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Oil and Paper: Ownership, Economic Development, and Iraq's 2007 Draft Oil and Gas Law

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OIL AND PAPER: OWNERSHIP, ECONOMIC DEVELOPMENT,
AND IRAQ'S 2007 DRAFT OIL AND GAS LAW

A Dissertation

Submitted to McAnulty College and Graduate School of Liberal Arts

Duquesne University

In partial fulfillment of the requirements for
the degree of Master of Arts

By

Peter Jackson

May 2009

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Peter Jackson

2009

OIL AND PAPER: OWNERSHIP, ECONOMIC DEVELOPMENT,
AND IRAQ'S 2007 DRAFT OIL AND GAS LAW

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ABSTRACT

OIL AND PAPER: OWNERSHIP, ECONOMIC DEVELOPMENT, AND IRAQ'S 2007 DRAFT OIL AND GAS LAW

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Peter Jackson

May 2009

Thesis supervised by Dr. Kent Moors

The 2007 Draft Oil Law's parliamentary collapse demonstrates that Iraqi legislation must settle the issue of ownership prior to determining foreign investment rules. The draft law has been criticized by western academics for its economic benefits to international oil companies, but in Iraq the law has been rejected more for its ambiguities and its lack of specific ownership language, apart from four disputed, classified annexes listing classifications of oil fields. Rather than pass empty legislation and fill it up at a later point, Iraq must draft its oil revenue sharing laws, model contracts, and an oil ownership law in tandem with creating contract law to sell oil rights.

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LIST OF ABBREVIATIONS

CIA	Central Intelligence Agency
FOI	Future of Iraq Project
ICP	Iraq Communist Party
ID	Iraqi Dinars
IMF	International Monetary Fund
INOC	Iraq National Oil Company
IOC	International Oil Companies
IPC	Iraq Petroleum Company (British)
KRG	Kurdistan Regional Government
Mbbl/d	Million barrels per day
OPEC	Organization of Petroleum Exporting Countries
PSA	Production Sharing Agreement
PUK	Patriotic Union of Kurdistan
RCC	Revolutionary Central Command
UNSCR	United Nations Security Council Resolution

All currency is expressed in terms of US Dollars.

Executive Summary

In a letter to the International Monetary Fund (IMF) dated 6 December 2005, the Iraqi interim government promised several conditions in return for approximately \$31.7 billion (bln). The money was offered in the form of a \$685 million loan and an 80 percent reduction of Iraq's \$38.7 bln international debt, with a six-year debt freeze period. Four years later, the last 20 percent debt reduction (worth nearly \$8 bln by itself) is pending only a final review by the IMF, and the loan has recently been renewed for \$744 million—but the help didn't come free. Perhaps the most dramatic requirements to grow out of the IMF deal were a December 2006 deadline for an Iraqi draft oil law and a mandate for US-supplied "assistance" in the project. International observers feared the worst; news reports claimed the new legislation would open up Iraq's oil industry—nationalized since 1975—to the sole benefit of domineering international oil companies (IOCs) and the Anglo-American powers. Amidst the mounting general opposition to the Bush administration, arguments began to form against the concepts of privatization, decentralization, regional autonomy and the presence of IOCs in Iraq.

A large part of the debate centered on Production Sharing Agreements (PSAs) and decentralization. Observers feared that the Bush administration was pressuring Iraq to include both concepts in the oil law for the good of the international oil industry, demonstrating that the two elements would prove dramatically harmful to Iraqi's economy. Business models, like the 2005 study *Crude Designs* from the Platform group, showed that PSAs are significantly less beneficial to nations with low-cost, high-volume oil reserves like Iraq; the estimated "loss" to Iraq (in terms of capital not realized) was in the ballpark of \$100 bln over 30 years. On decentralization, academic papers like Exeter

professor Dr. Kamil Mahdi's analysis, "Iraq's Oil Law: Parsing the Fine Print," pointed out that allowing smaller regional governments to settle contracts with IOCs—as the decentralized model would dictate—forces Iraqi negotiators into a position of greater weakness, resulting in contracts far less beneficial to Iraq than they should be.

In 2006, a working draft of the Oil and Gas Law, which was under construction in a subcommittee of Iraqi Prime Minister Nouri al-Maliki's cabinet, was leaked to the press. The law confirmed many observers' fears, calling for a return in part to PSAs and allowing regional governments the authority to negotiate them. However, the law also reorganizes the Iraqi National Oil Company (INOC) to oversee and produce a number of oil reserves. Four annexes attached to the draft law spelled out which oil fields belonged to regional control, and which were under the authority of INOC—but the annexes were classified and unavailable to the public, in which state they remain today. Arguments over the draft law's annexes raged behind closed doors. In Parliament, the Kurds parted with their Shi'ite political allies to stall the draft after it was presented by a united al-Maliki cabinet in February 2007, and staged another legislative block in 2008 to keep the law from coming to the floor for debate. Four amended versions of the law and its annexes were submitted to parliament; none were successful.

Kurdish opposition to the gas law is very likely incentivized by the disputed Kirkuk Super Giant oil field, which dominates in the northern Kurdish section of Iraq. While the annexes seem to designate the profitable Kirkuk field to the INOC, Kurdish parliamentarians see that regional control of the oil field would be incredibly profitable for their region. Meanwhile, Sunni elements in Parliament would prefer increased control by INOC, whose profits are dispersed more directly to the national government,

since the western Sunni regions are largely oil-dry. That these debates are being held over annexes to the law—not over the law itself—suggests that the issue of ownership and regional profitability from oil is a more important question than the time given it in the actual legislation.

The draft law leaves several key elements to be determined by future legislation; one is a model PSA, which does much to set the parameters and profitability of IOC participation in Iraq's petroleum industry; the other is the Iraqi oil revenue-sharing law, which would determine the distribution of the nationalized funds generated by the oil legislation through royalties and profit taxes. The exclusion of such potentially divisive and powerful pieces of legislature is reminiscent of the 2005 Iraqi Constitution's whole approach to oil ownership and legislation: oil is owned by "the Iraqi people," according to the Constitution; similarly, it is governed, in the Constitution, by laws which "will be developed" at a later time. The 2007 legislation certainly improves on the Constitution's ambiguity, but it sadly imitates the vague bullet-dodging that characterized the Constitution's approach to oil law.

The difficulties of oil legislation are compounded by ancient cultural, religious, and ethnic differences of the oil-rich Kurds in the northeast, oil-rich Shi'a Arab majority in the southeast, and the oil-poor Sunni Arabs in the western deserts and central urban areas of Iraq. While the draft law tries to achieve both a strong national, centralized oil industry while providing opportunities for privatization and decentralized revenues, years of oppression and suppressed internal conflict have made compromise a foreign language in Iraq. Rather than pleasing all sides in the argument, as seems to have been the intent,

the law appears to have raised the suspicion and ire of every political bloc in Iraq and among international observers who have weighed in over the last few years.

This paper argues that the draft's fatal flaw is its ambiguity, particularly in regards to ownership of the oil revenues and the parameters of foreign investment in Iraq. Not everyone can win in politics, and the Iraqis know it: until they know who loses, the draft law will never pass. Indeed, as far back as 2003, ownership rights were acknowledged as an absolute necessity and a precursor to determining contract law for Iraqi oil: in a report on Iraq's economy, the Congressional Research Service found that "first, clear title to [Iraq's] crude must be established, so that a would-be purchaser can be assured that he is buying oil from its rightful owners." By some appearances, the four unclassified annexes, which group oil fields into groups of "producing," "close to production contract," and "far from production contract," do attempt to solve the ownership question. However, there are two problems with the annexes: first, they are not public and so do not inform the public debate; second, they speak nothing of revenues and ownership, only of contractual authority.

Simply put, it is necessary for Iraq to answer the questions that have plagued their oil industry since the 2005 Constitutional ambiguity. This report finds that it should be possible to attract international investment with shorter-than-usual PSA contracts, minimizing the capital "lost" or not realized while still inducing the necessary international investment required to refit and revitalize the Iraqi oil industry. Decentralization is also found to be a less significant problem than anticipated, pulling on the draft law's provision for allowing smaller localities to join together to form larger regional negotiating parties. Overall, the draft law is smart and well-balanced, but in

crucial need of transparency, clarity, and a specific ownership clause. To this end, the annexes should be declassified as far as possible without violating industry norms, and the oil revenue law and model PSA contracts should be drawn up by the Oil Ministry for consideration as a party to the proposed legislation—not as an afterthought. Finally, this paper suggests that the draft law may be significantly improved by separating the issues of ownership into a separate legislative piece for the sake of separate, precursory debate to the long-forestalled oil legislation.

Chapter 1: The History of Modern Iraq

Before examining the proposals for Iraq's oil industry in its current situation, it is only appropriate to review the path of the industry from the era of the British Mandate and the Iraq Petroleum Company to the US invasion of 2003. From the concessionary period under the British to the total nationalization of the oil industry under Saddam Hussein, Iraq has experienced the full range of approaches to industry organization; similarly, from the vast profits of the early 1970s to the UN sanctions after the Kuwait war, Iraq has also run the gamut of industry profitability. This chapter will examine the history of modern Iraq, specifically focusing on the elements and situations that influenced the evolution of the oil industry.

It is safe to say that modern history in Iraq begins with WWI and the British Mandate in Iraq. Originally interested in Iraq for its importance as a trade route to their investments in India, Britain became more involved in Iraq after the 1908 discovery of significant oil deposits. A year after the discovery, the Anglo-Persian Oil Company was founded; by 1914, the refinery at Abadan was exporting a quarter of a million tons of oil annually (Farouk-Sluglett 8). Interested in oil for naval fuel, the British Parliament acquired a 51 percent holding in the Anglo-Persian company a few days before the outbreak of World War I; this provided a pretext for the invasion and subsequent occupation of Iraq when the ruling Ottoman empire—whose government in Mesopotamia dated back to 1534—joined the Germans in WWI and declared war on the British. In 1920, the League of Nations awarded Britain the mandate of all Iraq, and promptly set up a proxy monarchy in 1921, granting the minority Sunni population control.

Much has been said in condemnation of the British occupation in Iraq, and much of it is criticism well deserved, but it also must be understood that the resistance they encountered was, in large part, inherited. After 381 years under Ottoman rule, Iraqis were already in a persistent state of uprising; it is doubtful whether the British would have succeeded against the Ottomans in Iraq without British General Stanley Maude's proclaimed commitment to Iraqi self-governance, which led to a 1916 Arab revolt against the Ottomans. This revolt was significantly led by the Hashemite Sharif Husain of Mecca and his sons—one of whom, the Hashemite Amir Faisal, would later become the King Faisal I in Iraq's British-installed Hashemite monarchy (Tripp 32-33). Despite the Iraqi support, reciprocating respect from the British was in short wartime supply: "Maude's proclamation and the British assurances to Sharif Hussein were in direct contrast to the secret French-British 1916 Sykes-Picot Agreement [which] agreed to divide up the Ottoman territories into 'zones of influence' at the conclusion of hostilities. France would control Syria, Lebanon, and the province of Mosul, while Great Britain would gain dominion over the provinces of Basra and Baghdad" (Hunt 60-61). While the Sykes-Picot Agreement was superseded by the League of Nations, the contrast of public promises and private politics seems to have been a precedent set at the very dawn of the West's involvement in Iraq.

The Treaty of Versailles, by ending World War I and eliminating the Ottoman Empire, gave Arab leaders a false hope for dividing the Middle East into nations along their own cultural and social borders. Instead, Versailles decreed that the formerly held Ottoman territories would be divided into "mandates" governed by the European allies, setting up the San Remo conference to further delineate the region's governance. Thus,

in April 1920, the League of Nations created the modern map of the Middle East—creating arbitrary geometric nation-shapes with scant apparent concern for traditional boundaries, rivalries, and the impact such delineations would have on the local cultures and realities. Being such a product of uninformed statecraft, the new Middle East map manufactured difficulties and disadvantages for every nation it created, but in Iraq the problems were particularly severe. The creation of Kuwait, which had been grouped with Basra and Baghdad under the Ottoman rule, was apportioned away from the new mandate of Iraq; occupying 499 Kilometers (km) of coastline, the separation of Kuwait reduced the functional coastline of Iraq to 58 km, critically constricting the nation's maritime export industry. The League of Nations also discussed, in passing, the concept of creating a separate Kurdish region in the north as a buffer between Iraq and Turkey, and also debated splitting Iraq into two states in order to compensate for the Baghdad-based Sunni population and the Basra-centered Shi'ites; these two ideas were scrapped, however, leading to an oppressive rivalry and cultural tension in the nation that persists to current times.

1921-1958: The Monarchy

Already incited by European disregard for local traditions and realities, Arab leaders in Iraq reached a critical level of protest after the San Remo conference. To satisfy their mandate in Iraq, "the British intended to rule by proxy and set up a temporary government. They made no effort to align themselves with the local Arab leaders, but instead partnered with the Ottoman rulers and elite who remained in Iraq" (Hunt 62). In 1920, Iraqi elites led a popular uprising against the British, which resulted

in an Iraqi siege of British-held Baghdad before being quelled by the arrival of significant British reinforcements. The uprising marks the first significant collusion between the Shi'a, Sunni, and Kurdish elements in the area of modern Iraq. Unfortunately, further cooperation was precluded by Britain's next move, which installed a Sunni monarchy in Baghdad and set up a future of unbalanced power between the three major cultural factions in Iraq.

The 1920 uprising, along with the escalating cost of maintaining peace in Iraq, pushed the British to take another approach to their mandate. At the Conference of Cairo in March 1921, Winston Churchill, T. E. Lawrence, Gertrude Bell and other British politicians and Middle East authorities met to discuss the fulfillment of the British mandate in Iraq. The conclusion at Cairo found it most suitable to install a British-supported (and, therefore, both hand-picked and indebted) parliamentary monarchy in Iraq; for this purpose, the conference looked to the Western-educated Amir Faisal, son of the Hashemite leader who had helped the British against the Ottomans in WWI. Faisal was considered to have "a natural authority in the Arab world, but, equally importantly, he was believed to be amenable to British advice and well aware of the limitations that the reality of British power in the Middle East would place upon his ambitions" (Tripp 47).

In the fall of 1921, a one-question voting referendum was used to theoretically legitimate the rule of King Faisal I, who brought with him a loyal court of Sunni pan-Arab nationalists. Faisal's government promptly established a 20-year treaty with the British, securing a Western influence in Iraq and promising to consult with Britain on all matters of economic and foreign policy. In return, Britain financed the rebuilding and

development of Iraq's military and infrastructure. In 1924, Faisal's government also drafted a constitution, establishing the relative powers of the monarchy and the parliament and granting the king indirect power over the parliament through his ability to call for elections and confirm the laws of parliament (Hunt 66).

The British erroneously believed that the Hashemite dynasty would enjoy an implicit popularity with the Iraqis, being one of the older and more traditional Sunni families and having a track record of Arab leadership in Iraq. However, Britain failed to recognize their installed king's weakness with the majority Shi'a population. To risk an oversimplification, Shi'ism began in the belief that the leadership of the Islamic population (*ummah*) must personified by a direct descendent in Muhammad's bloodline; specifically, the original Shi'a were a minority who believed that the successor to Muhammad should have been his cousin and son-in-law, Ali. Originally called *Shi'ya* for "partisan," Shi'ism has "attracted the adherence of groups that were dissatisfied with the [Islamic religious] government for a variety of reasons" (Wiley 150). Alternatively, Sunnis believe that the successor of Muhammad may be elected from among any of the leaders of Islam. In Iraq, the Sunni population—which is the majority denomination globally, but remains a minority in Iraq and Iran—has tended to drift towards a more liberal, inclusive, pan-Arabic interpretation of Islam, whereas the Shi'a population is often characterized by very conservative beliefs and exclusivist religious attitudes. The installment of a Sunni king set a precedent that would outlast the monarchy: after the revolution of 1958, the Ba'athist party, with roots in Syrian Sunni academia, also heavily favored the Sunni population and took a largely secular approach to government.

In 1927, a major oil field was found near Kirkuk in northern Iraq, prompting the creation of the European-owned Iraq Petroleum Company (IPC) the next year. The United Kingdom followed with the negotiation of the Anglo-Iraqi Treaty of 1930, promising sponsorship to the League of Nations at the time of the Mandate's expiration in 1932 in return for a variety of commercial and military rights in independent Iraq—thereby also earning an imbalanced influence on the affairs of the IPC. This treaty, in turn, influenced the balance of power in internal Iraqi politics: "The most obvious difference between the politics of the 1920s and those of the 1930s was the emergence of the armed forces, or more correctly of factions within the armed forces, as a new locus of political power, although in many ways this was a change of style more than substance" (Farouk-Sluglett 14).

World War II had a profound impact on the economics and internal political situation in Iraq, setting up the possibility for a labor-centered revolution. One of the most significant developments was the rise of Iraqi labor unions: "between 1944 and 1946, a total of sixteen labor unions, twelve of which were controlled by the communists, were granted licenses. The largest unions were formed in the country's most important industrial undertakings, Basra Port, and the Iraqi Railways, which were both under British management. Major strikes for higher wages took place on the railways in 1945 and at the port in 1947" (Farouk-Sluglett 38-39). Additionally, Iraq joined the United Nations in 1945, sponsored by the British, and oil exports began increasing dramatically. The most significant growth in the industry occurred in 1952, growing from 8.4 million metric tons and 13.8 million Iraqi Dinars (ID) in 1951 to 18.2 million metric tons and

39.7 million ID the next year—an increase of 117% export totals and 188% profits (al-Marayati 192).

The clearest reason for this incredible change was a February 1952 agreement with the IPC, whereby "the IPC and the Iraqi government agreed to share profits on a '50-50' basis, IPC guaranteed a minimum revenue for the Iraqi government, agreed that Iraq could receive up to 12.5 per cent of the net production as part of its share, to sell on the world market, and agreed to the appointment of Iraqi directors to the board when the question of oil prices came up" (Tripp 128). A similar deal had been struck between Aramco in Saudi Arabia in 1951, and in Iran the oil industry had undergone total nationalization; these events inspired many elements in Iraq to make demands for a similar system—while also providing pressure for the IPC to cave (Farouk-Sluglett 43-44). At the same time, Iraqi resentment of Britain was reaching new highs under the strictures of the 1948 Portsmouth Treaty, which had allowed the British to reaffirm their hold on Iraqi economic and foreign policies. To the rising nationalist political movements, Portsmouth—along with the formation of Israel in 1948—only increased their motivation to succeed in their struggle for true sovereignty (Hunt 75).

All of these strains were also coming together to compose a significantly favorable atmosphere for the Ba'athist party. Begun by Syrian anti-imperialist academics in 1944, one of the Iraqi Ba'athist party's main tenants was the nationalization of industry and the eviction of imperialist interest. The Ba'athist party in Iraq at this time was led by a young Shi'ite scholar, who fit the mold of most adherents to Ba'athist ideology: "Arab nationalist and secular, but not atheistic and vaguely socialist in orientation, the [Ba'athist] party was critical of the more glaring inequalities of land ownership in the

Arab world. As such, its message was attractive for students and for others growing restive at the domination of an older, more conservative and more exclusive elite of Arab nationalists" (Tripp 143). However, religious Shi'ite leadership of the increasingly secular Ba'ath party led to a crisis of identity that crippled the party in the coming 1958 overthrow of the monarchy, leading to the rise of the Communist party until the Ba'athists could reorganize under Sunni leadership.

1958-1968: Revolving-Door Revolutions

On 14 July 1958, the modern state of Iraq established three precedents: 14 July became the celebrated day of Iraqi independence; the nation became officially the Republic of Iraq; and the monarchy was overthrown by military strongmen (Hunt 76). The coup, carried out by a military group called the Free Officers, was led by Abd al-Salam Arif and Abdel-Karin Qasim; Qasim was installed thereafter as Prime Minister. The new political leader, a son of both Sunni and Shi'a traditions, was perhaps the most balanced leader Iraq could have asked for; unfortunately, his success was limited by the dilapidated state of Iraq's infrastructure and by his own illusion of his representative capability for the Iraqi people (Tripp 151). The other limiting element on Qasim's effectiveness was the political struggle between Iraqi nationalists and the pan-Arab nationalists.

Qasim, who was described as being "more reformist rather than revolutionary," withdrew from Iraq's treaties with Britain but then began reaching out to nearby communist and socialist countries, including Russia, for help (Farouk-Sluglett 54). Related to building relations with the Eastern side of the Iron Curtain, the Iraqi

Communist Party (ICP) was allowed free reign to publish and organize, and in many ways came to be seen for the duration of Qasim's tenure as the primary political party in Iraq (Tripp 154). In 1960, under pretense of returning to the Ottoman bureaucratic divisions, Qasim announced its ownership of the newly-liberated Kuwait, but the proclamation was quickly dismissed as rhetoric, and any follow-through was deterred by the immediate deployment of British forces to Kuwait. 1960 was also significant for the creation of the Organization of Petroleum Exporting Countries (OPEC), a trading cooperative with enough market power to control the global price of oil in a significant way.

The Ba'athist party in Iraq, whose contribution to the 1958 revolution had been minimal at best, began its true gamble for power in 1959 with a failed assassination attempt on Qasim that led to a purging of the Ba'athist party in Iraq. The attempt was led by a young Saddam Hussein, who was at that time a young rising star in the party. After 1959, the Ba'athist party was forced into hiding. Using clandestine tactics, by 1962 the Ba'athists had established operatives in important political offices and military positions, waging a publicity battle against the ICP, and establishing a mobile popular base that could generate crowd support at crucial moments (Tripp 162). Meanwhile, although Qasim's rule had become increasingly despotic, "Qasim appeared to emerge as a genuinely popular leader of Iraq. Under his direction, oil revenues had been redirected towards the immediate needs of the poorer sections of society. Numbers of pupils and students at all levels of education trebled during this period and there was a burst of school-building activity" (Tripp 167). Qasim was also responsible for the cunning Law 80 of 1961, which nationalized 99.5% of the known oil fields—but left the IPC to

continue operations on its production-active oil fields, which fell well within the remaining half of a percent. The move satisfied the nationalists who argued in continued opposition to the memory of British imperialism, but it prevented the economic hemorrhaging that would have resulted from closing down the IPC.

1963 was a turbulent year for Iraq. The clandestine organization of the Ba'athist party finally put an enormous number of armed civilians on the streets, simultaneously calling on their allies and assets in the government and military to effect an overnight coup d'état. A subsequent ruling committee elected Qasim's original ally in the 1958 revolution, Abd al-Salam Arif, as President—a position with more apparent show than power in a nation run by the Ba'athist party, but still with direct control over the main military. Through the year of 1963, the various factions that had come together to form the Ba'athist revolution of 1963 turned inward and tore themselves apart, unable to agree on many things but significantly divided over the question of pan-Arab nationalism in light of Egypt and Syria's United Arab Republic (Tripp 173). In an unexpected move at the close of 1963, Arif exercised the power of his presidency and established military dominance over the Ba'athist civilian forces, pressing the Ba'athists out of power.

Arif died in a 1966 helicopter accident and was replaced by his brother until 1968, when a revolution of both non-Ba'athists and Ba'athists retook the capital and deported the Arif government. As in 1963, by the end of 1968 a second revolution had occurred; unlike the earlier revolution, this time the second move solidified—rather than removed—the Ba'athist control on power, eliminating their non-Ba'athist allies. Throughout the revolving-door governments of the 1950s and 60s, the Iraqi people had "continued to be denied representation, and thus the passing array of military rulers had

felt no need to account for their actions, reinforcing the tendency to look upon the state primarily as an instrument of power, in the service of those who had seized command at the center" (Tripp 192). This perception continued to be a significant obstacle to the establishment of democratic institutions in Iraq, even a near half-century later.

1968-1979: Ba'athist Beginnings

From 1968 to 1979, Iraq enjoyed the relatively stable tenure of President Ahmad Hasan al-Bakr, who had previously served as the Prime Minister during the brief Ba'athist reign from February to November of 1963. Al-Bakr's administration finished the nationalization of the oil industry and enjoyed the immense oil profits of the early 1970s. A relative of Saddam Hussein, al-Bakr appointed the now 31-year-old Hussein to the position of Deputy Chairman of the Revolutionary Central Command (RCC) in charge of intelligence.

At this post, Hussein was given the task of designing the *Jihaz Haneen*, "a special unit of the Iraqi branch of the Arab Ba'ath Socialist Party conceived in clandestinity sometime between 1964 and 1966, selected from the most committed cadre who became specialists in intelligence matters" (al-Khalil 5). Hussein used this unit to adjust the political scene in Iraq to his own advantage, creating an atmosphere where "the capacity of any other individual to remain in a position of power was almost entirely dependent on the degree of his acceptability to the Deputy Chairman of the RCC. Equally, those who disagreed with Saddam Hussein, or who posed a threat, actual or potential, to his position, were either summarily dismissed or, if they had a major power base of their

own, gradually eased out" (Farouk-Sluglett 134). When al-Bakr resigned in 1979, Saddam had created a secure context for his own ascension to power.

In 1971, three oil companies were producing every drop of oil in Iraq: the IPC and its two offshoots, the Mosul Petroleum Company (MPC), and the Basra Petroleum Company (BPC); at the end of the year, President al-Bakr announced that the IPC would no longer enjoy such a monopolistic relationship with Iraq, calling for negotiations in early 1972. Accomplishing little in these negotiations, other than an IPC drop in production (and therefore revenues) in retaliation, Iraq turned to the Soviet Union and signed a fifteen-year Iraqi-Soviet Friendship Treaty, "providing for cooperation in political, economic, technical cultural, and other fields" (Farouk-Sluglett 147). The al-Bakr administration then issued an ultimatum to the IPC on May 18, 1972: restore production or face nationalization. Consequently, after 44 years of concessionary profits, the IPC was fully nationalized in Iraq on June 1, 1972, closing the last significant relic from the British imperialist experiment in Iraq.

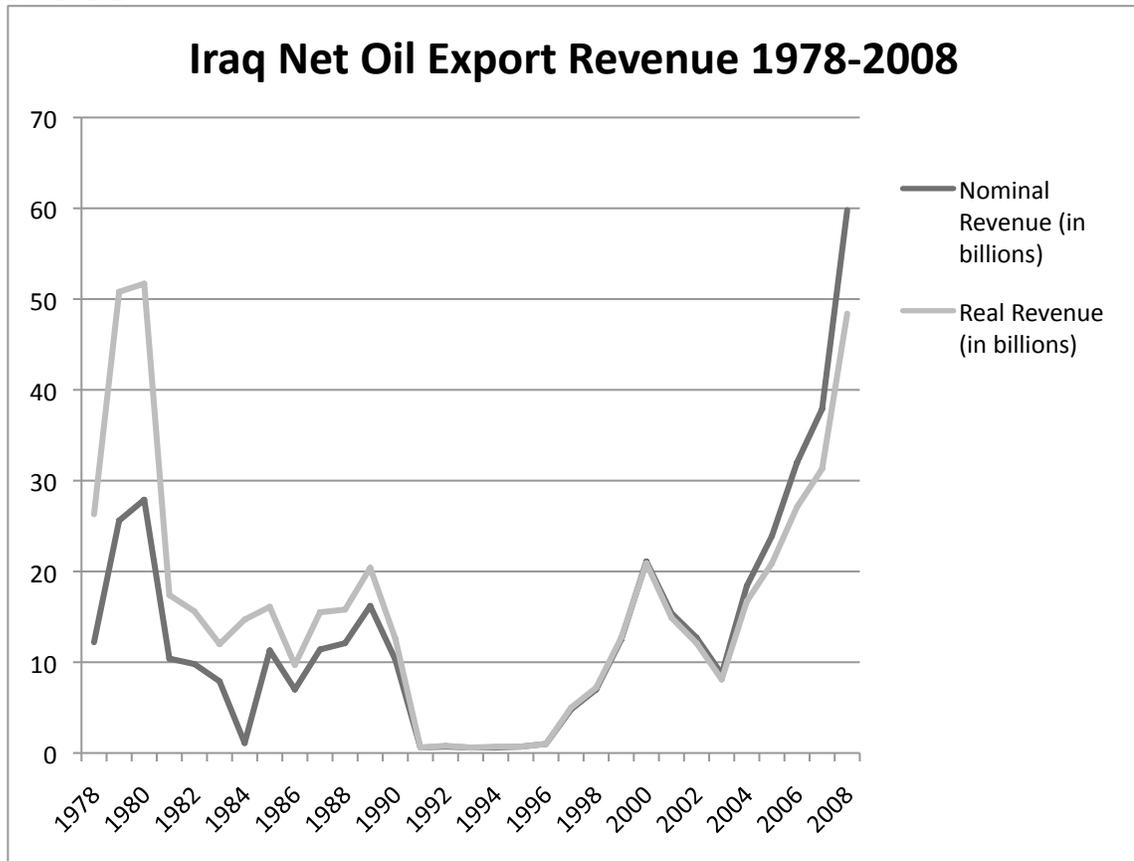
Although the IPC immediately filed legal action against Iraq, the real threat foreseen by the al-Bakr administration was whether the nation could afford to make the initial investments necessary to unleash the financial power of Iraq's vast oil reserves. To the contrary, the administration's fears proved needlessly pessimistic: "The nationalization of the IPC brought the country behind the Ba'ath as no other policy had done or could have done, and the regime made the fullest possible use of the new mood, by encouraging the belief that the victory over the company was not won by the Ba'ath Party alone but by the Iraqi people under the party's leadership" (Farouk-Sluglett 155).

A major contributor to avoiding financial disaster in Iraq was the 1973 oil crisis, in which OPEC declared an oil embargo specifically targeted towards the US and Netherlands after the Yom Kippur War, causing an increase in the price of oil from \$3.29 a barrel in 1973 to \$11.58 in 1974—adjusted for inflation to 2009, this is equivalent to a rise from \$16.17 a barrel to \$51.23 ("Crude Oil Prices 1861-1999," and Sahr). Simultaneously, in the years approaching 1973, oil production had increased by 217% in the Eastern Hemisphere (from 5.7 million barrels per day (Mbbl/d) in 1961 to 18.0 Mbbl/d in 1971) but only by 34% in the West (from 3.1 Mbbl/d to 4.2 Mbbl/d), forcing the mushrooming oil industry to pull more and more of its production from newly-nationalized fields like Iraq (Klebanoff 232). Although data is unavailable for net oil export revenues from 1973-1977, Iraq recorded nominal export revenues of \$12.2 bln in 1978, \$25.6 bln in 1979, and \$27.9 bln in 1980—numbers that would not be surpassed until the 2007 oil price spike (EIA). Adjusting for inflation, the 1978-1980 figures come out to \$40.7 bln, \$76.7 bln, and \$73.7 bln respectively, which have never been matched (Sahr). Measuring by real revenues, Iraq coming through the transition to Saddam Hussein's government possessed more wealth than at any other recorded point in its recorded history (Table 1.1).

The remainder of al-Bakr's tenure in office was marked by increasing tensions with the Kurds, culminating in the 1974-75 open war on the Patriotic Union of Kurdistan (PUK) and the increasing stratification of Iraqi society as al-Bakr and Hussein ramped up the Ba'athist party over all others in Iraq. Al-Bakr also completed the nationalization of the various foreign oil companies in Iraq, taking over the last shards of IOC interests in the Basra Petroleum Company at the close of 1975. Meanwhile, Hussein established a

strangle-hold on the power players in al-Bakr's administration. The power shift that put Hussein in office was done mainly behind the curtain: "Unlike their 1968-69 bid for legitimacy with the masses, [Hussein's takeover] was party-centered and shrouded in secrecy. All that is known for certain is that Saddam Hussein purged president al-Bakr sometime in June, and took over the presidency. For a month he held hostage the families of one-third of the members of the RCC while these officials continued to sign papers and make appearances. In the meantime, he purged hundreds of their cronies, and finally executed the lot, including some of the families (al-Khalil 70). The 1979 ascension is not universally decried as an "orgy of bloodletting," but it is, even

Table 1.1



Data from "OPEC Net Oil Export Revenues by Country," US Energy Information Administration; amounts are unadjusted for inflation.

generously, one of the more violent "peaceful" transitions of power in modern history. If nothing else, Saddam's rise indicated the state of political affairs in Iraq as it entered the 1980s: "Saddam Hussein and his dictatorship are the manifestations of a particularly potent narrative in the history of the Iraqi state—a narrative in which exclusivity, communal mistrust, patronage and the exemplary use of violence constitute the main elements, woven into a system of dependence on and conformity with the will of a small number of men at the center of the state in the name of social discipline and national destiny" (Tripp 194).

1979-2003: Saddam Hussein

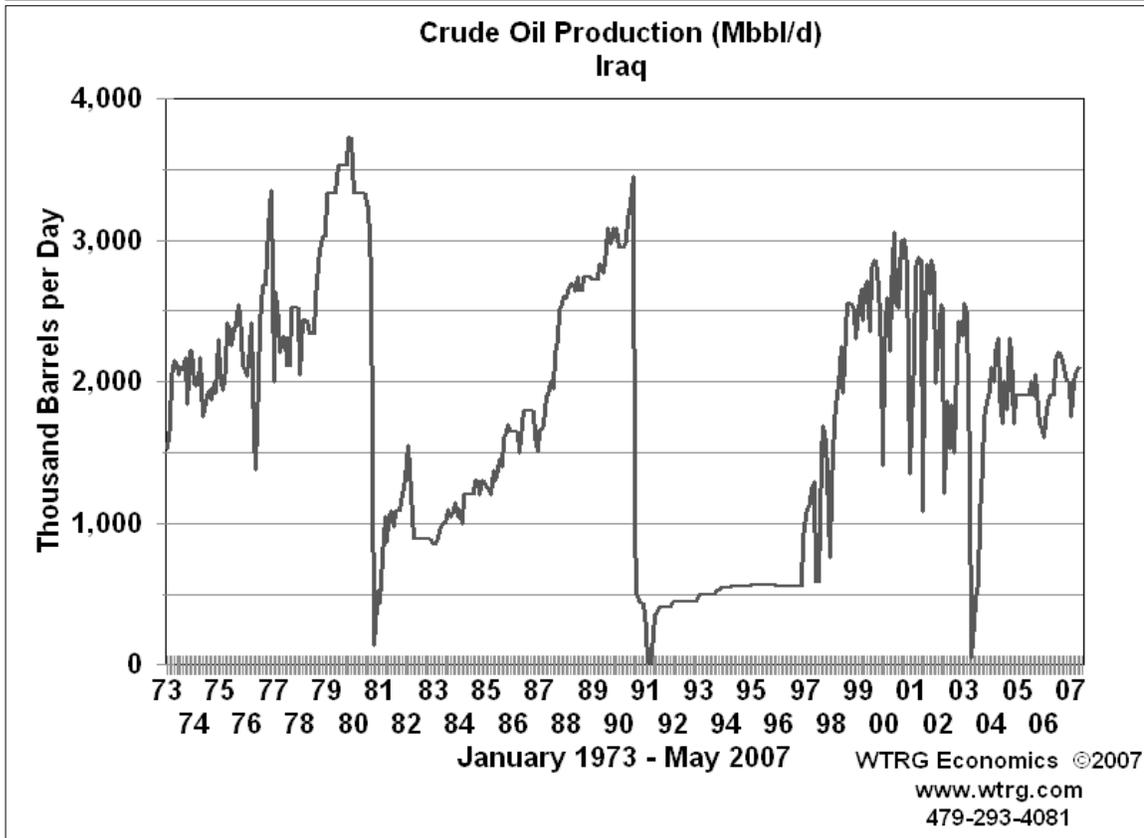
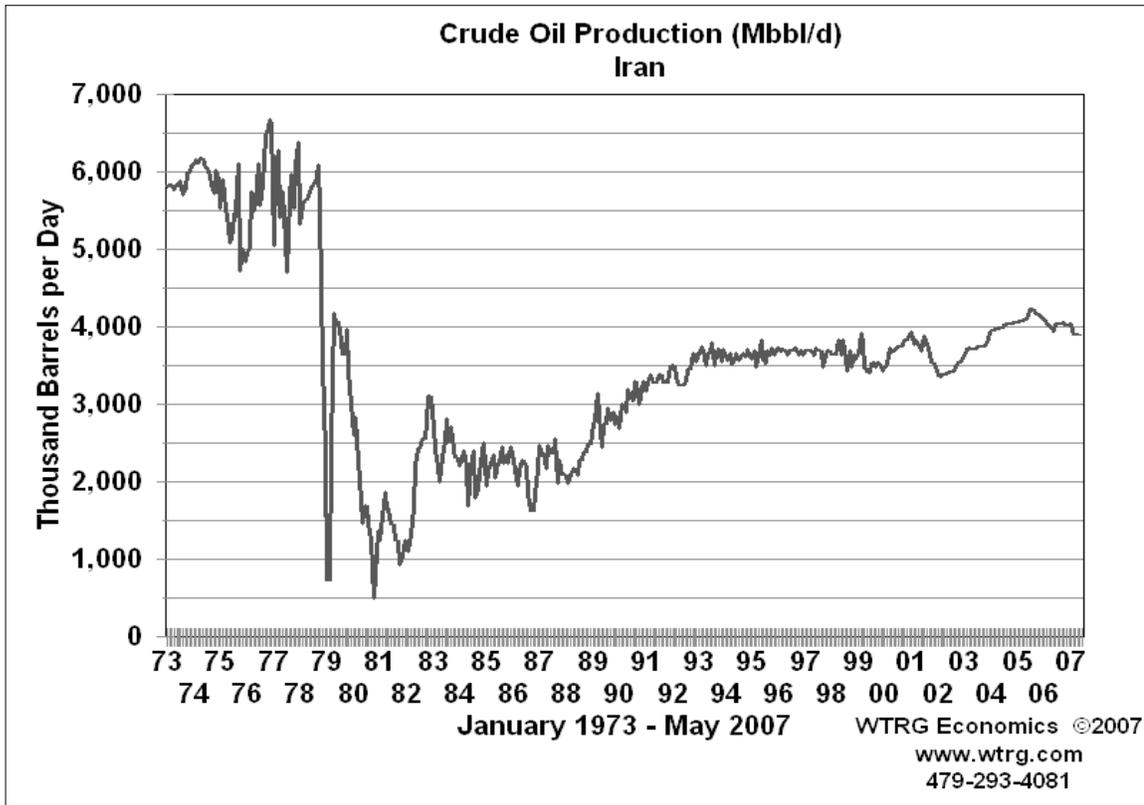
The radical wealth that Iraq enjoyed at the transition of power from al-Bakr to Hussein was extraordinary, but also relatively short-lived. Hussein inherited, and presided over, "a relatively good standard of living, producing a high level of literacy, the largest number of engineers per capita in the Arab world and a health care system considered the best in the region" (Wohlforth). But most of the funds that created these opportunities were generated in the heady days of the late 1970s oil boom, and war was on the horizon. In 1980, Iraq invaded Iran over a border dispute dating back to the Ottomans. Five years earlier in 1975, the Algiers Agreement had set forth Iraqi concessions on the border in return for the cessation of Iranian support for the Kurdish uprising, but with the Kurds defeated, Iraq returned to the dispute with a new energy (Ghareeb 8).

At the time of the invasion, the Iran-Iraq war was considered to be the most catastrophic endeavor either nation had encountered in recent history; the nominal

revenues from oil exports of both countries demonstrate that the war was, indeed, apocalyptic in the extent of its damage, both because of the revenue opportunities both nations were too busy to exploit and in terms of the damage done to the oil industry infrastructure on both sides of the border. In Iraq, nominal revenues for oil exports fell from their 1980 high of \$27.9 bln to \$10.4 bln in 1981, and continued falling to \$1.1 bln in 1984. In Iran, oil production fell from a pre-revolution high of just over 6 million barrels a day (Mbbbl/d) in 1978 to under 500,000 bbl/d in 1981; production in Iraq fell from 3.75 Mbbbl/d in 1979 to under 150,000 bbl/d in 1981 (Williams) (Table 1.2 & 1.3). More than 400,000 soldiers and civilians died in the conflict, which raged over the next eight years; 750,000 more were wounded (Farouk-Sluglett 271).

By 1983, talk had reached back to Hussein that some elements of Iraqi leadership were dissatisfied with his performance; apparently, there was even talk of reinstating al-Bakr. "One report has it that [al-Bakr] was murdered by a team of Saddam's security agents, posing as doctors who had been sent to treat al-Bakr for health problems. They injected the ex-president with a large dose of insulin, provoking a coma from which he never recovered" (Lando 45). However it happened, no threat to Hussein's power ever materialized. Ultimately, rather than becoming the last error made by Saddam Hussein, the Iraq-Iran war became the unfortunate introduction of American intervention in Iraqi politics. The US fostered a relationship with both Hussein and the leadership in Iran throughout the Iran-Iraq war, supporting one, then the other, and then both sides of the conflict at the same time.

Tables 1.2 & 1.3



By the time Iran and Iraq agreed to return the border to its original position, both nations were in shambles, and both regimes had inconspicuously dealt with arms traders and Western powers, threatening their legitimacy in the Arab world and among their own populations, which had only recently freed themselves from Western domination. Particularly in Iraq, the war was a financial catastrophe. It emptied the coffers of the 1970s oil boom and crippled the ongoing oil industry (Iran had destroyed many of Iraq's main export points, and had convinced Syria to cut off pipeline access from Iraq). Internally, the war had destroyed the infrastructure of Iraq's border territories and depleted the nation's skilled workforce. The war's price tag—\$452.6 bln in Iraq alone—launched a massive foreign debt problem that continues to plague Iraq to this day, only in part abated by the Paris Club and IMF debt forgiveness program started after the 2003 US invasion (Farouk-Sluglett 271).

Unfortunately, the war debt itself caused, in part, another war: "Iraq's biggest creditor was the tiny nation of Kuwait, its southern neighbor. Saddam now had a massive military to support and virtually no oil revenue to help him. Additionally, Saddam's hopes for his coveted leadership position in the Arab world were also fading. Rather than being the regional superpower, Iraq was now dependent on the neighboring Arab states" (Hunt 94-95). In line with boosting his image as a regional military and political powerhouse, Hussein spent \$5 bln annually on military upkeep. Comparatively, only \$2.5 bln was spent annually on the reconstruction of Iraq's cities; even at that, Hussein dipped into the reconstruction funds to build monuments and palaces for himself (Farouk-Sluglett 278-79).

Against this backdrop, in 1990 Saddam Hussein repeated Qasim's 1960 declaration of supremacy over Kuwait. Unlike his predecessor, Hussein did not invoke the memory of the Ottoman Empire: at an Arab summit in Baghdad the summer of 1990, "Saddam gave a secret speech warning the delegates that an economic war was being waged against Iraq and that Iraq could no longer stand the pressure, a clear reference to the overproduction by Kuwait and the United Arab Emirates that had driven oil prices down 30 percent over the course of the spring" (Ghareeb 144). With 100,000 Iraqi troops waiting on the border, Kuwait agreed to abide by OPEC production quotas, but subsequently rejected Iraq's terms of agreement; on 2 August 1990, Iraq invaded Kuwait, chasing military and government elements into hiding in neighboring Saudi Arabia. By November, the United Nations had declared the invasion illegal, demanding a withdrawal of Iraqi troops from Kuwait. In late January, coalition bombing commenced against Iraqi military positions in both Iraq and Kuwait; the ground war began on 24 February 1991 and lasted for about 100 hours. By 27 February 1991, Kuwait was declared liberated.

While the Iran-Iraq war carried with it a steep financial price as the natural consequence of an eight-year border war, repercussions from the Kuwait invasion significantly reshaped the future of Iraq. Although Hussein had long been at odds with the revolutionary elements Kurdistan, the failed Kuwait invasion led the Kurds to rebel en masse on a level not seen since 1975; it also sparked an unusual uprising from the Shi'ite population. Perhaps smarting from his military humiliation in Kuwait, Hussein used excessive force to put down both rebellions, causing massive refugee movements, particularly in northern Iraq. In response to this, "the United State created 'safe havens' in northern Iraq to be policed by allied troops; eventually the safe havens would become an

autonomous Kurdish region, beyond the control of Baghdad; a Kurdish government was elected in May" (Ghareeb 145). Kurdistan remains a "semi-autonomous region" in the 2005 constitution.

From 1990 until 2003, Iraq suffered from one of the most severe trade excommunications in the history of the UN. The UN Security Council had passed UNSCR 661 (1990) just days after Iraq invaded Kuwait, then reinforced and expanded it after the close of the Kuwait war in UNSCR 687 (1991). The two resolutions forbade any member-states to trade with Iraq until certain conditions of weapons dismantling and Iraqi submission to UN orders had been fulfilled; in particular, the UN mentioned the destruction and observation of biological and nuclear weapons and the fulfillment of Iraq's international debt as major items of contention. Hussein saw these requirements as an assault on Iraqi sovereignty, and refused to comply. Thereafter, except for "foodstuffs" and medical equipment, the UN froze Iraq's foreign assets and prohibited Iraqi trade with the rest of the world.

The UN sanctions were essentially an historical problem. The United States and the United Kingdom—the nations that pushed the hardest for strict economic sanctions—believed that by crippling Hussein's economic abilities, they would force him to comply with their demands. Unfortunately, in some cases, sovereignty from Western meddling is more important than any other aspect of governing; a similar scenario played out against North Korea after its 1953 war. Nations that are particularly sensitive to their own sovereignty will often not bend, even to impositions of severe poverty and international exclusion. This was certainly the case with Hussein and Iraq from 1991 to 2003. Even as late as 2002, President Bush was declaring the devastation in Iraq to be Hussein's fault:

"The world has also tried economic sanctions and watched Iraq use billions of dollars in illegal oil revenues to fund more weapons purchases, rather than providing for the needs of the Iraqi people" (Bovard 2).

The 1991 sanctions allowed for a very limited trade with Iraq in order to provide the food necessary for their survival. The program didn't supply enough: by the spring of 1996, according to the World Health Organization, child mortality had increased 600 percent since sanctions were imposed. One UN World Food Program manager commented at the time that "more than 4 million people, a fifth of Iraq's population, are at severe nutritional risk. That number includes 2.4 million children fewer than five and about 600,000 pregnant or nursing women and destitute women heads of households. 70 percent of the population has little or no access to food. Nearly everyone seems to be emaciated; we are at the point of no return. The social fabric of the nation is disintegrating. People have exhausted their ability to cope" (Simons 215).

By the summer of that same year, the international pressure grew too much, and the US and UK relented in UNSCR 986 (1996), which allowed Iraq to export \$1 bln in oil every three months, to be used to buy humanitarian products for the Iraqi population: the Oil for Food program. Despite the considerable hype in the West, however, the resolution committed 30 percent of the funds to Kuwait and the UN as reparations, leaving \$2.8 bln in annual revenues; Iraq continued to top lists as a humanitarian crisis. In 1999, the US and the UK agreed again to ease the pressure on Iraq by removing the limits on Iraq's oil sales under the sanctions; this increased the amount of food available, but left severe penalties in place for the Iraqi people.

Adding to the difficulty at this point were the internal limitations on Iraq's oil industry: crippled during the bombings of the Kuwait war, Iraq had never had enough financial power to repair and update its oil production capabilities. Even the oil Iraq did produce and sell earned far less money for the nation than it should have. "Of the \$64 billion earned during the period of the Oil for Food program, only \$28 billion actually arrived in Iraq. That amounted to \$170 per person per year, which, as one analyst pointed out, is less than one half the annual per capita income of Haiti, the most destitute nation of the Western Hemisphere" (Lando 209).

The sanctions against Iraq were not lifted until the 2003 US-led invasion to remove Saddam Hussein from power. It is arguable that because Hussein lasted through the entirety of the sanctions, UNSCR 661, 687, and 986 resulted in a "lose-lose" situation: Hussein never complied with the terms of the UN Security Council, but neither did Iraq retain a true sense of sovereignty, particularly at the end (Mack). Furthermore, the devastation wrought on Iraq by the combination of the sanctions' severity and Hussein's indomitability made nearly impossible the task the US chose in 2003 to take on: the re-modernization of a nation bombed, and then starved, to pre-industrial times.

Chapter Conclusion

After four centuries of Ottoman governance and a century of Western dominance or interference, Iraq has no convincing anchor of national identity—other than the massive oil wealth they exploited briefly in the late 1970s. Escaping from the brutal economic consequences of Hussein's reign is an essential priority, but unlocking Iraq's oil wealth has deeper social implications than the financial stability it could achieve. As the

Hashemite dynasty discovered, Iraq without the preoccupation of a fully functional oil industry is a nation given to great instability. As Hussein demonstrated against Kuwait and Kurdistan, external aggression and internal oppression are natural—but unacceptable—solutions to maintaining governmental authority in a destabilized Iraq. Securing a profitable oil industry in Iraq is vital to securing the authority of the representative government installed in 2005.

However, as the Ba'athists under al-Bakr found in 1972, the nationalization of oil and its economic benefits can afford a great sense of legitimacy to governments even in times of significant national upheaval. A similar move by the government of the 2005 constitution would be a long step towards securing their acceptance as the government of Iraq: not only would the move benefit Iraq economically, but it would resonate very deeply with a population nearly half a millennium apart from meaningful sovereignty.

Chapter 2: The Future of Iraq, Planned and Executed

In the fall of 2001, the US State Department began planning for a government presence in Iraq without Saddam Hussein. The Future of Iraq Project (FOI), directed by former State official Thomas S. Warrick, brought together over 200 Iraqi engineers, lawyers, investors, doctors, technocrats and other experts, separated into 17 focus groups to tackle issues as diverse as public health, defense policy, "anti-corruption measures," and "civil society capacity building." Among these was the "Oil and Energy" focal group, which published its own 94-page list of recommendations at the end of the FOI. According to a host site that archived the documents at George Washington University, "the Future of Iraq study remains the single most important documentary record for understanding US reconstruction planning" (Hassen).

Though initiated and funded by the US State department, FOI was in no way completely favorable to previous US policy in Iraq. This must be noted in contrast to claims that the 2007 Oil and Energy Draft Law bears a striking resemblance to several of the recommendations in the FOI, and that these parallels indicate US State Department influence in the 2007 law. Among other elements, the authors of the FOI were sharply critical of the US-backed economic sanctions. In particular, the Transparency and Anti-Corruption group wrote that "The US-backed international sanctions of the last decade have had the effect of expanding endemic corruption and black market activities into every sector of the economic life. Survival has been the only engine of the Iraqi economy beyond direct government expenditures for the past decade. The rules of expediency that dominate and characterize economic life and the methodology of

corruption are difficult to remove and replace" (Building a New Iraq 1). From another angle, the FOI's Economic group reported that "When sanctions allow export for oil only in return for a list of humanitarian goods in a country whose economic well being depends largely on its exports of oil, the scope of independent economic policy in every area is seriously constricted" (FOI Economic). Though the sanctions are an admittedly easy target, these entries demonstrate a difference of perspective on Iraq from the FOI and the official State Department issue.

Future of Iraq: Oil and Energy Working Group

The FOI's recommendations on oil and energy are the subject of an immense body of critique, both academic and popular in nature; much of it focuses on the FOI's prelude summary, which cites a "broad agreement that the focus of Iraq's oil policy needs to be decentralization of the industry if it is to resolve the economic impoverishment of the country" (Summary Paper 2). The report refers to three models of decentralization. The first model is to "regroup, part-privatize and retain control," which would reorganize the INOC into three or four independent entities broken into regional districts; these entities would be publicly traded, enticing private investors to provide the needed capital to the state and making them eligible for taxation. The second model would "regroup, partner and retain control," which would still reorganize and split up INOC but leave all the new entities in the ownership of the state; the post-INOC companies would operate reservoirs and existing fields and infrastructure, but contract out to private Iraqi firms for the operation of undeveloped fields and further exploration. The third model is "demonopolization," which would open upstream sectors of the oil industry to private

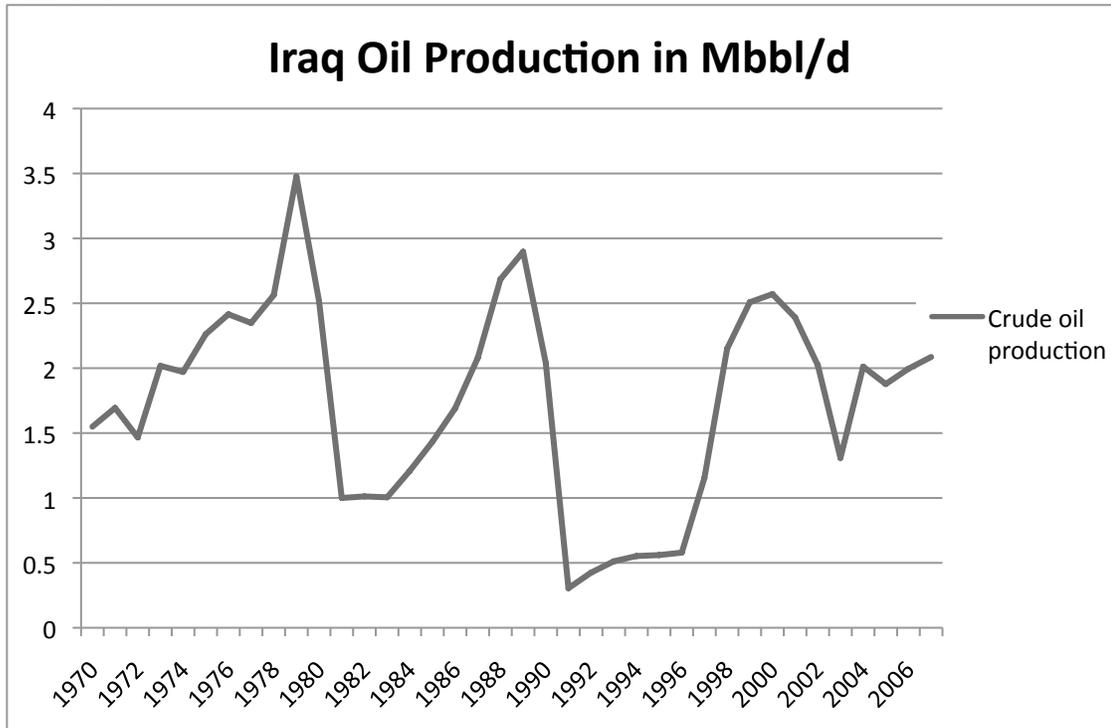
companies under the guidance of an interim administration; this administration would, among other things, restore production capacity to 3.5 Mbbl/d, actively seek out investment for exploration and to development, and prepare draft terms and conditions for PSAs with international oil and gas companies.

An addendum to the third model alludes to the resistance such a recommendation, with the barefaced return to PSAs, inevitably stirs up: "IOC participation through PSAs entered into directly with the Oil Ministry, rather than in conjunction with INOC, may engender opposition from those who see this as selling out to foreign oil companies. Rather than compromise the essential reform of de-monopolization, IOC participation might be induced through their participation in private Iraqi oil companies that are themselves widely-held by the Iraqi public, through the issuance of vouchers to all Iraqi citizens" (FOI Oil Summary 5). This solution must be tempered with the recognition of the US opinion, voiced by Paul Wolfowitz two years after the invasion, that Iraq "can really finance its own reconstruction, and relatively soon" (Blustein). In hindsight, six years after the invasion, Iraq's oil industry is still in relative shambles, unable to recoup the losses from 1990 forward. CIA estimates for 2008 list an average export of 1.83 Mbbl/d, down still from the 2004 postwar high of 2.0 Mbbl/d average and the pre-2003 high of just over 2.5 Mbbl/d (some analyses use pre-war highs of 3.0 Mbbl/d, which Iraq achieved in 1989, or 3.5 Mbbl/d, from 1979; as both of these figures are pre-sanction, they produce inaccurate expectations for a nation and industry coping with the impact of nearly two decades of extreme economic conditions: see Table 2.1). Although the current low levels of production are partly due to the sanctions, a major contributing

factor to Iraq's continuing weakness on oil production has been the damage done to the infrastructure of Iraq in the 2003 war and the following insurgency.

The FOI recommendations are based on two internally produced papers, "Considerations Relevant to an Oil Policy for a Liberated Iraq," (FOI Oil 21-32) which details the immediacy of Iraq's need for decentralization, and a second paper, apparently still classified and internally referred to as "Consultation...", which details the first two "Regrouping" models.

Table 2.1



Source: US Energy Information Administration, "Petroleum (Oil) Production" 10 March 2009.

The "Considerations" paper primarily argues that the limitations on Iraq's oil industry output are chiefly due to the market structure of the Iraq oil industry. "War and sanctions are not the reason that Iraq's oil industry has chronically failed to achieve its potential output. With political liberation and the associated removal of sanctions, but

without oil industry restructuring, Iraq's oil output will be constrained to some 3.4 million barrels per day, which is a mere 16% to 42% of its potential" (Considerations 1). The authors point to the industry's 2.5 Mbbl/d average from 1999 to 2001, noting that in contrast to Iraq's proven reserves of 112.5 bln barrels (as of March 2009, this figure was 115 bln barrels), the production rate in that country when expressed as a percentage is the slowest of the 18 nations producing more than 1 million barrels a day in 2001; the paper claims that an average yield by OPEC standards would be over 4.16 Mbbl/d, and an average yield by world standards would exceed 8.0 Mbbl/d. Since 2003, however, Iraq has struggled to make even 2.0 Mbbl/d (Considerations 2).

The authors' argument for decentralizing—and privatizing—the Iraqi oil industry is based on a twofold observation. First, further international measurements regarding the production per day taken as a percentage of the total oil reserves yield this conclusion: "five of the six countries with the highest production yields have highly decentralized oil industries; by contrast, five of the six countries with the lowest production yields have highly centralized oil industries dominated by their politically controlled, monopolized, nationalized oil industries" (Considerations 3). The second, and perhaps stronger, argument for decentralization lies in the observation that "Tens of billions of dollars of foreign investment can be induced into Iraq's oil industry over the next decade. No other industry or sector of Iraq's economy can attract anything like this volume of investment into the country" (Considerations 3-4).

The initial argument for decentralizing is somewhat suspect. First off, the calculation of oil yield as a percentage of total reserves heavily favors nations with small reserve holdings: the table provided in the FOI shows that the "highest" six in terms of

"oil yield" are the UK, Canada, Norway, Indonesia, USA, and Algeria, from 18.64% to 6.20% respectively; the "lowest" six are Iraq, Kuwait, United Arab Emirates, Saudi Arabia, Iran, and Venezuela, ranging from 0.78% to 1.61%, respectively. The average yield in OPEC is 1.35%; the average yield worldwide is 7% (Considerations 12). There is also a correlation between lower yields and less diversified economies: Iraq has very little other than oil to export, and after a generation of sanctions, every other economic strength has been effectively crippled (Mack).

On the other hand, the FOI authors seem to have hit upon a significant point on their second argument for decentralizing. Across the board, the FOI recommendations imply that money will be available in some form of foreign investment; the oil industry, as pointed out in the "Considerations" paper, is perhaps the perfect opportunity to induce just such investment in Iraq. Unfortunately, only two processes are understood for the inducement of foreign investment in Iraq: concessions and PSAs, both of which are throwbacks to imperialist relationships. When the idea of decentralizing for the sake of foreign investment was carried into the 2007 Draft Oil Law, it was roundly criticized as being a "back door" access card for US and UK international oil companies interested in exercising long-term control over Iraq's oil industry; to this end, critics point out that of the top seven oil producing countries, only Russia has any active PSAs, signed at the collapse of the Soviet Union in the 1990s; these agreements have long since become onerous to the Russians, who intend to exit the contracts as soon as feasible (Muttitt P).

While the PSA argument will be revisited in this paper, what is important to note here is that the goal behind the PSAs, as they continued to spark debate into 2007, is the foreign investment implicit in those agreements. As far back as the FOI, the most

acceptable strategy for inducing that investment has been decentralization of the oil industry; whether that is fair, or even feasible, remains to be argued and ultimately voted upon by the Iraqi government.

The Cost of Redevelopment

The exact amount needed to repair and update the Iraqi oil industry infrastructure depends on three objectives. The first, which is most commonly argued, is the production rate: since 2003, the US reconstructive goal in Iraq has been to average 2.0 Mbbbl/d, but only in 2004 was that objective realized. Second, the price of revitalizing the oil industry depends on what sectors are to be brought online—upstream (producing) or downstream (refining). A persistent problem with the Iraqi oil industry is that it is nearly all upstream, whereas a significant amount of profits are generated downstream; however, Iraq's refining operations are limited to 597,500 bbl/d, which even at their current rate is under a quarter of their upstream export rates (EIA Country Analysis Brief, "Refining"). The last objective to consider is the time frame in which these objectives are to be completed.

The FOI group estimated that the cost of reviving Iraq's oil production facilities, with a production goal of 3.4 Mbbbl/d, would be \$8.4 bln up front, with the total eventual investment capping at \$30 to \$50 bln (Considerations 4-7). The most recent Ministry of Oil estimates from Iraq, based on a goal of 6 Mbbbl/d by 2010, put the price of development at somewhere between \$25 and \$75 bln in investment (EIA Country Analysis Brief, "Upstream Development Plans"). To put these numbers in context, the national budget for Iraq in 2008 was \$42 bln; however, subsequent reports by the US

Government Accountability Office have demonstrated that Iraq has enjoyed significant budgetary surpluses from the oil industry: \$29 bln between 2005 to 2007 and a projected \$38 to \$50 bln for 2008 (CNN)

Concession, PSAs, and Nationalization

As it introduced the suggestion of PSAs into the debate on Iraq's future hydrocarbon law, discussion on the FOI is an appropriate place to delve a little deeper into the concepts behind the different models of oil policies around the globe. The 2005 project "Crude Designs," published by several oil policy groups in opposition to the idea of privatizing Iraq's oil, summarized the array of policy models into three categories: concessions, PSAs, and the nationalized industry. The oldest form, introduced into Iraq in the 1930 Anglo-Iraqi Treaty that allowed IPC a variety of privileges in Iraq, is the "concessionary" model, which is an essentially imperialist approach. In a concession agreement, governments grant privately-held companies a license to extract oil; once extracted, the oil becomes private property, and the company pays the government a variable level of royalties and taxes. In a Product Sharing Agreement—which Iraq developed in the 1952 "50-50" agreement with the IPC—the state retains theoretical ownership of the oil, while a private company provides the capital investment for exploration and development, with the expectation of government repayment. Once oil is being produced under a PSA, the state and company share profits: however, this situation is very vulnerable to corporate manipulation, as Iraq discovered with the IPC, which could lower production rates at any point to protest unfavorable legislation, starving Iraq of requisite funds for whatever period seemed an appropriate retribution. PSAs have

become significantly unpopular, with only 12% of the world's oil reserves subject to active PSAs today. The final model of oil policy is nationalization, which Iraq established from 1972-75; under a nationalized system, all oil assets in a nation are operated by a nationally-owned oil company, which is then normally responsible to the Ministry of Oil or related bureaucratic oversight (Muttitt CD 11-12).

In the long run, there is no debate that nationalization pays out a better return to an oil-producing nation. Contrary to the implications of the FOI "Considerations" paper, the nations most like Iraq in terms of oil reserve capacity and volume favor heavily (almost entirely, with the exception of Russia) nationalization over PSA structures to develop and extract their oil wealth. However, for a short-term infusion of investment, development, and recovery, there is no better arrangement in the current constellation than a round of short-term (5-12 year) PSAs.

Two speculative questions remain unasked by both the FOI and the commentary surrounding it. First, who actually owns the oil underneath the surface of Iraq? Second, can the Iraq situation really be compared significantly to other nations according to oil industry parallels, or have the events of the last 20 years sufficiently alienated the nation as to be its own set of problems with no valid regional comparisons? Of the two, the first is the more disturbing because it is never pursued in detail by any of the documentation leading up to the 2005 constitution or the 2007 Draft Law. The standard line, delivered by President Bush, the Coalition Provisional Authority, the interim Iraqi government, and eventually memorialized in the Constitution and repeated in the 2007 Draft Law is the politically ambiguous, "Oil and gas are owned by all the people of Iraq in all the Regions and Governates." To an extent, the omission of this question as a valid pursuit of legal

discourse can be traced back to the FOI and its focus on the industry side of oil, rather than the politically unsavory question of what belongs to whom. But in the increasingly democratized government of Iraq, oil ownership rights are an inescapable equation to solve in the mathematics of oil distribution policy: whether they are owned by the national government with equal disregard for all local positioning, or owned individually through vouchers in a national company—an idea floated in the FOI introductory remarks—the question must be answered. While the debate over oil distribution remains the primary focus of most Western academic attention on the draft law, the absence of a meaningful dialogue on ownership rights has become increasingly painful.

The 2005 Constitution

The 2005 Iraqi Constitution and the elections that followed and affirmed it are a striking accomplishment on a number of levels, marking a significant social achievement both for the United States and Iraq. But for all the good done by the Iraqi constitution, there remains a significantly unresolved issue, avoided by the constitution, which perhaps had no better place for resolution: oil ownership rights. In a 2003 report for the US Congress on Iraq's economy, the Congressional Research Service found that ownership rights were absolutely necessary as a precursor to determining the contract law for selling Iraq oil, whether as a product out of ground or as a rights document. Referring to oil ownership, the report on Iraq's economy looks forward with the observation: "clear title to the crude must be established, so that a would-be purchaser can be assured that he is buying oil from its rightful owners" (Sanford 25). While the ownership of oil was restricted under UN sanctions, those were lifted at the collapse of the Ba'athist regime,

and the new UN resolution "allows essentially free trade in non-military goods, authorizes procedures whereby Iraq can legally export oil, and also shields Iraq's oil revenues (until December 31, 2007) from seizure, attachment, or garnishment by creditors or claimants" (Sanford 25). In other words, the report states that the removal of UN sanctions gives Iraq its long sought-for economic independence—but to access its full potential, ownership rights must be decided.

On this point, the 2005 Constitution is intentionally vague. Article 108 reads, "Oil and gas are the ownership of all the people of Iraq in all the regions and governates," a legally ambiguous phrase repeated nearly word-for-word in the 2007 Oil Draft Law, and unfortunately, the sole reference to any ownership rights for Iraqi oil. Article 109 continues the trend of legal ambiguity by fudging the separation between local and federal governments and creating separate standards for new and old oil fields. The greater message, however, seems to be that ownership is less worthy of definitive deliberation, in the Constitution's framework, than guidelines for commercial contracts.

The Article reads,

First: The federal government with the producing governates and regional governments shall undertake the management of oil and gas extracted from current fields provided that it distributes oil and gas revenues in a fair manner in proportion to the population distribution in all parts of the country with a set allotment for a set time for the damaged regions that were unjustly deprived by the former regime and the regions that were damaged later on, and in a way that assures balanced development in different areas of the country, and this will be regulated by law.

Second: the federal government with the producing regional and governate governments shall together formulate the necessary strategic policies to develop the oil and gas wealth in a way that achieves the highest benefit to the Iraqi people using the most advanced techniques of the market principles and encourages investment.

In sum, old oil revenue will be distributed nationally while new oil revenue will be allocated to regional interests. Both federal and local governments are given the responsibility of making sure the nation develops equitably across Iraq's 18 regions and governates, compensating some for particular losses.

While perhaps somewhat idealistic, there is a logic behind these requirements: with varying degrees of oil industry development already in place across the nation, and with the industry heavily favoring regions with pre-existing industry infrastructure, the drafters hoped to achieve a relatively equitable distribution between regions.

Immediately, however, the ambiguities in Articles 108 and 109 create a plethora of new contradictions. Article 111 declares, "All powers not stipulated in the exclusive authorities of the federal government shall be the powers of the regions and governates that are not organized in a region," giving priority to regional law in cases of conflict. This is reiterated in Article 117, second section, which declares, "In case of a contradiction between regional and national legislation in respect to a matter outside the exclusive powers of the federal government, the regional authority shall have the right to amend the application of the national legislation within that region."

This leaves the federal legislative body with scant real power over the oil and gas industry, which is designated in Article 109 as a joint responsibility, not "exclusive," as specified in Articles 111 and 117. This is particularly significant if the government of Iraq's short-term goal is to equalize the distribution of oil and gas revenues between governates. Oil-rich governates can, with seeming constitutional legitimacy, refuse federal collection of their local oil revenue taxes, leaving oil-poor governates and the national government with little recourse.

The paradox of federal or regional control over the oil industry was examined shortly after the Constitution was published in 2005 for review before the national referendum, earning the attention of Dr. Nathan Brown—a senior associate at the Carnegie Endowment for International Peace—who notes, "It is unclear whether [Article 108] is intended to ensure that the benefits are distributed equally throughout the country or instead shared with the subnational units. Article 109 does not clarify matters. It first distinguishes between existing oil fields and new ones; although the central government must coordinate with subnational units for both new and old fields, only the benefits from older fields must be distributed nationally. The distribution of revenues from new fields is not specified, although there is a reference to "market principles" implying perhaps a degree of privatization" (Brown 13).

These observations became two of the finer points of contention in the approach to the 2007 proposed legislation: the difference between new and old oil fields, and the true implications of the phrase "most advanced techniques of the market principles." For the operation of existing production sites and new production sites, the chips fell on the side of upholding the intended meaning of the Constitution—established more by precedent than decision—which allows existing oil and gas production revenues to be collected and redistributed federally. In line with the drafters' original intent, the subsequent oil and gas revenues flow to the subnational units according to their population.

As new fields come online and the oil industry expands, however, the need for more concrete legislation regarding the oil and gas law is building significant pressure. As new fields are under the authority and sovereignty of the regions and governates as

they come online, the status quo "creates reasonable mechanisms for a transition to a more decentralized system and an assurance to those who don't have extensive oil and gas in their regions that there will be a long period in which they're supplied from old Iraqi revenues on a per capita basis" (O'Leary). This works only so far as a decentralized system is really the goal, but not everyone interested in the Iraqi economy is convinced that decentralization is the right direction to head. This greater debate, touched on in the latter half of Brown's analysis of the oil industry in the Constitution, lies in the question of where privatization fits into the "most advanced techniques" of the modern market, as phrased by the Constitution. The tension between nationalization and privatization defies ideological, national, and even industrial lines, sparking debate even between various factions of US neoconservatives and within the international oil industry itself (Palast).

In a 2003 report on Iraq's economy, the Congressional Research Service noted, "Among the key policy goals the Bush Administration specified when launching a war in Iraq was the economic and political reconstruction of the country. US advisers are expected to help promote appropriate macroeconomic policies and open the Iraqi economy to free-market private enterprise" (Sanford 45). The report continues on to suggest that the Bush administration would follow a precedent from the 1967 Israeli war—in which it was determined by international observers that oil drilling and development in occupied territory would be illegal, even if it were to the benefit of the occupied nation.

However, the implication that the US would "promote private enterprise" in the oil industry of post-war Iraq was enough to set off fireworks. Corporate watchdogs who had warned of US incentives to privatize the oil industry accused former Iraq oil ministry

official Fadhil Chalabi of parroting Bush administration talking points on privatization when he advised, echoing the Future of Iraq Project recommendations, "We need to have a huge amount of money coming into the country. The only way is to partially privatize the [oil] industry" (Klein). The battle lines were messy: in the US, both sides of the liberal-conservative divide accused the other of being both too imperialistic and idealistic; occasionally, the idea of privatization became so unpopular that both sides accused the other of coming up with it (Rockwell).

Ultimately, however, the US confusion in the privatization-nationalization debate might be the product of the populist approach that influenced the drafting of the 2005 Constitution. The US, in a backwards approach to introducing democracy, originally intended to handpick the Iraqi constitutional committee from a selection of qualified (and, for the most part, western-friendly) leaders among Iraq's formerly exiled political and industrial leaders. However, when this process became publicly apparent, the Grand Ayatollah Ali al-Sistani, who has been the ultimate authority in Iraqi Shi'ism since before the rise of Hussein, demanded a direct electoral process to establish the constitutional committee.

Paul Bremer, head of the US Coalition Provisional Authority in Iraq, originally denied al-Sistani's request, pushing the cleric to flex his muscle in the Shi'ite community. The results were overwhelming: "al-Sistani demonstrated the sort of hold he had on the Iraqi street by calling tens of thousands of demonstrators into the streets of Basra and Baghdad, demanding direct elections" (Cole). The Ayatollah's forceful—albeit peaceful—demand for democracy, in brazen defiance of an occupying military force, clearly demonstrated not only his own power over the Shi'a populace in Iraq but also

emphasized his personal commitment to true representative democracy in Iraq. Questions remain as to why al-Sistani pursued such a hard democratic approach; it seems likely that his purposes were not purely Islamic, but also attempted to counter what he saw as the secularizing Western influences of American policy on the ground in Iraq (Shadid).

In 2004, al-Sistani told a German newspaper that the only way forward in developing the burgeoning Iraqi federal government was through democratic elections; asked if these would produce a tyranny of the overwhelming Shi'ite majority, he responded, "Not at all: even if a certain community holds a majority in numbers, this will not lead to the creation of a political majority, because in every local community there are many different political orientations" (Der Spiegel). After the Constitution was drafted and voted upon by the national referendum, al-Sistani in 2006 declared a retirement from politics, stating, "I will not be a political leader any more. I am only happy to receive questions about religious matters" (Moubayed). Aides said al-Sistani was angry and disappointed that Shi'as were ignoring his calls for calm, instead switching their allegiance by the thousands to more militant groups like the al-Sadr Brigade, which were promising protection and retaliation against increasing Sunni violence (Chamberlain).

Because of al-Sistani's insistence that the constitution's drafters be elected by the Iraqi people and not chosen from a select group of technocrats or other industrial and political leaders, the resulting constitution tilted towards solving the more popular elements of political state building. Consequently, with the drafters serving as true representatives of the Iraqi people, crucial but divisive issues—like federal against local control, or nationalism against privatizing—came out with decidedly vague constitutional

commentary. While this has encouraged further debate and open discussion, thereby promoting a transparent and open democratic society, the constitutional ambiguity raises problems of its own. Specifically, the constitution fails in its primary use as a tool for directing future laws, even while many articles in the constitution promise further legal determination; constitutional ambiguity also damages the image of a strong central government, which, with Iraq on the brink of a Sunni-Shi'ite civil war in 2005, was the exact opposite of what some had hoped to gain from the constitution.

In the well-regarded bipartisan *Iraq Study Group Report*, the Iraqi Constitution's ambiguity problem is outlined specifically as a threat to the future stability of Iraq. With the national government still young, Iraq's national identity very weak, and armed uprisings threatening the peace from both sides of the Sunni-Shi'ite conflict, constitutional ambiguity over oil policy threatened much more than legal confusion for a few oil technocrats. The political tensions over oil distribution, worries the *Report*, could have damaged the "already fragile" efforts to keep the nation unified under a recently overhauled national government. "Senior members of Iraq's oil industry argue that a national oil company could reduce political tensions by centralizing revenues and reducing regional or local claims to a percentage of the revenue derived from production," the *Report* notes. "However, regional leaders are suspicious and resist this proposal, affirming the rights of local communities to have direct access to the inflow of oil revenue" (Baker 24).

The *Report* concludes with several recommendations for the US government to help the Iraqi oil sector get back on its feet; among them is the suggestion that the US assist in preparing a "draft oil law that defines the rights of regional and local

governments and creates a fiscal and legal framework for investment" (Baker 84). Other suggestions include encouraging international investment in Iraq, advising the reorganization of INOC into a commercial enterprise, and joint pressure with the IMF to reduce or eliminate the internal subsidies that provide cheap petroleum end-products to Iraqi consumers (Baker 84-85). Both the draft law and the IMF recommendations have been followed, and in fact the two recommendations wound up going hand in hand. To their relationship the focus of the paper now turns.

The International Monetary Fund Letter

On 6 December 2005, following months of negotiations with the International Monetary Fund, Dr. Sinan Shabibi, Governor of the Central Bank of Iraq, and Dr. Ali Allawi, Minister of Finance of Iraq, sent a joint, five-paragraph Letter of Intent to the International monetary fund with a request for a loan. Attached to the letter was a 21-page "Memorandum of Economic and Financial Policies for 2005-2006," which outlined the Iraqi government program and financing plans for the coming year. The packet was intended to reassure the IMF of Iraq's economic worthwhile as a stable investment. It worked: two weeks later, the *Seattle Times* ran a story with the results in the headline: "IMF approves \$685 million loan for Iraq" (Crutsinger). According to the *Times*, the loan was possible because, as one IMF official told the paper, "The Iraqi authorities were successful in promoting macroeconomic stability in 2005, despite the extremely difficult security environment" (Crutsinger). Oddly, the newspaper nowhere mentions the promises and stipulations under which the \$685 million was secured.

The Letter of Intent elucidates and clarifies several objectives for the government of Iraq to establish the sense of security awarded by the IMF. In the letter itself, the authors write, "A cornerstone strategy is the reduction of subsidies on petroleum products and the expansion of the market that is open to the private sector" (Shabibi L 1). This language carefully parallels a portion of Recommendation 62 in the 2003 *Iraq Study Group Report*: "In conjunction with the International Monetary Fund, the US government should press Iraq to continue reducing subsidies in the energy sector, instead of providing grant assistance. Until Iraqis pay market prices for oil products, drastic fuel shortages will remain" (Baker 85).

Language from the attached memorandum, listed under "Structural Reforms," paragraph 36, also parallels the *Report* in recommending US assistance to restructure the Iraqi oil industry and draft pertinent legislation. The memorandum recognizes "plans to (i) implement (with US technical assistance) a metering system for oil production by end-semester 2006; (ii) restructure oil sector operations toward putting oil sector enterprises on a full commercial basis and with the Ministry of Oil and industry regulators, and (iii) prepare a draft petroleum law in line with the new constitution and international best practice by end-December 2006" (Shabibi M 10). The first and third items bear a striking similarity to portions of Recommendation 62, which read: "Metering should be implemented at both ends of the supply line. This step would immediately improve accountability in the oil sector," and "As soon as possible, the US government should provide technical assistance to the Iraqi government to prepare a draft oil law that defines the rights of regional and local governments and creates a fiscal and legal framework for investment." The second item in paragraph 36 of the Memorandum copies the language

of Recommendation 63: "The United States should assist Iraqi leaders to reorganize the national oil industry as a commercial enterprise, in order to enhance efficiency, transparency, and accountability" (Baker 83-85).

The passages' similarities are clearly more than coincidental, but there is nothing explicitly untoward about Iraq adopting well-qualified recommendations from the US analysis. However, there does seem to be a sense in which Iraq's financial reliance on the IMF and the US precludes its ability to operate on an internally effective timetable.

Since 2005, Iraq's relationship with the IMF has shown itself to be a mixed bag: parts of it are dramatically helpful to Iraq's international financial situation, but other elements have proved more harmful than helpful on the internal economics in Iraq. The subsidies have proved divisive: Oil minister Bahr al-Uloum resigned over the price hikes in 2007—which increased by nearly 200 percent the State-controlled prices of petrol and diesel (BWP). On 11 March 2009, Vice President Tareq al-Hashemi, who heads an executive economic committee, "praised IMF and World Bank efforts to reduce Iraqi debt, but said steps to discourage subsidies for local industries had led to unemployment that could fuel instability. Unsubsidized Iraqi manufacturers and farmers struggle to compete with cheap foreign products, some coming from nearby countries that continue to subsidize their own industries, Hashemi said" (Abbas).

At the same time, the IMF plays a crucial role in the reduction of Iraq's international debts; initial forgiveness of liabilities and a standing grace period extended in 2006 have allowed Iraq to amass foreign reserves of \$27 bln by the end of 2007, a strong start towards reconstruction's estimated \$100 bln price tag (BIC). Foreign debt cancellation began with the Paris Club, an informal creditor group of major industrialized

governments. In November 2004, the Club voluntarily decided to reduce Iraq's international liabilities within the group, which totaled over \$38.9 bln, by a total 80% over a three-step process. The reduction began with an initial 30%, or \$11.6 bln, forgiven in January 2005; an intermediate 30% was forgiven in early 2006 at the IMF approval and adoption of a standard financial development program in Iraq. At this point, the remaining debt was rescheduled over a time frame of 23 years with a 6-year grace period. The final 20% reduction is pending the completion of a final IMF Board review of the three-year implementation of their programs in Iraq; the remaining debt will total \$7.8 bln (CdP).

With this larger picture in view, it becomes apparent that the value of Shabibi and Allawi's letter of intent and the attached memorandum was not only the \$685 million loan announced by the *Seattle Times*. Rather, as a step in the larger process of eliminating the massive foreign debts accumulated by Saddam Hussein, acquiescence to the IMF development models could be valued at nearly \$32 bln. With this incentive, it is not surprising that the government of Iraq suspended, in a sense, a level of its own resistance to policies that are otherwise harmful to Iraq's internal economic strength—such as the subsidy package.

Returning to the promises made in the 2005 letter of intent, other elements of the IMF deal attract a level of doubt, regarding which policy modifications were included on their own merits, and which were adopted in order to maintain access to the Paris Club's debt forgiveness. This casts a new and not altogether favorable light on the Iraqi Oil and Gas Draft Law of 2007, the creation of which was constitutionally mandated, but remained unscheduled until the promises of the 2005 economic memorandum delivered

to the IMF. Another aspect of including such vast monetary incentives for policymaking is the subsequent flavoring of that policy towards the required adjustments: since the IMF is concerned, by its constitution and construction, more with international markets than internal affairs, the oil law required by the IMF had no requisite commentary on producing a comprehensive understanding of ownership rights. By emphasizing legislation for the trade of Iraq's oil, the IMF influenced the circumvention of what should have been a natural process of determining ownership prior to establishing extraction and distribution legislation.

Chapter Conclusion

The FOI has become somewhat infamous for continually cropping up in the ongoing Iraqi oil debate. Its presence is usually interpreted as an unwelcome influence from the US State Department, and it cannot be denied that the authors of the FOI were certainly brought together with an eye towards Western-friendly opinions. At the same time, it must be reinforced that the FOI was written by Iraqis with an eye towards what would work best in a post-Hussein Iraq. To that end, while the short-term PSA model suggested in the FOI truly would be perhaps exploitatively advantageous to IOCs, it is valid to ask whether a better method exists for restarting the Iraqi oil industry after nearly two generations of war and sanctions.

It is unfortunate, to say the least, that the Iraq oil law was set in motion by an IMF requirement, rather than the 2005 Constitution. However, it is notable that the oil legislation actually promised in the Constitution intends to "distribute oil and gas revenues in a fair manner." In contrast to the point of view taken in the FOI and the IMF

letter of intent, both of which focused primarily on the responsibility for development, the Constitution apparently recognizes ownership—at least of revenues—as the primary issue regarding upcoming oil legislation. Though this seems a minor point (and the actual constitutional language is notably ambiguous, a characteristic that plagues much of the Constitution's approach to oil), it is an important distinction between the intent of the Constitution and the resulting legislation.

This brings new emphasis to questions of legitimacy concerning the IMF's relationship to the draft oil law. By promising a draft law specifically for the development of the oil industry, the letter of intent sets the deadline and tone for the legislation; at this, the letter's framework seems somewhat arbitrary and from debatable authority, as it was written and authorized by one office of the executive branch, not by the legislative body as a whole. While clearly illustrating some of the difficulties of involving international bodies in the planning of individual nations' legislative choices, the situation with the IMF also illustrates that more care must be given by foreign entities when dealing with the politics of internal Iraqi oil policy. The history of UN sanctions in Iraq and the Oil for Food program, if nothing else, should teach the lesson that Iraq is willing to play by rules they are forced into; this apparent willingness to concede must not be abused.

Chapter 3: Draft Iraq Oil and Gas Draft Law of 2007

Considering the historical intrusions on Iraqi sovereignty brought on by European lust for oil, it is not too difficult to see why PSA implications in the Draft Law of 2007 have come under such heavy fire. But the law contains some valid solutions to complex problems—solutions that should not be discarded only for raising the specter of British imperialism and the IPC. It is true that PSAs will not provide a long-standing conclusion to the argument of nationalization against privatization, but they could provide the short-term shock capital needed to bring Iraq's oil infrastructure up to par. Frankly, the security situation being what it was in 2007, steep profits for oil companies who would have been willing to risk an investment in Iraq were much more reasonable than they otherwise might be. At the same time, much has changed in the intervening two years, and this should reflect favorably for Iraq in negotiating less costly agreements with IOCs, were they to partially privatize their oil industry. Finally, in response to many international observers' vehement rejection of anything resembling the IPC, it would be prudent to recall that the IPC and other foreign companies developed all of the oil fields that were nationalized from 1972 to 1975; these investments contributed significantly to INOC's capability to post enormous revenues in its first several years.

The draft law, approved by Prime Minister Nouri al-Maliki's Council of Ministers on 26 February 2007, was sent for consideration to the Iraqi parliament with the cabinet's highest recommendations. An earlier version of the law had been leaked in 2006, and in a similar maneuver, the final Arabic version of the 2007 oil draft law was leaked to the

public. Shortly thereafter it was translated to English by an Iraqi blogger, Raed Jarrar, who noted similarities between the law and seminar papers produced by the US contractor Bearing Point, which was contracted to assist in the technical aspects of drafting the law according to Iraq's agreement with the IMF as review previously. Jarrar's comments accused the law of being directly imported from Anglo-American interests: "My translation was based on the previously leaked English version of the law. From what I can tell, the Arabic language was not native, it looked weak and translated. I have no doubt that the English version of the law is the original one" (Jarrar). With Jarrar's comments, as with other legislative similarities already discussed, it is important to note that criticisms of the draft law tended to both originate and resonate more significantly abroad than in Iraq. This was due in part to the groundswell of critics of the Bush administration, which mushroomed in 2006. Consequently, many criticisms are aimed more at discrediting the US administration than supporting a fair oil law for Iraqis.

Despite the accusations of being dominated by Western interests, the head of the drafting committee, Deputy Prime Minister Barham Salih, sounded a note of reserved confidence regarding the law as it moved toward Parliament for the first time: "At the end of the day, we all supported this thing because it's workable for all the parties and is all-inclusive. It will be tough, I want to admit it and I want to recognize that: it will be an interesting roller coaster, my friends" (Wong). Indeed it was—and remains so.

The draft law contains 43 articles, subdivided into eight chapters. From the outset, it is clear that ownership of the oil is to be put off for another debate. Article 1, titled "Ownership of Petroleum Resources," reads in its entirety: "Oil and gas are owned by all the people of Iraq in all the Regions and Governates." Articles 2 and 3 make clear

that the law intends only to "establish the regime for the management of Petroleum Operations." Ownership is not mentioned again until Article 9B, section four: "All model contracts shall be formulated to honor the following objectives and criteria: 1- National control; 2-Ownership of the resources; 3-Optimum economic return to the country; 4-An appropriate return on investment to the investor; and 5-Reasonable incentives to the investor for ensuring solutions which are optimal to the country in the long-term."

While this is acceptable as far as it goes, an example of the PSA contract model used by the Kurdistan Regional Government is not encouraging on the note of ownership of the oil. Nowhere does the Kurdish model PSA clarify the specifics of ownership or title; rather, the contract is modeled around a fictional relationship between the "Contractor" and "Government," and ownership is assumed to be settled according to the holdings defined by the "Government" before the formation of the PSA (KRG 54-57). Thus, all title and ownership issues are pressed into the crevice between the federal oil law and the individual PSA: neither one sets forth the specifics of federal and regional ownership rights. The Contract area as specified in the model PSA, Article 3, is a simple record of geographic boundary; the government's legal right to the oil is never established (KRG 16).

The draft law in Article 5D creates the Federal Oil and Gas Council, chaired by an appointee of the Prime Minister. This council would be populated by federal officials from the Oil Ministry and the Central Bank, regional and governate representatives, a limited number of civilian experts, and "the Chief Executives of important related petroleum companies including the Iraq National Oil Company and the Oil Marketing

Company." The Oil and Gas council would be responsible for all federal policies on oil, forming all model Exploration and Production contracts and reviewing any changes made to them; the council is further given the much-disputed ability to consult any number of external "independent advisors." Article 5F continues on to grant regional governments the authority to carry out "licensing process regarding activities within its respective Region related to Exploration and Production of discovered but undeveloped Fields mentioned in Annex no. 3."

The four annexes, which apparently remain classified, are explained as organizing 65 exploration blocs and 78 fields in varying degrees of development or discovery. The 78 existing fields are separated into three groups: Annex 1 is "producing," Annex 2 is "close to production contract," and Annex 3 is "far from production contract." Annex 3 consists of "26 fields, most of them in the provinces of Muthanna, Anbar, Sulemaniya (part of Iraqi Kurdistan), Tamim, and Najaf, which are seen as technologically challenging and expensive and have not been developed and often not even fully explored" (IHS). While the annexes became a major point of contention when the draft went before Parliament, the observation at this point is that it is the "technologically challenging and expensive" fields that are granted for regional contracts with international oil companies to develop—not the currently functioning fields (Annex 1) or those undeveloped, but cheaply accessible (Annex 2).

Article 6 of the draft recreates the INOC as "a holding company fully owned by the Iraqi government," with a responsibility for managing and operating the current Annex 1 fields and developing and producing the Annex 2 fields. The first annex "details the 27 fields already in production, including the South and North Rumala fields and

Majnoon in the south," while Annex 2 "names 25 fallow oil fields with proven reserves positioned near those that already pump crude. On paper, they are the easiest to develop because of their proximity to existing infrastructure" (Hafidh). This gives effectual control of 52 developed or discovered petroleum reserves to INOC—exactly twice as many as the regional governments. INOC is also responsible for managing and operating sundry oil infrastructure throughout Iraq, including the main oil and gas pipeline network and the export ports at al-Faw; the draft expects these duties to be relieved, however, by a new entity to be created by the Federal Oil and Gas Council from Article 5.

Article 9 lists the grant of rights, alluding to the question of ownership in 9B Fourth, as mentioned above. The article specifies that contracts will be offered to pre-qualified companies, designating the Oil Ministry or a Regional Authority as the qualifying agent. Article 9B Ninth sets the contentious objective of "achieving variety among oil companies and Operators with different background, expertise, experience and approach so as to enhance efficiency through positive competition, benchmarking of performance and transparency." Although this sets a precedent for avoiding the rise of a powerful international oil company throughout the whole of Iraq—avoiding ball-and-chain situations like the half-nationalized IPC in the 1960s and 70s—it also makes clear the Ministry's intention to indefinitely involve international companies in Iraq's oil industry. As perhaps the broadest issue of ownership overall, it seems a more prudent approach would be to leave such momentous statements—or even their originating decisions—out of what ought to be a nuts-and-bolts legal parameter on trading oil.

Article 11 sets forth the revenues expected from the passage of the draft law; Article 11A calls for the Council of Ministers to "submit a draft federal revenue law to

the Council of Representatives regulating these matters." The draft expects to see revenues from direct sale, royalties, signing bonuses and production bonuses of contracts, specifying that the contracts may be with either national or international companies; the article also creates the "Oil Revenue Fund" for collecting these monies, a certain portion of which will then be contributed to the "Future Fund," also newly created in Article 11. Specifications on the use of these funds would be set forth in the draft federal revenue law.

Article 12 outlines the state's intention to "achieve real national participation" in the oil industry, including a provision for the federal government to participate in Petroleum Operations at any point upon its own discretion. This article also makes a point of specifying INOC's control over the fields in Annex 2 (undeveloped but easily accessible).

Article 13 outlines the time frame for contractual obligations on Iraq, setting a general upper limit of 15 to 20 years for Exploration and Production contracts; although Iraq is already unlikely to enjoin itself to another 75-year contract with an imperialistic world power, the specifications of the draft law would make it illegal. More importantly, however, it is necessary to note that the 2007 oil law's upper limit for PSAs nearly halves the industry average of 30 years. This is significant, since the 30-year average was used in several projects between 2003 and 2007 to show how much capital would be lost or not realized if PSAs were used in Iraq. Considering that the first few years of a PSA contract are the least profitable for a company, it is fair to assume that the halving of the PSA length would more than half the amount of capital unrealized in his projections. Consequently, projections of PSAs costing Iraq \$100 bln would likely result in amounts

closer to \$40 bln. While the "loss" is still enormous, this is a significant difference between the 2007 oil law and the expectations of many international observers.

Article 16, under the heading "Unitization," alludes again to the struggle with ownership: "A Petroleum Discovery which is located partly in one Contract Area and partly in another Contract Area shall be developed and operated jointly pursuant to a unitization agreement which shall be submitted for approval by the Federal Oil and Gas Council to be approved" (Article 16A). If an agreement cannot be reached by the parties, 16A provides the Council authority to reach a decision for the parties. Under Article 16B, the Council is also granted authority over contracts for operation in areas that might extend from areas authorized for production to areas not authorized for production; this provision has the consequence—intended or unintended—of granting the Council choice over how conservatively or liberally to construe the annexed areas granted to INOC as opposed to the areas granted to the regions.

Article 33 mandates that oil companies are responsible for paying contract royalties, federal property taxes, municipal and local taxes, and federal income taxes. Article 34 specifies that "INOC and other holders of an Exploration and Production right shall pay a royalty on Petroleum produced from the Development and Production Area, at the rate of 12.5% of Gross Production" (Article 34A). Of some use here is a historical comparison to 1967, leading up to the nationalization of Iraq's oil industry, when a 13.5% royalty from the French ERAP company was considered an even worse deal than the earlier concessions to the British (Stork 190).

Overall, the draft law fails to argue from a position of strength—suing the persistent security questions that still plagued Iraq in 2006, while the legislation was

being drafted. However, as security risks have declined significantly, the focus must turn to Iraq's 115 bln barrels of crude oil reserves, the third largest in the world: Iraq now finds itself in a position of great strength, which must be reflected in future versions of its oil legislation (GAO). The draft law does successfully navigate the unpleasant waters between nationalism and privatization, allowing for a significant involvement of the INOC while also giving each region the power to choose localized positions on the subject. This is significantly preferable to holding a national referendum on the matter, which would only further calcify divisions the federal government has been trying to unify since 2003 (although a poll from July 2007 suggests that Iraqis support state ownership of the petroleum resources, 63% to 31%) (KA 2).

In a sense, the draft law allows Iraq to enjoy the best of all worlds. With part nationalized and privatized systems, operating to the benefit of both regional and federal governments, the solution is adaptable to whatever the Iraqis are willing to make of it. Unfortunately, therein also lays its weakness: the repetitive ambiguities and requests for further draft legislation are reminiscent of the Constitution's own distinctive ambiguity on the arguments that really matter. Ultimately, avoiding the hard decisions rendered the draft law its own worst enemy, as the Kurdish bloc resisted what they perceived as an overwhelming centralized force, and Western observers lashed out against what they saw as an open door for imperialism. What could—and should—have been a strength on both sides became instead an inescapable weakness.

Realpolitik: How the Draft Law Failed Parliament

At the cabinet's approval of the draft law introduction in late February 2007, many in the international community and the internal political structure of Iraq hailed the proposed legislation as a major breakthrough for the federal government; the *New York Times* called it "a major agreement among the country's ethnic and sectarian political blocs on one of Iraq's most divisive issues" (Wong). However, almost immediately, Kurdish representatives realized that what seemed at first minor differences were becoming major disagreements, particularly concerning the four annexes, which had not been approved in the Cabinet.

In April 2007, Dr. Ashti Hawrami, the Minister of Natural Resources in the Kurdistan Regional Government, published a five-page position statement on the oil draft law, citing six major problems with the draft. Among them, Hawrami noted the concentration of "unaccountable power" in the hands of the INOC, accused the draft of returning to "old regime methods," deterring investment, and breaching constitutional rights and revenue sharing rules under the 2005 Constitution. Stating that "these draft Annexes will not give control [over Iraq's petroleum sector] to the Iraqi people: it will create a new oligarchy in which Iraq's oil is left in the ground and the interests of Iraqi citizens are once again ignored," Hawrami attached amended annexes (not publicly available). However, he wrote, "Even under the KRG proposal, INOC will receive almost 58 per cent of Iraq's proven petroleum reserves, including INOC's carried interest on four projects" (Hawrami 4). The Minister had calculated that under the original draft Annexes, 93 percent of Iraq's proven petroleum reserves would be transferred to INOC's holdings, leaving 7 percent for "Regions and other entities to use for inward investments" (Hawrami 1).

In May, Hawrami's objections came under fire from a senior Shi'ite Arab legislator, Sheik Jalaladin al-Saghir, who discounted the disagreements as a stalling tactic; however, he told the *New York Times* he thought the Kurds—who held 58 of 275 parliamentary seats—would eventually withdraw their objection and allow the legislature to "move forward to pass the law, since everybody needs it" (Wong and Stolberg). Unfortunately, this was not the case: although Prime Minister Maliki presented an amended draft to Parliament in July 2007, it was too little, too late. Internal and foreign concerns were mounting that "Iraqi politics is in greater disarray than at any time since the 2003 invasion" (BBC). True to fears, the draft law continued to shuffle back and forth between Parliament and Maliki's cabinet until the legislature adjourned for summer.

Kurdish opposition to the draft is particularly acute regarding Article 6 and the control it gives INOC over all of the petroleum resources listed in Annex 1. Although the Annexes are not available to the public (presumably for security reasons, although there is no official statement on the omission; the annexes' unavailability is established by articles in the *Houston International Law Review* among other sources), analysis and argument over the Annexes suggest that the northern supergiant Kirkuk field—which the Kurds claim ownership of—is listed under Annex 1; therefore, the field falls into the jurisdiction of INOC, and out of the jurisdiction of the Kurds (IHS). This explains in part why Dr. Hawrami's position statement so emphatically points to INOC as having too great a percentage of the Iraqi oil reserves. Additionally, however, passage of the draft law would force reconsideration of several contracts the Kurds have already signed for foreign oil companies to develop and produce on several reserves in their region; while in the Cabinet, apparently the annexes gave the impression that the regional government

would be able to retain the power to sign such contracts—thus keeping the contracts already in force (Ridolfo). Modifications introduced to the annexes since the draft law was sent to parliament have apparently upset that balance.

Over the next year, the draft law eventually went through four more amendment sessions, each time getting bumped back to Maliki's cabinet. Finally, in October of 2008 it collapsed entirely, failing to win the backing of the parliament's Oil and Gas Committee. Ali Hussain Balou, who heads the committee and belongs to the Kurdish bloc in Iraq's parliament, told news agencies, "Regrettably, the cabinet has sent us a version that was altered by the Oil Ministry, which is different from the draft approved (by the Prime Minister's cabinet) in February 2007. We cannot accept it" (Rasheed). This perspective is apparently not shared by the committee's deputy head, a Shi'ite Arab, who said that the most recent revisions were unsubstantial and a renewal of cabinet approval was unmerited. In December 2008, former Iraqi oil minister Thamir Ghadban, an adviser to Maliki, told news agencies that the draft law version rebutted in October had been accepted by the Iraqi Council of Ministers and is now pending final agreement; Ghadban's reported timetable for the draft law put it in front of Parliament in the second quarter of 2009 (MEED).

In January 2009, Iraq went through major national elections. While the results are not certified at the time this paper is being written, indications are that the dominant Shi'a party may have gained an actual full majority in the legislature (Muir). If that is the case, Kurdish opposition will no longer have the comfort of being a key part of the majority coalition in Iraq's parliament—meaning, dependent on the election results, the staunch Kurdish opposition to the draft has potentially run out of steam.

Fears and Criticisms

The 2005 publication *Crude Designs* brought up several pertinent points of debate in warning against a US-led approach on the Iraqi oil law. In the paper, Greg Muttitt argues against what he foresaw as the rise of a PSA structure in the Iraqi petroleum industry: "PSAs are indeed quite common in countries with small oil reserves and/or high extraction costs. However, none of these conditions apply to Iraq: in fact, Iraq is quite the opposite. PSAs are not found in any other country comparable to Iraq" (Muttitt 14). While this is true in comparison to a comprehensive view of Iraq, it must be remembered that Iraq is currently in a state of dramatic transition. *Crude Designs* estimated an overall loss of \$74 bln over a contractual period of 30 years; however, review of the study's economic models shows that Muttitt neglected to note the compensation of over \$25 bln in initial investment capital that Iraq would not have spent developing the fields used in his model (Muttitt 39-42). *Crude Designs* also sets a low royalty standard for the model PSAs; given that Iraq's projected royalties in the current draft law are at 12.5%, that Iraq's position in negotiating contracts has only improved over the last several years, and that the potential PSAs are more likely to be 15 than 30 years long, it is questionable whether Muttitt's criticisms—though certainly valid of PSAs overall—hold up in the models projected by the 2007 draft law.

A more damning reaction against the oil law's specifics can be found in Kamil Mahdi's 2007 paper, "Iraq's Oil Law: Parsing the Fine Print," published at the school of Economics at the University of Exeter. Mahdi states that the draft law represents a reversal of the nationalizing movements in the 1970s, worrying that the law "is weak on

economic rationale and will serve to deepen ethnic and sectarian forms of economic and political organization, solidifying and calcifying communal factions by moving away from nationally-based control of the oil economy" (Mahdi 11). These arguments represent, in a nutshell, perhaps the widest base of international resistance to the draft law. Mahdi argues boldly that the law could lead to rapid development of Iraq's petroleum industry, but also makes the parallel contention that the uncontrolled, rampant development of Iraq's oil resources could be dangerous for Iraq's greater economic situation, becoming "a major destabilizing factor in Iraq and the entire region" (13). Another criticism of the oil law is that "many politicians now engaged in backroom bargaining are ultimately embroiled in a resource conflict—rather than a conflict of ideas and visions. What has been lost is even a minimal sense of a common national interest, or for that matter any sense of what are the 'communal' interests."

The main thrust of the paper presents a five-point argument against the breakdown of contractual negotiations between regional and federal governments. The first point presents Iraqi provinces as lacking "the managerial and technical competence to conduct their own oil operations" (17). This point is well taken: however, it also betrays perhaps a shoddy reading of the oil law, which provides for federal assistance from the Oil and Gas Council. The same point possibly contradicts Mahdi's third point, that "known oil and gas reserves are not neatly confined within provincial or regional boundaries" (18), as that item is addressed by Article 16B, which grants authority in disputes to the Council. Mahdi's second and fourth points essentially point to the inefficiency of a decentralized system; the fifth point suggests that the oil sector's "major contribution—beyond providing funds for subsidies, collapsing services, and incomes for

a proportion of the labor force—would be in promoting investment," and that a decentralized system weakens the investment opportunities the oil industry can induce (18). However, such a conclusion leaves Iraq in a conundrum of contradictions: Mahdi argues strongly for nationalization and against foreign privatization, and yet simultaneously argues against decentralization by observing its negative impact on opportunities to induce foreign investment. His paper, albeit points well taken, is a prime example of how the draft law opens itself to criticism from many sides at once, even while some of them oppose each other.

Aside from western critics of the oil law, Iraqi labor unions emerged as a significant opponent to the draft law. Though the arguments presented are far less academic in nature, the unions possess the face and immediacy that are lacking in arguments from Western academics and Baghdad politicians alike. From 4-8 June 2007, the Iraqi Federation of Oil Unions (IFOU) went on strike to protest the draft oil law, demanding benefits; a subsequent march against the oil law on 16 July reportedly brought "thousands" to the streets of Basra (Weinberg). David Bacon, a journalist working in Iraq, noted in a September essay that the oil workers' demands "reflect the desperate situation of workers under the occupations. In a country where housing has been destroyed on a massive scale and workers often live under primitive conditions in dilapidated structures, the union wants the government to turn over land for building homes" (Bacon 27-28). Fighting for such humanitarian needs, Bacon writes, increases the union's popularity—and thereby its power. "The one political demand that unites Iraqis above all others," he reports, is that "They want the country's oil (and its electrical

power stations, ports, and other key facilities) to remain in public hands" (29). Poll numbers from Iraq in July 2007 support this claim (KA 2).

What muddies the waters for politicians, of course—even in a burgeoning democratic society where the people's preferences are fairly clear—is that the choice is not simply between public or private hands. As seen throughout the discussion on Iraq's draft oil law, the issue is many-sided. Perhaps the broadest argument is between centralization and decentralization, or federal control against subnational government control, against the backdrop of existing cultural tensions. Closer to the industry itself, the three general models of oil distribution compete for primacy within ambiguous legislative statements and unwritten contract models. Finally, there is the question of revamping the oil infrastructure and bringing Iraq's massive reserves online, while resolving the existing national debt and avoiding the accrual of new debt. All of this is, unfortunately, much more than a simple choice between "keeping oil public" or not.

Chapter Conclusion

Given the contrasting goals going into the 2007 draft law—from the FOI and IMF models of PSA and privatization, in one corner, to the Constitution's implications of nationalism and requirements for a distributive system, in the other corner—the drafters actually seemed to have emerged with a very smart, well-balanced system.

Unfortunately, that balance seemed to turn against the law in Parliament, as the law was accused simultaneously of being both too nationalized and too opportunistic for IOCs.

However, behind the theoretical oppositions, the real block in Parliament came from the Kurds, who will lose the Kirkuk field if the law is passed with the super giant field still

marked in one of the annex categories appropriated to INOC. However, the legislative stall did create an opportunity for the public review and criticism due legislation of such importance.

Many of the resulting analyses seem to snag on the cost of partial privatization, without appropriately considering potential long-lasting benefits to the Iraq economy as a result of mechanisms like PSAs. It is certainly true that the cost of privatization, even partial, appears nearly criminal when compared to the revenues being gathered by other nations in the region with similar reserves. However, these parallels are called into question by crucial differences in government structure and the state of Iraq's oil sector and overall economy. As a representative government, Iraq cannot nationalize so simply as theocracies or monarchies: the good of the nation as a whole has become somewhat secondary to the good of parliamentarians' local electorates. Similarly, after nearly two generations of crippling war and sanctions, Iraq's economy and the oil sector are not yet prepared to properly exploit the nation's massive oil reserves, as would be preferred. Expensive as it may be in terms of capital not realized, Iraq does need a short term boost in the oil industry—the sort of boost IOC investment could provide.

However, even in the mix of debating the 2007 draft law—which, owing to the promises made to the IMF, focuses primarily on development and avoids ownership almost entirely—the need to settle ownership questions finds its way back to prominence. In a very real way, the Kurdish opposition to the law is based on ownership questions, as are opposition movements from unions and citizen groups. Separating ownership into secret annexes is clearly not enough: the attempt to avoid the question has only proven that ownership must be argued, publicly, in its own legislative construction.

Conclusions

Iraq's 2007 draft oil law seems almost an historical parallel to Prime Minister Qasim's Law 80 of 1961, which nationalized 99.5% of the national oil reserves, but left intact the IPC's operations in the remaining 0.5%. By giving the currently producing fields to the authority of INOC, the draft law assures that nationalists will be satisfied; by granting control of the more difficult fields to regional governments (and, therefore, likely IOC contracts), the law provides for the development of valuable fields whose development is currently unaffordable. However, it must be noted that Law 80 became the crucial stepping stone for full nationalization a decade later; similarly, it is possible that the draft oil law, if passed, could become a temporary fulfillment of the IMF requirements, but find subsequent replacement in a total nationalization policy.

As suggested in Chapter 1, a scenario allowing for short-term PSAs would afford Iraq's young federal government a future chance to attain a certain level of internal legitimacy, by providing an opportunity to affirm Iraq's sovereignty in phasing out PSAs and fully nationalizing the oil industry. Chapter 2 points towards in favor of this scenario's probability, as Iraqi legislators have proven adept at acquiescing when under pressure and withdrawing from unfavorable situations when capable of doing so from a position of strength. Chapter 3 indicates that the ambiguities throughout the 2007 draft law allow for the possibility of clauses to carry out this strategy.

However, the impact and importance of ownership cannot be underestimated in this debate: the possibility of future nationalization is essentially a question of ownership,

not development. Throughout Iraq's modern history, citizens have never really owned the oil that is the birthright of all Iraqis. Nationalized under an oppressive regime, the majority of the 1970s oil revenues disappeared in massively destructive wars abroad and internal oppression. This has had a crippling effect on the oil-rich national identity that Iraq should be able to enjoy. Ultimately, securing a profitable oil industry in Iraq that translates wealth directly to the population's benefit is vital to securing the national identity and regional honor of Iraq as well as the authority of its government.

To this end, it is vitally important that the Iraqi Parliament honor the promises of the 2005 Constitution, reiterated in the 2007 draft law, which pledge a policy governing the distribution of oil revenues to Iraqi citizens. This is the first step towards establishing true ownership of Iraqi oil, regardless of the form taken by later development. The Parliament must also separate the four draft law annexes into a separate ownership legislative construction, to be publicly debated and settled prior to any further debate on a development law. Additionally, the Ministry of Oil must provide a model PSA contract for use and adaptation by regional governments, if that avenue is to be discussed. These three actions alone will secure the ownership question for many Iraqis and make future oil law discussion more pliable and less ambiguous.

At that point, it will be necessary to revisit the limitations on PSA contracts listed in the draft law, which were written while the security situation in Iraq forced the national oil industry to negotiate with IOCs from a position of weakness. An amended draft law must reflect the significant improvements to the security situation since 2006, and allow Iraq's governates to argue from the position of strength that Iraq's massive oil reserves imply. Ambiguities on ownership and revenue distribution in the amended draft law may

instead refer to Parliament's actions prior to the legislation, adding levels of clarity and transparency that have been absent in prior legal commentary on Iraq's oil industry.

Out of respect for the nation's fragile sovereignty, it would be highly advantageous for Iraq to complete these legislative works after the IMF has finished their final economic review to satisfy the Paris Club's debt forgiveness program.

With functional oil legislation in place, it is expected that the governates of Iraq will be able to quickly acquire IOC bids for their oil holdings, particularly from Anglo-American companies, whose reserve depths have been curbed in recent years. With IOCs funding the development of Iraq's more expensive oil reserves, INOC can focus on bringing current production levels up and investing in downstream capability, including modernized refineries to keep more of the downstream revenues within Iraq borders. Ultimately, Iraq should profit, not suffer, from its vast oil wealth—but more than that, the nation must seize the current opportunity of increased security to develop their oil industry for the sake of their national stability, identity, and future.

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