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Iraq and KRG Energy Policies:

Actors, Challenges and Opportunities

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Institute of Regional and International Studies (IRIS)

Through the promotion of rigorous scholarship and open dialogue among academics and influential public leaders, the Institute of Regional and International Studies (IRIS) at the American University of Iraq, Sulaimani (AUIS) examines today's most complex regional and global development issues. Drawing from the diversity of fields of expertise at AUIS, the Institute includes in its scope of activities historical, cultural, socio-economic, anthropological, and religious dimensions pertinent to present day realities and problems. As a space for regional and international encounters, IRIS fosters mutual understanding and awareness that reaches across national borders, sectarian divisions, and differing perspectives.

AUIS is Iraq's only independent, not-for-profit, American-style institution of higher learning. It has excellent conference facilities, and is well placed to assist scholars with logistics, introductions, transport and other aspects of field work in the region. The University's location in the Kurdistan Region of Iraq offers a safe space and a climate of tolerance that is uncommon in the Middle East, making it an attractive meeting place for people who cannot easily convene elsewhere.

Table of Contents

Introduction

Governance and management of Iraq's hydrocarbon resources remain crucial in shaping Iraq's post-Saddam nation-building efforts, and in contributing to economic and political development. Ever since oil was found in Iraq, the resource has had significant political, economic and social impact on this post-colonial nation. Control of oil has been requisite for ruling the country.

Upon the fall of the Saddam Hussein regime in 2003, the U.S. government and Iraqi political factions embarked on rebuilding and restructuring the Iraqi oil sector. There was consensus around rule of law as the basis for shared management of the country's different ethnic and religious components. Iraqis sought a constitution, which was endorsed in a national referendum in 2005. The constitution enshrined democracy and federalism as the form of government. Federalism and "market principles"[1] shape Iraq's post-Saddam energy policy and industry, and have significant implications for ownership of and control over the country's petroleum resources.

However, understanding and interpreting the constitution in practice by the federal government in Baghdad and the Kurdistan Regional Government in Erbil has hampered the potential of Iraq's energy sector. This report will briefly describe the challenges and tensions over petroleum policy between Baghdad and the KRG. Then, key players--national, regional and international-- and their goals will be described. The report concludes by highlighting some opportunities for moving forward.

Note on Methodology

The American University of Iraq, Sulamaini (AUIS) and its Institute of Regional and International Studies (IRIS) aim to contribute to the policy debate in Iraq and the Kurdistan region regarding the energy industry and its contribution to a prosperous country and society. To this end, IRIS has brought together thought leaders and experts on energy policy and industry from government, energy firms, academia, and civil society. In mid- and late 2013, IRIS organized two roundtable discussions at AUIS. In addition to moderated discussions and interviews, participants took part in a mapping exercise that helped identify key actors in the policy networks, and their goals and influence.[2] Chatham House rules were observed; therefore, the names and affiliations of the participants will not be mentioned. IRIS also organizes the Sulaimani Forum, the university's annual signature event. In the 2013 and 2014 forums, there were special panel sessions examining Iraq's emerging energy sector, where the author also contributed. This report is based on the data gathered mainly through these events and its participants.

1. Policy Challenges and Risks

There are several challenges and risks facing the progress of Iraq and KRG's petroleum industries. The main ones include the dispute between the Iraqi federal government and the KRG on federalism and the competence over the management of petroleum resources, the lack of a national hydrocarbon framework, and the governance of the energy sector and its revenues.

1.1 KRG-Baghdad Dispute over Federalism

Iraq's constitution enshrines federalism and the separation of powers. The preamble to the Iraqi constitution describes governance in Iraq as a "republican, federal, democratic, pluralistic system." Also, Article 47 calls for establishing the separation-of-powers principle. Furthermore, the constitution recognizes Iraqi Kurdistan's special status as a region.[3]

Iraq's constitution also defines what constitutes a region, and delineates the exclusive and shared rights and responsibilities of the federal government, regional governments, and provincial governments. Article 110 identifies the exclusive federal powers.[4] According to Article 212 (First) on regional powers "The regional powers shall have the right to exercise executive, legislative, and judicial powers in accordance with this Constitution, except for those authorities stipulated in the exclusive authorities of the federal government." On shared powers between the national and subnational governments, Article 115 of the constitution prioritizes the rights of the latter, i.e. of regions and provinces.[5] Article 114 of the constitution enumerates the powers shared between the federal government and regional and local governments. Critically, neither article (110 on exclusive federal powers nor 114 on shared powers between national and subnational governments) refers to competence over the management of petroleum resources. Oil and gas matters are highlighted in separate constitutional articles—111 and 112. Article 111 states, “Oil and gas are owned by all the people of Iraq in all the regions and governorates.” Article 112 (First) states, “The federal government, *with* the producing governorates and regional governments, shall undertake the management of oil and gas extracted from *present fields*, provided that it distributes its revenues in a fair manner in proportion to the population distribution in all parts of the country” [emphasis added by author]. The cause of ambiguity in this article lies mainly in two parts, what the word “with” means, and what constitute “present fields.” The joint responsibility is mentioned again in the Second section of Article 112 on setting hydrocarbon policy: “The federal government, *with* the producing regional and governorate 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 encouraging investment” [emphasis added]. Policy formulation is thus envisioned to be a joint effort by the national and subnational governments.

The constitution, thereby, enshrines certain principles: that oil belongs to all Iraqis, that federal and regional governments should share power on making energy policy and managing Iraq’s petroleum resources, and that oil revenues should be distributed equitably among all Iraqis. These remain general principles and guidelines, according to which the Iraqi Council of Representatives should pass specific legislation and regulations. In practice and on the ground, however, the delineation of powers, rights and responsibilities of Iraq's federal and regional governments is all but clear. The Iraqi factions and political parties, have so far been unable to agree on how to interpret these principles into laws. Iraqi Kurds have been most adamant about oil federalism. Some Iraqi Shia groups initially supported decentralization of power from Baghdad during the writing of the constitution, but this trend has since increasingly shifted toward centralization.[6]

Among Baghdad's goals is to maintain centralized control over the making of policies and decisions related to the petroleum sector in Iraq. Contrary to this centralization tendency, it has been the primary goal of the KRG to maintain the autonomy of Kurdish policy and undercut re-centralization of petroleum management. Iraqi Kurdistan has been semi-autonomous since 1992, and the KRG wants to preserve its self-governance. In the absence of a national hydrocarbon framework, the Kurdistan regional parliament passed a regional oil law in 2007 as legal basis for its energy industry. The federal government has been using old laws and regulations to manage the energy industry in the rest of the country.

1.2 Iraq's Legal Vacuum and the Elusive National Hydrocarbon Law

Disagreement between the KRG and the federal government over the interpretation of oil and gas clauses in the Iraqi constitution has blocked the passage of the national hydrocarbon law. The Iraqi Council of Representatives (COR) deliberated but failed to pass a draft law in 2007. At the time, disagreements between Baghdad and Erbil were comparatively minor. But there was agreement on major issues—contracting rights, sale of oil and revenue sharing. However, both parts have gone to extremes since then, and a national oil law may need to be renegotiated after phases of mediated confidence-building between both sides. In 2011, two more draft laws were circulated, one written by the oil and gas committee at the COR and one presented by the federal cabinet. The latter, championed by Iraq's deputy prime minister for energy, Mr. Hussein Al-Shahristani, increases the central powers of the federal executive branch vis-à-vis the legislature, oil producing regions and the national oil companies.

The national oil law is instrumental for the progress of Iraq's energy industry, especially since it calls for the establishment of energy-related state institutions. In addition to the legal framework, crucially absent are "federal instruments," such as the proposed federal oil and gas council tasked with coordinating energy policy. More importantly, federal courts have not been the legal recourse to resolve disputes between Baghdad and the KRG. One IRIS panelist noted that the constitution is unrealistic, and each side's actions since 2007 have made agreement further elusive. Although both Erbil and Baghdad use legal and constitutional justifications to support their positions and actions, their arguments are essentially political. Therefore, "Neither position is clearly stronger than the other" as legal experts point out.[7]

In principle, the hydrocarbon law would set up structures of interdependence. According to the draft law and earlier negotiations, petroleum policy would be coordinated by a high federal oil and gas council that represents the federal government, the KRG, and producing provinces. The KRG has been receiving 17% of the national budget in return for selling oil from KRG oilfields through the Iraqi export infrastructure and State Oil Marketing

Organization (SOMO). The KRG expects Baghdad to remunerate the oil companies operating in the KRG. Hence, Iraq's oil revenues will flow into a federal pool managed by a federal commission that includes federal Iraqi and regional Kurdish representatives. These levels of interdependence would make room for auditing and more accountability.

However, such a management set up negotiated earlier and enshrined in draft national hydrocarbon law has been put on hold. The blame game between the KRG and Baghdad continues over who is responsible for the legal vacuum. In effect, however, Baghdad and the KRG petroleum policies are diverging, interdependence is waning, and the desire for a negotiated settlement is weakening. As one IRIS panelist put it, Baghdad-Erbil disagreements have created "a poisonous atmosphere in politics" that is conducive to corruption and elevated risk.

Such legal vacuum increases the risk factor for foreign investors operating in the KRG and Iraqi petroleum sectors. Absent an agreed-upon national framework that regulates the energy industry in Iraq, IOCs dealing with the KRG have had difficulty monetizing their oil finds. Hence, IOCs have had delays in recovering their costs. Securing oil outlets is also necessary for IOCs to be able to perform more exploration and boost production. Moreover, the absence of an agreed-upon legal framework has undercut rule of law and sanctity of contracts at the expense of politics and power rivalries between the KRG and Baghdad. Should the KRG and federal government energy policies continue to diverge, the likelihood of consensus and establishing federal institutions would be diminished. Any oil contract based on political alliances rather than on solid legal foundations faces the risk of amendments should the political tides change - and they do change with election cycles.

Moreover, the sour KRG-Baghdad relations led to the practice of blacklisting, which weakens the investment climate in the Iraqi energy industry. Oil firms operating in the KRG are blacklisted from bidding on federal contracts. IOCs working with the federal government are banned from dealing with the KRG (with the major exception of ExxonMobil). IOCs see Iraq's blacklisting policy and practice as illegal and unconstitutional. The right to blacklist is a prerogative practiced by the executive branch of the federal government, with no or weak legal basis, as IRIS panelists pointed out. Hence, the blacklisting process shrinks the pool of IOCs bidding for Iraqi oil contracts and reduces competition. For example, an IRIS panelist pointed out that the federal government's deal with Shell and Mitsubishi to capture associated gas was not competitive, since no other company was allowed to table their offers. On that account, 90% of Iraq's associated gas was contracted with a single oil consortium; in effect, a monopoly. Hence, politics curtails the adoption of "market principles" as prescribed in the constitution.

Ironically, this legal and policy vacuum, while slowing down the healthy progress of Iraq's energy industry, has been beneficial to rulers and politicians both in Baghdad and Erbil. In Baghdad, dispute with the KRG is being touted in terms of patriotism and national unity, masking inefficiencies of the energy sector. Baghdad has also used the example of the KRG to further centralize power over oil management in the rest of the country, and retrench any attempts by producing regions for any meaningful level of autonomy. On the other hand, the KRG has maintained the level of autonomy it desires. The price of autonomy has been limiting accountability and transparency in the KRG's energy industry and policy. Fearing Baghdad's retribution, the KRG has kept information about its oil dealings and revenues tightly held, including to the opposition parties and the Kurdish parliament. The KRG solicits nationalist Kurdish public buy-in and support for its energy policy against Baghdad at the expense of local calls for more accountability and transparency.

1.3 Development Phases of KRG Energy Industry, and its Tensions with Baghdad

Realities on the ground are drastically different from the vision set in the Iraqi constitution and the draft national oil law of 2007. The federal government and KRG petroleum policies have diverged and became a source of conflict between the two governments. When the national hydrocarbon law failed to pass in the Iraqi parliament, the Kurdistan parliament passed a regional law in 2007, creating the KRG's ministry of natural resources and authorizing it to sign contracts with IOCs. The federal government considers the KRG's oil law unconstitutional, its contracts illegal, and its exports smuggling.[8] The more extreme Baghdad's stance became against the KRG, the farther the latter moved toward independent policy making and implementation.

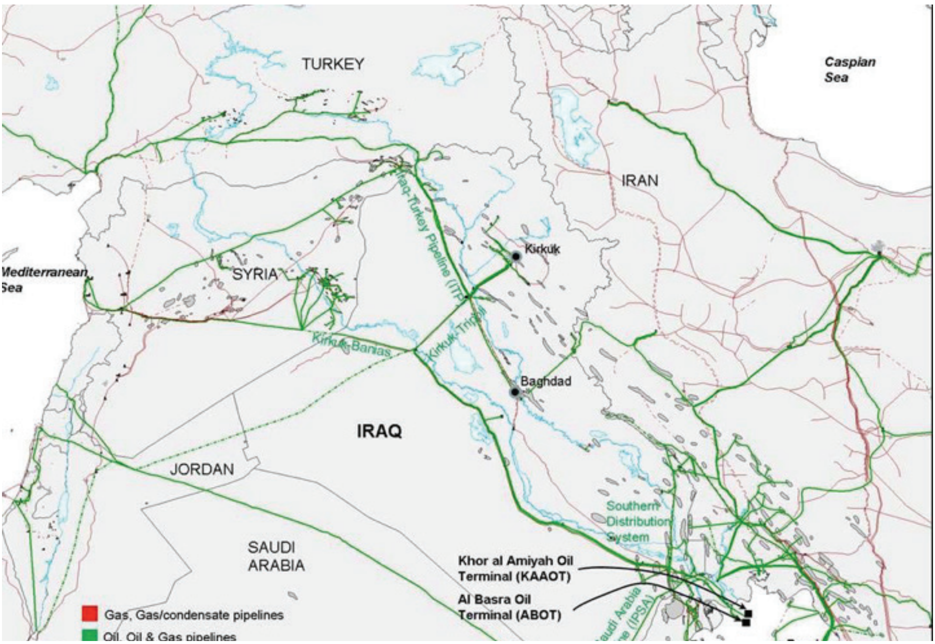
The KRG's main demand of Baghdad has been for the IOCs that operate in Kurdistan to be paid outside the KRG share of the national budget. The federal government, on the other hand, has attempted to control, or at minimum supervise KRG's oil policy and industry and integrate all energy decision making in Baghdad. The KRG has embarked on a strategy of creating facts on the ground large enough that that Baghdad cannot afford to ignore them. The KRG started a contract-signing spree-by December 2013, about 60 contracts have been signed with foreign oil firms. With 45 billion barrels of reserve, the KRG is currently at 400,000 barrel per day production capacity, slated to more than double by 2015 (see Map 1).[9] Legal or not in Baghdad's view, the KRG's energy industry is shaping up and demands to be reckoned with. Baghdad has threatened budgetary penalties against the KRG, by cutting or limiting its 17% share. Rather than budget to this leverage, the KRG has sought independent oil export and monetization routes, through Turkey, by tapping into the Iraq-Turkey Pipeline (ITP). (see map 2)

This map has been adapted by the International Crisis Group from a map made available by the U.S. Government. It is a modified version of a similar map appearing in Crisis Group Middle East Report N°88, *Iraq and the Kurds: Trouble Along the Trigger Line* (8 July 2009). Oil concession boundaries and lead operators with contracts with the KRG as of April 2012 have been added. The location of all features is approximate.

Map 1: Northern Oil and Gas Fields, KRG Oil and Gas Concessions, and Green Line (Source: International Crisis Group, N°120, p. 27)

Hence, Baghdad's pressure backfired, and rather than facilitating a deal, pushed the KRG closer to Turkey.

The road to this extreme divergence has been tortuous. The KRG and the federal government have tried to work out agreements regarding paying oil companies, oil exports and revenue sharing through numerous failed attempts at cooperation and conciliation. The KRG's energy industry fast-tracked in three phases, and in half a dozen years. Phase I: the KRG invited small to medium-size IOCs (known as wildcatters) en masse to explore the Kurdish region for oil and gas. The KRG also passed a regional hydrocarbon law, and



Map 2: Iraq's pipeline infrastructure
(Deutsche Bank, "Iraq: The Mother of All Oil Stories" 2010)

adopted the industry-favored production sharing contracts (PSCs). A Kurdish official called this approach the "smaller, faster, lighter" approach. The federal government responded by calling the law unconstitutional and the contracts illegal, and blacklisting the IOCs dealing with KRG from bidding on blocks in the south.

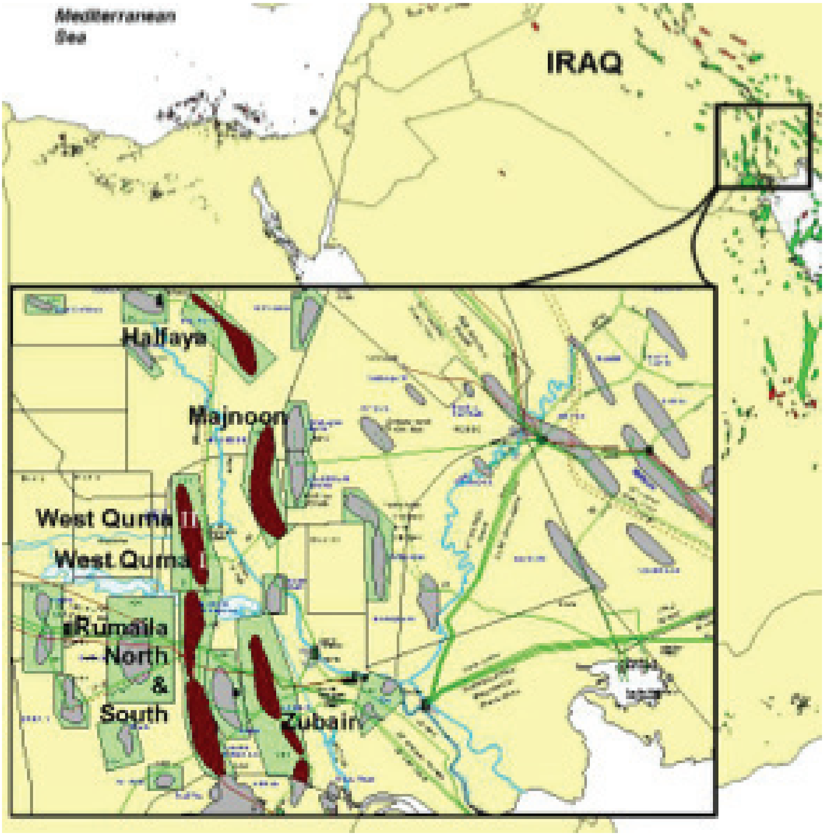
Phase II of KRG energy development is consolidation, which is an ongoing phase. Major oil companies were paying close attention as wildcatters struck oil. Once deemed commercially viable, major IOCs such as ExxonMobil and Chevron started entering the Kurdistan energy scene. ExxonMobil did this despite threats from Baghdad to blacklist it and expel it from West Qurna, a giant oilfield (see map 3). The KRG's contract terms are more attractive to IOCs, and the work environment is more business-friendly than that of the federal government. The federal government has not expelled ExxonMobil from West Qurna, despite threats to do so. The Final phase is independent monetization, which is crucial for the success of phase II and the long-term viability of KRG's energy industry. Hence, the KRG's

> ***«17 percent of Iraq's oil revenues remain larger than 100 percent of revenues from KRG oil exports, at least in the near term»***

pipeline projects to Turkey. IOCs need to export the oil they find in the KRG in order to get paid according to the terms of the PSC. Direct exports and sales by the KRG would weaken Baghdad's leverage to deny the KRG its share of the budget. Nonetheless, 17 percent of Iraq's oil revenues remain larger than 100 percent of revenues from KRG oil exports, at least in the near term.

The KRG's ability to directly export oil, and Turkey's political backing, may be game changers. This could put Baghdad further on the offensive against the KRG, hurting the latter's economy and oil industry. Rather than adopt such a confrontational response, however, it could be time for Baghdad to adopt a more conciliatory approach toward the KRG to avoid pushing it further toward Turkey. Should politics further diverge oil policies, unilateralism will go even farther.

> ***«The more extreme Baghdad's stance became against the KRG, the farther the latter moved toward independent policy making and implementation»***



Map 3: Iraq's Giant Fields": Rumaila, West Qurna I, West Qurna II, Zubair, Majnoon, Halfaya (Source: David Clark 2010, "IRAQ: Oil Development & Implications for the Global Market". Deutsche Bank Global Integrated Oil & Gas.

1.4 Efficiency, Transparency and Accountability

In addition to the vague legal environment and political disputes, weak governance and mismanagement mar Iraq's and the KRG's petroleum sectors. Convoluted bureaucracy, red tape at multiple agencies, and bribery make navigating the Iraqi bureaucracy a maze for businesses. When government functions are not streamlined, ample opportunities for corrupt payments arise. According to one estimate cited by an IRIS panelist, Iraq could be losing up to $55 billion a year of potential revenue to mismanagement and waste, such as shortages of power supply and fuel, and untapped energy sources such as gas flaring.

> *"If the government in Baghdad fails to institutionalize decentralization as envisioned in the constitution, oil policy could be further localized and fragmented"*

The KRG is not immune from governance challenges, but its problems are less pronounced compared to Baghdad's. The KRG's Ministry of Natural Resources (MNR) acts as a one-window shop for the IOCs, who do not need to deal with the wider and less efficient KRG bureaucracy. While convenient for IOCs, the rest of the KRG bureaucracy is not under pressure from energy firms to reform and enhance efficiency. The one-window shop policy also translates into too much power concentrated in the MNR. Although mismanagement and corruption are different, they are often perceived as the same. Furthermore, since the energy sector is among the most prone to corruption,[10] it is often perceived as guilty unless proven innocent through transparency.

The main challenge for Baghdad remains fixing the government, otherwise its grip will loosen over the remainder of Iraq's energy industry. The Iraqi federal government has been largely ignoring local governments and input from producing provinces. According to the draft federal hydrocarbon law, all oil contracts need to have the trinity of approvals by the federal, KRG and producing local governments. The federal government has contracted out 85 billion barrels of Iraqi oil without much input from the local governments of producing governorates, as one IRIS panelist pointed out. So far, the provincial governments have been weak vis-à-vis the federal government and succumbed to federal will or pressure. However, local governments are becoming more representative than the federal government. Elected provincial councils and governors will seek a larger say in the oil and gas beneath their feet, and some could follow the KRG model of seeking more autonomy. If the government in Baghdad fails to institutionalize decentralization as envisioned in the constitution, oil policy could be further localized and fragmented. Basra and Kirkuk are prime candidates to act more independently.

Among the major sources of challenges facing Iraq's and the KRG's petroleum industries is the politicization of petroleum management. More specifically, Iraq's Ministry of Oil (MoO) and the KRG's Ministry of Natural Resources (MNR) and the men at their helms enjoy significant powers. In both Baghdad and Erbil, the executive branch of government enters into contracts with IOCs, without much oversight from other branches of government. In comparison, national oil companies are either weak (as in Baghdad) or do not yet exist (as in the KRG). Giving oil ministries the upper hand vis-à-vis oil companies is a Saddam Hussein legacy that lingers; it should have been changed in favor of de-politicizing oil in the new Iraq. Sizeable amounts of oil revenues flow directly into governments' pockets without much restraint against their long arms. Best practices entail that the government should be a regulator, not a contractor, of the energy industry. Compared to the amount of power and money that contracting oil channels to the executive, the legislative and judicial branches of the governments in Baghdad and Erbil are rendered too weak to hold the executive to account. Moreover, crucially absent is a serious public debate about policymaking in the petroleum sector that involves institutions of civil society.

Compared to the large sums exchanging hands between IOCs and governments, the level of transparency remains limited. In 2013, Iraq ranked at the bottom of the Corruption Perceptions Index (171/177).[11] More transparency is key to building more trust between KRG and Baghdad on one hand, and to making the industry more viable on the other. According to one IRIS panelist, transparency comes in black and while rather than in shades of grey. Seen broadly, there should be transparency across the oil and gas value chain, from reservoir management, to revenue management and distribution. Signing up for the Extractive Industries Transparency Initiative (EITI) is positive, but inadequate, since EITI does not have access to the contracting network nor to some oil sale figures.

Baghdad often accused the KRG of a poor transparency record. This is a serious issue for the KRG's energy industry, since the opposition parties and the media also echo such criticism domestically.
The MNR signs the contracts without much oversight from the parliament. Hence, vertical accountability within the KRG is lacking. Also, horizontal accountability between Baghdad and KRG is also missing, since the KRG seems to be hiding oil proceeds from

Baghdad for fear of the latter's retribution through budget cuts.

No one is able to hold these strong executive powers in Baghdad and Erbil accountable better than each other. That is, *interdependence* between the federal government and the KRG is the way forward to improve accountability and transparency. The KRG has an interest in better governance in Iraq's energy sector; otherwise its better performance will be lumped in with Iraq's miserable record on international indices that measure corruption (CPI), governance quality (World Bank Governance Indicators), and human development indicators (UNDP).

Finally, Iraq and the KRG seem to be suffering from initial but serious symptoms of the "resource curse," especially the Dutch Disease. That is, the Iraqi economy and its government budget are becoming chronically dependent on oil and gas revenues. Petroleum revenues account for 75 percent of GDP, and 95 percent of government revenue. Despite rising government revenues, both the federal and Kurdistan regional governments have consistently spent about 70 percent of their budget on operations (as compared to investment), such as on nurturing a bloated public sector. Furthermore, linking Iraq's budget to international oil prices destabilizes the Iraqi economy. War-torn Iraq and Kurdistan need long-term investments in physical infrastructure and human capital. Such investment is crucial for diversifying Iraq's revenue sources and weakening its dependence on revenues from the sale of oil and gas.

2. Key Actors in Iraq's Energy Sector and their Goals

The key players and actors shaping and influencing Iraq's energy policy and industry can be listed as governments, the energy firms and civil society.[12] These actors and their actions can be categorized into multiple levels, such as national-regional, and international, public-private, and tactical-strategic among others. Contracts regulate government-IOC relations, the political system regulates government-citizen relations, and corporate social responsibility regulates public-IOC relations (See figure 1). The following sections will identify each of the major actors and discuss their role, objectives and relations.

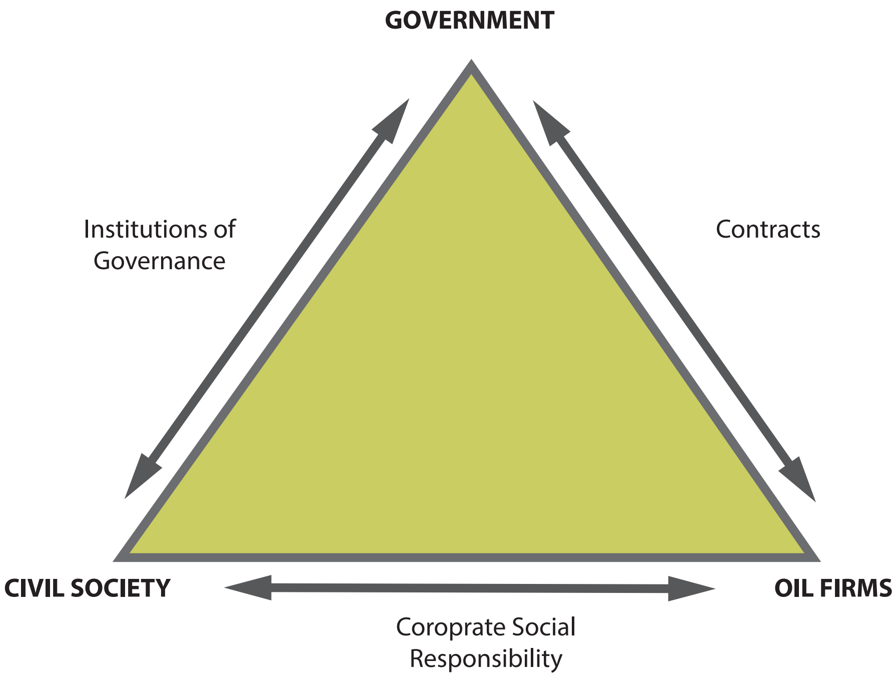


Figure 1: Key players and their relations

2.1 Iraq's Federal Government

The federal government's goals have been to centralize policy making in Baghdad, and to maximize oil revenues as quickly as possible. Because of years of sanctions and wars, the non-oil economic sectors are less attractive compared to the oil and gas sectors. The result has been increased dependence on oil for economic rent generation and government revenues. Iraq is planning to boost oil production to reach nine million barrels a day by 2030. Iraq was ambitiously hoping to hit that number a decade earlier. However, Iraq's strategy of maximum revenue generation is undercut by Baghdad's tactical inability to perform and implement oil contracts, and to spend the majority of the wealth accrued from oil on security and government operations.

> «The Iraqi economy and its government budget are becoming chronically dependent on oil and gas revenues. Petroleum revenues account for 75 percent of GDP, and 95 percent of government revenue»

A second goal of the government in Baghdad has been to maintain its centralized control over the petroleum sector. Maintaining an upper hand against producing regions has been relatively easy for Baghdad, since the balance of power on the ground is tilted in favor of the federal government. The main obstacle facing Baghdad's central grip on policy, however, has come from the KRG.

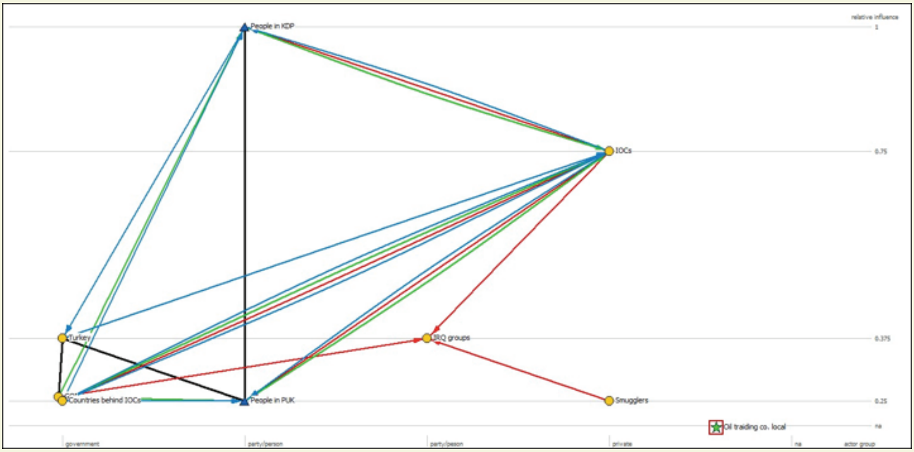
> ***«Individuals rather than institutions seem to be the key shapers of energy policy in Baghdad and Erbil»***

Individuals rather than institutions seem to be the key shapers of energy policy in Baghdad and Erbil. None more so than former Iraqi oil minister and now deputy prime minister for energy, Mr. Hussein Al-Shahsirtani. Mr. Al-Shahristani is a "politician with technocratic support," as one Iraqi energy expert described him. The role of powerful individuals in post-Saddam Iraq's energy policy is present in the Kurdistan region as well. Mr. Ashti Hawrami, the KRG minister of natural resources, plays a significant role. Compared to Al-Shahristani, he is "a technocrat with political backing" from the Kurdistan Regional Government. Whether these two personas lead or simply implement the policies of their respective governments and prime ministers is debatable. Nonetheless, the level of power and influence that Mr. Shahristani and Mr. Hawrami wield regarding the energy sector has to an extent personalized the decision making process regarding Iraq's energy sector. Government institutions, especially the Council of Representatives in Baghdad and the Kurdistan Parliament in Erbil, have played a lesser role, as have provincial and local governments (see box).

Box: Mapping out actors and their relationships

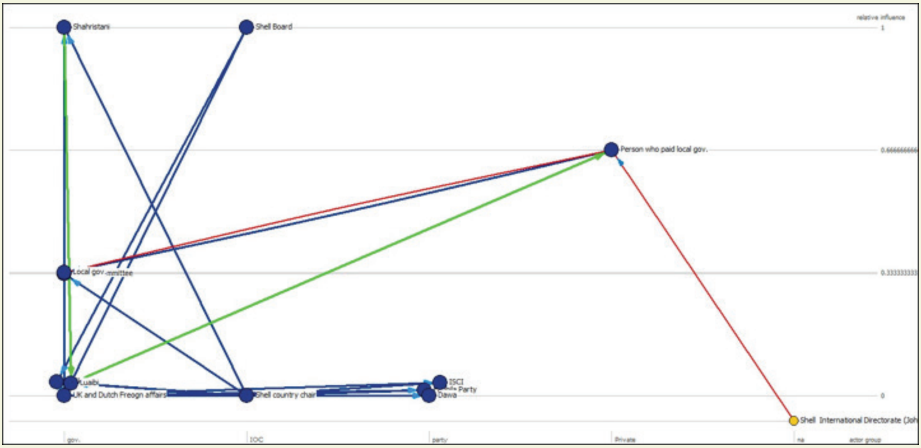
IRIS discussed Iraq's and KRG's energy policies and industries with experts from the energy sector, government, civil society, and the media. Focus group sessions were also geld, applying a mapping exercise where the experts methodically answered questions about key actors, their relationships, their goals, and each actor's relative influence. The analytic method is called Net-Map© and the software used to make the maps is called FisuaLyzer©. Below are sample maps from the discussions, with brief descriptions.

A. Actors and Relations that Influence the Making of KRG Energy Policy.
This map sought to map out general influence in the making of KRG energy policy.



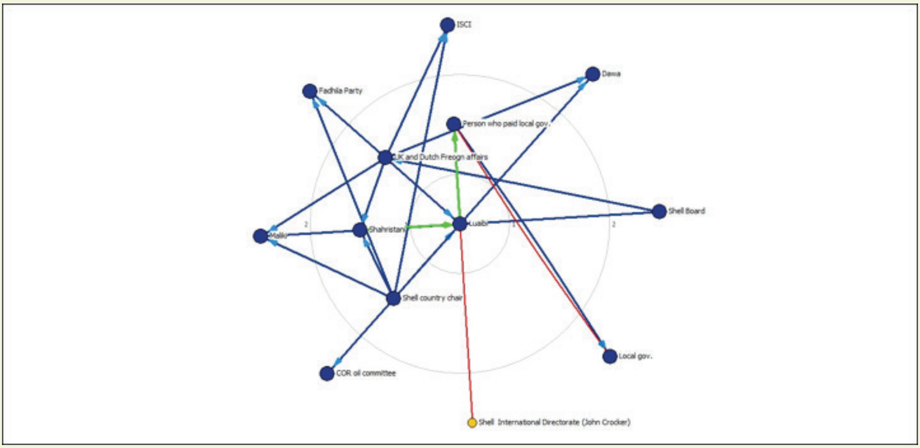
Nodes indicate actors.
Lines indicate relationships (arrows indicate direction). Black: Disagreement.
Green: Formal Cash flow. Red: Informal cash flow. Blue: Political influence.
X-Axis: Category of Actors.
Y-Axis: Their relative influence.

B. Actors and Relations that Influence the Signing of the Shell Gas Contract with the Federal Iraqi government.
The two charts below portray actors and relationships that influence the signing of a sample energy contract (Shell Gas deal). The two maps are the same, but with different configurations. The first highlights relative influence, and the second, the centrality of actors.
Lines indicate relationships (arrows indicate direction). Blue: Lobbying/persuasion.
Green: Order/command. Red: Informal cash flow.



X-Axis: Category of Actors.
Y-Axis: Their relative influence.

C. Centrality of Actors and Relations in the Signing of Shell Gas Contract with the federal Iraqi government. Focus of this chart is on centrality of the actors.



These charts solicit the perception and knowledge of industry experts and observers. They demonstrate that, on the Iraqi and KRG side, individuals rather than government institutions are perceived to be main influencers and shapers of Iraq's contracting policy in particular and KRG energy policy in general. This seems to be true both in terms of influence (A and B above) and centrality in the decision making network (C).

2.2 The Kurdistan Regional Government (KRG)

The Kurdistan region has quickly emerged as a significant player in Iraq's energy sector. The KRG has sought to build an energy industry from scratch in the shortest time possible. To date, the Kurdistan Regional Government has signed more than 60 oil and gas contracts with international oil companies (IOCs), including majors such as ExxonMobil. The KRG seeks to establish its own energy sector independent of Baghdad, as a guarantee of economic independence. Many perceive political independence as the long-term goal of the KRG's oil dealings, "a contingency plan" for pulling away from Iraq, as one panelist at IRIS put it. Economic independence could render political independence more feasible. Hence, the KRG seeks to build the capacity for statehood. Mr. "Hawrami is not only in the business of building an [oil] industry, but in nation building

Hence, the KRG seeks to build the capacity for statehood. Mr. "Hawrami is not only in the business of building an [oil] industry, but in nation building too," said another IRIS panelist

too," said another IRIS panelist. In the short run, however, the KRG seeks to achieve economic sustainability and provide services to KRG residents. As in Baghdad, however, the KRG's energy industry remains highly politicized, where economic and commercial interests come second to political objectives.

The KRG's strategy is to attract Big Oil and tie its security and autonomy to the interest of major international oil importers. It is politically important for the KRG that majors are able monetize their investment over the long run. The KRG's pipeline agreement with Turkey, although it has angered Baghdad, is an instrumental step toward creating a viable Kurdish energy industry. The KRG feels under pressure to achieve these goals in a short time, since the window of opportunity is closing on it—on one hand, Baghdad is getting stronger and therefore abler to undercut KRG's energy goals; on the other, internationally the recent technological developments in shale oil and renewable energy may attract investment monies elsewhere.

Despite different approaches and disagreements over power and control, the federal government and the KRG have shared goals, according to one IRIS panelist. They both seek to maximize production in record time, maximize their control and grip over their respective petroleum industries, and deepen the dependence of their respective economies on oil revenues.

2.3 International Oil Companies (IOCs)

International oil companies see an opportunity in Iraq, one of the least explored countries rich in conventional petroleum in the world. Since Iraq nationalized its petroleum industry in 1972, IOCs have not had a foothold in country. The 2003 invasion of

Iraq and the country's new constitution allowed for opening Iraqi oilfields to exploration and production by IOCs. IOCs are attracted to this new opportunity, but not as enthusiastically as initially expected, mainly due to the risks and challenges highlighted earlier in this report.

The relation between IOCs and governments in Iraq is regulated mainly through contracts (see figure 1). The federal government in Baghdad has adopted the technical service contracts (TSC) model, where the companies are paid a fee for their services. Iraq's oil ministry organized four licensing bidding rounds, where IOCs went through a prequalification phase before bidding publically for oil and gas blocs. Iraq has managed to attract several major IOCs to invest and boost production in Iraq's southern oil and gas fields. Iraq's fourth round of bidding had lackluster results, for the terms of the TSCs were unattractive. IOCs see lingering legacies of oil nationalism undercutting Iraq's ability to attract much needed foreign investment. The federal government may make the TSC more appealing to IOCs, or consider adopting alternative models, such as production sharing contracts (PSCs).

« ***IOCs see lingering legacies of oil nationalism undercutting Iraq's ability to attract much needed foreign investment*** »

2.4. Regional and International Actors

In addition to national and commercial players, there are regional and international players who influence the making and development of Iraq's energy industry and policy. Below, the roles of Turkey, the United States and Iran will be briefly highlighted.

Turkey

Turkey is becoming an increasingly active player in Iraq's energy scene. Turkey's economic growth is energy-thirsty. While Turkey has benefited from being an export route for Iraqi oil, it also is eying Iraq's natural gas, which Turkey needs for its domestic energy consumption and industry.

Turkey's relation with Iraq and Iraqi Kurdistan has transformed over the past few years. Ankara's mainstream foreign policy has been to maintain Iraq's territorial integrity, keep Kurdish independence aspirations in check, and contain the KRG's influence as a model for Turkey's own Kurdish population. Turkey was very skeptical and suspicious of KRG energy aspirations. In 2006, Turkey's trade regulating agency issued a special decree banning oil imports from Iraq except through SOMO. As late as 2007, trucks were not allowed entry into Turkey because they had the word "Kurdistan" written on them. This antagonism against the KRG has quickly evolved into what was described as a "catholic marriage" by an IRIS panelist.

Changes in domestic Turkish foreign policy orientation, coupled with its energy needs, and the Erdogan-Maliki fallout smoothed the path for a Kurdish-Turkish rapprochement. The KRG seeks an outlet for the oil produced in the Kurdistan region so its IOCs can get reimbursed for their investments. Furthermore, the KRG seems to have started to value Turkey's practical political support over Washington's critical rhetoric. For Turkey, an oil-exporting pipeline from the KRG offers Ankara leverage over the KRG, and turns Kurdish political parties into allies in Turkey and Syria. The ruling AK Party in Turkey could expedite the energy deal with the KRG before its domestic troubles further escalates. Moreover, the KRG could potentially provide up to a third of Turkey's gas needs in the future. Also, Ankara could strategically use its good relations with Erbil as a vehicle to better its relations with Baghdad, and to bring Baghdad and Erbil closer.

The U.S.

The United States remains an important player in Iraq's energy sector; both for its assistance in drafting the 2007 draft oil law, and as buyer of 19% of Iraq's oil exports. IRIS panelists debated and disagreed over the role and influence of the United States. The Obama administration has adopted a One Iraq policy, which weighs energy policy against preserving Iraq's territorial unity. Washington has been discouraging IOCs to sign oil deals with the KRG before a national hydrocarbon framework is agreed upon.[13] When ExxonMobil decided to sign deals with the KRG, Iraqi Prime Minister Nouri Al-Maliki wrote a letter to Obama asking him to stop ExxonMobil from dealing with the KRG. Although the Obama administration advised companies about the legal and stability risks involved in dealing with KRG without Baghdad's approval, an Obama official reiterated that the U.S. government couldn't stop ExxonMobil from making a decision that the company saw fit.[14] Some in Washington see KRG's actions as irresponsible. ExxonMobil has come north and has so far maintained its contracts in the south as well. The KRG is happy with the Exxon deal and sees it as a vote of confidence and legitimacy for its energy policy.

Regarding U.S. views on the Turkish-KRG relations, realities on the ground have been louder than feeble noises from Washington. Washington did not receive the news of the KRG-Turkey pipeline positively. There might be misconceptions in Washington and Ankara about each other, but as one IRIS panelist put it, indications from Washington have not been all that negative. The U.S. may eventually come to terms with the warming Ankara-Erbil relations, which Washington sees as too close at the moment. Some in Ankara have seen the presence of ExxonMobil in the KRG as tacit approval from Washington. In its relations with the KRG and Iraq, Turkey might be taking the lead on its own terms, rather than taking cues from Washington.

Iran

Iran may not have been visibly a major player in Iraq's oil industry; it remains a significant actor in general Iraqi politics. Iran favors a strong, Shia-led central government in Baghdad. Hence, Iran could limit policy options in favor of its goals, as one IRIS panelist put it. Iran also has leverage over the KRG and its two main ruling parties. Iran may seek to balance Turkish power and influence in Iraq and the KRG. Moreover, Iraq's rise as an energy giant could bolster the independence of Iraqi politicians and weaken Iran's influence in Iraq. Should international sanctions imposed on Iran be lifted, Iraq would be a competitor to Iran in the OPEC as well. Therefore, the IRIS panelists voiced anticipation of larger Iranian influence in Iraq's and the KRG's petroleum sectors and politics.[15]

3. Opportunities and the Way Forward

3.1 Public Debate

Decisions made today about the oil and gas industry will affect the current and future generations for decades to come. Among the conclusions of the IRIS roundtable is that the making of petroleum policy is concentrated in small, mainly political circles, often of few individuals. Brazenly absent is an informed public debate. Facts created on the ground since 2007 have pushed Iraqi national and Kurdish regional interests further apart. If Iraqi institution and elections have failed to create the right atmosphere for settling the differences, Iraqis may need mediation, as a few IRIS panelists recommended. The status quo is not sustainable and not conducive to an accountable and transparent petroleum industry that results in prosperity for Iraqis.

> «*NGOs and CSOs are generally sidelined in the oil discussions. Nor do they proactively engage*»

Moreover, NGOs and CSOs are generally sidelined in the oil discussions. Nor do they proactively engage. Absent also are well-informed business and finance journalists who can cover energy news. Also, the role of the local private sector is weak, almost excluded from the energy sector, as influence Net-Maps demonstrated. Hence, a more robust public engagement is needed and is necessary for the health and political sustainability of Iraq's and the KRG's energy industries.

3.2 Diversification and Future Funds

Furthermore, the lack of a vision and well-debated public policy could explain the spending spree that is

taking place in Iraq. It is imperative that Iraqi policymakers think ahead so the Iraqi economy avoids becoming an entrenched oil-dependent, rentier economy. Absent a strong and well-funded diversification strategy, the Iraqi and KRG economies will be extremely vulnerable to oil shocks and price fluctuations. Moreover, oil dependence and subsequent inflation will crowd out other economic activities (known as the Dutch Disease) and plunge the Iraqi society deeper into consumerism and away from productivity. As one panelist noted, rentier states have a 30-year window to diversify their economies; otherwise, they will become terminally oil dependent.

Both Iraqi and Kurdish governments are committed to maximizing oil revenues by increasing production and export of oil and gas. Some scholars of economic development in resource rich countries advise against this.[16] Iraqi and Kurdish policymakers should cap revenue generation at their capacity to spend. Similarly, government spending should also be capped in favor of investment. Alternatively, should the governments in Iraq and Erbil be unwilling to put a cap on production, they should create and invest in institutions that manage the excess wealth rather than spend it. An example of such institutions would be Sovereign Wealth Funds (aka Future Funds). Such a fund, if effectively managed, would help smooth revenue fluctuations that come with oil price volatility. If properly invested, the Fund can also ensure that future generations benefit from today's oil revenue once the resource is depleted.

3.3 Natural gas

Developing and producing natural gas would boost the economy and could be an opportunity to develop cooperation between Baghdad and the KRG. If the KRG more seriously developed natural gas, it could help Baghdad by providing it with natural gas and electricity. This would give the KRG leverage against Baghdad, and win public opinion in the rest of the country. As mentioned earlier, Turkey is also eying KRG's and Iraq's natural gas exports. Iraq should start eliminating waste--by one estimate, half of Nabucco's capacity is flared and wasted in Iraq due to lack of capturing technology. More investment in gas infrastructure and production is needed. The KRG was ahead of the gas game but slowed its development. Oil is contentious, but gas could be a source of harmony.

Moreover, natural gas could also spur local industries, such as petrochemicals and power generation. There is more potential to inject gas into the local economy to boost the private sector and lift some employment pressure off of the public sector. Domestic use of gas is preferable to exporting it, according to one expert at the IRIS panel.

Conclusion

Oil and gas are slated to shape Iraq's political and economic development trajectories. Despite conflicts between the federal government and the KRG over the management of the country's petroleum resources, there is more to be gained through cooperation. Mediation could help bring the two sides closer. With an increasingly viable KRG energy industry, a sustainable deal with Baghdad shoud be easier to achieve. However, for a long-term deal to be sustainable, the energy sectors need to be more transparent, especially to the regulatory and monitoring institutions. More transparency and accountability about oil and gas are crucial, especially as energy policy and revenue sharing find their way into election platforms. Post-election government formation negotiations will undoubtedly be anchored around oil as well. Finally, oil wealth will not automatically translate to prosperity. Sound long-term policies must be considered, informed through public and social input, in order to avoid the pitfalls of the resource curse.

Notes

1. Iraq's Constitution, Article 112, Second.

2. The social networking tool used is Net-Map©, developed by Eva Schiffer, PhD. More information about this tool at www.netmap.ifpriblog.org

3. Article 117 of the Iraqi constitution states, "This Constitution, upon coming into force, shall recognize the region of Kurdistan, along with its existing authorities, as a federal region."

4. These exclusive rights and responsibilities include diplomatic representation; international treaties and agreements; foreign sovereign economic and trade policy; and commercial policy among others.

5. Article 115 of the Iraqi constitution maintains that, "All powers not stipulated in the exclusive powers of the federal government belong to the authorities of the regions and governorates that are not organized in a region. With regard to other powers shared between the federal government and the regional government, priority shall be given to the law of the regions and governorates not organized in a region in case of dispute."

6. Raad Alkadiri, "Oil and the Question of Federalism in Iraq," *International Affairs (Royal Institute of International Affairs 1944-)* 86, no. 6 (2010): 1315–28..

7. Legal experts from Herbert Smith Freehills LLP, a UK based law firm, made a presentation at the annual Kurdistan-Iraq Oil & Gas Conference in Erbil on December 1, 2013. The author attended and has a copy of the presentation.

8. For more details, see International Crisis Group, *Iraq and the Kurds: The High-Stakes Hydrocarbons Gambit* (International Crisis Group, April 19, 2012), available at http://www.crisisgroup.org/~/media/Files/Middle%20East%20North%20Africa/Iraq%20Syria%20Lebanon/Iraq/120-iraq-and-the-kurds-the-high-stakes-hydrocarbons-gambit.pdf.

9. See The Ministry of Natural Resources website, "The Road to 1 Million Barrels," http://mnr.krg.org/index.php/en/the-road-to-1-million-barrels

10. J. Edgardo. Campos et al., *The Many Faces of Corruption [electronic Resource] : Tracking Vulnerabilities at the Sector Level* (World Bank, c2007.), http://aquadev.wrlc.org/?hreciid=%7clibrary%2fm%2fGW%7c7053155.

11. See Corruption Perceptions Index at www.transparency.org

12. Gavin Bridge and Philippe Le Billon, *Oil*, Resources (Cambridge, UK ; Malden, MA: Polity Press, 2013).

13. Even the Bush administration discouraged IOCs from signing contracts with KRG without the approval of the federal government. See the Washington Post report on KRG deal with Hunt Oil: voices.washingtonpost.com—dems_administration_knew_more.html

14. Reuters, June 19, 2012. http://www.reuters.com/article/2012/07/19/us-iraq-oil-kurdistan-idUSBRE86I1HL20120719

15. Read also, Startfor, Letter from Kurdistan, http://www.stratfor.com/weekly/letter-kurdistan

16. See for example, Michael Ross, *The Oil Curse: How Petroleum Wealth Shapes the Development of Nations* (Princeton, NJ: Princeton University Press, 2012).

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