

WASHINGTON

Washington Blocks Exports of Munitions Firm Suspected of Fraud

By C. J. CHIVERS APRIL 4, 2008

The State Department on Thursday suspended the international export activities of AEY Inc., a Miami Beach arms-dealing company led by a 22-year-old man whose munitions procurements for the Pentagon are under criminal investigation, according to American officials familiar with the decision.

The Army last week accused the firm's president, Efraim E. Diveroli, of fraud, claiming he shipped Chinese cartridges to Afghanistan after certifying they were made in Hungary. The Army also suspended Mr. Diveroli and the company from future federal contracts.

The latest decision blocks other elements of AEY's business.

Under federal rules, arms transfers across an international border in which the United States government is not the customer require a State Department license. A State Department official said that barring extraordinary circumstances, Mr. Diveroli's applications for licenses would be refused.

"AEY is under a policy of denial for future export authorization requests," said the official, who was not authorized to speak publicly and requested anonymity. Two other officials confirmed the decision. "The department may make exceptions to this policy of denial but only if there are overriding national security or foreign policy reasons to do so."

Mr. Diveroli's lawyer, Hy Shapiro, declined to comment.

AEY had been the principal supplier of munitions to Afghanistan's army and police forces since the Army awarded it a two-year contract in January 2007. The contract, now unraveling, was potentially worth \$298 million.

The company has also provided munitions and equipment to other federal agencies and to the Iraqi government. In a telephone interview last year, Mr. Diveroli claimed to do \$200 million in business each year.

His contract for Afghanistan has been beset by problems.

An examination by The Times found Mr. Diveroli shipped tens of millions of aging Chinese rifle and machine-gun cartridges from Albania, and provided munitions in crumbling and decomposing packaging. The contract and American law prohibit trading in Chinese arms.

Mr. Diveroli's company has also worked with a shell company in Cyprus and middlemen on a federal watch list of entities suspected of illegal arms trafficking, and was secretly recorded by a subcontractor in a phone conversation that suggested corruption.

His problems have grown. In early March he was charged with driving while intoxicated in Miami Beach. Late in March, Representative Henry A. Waxman, the California Democrat who leads the House Oversight and Government Reform Committee, scheduled a hearing to examine AEY's business with the Department of Defense.

On Thursday, an investigator for the Congressional committee contacted the subcontractor in Albania who had recorded phone conversations with Mr. Diveroli. There were indications, however, that Congressional inquiries could proceed only so far while the criminal investigation continued.

Marc D. Seitles, the lawyer who represents David M. Packouz, the licensed massage therapist who is AEY's former vice president, said he had sent a letter to Congress saying Mr. Packouz would speak publicly only if he was granted immunity from prosecution.

Mr. Packouz, 25, left AEY last spring and had no contact with the company since, Mr. Seitles said. Without immunity, he said, "I cannot allow my client to testify in this matter, and if he is subpoenaed he will invoke the Fifth Amendment."

The status of Mr. Diveroli's previously arranged shipments were also in question. A planned delivery of nearly two million cartridges has been idled in Slovakia, according to two Americans officials and the owner of another arms-dealing business, while the Slovak government reviews Mr. Diveroli's request for export licenses.

And MFS 2000, a Hungarian cartridge manufacturer, has also threatened legal action. Internal Army documents show that AEY purchased millions of cartridges from the company last year. Executives at MFS 2000 have said the munitions were Hungarian and in good condition.

Mr. Diveroli later certified that other munitions, made decades ago in China, had been manufactured by MFS 2000 as well, according to Army investigators. The Hungarian company suggested that Mr. Diveroli had blemished its reputation.

"MFS 2000 Inc. is absolutely guiltless in this matter," its director general, Gyorgy Karoly, wrote in an email message.

The Army has also begun to look past its relationship with AEY. A federal notice posted last Saturday sought new suppliers for millions of pieces of ammunition Mr. Diveroli had not yet delivered to Afghanistan, including cartridges, rockets and mortar and artillery rounds.

The notice showed that the Army was tightening contract standards. The contract with AEY had allowed for ammunition of any age, and did not specify that it must be packed in materials that could sustain the rigors of field conditions.

Documents from Albania showed that AEY bought more than 100 million Chinese cartridges that had been stored for decades in former cold war stockpiles. The cartridges had been manufactured as long ago as 1960.

Mr. Diveroli then arranged to have them repacked in cardboard boxes, many of which split or decomposed after shipment to the war. Different lots or types of ammunition were mixed. In some cases the ammunition was dirty, corroded or covered with a film.

The Army's new request specified the ammunition must be less than 20 years old, in durable packaging and in proper condition. "Each package will contain the same type of ammo," the Army wrote. "Materiel shall be free of dirt and other contaminants which would contribute to the deterioration of the item or which would require cleaning by customer prior to use."

Another lawyer involved in the case expressed amazement that Mr. Diveroli, who began receiving federal contracts at the age of 19, managed to continue in business so long.

AEY's office, he said, was raided by federal agents last year and its computers and records seized. But Army contracting authorities continued to work with him. "It was as if one hand of the government didn't know what the other hand was doing," the lawyer said.

C. J. Chivers reported from Moscow. Eric Schmitt contributed reporting from Washington.