

Kurdistan Regional Government: petro-politics in the post-2003 era

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Abstract:

Competition over natural resources between Baghdad and the Kurdistan Regional Government (KRG), which controls the Kurdistan Region in northern Iraq, has been a central component in the complicated relations between Arabs and Kurds in post-2003 Iraq. Particularly significant in this context has been the KRG's oil politics with regard to control over, and exploitation of, oil reserves in the Kurdistan Region. Such oil politics has been manifested in independent hydrocarbon legislation and the signing of independent extraction and production contracts with transnational energy corporations. This paper seeks to explain the main motivations of KRG's behavior in petro-politics in post-2003 era. It argues that the main motivations of KRG's behavior in petro-politics lies in the KRG's aspiration to legitimize its precarious existence but geopolitical obstacles and fall of oil revenues has hit aspirations to use oil for going through independence.

Key word: Petro-politics, Geopolitics, Kurdistan Iraq, Oil revenues

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Introduction

The development of major oil and gas reserves in the autonomous Kurdish Region of Iraq (KRI) is a recent phenomenon, dating back no earlier than 2005. Despite promising geological signs, political conditions largely prevented exploration and production until after the US -led removal of the Saddam Hussein regime. The story since then has attracted major media interest, perhaps even more than has been devoted to the larger fields in the south of Iraq, and there has been a wide range of publications on the politics of the region, as well as others on its culture and religion. Outside specialist industry publications, however, there has been less analytical work focusing on the region's oil and gas sector.

Study of the Kurdish oil story is important for various reasons. It represents the rare case, in recent history, of the discovery of a large new onshore conventional petroleum province. It illustrates the development of such a province under conditions of moderate technical challenge but major and volatile political uncertainty. Considered as a unit, the KRI could soon emerge as a significant oil producer on a par with, or even exceeding, Oman, Colombia or Azerbaijan and ,like them ,effectively outside OPEC.

The KRG's formulation of its own oil policy and laws, often in opposition to the federal government in Baghdad, presents an important case of sub - national authority over the natural resource sector , which may be relevant to other oil producing countries or territories exploring federal structures, for instance Yemen and Libya.

Most observers have focused on the implications of the KRG's petropolitics for either Iraq's territorial integrity or its oil-export capacity. Little, if any, attempt has been made to trace and explain the sources of the KRG's policies. Most accounts have followed the assumption that the KRG's (and Baghdad's) actions have been driven by a desire to gain access to a strategic source of revenues, either for the purpose of facilitating Kurdish autonomy or for personal greed. This perception has been shaped, directly or indirectly, by the political-economy-inspired greed thesis, which views natural resources and the hunger for revenues as a central, if not primary, cause of both interstate conflicts and civil wars. This paper seeks to explain KRG's motivations of KRG's behavior in petro-politics in post-2003 era. It shows that the main motivations of KRG's behavior in petro-politics lies in the KRG's aspiration to legitimize

its precarious existence but geopolitical obstacles and fall of oil revenues has hit aspirations to use oil for going through independence.

Theoretical argument

Realism is often seen historically as the dominant IR theory and this is certainly correct in terms of the study of security, conflict and war. This is reflected in the fact that International Security, as noted above the flagship IR journal, is dominated by realist and neo-realist authors. Classical realism includes the key early and mid-twentieth century scholars who developed a notion of the 'tragic' nature of international politics, arguing that there was a

radical difference between politics within a state and politics between states since inter-state politics lacks any overarching sovereign arbiter who is able authoritatively to repress the inexorable drive for power and the natural human tendency towards aggression (for key texts, see Carr 1946; Morgenthau 1960; Neibuhr 1960)

The logical consequence is that the international realm is characterized by anarchy, distrust and the ever-present prospect of war. Much of realism's initial momentum and subsequent popularity came from its critique of inter-war liberalism (or so-called idealism) and the optimism expressed by many liberals that international relations could be transformed through developing international law and international institutions such as the League of Nations (see especially Carr 1946). In 1979, Kenneth Waltz provided a more rigorous and parsimonious model of realism, known as neo-realism, whose main assumptions were that the international system is anarchical, that the structure of the system is determined by the distribution of power between states (the balance of power), and that the internal nature of the state (i.e. whether it is democratic or authoritarian) has no material structural impact on international relations (Waltz, 1979).

Realism's theoretical principles draw from deeper historical traditions of thinking about international politics and these help to explain the theory's popularity and theoretical dominance. This includes the tradition of Realpolitik developed from Machiavelli onwards, which preferences the interests of the sovereign, and where the key goal of statesmen seeking to preserve international stability is to contain the ineluctable drive for power by states, and the conflicts this inevitably produces, through the preservation of a durable balance of power.

As Kissinger has described, this was the foundation of the European order in the 18th and 19th century (Kissinger 1964). It was an approach to international politics he also sought to resurrect to develop his own foreign policy principles when he was a highly influential US Secretary of State in the 1970s (Kissinger 1979, 1982). Another tradition which realism draws from is that of geopolitics which includes the work of people like Mahan (1890), Mackinder (1919), Haushofer, (2002) Harold and Margaret Spout (1971), and Lipschutz (1989). This tradition draws from geography as well as IR and strategic studies and highlights the spatial dimensions of state power and identifies a continued international struggle for influence and control of critical geographical and geopolitical spaces, whether that be the Eurasian 'heartland' favored by Mackinder or the international sea lanes promoted by Mahan.

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- Access to and control of natural resources, of which energy is the most critical, is a key ingredient of national power and national interest
- Energy resources are becoming scarcer and more insecure (drawing often from the 'peak oil' thesis and the 'resource curse' and 'resource wars' literature)
- States will increasingly compete for access and control over these resources

Gaining and demonstrating its control over oil reserves in the Kurdistan Region and the territories claimed by the KRG has been viewed as essential in consolidating Kurdish sovereignty over the region and exhibiting this sovereignty to the international community, especially those objecting to Kurdish sovereignty.

Issues between the Kurdistan Regional Government and Baghdad

The Kurdistan Regional Government (KRG), the official ruling body of the semiautonomous region in northern Iraq that is predominantly Kurdish, has been involved in disputes with national authorities related to sovereignty. The plan by Iraq's North Oil Company (NOC) to boost production at the Kirkuk field in northern Iraq at the edge of the KRG region has been met with objections by the KRG, which insists that development plans at this field require KRG cooperation and approval.

More generally, the Iraqi Ministry of Oil insists that all hydrocarbon contracts must be signed with the national government, and that all oil produced in the KRG region be marketed and shipped via State Oil Marketing Organization (SOMO), Iraq's oil exporting arm. However, the KRG passed its own hydrocarbons law in 2007 in the absence of a national Iraqi law governing investment in hydrocarbons. In late 2011, the KRG challenged the authority of the national government when it signed oil production-sharing agreements with ExxonMobil to develop blocks in northern Iraq, some of which are in disputed border areas. The KRG has since signed additional contracts with major oil producers such as Chevron, Gazprom, and Total. ExxonMobil withdrew from some of its projects in Iraq, notably the Common Seawater Supply Project, and the company had been asked by the Iraqi government to choose between its involvement in the West Qurna 1 oilfield and its projects in the KRG. Turkish Petroleum Corporation (TPAO) had also been asked to withdraw from its involvement in the Block 9 concession that was awarded during the fourth bidding round because of disputes regarding Turkey's involvement in KRG energy projects.

Past agreements to export oil independently and via Iraqi state-owned infrastructure from Iraqi Kurdistan have fallen apart because of payment disagreements, security problems, and delays building infrastructure required to transporting the amounts of oil promised. Oil exports directly from the KRG have been another contentious issue. The KRG has been exporting crude oil and condensate to Turkey and Iran by truck. In May 2014, the KRG started exporting crude oil via a newly built independent pipeline to Turkey's Ceyhan port.

Iraq Northern production oil production

Oil production in northern Iraq is a contentious topic because of an ongoing dispute between the central Iraqi government in Baghdad and the KRG over the vast amount of oil resources in the Kirkuk structure. The tension and confusion over northern production has escalated since the ISIL offensive in 2014. Before 2014, Iraq (Baghdad) produced most of the oil in the north, mainly at the Kirkuk field (Avana and Baba Domes) and Bai Hassan field, along with other smaller fields. However, after the closure of the IT pipeline in March 2014 and the Baiji refinery in June 2014, northern production lacked its traditional commercial outlets. As a result, the KRG took over operations at the Avana Dome, a part of the Kirkuk field, and Bai Hassan in July 2014 and started exporting the oil through its newly built independent pipeline to Ceyhan, Turkey (Table 1). During this time, Baghdad's NOC continued to operate some of the northern fields, although the production was exported via KRG's pipeline and marketed by the KRG. (Iraq Oil Report, March 17, 2016).

The KRG began transferring some of the crude oil at Turkey's Ceyhan terminal to SOMO in late 2014 in accordance with a deal made between Baghdad and the KRG in December 2014. The two sides agreed that: (1) the KRG give 250,000 b/d of the crude oil produced in its territory to SOMO at the Ceyhan terminal to market the crude, (2) Iraq (Baghdad) export 300,000 b/d of Kirkuk crude through KRG's pipeline to Ceyhan, and (3) Iraq (Baghdad) resume federal payments to the KRG that will amount to a 17% share of Iraq's federal budget and pay KRG's Peshmerga military forces \$1 billion. The deal was intended to allow SOMO to reclaim marketing control over much of Iraq's northern crude exports. (Iraq Oil Report, March 17, 2016).

The deal has since collapsed. KRG oil allotments to SOMO decreased substantially in June 2015 and the last one was given in August 2015. The KRG started to directly sell all northern oil because it was receiving much less than the 17% of the overall federal budget from Baghdad. In response, in March 2016, the federal NOC stopped pumping oil into KRG's pipeline, upon guidance from Baghdad, in an attempt to leverage negotiations on northern oil revenue sharing with the KRG. The NOC-operated fields were producing between 150,000 and 200,000 b/d, of which now most is being reinjected into the oil wells to maintain natural gas production for local power generation (Oil & Gas Journal, January 1, 2016).

Iraq and KRG Crude Oil Exports

In 2015, India was the largest importer of Iraqi crude oil, importing slightly more than China. About 85% of Iraq's crude oil exports came from the country's southern export terminals along the Persian Gulf in 2015, which export Iraq's Basra light and heavy crude grades.

Total Iraqi crude oil exports averaged 3.3 million b/d in 2015, 0.7 million b/d higher than the previous year, based on Lloyd's List Intelligence (APEX tanker data) and data from the Iraqi Ministry of Oil . The expansion of onshore pumping and storage infrastructure in the south, improvements in crude quality as Basra Light and Basra Heavy were marketed separately starting in mid-2015, and an increase to the KRG's pipeline capacity in the north all contributed to production growth in Iraq. In 2015, about 85% of Iraq's exports were shipped from its southern export terminals in the Persian Gulf, which exports both the Basra light and heavy crude oil grades. Asia (led by India, China, and South Korea) is the main regional destination for Iraq's crude oil, importing more than half of the total exports in 2015. India imported slightly more crude oil from Iraq than China, making India the largest importer of Iraqi crude oil in 2015. Outside of Asia, the United States is the largest importer of Iraq's crude oil, although the volume has fallen over the past decade. The United States imported 229,000 b/d of crude from Iraq in 2015, more than 70% lower than the volume received at its peak in 2001. The growth in U.S. oil production has resulted in a sizable decline in U.S. imports. (Oil & Gas Journal, January 1, 2016).

The crude export estimates in Figures 3 and 4 include only seaborne trade crude oil. The estimates exclude crude oil transported by truck and volumes exported inland to Turkey via an onshore pipeline from the Ceyhan terminal to Turkey's Kirikkale refinery, near Ankara. The Ceyhan to Kirikkale pipeline has a capacity of 135,000 b/d, although transported volumes often fall below that amount. (International Energy Agency, 2013, 8)

Table 1. Status of main pipelines used to export crude oil produced in Iraq (including KRG area)

name/ description	pipeline direction	location	nameplate capacity (000' b/d)	status	notes
Turkey section of Iraq to Turkey (IT) pipeline	Fishkhabur (Iraqi-Turkey border) to Ceyhan port (Turkey)	southern Turkey	1,500	operating	The pipeline transports oil produced in northern Iraq to the Ceyhan port. It is connected to KRG's main pipeline. The pipeline is comprised of two parallel lines.
KRG's independent pipeline connecting to Turkey pipeline	Khurmala Dome to Fishkhabur	northern Iraq	700	operating	It carries crude produced at the Khurmala Dome and also crude sent there from nearby fields, including Taq Taq. The KRG is working to increase the pipeline capacity.
DNO-KRG connection to Turkey pipeline	Tawke field to Fishkhabur	northern Iraq	200	operating	The pipeline transports oil produced at the Tawke field, operated by DNO, to Fishkhabur. From there it connects to the Turkey pipeline for export at the Ceyhan port. DNO and its partners are expanding the pipeline's capacity.
Iraq (Baghdad) section of Iraq to Turkey (IT) pipeline	Kirkuk to Fishkhabur	northern Iraq	600	not operating	The pipeline was the target of militant attacks and stopped operating in March 2014. The pipeline's effective capacity was significantly lower than its nameplate capacity prior to its closure. Crude exports from the pipeline averaged 260,000 b/d in 2013.
Kirkuk-Banias/Tripoli Pipeline	Kirkuk to Banias (Syria) and to Tripoli (Lebanon)	northern Iraq	700	not operating	One section of the pipeline links to Syria, and a branch goes to Lebanon. The pipeline was closed in the 1980s to 2000. It was closed again in 2003 after it was damaged.
Strategic Pipeline	Kirkuk to Persian Gulf	north to south (Iraq)	800	not operating	This is a reversible pipeline meant to transport northern Kirkuk crude to the southern Basra Port and vice versa. The pipeline section from Basra to Karbala is operating and sending crude to Baghdad refineries.
Iraq Pipeline to Saudi Arabia (IPSA)	southern Iraq to port of Mu'ajjiz in Saudi Arabia	southern Iraq & Saudi Arabia	1,650	Iraq portion is not operating	The portion that runs through Saudi Arabia was converted to transport natural gas to power plants (see Saudi Arabia CAB).

Sources: U.S. Energy Information Administration, Arab Oil & Gas Directory, DNO, Genel Energy, BOTAS (Petroleum Pipeline Corporation)

Geopolitical obstacles to use oil for independence

1-Tensions over oil between KRG and Baghdad

The tensions between Baghdad and the Kurds over oil surfaced at the beginning of the reconstruction process after the overthrow of the Baath regime. The first battleground between Baghdad and the Kurdish leadership was the constitution. Under Kurdish pressure, it included Article 112, which stated that "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...."(Constitution of Iraq) The term present remained intentionally nebulous, serving the KRG's future claims to oil reserves in its region. Hence, the Kurds were successful in "creating a constitutional framework for Iraq where the main question was not what control regions should have over oil, but rather what role was left for the national government." (Kane, 2010: 6).

The second stage of contestation over oil was in the Kurdistan Region itself, in the form of the KRG's unilateral regional hydrocarbon legislation. The Kurdish representatives in Baghdad did initially participate in the Maliki government's efforts to formulate a federal hydrocarbon law. Yet, this cooperation encountered constant disagreements. One was over the KRG's support of the use of Production Sharing Agreements (PSA). Most other members of the coalition objected to this, viewing such agreements as a form of neocolonialism. Another issue revolved around the right to extract oil in the disputed territories in Kirkuk.

These disagreements eventually led the KRG to withdraw from negotiations with Baghdad. In June 2007, the Kurdistan Parliament passed a regional Petroleum Law, (Petroleum Law of the Kurdistan Region, June 29, 2007) ratified as a Hydrocarbon Law in May 2009, essentially declaring that the KRG would now contract independently with international oil companies through PSAs. Shortly after signing the draft legislation, the KRG declared it was capable of exporting crude oil in commercial quantities. The next step was to sign PSAs with several international companies. Here it should be noted that the KRG had already signed such contracts prior to the negotiations with Baghdad. One was with the Turkish Genel Enerji (joined later by Swiss Addax) in 2002. Nevertheless, the post-2003 government in Baghdad consented to this

agreement retrospectively. In contrast, the contracts that followed were signed against Baghdad's will. Nevertheless, most of the corporations that entered PSAs with the KRG were small or middle-sized, as most major oil companies feared alienating Baghdad, regardless of the stagnation in the political process (Kelly, 2010: 748-749).

Initially, the KRG expressed its commitment to sharing its oil income with the central government. But six months after the Hydrocarbon Bill was passed, the president of the region, Masud Barzani, threatened during a visit to the European Parliament that the KRG would keep for itself revenues from the extracted oil because "they [Baghdad] often use it [oil revenue] against us [the Kurds]." (Reuters, November 10, 2009).

This threat has not been fully implemented, but it indicates the KRG's perception of its rights over oil extracted from the region. In October 2011, the KRG had a significant achievement in the form of a PSA with ExxonMobil. This contract was even more controversial than previous ones, as two of the six blocks given to Exxon were actually located in a disputed part of the Kirkuk governorate (ICG, April, 2012: 2).

2- Objections of regional players

This unilateralism entailed immediate hostility and suspicion from Ankara. In Iraq, the KRG's "insistence on a decentralized oil regulation system... has helped awaken the sleeping giant of Iraqi nationalism." (Khalil, Brookings Institution, 2009).

Ankara was suspicious toward the KRG's actions. Iran and Syria as well feared Kurdish actions on the same grounds. Yet their objections were not as acute as Turkey's, from the KRG's perspective, mainly because Turkey is the Kurdistan Region's only land gateway for Kurdish oil to potential markets in Europe. Immediately after the KRG drafted its petroleum law, Turkey's energy and natural-resources minister, Hilmi Güler, traveled to Baghdad and met with Sahrstani. There he ratified the signing of the cooperation agreement between the two countries, notably a proposed pipeline to carry oil from Iraq to Western Europe through Turkey (Traihi , August 8, 2007).

In coordination with Iran and Syria, Turkey also made arrangements to "prevent the KRG from circumventing the central authority's embargo" (Dargin, June 2009).

The United States followed a similar line. In response to Baghdad's uproar following the signing of a PSA between the KRG and Texas-based Hunt Oil, one official in the U.S. embassy in Baghdad stated, "We think that these contracts have needlessly elevated tensions between the KRG and the Iraqi government," adding that companies "could incur significant political and legal risk by signing contracts with any party before the national law is passed" (Agence France Presse, September 27, 2007).

The KRG responses to the challenges reveal that its leadership was aware of the implications of its actions. The KRG's natural-resources minister, Ashti Hawrami, justified this move by stating, "We do not want to be hobbled by the political paralysis in Baghdad." He also invoked Articles 112 and 115 of the Iraqi constitution, arguing that they allow regional governments in oil-producing governorates to "administer and supervise the extraction process" and meant that "local oilfield managers are answerable to the local authorities." In its dialogue with Ankara, on the other hand, the Kurdish leadership tried to underline the potential financial and political benefits that its actions have carried for Turkey.

Prior to the passing of the law in the regional parliament, the KRG had already made efforts to showcase these benefits. In March 2007, for example, Hawrami affirmed in an interview to a Turkish reporter, "It is in Turkey's interest to be in direct contact with us. It is a 'first come, first served' situation. There are 20-25 billion barrels of oil reserves in Kurdistan. It is more than we need." He then added, "It is in Turkey's interest as well to establish relations with us." (Çandar, March 17, 2007). The urgency with which the Kurdish leaders approached Ankara is perhaps the best indication of the Kurdish leadership's sense of alarm.

This sense of alarm notwithstanding, the KRG nevertheless announced the Exxon deal in November 2011. Baghdad responded even more harshly to these steps. It began blacklisting companies with even indirect investment in regional oil initiatives, thus pushing further the limited embargo it set on unilateral Kurdish oil exports. In one instance, a Chinese oil company that had taken over Swiss Addax was blacklisted and barred from obtaining extraction licenses in Iraq and participating in oil and gas projects (Energy Intelligence Finance, November 23, 2011).

In March 2012, Baghdad halted the allocation of money to the region, as part of its post-2003 commitment, albeit for a short period of time. And in reaction to Baghdad's halting of the budget allocation, the

KRG stopped its own oil supply, thus threatening Baghdad's economy. In spite of the rising tensions, the KRG has made continuous efforts to woo other major oil companies, including Royal Dutch Shell. The latter, however, has been very hesitant in making contact with the KRG (Reuters, March 27, 2012).

Motivated by its hunger for energy and desire for regional stability, the AKP government around 2007 began a process of rapprochement toward the KRG. By so doing, it accepted the latter's right to take unilateral actions at both the national and international levels. The increased volume of bilateral trade and Ankara's opening of its first consulate in Erbil, in March 2010, signaled Ankara's new pragmatism. Nonetheless, the Exxon deal actually drove Ankara to step back from its high-profile collaboration with the KRG. At least for 2012, Turkey was still refusing to build a pipeline from the Kurdistan Region through its territory. Even its need for energy and deteriorating relations with the Maliki government did not resolve the AKP government's uneasiness toward Kurdish unilateralism (Energy Compass, November 18, 2011).

Perhaps the most important thing to note, given Baghdad's and Ankara's anxiety amidst Kurdish unilateralism, is the fact that the Kurdistan Region, being landlocked, must depend on Turkish infrastructure to export oil in commercial quantities to markets in Europe. Acting against Baghdad's whims in such a provocative manner, and arousing Turkey's old fears of Kurdish separatism, have been detrimental to the KRG's export of oil from its territory, preventing it from maximizing its capacity.

Kurdish unilateralism, meant to increase Kurdish revenues for whatever purposes, has not yielded the desired results. Even more important, it seems that the Kurdish leadership had actually predicted the consequences of its actions. One may argue that the KRG had actually taken a risk, gambling with Baghdad's willingness to prolong the conflict. However, such an explanation does not fit well with Kurdish conduct so far. First, the Kurdish leadership has proven to be risk-averse on most other fronts. For example, although conditions were ripe and the Kurdish public was eager, the KRG avoided publicly discussing or explicitly using the secession card. Kurdish willingness to cooperate with Turkey on the PKK front is yet another example. Second, even though its policy did not yield the desired outcomes, fierce Iraqi and Turkish reactions

have only emboldened the Kurdish leadership, particularly Oil Minister Hawrami. How can we explain Kurdish unilateralism?

3-International oil companies reluctance:

the KRG has been challenged on a number of fronts both internationally and domestically. In December 2013, the KRG announced the completion of the Kurdish-Turkish pipeline and its commitment to using it to export oil starting that month. However, since then the use of the pipeline for the exportation of Kurdish crude has been at best limited and its sale non-existent. The Iraqi Government's policies have been significant in thwarting the KRG's use of the pipeline. Amongst these policies is Baghdad's threat that it would file lawsuits against any third party that buys the crude exported through the Kurdish pipeline. This particular threat has been particularly effective, as most international oil companies (IOCs) prefer to maintain their goodwill when dealing with Iraq as a number of the largest oil and infrastructure projects are in Iraq. Although the threat has been used before against firms like Exxon-Mobil, in this particular occasion its success is based on two differences. Firstly, Exxon-Mobil has greater leverage when dealing with Iraq due to their capabilities in helping Baghdad. Secondly, other IOCs and Turkey do not want to get involved in a situation where they are perceived to be threatening the sovereignty of Iraq. Thus, in this way Iraq has placed significant limits on the international clout of the KRG.

However, Baghdad has also been significantly successful in creating challenges to the KRG's interests through the creation of domestic pressures. The freeze of the KRG's portion of the annual Iraqi budget is the most significant example of this. On a number of occasions, the KRG and its key leaders have voiced their voluntary membership to the Iraqi Government. They have argued that they are in a contract with Iraq simply because it suits the national security interests of the Kurdish people and once it stops doing that, they are willing to declare their independence. However, in response to the exportation of around a million barrels of oil to Turkey through the aforementioned pipeline, Iraq's Prime Minister Nouri al-Maliki cut off the portion of the Iraqi Budget due to the KRG. KRG President Masoud Barzani denounced the cuts and called it "a declaration of war against the people of Kurdistan." However, in the streets of Sulaymaniyah, the general consensus was that the Iraqi Government was not solely to blame and that the KRG was just

as guilty. Employee protests broke out outside water and electricity companies, lecturers and teachers boycotted schools and universities as they did not receive their payments on time. Such boycotts were an indication of their grievances with the KRG for not having reserves for an occasion such as this even though they claim they can declare independence at any point. Essentially the saga indicated that although corruption was no stranger to Kurdish politics and even if to an extent the KRG was aspiring to independence, as it stands, it simply is not feasible.

With around 90% of Iraq's revenue coming from the sale of natural resources and 17% of the Iraqi budget going to the KRG less costs, the KRG is significantly reliant on the sale of Iraq's oil. Of even more significance is that 75% of the KRG's annual portion of the Iraqi Budget goes towards paying the salaries of public servants. If bashuri Kurdistan were to declare independence at this point, they would not have the means to sustain the population, or maintain economic growth and security. Thus as it stands, it is far better for the KRG to return to the basic tenants of diplomacy. Diplomacy being defined not in terms of the KRG's relative gains in relation to Iraq but rather the maximum amount that the KRG can gain even if it means reaching agreements with the Iraqi government on the use of the crude pipeline.

Thus negotiations with the Iraqi Government on the use of the pipeline seem inevitable. While the KRG had already offered to export 100,000 barrels per day (bpd) through the pipeline in cooperation with the Iraqi National Company for marketing oil, the State Organization Marketing of Oil (SOMO). These developments have stalled due to attacks on the Kurdish pipelines. Agreements on both the Iraqi Budget and the pipeline have now been stalled till after the Iraqi Elections. Barzani argues that they will start using the pipelines with or without Iraq's consent. However, it is unclear still whether this was just political rhetoric prior to the elections or the legitimate policy of the KRG.

Oil revenue drop and K.R.G. Financial Crisis

Since the ratification of the new Iraqi constitution in 2005, the K.R.G. has received from Baghdad around 17 percent of Iraq's national budget annually after certain sovereign and governance expenses were deducted. That amounted to around \$13 billion per year in 2012 and 2013 when oil prices were at their peak. The injection of such hefty sums adds to at least \$37 billion (Kurdo, March 7, 2016).

In private foreign and domestic investment generated rapid economic growth and unprecedented signs of prosperity among Iraqi Kurdistan's approximately five million people. But this started to change when in November 2013 K.R.G. Prime Minister Nechirvan Barzani signed a "strategic" deal with neighboring Turkey to export Kurdish oil and gas to that country for the next 50 years (Anadolu Agency, June 5, 2014).

Although the deal was meant to cement Iraqi Kurdistan's position as a major energy exporter and assist its economic independence, the move backfired as Iraqi Prime Minister Nouri al-Maliki retaliated by suspending the K.R.G.'s budget share in February 2014. Pressed hard for cash, the K.R.G. sought to step up its independent oil sales, but Baghdad's threats to sue buyers meant there was little willingness to purchase Iraqi Kurdish oil internationally. The war with ISIS, however, eased the pressures on the K.R.G.'s efforts to export its oil directly as it was in urgent need of cash to both finance a costly war against the jihadist organization and also provide for its population in addition to nearly two million Syrian refugees and internally displaced Iraqis who had relocated to Kurdistan. But fluctuating levels of oil production coupled with a dramatic drop in oil prices starting in Summer 2014 meant that the K.R.G.'s total revenues from oil sales did not even reach \$6 billion per year in either 2014 or 2015 (Osgood, et al, 4, 2016).

By the end of 2015, the K.R.G. was between three and five months behind in paying its nearly 1.4 million employees. Faced with grim economic and financial prospects, the K.R.G. has now slashed the salaries of its civil servants, ranging from 10 to 75 percent depending on rank and salary level. The salary cuts, however, have not included the security forces in an apparent attempt to maintain order and stability. The government has come under heavy criticism for not articulating a clear vision for serious reforms beyond the strict austerity measures it has introduced (Osgood, et al, 4, 2016).

As a result of the economic crisis, much of Iraqi Kurdistan's public sector is now paralyzed as many government institutions, including at times the health and education sectors, have gone on strike. The situation is particularly acute in Sulaimaniyah province and the nearby Garmiyan area where anti-establishment sentiments are stronger. Struggling to pay its dues, the K.R.G. is estimated to now be \$14 to \$20 billion in debt. This includes a \$1 billion loan from Turkey, entitlements owed to

international oil firms and local companies and delayed payments to those on the K.R.G.'s payroll (Sabir, interview January 2016).

The deteriorating economic conditions in Iraqi Kurdistan will likely restrict the K.R.G.'s maneuverability with regard to its declared efforts for independence and render it more susceptible to pressure from the outside world, in particular powerful neighboring countries such as Turkey and Iran. Voices opposing Kurdish independence have been also rising on the international arena, with German and E.U. foreign policy chiefs expressing concern over such attempts (Daily Sabah, February 23, 2016).

Struggling hard to pay people on its payroll and under heavy debt, it is difficult to foresee how the K.R.G. is going to administer an independent country given the risks that will arise as a result of it. None of the neighboring countries of Iraqi Kurdistan have voiced support for Kurdish statehood. Although many might pin their hopes on the region's oil exports, the government's levels of production are far behind declared targets. The K.R.G.'s energy minister stated in 2013 that oil production in the Kurdish region will hit one million barrels per day by 2015, but a recent report by his ministry put production level at the end of last year at around 436,000 barrels per day (Rudaw, June 6, 2013).

The K.R.G.'s oil is largely exported through a pipeline to the Turkish port of Ceyhan on the Mediterranean Sea and the rest is shipped to Iran and Turkey by trucks. Iraqi Kurdish oil is believed to be sold at rates lower than the Iraqi national oil largely due to risks associated with purchasing it. Moreover, given that the pipeline passes through an area in Turkey that witnesses frequent clashes between Turkish forces and the Kurdistan Workers Party (P.K.K.), the K.R.G.'s exports are at the mercy of geopolitical events beyond its control. Oil exports have been currently on hold for several weeks due to an act of sabotage against the pipeline, costing the K.R.G. a loss of around \$200 million in oil revenues. Such occurrences will further undermine the K.R.G.'s ability to meet its budget requirements (Johnson, March 2, 2016).

The major proponent for the push toward statehood is the K.D.P. and its leader Massoud Barzani, who also serves as the president of the K.R.G. despite ongoing objections from rival Kurdish parties about the legitimacy of his tenure. He has called for a referendum to be held, but cautioned that it will not mean immediate independence. While many might find it perplexing that Iraqi Kurds would push for independence

under such exigent circumstances, an important part of the K.D.P.'s calculation is that there is no longer a future for Kurds in an Iraq torn apart by sectarian strife. (Christian Science Monitor, July 11, 2014).

Conclusion

Baghdad depends heavily on the region's oil production to meet its budgetary needs. The Iraqi federal government has therefore pursued all possible political routes to prevent the loss of Kurdistan and its oil. Likewise, the KRG and Baghdad frequently find themselves at loggerheads over an oil agreement in which the KRG is required to export 250,000 barrels per day through the state oil marketing company in exchange for 17% of the federal budget. Each side frequently accuses the other of renegeing on its share of the bargain, stymieing Kurdish oil exports and causing Baghdad to periodically halt budget payments. These disputes compromise the KRG's ability to pay salaries and undermine investors' confidence, impeding the realization of financial and political stability.

Furthermore, as of 2014 over two million barrels of Kurdish oil shipped through the newly constructed Ceyhan pipeline were sitting in storage due to a lack of buyers. Baghdad's threats of legal action against Turkey, the KRG, and any states that purchase Kurdish oil have effectively deterred most would-be-buyers. Any oil that the KRG does sell is sold at a discount to compensate for purchasers' fear of reprisal from the Iraqi government.

Politically, fear of the precedent of an independent Iraqi Kurdistan and reluctance to cross Baghdad will ensure that Ankara consistently stops short of supporting a bid for statehood. Instead, Turkey will use its leverage over the KRG's oil production to ensure that just enough revenue flows to Arbil to maintain a stable buffer zone along the Turkish border while actively discouraging any moves towards independence.

Oil prices hovering below \$30 per barrel exacerbate already stunted revenues, burgeoning oil contract payments, a bloated government payroll, and continued conflict with Baghdad, leaving the KRG in a steadily worsening budget crisis. Growing financial pressure has triggered widespread popular protest and political infighting, leading to the breakdown of the government in October 2015.

As a result, the future of the KRG's quest for independence is far bleaker than it appeared in 2014. While an independence bid remains an

option due to considerable doubts regarding Baghdad's ability to pay the KRG's share of the budget, any moves towards statehood will surely not proceed with the promise and fanfare predicted in 2014. Alternatively, should the Kurds reach an accommodation with Baghdad, one can only expect these geopolitical challenges to continue to undermine the KRG's desire for the economic self-sufficiency necessary to pave the way for independence.

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