

The Iraqi oil sector, privatisation and the UK's role

Submission by PLATFORM to the Iraq Commission
14 June 2007



About PLATFORM

PLATFORM is an interdisciplinary organisation, working on development, environment and human rights issues, and specialising in the impacts of the international oil industry. PLATFORM has been monitoring and researching Iraqi oil policy since 2003.

PLATFORM's research on Iraqi oil has been published by *Arab Studies Quarterly*, *The International Journal of Contemporary Studies* and *Economists for Peace and Security*. We have spoken at international and Iraqi conferences, of policymakers (including Iraqi, British and German MPs, and EU member states), of academics, of civil society, and of the oil industry. PLATFORM's partner organisation in Iraq is the Federation of Oil Unions, the largest trade union in the oil sector, with over 26,000 members. PLATFORM has also carried out training for other Iraqi trade unions, and workshops for other civil society groups.

For more information, please see <http://www.carbonweb.org/iraq>

Executive summary

1. Iraq is highly dependent on oil income, which accounts for around 95% of government revenues. Iraqi oil production has been in the public sector since the 1970s, and most Iraqis firmly believe it should stay so.
2. However, an oil law is being considered by the Iraqi parliament, which would reverse this, giving multinational companies the lead role in developing the country's oil, under contracts of up to 30 years. Depending on how it is applied, the current draft of the law could increase poverty, undermine state institutions and worsen the conflict in Iraq.
3. The Iraqi government is being heavily pressured to pass this law, primarily by the USA and the International Monetary Fund. According to media reports, advisers to Prime Minister Maliki believe that the USA threatens to bring down his government if the law is not passed.
4. The law has been wrongly described as providing a mechanism for sharing revenue among Iraq's sectarian groups; in fact, this law does not deal with that issue, which will be the subject of a separate law, not yet drafted.
5. The British government has also played a key role in influencing Iraqi oil policy, including assisting the lobbying efforts of multinational oil companies, and representing those companies. Teams of British officials in both Whitehall and Baghdad have been working on the oil law since its first draft was produced in summer 2006.
6. It is inappropriate for the UK, as an occupation power, to play a role in shaping the future of Iraq's natural resources.

7. The UK government should disclose all representations it has made in Iraq to date on the subject of oil. It should make a statement that Iraqis should make these decisions, free of external interference, and when Iraq is fully sovereign. It should refrain from further involvement in Iraqi oil policy, and should use diplomatic channels to push for its Coalition partners, and for international institutions of which it is part, to do the same.

Iraq's oil industry

8. Iraq's economy is heavily dependent on oil, which accounts for about 70% of GDP, and 95% of government revenues.¹ Iraq has the world's third largest proven oil reserves, accounting for around 10% of the total.² There is also considerable unexplored potential; recent estimates by the consultancy IHS suggest that with likely new discoveries, Iraq's reserves could double.³
9. Oil was first developed under a concession contract signed in 1925 with the Iraq Petroleum Company (IPC), a consortium comprising the precursors of BP, Shell, ExxonMobil and Total. The terms of the contract reflected the fact that it was signed whilst Iraq was controlled by Britain under a League of Nations Mandate, but those terms long outlasted the Mandate.
10. The contract was for a period of 75 years, and covered the entire territory east of the Tigris. Two subsequent contracts, one with a subsidiary of IPC, and another with a company that was later acquired by IPC, covered the remainder of Iraq. The contracts gave IPC complete control over decision-making, a monopoly on information and the right to dictate the price. It deprived the government of the right to tax IPC or its member companies, specifying instead a fixed royalty to be paid, allocating the vast majority of the revenues to the companies.⁴
11. Following decades of efforts to renegotiate the terms of the contract, its scope was finally reduced in 1961, when the consortium's oil rights were limited to the oilfields already in production. Rights to the oil in the remainder of Iraq were returned to the state. Iraq ultimately nationalised the concessions between 1972 and 1975. By the end of the 1970s, the world's oil largest oil exporters had all done the same. Since then, oil production has been in the public sector. Most Iraqis firmly believe it should remain so.
12. However, an oil law is currently being considered by the Iraqi parliament, which would reverse this, giving the primary role in developing Iraq's oil to multinational companies, under contracts of up to 30 years.⁵
13. The oil law is opposed by many Iraqi civil society groups, including trade unions⁶ and religious groups, and also by over 60 senior Iraqi oil experts (who include former Ministers and Directors General of the Oil Ministry)⁷.
14. Reliance on multinational companies is not economically necessary for development of Iraq's oil. Iraqis have considerable technical skills, and any new technology they lack can be provided under service contracts, which do not cede control over the resource, and are commonly used in the region. The capital requirement is quite achievable from public budgets, or alternatively from bank loans.⁸ The decision of where to obtain these funds is a political one.

External pressure for the oil law

15. Passage of the oil law is the most important of the benchmarks (announced in January 2007 by President Bush) that the US government insists the Iraqi government must achieve.

16. On all visits to Baghdad by senior administration officials since summer 2006, they have pressed Iraqi officials for progress on the law.
17. A report by the Associated Press in March 2007⁹ cited advisers to Prime Minister Maliki as saying that he believed that if the law were not passed by June, the USA would seek to topple his government by withdrawing military support for it. On 10 June 2007, Admiral William Fallon (Commander of US Central Command) met Maliki, to insist that the law be passed by a new deadline of the end of July.¹⁰
18. Passage of the law was also made a condition of relief of the foreign debts accumulated by the Saddam Hussein dictatorship, during his wars, and through his personal enrichment. In November 2004, the Paris Club of wealthy creditor nations agreed to conditionally cancel 80% of Iraq's debts to them in three stages: 30% immediately, 30% when Iraq entered into an International Monetary Fund (IMF) programme, and 20% following a satisfactory review by the IMF after three years of the programme. Iraq entered an agreement with the IMF in December 2005. The conditions included the passage of a law opening Iraqi oil to foreign investment, by the end of 2006.¹¹

Revenue sharing

19. The oil law has been described by the US government as a mechanism for fairly sharing oil revenues between Iraqis – a characterisation largely repeated by the media. One only has to read the draft law to see that this is not what it is about. Out of 43 articles in the law, only one (Article 11) deals with revenues. That article merely establishes two bank accounts, and states that a separate law will be passed to determine the sharing of revenues.
20. The US government argues that the allocation of shares of the wealth among the sectarian groups will help to bring reconciliation. Even if this were the content of the oil law, a more likely outcome is the opposite. Now that Iraqi politics is sectarianised, to make the economy also something to be struggled over, and ultimately parcelled out according to sectarian identity would seem only to contribute to the fragmentation of the country, and an increase in conflict.

British involvement in Iraqi oil policy

21. The UK government has played a key role in developing the oil law, alongside the US government. There are serious questions regarding the appropriateness of the UK, as an occupation power, participating in policy discussions on the future of Iraq's natural resources. While attempts have been made to describe the British role as "advice", it is highly unlikely that Iraqi officials would treat it as neutral advice, to be taken or left, given the UK's military position.
22. The origins of the policy lie in the 'Future of Iraq' planning exercise coordinated by the US State Department, whose working group on Oil and Energy met in Washington DC and London from October 2002 to April 2003.¹² That exercise brought together Iraqi exiles – many of whom subsequently became part of the Iraqi government – with US and UK officials and "international experts".
23. Future Iraqi oil policy was further developed under the Coalition Provisional Authority. During that time, former executives of multinational oil companies were appointed as senior

oil advisers. Two of these advisers were paid by the UK taxpayer, and reported to the UK authorities in Iraq.¹³

24. One of these advisers, a former head of BP Azerbaijan, subsequently continued to work on Iraqi oil policy, as a consultant to the Foreign and Commonwealth Office (FCO). In late summer 2004, he authored a Code of Practice on Business Ethics and Transparency for the Iraqi Oil Ministry. This paper argued that Iraq would need multinational companies to develop its oil sector, so should develop policies compatible with those of the companies. The paper reproduced BP's transparency policy in full.¹⁴
25. Six oil companies collectively appointed lobbyists, the International Tax & Investment Centre (ITIC), to push for Iraq to offer long-term oil production contracts known as production sharing agreements. ITIC was advised by officials of the FCO and HM Treasury on their strategy for influencing Iraqi decision-makers.¹⁵
26. ITIC's primary lobbying document, entitled *Petroleum and Iraq's Future*,¹⁶ was sent to the Iraqi Minister of Finance in late 2004 by the British Ambassador to Iraq. According to ITIC, he "formally" submitted it to the Minister, implying UK endorsement of its contents¹⁷, and likely increasing the seriousness with which the Minister would have taken it. The FCO denies any endorsement, and now claims that the Embassy was merely acting as a delivery service.
27. A diplomat from the British Embassy played a key role in organising a meeting of ITIC and its six oil company sponsors with Iraqi ministers and officials in January 2005: suggesting invitees, and delivering invitations to them.¹⁸ Again, the involvement of the UK – a military power in the country – will have encouraged Iraqis to pay more attention.
28. Since the completion of the first draft of the oil law in July 2006, British officials in both Whitehall and Baghdad have actively worked on the law. It was first seen by British officials in July, eight months before it was seen by members of the Iraqi parliament, who first saw it in March 2007.¹⁹
29. The FCO Minister of State responsible for the Middle East told the House of Commons in February 2007 that in these efforts, the UK government had sought the views of multinational oil companies, *inter alia*, on the types of contracts they wanted to see in Iraq.²⁰

Likely consequences of UK involvement in Iraqi oil policy

30. This British (and American) influence is likely to undermine the legal or political sustainability of the Iraqi oil law. It is likely to be considered a product of occupation, and of coercion – including potentially by international courts.
31. In June 2006, a survey by the University of Michigan found that 76% of Iraqis believe that "to control Iraqi oil" was one of the main reasons for the war.²¹ UK involvement in oil policy decisions is likely to reinforce this suspicion, and damage the UK's reputation in the region and internationally, as well as in Iraq.
32. That UK officials have played a larger role in the oil law than Iraqi parliamentarians (and whilst Iraqi civil society has been excluded altogether) is likely to undermine the credibility of UK claims to support democracy and human rights in Iraq.

Possible consequences of the oil law

33. Depending on how the oil law is implemented, as currently drafted, it could increase poverty, damage the viability of the state and the democracy of its institutions and further worsen the conflict.
34. In the current circumstances – of occupation, daily violence and political divisions in the institutions of state – Iraq’s bargaining power in negotiations on any contracts would be extremely weak. Meanwhile, oil companies would insist on ‘risk premia’. The result would be contracts with economic terms highly favourable to investors, at the expense of government revenues, but long outlasting the circumstances in which they are signed – just as happened in 1925. Similar problems, of unbalanced terms, were seen in the oil contracts signed in the former Soviet republics during the rapid changes of the early 1990s.²²
35. This loss of revenues to the state would constrain future Iraqi governments’ resources to provide much-needed services and reconstruction. The draft oil law (Article 33D) also allows 100% repatriation of investors’ profits, depriving Iraq’s economy of the reinvestment of oil proceeds.
36. Multinational companies commonly rely more heavily on technology and capital investment than state-owned oil companies, and employ correspondingly smaller workforces. Meanwhile, important technical and management roles tend to be given to expatriate staff. The draft oil law places no lower limit on the hiring of Iraqis, or procurement of goods and services from Iraqi companies (Article 15). Thus the oil law is likely to increase unemployment, estimates of which already range from 30% to 70%.
37. Decisions on the development of Iraq’s oil would be transferred from government to private foreign companies: this could deprive the government of the ability to manage its economy, for example, by setting depletion rates of oilfields. Furthermore, oil production contracts commonly contain stabilisation clauses, which are designed to protect investors from any changes in legislation – these could restrict the ability of future Iraqi governments to regulate the oil sector, or even to pass any new laws if they affected oil company profits.²³
38. Even though a single large oilfield could account for a large share of government revenue, the terms of contracts would not be subject to parliamentary scrutiny, under the draft oil law.
39. Iraq currently suffers from chronic levels of corruption, which not only impede development but also help to finance militias and terrorists. If large-scale foreign investment takes place before significant progress has been made on tackling this, it is very likely to exacerbate this problem.
40. It is unclear whether multinational companies would invest in the current security environment: many have said that they would not; some US government officials and analysts say that this concern, while real, is overstated. According to one oil company representative, “Security is an issue – but everyone’s realistic, you’re not going to wait until it’s perfect.”²⁴ This assessment is probably right – whether that time is now or later, the point at which companies decide to invest is likely whilst there is still serious violence in the country.
41. The past record of the companies shows that they are able to operate in conflict zones, such as Colombia and Nigeria. However, in these cases, security forces (whether public or private) protecting the oil facilities have tended not just to defend oil installations from physical attack, but also to proactively target any threats to oil company interests, and this role has extended to

unarmed critics of the companies.²⁵ In the case of Iraq, a new set of interests protected by well-armed force is perhaps the last thing the country needs in the current situation.

Recommendations

42. The UK government should disclose all representations it has made to Iraqi officials on the subject of oil policy and the oil law.
43. The government should publicly state that it is for Iraqi people to decide the future of their natural resources, without external pressure or influence. It should refrain from further substantive engagement on Iraqi oil policy.
44. The government should recommend that the Iraqi government not make long-term decisions about its natural resources until there has been a full consultation with Iraqi civil society groups, and until Iraq is fully sovereign, free of foreign troops.
45. The UK should call on its Coalition partners to cease efforts to influence the oil law, and especially should ask the USA to drop its benchmark for passage of the oil law.
46. The UK should ask for international institutions of which it is part – including the International Monetary Fund, the European Union, the Paris Club and the United Nations – to refrain from intervening in Iraqi oil policy. Specifically, it should ask the Paris Club and IMF to drop conditionalities associated with the oil law.

Footnotes

¹ IMF (International Monetary Fund), December 2005, Request for Stand-By Arrangement, pp. 19, 27; at <http://www.imf.org/external/pubs/ft/scr/2006/cr0615.pdf>

² BP, 2006, *Quantifying energy - BP Statistical Review of World Energy*, <http://www.bp.com/productlanding.do?categoryId=6842&contentId=7021390>

³ IHS Inc, 18 April 2007, 'IHS launches first detailed report on Iraq's oil reserves and production potential since start of Iraq conflict', at <http://www.ihs.com/News/Press-Releases/2007/IraqAtlas.htm>

⁴ See, for example, George Stocking, 1970, *Middle East Oil*, Vanderbilt University Press (Nashville)

⁵ The law has been translated by the Kurdistan Regional Government, and is available at http://www.krg.org/uploads/documents/Draft%20Iraq%20Oil%20and%20Gas%20Law%20English_2007_03_10_h23m31s47.pdf Another translation, by Raed Jarrar, is available at http://www.al-ghad.org/wordpress/wp-content/uploads/2007/02/iraqi_oil_law.pdf

⁶ Statement issued by the Iraqi Labor Union Leadership at a Seminar held from 10 to 14 December 2006, in Amman, Jordan to discuss the draft Iraqi Oil Law, available at <http://www.carbonweb.org/showitem.asp?article=222&parent=4>

⁷ The Preparatory Committee for the symposium Iraqi oil experts, 17 February 2007, Letter to the President and the Members of the Iraqi House of Representatives, available at http://www.iraqrenewwatch.org/documents/symposium_oil_experts.pdf

⁸ This point has been demonstrated by numerous Iraqi and non-Iraqi experts. See for example, Helmut Merklein, 2006, 'Who needs Big Oil in Iraq?', *Middle East Economic Survey*, 49:29, 17 July, pp.25-29, and 49:30, 24 July, pp.29-33

⁹ Associated Press, 14 March 2007, 'Iraqi Leader Fears Ouster Over Oil Money', by Steven R Hurst

¹⁰ *New York Times*, 12 June 2007, 'U.S. Warns Iraq That Progress Is Needed Soon', by Michael Gordon

¹¹ IMF (International Monetary Fund), December 2005, Request for Stand-By Arrangement, pp.14,17,18; at <http://www.imf.org/external/pubs/ft/scr/2006/cr0615.pdf>

¹² US State Department, Future of Iraq Project, Oil and Energy Working Group (Oil Policy Subgroup), April 2003, published in *Middle East Economic Survey*, 5 May 2003, 'Iraqi oil policy recommendations after regime change', pp.D1-D11

¹³ Dr Kim Howells MP, 13 July 2005, answer to Parliamentary Question by Harry Cohen MP, Hansard column 1123W

¹⁴ FCO, undated (late summer 2004), Code of Practice for the Iraq oil industry, 'Transparency and business ethics and the long-term renewal of the Iraqi oil industry', authored by Terry Adams. Obtained by PLATFORM through the Freedom of Information Act.

¹⁵ Email correspondence between ITIC, FCO and HMT, Sept-Oct 2004, obtained by PLATFORM under the Freedom of Information Act

¹⁶ Available at www.iticnet.org/publications/Iraq-book.pdf

¹⁷ ITIC Bulletin, Nov/Dec 2004, p.8, available at <http://www.iticnet.org/publications/ITIC%20Bulletin%202004%20November%20December.pdf>

¹⁸ Telephone interview of Dan Witt, President, ITIC, 17 May 2006 (interviewed by PLATFORM)

¹⁹ Personal communication with UK officials

²⁰ Kim Howells MP, 19 February 2007, response to parliamentary question by Alan Simpson MP, available at

<http://www.publications.parliament.uk/pa/cm200607/cmhansrd/cm070219/text/70219w0024.htm#0702212003190>

²¹ University of Michigan, 14 June 2006, 'Iraq attitudes: Survey documents big changes', available at www.umich.edu/news/index.html?Releases/2006/Jun06/r061406a

²² Muttitt, G., 'Nationalising risk, privatising reward', in *International Journal of Contemporary Iraqi Studies*, forthcoming June 2007 (available on request)

²³ Hildyard, N. and Muttitt, G. (2006), 'Turbo-Charging Investor Sovereignty – Investment Agreements and Corporate Colonialism', *Destroy and Profit - Wars, Disasters and Corporations*, pub. Focus on the Global South, <http://www.focusweb.org/destroy-and-profit-wars-disasters-and-corporations.html?Itemid=94>

²⁴ Rowell, A. (2006), 'Undue influence', *al-Khaleej*, 4 June, published in Arabic; English original sent by author

²⁵ See, for example, *The Guardian*, 17 October 1998, 'BP hands tarred in pipeline dirty war', by Michael Gillard, Ignacio Gomez, and Melissa Jones; Andrew Rowell, James Marriott and Lorne Stockman, 2005, *The Next Gulf*, Constable (London)