# A Critical Look at Iraq's Oil Contracts, By Munir Chalabi *

*This report examines Iraq's current hydrocarbon contracts. It posits that they leave IOCs with too much control over the country's producing fields, and suggests alternatives.*

Since 2009, the Iraqi federal Oil Ministry has signed 11 so-called Technical Service Contracts (TSCs) and Development and Production Service Contracts (DPSCs) with some of the world's largest international oil companies (IOCs). On paper, these 11 contracts will help boost the country's production capacity from 2.4mn b/d in 2008-10 to 13.5mn b/d by 2020, which would make Iraq the largest producer in history – though some of Iraq's own leaders have suggested that production will probably not rise that high. Former Oil Minister Husain al-Shahristani said on 10 October 2012 that production will reach 9-10mn b/d in 2020 and will be sustainable for 20 years, while Thamir Ghadhban, the head of the Prime Minister's Advisory Commission (PMAC), endorsed a production plateau of just over 9.0mn b/d to be reached by 2020.

The International Energy Agency (IEA) report presented in Baghdad in October 2012 presents three scenarios for oil production in 2020 and 2035. A 'High' case gives 9mn b/d and 10.4mn b/d respectively; the 'Central' scenario gives 6.1mn b/d and 8.3mn b/d; and the 'Delayed' case gives 4mn b/d and 5.3mn b/d (1). Some Iraqi oil experts believe that due to infrastructure problems with transfer pipelines, storage tanks, electricity and water, the IEA's central scenario is likely to be the most accurate forecast

Additionally, since 2007 the Kurdish Regional Government (KRG) has signed 49 oil and gas Production Sharing Contracts (PSCs) with IOCs, which are expected to raise production from 0.3mm b/d today to 2mn b/d by 2020, according to KRG Oil Minister Ashti Hawrami (2). If we assume that KRG oil production will reach an average of 1.4mn b/d in 2020 (since there are no other sources to confirm Dr Hawrawi's statement), that oil production by the IOCs for the Ministry of Oil will be around 6.1mn b/d and that 0.5mn b/d will continue to be produced by the Iraqi national oil companies, total Iraqi oil production in 2020 will be about 8.0mn b/d.

## Iraq's NOCs – Projected 2020 Production

In 2008-10, Iraq's national oil companies – the South Oil Company (SOC), North Oil Company (NOC), Misan Oil Company (MOC) and the new Iraq National Oil Company (INOC) – produced 100% of average Iraqi oil production of 2.4mn b/d.

However, four of the giant oil producing fields, which were operated by the Iraqi national oil companies in 2008-10 and are shown in Annex 1 of the February 2007 draft of the Iraqi oil and gas law as continuing to be operated by SOC, NOC and MOC, were actually contracted to IOCs in the first bid round in 2009.

They include Rumaila North with reserves of 10.3bn barrels and Rumaila South with reserves of 7.5bn barrels, both contracted to BP/CNPC; Zubair with 4bn barrels of reserves, contracted to Eni/Occidental/Kogas; and West Qurna Phase-1 with 8.5bn barrels, contracted to ExxonMobil/Shell. Between them, these fields are responsible for about two thirds of the 2.4mn b/d of oil produced in 2008-10 (3). Furthermore five of the largest oil fields contracted to IOCs in the second bid round are listed in Annex 1 of the draft oil and gas law and were supposed to be developed by INOC. Three of the five are super giant fields by international standards: Majnoun with 12.6bn barrels contracted to Shell/Petronas; West Qurna/2, with 13bn barrels contracted to Lukoil/Statoil; and Halfaya with 4.1bn barrels contracted to CNPC/Petronas/Total.

This ensures that some 7.5mn b/d out of the 8.0mn b/d total forecast Iraqi production in 2020 will be produced by the IOCs under the first and second bid round agreements and the KRG's 49 PSCs. This will result in the new INOC, comprising the existing four Iraqi national oil companies, producing around 500,000 b/d or about 6% of the total, down from the 2.4mn b/d which represented 100% of Iraqi oil production in 2008-10. The above figure excludes the Kirkuk oil field which was offered to the IOCs in the first bid round unsuccessfully due to the disagreement between the federal Oil Ministry and the KRG, which scared the IOCs away. Such an amount will be so negligible that it may make it economically advisable to halt all INOC production activities in the future.It is evident that the first and second bid rounds will not rebuild and develop an independent Iraqi national oil and gas industry. On the contrary, they will hand real control of both industries to the IOCs for the first time since nationalization in the 1970s

The creation of 'field operating divisions' (FODs) in the first bid round gave a major role to the IOCs in the decision-making, control, management and operation of all the giant oil fields. In the second bid round, the IOCs will fully operate the fields on offer, including exploration, development and production. The question this raises is whether there will be any real Iraqi national oil industries left or whether INOC's future role will be reduced to no more than a holding company for the giant oil fields which are to be fully managed by the IOCs, with INOC's management restricted to distant and marginal fields.

## Need To Consider Iraq’s Priorities

It is time for the federal Ministry of Oil to stop and consider Iraq’s priorities. The Ministry has set both short and long-term targets for production capacity. However, it is clear that this is not part of a well-structured policy that defines where the sector is heading or how it should be run.Output targets are not a policy in themselves,nor are successive bidding rounds, unless they form part of a well-considered plan that ties all the elements together.

The Oil Ministry’s strategy for the medium and long term should focus on building a strong upstream and downstream national oil and gas industry. Plans to increase oil and gas production capacity should be part of this strategy and should not become the only priority.

Many oil producing countries went through a similar transformation as they re-opened their doors to international oil companies. Those that succeeded had strong, modern laws which gave priority to national interests and laid down regulations that clearly defined the roles and responsibilities of state companies and foreign partners. Iraq is clearly not doing this.

The Ministry would have done much better to adopt a more gradual approach prioritizing the rehabilitation of the existing oil producing fields and concentrating on work which is within the capabilities of the national companies, utilizing foreign oil service companies such as Halliburton and Weatherford where required. This would have provided an opportunity to develop Iraq’s capacity at the same time.

Instead what we see today after more than 30 years of wars, sanctions, occupation and political instability is that in the first and second bid rounds the Ministry has signed 20-25 year contracts with the IOCs for fields containing 90bn barrels, or around two thirds of Iraq’s proven reserves. No other oil producing country has ever tried to develop its oil and gas industries in such a hasty and ill-considered way.

## Impact On Prices, OPEC

A second important concern relates to Iraq’s future place in the Organization of Petroleum Exporting Countries (OPEC)

Iraq is a member of OPEC, but in 2008-10 it exported only 1.9mn b/d. If we assume that the Iraqi export oil quota will be allowed to increase to 3.2mn b/d, which was the level accepted by OPEC in 1979 and again in 1990 (out of the 3.9mn b/d Iraq was producing), what will become of the additional 4.3mn b/d which Iraq will have as a surplus from its 8.0mn b/d of production and 7.5mn b/d of exports in 2020? Such an increase in exports would pose two major challenges for OPEC. One relates to the organization's ability to maintain supply at a level that ensures that oil prices remain within a range that guarantees adequate revenues for its member countries. The other concerns the unity of the organization as members compete for higher production quotas.

OPEC's medium-to-long-term outlook forecasts world oil demand will rise from 87.0mn b/d in 2010 to 91.8mn b/d in 2015 and 96.9mn b/d in 2020 (4). Such expectations raise the question whether, if Iraq remains a member of OPEC, the other OPEC members will accept that Iraq should raise its export levels to meet virtually all the projected increase in world oil demand. And if not, whether Iraq will stay in OPEC or will abandon it and increase its oil exports independently, which would, very likely, lead to an oil price collapse. In such a scenario, Iraq would be little more than a "global oil and gas pump" used by the US and Western Europe to service global markets and enrich local elites. Any Iraqi national oil and gas strategies should therefore also aim to strengthen OPEC and the Organization of Gas Exporting Countries (OGEC) rather than weakening these vital institutions.

**Conclusions**

1. This analysis is not intended to accuse the Oil Ministry in Baghdad of being part of an international conspiracy to hand over Iraqi oil and gas to the IOCs. On the contrary, it is important to support positive Ministry policies including its opposition to the KRG's drive to sign PSCs and the campaign to centralize strategic planning for the development of oil and gas resources so that decisions are made and carried out at the federal ministry level.

2. The existing policies of both the federal government and the KRG will lead to the control of all of Iraq's oil and gas production being placed in the hands of the IOCs.

3. In addition the KRG's policies will lead to the destruction of Iraqi's oil and gas industries and the privatization of the national industries.

4. The policies of both the federal government and the KRG will leave INOC with no real production role.

5. Moreover the TSC contracts signed with the IOCs will give control of 94% of Iraq's producing oil fields to the foreign companies for 20-25 years through their control of the "field operating divisions." In addition, all indications are that this will entail the downsizing, if not the

disappearance altogether, of SOC, NOC and MOC, and the same future will face INOC.

6. A better option back in 2009 would have been for the Ministry of Oil to revise the terms of the TSCs for some of the fields in the first round with the IOCs in order to reach the required production levels, in accordance with competitive agreements and for a maximum period of two to five years, renewable for fields which produce results more swiftly and easily without causing any economic damage.

7. However, as things stand today, and in order to reduce the damage which has already been done, the Oil Ministry should:

- Terminate TSCs with all the IOCs which do not follow the federal ministry's policies, such as ExxonMobil (West Qurna 1), Total (Halfaya) and Gazprom (Badra), which have signed contracts with the KRG.
- They should also amend and renegotiate the concluded contracts, especially those for bid rounds one and two.
- There is no convincing reason to hold further bid rounds, especially for oil-prone exploration blocks, for a considerable period of time, or at least until 2020

8. The Oil Ministry's strategy for the medium and long term should focus on building a strong upstream and downstream national oil and gas industry. Plans to increase oil and gas production capacity should be part of this strategy and should not become the only priority.
These types of policies will serve the interests only of the US and western European governments, who are solely interested in seeing Iraq functioning as an "oil state" working closely with foreign energy firms to boost global oil supplies.

9. Any Iraqi national oil and gas strategies should also aim to strengthen OPEC and the newly formed OGEC and should not lead to the weakening of such vital institutions.

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