produces rules that are impenetrable to citizens, virtually incomprehensible to politicians and a nightmare for the tax authorities that actually try to apply them. The only people who really like this approach are the employees of global accounting and tax advisory firms. PricewaterhouseCoopers, Ernst & Young, Deloitte and KPMG dominate this tax-avoidance industry: it is one of the fatal absurdities of our financial system that, as accountants and auditors, these businesses are assuming quasi-state functions while, at the same time, making every effort to help their clients do the state out of its tax revenues.

The more complexity there is, the more specialised advisors are needed and the larger the legal grey areas become, which can be exploited for tax purposes. A refreshingly candid advertisement reflecting this fact appeared in the Swiss daily *Neue Zürcher Zeitung:* "Effectively implemented transfer pricing can save a great deal of money and trouble. Charging correct prices internally is one thing. Extracting the maximum tax savings out of the different rules applying in different countries quite another. PricewaterhouseCoopers offers globally operating companies customised solutions."[10]

In Switzerland the prices charged within a company are not subject to statutory regulations. The Swiss Federal Tax Administration publishes handouts from time to time with the timid note that Switzerland applies an arm's length approach but unlike in other countries, companies in Switzerland are not obliged to document the prices they charge internally. It is little wonder then that Angelo Digeronimo, an expert in international corporate taxation at the Swiss Federal Tax Administration, said: "As a relatively low-tax country, we are not often confronted with the problem of 'transfer pricing' at our expense." No more than ten complaints cases were landing on his desk per year.[11]

LOST TAX REVENUES GREATER THAN GLOBAL DEVELOPMENT AID

The fact that the public hardly ever hears anything about internal price manipulating and moving profits comes as no surprise, given that tax-avoidance strategies are one of the most profitable corporate activities and therefore one of the best-kept company secrets. Furthermore, there are only extremely scanty details about the resulting tax losses as regards individual countries. International organisations that conduct large-scale economic research projects, such as the OECD, the International Monetary Fund (IMF) or the World Bank, have so far kept a remarkably low profile when it comes to this fundamental problem of globalisation. In a 450-page book on the taxation of petroleum and minerals by three IMF employees, the authors failed to devote little more than four pages to "aggressive tax planning".[12] Not surprisingly, the most reliable estimates are those by

TAB. 2

LOSSES OF DEVELOPING COUNTRIES DUE TO COMPANIES MINIMISING TAXATION

Source	Description	Amount
Baker 2005	Illicit capital outflows: - Abusive transfer pricing	100-150 billion dollars/year
	- Mispricing, fake transactions*	250-350 billion dollars /year
Christian Aid 2008	Tax lost due to false invoicing and abusive transfer pricing	157 billion dollars/year
Christian Aid 2009	Tax revenue lost due to abusive transfer pricing	122 billion dollars/year
Global Financial Integrity 2010	Tax revenue lost due to abusive transfer pricing	99-107 billion dollars/year

**Transactions between independent businesses can be manipulated in order to avoid taxes. For this the purchaser must, for example, be willing to make a cover payment in addition to offering a low official selling price to a vehicle in a tax haven ('mispricing'). According to Baker even totally fictitious transactions are very often used for capital flight and tax avoidance ('fake transactions').*

Source: compiled by the author

TAB. 3

COUNTRIES WITH THE MOST TAX REVENUE LOST DUE TO 'TRADE MISPRICING'

	Country	Tax revenue lost (in % of state revenues)
1	Zimbabwe	31.5%
2	China	31.0%
3	Philippines	30.7%
4	Nicaragua	27.7%
5	Mali	25.1%
6	Democratic Republic of Congo	24.9%
7	Costa Rica	22.2%
8	Zambia	21.7%
9	Honduras	21.6%
10	Belarus	21.5%
11	Cameroon	17.1%
12	Guinea	16.5%
13	Ethiopia	16.2%
14	Malaysia	15.4%
15	Central African Republic	14.6%
16	Cambodia	13.9%
17	Togo	13.5%
18	Panama	13.5%
19	Tajikistan	13.3%
20	Solomon Islands	13.0%

**According to the World Bank the countries highlighted – as many as six out of twenty – are heavily dependent on mineral (ores and oil) exports.*

Source: Global Financial Integrity 2010

non-governmental organisations. TAB. 2 gives an overview of the estimated tax losses (via different methods) of the developing countries.

A comparison between cumulative tax revenue losses and development aid given worldwide illustrates the economic relevance and political sensitivity of tax optimisation by transnational corporations. Development aid totalled 129 billion dollars in 2010. Even the most conservative estimate of tax losses is of a similar magnitude but it is quite possible that developing countries are losing still far greater sums. The losses to individual countries are considerable, as the list of the 20 worst-hit countries shows. TAB. 3.

COMMODITY TRADERS ARE EXCEPTIONALLY GOOD WITH FIGURES.

The methods described above are widely used in the commodity sector too. Below three randomly selected but representative examples:

- Russia: in 2009 the Chamber of Control and Accounts responsible for auditing state finances published a report on underfactoring in coal exports. According to this report 80 per cent of Russian coal is sold to offshore (i.e. registered in tax havens) trading companies and is sold at prices that are between 30 and 54 per cent below the world market price.[13]

- Tanzania: during an audit in 2003 the government discovered that four foreign gold-mining companies operating in the country had all reported unsubstantiated losses totalling 502 million dollars within the last five years. This meant a loss of 132 million dollars in tax revenues to Tanzania, one of the poorest countries in the world.[14]

- Senegal: in 2009 two subsidiaries in Senegal belonging to the Australian mining company Mineral Deposits paid 42 million Australian dollars in interest to a shell company based in Mauritius. A loan of at least 800 million dollars would have been necessary to justify such a high interest payment. Yet in the entire group only 65 million Australian dollars had been lent to various subsidiaries.[15] This was no ordinary case of undercapitalisation, but largely fictitious interest payments in order to move profits.

ZAMBIA: COPPER EXPORTS TO NO-MAN'S-LAND

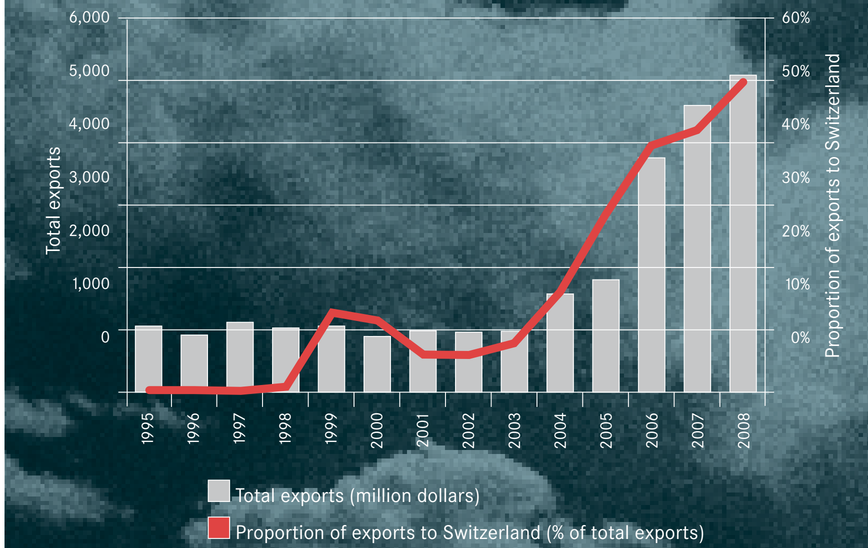
According to UN trade statistics the proportion of exports from Zambia to Switzerland has increased dramatically since 2002 FIG. 3. In 2008 half of all exports were to this small Alpine country. The rise paralleled a five-fold increase in Zambia's exports. The background to this boom in exports was the expansion in copper mining. In 2008 mining products, of which copper was by far the most important, made up nearly 80 per cent of exports.

Coincidentally, Zambia did not appear anywhere in the import statistics of the Swiss Federal Customs Administration for copper and copper products. The exports from Zambia to Switzerland did not tally with the imports into Switzerland from Zambia.

The reason behind this is called Glencore CHAP. 6. Glencore is the majority shareholder in Zambia's Mopani copper mine via its subsidiary in the tax haven, Bermuda, and an investment vehicle in the Caribbean haven the British Virgin Islands. FIG. 4. Virtually the only customer for the products is Glencore itself. This is why 'Switzerland' is always the named destination of exports from Mopani recorded in Zambia. Of course, Glencore's goods never physically reach Switzerland: they are delivered straight to a customer in China for example, which is why copper from Zambia never appears in Swiss import statistics.

FIG. 3

SWITZERLAND IS ZAMBIA'S MAIN TRADING PARTNER



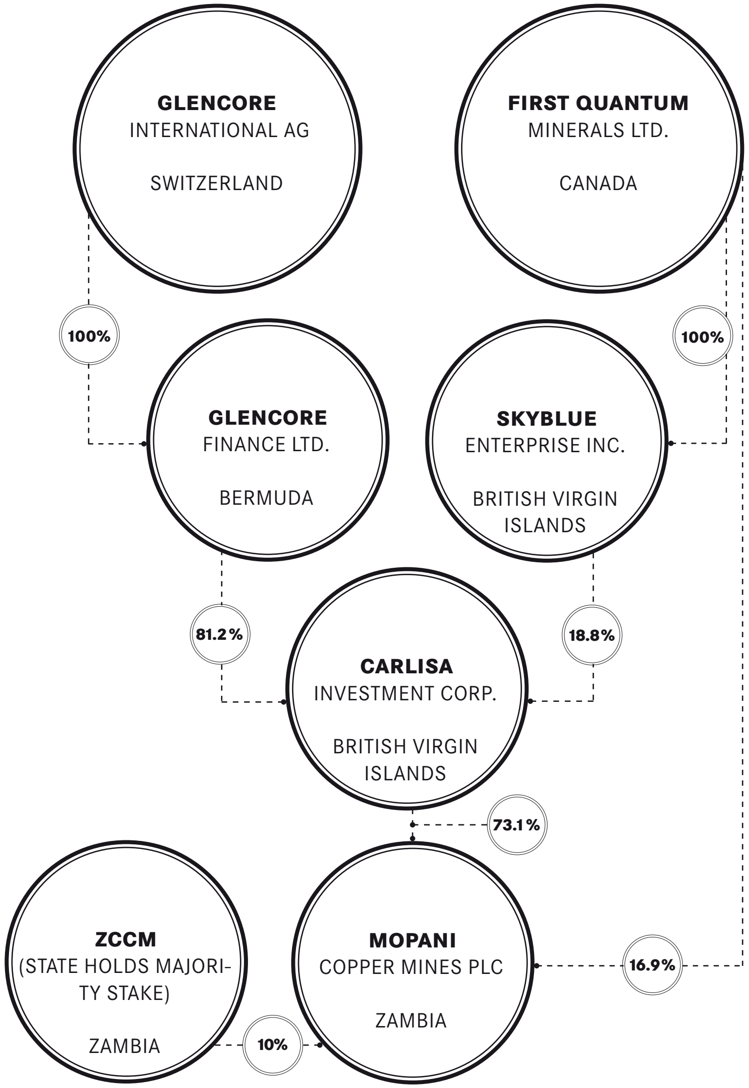
Source: Cobham 2009; UN Comtrade

HOW DOES GLENCORE PRODUCE BOTH LOSSES AND COPPER?

Despite the copper boom Glencore has been making a loss in Zambia for years and paying no profits taxes as a result. Due to the resulting losses suffered by the country the Zambian tax authorities had some mines audited by the international accountancy firm, Grant Thornton, and the Norwegian consultancy firm, Econ Pöyry. Mopani/Glencore was chosen on account of both its size and its abnormally high costs. Completed in 2010, the audit was leaked to non-governmental organisations including Berne Declaration (BD) who published it in early 2011.[16]

FIG. 4

GLENCORE'S INTEREST IN THE MOPANI MINE



Source: Sherpa et al. 2011

The fact that Mopani did not make a profit can only be explained in part by the very investor-friendly mining laws in Zambia CHAP. 17. These allow businesses to deduct all their prospecting and exploration expenses from their tax payments. The costs for these can be set against the profits as tax losses for ten years. This permitted the company to deduct 260 and 371 million dollars respectively from its profits in the years 2006 and 2007, covered by the audit.

However, the audit also reveals how Mopani deliberately inflated costs and did not charge market prices internally. The management of the Glencore mine hindered the auditors' work at every turn. Although the start of the audit had already been postponed several times to give the company more time to produce the necessary documents, the audit then had to be adjourned for a further six months because the documents were full of gaps. Even so, when they could at last continue, the auditors found various irregularities:

- The general ledger were delivered in continually changing formats. Despite this the figures in them never tallied with the trial balances.
- There were no original documents for many transactions; sometimes there was no documentation at all.
- Elementary data, such as the quantities of ore, copper concentrate and copper produced, were missing as were import and export statistics (for which the auditors also lay some of the blame at the door of the Zambian state).

Again and again the auditors encountered impasses and at one point communicated their exasperation by stating, "It should be noted that the international team leaders have not experienced such a lack of compliance in any other country, and Grant Thornton Zambia confirmed that this attitude is also not typical for other industries/companies in Zambia."[17]

Notwithstanding the adverse circumstances, the Mopani audit reached the following main conclusions:

- Costs at the Mopani mine are higher than in comparable mines.

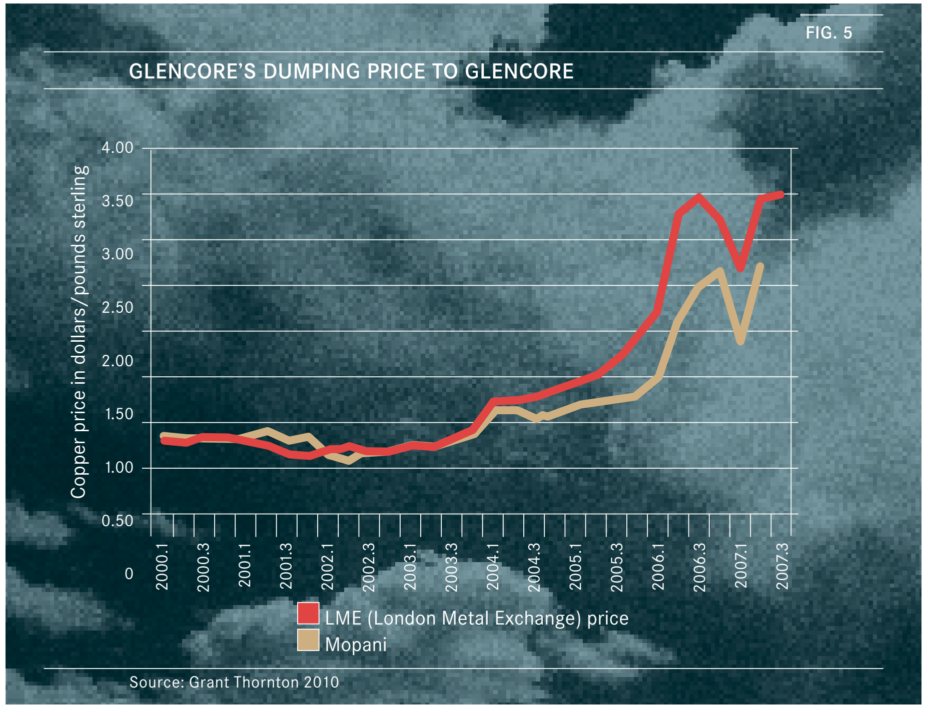
- Revenues are lower than they would be if, as stipulated by law, the prices were set in line with the price of copper on the London Metal Exchange (LME).

The copper prices charged by Mopani deviated significantly and increasingly from the LME reference price during the period in question. FIG. 5.

As sole 'sales and marketing agent' for Mopani, Glencore is in charge of almost all of the mine's production. The audit report stresses that market prices were not charged for internal transactions: "The Company has not been able to provide us with evidence that the Company sales, which mostly are related party transactions, have been entered into according to the arm's length principle."[18] In numerical terms: between 2003 and 2007 Mopani's revenues from the sale of copper were 700 million dollars lower than they would have been at LME prices – a gigantic gift from Glencore to Glencore.

Although the auditors did not calculate the tax losses suffered by Zambia, they did discover that manipulating had also led to lost revenue from royalties that were already low CHAP. 17. On the basis of the audit the British development organisation ActionAid calculated that the annual tax losses suffered by Zambia at the hands of Mopani amounted to 124 million dollars, plus the 50 million dollars lost in dividends for the state's ten per cent stake in Mopani.[19]

The irregularities concerning cobalt, the second product from the Mopani mine, are even greater. According to company figures, Mopani was only obtaining half as much cobalt from the ore mined compared to other mines in Zambia. The auditors commented: "Mopani has either failed to provide us with correct production figures or they are faking



the numbers in order to have the production figures fit with the cobalt revenue in the accounts."[20] Given the incomplete or entirely missing export statistics, concealing part of the production sold was easy. Glencore seems to have had no qualms about carrying out a form of tax evasion, simple and brazen though it is.

Lastly, Mopani used hedging deals, normally used to limit trading losses due to price volatility, for tax evasion also. The auditors discovered hedging deals at Mopani which were structured in such a way that ensured Mopani would make a loss whether prices rose or fell, while the other party to these deals, another Glencore subsidiary, would always earn a profit. The final goal is simple, "There is […] reason to recognize the 'hedging' of Mopani […] as moving taxable income out of Zambia."[21]

From the age-old method of concealing revenues to sophisticated hedging operations, Glencore knows and uses all the available instruments for avoiding paying tax.

SWITZERLAND – A PARADISE FOR COMMERCE

In 2010 the ten European regions with the lowest corporate tax rates included three Swiss cantons: Appenzell-Ausserrhoden and Obwalden were in joint fifth place (each with 12.7 per cent), Zug was in tenth place with 15.8 per cent. Another eight cantons appear in the top twenty.[22] However, the crucial factor is not the relatively favourable standard tax rates, but the special rules. All the cantons apply these which is why Switzerland's attractiveness to commodity traders in relation to tax is not limited to the well-known locations of Zug and Geneva. Hence there are also branch representatives in Vaud (Vale), Lucerne (Trafigura), Zurich (ENRC), Basel-Landschaft (Ameropa) and Ticino (Duferco).

The classic among special cantonal tax rules is the 'Holdingprivileg'. Typically, the headquarters of companies are holding companies; an American or Asian company can also manage its European business from a holding in Zug. Holding companies do not pay taxes on profits in the cantons, merely a negligible charge calculated on the basis of the share capital recorded in the commercial register. The rate that applies in Zug is 0.002 per cent (!).

In theory, a uniform profits tax rate of 8.5 per cent applies at national level. However, dividend revenues are tax-deductible. With a pure holding company, which receives all its revenues from dividends, these deductions can result in total tax exemption. 'Tax privileges' and special rates apply to domiciled companies and mixed companies alike at cantonal level CHAP. 4. The cantonal specifications for domiciled companies vary: in Zug, for example, they cannot have any employees nor any offices. Companies domiciled in Zug pay a capital tax of 0.0075 per cent whereas revenues from abroad are tax-exempt.

Mixed companies are companies or branches of foreign companies that operate mainly abroad and carry out secondary business activities in Switzerland. In the canton of Zug at least 80 per cent of sales and purchases must take place abroad. Taxation on capital is 0.001 per cent. The Swiss revenues of a mixed company are taxed at the standard rate; any revenues earned abroad are only taxed at between five and twenty-five per cent, depending on the number of employees. Unless you are as large as Glencore. Since 2007 there is a rule that could be labelled the 'Glencore Clause.' Revenues from business abroad totalling over 200 million Swiss francs must only be taxed at ten per cent (instead of 25 per cent with more than 30 employees).

In addition to the favourable tax rates and special rules, Zug publically advertises itself as offering another important advantage: "However, the real advantage of Zug as a business location is not so much its favourable tax regime, but the generally uncomplicated, unbureaucratic way the cantonal tax authority deals with taxpayers."[23]

The cantonal special rules combined with the participation deductions for holding companies at the federal level are ideal for businesses that not only earn high revenues abroad, but also have interests in many foreign companies. Both definitions apply to commodity traders in particular. The favourable tax regimes and compliant tax authorities are the key factors which explain why this industry feels so comfortable in Switzerland.

CUSTOMISED PRIVILEGES INSTEAD OF FISCAL TRANSPARENCY

Swiss cantons do not publish lists of firms that enjoy tax privileges which is why it is not public knowlegde which companies are taxed as mixed companies. For the canton of Geneva we at least know that over 1,000 companies are taxed as holding, domiciled or mixed companies, and that these together pay one quarter of all corporate taxes.[24] But, to make matters worse, the cantons may grant a company customised privileges, using so-called 'tax rulings'. Hence Pierre-Olivier Gehriger, tax-avoidance expert and partner in the law firm of the former Glencore board member Peter A. Pestalozzi, commented: "[T]he advantage of the ruling system that usually functions well [can] not be overestimated."[25] It is little wonder then that a query to Glencore as to which of its companies and subsidiaries are taxed as domiciled or mixed companies was met with indignation rather than information. "But we don't even tell our investors that!" was the response.

According to a letter from the Geneva Ministry of Finance, most commodity traders are treated fiscally as mixed companies. The tax rate of 12 per cent (as a general rule) mentioned by the same ministry for such 'Sociétés auxiliaires' (auxillary companies) comprises 8.5 per cent for the normal direct federal tax and 3.5 per cent for the reduced cantonal and municipal tax.[26] The industry lobby GTSA refers to an effective tax rate of 9 per cent.[27] In the canton of Zug, the rate may be even lower for profits above 200 million Swiss francs because of the 'Glencore Clause'.

BABYLONIAN STRUCTURES: TRAFIGURA'S MULTIPLE BUSINESS IDENTITY

Where the Swiss tax authorities stonewall, the Dutch Trade Register is helpful. This is where the annual reports of Trafigura, Vitol, Gunvor, Mercuria and Dreyfus can be accessed and which contain (as do those of Glencore) some information on the effective tax rates these companies have paid TAB. 4.

Trafigura's record-low tax rate for 2010 was due to a substantial tax credit. However, the rate would have been a mere 6.2 per cent even without this. Given the standard Dutch tax rates (2005: 32.25%, 2006: 30.09%, 2007: 26.53%, since 2008: 25.5%) and without tax credits the tax savings of this scandal-ridden company CHAP. 10 totalled more than 500 million dollars between 2005 and 2010. Moreover, these effective tax

TAB. 4

TAX MINIMISATION AT SWISS COMMODITY COMPANIES

	Trafigura ('effective tax rate')	Glencore ('effective tax rate')	Vitol ('total income tax')
2005	15.1%		
2006	16.4%	16.0%	
2007	16.4%	13.4%	12.1%
2008	8.5%	8.9%	7.5%
2009	11.8%	12.6%	19.6%
2010	0.6%	9.3%	

Source: company annual reports

rates are only the visible side of the coin. On the other, totally opaque, side it is usually the companies themselves who decide just what they report as taxable profit. For example, Glencore was able to pass on billions tax-free to its shareholders (in other words, the managers with shares) year after year before its stock market listing.

Equally impressive is the list of Trafigura's subsidiaries in tax havens (excluding Zug and Geneva), which number no less than 40 TAB. 5.

According to official Trafigura information Lucerne functions as the main trading centre of its rambling business empire and Switzerland as its principal residence for tax purposes.[28] Apart from the network of tax-haven subsidiaries stretching all over the world, some of Trafigura's tax savings stem from the tax regime in Lucerne and, presumably, the one in Geneva. Trafigura has two businesses registered in Lucerne: a branch of the company legally domiciled in Amsterdam, Trafigura Beheer BV, and Trafigura AG. In 2010 the Swiss weekly newspaper the *Sonntagszeitung* surmised that what had attracted Trafigura to the shores of Lake Lucerne was the special privileges there and that, as a 'Verwaltungsgesellschaft' (the equivalent of a mixed company in Zug), it paid a profits tax of only three per cent. In 2007 tax was paid in Lucerne on a profit of 212 million Swiss francs,[29] just short of 40 per cent of the overall profits for that year. When questioned by the cantonal parliament in 2010, the cantonal government in Lucerne refused to provide any information whatsoever about Trafigura's tax rate, but denied that the company enjoyed any exclusive privileges.

DUTCH AGREEMENTS, SWISS TAX RATES: IT'S ALL IN THE MIX

Like many commodity traders Trafigura's structure resembles that of the legendary Russian matryoshka dolls. FIG. 6 gives a brief impression of this 'nesting' principle.

Such a Babylonian complexity begs the question whether this rambling structure is not at odds with the industry's revered principles of 'lean-management' and extreme cost-consciousness? Old companies are constantly replaced, new ones founded and existing ones rechristened. Between 2005 and 2008 the subsidiary at present known as Puma Energy International BV had three different names in as many years. What looks like mere administrative expense and pointless logistics at first glance, is a continual optimisation of location in terms of tax, which seems to pay off. Moreover, its labyrinthine structure can prove very useful should the business encounter problems with the authorities. With companies structured in this way, it is often well-nigh impossible to prove which part of the business is controlling which activity and who has conducted a shady deal on behalf of whom.

A recurring element in many companies in Switzerland is the presence of a Dutch holding company somewhere high up in the organisational structure. This is quite surprising since Switzerland offers such ideal conditions for holding companies. The explanation lies in a special feature of Dutch tax laws: only a small portion of profits are taxed in the Netherlands, ten per cent in the specific case of Gunvor. The Dutch

TAB. 5

TRAFIGURA PRESENCE IN TAX HAVENS (EXCLUDING ZUG AND GENEVA)

Tax haven	Name	Capital interest*
Bahamas	Argomar International Ltd.	50%
Bahamas	Congofret Limited	100%
Bahamas	DT Trading	100%
Bahamas	Leeuwin Holdings Co. Ltd.	100%
Bahamas	IVCO International Limited	73.1%
Bahamas	Puma Energy Bunkering SA	100%
Bahamas	MOZA International Limited	73.1%
Bahamas	Puma Energy Funding Ltd.	81.3%
Bahamas	Puma Energy International SA	81.3%
Bahamas	Puma International Bunkering SA	81.3%
Bahamas	Puma RDC Ltd.	73.1%
Bermuda	Napoil Ltd.	49%
Caribbean**	ECG	40.6%
Cayman Islands	Galena Cassiterite Limited	100%
Cayman Islands	Galena (Cayman) Limited	100%
Cayman Islands	Galena (Malachit) Limited	100%
Isle of Man	Meteor Limited	100%
Malta	Trafigura Maritime Ventures Ltd.	100%
Marshall Islands	DT Refining Inc.	50%
Marshall Islands	DT Shipping Holding LLC	50%
Marshall Islands	Pumangol Energy Bunkering LLC	81.3%
Marshall Islands	Pumangol I	50%
Marshall Islands	Pumangol II	50%
Marshall Islands	Pumangol III	50%
Marshall Islands	Pumangol VI	50%
Marshall Islands	Pumangol V	50%
Marshall Islands	Pumangol VI	50%
Marshall Islands	Pumangol Shipping LLC	50%
Mauritius	Petromoc International	51%
Netherlands Antilles	Blue Streak International NV	100%
Netherlands Antilles	Mero NV	100%
Netherlands Antilles	Gulf Refining Company	52%
Netherlands Antilles***	Union Mining International NV	100%
Singapore	AngoEncore Ventures Pte Ltd.	25%
Singapore	NEMS (Singapore) Pte Ltd.	50%
Singapore	Trafigura Overseas Projects Pte Ltd.	100%
Singapore	Trafigura Pte Ltd.	100%
Singapore	Trafigura Services Pte	100%
Cyprus	Areva Navigation Company Ltd.	40%
Cyprus	NWE Logistics Limited	38.8%

**between 2009 and 2010 its interest in many oil subsidiaries decreased from 100% to a majority interest **Exact location not given ***2009 in the Netherlands Antilles, 2010 in the Netherlands*

Source: Trafigura annual report 2009

holding company's definitive principal residence for tax purposes remains Switzerland with its favourable tax rates. The Dutch holding company still profits from the double taxation agreements there, which prevent profits being taxed in the country of origin (for example a producing country in the case of a subsidiary). Although the Netherlands have entered into roughly the same number of such tax agreements as Switzerland, about 90, prominent countries with whom Switzerland does not (yet) have agreements feature the likes of Argentina, Brazil, Nigeria, Saudi Arabia and Turkey. And since Switzerland did not accept the OECD standard on the exchange of information in these agreements until 2009, the previous Swiss double taxation agreements were therefore not as favourable to companies as those of the Netherlands. The EU membership of the latter may also be an advantage.

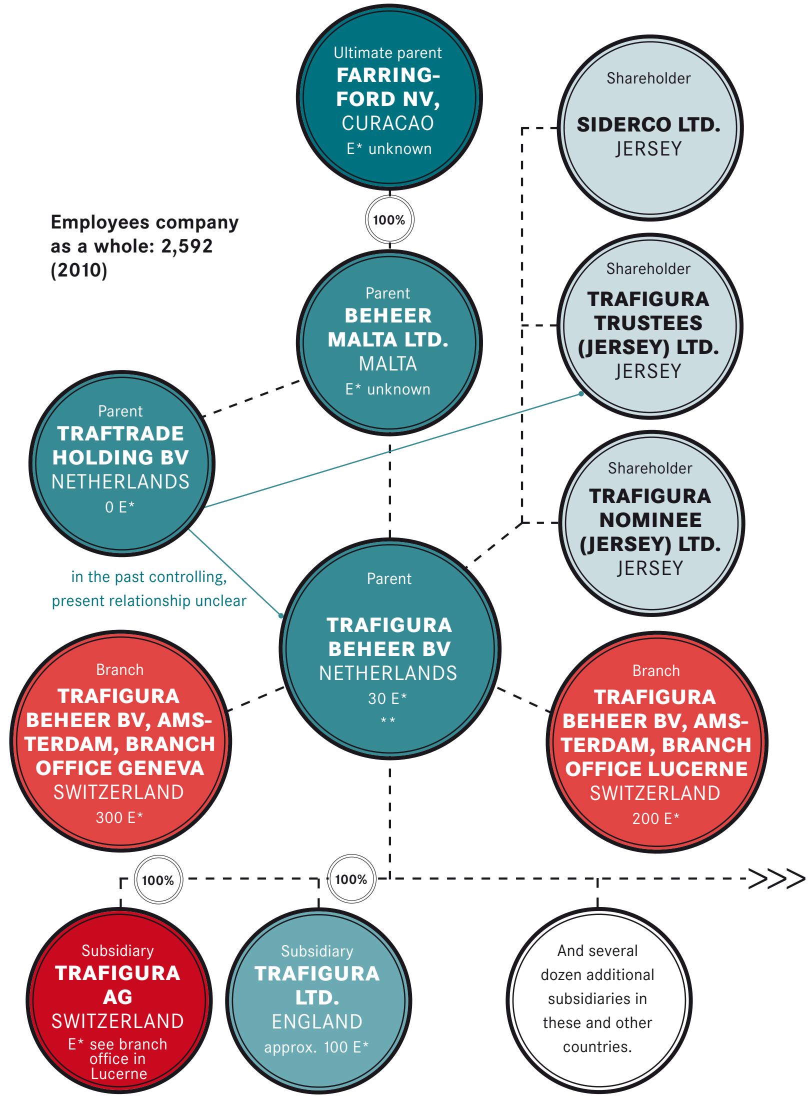
However, a Dutch holding company is never right at the top of such a rambling company pyramid. The ultimate owner is invariably a shell company in an offshore centre, such as Curaçao, Cyprus, Jersey or the British Virgin Islands. It is out of the Dutch holding company that the profits are then channelled to wherever they can be distributed tax-free to the real owners. In addition, these tax havens offer maximum opacity so that not even all Gunvor's owners, for example, are known. Thus the typical structure of a Swiss commodity trader has three parts: trading activities and a principal residence for tax purposes in Switzerland, above that a Dutch holding company for temporarily depositing the global revenues, and one or more vehicles in tax havens as opaque end-repositories of the profits.

MANY MICRO-GLENCORES AND A NEW META-GLENCORE

Glencore uses Zug primarily as its principal location in order to optimise its tax position worldwide. Besides its head office, there are 14 more subsidiaries registered in Baar, in the canton of Zug. The possibility of being able to manage all the individual components of

FIG. 6

A DIAGRAM OF TRAFIGURA'S STRUCTURE



E = employees*

***Includes employees of other parts of company, established at the same address.*

Source: Trafigura annual reports; various commercial registers such a 'mixed bag' as holding, domiciled or mixed companies creates plenty of room for manoeuvre when it comes to tax optimisation. Moreover, Glencore has a massive presence in other tax havens. There are even more registered 'Glencores' in the USA's prime tax haven, the state of Delaware, than in Zug:

GLENCORE ACQUISITION III LLC; GLENCORE ACQUISITION II LLC, GLENCORE ACQUISITION I LLC, GLENCORE AG LLC, GLENCORE ALUMINA (USA) INC., GLENCORE CANADA INC., GLENCORE COPPER USA LLC, GLENCORE FUNDING HOLDINGS INC., GLENCORE FUNDING INC., GLENCORE FUNDING LLC, GLENCORE GRAIN (USA) LLC, GLENCORE IDB LLC, GLENCORE INTERNATIONAL LLC, GLENCORE LTD., GLENCORE MARKETING INC., GLENCORE NICKEL (USA) LLC, GLENCORE OIL RISK MANAGEMENT LLC, GLENCORE PRIMARY ALUMINUM COMPANY LLC, GLENCORE RECEIVABLES LLC, GLENCORE TRADING INC., GLENCORE (USA) INC., GLENCORE USA LLC.

Its initial public offering prospectus contains enlightening information on Glencore's tax payments TAB. 6. Two things strike one immediately: in 2008 and 2010 more than half its revenues were tax-free. Furthermore, it appears that Glencore is able to keep its tax payments more or less uniformly low, regardless of the revenues in any given year.

Glencore used the stock market listing to give itself a new parent company as a legal entity, Glencore International plc, which has its headquarters on the Channel Island tax haven of Jersey. The company maintained that the fact that there is zero taxation on Jersey had nothing to do with the founding of this new 'ultimate parent company' there: "Switzerland and the Swiss tax authorities have confirmed that, on the assumption that the affairs of the company are conducted as the directors intend, they will regard the company as a resident of Switzerland for the purposes of Swiss taxation law." If still more proof for Switzerland's

TAB. 6

THE HIGHER THE EARNINGS, THE HIGHER THE TAX ALLOWANCES*

	2008	2009	2010
Earnings before tax[30]	269	1,885	2,511
Taxes according to standard rate in Zug	43	297	401
Tax-exempt amount	26	56	254
Tax payments**	268	238	234

**Figures in millions of dollars*
***Besides the tax-exempt earnings, other factors determine the effective tax payments that are not illustrated here.*

Source: Glencore IPO prospectus

attraction as a favourable tax location were needed, it would be this sentence in Glencore's prospectus: "It is not intended that the company will be tax resident in any other jurisdiction."[31]

INTERIM CONCLUSION

If one were asked to give a single reason why commodity traders find Switzerland such an attractive location, then it would be its tax regimes. Although there are tax havens that go still further and – such as offshore centres – do not levy any corporation tax at all, Switzerland offers a combination of very low taxes and the advantages of being one of the richest countries in the world which brings with it political stability, a perfect infrastructure and a high quality of life. In addition, the tax rates for private individuals are idyllic as well, which is crucial given the high salaries, bonuses and company share ownership that are common in the commodity business.

The ingenuity shown by the commodity companies, with the assistance of the tax-avoidance industry, when creating artificial complexity knows no bounds. The tax authorities are always two to three steps behind the latest accounting tricks. In Switzerland the authorities actually turn a blind eye deliberately. In developing countries such as Zambia, which does not even keep complete export statistics, tax avoidance is easy and has particularly serious consequences since any money lost is not available to states to fund schools and hospitals or help to feed the population.

It is as if the cantonal special rules in Switzerland were tailor-made for mobile global commodity traders. However, the EU has had these rules in its sights for a long time now CHAP. 11 since they are also costing our European neighbours billions in lost tax revenues. The commodity companies will fight tooth and nail to protect their privileges in the battles to come.

There is a lack of fiscal transparency not only in the commodity companies – not even a stock market listing is going to change that – but also on the part of the Swiss tax authorities. The cantons that are the preferred locations will not publish their fiscal registers and not even a parliamentary question can elicit information. We only know many of the facts about the structures of the businesses or the amount they pay in tax thanks to the business reports published in the Netherlands.

"Commodity trading only works thanks to corruption: it always involves buying political favours. That has always been the case and will probably remain so,"

GREY AREAS //

says Industry Insider James Dunsterville

15 //

CORRUPTION AND CONFLICT ZONES: FROM ‘KAZAKHGATE’ TO ‘OIL FOR FOOD’

This chapter turns the spotlight on four very different issues in the Swiss commodity business. In current and former conflict zones, the problems that are particular to mining and oil production arise in an altogether more severe form. Some Swiss players actually seem to be drawn, as if by magic, to the high-risk but equally high-profit business opportunities that these zones offer, as is demonstrated by the examples of Sudan and the Democratic Republic of Congo (DRC).

Bribery was and will remain the dark side of commodity trading. “Commodity trading only works thanks to corruption: it always involves buying political favours. That has always been the case and will probably remain so,” explains industry insider James Dunsterville of the Geneva-based Global Commodities Group, speaking in an astonishingly open manner in his Geneva Office. The example of Kazakhstan highlights the complicity of commodity trading with a thoroughly corrupt regime.

‘Soft commodities’, i.e. agricultural products, are only ‘soft’ in industry slang. The industrial-scale cultivation of export products is a brutally hard business and, against the background of increasingly scarce cultivated land, also a highly problematic one. A particularly unpleasant, but by no means wholly exceptional, example is that of cotton production in Uzbekistan. For many years, this ‘white gold’ has been harvested using forced and child labour, a fact that is tolerated by the traders.

Finally, we conclude with an analysis of an older scandal, the mechanisms of which are still used as a model by some to this day. Hardly anyone was ever held to account for the illegal purchase of Iraqi oil in the era of Saddam Hussein. This is in part because the companies responsible for the trade used a shield of middlemen and front companies to do lucrative business with an internationally reviled regime of terror.

15.1 //

SUDAN AND CONGO:
DANGER PAY FOR OPPORTUNISTS

In the second half of the civil war that raged in Sudan from 1983 to 2005, the south of the country increasingly became a taboo zone for western companies. For US companies, doing business in the crisis-ridden African State actually constituted an offence, because the Clinton Administration had imposed sanctions against Sudan in 1997 as a result of its support of terrorist activities.[1] When US firms are not allowed to do business, and most other large companies do not want to out of concern for their reputation, unscrupulous niche players scent their opportunity of doing brilliant business in legal/political grey areas.

One such company is the Swedish-Swiss company Lundin, who has been based in Geneva since 1966. In 1997 Lundin Oil formed a consortium to exploit the Block 5A concession area FIG. 1 in southern Sudan. In addition to Lundin (40.4%), Malaysian Petronas (28.5%), Austrian OMV Exploration GmbH (26.1%), and the Sudanese national oil company Sudapet (5%) were involved.[2]

FIG. 1

OIL CONCESSION AREAS IN SUDAN

Lundin bought the rights to Block 5A in February 1997 with a consortium and sold its share in June 2003.

Source: ECOS 2010

The oil reserves in Block 5A proved to be rich, but in 1997 the area was not fully under the control of the Sudanese government in Khartoum, which is why this previously relatively peaceful area was drawn into the middle of the civil war. The south of the country, inhabited by a majority of Christian-Animist black Africans, contains 85 per cent of the 6.8 billion barrels of Sudanese oil reserves discovered to date (world ranking number 20).[3] Oil wealth was one of the reasons for war, because the central government – dominated by Arab North Sudanese – refused to share the revenues from oil production with the South.

Until 1997 Block 5A remained relatively untouched by the fighting. After the concessions had been awarded, Khartoum was ready to use almost any means to ensure safe working conditions for the foreign oil companies. The continually escalating situation developed into a bloody war, which by 2002 had resulted in 12,000 dead, 160,000 refugees, 40,000 destroyed homes and barns, and 500,000 head of livestock killed. One could be forgiven for thinking that no successful business could be carried out in such a violent environment. Lundin did, in fact, have to interrupt the drilling operations again and again, but they were highly lucrative nevertheless; in June 2003 Lundin sold its concession rights to Petronas Carigali Overseas for 142.5 million dollars. According to the European Coalition on Oil in Sudan (ECOS), a group of over 50 European organisations who work for justice and peace in Sudan, this earned over 90 million dollars for Lundin.[4] Another Geneva company, Cliveden Petroleum SA, was also involved in the war zone during the next stage of the escalation of the war in Sudan, the Darfur conflict.

'DOING BUSINESS IN TOUGH PLACES'[5]

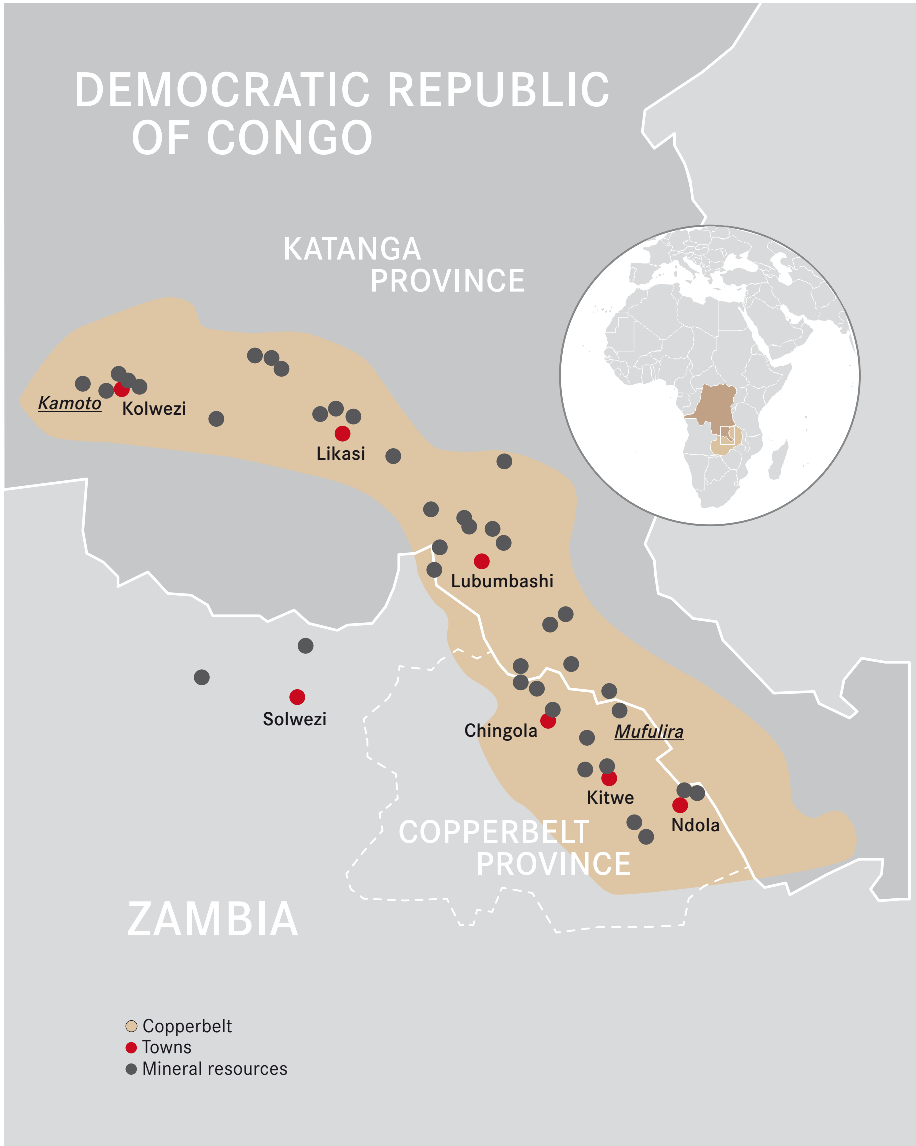
The business model practiced by Lundin can also be found in the mining industry. In this sector, small aggressive companies of this type even have a generic name: 'Mining Juniors'. These are companies – often Canadian – that develop specific individual mining projects under precarious conditions in order to hive them off profitably to a large mining company after the reputation-endangering development phase. One example of a playground for such Juniors is the Democratic Republic of Congo (the DRC), one of the poorest and most corrupt places on the planet. The huge central African country occupies the second-last position in the Human Development Index ranking. For a sobering comparison, consider the country's immense wealth in copper, diamonds, cobalt, coltan, zinc and gold.

A radical economic transformation occurred in 1997 after the fall of the dictator Mobutu Sese Seko, who had ruled for more than 30 years. The mines, processing plants and exploration licences belonging to the State-owned and highly indebted mining company La Générale des Carrières et des Mines (Gécamines) were privatised in Wild West style. Former Glencore CEO Willy Strothotte said accordingly: "This is a very big deal. […] There are huge investment opportunities. We are very interested and open about it."[6] Systematic bribery and the absence of public tendering procedures led subsequently to contracts that mainly served the interests of the private mining companies and corrupt high-ranking officials. In this regard, almost nothing has changed to this day. A foreign mining manager who wishes to remain anonymous summed up the situation: "The whole place is one big scam and everybody is being paid off."[7] The 15 or so major mining companies that wanted to exploit this opportunity, in spite of the scandalous safety and human rights situation and the corrupt structures in the DRC, included the two Swiss giants Glencore and Trafigura.

In the south-east Congolese province of Katanga, which is about 12 times larger than Switzerland, both companies are continuously expanding their holdings by means of share acquisitions and takeovers. This region contains 34 per cent of the world's cobalt reserves and 10 per cent of its copper reserves. Katanga is bordered by Zambia CHAP. 6, where Glencore, with its investments in Mopani Mining, exploits more copper mines in the Copperbelt that runs East-West through the DRC and Zambia FIG. 2.[8] Although southern DRC has been less badly affected by inter-state conflicts and civil wars than the eastern region on Lake Kivu, there is nevertheless a tense situation there, too. The main conflict is between the professional mining companies and the tens of thousands of 'artisanal miners', men and children known as 'Creuseurs,' who, in trying to

FIG. 2

THE RESOURCE-RICH ‘COPPERBELT’



Source: www.tcemco.com

secure a share of the mineral wealth by hand, dig holes and tunnels barefoot and with primitive appliances. The working conditions are life threatening, safety precautions constituting a prohibitive luxury.[9] The Creuseurs sell their meagre amounts of copper or cobalt to middlemen who sell it on to businesses such as Katanga Mining Limited (KML), over 75 per cent of which is owned by Glencore. When one of the former State-owned production areas passes into private ownership, the terms of the contract require the Creuseurs to sell their products exclusively to the respective company, or they are treated as illegal intruders and forcibly expelled as soon as industrial mining begins. In the period from August 2010 to February 2011 alone, over 10,000 people were affected by such expulsions by KML.[10]

Katanga Mining Limited is a classic Junior, registered on the Toronto stock exchange. Glencore smelt an opportunity during the financial crisis. In the autumn of 2008 the banks had virtually stopped lending and naked panic reigned on the capital markets. KML had got into serious financial difficulties and Glencore extended it a loan of 265 million dollars to allow it to continue operations. The contract included a clause under which KML had to repay 165 million dollars as early as February, failing which the lender would receive the equivalent value in shares. As expected, this happened, and Glencore acquired KML at an absolute bargain price. KML owns six copper and cobalt deposits on more than 40 square kilometres in Katanga, and by 2015 it wants to be the world’s largest producer of cobalt and the largest copper producer in Africa. Glencore has also secured the right to sell the entire KML output of cobalt and copper for the next 10 years.[11]

The working conditions in KML mines are appalling, however; the underground mining in Kamoto is said to be one of the most dangerous in the country. Hardly any attention is paid to safety regulations and there are no signs communicating basic safety procedures. The result: three fatal accidents just in the period from April 2009 to February 2010. And what is more, because the miners are rarely given protective clothing, they are exposed to major health risks. This is because the mined rock also contains uranium and other radioactive compounds.

Anaemia, diabetes, kidney problems and infertility are among some of the consequences. Four out of ten miners work without fixed contracts and often have correspondingly less experience and training, which further increases the risk of accidents.[12] But as Tim Huff from the Royal Bank of Canada, which is heavily involved in the mining industry, put it so nicely, "With Glencore, places like Congo are not outside their comfort zone, they are its comfort zone."[13]

AGGRESSIVE CANADIAN 'JUNIORS' AND SWISS SME'S

Trafigura, too, has bought itself a Junior in the DRC. Since December 2009, the Swiss-Dutch trading giant has owned 36 per cent of the notorious Anvil Mining Limited of Canada, a copper exploration and development company. Anvil did not shy away from the prospect of grasping dubious business opportunities in the East Congo civil war zone. That is why a process for the examination of a class-action lawsuit against Anvil Mining is currently underway in Quebec. This particularly aggressive Junior is accused of having provided significant logistical support to Congolese military personnel in a massacre in the town of Kilwa. The action in October 2004 was intended to prevent rebels from occupying Kilwa, which was important for Anvil's mine operations in Dikulushi at that time. According to the UN, over 70 civilians were killed in the action and serious ill treatment and rapes were committed. The Canadian Association against Impunity is representing the survivors of the Kilwa massacre, and submitted their class action on 8 November 2010. Anvil's application to have the case rejected was turned down by the highest court in Québec in April 2011. It is the first time ever that a Canadian court has accepted a complaint concerning offences by a company in another country.[14] However in January 2012 the Québec Court of Appeal refused to hear the case and the case will go to the Supreme Court of Canada.[15]

In 2006, several people died during protest actions related to Anvil's activities in the Congolese province of Katanga. The wrath of the Creuseurs was directed against their exploitation by industrial mining operations and against their obligation to sell their goods to Anvil exclusively. The Canadians shamelessly exploited these restrictive contracts, further by designating the material produced by hand as being of inadequate quality, and drastically reducing the buying price.[16] In the course of efforts to expel Creuseurs, Anvil's security forces are said to have drowned a man, whose enraged colleagues then set fire to an Anvil hostel. A cook and a security guard died in the flames. The police broke up the ensuing protests with live ammunition, which resulted in the deaths of several more people.[17]

The company Ameropa, based in Binningen in the Swiss Canton of Basel-Landschaft since 1948, is also active in the DRC. This privately held company with 2,265 employees worldwide CHAP. 12 is mainly active in the artificial fertiliser and grain trades. It began doing business in a conflict area when an Australian fertiliser company, in which Ameropa has had a majority shareholding since 2010, exported phosphate from Moroccan-occupied Western Sahara. The small metals-trading division of the Basel-based commodity SME was set up by Isaac levy a former Glencore executive for cobalt, molybdenum and vanadium, who is himself involved as a shareholder ('equity partner') in Ameropa's subsidiary, ROQ Mining. Through ROQ, Ameropa operates two small open-pit mines in Congo with 500 employees and acts as buyer for the cobalt extracted from the small-scale mines. The ore is transported on trucks to Dar es Salaam and Durban, where it is transferred to ships. The customers include a refinery in Norway that belongs to Xstrata. There is scarcely any information about ROQ and its parent company, Ameropa; the most detailed part of their website praises the bold design of the headquarters, designed by the star architects Herzog & de Meuron.

15.2 //

'KAZAKHGATE', OR THE ART OF CORRUPTION

It always takes two to tango. The kleptocratic elite in resource-rich countries and the trading houses will reach an agreement more quickly when the deal is sweetened with a discrete 'allowance'. In this respect, 'Kazakhgate' has some symbolic value for Switzerland – in terms of the mechanisms, but also in terms of the result.

'GREASY' OIL CONCESSIONS

The date is April 2001. The authorities in Geneva have just received a request for mutual legal assistance (MLA) from the USA. The US authorities are trying to find out why the four oil companies ExxonMobil, Amoco, Texaco and ConocoPhillips recently transferred several million dollars to Switzerland. Specifically, 120 million dollars are now lodged in nine suspicious accounts with three banks, including Pictet and

Crédit Agricole Indosuez (CAI), which at that time was already frozen by the Geneva authorities. On 14 September 2001, the Federal Office of Justice passes a report to its American partner authorities about a bribery ring that had been built up in the 1990s by businessman James Giffen. This US citizen, welcomed in the circles of former Soviet rulers, paid Kazakh officials to ensure that they issued drilling licences to American oil companies. Amounts for 'legal costs' or 'geological studies' were first transferred to accounts that had been opened in the name of the Republic of Kazakhstan. From there, the bulk was diverted to the accounts of a Liechtenstein Foundation behind which hides Nursultan Nazarbayev, who in 1991 was elected President of Kazakhstan with a phenomenal 98.7 per cent of the vote and has ruled the country since with an iron fist. These transfers financed Nazarbayev's cash withdrawals on his travels or funded the school fees for his daughter at the Leysin American School located above Lake Geneva. The Kazakh Oil Minister, Giffen himself and Amoco also benefited from such transfers.[1]

This case is typical of a particular type of commodity exploitation. Kazakhstan is not only in first place for global uranium mining, this ninth largest country in the world by area also has huge gold, zinc, cobalt and copper mines. Gas reserves as well as the largest crude-oil deposits outside of Saudi Arabia were discovered here in the 1990s. But the extraction and sale of these riches benefit only a few people in this Central Asian state. While 17 per cent of the population still live below the poverty line, Nazarbayev and his clan control all the important sectors of the country's economy. International non-governmental organisations regularly denounce the regime for human rights violations[2] and in the corruption rankings produced by Transparency International, Kazakhstan occupied position 145 from a total of 180 countries in 2009.[3]

COMPLICITY AND SYMBOLIC POLITICS

Swiss financial service businesses provided the Kazakh authorities with all the means required for the discrete redirection of revenues from the sale of state-owned natural recourses to their own private accounts. The preliminary investigation, which opened in 1999 and led to the MLA request mentioned in the introduction, lifted just a corner of the veil that covers this decades-old method of aiding and abetting corruption. Hundreds of millions of dollars have been transferred by US companies to accounts in Geneva.[4] The Swiss investigating authorities have not even taken the briefest of looks at these, since they are regarded as government accounts, which enjoy immunity – even though the Kazakh Parliament was not informed about the existence of the accounts until years after they had been set up.

After many attempts to get the Federal Department of Foreign Affairs to conclude the preliminary investigation in Geneva, the Kazakh authorities and their Swiss lawyer Marc Bonnant still claim that the frozen accounts are government property. On 30 March 2003, Giffen is arrested in New York just as he is about to board the plane to Kazakhstan. But the case against him in the USA does not get off the ground because he refers to his contacts in the US intelligence services to claim that the authorities were not in the dark about his activities in Kazakhstan.[5] And indeed, the US authorities strive to reach an amicable settlement. Since the Nazarbayev regime is providing important logistical support in the 'fight against terrorism', the Bush administration adopts a conciliatory attitude towards him because of their Afghanistan campaign.

Against this background, the Swiss attempt to settle the affair pragmatically. As early as 2004 the federal authorities hint that they want a political agreement which would allow the funds frozen in Geneva to be released for the benefit of the Kazakh population.[6] On 2 May 2007, such an agreement is finally concluded between Switzerland, the Republic of Kazakhstan and the USA. Since then, Swiss-Kazakh relations have been all sunshine and roses; at the end of 2009 the Federation and the authorities in Kazakhstan signed an OECD model convention for the avoidance of double taxation. And a few months later Kazakhstan joined 'Helvetistan,' a group of countries most of which are in Central Asia, are represented by Switzerland at the International Monetary Fund and the World Bank. As the last symbolic gesture of the re-admittance of Kazakhstan into the international community, in 2010 the country is even asked to chair the Organization for Security and Cooperation in Europe (OSCE). In 2005, the OSCE was still censuring the poor compliance with democratic standards that had enabled Nazarbayev to secure his re-election with 91 per cent of the vote this time. In 2010, the US proceedings are also concluded – by a compromise settlement under which Giffen receives a 25 dollar fine. At the same time, all charges against Nazarbayev are dropped.

COMMERCIAL AGENCY INSTEAD OF NUMBERED ACCOUNT?

Since 1997, the Swiss Money Laundering Act has required Swiss banks to check the origin of all funds that they accept. Commodity trading is not subject to these provisions, however. CHAP. 16 In other words, Glencore & Co. can, without challenge, conclude deals with the very same dictators that are on the list of 'politically exposed persons', the list banks must be able to demonstrate they have used for vetting purposes. The example of Kazakhstan shows that the lack of transparency and the complexity of this sector and all that surrounds it practically invites the embezzlement of funds.

And it looks as if 'Kazakhgate' will not remain an isolated case. Since 2010, the Office of the Attorney General of Switzerland has been looking into a transfer of 600 million dollars by UBS to a trust account at Credit Suisse. One of the beneficiaries is Timur Kulibayev, the husband of one of Nazarbayev's daughters, whose wealth is estimated by *Forbes* at over a billion dollars. Kulibajew is suspected of having used a network of shell companies to launder money in Switzerland that he had embezzled as Director of the State pipeline operator KazTransOil from 2000 to 2005 and as Vice-Director of the state oil company KazMunaiGas (KMG). KMG also owns the Vector group, which in turn emerged from the Romanian Agency for Oil Sales. Today Vector sells oil and gas from Kazakhstan – namely through Vector Energy AG in Baar, a subsidiary of the KMG affiliate in Lugano. It would appear as if the rulers of this world have switched from opening numbered accounts in Swiss banks to establishing trading companies in Switzerland.

15.3 //

UZBEK CHILD LABOUR FOR THE GLOBAL COTTON BOOM

Since the autumn of 2010, the price of cotton has been breaking all records. As the world's sixth-largest producer and third-largest exporter of raw cotton, the autocratically ruled Uzbekistan is one of the major profiteers from the cotton boom.[1] But in this Central Asian former Soviet Republic, the sunny prospects are massively clouded by the use of millions of children in the cotton harvest. Despite this exploitation, common since the Stalin era, companies such as Winterthur-based Paul Reinhart AG, and ECOM Agroindustrial Corporation and Louis Dreyfus Commodities, who have subsidiaries in Switzerland, do profitable business with Uzbekistan.

In the 2006/07 harvest season, child labour was still involved in more than half of all raw cotton. All schools were closed in autumn, because more than two million children were sent for weeks to pick cotton in the fields. In addition, hundreds of thousands of Uzbek workers and university students are forced to do compulsory labour for the State. Over 90 per cent of Uzbek cotton is harvested by hand and, following the

Soviet model, all farmers and pickers have performance quotas imposed on them.[2]

RURAL SHREWDNESS AND OFFICIALS' TRICKS

In 2006 numerous international NGOs and trade unions called for a boycott of Uzbek cotton, a boycott that was observed by many but by no means all textile and supermarket chains. According to self-declarations, more than 25 companies today comply with this goal, among them C&A, Walmart, Levi Strauss, Tesco, Marks & Spencer, Nike, Gap and H&M.[3]

In 2008, increased international pressure persuaded Uzbekistan to sign the conventions of the International Labour Organization (ILO) on the minimum working age and the elimination of the worst forms of child labour.[4] The Government in Tashkent thus committed itself to periodically reporting on appropriate measures and progress.[5] The law against child labour introduced by President Islam Karimov in 2009 did not produce results until the following year, and its effects included not just the desired ones. In many districts, the enforced school holidays and government bus transport ceased. But the pressure on parents to consent to their children's forced labour continues. In addition, there is an increase in the number of soldiers who monitor the workers and keep away the curious, as well as attempts by farmers to conceal the employment of children by using guards and alarm systems. Still unchanged, university students and workers from other sectors are required to pick cotton. More recently, mosques have also become recruiting centres; after prayers, Imams extend the call to pick cotton.[6]

The steep rise in the global market price of cotton brings enormous profit margins to the State companies, which have an export monopoly – especially since price fixing by the Government means that farmers receive only 10 to 33 per cent of the market price. For their work in the fields, the children get on average just 2.6 per cent of the market price.[7] There is not the slightest problem in selling the 'white gold' that accounts for 60 per cent of Uzbekistan's export revenues; in 2010, almost the entire annual harvest was sold in advance.[8] Quite remarkable for a product that is still confronting calls for an international boycott.

THE SILENCE OF THE TRADERS

Uzprommashimpeks, one of the most important Uzbek cotton dealers, has had a subsidiary in Altendorf in the Canton of Schwyz since August 1995, whose management included several people close to the Karimov regime.[9] Its customers include Paul Reinhart AG, ECOM Agroindustrial Corporation and Louis Dreyfus Commodities.[10] At the end of 2010, the European Centre for Constitutional and Human Rights (ECCHR) submitted a complaint against these three companies for violation of the OECD guidelines for multinational companies. It accused them of continuing to buy cotton from Uzbekistan, although it has been proven that the Government promotes, or at least allows, child labour and knowingly benefits from it. The complaints are part of a broad civic campaign against child labour in Uzbekistan, which targets many more European companies.

Industry leader Dreyfus saw no need to make any response, not even after requests from the ECCHR and the media. ECOM's response was to claim simply that a trade boycott would only harm the Uzbek people.[11] Reinhart gave the most extensive responses to media enquiries and at first denied any connection with Uzprommashimpeks.[12] Reinhart claims that were it to stop buying Uzbek cotton, this would have no impact on the situation because it buys less than 5 per cent of the Uzbek harvest. For the 2010/11 season, which yielded more than one million tonnes, that would still amount to more than 50 000 tonnes. Of the more than 300 companies that met at the annual cotton fair in Tashkent in 2010, Paul Reinhart AG therefore remains one of the largest purchasers. The Winterthur-based company operates its own 'Representative Office' throughout the year in Uzbekistan's capital. "Should trade with Uzbekistan or any other country be prohibited under Swiss law some day, we would of course comply with the law," according to Paul Reinhart AG.[13] But today it is not enough for a Swiss company to evade its social responsibilities by simply claiming that it is abiding by the law in a country whose laws clearly do not prevent the violation of basic human rights.

15.4 //

THE UN IN IRAQ: 'OIL FOR FOOD' MEANS 'CASH FOR SADDAM'

In 1996, with its large-scale 'Oil for Food' aid programme, the United Nations launched an attempt to alleviate the dramatic effects of international sanctions on the Iraqi civilian population. On the one hand, the UN allowed the regime to generate additional financial resources from oil exports, and on the other hand it specified how this money was to be used. First and foremost, Iraq had to buy humanitarian goods with the money, and secondly it also had to pay compensation (to Kuwait, for example).

Although Iraq did indeed buy humanitarian goods with the oil revenues, in secret Saddam Hussein and his leadership circle soon found ways and means to fill their own coffers at the same time. In 2004, when the scandal emerged, the UN established the Independent Inquiry Committee (IIC) consisting of Paul Volcker, Richard Goldstone, and Mark Pieth CHAP. 16. The committee painstakingly investigated the regime's frauds and the companies involved. The Swiss oil-trading business played an especially important role in this affair.

BRIBES ARE CALLED 'ILLEGAL SURCHARGES' HERE

From the end of 1996 to the summer of 2003 as part of the Oil for Food programme, Iraq sold to various companies crude oil worth 64.2 billion dollars.[1] In Autumn 2000, the Iraqi Oil Ministry announced to buyers that, with immediate effect, they were required to pay a 'surcharge', bypassing the UN and paying it directly into Iraqi accounts. Despite this additional 10 to 30 cents a barrel, Iraqi oil was still attractively priced. But as a result, the direct customers now had to set their resale price at a level that was suspiciously higher than the official UN price for Iraqi oil. According to the *Wall Street Journal,* a markup of only 1 to 5 cents a barrel was the market norm.[2] The oil market therefore knew immediately what was going on. The UN responded on 15 December 2000 and by fax explicitly warned oil buyers against making such illegal payments,[3] with the consequence that most established customers withdrew from the Iraqi market.

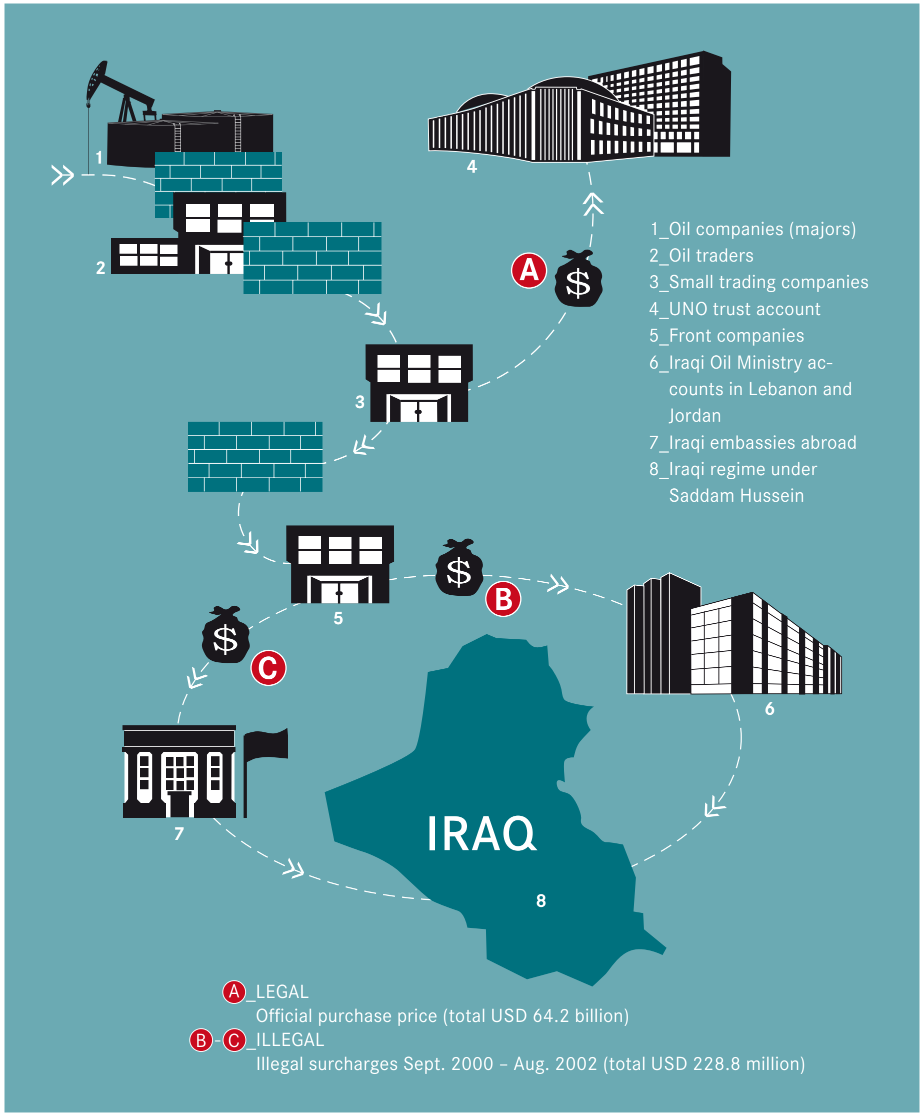
What then happened is typical of the commodity business. When a political situation becomes too precarious, the curtain closes, the stage is quickly rearranged, and shortly thereafter the actors reappear before the audience in new roles. While renowned oil companies bowed out from Iraq, traders who were willing to take a risk scented their opportunity. In the first half of 2001, four companies that previously had scarcely been involved suddenly made over 60 per cent of the oil purchases; the American companies Bayoil and Taurus Petroleum plus the Swiss Vitol SA and Glencore.[4]

Of course, they too were anxious to incorporate legal safeguards and operational firewalls. For the purchase of the oil, and particularly for the sensitive transfer of the bribes to Saddam Hussein and his entourage, small companies, often specially founded for the purpose, were put forward FIG. 1.

Of the 248 oil companies that officially took part in the 'Oil for Food' programme between 1996 and 2003, 139 paid bribes amounting to a total of 229 million dollars. And Swiss traders played a dominant role. Based on the result of the IIC's investigations, it is possible to conclude

FIG. 1

ILLEGAL FLOWS OF MONEY IN OIL TRADING UNDER 'OIL FOR FOOD' WITH BUILT-IN 'FIREWALLS'



Source: authors' illustration (data based on IIC 2005)

that Glencore made about 12 per cent of these direct and indirect payments. The same analysis suggests that Vitol, Glencore, Trafigura and countless other smaller Swiss firms had their hands in 24 to 33 per cent of all illegal oil surcharges. In addition, the above-mentioned Taurus Petroleum, which is US-owned but since 2003 has also traded through Geneva, was alone involved in about 14 per cent of the illegal payments.[5] The US Senate further estimates that half of the oil that filled Saddam's war chest ended up with the 'majors', i.e. the large US oil companies.[6]

MANY ROADS LEAD TO SADDAM'S ACCOUNTS

Most companies paid the bribes in tranches via intermediaries to Iraqi accounts in Lebanon and Jordan. According to the IIC, however, Glencore sometimes used a method that was really more suited to Hollywood. On various occasions, a man named Murtaza Lakhani would act as a money courier. For example, on 15 May 2002 this messenger received 415 000 dollars in cash from Glencore, a fact supported by an official receipt. Two days later Lakhani drove to the Iraqi Embassy in Geneva with 400,000 dollars in his briefcase.[7] And yet, Group spokeswoman Lotti Grenacher maintained in 2005 that, "Glencore has made no illegal payments whatsoever to representatives of the Iraqi Government."[8] According to publicly available information, it would seem that the Zug-based giant has in fact never been held to account for this by the judiciary.

Trafigura, on the other hand, probably bought only a few shipments with surcharges, but was involved in a smuggling scandal with Iraqi oil that pumped 8.3 million dollars into the regime's kitty. The trade was exposed by the captain of the 'Essex', a ship that twice in 2001 had taken on illegal extra cargo. This additional oil was not reported to the UN and the full purchase price made its way not to the UN trust account but through front companies directly into Iraqi accounts.[9] While Trafigura likes to portray itself as the unsuspecting victim of the criminal machinations of its partner firm Ibex Energy and the Iraqi authorities, the IIC concluded that Trafigura set up the deal in Baghdad to compensate itself for losses in Iraqi business in 1999. Before the case came to court in the Netherlands, Trafigura concluded a compromise settlement in the State of Texas in 2006 and pleaded guilty to the 'false declaration'. This step cost the company 19.7 million dollars, but saved it further legal involvement and negative publicity.[10]

THREE-POINT PROGRAMME FOR IMPUNITY

There are striking parallels between Trafigura's behaviour in Iraq and its 'crude' business model CHAP. 10 where, the company shifted its responsibility onto a small firm and ignored all the warning lights. Both cases exemplify how, in the hard life of the trader, legal grey areas are made profitable and at the same time legal risks are minimised. Like this:

- Safeguard clauses: According to the IIC, many traders reacted to the Iraqi surcharge with a contractual clause that committed the intermediaries to buy Iraqi oil only without illegal payments. "This was done notwithstanding the near-universal market recognition that Iraqi oil could not be purchased [anymore] without payment of a surcharge." [11]

- Intermediaries: High mobility of corporate parts and nested holding structures do not just work miracles in the face of tax authorities CHAP. 14, they also provide protection against potential complainants and inquisitive public prosecutors' offices. 'The devil takes the hindmost', which is why in risky business an intermediary, a front company or a naive business partner is incorporated at the bottom of the (corrupt) food chain. With the 'lizard technique', this tail can be quickly uncoupled in an emergency.

- PR or settlement: At first, everything is denied in principle. In the unlikely event that even the most professional PR apparatus and the best law firms cannot prevent an investigation from getting under way, there still remains the much-favoured option of reaching a compromise settlement. In this way, the case – including any explosive details – remains under wraps and any parallel court cases are usually concluded as well.

But there is no rule without an exception. In 2005 the oil trader Vitol, in response to the IIC, stressed that it had never knowingly made any illegal payments. But in fact the UN Committee of Inquiry could prove that Vitol had made a direct payment to the Iraqi Oil Ministry's account. In 2007 Vitol finally pleaded guilty before a New York Court to having paid Saddam's regime 'surcharges' amounting to 13 million dollars.[12]

INTERVIEW //

"Why are foreign exchange dealers subjected to very strict scrutiny, but not commodity traders? Is the underlying reason plain carelessness or political will?" asks Mark Pieth, Professor of Criminal Law.

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"COMMODITY TRADING INVOLVES CONSIDERABLE RISKS FOR SWITZERLAND": PROFESSOR MARK PIETH IN CONVERSATION

Renowned professor in Criminal Law, Mark Pieth, is internationally one of the most-quoted Swiss experts on subjects such as tax policy, bank secrecy, corruption and commodity trading. Pieth is Professor at Basel University and has been Chairman of the OECD Working Group on Bribery in International Business Transactions since 1990. In 2004 he was also appointed to the UN Independent Inquiry Committee into the Iraq Oil-for-Food Programme.

— Berne Declaration (BD): Mr Pieth, is the commodity sector a business just like any other?

Mark Pieth: Of course not. Commodities are precarious and therefore hard-fought goods. This applies to inorganic commodities, such as fossil fuels, due to their finite nature, and organic commodities, such

Prof. Mark Pieth

as foodstuffs, due to their importance for our survival, and their unjust distribution. Anyone who owns natural resources wields great power …

— … as does anyone who trades them. A substantial share of the global movement of commodities is controlled from Zug and Geneva.

Switzerland is a country where the lack of raw materials contrasts grotesquely with the plethora of middlemen trading them.

— Are the commodity companies located here political players?

All large transnational companies have and exert political influence. However, globally operating commodity companies feature particularly prominently in the North-South debate and are so powerful that they can control entire extraction regions and overrule governments. Therefore countries like Switzerland, where many of the companies that often decide the fate of developing countries have their headquarters, bear a corresponding degree of responsibility.

— What makes Switzerland so attractive to this branch of the economy?

The combination of low corporate taxes, including many cantonal special rules, and a financial centre that is as healthy as it is liberal. In addition, there are the advantages of social stability and quality of life. However, what played a decisive role in Switzerland's ability to outstrip even London as a commodity hub was bank secrecy and the tendency towards very little regulation found in our national policies. Even today policy makers in Berne do not see the problems this area brings.

— Stricter rules in Switzerland might indeed prompt Glencore, Vitol und Co. to migrate to the Channel or South Sea Islands, which have even lower taxes and much better kept banking secrets.

No, a commodity trading centre can only originate and thrive somewhere where a large, traditional financial centre already exists. There may be better financial boundary conditions in more exotic climes, but you are forced to live in fear of your hard-earned cash being stolen from you there. The only place that could be considered as an alternative location at some time or other would be Singapore, where the banking laws were radically liberalised ten years ago.

— Does Switzerland profit from its status as a commodity hub?

Today our country is internationally important as the financial centre and location of many global players in strategically significant industries, such as chemicals and foodstuffs. The commodity business done here gives Switzerland a further opportunity to remain on the geostrategic map despite its lack of G20 membership and problems with the IMF. The question is, whether the politicians responsible are even aware of this, whether, in fact, 'Switzerland' as a single entity even exists in this respect. My impression is that for a long time now things have just been left to take their own course – that there is neither a plan nor a purpose. This was the case with issues, such as looted art, the arms trade, embargo breaches or, most recently, tax avoidance, and could well be no different with the commodity trade.

— What we need therefore is a central authority, which plans ahead and maintains strategic control …

… enabling Switzerland to recognise and resolve controversial issues before being pressured to do so from outside. It is true foreign criticism is often motivated by envy and the politics of naked self-interest. However, I cannot see any signs of policies on the part of the Swiss, which would enable them to protect their own interests, by countering such attacks and actively using their booming commodity industry to their own advantage.

— Who would be responsible for this kind of political issue management?

A centre of power that not only formulates but also implements a strict Swiss foreign policy. Instead, what we have is a government committee adorned by seven dwarfs, which so far has been neither able nor willing to do anything to combat the image of Switzerland as a pirate haven. Yet the commodity trade is not intrinsically bad. In its present form, however, it involves huge risks for Switzerland's reputation.

__ What are the levers that could reduce these risks?

In my view, first and foremost the middlemen must at last be forced to comply with the Money Laundering Act. Although this has been the case since 1999 in theory, the Anti-Money Laundering Control Authority has developed a problematic practice that I consider illegal. According to Article 2, paragraph 3c, the financial intermediaries falling under the Federal Anti-Money Laundering Act are quite clearly 'also persons who trade for their own account or for the account of others precious metals, commodity as well as their derivatives'.

__ If it is so unambiguously formulated, why then is this paragraph not enforced?

One of the reasons is because at the time Glencore threatened to relocate its headquarters if it were. The instructions issued by the then Director of the Federal Finance Administration, Peter Siegenthaler, and the chief counsellor of the Federal Department of Finance could well have been the main reason behind the customary interpretation of this article that persists until today. The question is, why are foreign exchange dealers subjected to very strict scrutiny, but not commodity traders? Is the underlying reason plain carelessness or political will? Just how important it is to identify the customers and impose a duty to report them when carrying out commodity transactions, I realised when investigating breaches of the UN Oil-for-Food programme. At the time dossiers for banks turned up with stamps bearing words such as 'the name of Marc Rich is not to appear on any transmission to BNP New York'.

__ Which brings us to the corruption that is so much a part of this business.

In order to stay in the market, those involved are forced to pay commissions – for anything from acquiring licences and mining to trading. Even the leaders of the commodity companies located here would

probably confirm this to you. However, they do not see it as corruption if, for example in the oil trade, someone is paid five to ten per cent of the value of the goods just so that these goods can be bought later on.

__ The illegal premium demanded by Saddam Hussein's regime during Oil-for-Food was roughly this amount too.

Indeed, Iraq continued to maintain a tariff typical for the industry. The problem is not that there are intermediaries and that they charge for their services via price mark-ups. The problem is that compensation for these services is processed through lump-sum payments. Nonetheless, nowadays many tax authorities are inclined to reject anything over five per cent of a product's market value.

__ Does that mean that expenditure on corruption is officially declared for tax purposes in Switzerland?

Well, not directly. Although bribes have not been considered allowable expenses since the year 2000, they have certainly been vaguely defined as 'agent's fees'. Switzerland could lern from France where the tax authorities interpret any payment over five per cent as indicative of corruption and reverse the burden of proof.

__ Are there any other regulatory loopholes in the Swiss financial sector?

In the Oil-for-Food scandal the banks themselves flouted the most elementary rules of due diligence in banking law. No one knows and no one checks whether the same financial institutions actually implement the declarations required for letters of credit today. I can well imagine they clearly identify their customers and look closely at individual transactions. Whether they understand the – possibly hidden – motives behind often highly complex transactions, however, is open to question. This is the very point at which the door is left ajar for abuses.

Another way of solving the problem would be to harmonise or completely do away with the cantonal tax privileges for companies.

Measures aimed at this would probably curb tax competition within Switzerland but not solve the main problem of concessions for holding companies. In the end effective regulations for the global commodity industry can only be implemented if the other major trading hubs are on board. What we need is an internationally coordinated commodity task force that creates a level playing field for all the players. I believe that the industry itself would be interested in an end to distortions as regards tax and competition.

Returning to the topic of the Anti-Money Laundering Act, which is your preferred lever. What will it take to make the authorities apply the current law to commodity traders as well?

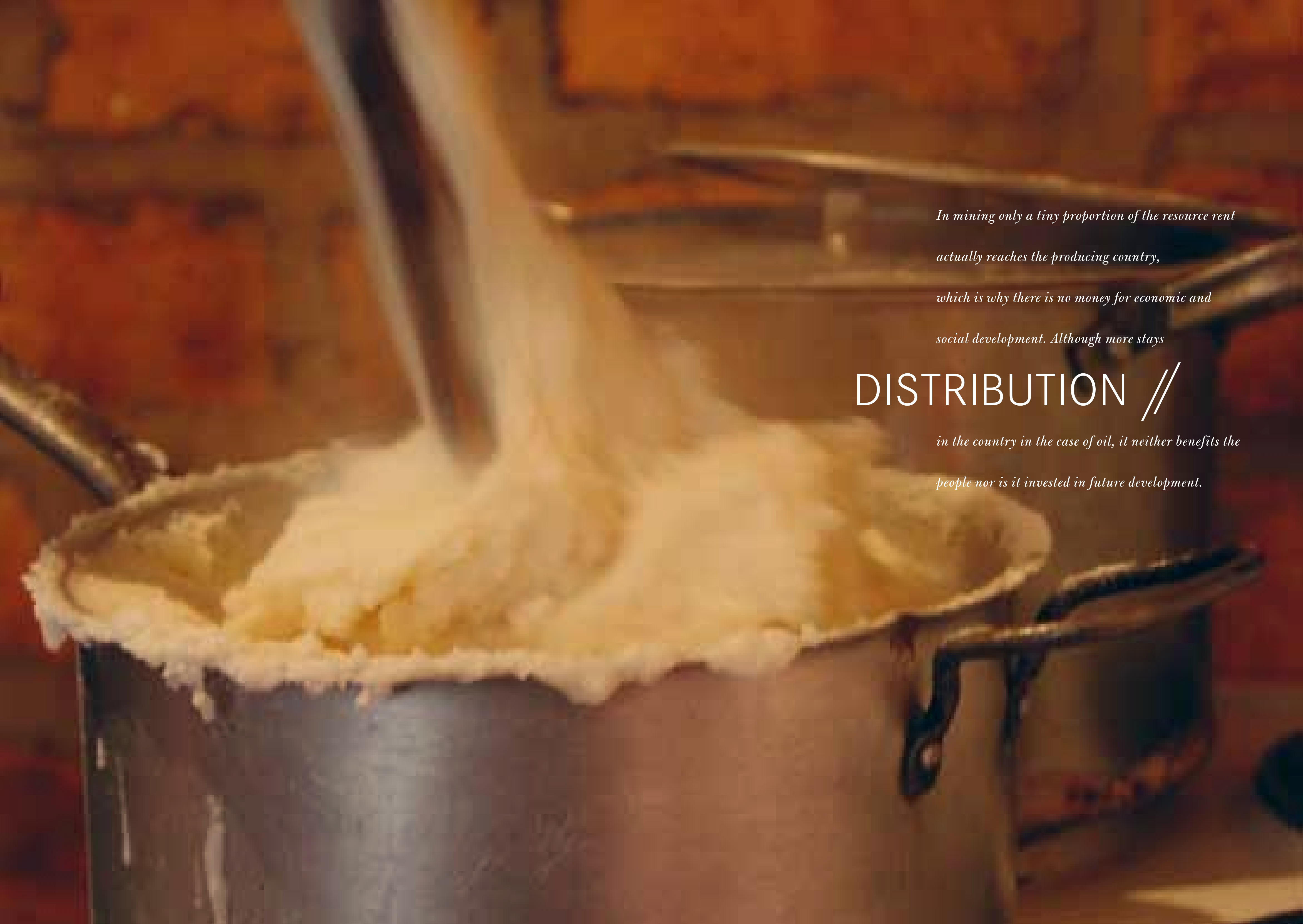
International pressure. Current practice is politically motivated and can therefore only be revised politically. In another context, there would be no problem with applying the recommendations of the Financial Action Task Force on Money Laundering, an international initiative launched by what was then the G7 and now supported by the OECD states, to the commodity players as well. Perhaps even more could be achieved by implementing these recommendations step by step than by revising the Anti-Money Laundering Act.

Commodity traders generally consider ethical behaviour as a competitive disadvantage. Do you share this view?

No, this important sector is simply in a period of transition. Other industries have been showing the way forward for a long time now. For example, Siemens learned a great deal from its costly corruption scandal and has now gone on the offensive as the cleanest energy and industrial company in the world (a strategy that pays off financially apparently). Moreover, there will soon be examples of best practice such as this in the commodity sector as well, in all likelihood first from the producers and then at some point from the traders. Pressure from non-governmental organisations plays an important role here. This process is being accelerated by an increasing number of institutional investors, who value the verifiable achievement of minimum environmental and social standards – not merely in order to minimise risks but also for ethical reasons. This will give even the most die-hard managers in Geneva and Zug something to think about.

Is this not wishful thinking? All the major investors who queued up for Glencore's stock exchange flotation did not appear to have any ethical concerns.

I see it differently. Even in the defence sector, which is itself none too squeamish either, companies are having to put up with increasingly uncomfortable questions, especially from institutional investors. And arms are surely no less controversial than commodities.



DISTRIBUTION //

In mining only a tiny proportion of the resource rent actually reaches the producing country, which is why there is no money for economic and social development. Although more stays in the country in the case of oil, it neither benefits the people nor is it invested in future development.

17 //

UNREGAL 'ROYALTIES': RESOURCE CURSE AND DISTRIBUTION ISSUE

The fate of many developing countries shows that a wealth of natural resources does not guarantee economic development. All too often rich raw materials reserves turn out to be more of a curse to their 'natural' owners; instead, the country and its people remain trapped in poverty and misery. The following analysis of the reasons for this 'Paradox of Plenty' combines two complementary dimensions of the same distribution problem: on the one hand, the sharing of resource revenues between countries and foreign commodity companies and, on the other, their domestic distribution between the governments and the inhabitants in the resource-rich countries. The extraction of raw materials will only be fair and contribute to development if the balance of power in both areas alters: the producing countries need to receive a higher proportion of the revenues generated from the sale of commodities and these revenues need to be invested in economic and social development and towards combating poverty so that their populations may benefit from them. Fair distribution between the companies and the state is a necessary, but far from sufficient, condition to ensure that the people profit from the proceeds of the extraction of raw materials. Only if their natural resource wealth is properly distributed between a country's political elite and the inhabitants will the broad masses be able to enjoy it.

Depending on the focus of the analysis, the two dimensions of fairness can be allocated to individual groups of commodities. As regards ores and metals it is mainly the distribution of revenues between companies and governments that is the problem, whereas in the case of energy (in particular oil) that between governments and the poor majority. A glance at TAB. 1 illustrates this. Whereas the proceeds from oil exports usually make up the major part of the incomes of producing countries, ores and metals usually contribute little to these.

AGRICULTURAL COMMODITIES: A SPECIAL CASE

Agricultural commodities are not included in this analysis. They are a class apart because they are cultivated rather than mined, i.e. renewable, and therefore resource rents are not relevant. This certainly does not mean there are no problems with grains, cocoa and cotton; they are just in a different league. Increasing speculation in commodities and the financial products derived from them is a feature of other sectors besides agriculture CHAP. 13. However, in the latter it can be a factor that threatens food security directly and therefore the basic human right to food. This is particularly true in situations in which powerful commodity traders speculate with staple foods, as the case of Glencore and the Russian ban on wheat exports illustrates. Besides speculation, another problem with many agricultural products is the growing market power of just a few players, including the commodity traders. It is the result of increasing vertical integration, which is the current growth strategy of many agricultural companies CHAP. 12. In the interaction between the components of the typical structure of agricultural markets – just a few traders confronting millions of producers and/or consumers in the buying and selling processes – there is a very real danger that this market power will be abused.[1]

The fact that fossil fuels are much more important to the economy of the countries of origin than minerals or agricultural goods relates to the huge volumes extracted and their high prices. Another explanation for this difference is the fact that the share of the revenues remaining in the country is significantly smaller in the case of minerals. Partly to blame for this are mining laws that strongly favour investors. This is why the producing countries profited far too little from the price boom between 2003 and 2008 and from 2010 onwards (the financial crisis occurred in between).

THE STATE/COMPANIES: HAGGLING OVER RESOURCE RENTS

In times of rising commodity prices, the difference between the value of the commodities and the cost of their exploration and extraction increases. This difference is referred to as resource rent. Since the raw materials in the ground belong to the respective country as a rule (the exception is the USA where they can belong to private-property owners) and they are mined by private companies, the rents are shared between the state and the companies. The state takes its share in the form of duties and taxes, the remainder constitutes the profit of the mining company concerned. Those who do not get a share of the rents on the other hand are the local communities and people affected. These affected communities suffer directly from this resource exploitation, i.e. the use of the land, resettlement and pollution of the water supplies and the air, for which they usually receive no compensation from either the companies or the state. For indigenous communities, who are very closely tied to their land and the natural environment, the arrival of giant diggers and bulldozers can even mean an end to their culture.

TAB. 1

INCOME FROM RAW MATERIALS EXTRACTION*

Hydrocarbons (Oil, natural gas, coal)		Minerals (precious stones, ores and metals)	
Iraq	97	Botswana (diamonds)	44
Oman	83	Guinea (bauxite/aluminium)	19
Kuwait	79	Chile (copper)	12
Nigeria	78	Mongolia (copper, gold)	9
Equatorial Guinea	77	Liberia (iron ore, gold)	8
Libya	77	Namibia (diamonds)	8
Angola	76	Peru (gold, copper, silver)	5
Bahrain	74	South Africa (gold, platinum)	2
Democratic Republic of Congo	73	Zambia (copper)	1**
Algeria	72	Jordan (phosphate)	1
Yemen	72	Sierra Leone (diamonds/bauxite)	1
Saudi Arabia	72		
East Timor	70		
United Arab Emirates	69		
Qatar	68		
Iran	65		
Azerbaijan	59		
Sudan	50		
Venezuela	48		
Turkmenistan	46		
Syria	39		
Trinidad and Tobago	38		
Sao Tome and Principe	35		
Mexico	34		
Vietnam	31		
Cameroon	27		
Kazakhstan	27		
Chad	27		
Indonesia	26		
Norway	26		
Ecuador	25		
Bolivia	24		
Russia	22		
Papua New Guinea	21		
Mauritania	11		
Gabon	10		
Colombia	10		

**Average between 2000 and 2007, in per cent of state revenues*

*** 2% was forecast for 2010[2]*

Source: Boadway et al. 2010

The contribution of natural resource wealth to a nation's development is almost entirely limited to the share of the resource rents allocated to the state (and only then if this is invested in development). Although mining in the 21st century can be very capital-intensive due to expensive production machinery, it requires a relatively small labour force. Even in a country with a large mining sector, such as South Africa, only one to three per cent of the labour force work in this sector, depending on the method of calculation.[3] Elsewhere in Africa, where industrially operated mines replace individual small-scale mines, mining has a negative effect on the labour market. For example, in Tanzania about 400,000 people are estimated to have lost their jobs in gold mines.[4] Moreover, machines and tools are usually imported from the industrial countries. There is little economic interdependence between mining and other sectors: mining rarely stimulates development, except perhaps in some areas of infrastructure. Also, the mining companies make minimal direct payments and provide minimal services to the local communities who are directly affected by their activities.

OIL: FROM CONCESSIONS AND ROYALTIES TO SPECIAL TAXES

Governments and companies have been wrangling over their shares of the rents for oil for over 100 years. However different the actual contracts may look, the vital ingredients are always the same: royalties, taxes, and contracts for the distribution of products and services. The concept of royalties dates from the Middle Ages when countries were ruled by royalty and the British crown (royalty) demanded rents for the use of its land. In today's commodity business, royalties are fixed payments to the state based on a per centage of production or sale value. Consequently, they do not depend on profit and become due from the moment the oil first flows. They differ from taxes that assume a company is recording a profit, which is not always the case, particularly at the start of production or given aggressive tax avoidance CHAP. 14. Under Production Sharing Contracts a private company only gets part of the oil produced; the rest goes to a state-owned oil company. Finally, under Service Contracts all the oil goes to a state-run oil company and the private oil company concerned is compensated for the services it provides. These four rent categories are explained in greater detail below.

The first agreements regulating the distribution of oil revenues between a state and companies were known as concessions. Companies paid royalties and taxes and in return obtained the right to look for and extract oil in a certain region for a certain length of time. An extreme example is the concession given by the Shah of Persia to the English lawyer, William Knox D'Arcy, in 1901: it involved three-quarters of Persia's geographical area and a period of more than 60 years. D'Arcy paid 40,000 pounds in cash and shares and the Shah received 16 per cent of the annual 'net profit' (exactly what this meant turned out to be highly controversial). The discovery of oil in 1909 led to the founding of the Anglo-Persian Oil Company for further production, which was renamed the Anglo-Iranian Oil Company in 1935 and became the British Petroleum Company in 1954 – BP today. These concessions gave the company sole control over Persian oil. The company could decide independently whether to develop new oilfields and it could control how much oil to extract.[5]

From the Second World War onwards the oil-rich countries made greater efforts to (re)gain control over oil production. Concessions were divided up into individual geographical blocks and deliberately granted to rival companies. The length of the contracts was cut substantially and the concessionaires lost their rights if they failed to start production in their blocks within a certain period of time. The state's share of the revenues also increased. Nowadays royalties amount to 10 and 15 per cent in most countries and the taxes on profits are usually between 25 and 35 per cent. Most countries allow companies to write off the costs of exploration and development in the first (often five) years, which means companies do not record any profits during this time and do not pay any taxes as a result.

SOVEREIGNTY OR PROFITABILITY?

In addition many countries impose a special petroleum tax to boost their resource rents. This is due when a company has covered its costs and achieved a fixed level of profitability. Furthermore, bonus payments are demanded occasionally by governments, for example when a new oilfield is discovered or a certain production volume is achieved. If the rates in question are high enough, the combination of royalties and taxes can prove very lucrative. For example, Norway has secured a handsome 78 per cent of revenues earned from its oil and the UK's share was as much as 87 per cent at the beginning of the 1980s.

High revenues notwithstanding, some countries still consider on principle concessions to be incompatible with their national sovereignty. As a result they have been trying to shift the balance of power further in their favour since the 1960s, by means of what are known as Production Sharing Contracts (PSC) or Service Contracts. Both types of contracts have one thing in common: the state retains ownership of the oil produced and compensates the private company for the use of its services. In Saudi Arabia, Kuwait and Mexico almost all the oil reserves are under the sole ownership of state enterprises.

In practice, under a PSC production is divided into two categories known as 'cost oil' and 'profit oil'. The company receives the former to cover its exploration and development costs, while the private and state-run companies each divide the latter between them according to a contractually agreed formula. In a pure Service Contract, the service provider receives compensation in the form of cash or oil. In any event, production is wholly controlled by the state or rather its oil company. In this case the state's share of the total profit from an oilfield can amount to as much as 97 per cent.[6]

SWITZERLAND'S DUPLICITY OVER EXPORT DUTIES

Imposing export duties can help a producing country to ensure it receives appropriate returns on its natural resources. The International Monetary Fund (IMF) estimates that the royalties, taxes on profit and other payments required from the commodity industry are significantly more important to a country's development than its positive effect on the domestic economy. The IMF also mentions export duties on natural resources explicitly, which enable governments to finance key public services for development and for combating poverty.[7] The IMF intends that its Topical Trust Fund on Managing Natural Resource Wealth should support those resource-rich countries in their efforts in this regard. The most important contributor is Switzerland, which has given five million dollars to this initiative.

Elsewhere Switzerland is at the same time a vociferous opponent of export duties on natural resources. Vietnam, for example, imposes these duties on certain minerals and natural resources. In the 2011 feasibility study on a bilateral free trade agreement with Vietnam, Switzerland has explicitly demanded (via EFTA) a general ban on such export duties.[8]

MINING: FATAL LOCAL POLITICS, WASTED BOOM

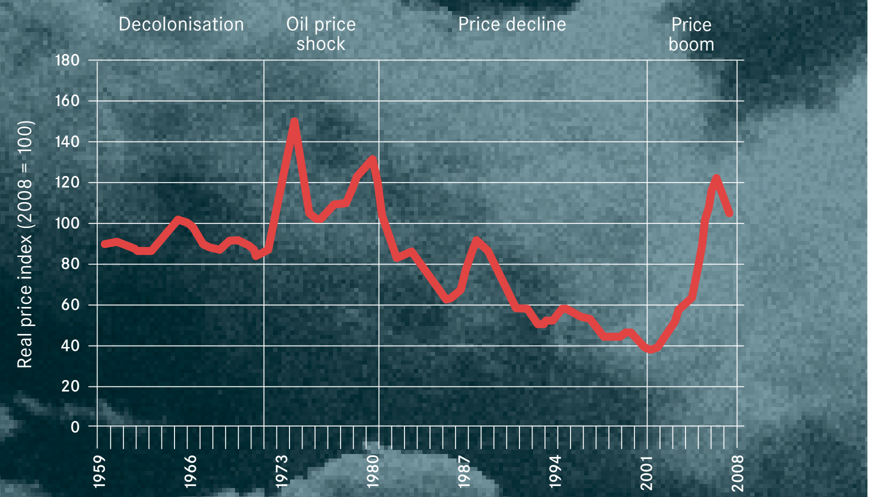
Many mining products come from the southern hemisphere: 60 per cent of all the ores (or concentrates) are mined in developing countries.[9] In the first half of the last century concessions were also granted for mining as a rule. After the Second World War the former colonies in Asia and Africa became independent and many of these newly independent countries nationalised their mining industries, for example Bolivia (zinc), Jamaica (bauxite), Zambia (copper), the Democratic Republic of Congo (copper) and Ghana (gold).

Where mines remained privately owned, it became usual to impose a combination of royalties and taxes. Following the oil price shock in 1973 the prices of the other commodities shot up too, as illustrated in FIG. 1. Many countries seized the opportunity to impose additional taxes and duties to ensure they received higher resource rents. In addition, processing (of ores into metals mainly) was supported by the state in order to secure a higher share of the added value for the country concerned.[10]

In the 1980s a deep recession in the industrial countries and debt crises in the developing countries caused a sharp drop in demand and the price of commodities fell. After the collapse of the Soviet Union,

FIG. 1

ORE AND METAL PRICE FLUCTUATIONS*



*Average for aluminium, copper, gold, iron ore, nickel, uranium, tin, zinc

Source: Hogan et al. 2010

the prices of mineral commodities fell further in the 1990s as demand declined and commodities from the former Eastern bloc flooded world markets at the same time.

During this long period of decreasing revenues many of the previous nationalisations and tax increases were reversed, often under pressure from the International Monetary Fund and as part of what was called Structural Adjustment Programmes designed to ensure interest and debts were paid. The World Bank advised over 100 developing countries on reforms to deregulate the extractive sector. The recipe was everywhere the same: state-owned companies were privatised, the conditions for foreign companies greatly improved and taxes cut drastically TAB. 2.[11]

Mining royalties were reduced or even suspended (Chile, Peru) in many cases. At between zero and six per cent today, royalties for mining are much less than those for oil; only for diamonds and other precious stones do the royalties reach ten per cent. In some countries, notably in Africa, companies can negotiate special provisions for particular mining projects. For example, Zambia accepted royalties of 0.6 per cent from Glencore for the Mopani copper mine – a fifth of the official three per cent CHAP. 6. The conditions were even more extreme in Congo where in 2007 a commission of inquiry discovered that none of the agreements with mining companies that were analysed met the statutory requirements. In reality, by bribing politicians foreign companies had achieved complete exemption from royalties and taxes on profits.[12]

As a result the state's mining revenues fell sharply. Zambia produced as much copper in 1992 as it did in 2004; in the same period the price per tonne rose from 2,280 dollars to 2,868 dollars. Yet in 2004 Zambia received only a miserly eight million dollars in taxes, less than five per cent of the tax revenue received in 1992 (200 million).[13]

Given this background, it is not surprising that the Tanzanian minister for mining concluded, "The surge in price for gold and other precious metals has not been felt in our economies."[14] The tragic irony of this unfortunate development lies in the fact that the prolonged price slump in the commodity business tempted the producing countries to pass extremely investor-friendly mining laws. As a result of these

TAB. 2

MINING CORPORATE INCOME TAX RATES (IN PER CENT)

	1983	1991	2008
Chile	50	35	35
Indonesia	45	35	35
Mexico	42	35	28
Papua New Guinea	36.5	35	30
South Africa	46 (55 for gold)	50 (69 for gold)	28
Zambia	45	45	30

Source: Hogan et al. 2010

attractive local policies, they then lost billions following the price hikes just a few years later and the enticements for the foreign companies were not even necessary. Unlike say an automotive company, a commodity company cannot simply seek out the best investment conditions; it has to go where there are cost-effective mining deposits.

Consequently, the developing countries have made hardly any profit from the commodity boom since the turn of the century. A comparison between the limited increase (or decrease in the case of South Africa) in the natural resources revenues of the producing countries and the revenues of major mining companies shows just who has profited from the huge rise on volume and price TAB. 3.

TAB. 3

INCREASE IN STATE REVENUES VS COMPANY REVENUES

Country/ Company	**Commodity**	**% change in absolute government revenue from extractives, 2002–2004/5**	**Increase in gross profit 2002–2004/5**	**Increase in net profit 2002–2004/5**
Ghana	Gold	30 %		
South Africa	Gold, nickel, platinum	-62%		
Tanzania	Gold	40%		
Zambia	Copper	1.7%		
BHP Billiton	Copper, nickel		211 %	251 %
Glencore	Copper, coal, nickel, tin, zinc		319 %	403 %
Inco	Nickel		163 %	243 %
Newmont Mining	Gold		392 %	282 %
Rio Tinto	Copper		458 %	812 %

Source: Christian Aid 2007; Glencore annual reports

BOTSWANA AND BOLIVIA: FUTURE-ORIENTED PARTNERSHIPS AND SPECIAL TAXES

That it can all be done very differently is evident in the example of Botswana. The landlocked South African country has a very scarce and therefore coveted and expensive resource: diamonds. The role of conflict diamonds in financing the civil war in Sierra Leone is a striking example of how these precious stones can reduce a country to corruption, devastation and death.

Between the years 2000 and 2007 diamonds contributed 70 per cent of Botswana's export earnings and 44 per cent of the state's revenues. Since their discovery in the 1960s they have been produced by Debswana, a company jointly owned by De Beers and the government of Botswana, who each hold a 50 per cent stake. The state's earnings from diamond production are made up of royalties (10%), profits taxes (35%) and the dividends that Debswana distributes. In addition, Botswana owns 15 per cent of the shares in the parent company, De Beers, whereby it again profits from the diamond business.[15]

On the other hand, Bolivia demonstrates how gifts given in desperation to commodity companies can be taken back. Like many other countries the Andean country privatised its state-run oil business in 1996. At the same time the royalties from new oil and gas fields were reduced from 50 to 18 per cent and the profits tax to 25 per cent. Following a huge outcry that led to the resignation of President Gonzalo Sánchez de Lozada who was responsible for the privatisation, the Bolivian government passed a new law in May 2005. Because the existing contracts precluded an increase in the royalties, a special tax at 32 per cent was introduced. The bottom line was that Bolivia regained the revenues it had earned before the reduction on royalties. Although companies like BP, Exxon, Spain's Repsol and British Gas first uttered angry threats about leaving the country, in the end they stayed there all the same.

The government of Evo Morales, which came into office a year later, even went a step further and renegotiated all the contracts with foreign companies. At the same time the state-run company, Yacimientos Petrolíferos Fiscales Bolivianos (YPFB), assumed total control of the development, production and marketing of Bolivian oil and natural gas. Half of all the revenues go directly to the state as before; the foreign company concerned can claim up to 30 per cent of the rest at the most to cover its costs and the remaining 20 per cent is divided between the state and the company. Bolivia's revenues from the oil and gas business rose from 5.6 (2004) to 24 per cent of GDP (2008) in four years.[16] An important factor in the country's successful stand against the powerful oil companies was the support it received from Brazil. Semi-public Petrobras is one of the major oil companies operating in Bolivia. By accepting the new, politically controversial conditions at the behest of President Lula da Silva, Petrobras in effect ruled out the possibility of a united front against the Morales government.

USING COMPANY LAWYERS AND LOBBYISTS TO OPPOSE REFORMS

Even in previous periods of highly volatile commodity prices the producing countries were able to increase their share of resource rents. Two more Latin American examples, Venezuela and Ecuador, illustrate that the situation with oil is no different this time. Not only does the metal and ore business here badly need to catch up, it also has enormous potential thanks to high market prices. However, many a national mining law frustrates reform, for example it may contain stability clauses assuring companies that taxes and duties will not increase in future. It was on the basis of one such clause that foreign mining companies in Peru refused to pay royalties of between one and three per cent after these had been reintroduced. As a result the state lost over 350 million dollars between 2004 and 2006. The refusal to pay by the Xstrata subsidiary, Tintaya, alone cost Peru close to 30 million dollars.[17] Also investment protection agreements often prevent developing countries from increasing their taxes and duties, moreover, they enable the affected companies to bring the matter before the courts.

The example of Australia illustrates that even governments of industrialised countries cannot win against the powerful 'mining majors'. When Prime Minister Kevin Rudd announced a special 40 per cent tax (Resource Super Profits Tax) on the unusually high profits of the Australian commodity multinationals, the companies (including

Xstrata) threatened en masse to boycott investment. Mining projects worth 186 billion dollars were apparently put on ice and the mining lobby warned of mass redundancies and economic decline. Pressure from the mining industry was a decisive factor in Rudd's downfall at the hands of his opponent Julia Gillard from within his own party. The moment she took office, Gillard scrapped the radical tax plans.

STATE/POPULATION: FACTORS AND EFFECTS OF THE RESOURCE CURSE

Teodoro Obiang Nguema Mangue forked out 35 million dollars for the villa in sophisticated Malibu. Situated in one of California's most exclusive residential neighbourhoods, the property includes a large swimming pool, tennis courts, a golf course, sufficient parking spaces for his various luxury cars and six hectares of grounds with magnificent sea views. The proud owner would have had to work for more than 583 years to be able to afford this grand house, given his official annual income of 60,000 dollars. However, he has been spared that, because 'Teodorín', as he is known to his fellow countrymen, is the son and potential successor of Teodoro Obiang Nguema Mbasogo, the long-time President of Equatorial Guinea. According to the US magazine *Forbes* , the latter has a fortune worth an estimated 600 million dollars and is one of the richest heads of state in the world.

What made all this possible were vast earnings from oil: since crude oil was discovered off the coast of Equatorial Guinea early in the 1990s, the Central African country with a population of around 650,000 inhabitants has become the fourth-largest exporter of oil on the continent.

Glencore too would like its share of the profits from this economic miracle. The company has a minority share in the Aseng oilfield via its subsidiary, Glencore Exploration (EG) Ltd and has invested nearly 800 million dollars in developing the oil and gas reserves over the next two or three years, which were discovered 945 metres below sea level in 2007.

A COUNTRY AS RICH AS ITALY, A GOVERNMENT AS CORRUPT AS THE MAFIA

Having come to power in 1979 by means of a bloody coup, Obiang Nguema was last re-elected for a further six-year term in November 2009 with more than 95 per cent of the vote. A report on Equatorial Guinea by the US think tank, Freedom House accounted for this result: Sham elections, a restricted right of association and assembly, lack of press freedom and no independent judiciary.[18] However, these do not come close to exhausting the President's repertoire of repressive measures as documented by various human rights organisations. Nepotism and corruption have also played a crucial role in enabling him to consolidate his power and safeguard his oil revenues. Members of his family own various national companies, including the one and only television station, and occupy several ministerial posts. The government of Obiang Nguema has deposited over two billion dollars in private banks abroad. When the US Senate took an in-depth look at suspect transactions worth several hundred million dollars, it found dozens of accounts, some of them under the names of members of the President's entourage. It was to these that Obiang Nguema and his family had direct access.[19] Hence Equatorial Guinea ranks 168th out of 180 countries in the Corruption Perceptions Index published by Transparency International.

Since the discovery of oilfields in the waters off its coast, Equatorial Guinea's gross domestic product (GDP) has grown more than fifty-fold. Oil revenues contribute around 85 per cent of GDP and poured over 4.8 billion dollars into the state coffers in 2007. The country has a GDP at purchasing power parity per capita comparable to that of Italy. At the same time it ranks only 118th out of 169 in the Human Development Index (HDI) of the UN Development Programme. This makes Equatorial Guinea the country with the greatest difference between GDP and HDI rankings in the world. Why exactly? Whereas the Obiang clan has grown immeasurably rich from the discovery of oil, more than three-quarters of the population live below the poverty line. Equatorial Guinea is therefore a prime example of the importance of the second dimension of distribution in the context of raw material extraction: the one between the state, or rather its government, and the population.

No wonder that many people in Equatorial Guinea regard natural resource wealth as the opposite of a blessing although very few would be familiar with the resource curse thesis. Coined by Richard Auty in 1993[20], the term describes the relatively common phenomenon whereby states with an abundance of natural resources are often politically unstable and led by autocratic governments dominated by kleptocratic clans. The effects of such a lack of 'good governance' are social and economic evils, from which the population suffers while the country's elite, and also the commodity companies operating there, unashamedly amass fortunes.

THE RICHER THE SOIL, THE POORER THE PEOPLE

Many poor countries have rich deposits of natural resources. For a long time it was assumed that exploiting such mineral and fossil resources would help these countries become prosperous. However, numerous studies dating from the 1990s onwards prove that in many cases natural resource wealth does not bring economic success and prosperity; on the contrary, it leads to poor growth rates, greater inequality, more corruption, authoritarian regimes, high military expenditure and warlike conflicts.[21] For example, it has been shown that in the OPEC countries real GDP per capita fell by 1.3 per cent a year on average between 1965 and 1998.

The negative effects associated with natural resource wealth have a socio-political, as well as an economic dimension. The first category includes corruption and mismanagement, authoritarian regimes, political instability and conflict, as well as poverty and social inequality; the second, the Dutch Disease (see below), volatility and debt. Obviously not all the negative effects occur in every case. Despite this, the development, or rather the lack of it, observed in many resource-rich countries follows a pattern that supports the resource curse thesis.

HAND IN HAND: CORRUPTION AND MISMANAGEMENT

Presenting the 2004 Corruption Perceptions Index, Peter Eigen, Chairman of Transparency International at the time, said, "The 2004 Corruption Perceptions Index shows that the oil-rich countries, Angola, Azerbaijan, Chad, Ecuador, Indonesia, Iran, Iraq, Kazakhstan, Libya, Nigeria, Russia, Sudan, Venezuela and Yemen have all achieved a very low score. The awarding of public contracts in the oil sector in these countries suffers from the fact that the revenues line the pockets of western managers in the oil industry, middlemen and local officials."[22] Alongside Equatorial Guinea Nigeria is also a particularly blatant example of corruption. After just four years at the helm of this oil-rich country, General Sani Abacha and his family have embezzled around three billion dollars. A sizeable proportion of this wealth has landed in Swiss bank accounts, and it hasn't been only the banks who assisted them in gaining this wealth: Halliburton, a service provider to the oil industry, admitted in 2003 that its subsidiary Kellogg Brown & Root (KBR) had paid Nigerian state officials about 2.4 million dollars in bribes in return for tax concessions.[23]

Corruption, that is, the misuse of entrusted power for personal gain, knows few winners and many losers. The concentration of power in a ruling elite combined with a lack of democratic government has disastrous effects on the poorer classes in particular.

ROUGH HANDS: AUTOCRATS AND KLEPTOCRATS

Countries that depend heavily on the extractive industry are less democratic on average than those with a broad economic base.[24] There are two reasons for this: firstly, revenues of natural resources enable governments to keep taxes low. This means the people have little incentive to insist on transparent government and state finances – after all, it's not their money. At the same time, the dollars earned from natural resources sometimes enable generous public expenditure, which tends to undermine any demand for greater democracy. Secondly, full state coffers enable governments of resource-rich countries either to buy off opposition movements or suppress them with heavily-armed security apparatuses. The case of the Chad-Cameroon pipeline described below is an example of the arrogance of the authoritarian regimes of resource-rich countries towards their people and their international partners alike.

A TRIP TO CHAD: WHERE THERE IS NO POLITICAL WILL, THERE IS NO WAY. | It was to be a 'flagship project' for sustainable development and free Chad's population from poverty, explained representatives from the World Bank when they launched the project in June 2000. Oil from southern Chad would flow along a 1076-kilometre pipeline to the coast of Cameroon and from there to international markets. It was the largest development project on the African continent and the World Bank claimed it met its social and environmental standards. However, even then critical voices warned that the government and social system were not sufficiently prepared for the windfall: Chad needed more time to develop the necessary capacities. In fact, eleven years after the project began, the result has been sobering even though all the technology and funding had worked: 170,000 to 200,000 barrels of oil a day pours forth out of Chad, an even larger volume than hoped, giving the government revenues of 4.3 billion dollars up to the end of 2008. Yet, at the same time Chad had dropped ten places in the Human Development Index compared to 2003, i.e. before the oil exports began, and was placed 175th out of the 182 assessed nations. Having evaluated the project in detail, even the World Bank came to the unambiguous conclusion: "Despite the technical and financial success of the pipeline project, […] this fundamental objective [to reduce poverty and improve governance in Chad] has not been achieved."[25]

What went wrong? The conditions for such a large-scale investment in the oil industry of a developing country had never been so good. By passing Law 001, the Chad government had declared its willingness

to accept a detailed plan for managing the oil revenues – an absolute innovation. According to this, ten per cent of oil revenues were to go to a Future Generations Fund and 90 per cent to the Central Bank of Chad. Four-fifths of the latter were earmarked for priority sectors, such as health, education and rural development, five per cent for investments in the extraction region around the town of Doba and the remaining 15 per cent for the state coffers in general. By January 2006 President Idriss Déby had breached this agreement with the World Bank. The Future Generations Fund was cancelled and not replaced. The five per cent for the extraction region was retained (in theory), but an amendment was introduced, stating that 30 per cent was to go into the general state coffers and 'security' was to be added to the priority sectors. Having protested at first, the World Bank then accepted the breach of the agreement. The oil consortium with an interest in the project (Esso, Petronas, Chevron) did not support the original agreements either.

From then onwards Déby and his entourage controlled and manipulated the oil business as they liked. A gradually increasing share of the proceeds flowed into the elaborate system of political patronage that the President had installed in order to stay in power. Then there was the militarisation of the country: according to the Stockholm International Peace Research Institute (SIPRI) weapons imports increased five-fold between 2004 and 2008 compared to before the oil boom (1999-2003).

The handsome oil profits enabled the government to pay back the loans from the World Bank in the autumn of 2008. The latter threw in the towel, accepted the offer and withdrew from Chad without so much as a murmur. Thus civil society in Chad, which had fought for compliance with the original laws since the project started, lost its most important ally. Moreover, the situation became more serious with the arrival of Chinese investors: shortly after Déby had established diplomatic relations with Beijing, the China National Petroleum Corporation (CNPC), number 8 in the global gas and oil business, obtained concessions in Chad from the Cliveden Group operating in Geneva.

Their declared original intention, that the oil would assist development, began to sound cynical with 70 per cent of the population in the southern oil regions still below the official poverty line of 330 dollars a year – much more than the national average. The five per cent of the revenues earmarked for the extraction region were reaching it merely in dribs and drabs, only to be squandered on prestigious projects such as a 4.7 million dollar sports stadium in Doba.[26] "The Head of State asks us to implement—we implement", commented the coordinator of the 'five per cent committee'.[27]

RISK FACTOR NATURAL RESOURCES: POLITICAL INSTABILITY AND CONFLICTS

According to an Oxford study, there is a far, far higher risk of civil war in countries rich in raw materials than in those with few natural resources. The authors state that these resources are the crucial risk factor for violent conflicts in a community – even more important than historical, geographical and ethnic reasons.[28]

The evidence for this is overwhelming: one of the most brutal examples is the conflict diamonds of Sierra Leone. In the 1980s the government there lost control of the armed groups guarding the mines where the diamonds were being extracted. The conflict escalated early in the 1990s when the rebels, supported by Charles Taylor who later became the President of Liberia (on trial in the Special Court for Sierra Leone since 2006), terrorised the country. With the dollars they obtained from the diamonds the rebel groups bought the most advanced weaponry, with which they very nearly brought down the government. The conflict cost 50,000 people their lives and reversed development in Sierra Leone by decades.

See CHAP. 15 for further examples illustrating the link between natural resource wealth and violent conflicts. Although a dependency on natural resources is less evident in Latin American than African countries, here too resources can spark off conflicts, especially in the Amazon basin. In 2009 indigenous Peruvians blockaded the roads to their traditional homeland in the Amazon territories in protest against the laws that would have granted foreign oil and mining companies access to the mineral resources therein. The ensuing bloody confrontation made international headlines, in the end forcing the government in Lima to repeal these laws.

BACKWARDS DEVELOPMENT: POVERTY AND SOCIAL INEQUALITY

Some of the reasons why the broad masses of a country do not profit from its natural resource wealth lie in the factors listed above. Corruption and mismanagement benefit a privileged few at the expense of the vast majority, and authoritarian regimes prevent the poorer classes being able to fight for an improvement in their living conditions. As the example of Sierra Leone shows, warlike conflicts have disastrous effects on people and reverse development. As well as, and frequently in combination with, these mechanisms, (forced) resettlement and environmental damage caused by mining undermine the livelihoods of the affected communities. Nigeria is another striking example of how the majority of a population can remain trapped in poverty, and social differences often become even greater, natural resource wealth notwithstanding. Despite the fact the oil revenues per capita increased almost ten-fold in the country between 1970 and 2000, GDP per capita stagnated, so that by the year 2000 Nigeria was one of the fifteen poorest countries in the world. In the same period the proportion of the inhabitants living in extreme poverty (on less than one dollar a day) shot up from 36 to nearly 70 per cent. This meant an increase from 19 to 90 million people in real terms. Inequality also increased dramatically. Whereas in 1970 the richest two per cent earned as much as the poorest 17 per cent, by the year 2000 the former group was earning as much as the poorest 55 per cent.[29]

IN THE DOWNWARD SPIRAL: THE DUTCH DISEASE

The discovery of substantial raw materials reserves can also have negative economic consequences. The most important effect is known as the Dutch Disease and refers to the experience of the Netherlands in the 1970s after the discovery of large natural gas reserves in the North Sea. Earnings from the export of natural resources causes the country's currency to appreciate, making exports from other industries, such as services or agricultural and industrial products, more expensive and therefore less competitive on the world markets. This paradoxical effect is further magnified by the pressure of higher salaries in the commodity industry, which in turn raises wage costs in the rest of the export sector.[30]

This threatens to become a vicious circle: the declining significance of other industries enhances the importance of the commodity sector in a national economy, which in turn further eclipses the other areas. This development usually entails a rise in unemployment since the redundant workers cannot be absorbed by the commodity sector because this sector is capital-intensive rather than labour-intensive. Nor are there usually any upstream and downstream industries or services in the producing countries, which prevents these from profiting from a more broadly based added value.

ON SHAKY GROUND: VOLATILITY AND DEBT

A direct consequence of the Dutch Disease is the constantly increasing dependency of countries on their natural resources. This makes resource-rich nations unusually susceptible to the extreme price fluctuations that regularly occur in the commodity markets CHAP. 3. A high degree of price volatility translates directly into fluctuations throughout a nation's economy. These dynamics make it far more difficult for governments to draw up budgets and make decisions on investments. In a situation such as this, high commodity prices and corresponding surpluses often lead to unwise investments, while low prices result in too little spending on necessities.

Moreover, governments of nations rich in raw materials tend to incur huge debts. An effect of the Dutch Disease is the appreciation of a nation's currency. This makes running up these debts seem attractive, because it reduces the cost of servicing foreign debt. A further factor is that countries with natural resource wealth are often perceived as having greater credit-worthiness, and consequently are granted greater access to global capital markets. However, when the prices of these commodities fall, revenues shrink and the exchange rate drops, leaving these countries without enough money to service the debt, which in turn has become more expensive.

ACCURSED RESOURCES OR DAMNING CONDITIONS?

The British Overseas Development Institute (ODI) has calculated that eight African countries, Angola, Equatorial Guinea, Chad, Congo-Brazzaville, Gabon, Cameroon, Nigeria and Sudan all generate enough income from oil extraction to be able to achieve the Millennium Development Goals (MDG).[31] In reality these states are among the poorest on the continent and for the most part miles from achieving the MDGs. The real tragedy, however, is the fact that as much as two-thirds of the world's poorest people live in resource-rich countries.[32]

The situation is desperate and the existence of the resource curse beyond any doubt. Politicians in resource-rich countries face enormous challenges when it comes to ensuring that the wealth that lies in the ground can enable those who inhabit these lands to live in dignity and relative prosperity. The various experiences of these countries reveal a scandalous failure but also offer some hope of success, thereby suggesting that the resource curse is not an inevitable but a preventable fate.

When the decision by the son of Equatorial Guinea's President, 'Teodorín' Obiang to have one of the world's largest luxury yachts built for 380 million dollars was made public, it was by no means good news for the betrayed people of this country so richly blessed with natural resources.[33] However, after the disclosure of his extravagant plans the likely future President appears to have had to say goodbye to them. A sign of hope?

INTERIM CONCLUSION

The issue of resource rent distribution can be approached on two levels: firstly, the level between the producing countries and the (mostly) foreign commodity companies and secondly, the level between states, or rather their governments, and the people. As regards mining, only a tiny proportion of the resource rents actually reaches the producing countries, which is why there is no money for economic and social development. Although more stays in the country in the case of oil, it rarely benefits the population, nor is it invested in future development.

Basically, a lack of transparency and democratic governance encourages governments and commodity companies to join forces, which has an even more serious impact on the inhabitants, especially those communities directly affected.

Although commodity companies are mainly actors in the first distribution dimension, they also bear principal responsibility for the second. Firstly, they must offer the governments of their host countries a fair deal, then they must use their wide-ranging influence to exert pressure on governments on issues such as good governance and internal distribution. The means: no bribes, no deals with governments not legitimised by the people, and total transparency.

The distribution of commodity revenues is not a law of nature, neither in the first nor in the second dimension. Given the political will, the governments of developing or emerging nations, which have the broad support of the people, can successfully defy even the interests of multinational commodity companies. Conversely, populations equipped with well-organised civil societies can exert the necessary pressure on their governments to use commodities revenues to improve their standard of living and enable, instead of hindering, development.

No change without 'good governance'.

This key concept applies not only to the governments of the producing countries, but also to the frequently symbiotic relationship between them and the commodity businesses. Oil and mining

ALTERNATIVES //

companies often profit as much as, and sometimes an even more than, governments of host countries and therefore share responsibility for the consequences of resource exploitation.

IDEAS AND INITIATIVES: SHEDDING LIGHT ON THE DARK DEALS

"The logic was sound, but then reality interfered."[1] This cynical remark of November 2009 summed up the World Bank's assessment of the Chad-Cameroon Oil & Pipeline Project CHAP.17. Development in Chad is quite typical of a resource-rich developing country, but its not necessarily inevitable. There are some instances where countries, including Botswana, have seized the opportunities their natural resources offered. The way out of the resource trap is difficult but it is by no means impossible.

In public, no one is going to deny that the populations of resource-rich countries should be the first to benefit from the extraction of their natural resources. After all, according to universal human rights (Article 1 of the International Covenant on Civil and Political Rights), it is they who are the owners of the natural wealth that lies in the soil of their countries. However, the reality appears to be quite different. Today the struggle against such injustice is waged on two main fronts: via economic and fiscal policy initiatives to counteract the macroeconomic causes of the resource curse, and via all those measures which use transparency, better governance and improved corporate responsibility to change the political and social context in which the exploitation of (raw materials in) developing countries occurs.

Both approaches focus on the second dimension of the issue of distribution and justice, as illustrated in the previous chapter. Hitherto, there has never been a convincing international initiative to support producing countries that seek to improve their political standing in relation to the major consuming countries in which the mining and trading businesses are located. The imbalance of power in this relationship is nothing short of grotesque, as the following example demonstrates.

WRETCHED CONFIDENTIALITY

When Mozambique proposed granting various exploration and mining licences to private companies, one lone secretary of state sat down to face about 20 legal advisors and academics belonging to an international business consortium. Peter Eigen, former chairman of the Extractive Industries Transparency Initiative (EITI) and founder of Transparency International, declared contracts drawn up under such conditions to be inherently unjust during a hearing of the German Bundestag in March 2011. It is above all in the mining sector that developing countries fail to secure 'good deals', not least due to their lack of human and material capacities.

Moreover, how good a deal actually is will often remain in the dark because most contracts between countries and commodity businesses are closely guarded state secrets. Hence the NGO coalition, Publish What You Pay, has long been calling for the disclosure of mining licences and concession contracts. Companies and governments argue on the other hand that such contract transparency would betray company secrets and breach confidentiality clauses. Nevertheless, the trend is still to move towards greater openness. For example, Guinea, Liberia, Ecuador, Peru, Bolivia, East Timor, and Azerbaijan have decided to publish all their contracts with companies in the extractive industries. In Niger contract transparency is even included in the new constitution that was accepted in a referendum at the end of 2010.

GOOD GOVERNANCE AND OTHER COUNTERMEASURES

Although the list of proposals for combating the resource curse via economic policy is long, the list of those developing countries that have implemented these successfully remains relatively short. The best and most well-known example is Botswana, which, thanks to (or even in spite of) its rich diamond deposits, has developed from what was one of the world's poorest countries into a relatively prosperous and politically stable democracy CHAP. 17. The establishment of stabilisation funds or funds for the benefit of future generations can ensure that the profits from limited raw material deposits, which are exploited at one time or another, flow into longer-term development strategies. The most successful example of this is the Norwegian State Petroleum Fund, but also in Chad a Fund for Future Generations was included in the original contracts with the World Bank. Besides stabilising economic effects, e.g. uncoupling volatile raw materials revenues from public expenditure at the political level, pools of money such as these also put parts of the resource rents beyond the direct reach of governments, thereby reducing the potential for conflict within states. To ensure success, these rents must be managed independently.

In addition, development economists propose other measures. Countries could deliberately delay or forgo extracting raw materials (a 'No-Go Policy') in order to develop the agricultural and production sectors first. Also important are:

- Exchange-rate policies, that is, efforts to reduce the appreciation of a country's currency, resulting from the export of natural resources, in order to safeguard the competitiveness of the other sectors,
- Attempts, through appropriate expansion into the production sector, to better take advantage of the demand of commodity companies for goods and services,
- Concerted efforts to negotiate better conditions in the contracts with mining and trading companies in order to increase the state revenues of the producing countries.

One thing is clear, however; effectively implementing economic and fiscal measures requires political will and strong state institutions. Local civil society, contract transparency, political representation of the people and corporate accountability are also of vital importance.[2] In short: there can be no change without 'good governance'. This key concept applies not only at the governments of the producing countries, but also at the frequently symbiotic relationship between them and commodity businesses. Oil and mining companies often profit as much as, and sometimes an even more than, the governments of host countries and therefore share responsibility for the economic, environmental and social consequences of resource exploitation. In the face of the resource curse, companies are just as accountable as the political authorities of those countries in which they operate.

SECRECY AS A BUSINESS MODEL

"It is high time we woke up; we are in the era of WikiLeaks. Nowadays everything is made public; we are all naked. Or do we want to be the Mubaraks of tomorrow?"[3] This was the rhetorical question put by Sudanese entrepreneur Mo Ibrahim in March 2011 when he called for the oil and mining business to be brought out of the darkness and into the light of public scrutiny to allow more transparency. His audience included heads of state and government and leaders of mining and trading businesses. The commodity industry, like the finance and banking sectors, is dominated by impenetrable structures and obscure deals. Secrecy is a part of the business model – not just in Switzerland, but also in the producing countries. Just how much the governments of many resource-rich countries earn from the export of their natural resources, and where this money goes, is a closely guarded state secret.

It is obvious that such a systematic lack of transparency will leave the gates wide open to corruption, patronage and poor management. However, the days when commodity companies could stage deals in back rooms with those in power in the producing countries are coming to an end. Prompted by a worldwide network of 'watch dogs' including NGOs such as Global Witness and Revenue Watch, diverse initiatives aimed at making both commodity companies and states more accountable have been gaining ground over the last ten years. Broadly supported by civil society, companies and political institutions alike, these initiatives use a wide range of instruments to ensure that in the future the inhabitants of producing countries will benefit from their wealth of natural resources.

This movement began in Angola, a desperately poor country, ravaged by civil war but rich in diamonds and oil. In 1999 and 2002 Global Witness published two reports on the shameful role played by multinational commodity companies and banks in the civil war, and the devastating effects of corruption.[4] Every year billions of dollars disappeared into the pockets of the Angolan elite while the people were left to starve. Both UBS and Glencore were involved in this 'Angolagate'. BP became the first company to announce its willingness to disclose the payments it had made to the Angolan government. When Angola's state-run oil company, Sonangol, threatened to withdraw BP's licence for this 'breach of contract', BP backtracked on its promised transparency. This episode made considerable waves worldwide, drawing attention to the problem of corruption in the oil sector and the complicity of companies. With the support of financier George Soros the NGO coalition Publish What You Pay (PWYP) was launched in June 2002. This marked the birth of an alliance of organisations, now more than 600 in number from over 50 countries,[5] which in just ten years has succeeded in putting a topic previously considered a state secret in many countries onto the political agenda.[6]

The idea behind PWYP is simple: companies in the extractive industries should declare their payments to producing countries, i.e. disclose how much they pay in taxes, duties and fees per country and project. First and foremost, this enables the population concerned to demand that their government explain the whereabouts of the monies received. The more open state finances and company accounts are, the more difficult it is to conceal corruption. The more transparent the flow of funds and distribution of the earnings from the export of natural resources are, the less incentive there is for people to resort to violence in order to get access to the treasure chests of power. How then can these aims be achieved? Essentially there are two options: voluntary initiatives, or legally binding regulations and laws. It is the contrast between these two very different options that has dominated the transparency debate in the last ten years.

BINDING REGULATIONS: DODD-FRANK AS A TURNING POINT

It was an outrageous demand: in 2009 Muammar al-Gaddafi's advisors requested that the foreign oil companies operating in Libya fork out the 1.5 billion dollars the country had been ordered to pay the victims of the Lockerbie bombing orchestrated by Gaddafi. Most of the companies refused, although according to the *New York Times* some smaller companies might have agreed, but which ones remains unknown[7]. On the other hand, what did become public knowledge was the fact that in 2008 the Californian Occidental Petroleum Corporation paid the Libyan dictator a billion dollars as a signing bonus for a long-term contract. Again according to the *New York Times,* Gaddafi siphoned off billions of dollars in cash from oil transactions – money that he may have used in the spring of 2011 to pay his mercenaries in the war he waged on his own people. All this time Occidental Petroleum was lobbying intensively against a law passed in the summer of 2010 which required commodity companies listed on the US stock exchanges to disclose their payments to foreign governments. In the view of Occidental Petroleum this was damaging to the competitiveness of the companies involved. In contrast, the company did not seem unduly concerned about the fact that the billions it had paid were financing the fight against the movement for democracy at precisely the same time.

This example demonstrates the futility of using voluntary agreements to rein in autocratic states like Libya. Only legally binding and enforceable transparency laws are fit for purpose, and can ensure that oil and mining industries will not use voluntary agreements as a fig leaf. This is the method clearly favoured by Publish What You Pay. In addition, legally binding regulations create a level playing field for all players, which is in the industry's best interest. Last but not least, the introduction of political rules leads to public debate and therefore increased democratic legitimacy.

In this context a decisive breakthrough occurred in the United States in July 2010. There, reform of the finance market (Dodd-Frank Wall Street Reform and Consumer Protection Act) included enforcing the aforementioned provisions, which require all oil, gas and mining companies listed on US stock exchanges to declare all their payments to their individual producing countries. This groundbreaking law even demands that they list their payments for individual 'projects'. This impacts 90 per cent of the oil and gas companies with the largest

revenues, as well as eight of the world's ten largest mining companies listed on stock exchanges. The unusually heavy fight for the implementing provisions, which the US Securities and Exchange Commission (SEC) must introduce, is still underway as this book goes to press. The most controversial points concern the definition of a 'project', ultimately, that is, the aggregation level of the payments to be published, as well as the question as to whether exemptions should be granted if national governments in the producing countries explicitly forbid the publication of this type of information. Logically, NGOs fear that if this is the case governments of individual countries could subsequently pass laws designed to get round the US provision.

EXEMPLARY US REGULATION EXERTS PRESSURE WORLDWIDE | It is not possible to estimate the consequences of the US regulation at the time of writing since the companies do not have to begin submitting reports in accordance with the new regulations until implementing provisions have been enacted. However, the new regulation has put pressure on other countries and financial centres to follow the US example. In October 2011 the EU's internal market commissioner Michel Barnier tabled the Commission's proposals to amend the EU's Transparency and Accounting Directives. In some respects these proposals go further than the US law by including forestry and by requiring not only publicly traded but also large private companies to make public their payments to governments for extracting oil, gas and minerals. In the ongoing debate the position of Great Britain is crucial because, for example, in March 2011, 59 per cent of all the commodity companies listed on stock exchanges in the EU are traded on the London Stock Exchange, including those of Swiss company Xstrata.

The European Parliament had earlier called for the amendments being proposed by Barnier. The European Parliament has also called on the Commission "at the international level to exert pressure on the IASB (International Accounting Standards Board) swiftly to develop the corresponding comprehensive standard."[8] Here the European

Parliament is referring to another on-going process: the possible revision of the International Financial Reporting Standard (IFRS) for "Extractive Activities".[9] A discussion paper was launched in April 2010, and during the consultation process the World Bank and renowned investors have called for the introduction of country-by-country disclosure.[10] However, the IASB has decided to halt the process.

Nevertheless, having sensed the changing mood, some companies, such as Statoil (Norway), Talisman Energy (Canada) or Newmont Mining (USA), have already begun disclosing their payments to individual countries. In the context of the Frank-Dodd debate, mining giants such as Barrick Gold or AngloGold Ashanti have declared themselves firmly in favour of achieving the utmost transparency. Investors also value the new information on company activities in what are often politically unstable countries. For example, Paul Bugala, an analyst at the US investment company Calvert Asset Management, wrote that the transparency regulations enabled investors to assess and compare country-specific regulatory and fiscal risks for the first time.[11] This refutes the argument frequently put forward by critics that transparency creates a competitive disadvantage.

SWITZERLAND ON COURSE TO BECOME A REGULATORY OASIS IN TERMS OF COMMODITIES | Only in Switzerland the global winds of change are not yet felt or taken seriously. Country-by-country itemising of accounts, which is known as 'Country-by-Country Reporting' (CBCR), was an issue during the revision of the law on accounting at the end of 2010. An amendment introduced by MP Susanne Leutenegger Oberholzer (Social Democratic Party) would have required all multinational companies located in Switzerland to disclose their revenues, profits and tax payments country by country. Launched by the international Tax Justice Network, CBCR includes not only Publish What You Pay, but also Publish Where You Earn (where companies achieve added value provisions). Such a law would also reveal transfer pricing payments and profit transfers CHAP. 14. However, the adoption of the law failed as a result of opposition from the centre-right parties. Even in the wake of an impending IFRS revision the State Secretariat for Economic Affairs (SECO) still does not consider country-by-country itemising feasible.[12] This threatens to make Switzerland even more of a regulatory oasis in that it continues to attract and safeguard opaque companies.

VOLUNTARY INITIATIVES AS CONFIDENCE-BUILDING MEASURES

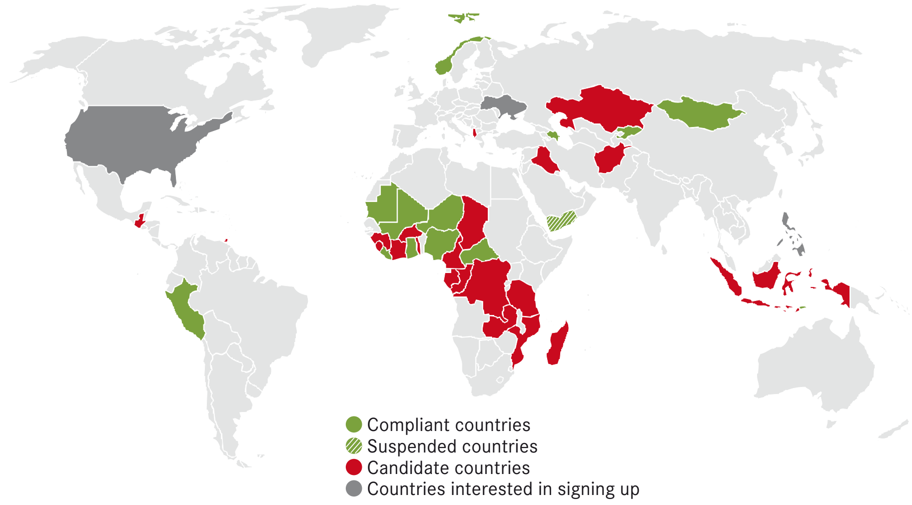
The driving force was certainly Publish What You Pay. However, at the Johannesburg Earth Summit in the autumn of 2002 British Prime Minister Tony Blair got on board the transparency train and launched the Extractive Industries Transparency Initiative (EITI), which, like PWYP, brought together companies, governments and civil societies. Countries that sign up to the EITI require all oil, gas and mining companies operating in their territory to declare their payments. These are compared to government revenues in a publicly available report and any apparent discrepancies accounted for, where possible. Once a country has completed all twenty steps of the implementation process successfully, it is designated 'EITI compliant' by a Board comprising an equal number of representatives from government, industry and civil society.

Over 50 of the largest oil producers and mining companies, including Swiss mining giants Glencore and Xstrata, as well as around 80 investors with assets totalling more than 16 billion dollars, support the EITI. Yet, the only participating investors from Switzerland are the Ethos Investment Foundation, the Guilé Foundation, Bank Sarasin and the reinsurer, Swiss Re. The federal authorities in Berne support the EITI through the State Secretariat for Economic Affairs', annual financial payments to the Multi Donor Trust Fund managed by the World Bank, the initiative's main source of funding. In addition, SECO committed itself to paying five million Swiss francs into the IMF's new Topical

Trust Fund on Managing Natural Resource Wealth CHAP. 17. The aim of the Trust Fund is to increase the transparency of financial flows and to promote the 'wise' use of revenues from natural resources.[13]

FIG. 1

THE EITI WORLD



Source: eiti.org/countries

By February 2012 eleven countries (Azerbaijan, Ghana, Kyrgyzstan, Liberia, Mali, Mongolia, Niger, Nigeria, Norway, East Timor and the Central African Republic) were EITI compliant and twenty-two more, most of them in Africa, were candidate countries FIG. 1. So far 29 countries rich in raw materials have published their revenues and over 150 companies have declared payments totalling more than 550 billion dollars. Some considerable differences have come to light: for example, in Nigeria the sums declared by companies as signing bonuses, dividends and interest payments, and the sums government agencies reported being paid for the year 2005 amounted to a discrepancy of about 300 million dollars. Where this money then went remains as much of a mystery as do the whereabouts of the 17 million dollars that, according to the first EITI report from Tanzania for the year 2009, was paid by commodity companies but never reached the government of this East African country – at least not officially.[14]

Submitting reports in accordance with EITI criteria has since become anchored in the law in Ghana, Liberia, Nigeria, Sierra Leone, Norway and Mongolia; in Niger some of the EITI principles have even been introduced into the new constitution that was accepted in a referendum at the end of 2010.

The only estimates of any specific effects of the EITI at the time of writing are those made by the players involved.[15] One key benefit reported is the improved dialogue between populations, governments and companies. What the EITI has created, however, is the first-ever platform enabling the exchange of information and discussions, and therefore the establishment of an atmosphere of trust. Moreover, this initiative affords activists some protection in countries with weak justice systems, thereby opening the door for greater political participation on the part of civil society. For example, in Chad the debate on a pipeline project and transparency in the natural resources sector has led to the formation of a group of NGOs, which has since become active in other political spheres.

However, the EITI does contain some weak elements. The most important is the fact that legal sanctions are not an option (apart from suspension of an offending member) if governments or companies break the rules. So it is hardly surprising that oil and mining industries in particular prefer this voluntary approach to any binding regulation. In addition, the quality and therefore the reliability of the information in the EITI reports vary enormously. In so far as the EITI requires reporting merely on the flow of payments, important upstream processes (for example the granting of licences and contracts) are excluded. "Transparency is important but without accountability it means nothing," according to the Deputy Head of the EITI International Secretariat in Oslo. His opinion raises a controversial point: even if state revenues from natural resources are out in the public domain, this is no guarantee that the money will be used wisely at the political level to promote development that will reduce poverty and improve living conditions in countries rich in raw materials. In 2011 the Board of the EITI initiated a strategic review in 2011 to guide the future of this initiative.

BLOOD DIAMONDS & CO: THE STUFF CONFLICTS ARE MADE OF

Armed conflicts have regularly occurred where natural resources are profitably accessible. The recent history of the world is full of such conflicts, particularly over the strategically important energy source oil – from the 'Great Game' between Russia and Great Britain over dominance in Central Asia right up to the US interventions in Iraq. At regional and national levels the intensity of such conflicts ranges from political instability, as in Niger for example, to the periodically occurring armed conflicts such as those in Chad, to bloody civil wars, such as the ones in Liberia, Angola or the Congo. The diamond trade is even more susceptible to conflict, since diamonds are easy to transport and even small quantities can generate substantial proceeds. In 1998 the UN Security Council banned the export of diamonds by the Angolan rebel movement, Unita. Unita ignored the ban, whereupon the major diamond-exporting countries met in Kimberley in South Africa in the spring of the year 2000 to tackle the root of the problem. The result was the development of the Kimberley Process (KP), a certification scheme supported by 75 countries at present (including Switzerland), whose aim is to prevent the trade in conflict diamonds. The KP countries must enact appropriate legislation to establish a customs control system for certifying raw diamonds, and can only trade with other KP-compliant countries.

Despite some successes, this system of rules is far from watertight. Breaches of the Kimberley Process in Sierra Leone, the Democratic Republic of Congo, Ivory Coast and, most recently, Zimbabwe have come to light. One of the problems in the fight against smuggling, money laundering and human rights violations is the lack of both independent controls and sanctioning mechanisms. For instance, exports from Zimbabwe's controversial Marange diamond fields were still authorised in November 2011 despite the fact that reforms, promised after Zimbabwe's security forces murdered more than 200 small scale miners there in 2008, have yet to be implemented. Because of this situation, the watchdog Global Witness, an official Observer and driving force behind the KP, left the process in December 2011. The voluntary 'guarantee system' for certifying polished diamonds used in jewellery also contains weaknesses because independent checks are seldom carried out on the supply chains. This makes it still virtually impossible for consumers to buy diamonds, which are guaranteed 100 per cent conflict-free, in a jeweller's shop. Furthermore, the Kimberley Process aims merely to stop the trade in blood diamonds; issues around working conditions, payment flows, sustainability and human rights are excluded. These are the shortcomings the voluntary Diamond Development Initiative (DDI) and Responsible Jewellery Council intend to remedy by promoting both a fairer distribution of the proceeds from diamond mining and trading, and compliance with minimum social and environmental standards.

It is not only diamond necklaces and wedding rings that are blood-stained but also goods that have become more and more indispensable today such as mobile phones, laptops and many other electrical devices, all of which contain coltan (tantalum). The Democratic Republic of Congo has over 80 per cent of the world's coltan reserves and the conflict surrounding this commodity (and other 'conflict minerals') was and is a significant driving force behind the war there. This conflict has so far claimed almost six million victims, the highest price paid in blood since World War II. A major breakthrough in the battle to combat the fatal consequences of the exploitation of coltan, tin, tungsten and gold was achieved in July 2010 when sections of the Dodd-Frank law were passed. These require any company listed on a US stock exchange to reveal in an annual report whether any of their products contain these four sensitive metals sourced from the Congo or one of its neighbouring countries. Here too the Securities and Exchange Commission, the SEC, has not yet introduced the implementing provisions at the time of writing, and so the specific effects of the law are hard to predict. Nevertheless, demonstrating that a product is 'conflict-free' will prove difficult, and as a result some companies and suppliers may be forced to withdraw from the Congo and the Great Lakes Region.[16]

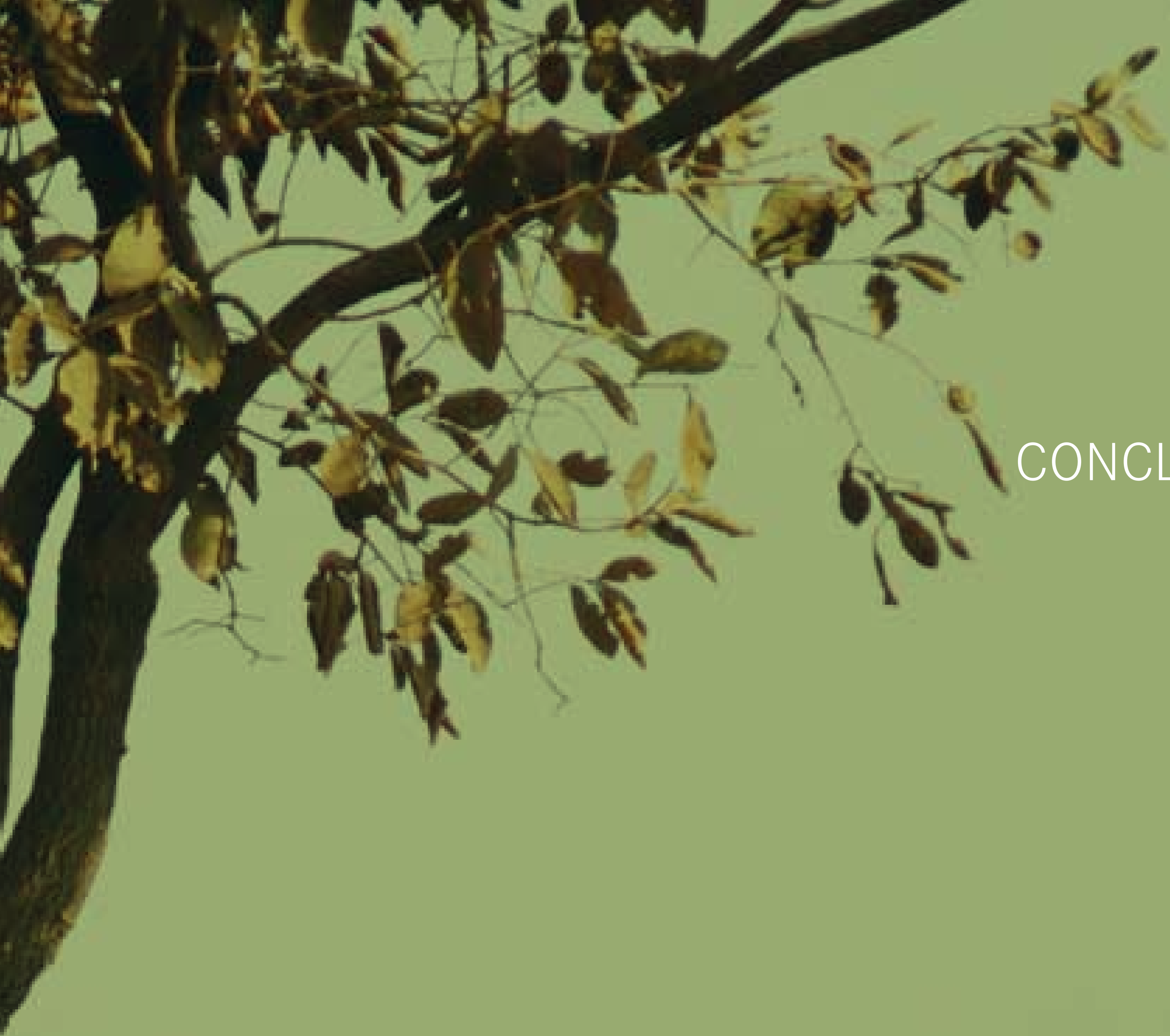
MOTHER EARTH: GROUND-BREAKING EXPERIMENTS IN ECUADOR AND BOLIVIA

Yasuni National Park, a global biodiversity hotspot, lies in the Ecuadorian Amazon lowlands. There are more different species of trees in a hectare of tropical rainforest here than in the whole of North America. The problem is, oil lies beneath the soil that is so rich in biodiversity: 846 million barrels of it to be precise, roughly 20 per cent of the reserves of this small Andean country. In August 2010 Ecuador's president, Raffael Correa, made Yasuni the setting for a ground-breaking experiment: he would forgo exploiting the oil reserves if the international community paid Ecuador 3.6 billion dollars, roughly half the total amount the country could earn from the exploitation of these reserves. The money was to go into a fund whose main purpose was to finance renewable energies and reforestation projects. After a lukewarm initial response by the international community, President Correa had threatened to cancel the experiment if at least 100 million dollars were not contributed to the fund by the end of 2011. While in the end the money was successfully raised Correa saw fit to raise the ante yet again by setting a new target of raising 291 million dollars a year in both 2012 and 2013. Whether the money will be found remains just as open to speculation as does the question of who will guarantee the donors that future governments in Ecuador will also leave the oil in the ground. Rebeca Grynspan, the Deputy Head of the UN Development Programme, who signed

the relevant agreement alongside the government of Ecuador, has described the proposal as groundbreaking and courageous. Moreover, in 2008 Ecuador became the first country in the world to codify in its constitution nature's right to exist. However, to date this abstract right has neither produced specific laws nor has it stopped oil extraction in the Amazon Region. Bolivia has said it intends to go a step further. In April 2011 the government tabled a draft Law on the Rights of Mother Earth (Ley de Derechos de la Madre Tierra) before parliament. The eleven new basic rights formulated in law include nature's right not to be damaged by infrastructure and development projects which upset the balance of ecosystems and local communities.

Drawn up by local social movements, the draft law is likely to receive broad support in parliament. Once in force, the Bolivian government is expected to establish a Ministry for Mother Earth and appoint an ombudsperson. Furthermore, the communities have been assured that this person will be given new powers to monitor and inspect industries that have traditionally had an adverse impact on the environment.

The vehement opposition from mining and agrochemical companies indicates the potential of the new law to impose narrow constraints on the natural resources industry. At the same time, the challenge facing the Bolivian government is that currently more than two-thirds of the country's export earnings come from minerals, oil and gas. Nonetheless, Vice President Álvaro García Linera is convinced that the Andean country will be writing history with this new law, given that the Law on the Rights of Mother Earth would define a wholly new relationship between man and the natural world.[17]



CONCLUSION //

"If there are no regulations,

the law of the jungle rules."

19 //

WHAT NOW? IMPLICATIONS AND DEMANDS

Geneva, Rue du Rhône, 5 July 2007: during their traditional 'school trip' the Swiss Government – all of them, under the expert leadership of the then Federal President and former Geneva Finance Minister, Micheline Calmy-Rey – pays the offices of the trading company Mercuria a visit. Delighted, the Mercuria owners and directors sum up the state visit in the following press release: "We thank the Swiss government for creating and preserving an economic, political and legal environment which allows companies like ours to develop and contribute to the common good."

How would the public react then, if the entire US cabinet with Barack Obama at its head just popped into the investment bank, Goldman Sachs, at 200 West Street in Lower Manhattan for a coffee? At first perhaps with utter amazement, then, however, with a huge outcry. The fact that this did not happen in Switzerland says something about the lack of a critical stance in the press, but far more about the crucial locational advantage of this country. This episode CHAP. 11 is indeed a shining example of the contact between two camps of ruthless opportunists: the commodity business and the largest part of the Swiss political class, so close to the economic scene that they are blind to unethical business practices and the ensuing risks for reputations.

It is an unholy alliance between naive ministers and compliant civil servants on the one hand, and clever commercial lawyers and unscrupulous company accountants on the other. In an interview CHAP. 16 Professor of Criminal Law and Criminology, Mark Pieth, describes the serious consequences of this partly unconscious and therefore all the more dangerous liaison. An empty threat to leave the country made by trading houses is used as sufficient reason – or pretext? – for policy-makers to refrain from applying the nation's Anti-Money Laundering Act to commodity traders. This, even though the latter are explicitly mentioned in this Act. As with many other regrettable incidents described in this book, the real scandal lies in the fact that in Switzerland such behaviour is not (yet) considered to be scandalous.

INTEGRATED COMPANIES AND EXPOSED PEOPLE

Besides profiting from the perfect political context and unfettered growth of the industry, the commodity companies represented in Switzerland have still more in common: regardless of whether they trade in metals and ores or agricultural products, 'vertical integration' is a ubiquitous feature of these companies. Oil traders (for example Trafigura in Africa) are expanding into selling to end-customers on the one hand and into operating their own oil rigs on the other. Purely a commodity trader at one time, Marc Rich + Co. has since become a fully integrated and highly diversified mining company that already owes half of its profits to production from its own mines and processing facilities. Equally, the large agricultural traders are buying or leasing farmland themselves to ensure security of supply to the increasing number of processing companies they also own.

Fuel and ore traders are now competing as latecomers with the established mining companies and oil multinationals. This is why they take greater risks and venture into the 'tough places'. Exploiting raw materials is and remains a difficult and often dirty business anyway, especially in weak states. Mines, oil rigs and production facilities are essentially dangerous for those people who have the misfortune to have always lived, as it were, 'on' mineral deposits. Without effective environmental and social legislation worthy of the name, the possible wrongdoings of the companies have an immediate impact on the local inhabitants. It is they who have to face the major (often existential) risks if, for example, Glencore seizes a business opportunity in the Congo.

IS SWITZERLAND A BLIND SPOT FOR ACCOUNTABILITY?

As far as the 'resource curse' is concerned, the danger that the poor majority of the inhabitants of countries rich in natural resources will derive no profit from their resources is not just a threat, it has long since been a certainty. The reasons? Systematic corruption and aggressive tax avoidance. In the global South and East alike. Geneva's leading role in the trading of oil from Russia and Central Asia constitutes a gigantic concentration of risks for the good reputation of the whole country.

Another worrying development is one we have been able only to sketch the outlines of the boundaries between the traders and their financiers are becoming increasingly blurred. There are banks who hoard physical commodity and traders who conduct highly opaque paper trading and speculative deals that go beyond hedging in order to safeguard themselves. Herein lurk several risks at once for Switzerland's reputation:

- Glencore plays such a dominant role in so many commodities and has such a vast storage capacity that manipulating prices by creating artificial shortages or flooding the markets in the short term seems at least possible.

- Today's traders and their banks are already using their insider knowledge for reckless speculation in legal grey areas.

- Given the current international efforts (above all in basic foodstuffs) to curb these kinds of activities that push up prices and increase volatility, Switzerland threatens to become a blind spot for accountability.

SHEER INJUSTICE

It was the glaring discrepancy between the poverty in countries with mineral deposits and the wealth of some Swiss companies and their owners that prompted the authors to write this book. Yet even we were shocked by how great this discrepancy really is. In each of the world's 96 poorest countries the following is true: even if the entire population slaves away for a whole year, they will not achieve the same 'value' as six Glencore managers will have earned with their stock market flotation. But still, the global economy is and remains dependent on raw materials from finite sources in the southern hemisphere (at least until a truly sustainable economy becomes a reality). We can no longer afford to continue producing and trading these resources in a way that merely makes a few hundred managers and a couple of Swiss cantons richer. The distribution of the profits from natural resources is not a law of nature, and changes are also needed in the producing countries – to combat corruption, increase the prices of the raw materials, safeguard the population and the environment, and to invest the revenues from this resources in sustainable development. However, the main responsibility lies in Switzerland.

WHAT MUST CHANGE IN THE COMPANIES?

Swiss commodity companies, or commodity companies operating out of Switzerland, must accept their responsibility to respect human rights. Since the UN Guiding Principles on Business and Human Rights came into force in June 2011, this means that companies must develop and implement policies, measures and procedures to prevent, mitigate and account for adverse impacts in all their business activities ('Human Rights Due Diligence'). Furthermore, companies directly involved in mining should not only comply with local environmental legislation, but meet the most stringent international standards and take into account the concerns of local people. Extracting raw materials in the regions of indigenous peoples also requires the consent of those affected, consent given freely and in full possession of the facts ("free, prior and informed consent", according to the UN Declaration on the Rights of Indigenous Peoples). Last but not least, Swiss commodity traders and producers should ensure that the producing countries receive a fair share of the revenues from their raw materials. This means renouncing accounting tricks and aggressive tax avoidance and not refusing to renegotiate royalty and tax regimes.

WHAT MUST SWISS POLITICIANS DO?

Switzerland needs a coherent strategy that applies to all areas of its domestic and international economic policy, a strategy which guarantees that Swiss companies accept their responsibility to respect human rights. Switzerland must also ensure that companies, legally headquartered or carrying out core commercial operations in Switzerland, can be held responsible for any violations of human rights and environmental laws perpetrated by any of their entities. In addition the cantonal tax privileges enjoyed by holding, domiciled or mixed companies must be abolished. Switzerland should prevent companies misusing their Swiss headquarters, branch offices or subsidiaries to avoid taxes, at the expense of countries rich in natural resources. For this the following specific changes are needed:

- The Swiss Anti-Money Laundering Act must finally be applied to commodity traders as well and there is an urgent need for a comprehensive regulation to tackle the high risks of corruption in the sector.
- All details regarding ownership must be disclosed in the cantonal commercial registers so that the ultimate beneficial owners and controllers and all the intermediary company structures are equally identifiable.
- Country-by-Country Reporting must be compulsory for all companies, including those not listed on an exchange. This means that information on employees (including wages costs), on turnover, profits, financing costs and tax payments must be disclosed for all subsidiaries in each and every country.

"If there are no regulations, the law of the jungle rules,"[1] commented French President Nicolas Sarkozy at the start of 2011, fiercely condemning speculation on foodstuffs. No doubt, it's merely a matter of time before the entire commodity business, including the Swiss commodity hub, receives the international attention both of them have long since deserved. The USA have already taken a strong lead with their pioneering regulations on transparency in the 'Dodd-Frank' Act CHAP. 18 and the European Commission has proposed similar directives in autumn 2011. If Switzerland is not to become the pariah of the international community once again, it must take these clear warnings very seriously and act once and for all. There is still time to bring an end to the regulatory vacuum and implement ethical, fair behaviour in the increasingly important commodity sector. Should it succeed, Switzerland would indeed have the economic locational advantage of the future.

APPENDIX //

ILLUSTRATIONS

Audrey Gallet
Pages 18/19, 29, 33 (top), 35 (bottom), 56/57, 84/85, 92 (both), 98 (both), 106 (both), 118, 125, 134, 154, 169, 174, 212, 246/247, 249, 256/257, 273, 277, 330/331, 340, 376/377

Meinrad Schade
Pages 26/27, 33 (bottom), 35 (top), 36, 41 (both), 74/75, 80, 88, 94/95, 102, 108, 112/113, 148/149, 216, 220, 224, 226, 290/291, 298/299

Daniela Trunk
All graphs

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Cover: photographs and illustrations

Simon Barber/Camera Press/Keystone
Pages 358/359

Christian O. Bruch/Laif/Keystone
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Alfredo Caliz/Panos
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