

HANDS OFF IRAQI IL

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A Guide to dispelling the myths on Iraqi oil policy

Mainstream media coverage of Iraqi oil investment issues has uncritically reproduced and popularized a wide range of myths about Iraq's economic options. Iraq is currently subject to intense pressures from external actors pushing foreign economic and military interests and agendas. The reproduction of these myths reinforces these agendas. The following responses aim to challenge the largely corporate and US/UK promoted representations of Iraq's oil policy options.

An Oil Law giving foreign companies the primary role in developing Iraqi oil is about to go before Iraq's parliament. The current draft favours Production Sharing Agreements (PSAs) - exclusive 30-year contracts allowing companies to control the extraction, development, and depletion of Iraq's oil, which has been in the public sector since the 1970s.

Challenging the myths on Iraqi oil policy and the current Oil Law is an important part of the debate on resource sovereignty and the future independence of Iraq. Who should decide the future of Iraq's oil industry and through it, the economy of the country? The people of Iraq, free from duress and external pressures, or foreign companies and occupying powers?



Myth 1 - Iraq needs foreign investment



The need for investment in Iraq's oil sector is widely accepted. However, the question is where this investment should come from, and on what terms. Bringing Iraqi oil production to a peak level of 5million bpd is estimated to cost \$20-25bn over a five year period – this capital requirement of \$4-5 billion per year is achievable from Iraqi government budgets. According to the US Government Audit Office, the Ministry of Oil spent less than 1% of its 2006 capital budget of \$4 billion intended for the enhancement of production, distribution and export facilities. Iraq has funds which it can plough into its own oil industry. Alternatively, Iraq could secure loans from banks, multilateral agencies and other lenders, against projected future oil revenues.



Myth 2 - The oil law is all about a just distribution of oil revenue



1 out of 43 clauses in the Oil Law is about revenue sharing – and that clause merely states that the mechanisms for revenue sharing are the subject of a separate law. The US administration and much of the international media have represented the law as part of a peace plan for Iraq – a recipe for overcoming sectarianism. However, the US proposal that revenues be divided along sectarian and ethnic lines (in that separate law) is more likely to do the opposite.

Furthermore, the existing oil law risks enshrining sectarianised decision-making through the creation of a Federal Oil and Gas Council (Article 5c). This council will have supreme decision-making powers over how and with which companies' Iraqi oil will be developed and controlled. Its authority will exceed that of the cabinet, parliament, Ministry of Oil and Iraqi National Oil Company. Council members are likely to represent the parties and forces currently in government in Iraq. These parties have been organized along ethnic and sectarian lines rather than on the basis of political platforms.

Current competition between political forces in government with sectarian agendas and ambitions regarding the religious and political map of Iraq, could escalate if decision making powers over economic development are added to their spheres of authority. Iraq's economic development risks becoming politically sectarianised. This would have serious social and political implications for the inhabitants of those regions and risks deepening and entrenching existing divisions.



Myth 3 – Iraq Needs Foreign Expertise



Iraqi oil production was at its height in the 1970s when the industry was nationalized. Output in 1979 reached 3.8 million b/d with Iraq the third biggest oil producer in OPEC after Saudi Arabia

and Iran. Baghdad was a centre of engineering excellence until the impact of international sanctions. Many Iraqi oil specialists and technocrats were forced to flee the Baath regime, and later the dangers of the occupation. This has resulted in a 'brain drain' – the exodus or loss of many of Iraq's best minds. One solution would be to offer them lucrative incentives and maximum security to accept the risks of working in Iraq. Another alternative is to roll-out management and technical training programmes in Jordan, Kuwait and the Gulf. Many engineers and technocrats currently working inside the country are also highly skilled – in the case of the Iraqi Drilling Company in Basra – workers managed to reconstruct 12 drilling rigs following three months of looting using minimal resources and spare parts. Iraqi workers are proud of the efforts they have made to rebuild their industry and have accused the ministry of oil of withholding spare parts and equipment in order to justify private foreign investment. Where there are technical gaps (especially as a result of the sanctions), Iraq could employ foreign technology and knowledge transfer through simple technical service contracts, which could cultivate and contribute to the existing skills base and expertise within Iraq, without giving away control or property rights over the oil. The Oil Law does not set any minimum standards for foreign companies to employ Iraqi workers or give training or knowledge transfer. Foreign corporate investment under the law does not necessarily translate into a transfer or investment of foreign expertise into Iraqi companies and their workers.



Myth 4 - PSAs are normal – lots of countries have them



PSAs are commonly used in countries with reserves which are small or difficult to access (eg offshore), or where there is high exploration risk. They are not used in countries like Iraq, which has proven reserves of 115bn barrels (the world's third largest), with an additional potential total of 100bn according to Energy analysts IHS. Extraction costs are among the cheapest in the world – estimated at \$1.50 per barrel. None of the top six oil producing countries in the world use PSAs and the contracts are non-existent amongst Iraq's neighbours in the Middle East. In fact, only 12% of global oil reserves are covered by PSA contracts.



Myth 5 - The Iraqi national oil company and state institutions are too corrupt to develop Iraq's Oil



There are indeed high levels of corruption within Iraq. According to the Oil Ministry Inspector General, Iraq lost \$4.2bn through oil smuggling in 2005. The New York Times reported in May 2007 that between \$5 million and \$15 million worth of oil a day is unaccounted for in Iraq and could have been siphoned off through corruption or smuggling. But investing large sums of fresh capital into such a system would appear to be an invitation to yet more theft and embezzlement of funds. Instead, building up governmental capacity in order to monitor and manage finances and develop a culture of transparency and accountability should happen BEFORE large capital investments are made; indeed such governance measures should be seen as a prerequisite.



Myth 6 – If they're unfair, Iraq will be able to renegotiate the terms of PSAs later



In fact, common practice in oil investment contracts is that unless the terms of the contract include a specific right of renegotiation, the state will have no such rights. Thus any terms agreed at the time of signing – likely while Iraq is still weak and under occupation – would persist for the whole length of the contract

Furthermore, international investment contracts signed with foreign oil companies are likely to contain 'stabilisation clauses'. These protect the stake of companies also from any broader economic, legislative or regulatory changes which affect their profits. The state is forced to bear any costs accrued by the foreign investor relating to changes in law and investment conditions. If the state did not want to incur such costs, the companies could effectively be exempted from having to comply with new environmental or labour laws which a state could pass in the coming decades. Stabilisation clauses ensure that the contract outlives any change in government.

According to the likely terms of any contracts, any dispute between the state and companies would be settled in a remote international investment tribunal - Iraq's laws and courts would be rendered powerless. The way such tribunals work routinely favours investors over states.