

27 April 2007

STATEMENT FROM MINISTER OF NATURAL RESOURCES KURDISTAN REGIONAL GOVERNMENT - IRAQ

The Kurdistan Regional Government (KRG) clarifies its position regarding the latest developments on the Draft Oil Law

In the light of the recent developments, the Kurdistan Regional Government (KRG) expresses serious concerns regarding the draft Annexes to the proposed Oil and Gas Law that were recently circulated, and that were discussed last Wednesday at a conference in Dubai (“the Dubai Annexes”).

These are concerns that should be shared by all Iraqi citizens. In summary, the Dubai Annexes are inconsistent with the overriding policy goal of maximizing economic returns to the Iraqi people, and inconsistent with Iraq’s federal Constitution. The Dubai Annexes are inconsistent with the proposed Oil and Gas Law that was agreed by the Council of Ministers on 15 February 2007.

As a member of the Federal Oil and Energy Committee, I urge the Committee to address these concerns, and consider the merits of the attached KRG-proposed amendments to the Annexes. Until our concerns are addressed, the KRG cannot support any Oil and Gas Law package of legislation in the Council of Representatives.

Our concerns with the Dubai Annexes are as follows:

1. Concentration of unaccountable power: The Dubai Annexes attempt to allocate almost 93 per cent of Iraq’s proven petroleum reserves to a new “Iraq National Oil Company” (INOC), leaving barely 7 per cent for Regions and other entities to use for inward investments. Furthermore, the majority of the fields included in the 7 per cent remainder are marginal or not commercial. Massive power will be concentrated in the hands of INOC without any clear investment and production targets, and without clear accountability to the people of Iraq. With this level of concentration, the proposed Oil and Gas Law, and any regulatory apparatus, will become irrelevant.

The Board of INOC must be entirely separate from the Oil Minister and the Oil Ministry: INOC must be a regulated, not a regulatory, body. Because it is supposed to be a federal institution, INOC must be accountable to the Federal Oil and Gas Council, and not to the Council of Ministers. INOC must not be given almost the entirety of Iraq’s oil and gas reserves.

The proposed Federal Oil and Gas Council, an intergovernmental institution, will recognise to the fact that Regional rights over petroleum have paramountcy in the Constitution over federal rights (Article 115) and the right of Regions to be represented in federal decision-making (Article 105).

2. Return to old regime methods: The concentration of power in the hands of INOC will represent a return to method of petroleum management of previous Iraqi regimes, where centralized oil power was a corrupting influence, and used to fund violent campaigns by elites against neighbouring countries and against our own Iraqi citizens.

Iraq's petroleum regime must be modern. The KRG is well aware that all successful oil producing federations have a decentralized petroleum sector, with some level of national co-operation, and all are open to private investment. Iraq's Constitution, in Article 112, mandates just such a petroleum sector, and the Constitution must be honoured.

3. Breach of constitutional rights of Regions: The allocation of petroleum to INOC as proposed in the Dubai Annexes is unconstitutional. Specifically:

(a) The Dubai Annexes purport to give to INOC petroleum fields that are undeveloped, including fields that must be managed by future Regions in Iraq, including a future southern Region or Regions. These fields must be under the management control of Regions and Governorates pursuant to Article 112 of the Constitution. Undeveloped fields over which no Region or Governorate asserts jurisdiction should be allocated, temporarily, to the Oil Ministry, and open to bidding.

(b) The Dubai Annexes give to INOC currently producing fields, but do not place INOC under an obligation to manage those fields *jointly* with Regions and Governorates. Article 112 of the Constitution is clear on this point also, but the INOC law, as drafted, does not acknowledge the role of Regions and Governorates as joint partners in management decisions, but rather refers only to a diluted consultation mechanism.

(c) The Dubai Annexes do not clearly recognize KRG authority to contract in the Kurdistan Region, and indeed propose exploration and development blocks in the Kurdistan Region that differ from those which are already the subject of KRG contracts with private investors. Annexes 3 and 4, in particular, must recognize the fact that the Constitution itself, in Article 112, allocates fields other than currently producing fields to the Regions and Governorates, including the Kurdistan Region. The Annexes must recognize that the KRG has already allocated exploration and development blocks in the Kurdistan Region under Production Sharing Agreements pursuant to the Iraq Constitution. The Annexes must clearly acknowledge that fields and blocks in the Kurdistan Region are under the KRG's jurisdiction, that it is for the KRG to define the coordinates of the fields and blocks, and that the KRG will be contracting authority for those fields and blocks.

The KRG considers that, in the unlikely event the proposed Law with the Dubai Annexes were presented to the Council of Representatives and approved by the Council, the law would be immediately void as unconstitutional by virtue of Article 13 of the Constitution.

4. Breach of constitutional revenue sharing rules: It is also unclear whether the Dubai Annexes will require INOC's revenues to be shared throughout Iraq according to population. Article 112 of the Constitution is very clear on this requirement.

With these Dubai Annexes, Iraq is in great danger of losing its main source of revenue to an unaccountable entity that will absorb funds for alleged reinvestment and expansion but without returning funds to the people of Iraq. The KRG has advanced several discussion

drafts of a revenue sharing law for Iraq that would pool all petroleum revenue, wherever that revenue is raised, for sharing throughout Iraq according to the Constitution. We have received no response.

5. Failure to maximize revenue for Iraq: The legal obligations of INOC to develop Iraq's petroleum are unclear in the Dubai Annexes. Article 112 of the Constitution requires oil production in Iraq to maximize returns to the peoples of Iraq. The Dubai Annexes provide Iraq with no assurance that INOC will be any better than the current bureaucracy in increasing petroleum revenue for Iraq. Many of the fields which are proposed to be allocated to INOC have been discovered for up to 30 years, without any development. With no accountability or contractual requirements to produce, why should we expect the performance of INOC to be any better than that of the Oil Ministry in past years and decades?

INOC must be clearly defined as a contract-holder for each of the particular fields allocated to it, like any other contractor in Iraq, with contractual obligations to the Iraq federation to develop fields and generate revenue for Iraq-wide sharing. This was the intent of the 15 February Draft Oil and Gas Law. Each field for which INOC is the contractor must, depending on the particular nature of the field, have a mandatory program for field development. If the mandatory program is not met, the field should be put on the market for open bidding, to obtain maximum timely returns to the Iraqi people. INOC should be given a mandatory target of increasing Iraq's petroleum production to 4.5 million barrels per day within 5 years, and should lose some of its contractual rights if individual field targets are not met.

6. Deters investment: The Dubai Annexes will deter investment in Iraq's petroleum sector. The Annexes, and the comments conveyed by some of the presenters at the Dubai conference, send a clear message: Iraq is closed for business. This message is obviously designed to undermine the 15 February proposed Oil and Gas Law with respect to private sector opportunities in Iraq, and to stir up anti-foreign and reactionary sentiment. This was the message that the organizers wanted to convey through their hand picked speakers.

The authors of the Dubai Annexes announced to the conference that INOC will not enter into any contractual arrangements with the private sector, including Iraqi companies. They also announced that the earliest possible bidding round for the very small number of non-INOC fields will be December 2008. One Iraqi expert who had been originally invited to speak at Dubai was at the last minute barred from addressing the conference when the organisers realised that he would be supporting private sector participation in Iraq's oil and gas sector. The authors of the Dubai Annexes also announced that the Annexes had been made available for discussion "three months ago", a statement was blatantly false.

This is an obvious effort to return, by the back door, to the early anti-investment negotiating drafts of the Oil and Gas Law that the Oil and Energy Committee rejected as long ago as August last year. The principle underpinning the 15 February 2007 draft Oil and Gas Law approved by the Council of Ministers was that private sector investment under Production Sharing Agreements would be at the center of Iraq's petroleum strategy, with the additional use, if necessary, of risk-reward service contracts. This principle was agreed in the draft Law. The principle is inscribed in strong terms in Article 112 (2) of the Constitution itself, which *obliges* the federal government, with Regions and Governorates, "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). One of authors of the Dubai Annexes, himself serving under a Constitution adopted by nearly 80 percent of Iraq’s voters, denigrated key provisions of the Constitution. As our Prime Minister has repeatedly stressed, the people of Kurdistan are only willing to remain part of the Iraqi Federation on the basis of full implementation of Iraq’s Constitution.

The Dubai Annexes are unconstitutional, against the interests of the Iraqi people, and contrary to the 15 February agreement and Draft Oil and Gas Law. The undeveloped fields to be listed in Annex 3 and the blocks to be listed in Annex 4, must be clearly stated as fields and blocks which will be developed using Production Sharing Agreements.

KRG-proposed amendments to the Annexes:

I understand that some members of the Federal Government wish to maintain firm Iraqi control over Iraq’s petroleum sector. That wish is understandable. However these draft Annexes will not give control 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.

The overriding goal of the Oil and Gas Law must be to maximize returns to the people of Iraq in all the Regions and Governorates, consistent with the Constitution of Iraq. The KRG has proposed Annexes which I believe will achieve this goal, and which strike a fair balance between the interests of the Federal Government, the Regions, and Governorates. 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. This will enable INOC, under a clear mandatory program, to raise its share of production to around 4.5 million barrels per day, but still to allow reasonable scope for the private sector and inward investment to boost Iraq production levels to approximately 8 million barrels per day. The result will be a united and prosperous federation.

In the attached KRG-proposed Annexes, I have moved fields from the jurisdiction of INOC, setting out my reasons for doing so in Tables 1A, 2A, and 3A, and have included language recognizing the KRG’s contracting rights. These Annexes must be adopted to enable KRG to lend its support to the Draft Oil Law.

Outstanding matters:

In these circumstances, I note the outstanding matters that must be agreed before there is a serious oil and gas package for the Council of Representative’s consideration:

1. *Annexes*: The Oil and Energy Committee must agree the Annexes to the Law.
2. *Model Contracts*: The Oil and Energy Committee must agree model production sharing and service contracts. I note that the KRG has seen no proposed model contracts of any sort from the federal government. We once again strongly urge the federal government representatives on the Oil and Energy Committee to adopt model contracts that are similar to the Model Production Sharing Agreement that the KRG has adopted and will continue to use in the Kurdistan Region.

3. *INOC and Ministry of Oil Laws*: The Oil and Energy Committee must agree laws for the structure and organization of INOC and the Oil Ministry. The KRG has received from the federal government representatives no official draft of a proposed INOC law or Ministry of Oil Law, though they have been promised for some time. These draft laws must be consistent with the Constitution and the principles of the draft Oil and Gas Law.

4. *Revenue Sharing Law*: The KRG has to date received no response to its proposed Federal Revenue Sharing Law, which we circulated in early March. The KRG draft proposes that all petroleum revenues, defined as broadly as possible, should be received and shared by an intergovernmental entity pursuant to Articles 106 and 112 of the Constitution, so that all Iraqis, and all levels of government, may benefit from Iraq's petroleum assets. To date there has been no response and not one single meeting regarding a Federal Revenue Sharing Law.

The time has come for a serious discussion on revenue sharing. The KRG still awaits the Federal Government to authorize its representatives to meet with the KRG at the earliest opportunity to discuss the draft Federal Revenue Sharing Law. This is obviously a critical piece of legislation without which the Oil and Gas Law cannot progress.

Finally, I express the hope that all these matters can be concluded as quickly as possible. The KRG has at every point in these discussions worked diligently and honestly to solve the difficult problems that face Iraq's oil sector. We have done so not only in the interests of the Kurdistan Region, but also in the name of the Constitution of Iraq and, we believe, in the interests of all the Iraqi people. We remain available to the Federal Oil and Energy Committee to agree the remaining issues. In the meantime, the KRG remains open to business and will continue to exercise its full authority under the Constitution of Iraq, including the negotiation of competitive Production Sharing Agreements with experienced international investors, for the benefit of all Iraqi people.


27 April 07

Dr. Ashti Hawrami
Minister for Natural Resources, Kurdistan Regional Government