

**IRAQ AND THE KURDS:
THE HIGH-STAKES HYDROCARBONS GAMBIT**

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EXECUTIVE SUMMARY AND RECOMMENDATIONS

A simmering conflict over territories and resources in northern Iraq is slowly coming to a boil. In early April 2012, the Kurdistan regional government (KRG) suspended its supply of oil for export through the national Iraqi pipeline, claiming Baghdad had not fully repaid operating costs to producing companies. The federal government responded by threatening to deduct what the oil would have generated in sales from the KRG's annual budget allocation, potentially halving it. This latest flare-up in perennially tense Erbil-Baghdad relations has highlighted the troubling fact that not only have the two sides failed to resolve their differences but also that, by striking out on unilateral courses, they have deepened them to the point that a solution appears more remote than ever. It is late already, but the best way forward is a deal between Baghdad and Erbil, centred on a federal hydrocarbons law and a compromise on disputed territories. International actors – the UN with its technical expertise, the U.S. given its unique responsibility as well as strategic interest in keeping things on an even keel – should launch a new initiative to bring the two back to the table.

Each side has its narrative, based on history, accumulated grievances and strong sense of entitlement. For now, neither is inclined to settle the conflict peacefully through serious, sustained negotiations, as each believes its fortunes are on the rise, and time is on its side. They are wrong: time is running out, as unilateral, mutually harmful moves are pushing the relationship to the breaking point, with the hydrocarbons-driven stakes and attendant emotions so high that conflict looks more promising to them than accommodation and compromise.

The two unwilling partners in an Iraqi enterprise born of colonial machinations – Arabs and Kurds – have spent 90 years in unhappy cohabitation. Kurds have waited for the moment when they will succeed in removing the shackles of an overbearing, at times highly repressive, central state. They know that when Baghdad is weak, they can take steps to bring their dream of statehood closer to reality, but that when the centre is strong it will use its superior resources to push them back into their place – or worse. This is why the Kurds are so alarmed at attempts by Prime Minister

Nouri al-Maliki to amass power at the expense of his rivals and rebuild a strong state, armed with U.S. weaponry, under his unchallenged control.

Ever since arriving in Baghdad on the coattails of the U.S. invasion in 2003, the Kurds understandably have used their new position and the centre's weakness to develop their own region. They seek to reverse a legacy of discrimination and economic neglect but also to create an escape route should relations with Baghdad sour beyond repair. Yet, in many ways, this approach contains elements of a self-fulfilling prophecy: by pressing their advantage, Kurds inevitably aggravate matters, convincing the federal government that they are aiming for secession – and aiming to take with them a good chunk of disputed territory that Kurds claim as historically part of a notional Kurdistan but that also appears to be immensely rich in oil and gas.

Perhaps most worrying to Baghdad, Kurdish leaders have lured international companies to explore and exploit the region's suspected hydrocarbons wealth. Nor have they stopped at the Green Line that divides their region from the rest of Iraq; instead, they have signed contracts for acreage located squarely in disputed territories. The latest (and largest) to agree to play this game was ExxonMobil, which arrived on the scene in October 2011, taking six blocks, two of which, along with a corner of a third, lie across the Green Line. It thus placed itself at the heart of the conflict, potentially accelerating the centrifugal forces that are tearing at the Iraqi fabric. While ExxonMobil may have calculated that by doing so it could help bring Baghdad and Erbil to the table and effect progress on a federal hydrocarbons law, the likelier outcome is that both sides will further entrench their positions, thus increasing the chances of violent conflict. From Baghdad's perspective, the Kurds are making mincemeat of any attempt to have a unified federal oil strategy; increasingly, it views them as untrustworthy partners in government who are seeking to break up the country.

But the Kurds face a problem. While they pursue an independent oil policy and have taken important steps toward that end by drafting their own oil law in 2007 and signing

over 40 contracts with foreign oil companies without Baghdad's input or approval, they lack the means to export their oil without Baghdad's help and therefore its permission. To date, the federal government has used its control over the national pipeline network, as well as its hold on the treasury and budget, to rein in the Kurds' ambitions.

Hemmed in by Baghdad and anxious to become economically self-sufficient, Erbil is turning its eyes to another potential outlet for its oil: Turkey. Masoud Barzani, the Kurdish region's president, reportedly told foreign visitors to his mountain redoubt that if Maliki remains in power beyond the 2014 parliamentary elections, the Kurds would go their own way. Not coincidentally, 2014 is when the Kurdish region expects to complete construction of its own strategic oil pipeline, one that skirts (federal government) Iraqi territory before reaching the border with Turkey. For Kurdish leaders, economic dependency on a democratic neighbour with an attractive window on the West is far preferable to a continued chokehold by a regime displaying authoritarian tendencies – all of which raises the question of what Ankara would do if the Kurds ask it to take their oil without Baghdad's approval.

Turkey's main objective in Iraq has been to keep it unified. To this end, it has undertaken economic steps since 2007 that would bind the country's various parts into an economic union, hoping that politics, especially the relationship between Baghdad and Erbil, would follow suit. It also has encouraged both sides to agree to a federal hydrocarbons law, the added benefit of such legislation being that energy-poor Turkey could import oil and gas from Iraq's immense southern fields, as well as from the Kurdish region, coming closer to fulfilling its aspiration of becoming a major transit corridor for regional hydrocarbons. The Kurds hope, however, that Turkey's thirst for oil and gas will align with their own thirst for statehood.

Ankara is unlikely to shift course, frustration with its neighbour's failure to agree on oil legislation and its eagerness to purchase oil and gas from the Kurdish region notwithstanding. Ideally, it would import Kurdish products without jeopardising its relationship with Baghdad, though that seems beyond reach.

The Kurds have not lost hope. As they see it, a regional crisis – such as war between Iran and the U.S. or the break-up of neighbouring Syria – might constitute a game-changing occurrence, persuading Ankara to risk its relations with Baghdad in exchange for energy security and a stable (Kurdish) buffer against an unpredictable, possibly chaotic, suspiciously pro-Iranian and increasingly authoritarian Arab Iraq. But such scenarios might not unfold and, for a multitude of reasons, one must hope they do not. The answer to the current impasse, in other words, is not to wish for a cataclysmic event with potentially devastating repercussions for all. It is not to bank on the central Iraqi gov-

ernment surrendering resource-rich territories it deems its own and has the means to hold on to by force. And it is not to gamble on a radical move by Turkey toward a separate deal with the KRG when Ankara has its own, deep-seated fears concerning a potentially newly invigorated Kurdish population on its own territory.

For Baghdad and Erbil, reaching a deal will be very difficult. But the alternatives surely would be far worse.

RECOMMENDATIONS

To the Government of Iraq and the Kurdistan Regional Government (KRG):

1. Reduce tensions and improve the environment for resolving differences by:
 - a) re-committing publicly to a negotiated solution to the status of disputed internal boundaries and the conflict over oil and gas contracts;
 - b) agreeing to take no further unilateral steps in disputed territories, such as issuing new oil and gas contracts; and
 - c) refraining from inflammatory rhetoric concerning mutual relations, the status of disputed internal boundaries and the issuance of oil and gas contracts in disputed territories, especially (in the Kurds' case) in the run-up to provincial elections in the Kurdish region on 27 September 2012.
2. Work, along with other Iraqi parties and alliances, toward the success of a planned but delayed national conference regarding a practicable power-sharing arrangement in Baghdad.
3. Resume negotiations promptly on the status of disputed internal boundaries and a federal hydrocarbons law and agree, as part of such negotiations, to open channels of communication and coordinated action, including:
 - a) a channel for frequent communication between Prime Minister Nouri al-Maliki and KRG President Masoud Barzani or their designated senior representatives; and
 - b) the appointment of a non-voting official from each side to, respectively, the Iraqi cabinet and the KRG's council of ministers to promote early flagging of disputes.

To the Government of Iraq:

4. Speed up payments to producing companies operating in the Kurdish region, as agreed.
5. Refrain from inflammatory rhetoric toward Turkey.

To the Kurdistan Regional Government:

6. Resume export of oil through the Iraqi national pipeline at agreed volumes.

To International Oil Companies:

7. Refrain from signing contracts with either the government of Iraq or the KRG for acreage located in disputed territories; and suspend all operations in disputed territories until the status of internal disputed boundaries has been resolved.

To the Government of Turkey:

8. Refrain from inflammatory rhetoric toward the Maliki government, continue to emphasise Turkey's interest in the unity of Iraq and engage with the Maliki government and the KRG to assist them to come to an agreement over the status of disputed internal boundaries and a federal hydrocarbons law.

To the UN Assistance Mission for Iraq (UNAMI):

9. Revive the high-level task force, at least to address flare-ups along the trigger line; support negotiations between Iraqi stakeholders on disputed internal boundaries by providing technical expertise and political advice at all levels; and propose specific confidence-building steps in the disputed territories based on its April 2009 report.
10. Should these negotiations reach a dead end on their individual tracks, move Iraqi stakeholders toward a grand bargain combining the issues of power, resources and territories, as proposed in the mission's April 2009 report.

To the U.S. Government:

11. Support the early start of negotiations between the Iraqi government and the KRG on the status of disputed internal boundaries and a federal hydrocarbons law and provide full financial and diplomatic backing to UNAMI in mediating stakeholder talks.
12. Use military assistance (equipment and training) as leverage to press the Iraqi government and the KRG to refrain from unilateral steps in disputed territories, including by army and Kurdish regional guard units or by issuing oil and gas contracts; and strengthen mechanisms aimed at improving communications and security cooperation to reduce chances of violent conflict.

13. Announce and reaffirm publicly its policy of advising international oil and gas companies not to sign contracts for acreage located in disputed territories, and persuade those that have signed such deals to suspend all operations in disputed territories until the status of internal disputed boundaries has been resolved.

**Baghdad/Erbil/Washington/Brussels,
19 April 2012**

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I. INTRODUCTION

Until ExxonMobil, the world's largest oil company, invested in Iraqi Kurdistan, contracting for six oil exploration blocks in October 2011, the region had been on a steady path toward developing its hydrocarbons resources independent of the federal government in Baghdad but also without a clear prospect of independently monetising its wealth. The political standoff between Baghdad and Erbil had left pressing disputes over oil and territories unresolved. In the vacuum, the Kurdistan regional government (KRG) unilaterally issued licenses to international oil firms, asserting that the region's 2007 oil and gas law permitted this. However, the region remained dependent on Baghdad's permission to put the oil and gas it produced into the national pipeline and continued to rely on the 17 per cent share of the federal budget Baghdad allots it, which is funded almost entirely by revenues from oil and gas exports.¹ The Kurds have long chafed under Baghdad's chokehold control exercised in this fashion but had no viable means to extricate themselves. ExxonMobil's entry could tip the balance in their favour but also carries the potential to ignite a more serious conflict.

It has long been argued – by the U.S., Turkish and other governments – that Iraq should remain united and that the best mechanism to ensure this is a federal hydrocarbons law that would draw the Kurds closely into the state structure on terms acceptable to both Baghdad and Erbil. But negotiating such a law has proved devilishly difficult. An effort foundered in 2007 and has not been revived, despite multiple attempts. From 2007 onward, both sides have

unilaterally developed acreage under their control.² The Kurds argued that Baghdad was seeking to perpetuate the pre-1991 situation,³ when Saddam Hussein's regime allowed no significant development in the Kurdish region, especially not in hydrocarbons, so as to dam up Kurdish nationalism. Kurdish leaders, therefore, claimed the right – under their interpretation of the 2005 constitution – to sign more than 40 contracts to date with international oil and gas firms without Baghdad's approval. This has enraged the federal government, which accuses the KRG of undermining its authority to set a national energy strategy, and thus Iraq's unity, given the country's heavy dependence on oil exports.⁴

If this dispute were not sufficiently incendiary, the KRG's decision to direct international investments to areas it claims for the Kurdish region that were designated as disputed in the 2005 constitution could provide new triggers for conflict. Just as negotiations over a hydrocarbons law have stalled, so has the process designed to address disputed internal boundaries.⁵ Despite the release of a major UN

¹ The revenues from all of Iraq's oil exports accrue to central coffers and are distributed as part of the annual budget to the governorates proportionally, based on population (calculated, in the absence of a census, on the UN food ration system created in the 1990s and regularly updated). As an exception, the Kurdish region (three governorates) receives a flat 17 per cent of the federal budget annually (before deductions to cover federal expenditures from which the region benefits). This system, while fair to individual Iraqi citizens, who theoretically receive an equal share, is weighted against the producing governorates, especially Basra in the south, where the majority of Iraq's oil wealth is located.

² They have done so within the confines of a federal revenue-sharing arrangement that sees all profits managed centrally. The term "unilaterally" should be understood in the context of Iraq's federal system, in which the federal government has no representation in the KRG, while Kurdish officials play a prominent role in Baghdad, occupying the senior positions of president (Jalal Talabani), deputy prime minister (Rozh Nouri Shaweis) and foreign minister (Hoshiyar Zeibari), among others. This is an issue that has long rankled Iraqi officials, who frequently describe it in conversation as a basic unfairness deriving from the 2005 constitution.

³ In October 1991, Kurdish rebel groups gained full control over most of the three Kurdish governorates of Erbil, Suleimaniya and Dohuk, following a unilateral Iraqi army withdrawal to what became known as the Green Line. Elections in May 1992 brought to power a Kurdish government that ruled independent of Baghdad.

⁴ See Crisis Group Middle East Report N°80, *Oil for Soil: Toward a Grand Bargain on Iraq and the Kurds*, 28 October 2008.

⁵ During the 2003 U.S. invasion of Iraq, Kurdish security forces rushed across the Green Line to gain control over areas they considered historically part of the Kurdish region. In the 2005 constitution, these areas were termed "disputed territories", whose status was to be resolved through a three-step process of "normalisation", a census and a popular referendum before the end

study on this issue in 2009 that the UN Assistance Mission in Iraq (UNAMI) had prepared in the hope it would form the basis for negotiations leading to a compromise solution,⁶ Baghdad and Erbil have barely discussed the matter. In the meantime, the Kurds have continued to extend their writ beyond the Green Line that divides the Kurdish region from the rest of the country in the direction of a new “trigger” line that runs somewhere along the centre of the disputed territories and along which entrenched Iraqi and Kurdish security forces face each other in an uneasy military stalemate.⁷

As part of this effort, the KRG has also signed contracts with international oil companies for acreage that is squarely located in territories whose status remains unresolved, that remain under Baghdad’s sovereignty, and over which the federal government in theory continues to exercise authority. In practice, Kurdish security forces control these areas, and the KRG exercises de facto sovereignty through its political representatives and the civil servants it has appointed. The voluminous presence of oil and gas in the disputed territories raises their economic and political value; the KRG’s active development of these resources makes it an issue of imminent concern to Baghdad, which fears that a sizeable chunk of the nation’s wealth could soon slip from its control.

ExxonMobil’s decision to deal directly with the KRG over Baghdad’s protests not only shifts momentum for further hydrocarbons development in Iraq to the Kurds – with pressures building on Baghdad to allow greater volumes to be exported from the Kurdish region through the national pipeline – but also increases chances for a violent backlash from the federal government, since two of ExxonMobil’s blocks and a small part of a third are situated across the Green Line inside disputed territories. The company’s acceptance in effect of the KRG’s interpretation of the Iraqi constitution as well as the KRG’s definition of the

Kurdish region’s boundaries places it at direct loggerheads with Baghdad and potentially accelerates the centrifugal forces that are tearing up Iraq. The cardinal question is whether the looming conflict can be prevented, and if so, how.

of 2007. While some Arabs left or were pushed out of the disputed territories, and many displaced Kurds returned, no census or referendum has taken place, primarily because the federal government has had no interest in organising a population count it believes would embolden the Kurds by potentially showing a Kurdish plurality in some disputed areas such as Kirkuk, or in staging a plebiscite it fears the Kurds might win. See Crisis Group Middle East Report N°56, *Iraq and the Kurds: The Brewing Battle over Kirkuk* (18 July 2006), and Crisis Group Middle East Report N°64, *Iraq and the Kurds: Resolving the Kirkuk Crisis*, 19 April 2007.

⁶ The UN Assistance Mission in Iraq (UNAMI) released this detailed report on the disputed territories only to the principal stakeholders. It has never been made public.

⁷ See Crisis Group Middle East Report N°88, *Iraq and the Kurds: Trouble Along the Trigger Line*, 8 July 2009, and Crisis Group Middle East Report N°103, *Iraq and the Kurds: Confronting Withdrawal Fears*, 28 March 2011.

II. THE KURDS' STRATEGY

Since the 2003 U.S. invasion, Iraq's Kurdish leaders have repeatedly stated they are prepared to see the region remain part of Iraq – as long as the state is federal, democratic and pluralistic – even as they never cease to dream they will gain their independence one day.⁸ Indeed, Kurdish officials have played their part in Baghdad as government leaders, military commanders and senior civil servants, sometimes mediating intra-Arab conflicts and otherwise playing by the rules of the game established by the U.S. occupying power and elected Iraqi governments.⁹ Throughout this period, however, and notwithstanding their constructive participation in the federal government, these leaders have also taken advantage of their powerful positions in Baghdad to enhance the Kurdish region's chances of seceding sometime in the future, if and when the international situation permits.

To this effect, they have worked hard to maximise the KRG's autonomy and extend its control over territory and resources. They hope that by ruling independent of Baghdad, establishing a historical record of sovereign acts and creating a powerful economic base, they will be able to seize the opportunity to declare statehood when it presents itself and be widely accepted as a new member of the community of nations.¹⁰ In public, they insist their im-

mediate aim is to stay within a united Iraq – just as the U.S. and Turkey are telling them should be their objective.

Crisis Group has highlighted the Kurds' quest to incorporate disputed territories into the Kurdish region in previous reports, while noting their parallel effort to strengthen the region's economic base. Despite the Kurdish region's potentially strong agricultural sector (fed by rivers flowing in from Turkey and Iran), this latter effort has focused almost exclusively on its suspected vast hydrocarbons wealth. Already a decade ago, the KRG signed contracts with small Norwegian and Turkish companies to start prospecting for oil.¹¹ These were production-sharing agreements, whose terms on balance were favourable to the companies in recognition of the high up-front risk involved in exploration of new and difficult terrain.¹² Today, these companies are pumping oil – evidence of their success.

From the beginning, the KRG's strategy – led by its natural resources minister, Ashti Hawrami, and escalating after the failure in 2007 to agree with Baghdad on federal legislation – has been to gradually draw in ever-larger companies based on the success of their predecessors, offering new fields and allowing bigger companies better equipped to handle the multifarious aspects of oil exploitation to buy out the so-called wildcatters.¹³ This strategy,

⁸ Masoud Barzani, the Kurdish region's president, often alludes to the Kurds' right to secede, or uses language that his followers interpret as such. On the occasion of the Kurdish New Year in 2012 (Nowruz, 21 March), he said, for example, "it is time to say enough is enough. The current state of affairs is unacceptable to us, and I call on all Iraqi political leaders to urgently try and find a solution or we will return to our people and will decide on whatever course of action our people deem appropriate", speech, 20 March 2012 (in Arabic), http://krp.org/arabic/article_display.aspx?id=25866; for a summary in English, see <http://krp.org/english/articledisplay.aspx?id=25868>. Those comments came only five days after he said in a speech to a youth conference that soon there would be (unspecified) good news, (in Arabic), <http://krp.org/arabic/articledisplay.aspx?id=25859>. That was widely interpreted in the Kurdish media as hinting that Barzani would declare Kurdish independence in his New Year's speech.

⁹ In his 2012 Nowruz speech, op. cit., Barzani put it this way: "Iraq is facing a serious crisis. We have tried our utmost to prevent Iraq from descending into a sectarian conflict, and we have consistently avoided taking sides in this conflict. The Kurds have played a pivotal role in bringing about the new Iraq, particularly two years ago when our initiative resulted in the formation of the current government. Had it not been for our role, one can only guess what an unknown fate would have beset Iraq".

¹⁰ For an analysis of this strategy, see Joost Hiltermann, "To Protect or to Project? Iraqi Kurds and Their Future", *Middle East Report*, no. 247 (Summer 2008), <http://merip.org/mer/mer247/hiltermann.html>.

¹¹ The KRG signed a contract with Genel Enerji of Turkey in 2002 to develop the Taq Taq oil field in Suleimaniya governorate, and with DNO of Norway in 2004 to develop the Tawke block in Dohuk governorate.

¹² Under a production-sharing agreement, companies, in return for their investments, their work and the commercial and political risks they assume, receive a share of profits rather than compensation for their services, as Baghdad prefers. Moreover, they are allowed to list oil reserves they discover as their own holdings, which helps drive up the value of their stock market shares. Many Iraqis consider such practices an intolerable transfer of control over their country's national resources to foreigners, which is the key reason Baghdad has not supported production-sharing agreements.

¹³ The wildcatters' strategy is to sell their operations to the highest bidder. To this end, they try to stay in the game as long as possible, with international oil prices rising and oil development in the Kurdish region taking off. Hawrami said, "the small and the beautiful [oil companies] found the oil, and they are normally more aggressive, very quick movers [who] put their investment very rapidly into the ground. They discovered [oil], and then you need a new way of managing these finds. So they require more, for example, more drilling, more facilities, more investments – where the medium size and the large companies actually have better skills to do that". Quoted in "Oil majors could follow Exxon into Kurdistan", *Financial Times*, 21 November 2011. A Turkish entrepreneur said in response to the ExxonMobil deal with the KRG, "today the KRG prefers bigger companies. Natural Resources Minister Hawrami says it's a time for consolidation. Before, it was only smaller companies that would take the risk, but now things have changed. There are

which makes great commercial sense, found its apogee with ExxonMobil's arrival. Other major companies, such as Chevron, Total, ENI and Statoil, reportedly are deliberating whether they also should take the plunge.¹⁴

The KRG has been keen to attract companies from Western countries, especially the U.S. and Turkey, in hopes of securing political support and even physical protection from those countries' governments should the Kurds' gains in northern Iraq, and the companies operating there, come under threat.¹⁵ U.S. companies, ranging from Hunt Oil to HKN, Murphy, Hess, Marathon and now ExxonMobil, have descended on this potentially lucrative new acreage. During a visit to Washington in early April 2012, the president of the Kurdish region, Masoud Barzani, sought to persuade the Obama administration to agree to a "special relationship" between the U.S. and the KRG, one element of which would be a U.S. security guarantee for the Kurdish region and another its green light for a gas pipeline running directly from the Kurdish region to Turkey.¹⁶ The visit reportedly was not a great success in this regard, with the U.S. merely reiterating the need for the KRG to work closely with Baghdad in a unified Iraq.¹⁷

Furthermore, the KRG has tried to lure companies, especially U.S. companies, into those parts of the disputed territories its security forces control in order to strengthen its claim to these areas and increase chances it can integrate

more flights and better hotels and better organisation and governance. So small companies like ours will get pushed out of the Kurdish region. We will sell our assets to the bigger companies. This is the natural progression of things". Crisis Group interview, Ankara, March 2012.

¹⁴ Crisis Group interviews, oil industry experts, Europe and the Middle East, March 2012; and "In Iraq, oil majors play north versus south", Reuters, 5 April 2012.

¹⁵ A Turkish entrepreneur said, "the Exxon deal was not controversial in Turkey, because by this point, both the Turkish and Iraqi Kurdish sides have realised that we need each other. We provide them with security, and they provide us with energy". Crisis Group interview, Ankara, March 2012.

¹⁶ Iraq has no gas pipeline, as it has never produced gas or tried to export its associated gas (gas released when drilling for oil), preferring to flare (burn) it. A pipeline from the Kurdish region to Turkey not only would give the KRG a strategic advantage over Baghdad in Iraqi gas exports but also would constitute another step toward the region's economic self-sufficiency and thus political independence. In that sense, the decision to build such a pipeline would be considered highly provocative by Baghdad. Crisis Group interviews, Baghdad, January 2011, and Erbil, December 2011.

¹⁷ The White House announced on the heels of a meeting between Obama and Barzani that the U.S. is "committed to our close and historic relationship with Kurdistan and the Kurdish people, in the context of our strategic partnership with a federal, democratic and unified Iraq". Statement, Office of the Vice President, 4 April 2012.

them into the Kurdish region. A U.S. official commented: "The KRG has insisted that American companies come in on oil development in the disputed territories. They want to bring in the U.S. government that way. The KRG is very smart"¹⁸.

Some companies were aware that their blocks were located across the Green Line; others apparently were not.¹⁹ The KRG has used subterfuge, pretending that blocks in the disputed territories were actually inside the Kurdish region.²⁰ Ashti Hawrami has explicitly stated that "we don't have anything in disputed territories", and "there is no particular line"²¹ – a position that directly contradicts

¹⁸ Crisis Group interview, 19 May 2010.

¹⁹ See Ben Lando, "Hunt Oil knew KRG oil deal in disputed territory", *Iraq Oil Report*, 25 August 2011, which quotes a U.S. State Department cable released by WikiLeaks. Hunt's blocks are in an area that has a mixed population of Kurds and Chaldo-Assyrian Christians. Anecdotally, some oil company executives expressed surprise after signing their contracts to learn that their operations were situated across the Green Line. Crisis Group interviews, oil industry experts, Europe and the Middle East, March 2012.

²⁰ Contracts state that blocks are located in the Kurdish region, and there is anecdotal evidence to suggest that the KRG natural resources ministry actively discourages contracting companies from using maps that show the Green Line. Crisis Group interviews, oil company staff, Kurdish region, 2010 and 2011. As early as 2008, ministry officials instructed oil and security companies operating under KRG contracts to remove any maps in their possession that showed the Green Line, while contracts of employees working for such companies stated they were employed in the Kurdish region, even when they were operating in disputed territories. Crisis Group interviews, company officials, during visits to drill sites in the disputed territories, February and October 2009 and June 2010. The companies in question all had maps that purportedly showed the Green Line. However, these displayed significant differences, and all were very much at odds (in the KRG's favour) with a 1996 UNICEF map that an adviser to the KRG prime minister gave Crisis Group in January 2008 as showing the Green Line's correct location. The latter map is the basis for the maps in the Appendix to this report.

²¹ In a November 2011 interview with Ben Lando (BL) of *Iraq Oil Report*, Ashti Hawrami (AH) made the following comments: "BL: Taking into consideration the development you have had, which will be part of the discussion to update the draft law, how do you deal with the contracts that are in disputed territories? AH: No, we don't have anything in disputed territories. BL: There are blocks, such as the Hunt block ... AH: It is not; it is within Kurdistan. BL: It's not within disputed territories? AH: We are administering, we have elections, we have everything which is run from Kurdistan. What are you talking about? We have everything contracted by Kurdistan, within Kurdistan. Remember there is disputed territories; I'm not an expert in that. There is no particular line. It comes down to who is in charge of it, now or then. It is bigger than where you draw a line. It needs to be fundamentally sorted out, so it's a different article, different thing. It's not my department. I don't want to get involved with that". *Iraq Oil Report*, 15 November 2011. A senior

the same constitution that the Kurds say they consider sacrosanct and repeatedly accuse the Maliki government of violating.²² Hawrami also routinely claims the Kurdish region holds 45 billion barrels of oil, a figure that almost certainly includes oil in the disputed territories, such as the Kirkuk field's reservoir (which alone holds an estimated ten billion barrels).²³ Regardless, for companies the disputed territories hold great promise, despite the evident political risk. An oil industry expert said, "the risk with the contracts in the disputed territories is huge, but these

contracts ... offer very rare rates of return. It's almost like gambling".²⁴

The KRG's aggressive entry into the disputed territories through oil contracts is at variance with its position on the federal government's role there. In its own 2007 regional oil and gas law, the KRG seeks to prohibit Baghdad from carrying out hydrocarbons-related operations in the disputed territories without the KRG's approval, as long as these areas' status has not been resolved through a referendum.²⁵ This injunction makes it difficult to justify the KRG's own unilateral operations there, especially because the disputed territories remain under the federal government's jurisdiction until their status is resolved.

Kurdish official similarly has been quoted as saying, "we are dealing with these areas as part of Kurdistan". Sam Dagher, "Kurds seize on Iraqi crisis to advance bid for oil and disputed lands", *The Wall Street Journal*, 2 February 2012. Hawrami has a long record of wishing away the Green Line. In 2008 he said, "you show me the green line in the constitution. You show me a green line that officially anybody signed on to. There are many green lines. But what counts really is what is currently under the KRG authority". Quoted in United Press International, 17 June 2008. Earlier he said, "there is no hard line drawn somewhere that says this is KRG-controlled territory, and these are disputed territories; it is all gray areas. We provide the security; administratively we run the towns and villages in that area. It is and has always been under control of KRG, under our security". Quoted in United Press International, 28 November 2007.

²² Hawrami's position is difficult to reconcile with the KRG's stated adherence to the 2005 Iraqi constitution, including Article 140 on disputed territories. The constitution (by incorporating Article 53A of the 2004 interim constitution) defines the Green Line as the line bordering the area the KRG administered until the previous regime's removal: "The Kurdistan Regional Government is recognized as the official government of the territories that were administered by that government on 19 March 2003 in the governorates of Dohuk, Arbil, Sulaimaniya, Kirkuk, Diyala and Neneveh". "Law of the Administration for the State of Iraq for the Transitional Period" (also known as the "Transitional Administrative Law", TAL), U.S. Coalition Provisional Authority, 8 March 2004. (Article 143 of the 2005 constitution incorporates Articles 53A and 58 of the TAL.) This leaves little doubt as to what is meant by the Green Line. Moreover, UN maps exist from the 1990s showing its location (see above). On the ground, it was marked by Iraqi-laid minefields and, on the roads connecting the two parts of Iraq, Iraqi and Kurdish military check-points. Crisis Group observations in the Kurdish region at the time. In a speech in March 2012, Masoud Barzani, president of the Kurdish region, again accused the Maliki government of violating the constitution: "Power-sharing and partnership between Kurds, Sunni and Shiite Arabs and others is now completely non-existent and has become meaningless. The Iraqi Constitution is constantly violated and the Erbil agreement, which was the basis upon which the current government was formed, has been completely ignored. As soon as they came to power, they disregarded the Constitution, the previous agreements that we had, and the principle of power-sharing". www.krp.org, 20 March 2012.

²³ Cited in Sylvia Pfeifer, "Exxon signs Kurds exploration contracts", *Financial Times*, 10 November 2011.

The KRG's biggest coup was gaining access to Khurmala Dome, geologically an integral part of the Kirkuk oil field that is located in a small part of Erbil governorate across the Green Line.²⁶ The KRG started pumping there in 2008, piping most of the oil it produced to the region's main refinery outside Erbil²⁷ and the rest into the export pipeline – with Baghdad's grudging consent.²⁸ Hunt Oil, Dana Gas and a series of smaller companies also invested in the disputed territories, as did ExxonMobil in 2011. (See maps

²⁴ Crisis Group interview, Erbil, 4 October 2009.

²⁵ Article 19(4) of the 2007 Oil and Gas Law of the Kurdistan Region – Iraq states: "The Federal Government must not practise any new Petroleum Operations in the disputed territories without the approval of the Regional Government until such time as the referendum required by Article 140 of the Federal Constitution is conducted".

²⁶ See Crisis Group Report, *Trouble Along the Trigger Line*, op. cit., pp. 20-22. Baghdad, along with major oil companies, sees the Kirkuk field and its four domes (Baba, Avana, Khurmala and Zab) as a single geological structure, therefore a "current" field under the terms of the 2005 constitution, which Baghdad and Erbil should jointly manage. The KRG, by contrast, sees Khurmala as a separate structure, not developed before 2007 and therefore in its view a new field over which it should have sole authority, according to the constitution. Crisis Group interview, oil industry expert, Erbil, 22 January 2011.

²⁷ The refinery is owned and operated by the KAR Group, a Kurdish firm.

²⁸ Of Khurmala Dome's three parts, South Khurmala produces for export through the Kirkuk pipeline, while Middle and North Khurmala produce for the Erbil refinery. Crisis Group site visit to Khurmala Dome, 3 June 2010. The federal government accepted the arrangement because it saw it as benefiting Iraq (rather than primarily serving the KRG's interest in its struggle with Baghdad), on grounds that the oil's beneficiaries, through the supply of electricity to homes, would be the people of Erbil and other places in the Kurdish region, all Iraqi citizens. The Erbil refinery currently has capacity to process 60,000 b/d of oil and has been producing electrical power as well as other petroleum by-products (LPG, naphtha, kerosene, jet fuel, diesel and heavy fuel oil). Crisis Group site visit to the Erbil refinery, 3 June 2010; and Ben Van Heuvelen, "KRG oil deals buoyed by refinery plan", *Iraq Oil Report*, 29 March 2012.

in the Appendix below.) Moreover, in 2011 the KRG started replacing foreign security contractors deployed on oil and gas fields on both sides of the Green Line with Kurdish regional guard forces (the *zerevani*²⁹), sending the bill to Baghdad as part of cost recovery, thus seeking monetary reimbursement for a policy that, contrary to Baghdad's interests, keeps Kurdish security forces mobilised, including in territories the Kurds hope to wrest from the federal government.³⁰

On balance, the KRG has done remarkably well. Since it passed its own oil and gas law in 2007, it has signed more than 40 contracts with international oil companies, giving out most of the Kurdish region and a good part of the disputed territories for exploration. Companies have been conducting seismic tests and initial drilling to assess their blocks' potential. Results have varied, but the mood has been buoyant because of constant finds and the strong expectation that the area is immensely rich in resources; firms report a 70-per-cent success rate, which they call "fantastic".³¹ In 2009, the KRG forced Baghdad's hand by offering to export oil and thus contribute to national revenues. Given the dramatic drop in the oil price (from \$147 per barrel in mid-2008 to \$30 half a year later), the federal government was in no position to refuse, and the two sides negotiated an agreement by which the KRG would start sending oil through the export pipeline. This involved oil from the two fields that had started to pro-

duce – Taq Taq and Tawke – operated by companies with which the KRG had signed contracts prior to 2007.³²

It turned out, however, that the KRG had rushed into the agreement, possibly overestimating its leverage. It had failed to understand that, although Baghdad had opened the pipeline to Kurdish crude, it was only prepared to pay the producing companies for their costs through the KRG's established share of the federal budget. In other words, the KRG would have to pay the companies from its own funds rather than as a direct cost recovery from Baghdad's revenues. The realisation prompted a KRG boycott of the arrangement for several months. It subsequently resumed exports based on a new agreement under which Baghdad would reimburse the companies following an audit of their expenses.

The two sides renewed this arrangement in November 2010, just after the KRG's political support had helped Maliki to a second term as prime minister. The KRG promised to export 100,000 barrels per day (b/d) in 2011. In exchange, the federal government pledged to use (a reasonable, cost-covering) 50 per cent of the U.S. dollar value of those exports' revenues to repay (via the KRG) the producing companies for their investment and operating costs ("cost oil") – as long as it could audit their receipts³³ – but not to pay their profits ("profit oil"), because it argued that production-sharing agreements assigned unjustifiably high returns to the contracting companies,³⁴ those funds would have to come out of the KRG's annual budget

²⁹ The *zerevani* are a paramilitary force, technically under the KRG but in reality controlled by Masoud Barzani's Kurdistan Democratic Party (KDP). In February 2011, the KDP deployed *zerevani* units in Suleimaniya in an attempt to put down a popular protest – the Kurdish version of the Arab Spring – and shortly afterward sent them to Kirkuk, ostensibly to prevent unrest in Arab quarters; they withdrew only following direct U.S. pressure. See Crisis Group Report, *Confronting Withdrawal Fears*, op. cit., pp. 25-26.

³⁰ In a deal forged in January 2011, the federal government committed to paying half the dollar value of revenues in order to reimburse the investment and operating costs incurred by companies whose contracts with the KRG preceded the 2007 stalemate over the federal hydrocarbons law. Baghdad has not agreed to pay these companies their profits, saying they should come out of the KRG's annual share of the federal budget (see below). By invoicing Baghdad for the cost of protecting oil and gas fields in both the Kurdish region and the disputed territories, the KRG has shifted the financial burden for keeping some of its regional guard forces mobilised to the federal government. Moreover, in the disputed territories, this means that in effect Baghdad is paying the Kurds for consolidating their control over these territories, directly contrary to its declared objective of keeping Kurdish security forces confined to the Kurdish region. Crisis Group interviews, oil company officials, Europe, March 2012.

³¹ Crisis Group interview, oil industry expert, Erbil, 13 December 2011.

³² Baghdad in principle acknowledges the validity of KRG contracts signed before 2007 (when talks over a federal hydrocarbons law broke down, and the KRG issued its own hydrocarbons law) but not that they are production-sharing agreements, which it claims do not conform to its model contracts – based on its interpretation of the constitution – and were not approved by the federal oil ministry.

³³ Under the agreement, Baghdad offered to reimburse the companies by making up-front lump-sum payments to the KRG, in exchange for which the KRG would send receipts for the companies' equipment and operating expenses. Following an audit and determination of acceptable expenses, the federal government would then settle any outstanding balance.

³⁴ A senior adviser to the oil ministry and chairman of the advisory committee to the prime minister's office said in early 2011 that the problem with the KRG's contracts was that at that time the government had not seen them and therefore did not know their financial or legal terms: "Without the terms, they can't be audited, and therefore we won't be able to pay these companies". Crisis Group interview, Thamir Ghadhban, Baghdad, 16 January 2011. The government started making payments once it had seen the text of the two companies' contracts. In 2011, the KRG posted on its website the text of most of its contracts with oil and gas companies (not including its contract with ExxonMobil), <http://krq.org/pages/page.asp?lngnr=12&rn=296&PageNr=1>.

allocation.³⁵ In October 2011, Baghdad and Erbil agreed that in 2012 the KRG would contribute 175,000 b/d to Iraq's exports on roughly the same terms. That deal, enshrined in the 2012 budget law, is again for one year, with no renewal guarantee. In April 2012, after complaining Baghdad had not made payments since May 2011 and was \$1.5 billion in arrears,³⁶ the KRG halted all exports via the Iraqi pipeline "until further notice".³⁷

To have a realistic chance at becoming politically independent, the Kurdish region would not only need to gain the consent of powerful neighbours such as Turkey, but also to reach a degree of financial independence from Baghdad. The KRG would have to replace a good share of the yearly budget allocation it receives from Baghdad (almost \$11 billion in 2012) with its own funds.³⁸ Given the importance of hydrocarbons revenues to the budget in both Iraq as a whole and the Kurdish region,³⁹ this means the

KRG would need to export oil and gas via its own yet-to-be-built strategic pipeline directly to Turkey at a value equal to or exceeding its annual income from Baghdad.⁴⁰ Having pledged to export 175,000 b/d in 2012 (with an additional amount produced for local consumption), and with Iraq's overall production expected to rise to 3.6 million b/d this year, the Kurdish region would reach roughly 5 per cent of total Iraqi output even as it receives the equivalent of 17 per cent of the Iraqi budget (more than 90 per cent of which derives from oil revenues).

In other words, as long as it has no alternative to the Iraqi pipeline, the Kurdish region remains heavily dependent on Iraq's southern oil fields for its income. However, Hawrami repeatedly has stated he expects to increase the Kurdish region's oil production to one million b/d by 2015.⁴¹ Even an increase to 400,000 b/d, conveyed through a new Kurdish pipeline to Turkey, would bring the region an important step closer to political independence by achieving budgetary self-sufficiency: at \$100 per barrel (which is below the current world price), the KRG would stand to make \$14.6 billion annually at that level of output.⁴² An oil industry expert in the Kurdish region said:

We are giving the KRG a very strong weapon against Baghdad: the promise of one million b/d. This would lift the KRG over 17 per cent of the national budget, and thus the KRG would be a net provider to that budget. This would give it lots of leverage and a seat at the table. Or it could contemplate becoming independent.⁴³

Of course, as long as Baghdad limits the Kurdish region's exports, the KRG will not come even close to producing one million b/d.

In sum, the Kurds are trying to free themselves of Baghdad's embrace by creating political, constitutional, territorial, economic and security "facts" on the ground. Should

³⁵ In April 2011, Shahrstani reaffirmed Baghdad's position that it does "not recognize the [KRG] contracts. The companies will not be paid any profits or profit oil. That is for them to agree with the KRG, which signed the contracts with them. Unless the contracts are submitted to the government of Iraq and the government accepts them, modifies or rejects them, only then can the amended contracts be the responsibility of the government of Iraq". Quoted in *Middle East Economic Survey*, 7 April 2011. A senior KRG official said the deal's terms, which he called "win-win", were as follows: the KRG would start sending oil into the export pipeline by 1 February 2011, pumping 85,000 b/d initially but hopefully going up to 150,000 b/d; the 2011 budget law would be amended to reflect this and reduce the percentage Baghdad deducts for "federal expenditures"; revenues would flow to the central treasury; Baghdad would conduct a full audit of the companies' operations and, following that, pay them for their costs; Baghdad would supply fuel oil, gasoline and other fuel products to the Kurdish region; the KRG would close its borders to oil smuggling and close down the small privately-owned "backyard" distilleries ("topping plants"). Crisis Group interview, Erbil, 19 January 2011.

³⁶ According to U.S. officials, the federal government has made two payments so far to the KRG for oil company payments: \$250 million in May 2011 and \$204 million in September 2011. Crisis Group interview, Washington DC, February 2012. The KRG claims that Baghdad has paid nothing since May 2011 and is \$1.5 billion in arrears. "Kurdistan oil exports down and may stop due to non-payment by federal government", www.krg.org, 26 March 2012. Genel Energy, which is the main operator at the Taq Taq field that has been producing for export through the Iraqi pipeline, said it had received two payments in 2011. Quoted in Ben Lando, "Q&A: Genel Energy's Tony Hayward and Mehmet Sepil", *Iraq Oil Report*, 22 November 2011. After Genel Enerji was bought by Vallares (owned by Tony Hayward, the former CEO of BP) in 2011, its name was changed to Genel Energy.

³⁷ Reuters, 1 April 2012.

³⁸ The KRG was allocated \$10.8 billion in the 2012 Iraqi budget.

³⁹ The 17 per cent allocation from Baghdad constitutes an estimated 95 per cent of the KRG's budget.

⁴⁰ The KRG is allocated 17 per cent of the national budget, but it receives less, perhaps 13 per cent, as a result of deductions to cover federal expenditures on items from which the Kurdish region benefits along with the rest of Iraq. Other factors affect the calculation of Kurdish budgetary self-sufficiency, however, such as the international market price of oil.

⁴¹ Cited in Sylvia Pfeifer and Javier Blas, "Overview: Politics casts shadow over energy wealth", *Financial Times*, 7 December 2011. In 2010, Hawrami said the KRG could reach that volume by 2014. Crisis Group interview, Erbil, 22 May 2010. The Kurdish region could also become a gas exporter, but this is a more distant prospect, as Iraq lacks a gas export infrastructure.

⁴² KRG Prime Minister Barham Salih put it diplomatically: "With the production of oil increasing in Kurdistan we eye the opportunity in the next few years for Kurdistan to become ... from an oil point of view ... a net contributor to the Iraqi budget". Quoted in Ben Lando, "Q&A: Barham Salih", *Iraq Oil Report*, 25 November 2011.

⁴³ Crisis Group interview, Erbil, 13 December 2011.

they choose to move decisively toward political independence, they would do so only when they believe it would not render them vulnerable to serious reprisals from Baghdad or neighbouring states. Therein lies the challenge, for Kurds remain at the mercy of their territory's landlocked character. Their logical, most commercially lucrative, export route runs through Turkey, which has been eager to buy Kurdish crude in addition to the oil it has acquired from the super-giant Kirkuk field, most of which lies under Baghdad's control. Yet Ankara has insisted, in keeping with its strategic goal of keeping Iraq whole, that all sales be made via the Iraqi state marketing board, SOMO (see below). This has reinforced the Kurds' reliance on Baghdad instead of loosening it.

Meanwhile, most international oil companies that have invested in the Kurdish region have yet to see one penny in return for their efforts. As long as the stalemate between Erbil and Baghdad endures and exports are blocked,⁴⁴ they have no realistic prospect of recovering their costs, much less turning a profit. The question is how long it will take before the first company goes belly up or pulls up stakes in search of more lucrative possibilities – a subject of intense discussion among these companies and their shareholders.⁴⁵ If banking on a breakthrough in Erbil-Baghdad

relations may have appeared a reasonable gamble once, five years hence it clearly no longer is so.

How to escape this bind? By exploring more blocks, finding more oil and attracting ever more powerful international oil companies such as ExxonMobil, the KRG hopes to generate powerful pressures on Baghdad, via Ankara's mediation, to allow greater export volumes. Ideally, however, it would like Turkey to forsake its vision of a functioning and united Iraq in favour of bilateral Turkish-KRG relations based on mutual economic interest. Turkey, in other words, would be the Kurds' final "acquisition" in their hydrocarbons gamble; Ankara's putative about-face would release them from 90 years of Iraqi custody and if not turn them into an independent state at least put them one step up from their current dependence on Baghdad: a hydrocarbons-rich, Kurdish statelet dependent for its exports on a Turkey thirsty for oil and gas.⁴⁶ This would offer them hope they could turn their newly won halfway status into real independence sometime in the future, regional circumstances permitting.⁴⁷

⁴⁴ Baghdad has allowed export of oil only from the two companies, DNO and Genel Enerji, that signed contracts with the KRG prior to the 2007 breakdown in negotiations over a federal hydrocarbons law, at which point the KRG passed its own oil and gas legislation. In the absence of export channels, the KRG has allowed operating companies to sell oil to private (Kurdish) traders, who have trucked it across the Iranian border. Sam Dagher, "Smugglers in Iraq blunt sanctions against Iran", *The New York Times*, 8 July 2010. Exposure of this illicit trade in *The New York Times* caused an outcry in both Baghdad (which asked the KRG about the revenues) and Washington (which pushed it to stop breaking sanctions on Iran). According to an oil industry expert, the trade appears to have continued, mostly because it provides the KRG with an escape valve: by trucking oil to Iran (and potentially Turkey), it generates revenues, part of which it can use to pay the producing companies. Even if trucked oil cannot be sold for more than \$50 per barrel, close to half of which the KRG reportedly keeps, the companies at least see part of their expenditures reimbursed this way. Indeed, the expert said, "the KRG is giving less oil to Baghdad than it could or the Iraqi government wants, because it makes more money by trucking it out". Crisis Group interview, Washington DC, 22 March 2012.

⁴⁵ Some companies with deep investments and great potential face serious decisions. Gulf Keystone, for example, a British company, reportedly has invested \$7.5 billion for a field that appears to have 10.5 billion barrels of oil, a major discovery. Yet so far it has been able to export only a very small volume of oil (reportedly 5,000 b/d) and has seen little or no return on its investment. According to local rumours, the company is hoping to be bought out by ExxonMobil. Crisis Group interview, oil industry expert, Erbil, 13 December 2011.

⁴⁶ Tellingly, the KRG reportedly has asked oil company executives wanting to invest in the Kurdish region to team up with Turkish companies – as a way of increasing Turkey's political stake in the region. Crisis Group interview, oil industry expert, Washington DC, March 2012.

⁴⁷ As noted above, the KRG does not publicly acknowledge pursuing a strategy to achieve political independence. Ashti Hawrami declared at a conference in 2010, for example: "The KRG doesn't need Baghdad's permission [to produce and export oil]. We're not asking. We don't want poverty and instability. We're not after exclusive revenue. We're one country, and I hope we remain that". Presentation at the Atlantic Council's Black Sea Forum, Istanbul, 1 October 2010.

III. BAGHDAD'S RESPONSE

Alarmed by the secessionist tendencies – even as Kurdish leaders profess to be responsible players in a united Iraq – Baghdad has used various means to thwart the Kurds' ambitions. Although the federal government does not have complete freedom of manoeuvre vis-à-vis the Kurds – after all, Kurds hold some of its most senior positions – it has exploited several advantages: Kurdistan's landlocked nature, its own monopoly over the export infrastructure and the presence of a far greater volume of oil in non-Kurdish Iraq, especially in the area around Basra.

Initially, Baghdad's problems far outweighed the KRG's. Due to prolonged instability created by an eight-year war with Iran, more than a decade of international sanctions and the 2003 U.S. invasion, Iraq saw its oil production plummet from a high of 3.6 million b/d in 1979 to less than 500,000 b/d during the worst years of crisis. By early 2003, it had recovered somewhat, producing 2.4 million b/d,⁴⁸ but the invasion wiped that out, and after 2003, it lacked the investments to rehabilitate its super-giant oil fields in the south and Kirkuk. Production hovered just below two million b/d, and investors were wary of entering the country as long as violence endured, the government remained weak and dysfunctional, and leaders failed to agree on a federal oil law that could provide legal security for them.

Only in 2009 was Oil Minister Hussain al-Shahristani finally able to stage two bid rounds for these fields. Oil companies jumped in, acknowledging that the government's terms were perhaps less advantageous than the KRG's but viewing Iraq as the first new world-class area to be opened for oil exploration since the end of the Cold War, with a higher potential for access to large volumes of oil and gas reserves than anywhere else. They expected volumes to be large enough to create economies of scale that, on paper at least, would yield an acceptable return regardless of relatively unfavourable contract terms.⁴⁹

⁴⁸ Production dropped following Iraq's 1980 invasion of Iran from 3.6 million b/d to less than 1 million b/d. Output recovered after war's end, reaching a plateau of 3.4 million b/d, but then the 1990-1991 Kuwait invasion, sanctions and Gulf War wiped out production, as they deprived Iraq of the ability to export. Production hovered under a half million b/d until the UN's oil-for-food program allowed for a resumption of exports. By early 2003, Iraq was producing 2.4 million b/d. For statistics, see "Iraq crude oil production by year", *Index Mundi*, www.indexmundi.com/energy.aspx?country=iq&product=oil&graph=production, and "Crude oil production: Iraq", *Economagic*, www.economagic.com/em-cgi/data.exe/doeme/paprpqi.

⁴⁹ The key advantages for companies deciding to invest in Iraq's southern oil fields were that the contracts were without direct

The first to bite was BP, which had a long history of engagement with the Rumaila field and now agreed to be the lead contractor there (joined by CNPC of China and Iraq's South Oil Company). The contract's low profit margin was offset by the promise of managing a reservoir containing two billion barrels of oil, with an expected output of 2.85 million b/d, that relative to other existing fields required no major rehabilitation; in other words, sheer volume would compensate for a low per-barrel return.⁵⁰ Once BP made its move – apparently perceived by many as a leap of faith, akin to a huge commercial gamble – other internationals joined the fray for fear of losing out,⁵¹ and within weeks major oil companies such as ExxonMobil, Royal Dutch Shell, ENI, Total, Statoil and Lukoil had negotiated technical service contracts with similar terms for the other major fields in the south. The lone exception was the Kirkuk field, for which the government could find no immediate takers.⁵²

The cumulative output for which the companies had contracted was twelve million b/d within six years (2016) – a figure that, if reached, would put Iraq far past its neighbours Iran (3.5 million b/d in 2011) and Saudi Arabia (close to 10 million b/d), but that critics promptly derided as un-

financial risk (the government offered to pay all costs) and gave them the right to post barrels to their balance sheets (the volume a company agrees to produce during the contract's duration), thus increasing their market value. This is not to say that the contracts are guaranteed to be profitable: while companies face no costs, their profits derive from sales; if they fail to meet production targets, because of poor infrastructure and an abundance of red tape, they will make less money than anticipated. Crisis Group interviews, international oil company officials, Europe, March 2012.

⁵⁰ An oil industry expert said in 2010, "BP has a very small margin of profit (\$2 per barrel), but it works for the company because of the size of the field. BP hopes to move from one million b/d to three million b/d in seven years". Crisis Group interview, Baghdad, 31 May 2010.

⁵¹ As an international oil expert put it, "BP entered Iraq first, on terms that were profitable. Then everyone else rushed in with a herd mentality, just to be there". Crisis Group interview, Europe, March 2012.

⁵² Discovered in the early 1930s, the Kirkuk field appears to be past its peak. Maltreatment and poor maintenance (especially during international sanctions in 1990-2003) have combined to depress its output. Politics, especially the dispute over Kirkuk's status and the fact that part of the Kirkuk field – Khurmala Dome – is under the KRG's military control, have discouraged international oil companies from taking a sustained interest. This includes Shell, which has extensive experience in Kirkuk; it submitted a bid in 2009 but could not reach agreement with Baghdad over contract terms. Crisis Group interview, Shell official, The Hague, 2010. The two domes under the federal government's control, Baba and Avana, appear to be declining at a rate of 18 per cent per year, which is an estimated 8 per cent over their natural rate of decline. Crisis Group interview, U.S. official, Washington DC, February 2012.

realistic and even unwise.⁵³ They pointed at the poor state of infrastructure (notably pipelines, pumping stations, oil export terminals and the main Um Qasr seaport designed for imports, including building materials for the oil industry) and a notoriously inefficient bureaucracy as huge stumbling blocks on the way to achieving even half that volume. Shahrستاني brushed these concerns aside, however, and organised a further two bid rounds for oil as well as gas fields, both current and yet unexplored.

By March 2012, output had inched up to three million b/d, of which 2.1 million b/d were exported, with the promise of a steady further increase upon inauguration of a new offshore single-point mooring facility in the Gulf.⁵⁴ Thus Iraq started to gradually hoist itself back up to the elite of oil-exporting countries, with the realistic aspiration of producing at least five to six million b/d by 2018, a major proportion of which would be for export.⁵⁵

Following the failure in 2007 to agree on terms for a federal hydrocarbons law with the KRG and the KRG's subsequent all-out effort to sign production-sharing contracts with foreign companies, Shahrستاني used the bully pulpit of his position as oil minister to denounce the KRG for pursuing an oil policy at variance with Baghdad's, one, he said, that threatened to break up the country.⁵⁶ He ar-

gued that the KRG had no right under the constitution to conclude its own contracts with oil companies, and that production-sharing agreements in particular are "illegitimate" and could even be deemed illegal if they failed to yield the greatest benefit to the Iraqi people, as the constitution enjoined.⁵⁷ Shahrستاني, by then deputy prime minister for energy, told Crisis Group:

There are things that I think both sides can easily agree upon. That is that any oil produced has to be handed over for export through legal means, and this should be approved by the central government. That is a point that nobody disagrees with – even the KRG says they

absolutely. Oil can be used to unify Iraq and build a prosperous, progressive country where people can live in peace, with a share of the oil wealth Or it can be a tool for the disintegration of the country, civil war, among different regions, different governorates, and even different tribes. So, for me, the unity of the country, the peaceful coexistence of its ethnic and religious and sectarian factions, is extremely important. And unless oil is managed centrally and revenues are distributed equally to all Iraqis, oil can be very dangerous, to be used in the civil war among the different factions". Ben Van Heuvelen, "Q&A: Hussain al-Shahrستاني", *Iraq Oil Report*, 22 December 2011.

⁵⁷ Article 112(2) of the 2005 constitution states: "The federal government and the governments of the producing regions and governorates shall jointly formulate the necessary strategic policies to develop oil and gas wealth in a way that yields the greatest benefit to the Iraqi people and relies on the most advanced techniques of market principles and investment promotion". (An English translation of the 2005 constitution is at www.krg.org/articles/detail.asp?lngnr=12&smap=04030000&nr=107&nr=12329, but such translations of the constitution have tended to be very poor. The translation rendered here is Crisis Group's own. The original Arabic version is available from the Iraqi presidency's website, www.iraqipresidency.net.) Shahrستاني has hinted that the KRG contracts might not produce the greatest benefit to the Iraqi people, especially compared to the contracts Baghdad has signed with foreign companies since 2009: "We have always said and told them [the KRG] that these contracts have to be reviewed by the ministry of oil. We have to make sure that they provide Iraq with the best or highest revenue possible and they have to be approved by the Iraqi government like any other oil contract But now, everybody realizes the kind of contracts that Iraq is able to get, the kind of service fees the companies are willing to pay and we have to be in conformity basically with the general form of contracts in the country". Quoted in Ben Lando, "Ten deals makes a happy minister", *Iraq Oil Report*, 4 February 2010. Hawrami has countered: "I don't want to prejudge, but we are confident that what we have done is fully constitutional. I don't have to say: forty companies working here, everybody has a legal counsel, everybody looks at the constitution of Iraq, everyone looked at our model contract, everyone looked at our oil and gas law of the region. If these independent [companies] and expertise came to the conclusion we are sound constitutionally and legally, that is good enough for me and good enough for investors. I hope it is good enough for the parliament in Bagdad as well". "Oil majors could follow Exxon into Kurdistan", *Financial Times*, 21 November 2011.

⁵³ An independent Iraqi oil expert who advises the oil ministry, criticised what he termed "the big push theory" of oil development, of which Shahrستاني has been the architect, for setting an impossible production target and therefore creating a very costly idle capacity: if investments are directed toward producing twelve million b/d but exports realistically won't exceed half that, the country will have significant unused facilities. Crisis Group interview, Ahmed Mousa Jiyad, Amman, 1 March 2012. See also his "Oil upstream development: The feasibility of a fast-tempo, big-push strategy", *International Journal of Contemporary Iraqi Studies*, vol. 5, no. 1 (2011), especially pp. 39-43. The reason for setting the high target could be that further exploration will yield an increase in Iraq's proven reserves. This would give Baghdad ammunition for a future request to OPEC to receive a greater market share, but any benefit deriving from its success would have to offset the significant financial cost of any remaining idle capacity.

⁵⁴ Announcement by Oil Minister Shahrستاني, quoted in Reuters, 5 March 2012.

⁵⁵ Making predictions on Iraq's future output is an art more than a science. The five-to-six million b/d estimate is conservative. A former Iraqi oil minister more optimistically predicted a production capacity of ten million b/d by 2020, of which 6.5 million b/d would be for export and 1.5 million b/d for domestic refining, leaving a two million b/d spare capacity. The spare capacity would put Iraq on a par with Saudi Arabia, which can influence world prices by its ability to quickly and significantly increase production. Presentation by Ibrahim Bahr Alolom, Washington DC, 1 November 2011.

⁵⁶ Shahrستاني said, in response to the question whether he thought it very important for Iraq's oil sector to be centralised, "yes,

agree with it. The fact is that all oil contracts have to meet certain criteria, and that is that they be competitive, transparent and have fairness for Iraq.

At the end of the day, the problem is not with the companies. They wanted to obtain the deals, make some reasonable profit, and keep things moving. We have no objection to that. The objection basically comes from the KRG, and that is that they will not allow any amendments to the contracts to be negotiated. All that we are asking now, as far as what we are paying the oil companies [in the Kurdish region], is that we pay them for their actual expenditure – the capital investment they have actually spent on equipment, and after that would come operating costs. This was the KRG's proposal, and we immediately accepted it, and we asked to look at the costs – to see the receipts. We don't have a problem with the capital investment, and we don't even have a problem with the operating costs – the problem is with some KRG officials making their agendas with Iraqi oil, which will never work.

In response to the question whether wildcatters in the Kurdish region could be bought up by large corporations that have technical service contracts to operate in the south, Shahrستاني added:

That would be one way – for the companies that have contracts with us to buy the small companies over there and accept a similar contract to what they have already with us. That's fine; we would have no problem with that. It could basically be a service contract like we already have with them. It is only a matter of negotiating what we call the remuneration fee. The other way would be for these small companies to keep their contracts, but for these to be renegotiated as service contracts with a reasonable profit margin, and to let them continue their work.⁵⁸

Later, Shahrستاني warned the KRG that fuelling federalist sentiments elsewhere in Iraq by insisting on the Kurdish region's right to issue oil contracts could boomerang, leaving the KRG "the biggest loser ... because they are already taking 17 per cent of the oil [revenues] from the south. And if the south wants to behave the same way as the KRG are behaving, the first victims will be the KRG with their 17 per cent".⁵⁹

While exports remained low, and as the KRG started to develop its own oil fields, Baghdad was in a weak position to reject Kurdish oil for export, however. It worried about setting a precedent that would further entrench the Kurdish region's autonomy in a way that could undermine its own ability to set a national oil policy, but it needed the revenues that would accrue from these exports. Hence its 2009 agreement with the KRG, which has been renewed and expanded twice. Still, even as it allowed Kurdish crude into the national pipeline, Baghdad continued to reject the KRG contracts' appropriateness as production-sharing agreements. On this basis, it agreed to partially defray the companies' reasonable expenses for producing and selling oil that contributed to the national treasury, but not to pay them the profits on their sales as stipulated in their contracts.⁶⁰

When the KRG suspended its oil exports in April 2012 over Baghdad's alleged non-payment of the producing companies' operating costs, Shahrستاني claimed that by doing so and by smuggling oil to Iran, the KRG was depriving the country of \$5.65 billion in potential oil revenues.⁶¹ He threatened retaliation: "The (2012) budget law now obliges the federal Finance Ministry to get these audited figures from the Oil Ministry and to cut the same amount of money from the [Kurdish] region that the federal budget lost because of the undelivered oil".⁶² If carried out, the threat would halve the KRG's income from Baghdad in 2012.

The government has appeared content to let the KRG prospect for oil in the disputed territories, perhaps calculating that once it reasserts control there, it will be in charge

could use its new influence to set national oil policy and claim a bigger share of oil revenues – at the expense of everyone else, including the Kurds. Basra has been pushing for greater control over its hydrocarbons wealth. See, for example, Ali Abu Iraq and Ben Lando, "Basra leaders threaten lawsuit", *Iraq Oil Report*, 24 November 2011.

⁶⁰ See Walter Gibbs, "Iraq's Shahrستاني retains hard line on Kurdish oil", Reuters, 10 October 2011.

⁶¹ The KRG has in the past admitted to sending "surplus fuel" (mostly heavy fuel oil) abroad. See Ben Lando, "Kurdish oil boom begins", *Iraq Oil Report*, 29 June 2011. An oil industry expert claimed in 2010 that some 5,000 b/d of crude from Taq Taq was unaccounted for (a figure not including crude from other fields) and was likely smuggled into Iran. Crisis Group interview, Erbil, April 2010. A retired Iraqi oil executive alleged in May 2010 that the KRG trucked little – some 10,000 b/d – of its Taq Taq production to Khurmala (where it enters the Kirkuk pipeline), shipping the rest to Iran: "The KRG could be selling 100,000 b/d to the central government via K1 [the Kirkuk pipeline], but they choose not to do so. They want to truck it to Iran", in order to have a revenue stream independent of Baghdad. Crisis Group interview, Kirkuk, 23 May 2010.

⁶² Quoted in Ben Lando, "Iraq oil fight worsens with budget threat", *Iraq Oil Report*, 3 April 2012.

⁵⁸ Crisis Group interview, Baghdad, 16 January 2011.

⁵⁹ Ben Van Heuvelen, "Q&A: Hussain al-Shahrستاني", op. cit. Shahrستاني was referring to federalist tendencies in Basra. If Basra were to declare itself a region under the terms allowed by the 2005 constitution, it would gain far greater control over its oil and could, like the KRG, claim the right to issue its own contracts. Given the amount of oil in its territory, a Basra region

and benefit from ongoing operations. That said, Baghdad clearly is unhappy about the contracts, directing its anger at ExxonMobil in particular. In response to the question why he thought ExxonMobil's contract for blocks in the disputed territories would complicate efforts to resolve the territorial conflict, Shahrastani said:

Because these are disputed territories: Iraqis have been discussing it – it's one of the most difficult unresolved issues in Iraq. And when an oil company comes and puts its nose into such delicate internal affairs, it reminds people of the role of the oil companies in the '50s and '60s in the region, and I don't think that will serve at all to change the image of ExxonMobil, in particular, in the region.⁶³

Quite apart from the escalating war of words over the ExxonMobil deal, tensions between Baghdad and Erbil had already increased in late 2011 following accusations that one of Iraq's two vice presidents, Tareq al-Hashimi, had been running death squads. Hashimi, who has denied the charges, fled to the Kurdish region, whose leaders have sheltered him ever since despite repeated requests from Baghdad that they hand him over.⁶⁴ In March 2012, Barzani directly attacked Maliki for edging out his governing partners and consolidating power:

There is an attempt to establish a one-million-strong army whose loyalty is only to a single person. Where in the world can the same person be the prime minister, the chief of staff of the armed forces, the minister of defence, the minister of interior, the chief of intelligence and the head of the national security council?

Then he warned:

It is time to say enough is enough. The current state of affairs is unacceptable to us, and I call on all Iraqi political leaders to urgently try and find a solution; otherwise we will return to our people and will decide on whatever course of action that our people deem appropriate.⁶⁵

Fearing a resurgence of a strong central state, Kurdish leaders want to leave Iraq, and they appear to believe that their moment to do so may soon arrive.

IV. TOWARD A TIPPING POINT?

A. BUILDING MOMENTUM

All things being equal, Kurdish leaders have no rational ground to believe they can escape Baghdad's clutches anytime soon. All the same, they continue to prepare for eventualities that might tip the balance in their favour; in any event, their actions serve the region's more immediate agenda of expanding its economic autonomy and increasing the KRG's political leverage vis-à-vis both Baghdad and the principal consumer of Kurdish oil, Turkey. This effort has set in motion a dynamic that is starting to assume a momentum of its own. Kurdish leaders feel strongly encouraged by a series of developments that could push matters to the tipping point:

- ExxonMobil's October 2011 signing of an oil contract with the KRG over Baghdad's express objections, including for three blocks that lie wholly or partially in disputed territories (see below);
- a steady increase in Kurdish oil production, mentioned above; the projected start later in 2012 of construction of a strategic Kurdish oil pipeline to Turkey capable of carrying 420,000 b/d that would bypass the Iraqi export network (expected completion date: 2014);⁶⁶ and talk of building a gas pipeline – Iraq's first – from the Chamchamal and Kor Mor fields to Ceyhan on Turkey's Mediterranean coast;⁶⁷

⁶⁶ In April 2012, the Taq Taq Operating Company was expected soon to award a contract for the construction of an oil pipeline that could carry 420,000 b/d from the Taq Taq field to Fish Khabour in Dohuk governorate, where the Kirkuk-Ceyhan pipeline crosses from Iraq into Turkey. Significantly, the pipeline is to be built by Genel Energy, a Turkish company, and therefore with the evident blessing of the Turkish government. "Genel to build direct Kurdistan-Turkey oil export line", Platts Commodity News, 21 March 2012. A Kurdish oil pipeline is not necessarily an act inimical to Baghdad's interests – at least as long as Turkey does not accept Kurdish oil without Baghdad's permission. Until that time, a Kurdish pipeline would be an Iraqi pipeline, relieving pressure on the existing pipelines network and with revenues accruing to central coffers.

⁶⁷ The Turkish consul-general in Erbil, Aydın Selcen, said, "the most commercial alternative [to Turkey's dependence on high-priced Russian gas] seems to be the Kurdistan Regional Government (KRG). We have a long shared border". Quoted in Javier Blas, "Natural gas: North looks to tap into long-term export potential for vast reserves", *Financial Times*, 7 December 2011. The Chamchamal field lies inside the Kurdish region (Suleimaniya governorate) but juts into the disputed territories (Kirkuk governorate), while Kor Mor is squarely in disputed territories (Salah al-Din governorate). Kurdish leaders claim both Chamchamal and Kor Mor as part of Kirkuk. The Iraqi gov-

⁶³ Ben Van Heuvelen, "Q&A: Hussain al-Shahrastani", op. cit.

⁶⁴ Hashimi has remained in the Kurdish region except for an official visit to Qatar in early April 2012. "Hashimi leaves to Doha, Maliki threatens with Interpol", *Aswat Al Iraq*, 1 April 2012.

⁶⁵ Speech, 20 March 2012, op. cit.

- ❑ the five-year contract awarded to a private Kurdish company in Erbil in August 2011 to provide electrical power to Kirkuk, turning the Kurdish region into a net exporter of electrical power to Iraqi provinces that, while connected to the national grid, receive quantities far below their needs;⁶⁸
- ❑ a July 2011 ministerial decree signed by Turkish President Abdullah Gül, Prime Minister Recep Tayyip Erdoğan and the Turkish council of ministers allowing oil and gas imports by road or rail from neighbouring states when necessitated by Turkish national interest, apparently in circumvention of established agreements with those states' governments (see below);
- ❑ the post-2007 rapprochement between Ankara and Erbil, allowing for the Kurdish region's gradual integration into the Turkish economy, but especially the emergence of a Turkish lobby of entrepreneurs and diplomats that favours direct oil and gas exports from the Kurdish region to Turkey, cutting out Baghdad;⁶⁹
- ❑ the increasing turn of their relationship from its predominantly economic character (though reflecting Ankara's then-new approach in dealing with the presence of the PKK in northern Iraq, encouraging the KRG to contain and squeeze it) to more overtly political in the wake of the U.S. troop withdrawal from Iraq in late 2011 and Ankara's renewed interest, after the outbreak of the Syria crisis, in defeating the PKK with Erbil's help; and
- ❑ growing tensions between Ankara and Baghdad over Turkey's decision to help build and support a political alliance against Prime Minister Maliki's State of Law list in the 2010 parliamentary elections, Turkey's support for the Syrian opposition in 2011 and a war of words with sectarian overtones between Maliki and Erdoğan in January 2012.⁷⁰

ernment also is seeking to build gas export pipelines, including to Syria and Turkey.

⁶⁸ The *Financial Times* reported: "The short-term solution [to the electricity crisis] eventually hit upon was particularly galling for the Arab and Turcomen members of the [Kirkuk provincial] council, not to mention Baghdad – Kirkuk now obtains its energy from the Kurdish regional government's grid. This is likely to be used as political capital by the latter to bolster its claim to ownership of the disputed city. Although Kirkuk is buying the supply from a private company, the KRG ministry of electricity was a co-signatory to the deal". Abigail Fielding-Smith, "People power keeps lights burning in Kirkuk", *Financial Times*, 12 September 2011.

⁶⁹ This finding is based on Crisis Group interviews, Turkish diplomats and entrepreneurs, Turkey and Iraqi Kurdistan, 2011.

⁷⁰ After Erdoğan publicly criticised Maliki in January 2012 for seeking the arrest of Vice President Tareq al-Hashimi, Maliki stingingly alluded to Turkey acting like the Ottoman Empire and played on Turkey's Kurdish insecurities: "Recently, we no-

There has been much speculation about ExxonMobil's business calculations in defying Baghdad at the risk of losing its investments in the south, not least because the company has not publicly commented since the KRG broke news of the signing almost a month after the deed.⁷¹ Based

ticed their [Turkey's] surprise interventions with statements, as if Iraq is controlled or run by them ... Turkey is playing a role that might bring disaster and civil war to the region, and Turkey itself will suffer because it has different sects and ethnicities". "Iraq PM denounces Turkish 'interventions'", Agence France-Presse, 13 January 2012. No less harshly, Erdoğan responded with a speech indirectly but clearly likening Maliki to Yazid, the single most despised historical figure to Shiites (Yazid killed Hussein, splitting Islam in the seventh century). "Erdoğan urges common sense in Iraq but says current picture is not promising", *Today's Zaman*, 10 January 2012. The remark was all the more stinging from a Sunni leader to a Shiite one. Following this exchange, Iraqi politicians sounded outright suspicious of Turkey's motives in Iraq and elsewhere in the Middle East. For example, a Sadrist lawmaker said, "Turkey says that because Iran is controlling Iraq through the Shiites, then it must do the same through the Sunnis. Erdoğan has said that Turkey will have to intervene to protect Iraq's Sunnis. This was a sectarian speech which even our Sunni brothers rejected. This is why Turkey needs a pretext to enter Iraq and dominate the region. Turkey lives in the illusion of the Ottoman Empire, but this will never happen again". Crisis Group interview, Husein al-Sharifi, Baghdad, 16 February 2012. A Turkish official responded: "We did not shift our policy or change our approach to groups in Iraq, but when our government leaders made strong statements against [Syria's president] Bashar al-Assad, some people tried to portray this as a sectarian approach. They tried to exploit this in Iraq, which is a mostly Shiite country. [Shiite politician] Ammar al-Hakim was here last month, our foreign minister met with [Shiite politician] Muqtada Sadr in Tehran in January, and our ambassador in Baghdad is in touch with Shiite groups. We try to allay misperceptions about Turkey, but some groups that don't want Turkey to play a role in the region try to make us look sectarian. But for us sectarianism doesn't factor in; this is a manipulation of the reality". Crisis Group interview, Ankara, March 2012.

⁷¹ At a meeting with financial analysts at the New York Stock Exchange in March 2012, ExxonMobil CEO Rex Tillerson offered a glimpse on his thinking, declaring that the company was proceeding with contracts signed for oil fields in both the south and the Kurdish region: "We're committed to both of those developments, and have indicated to the [Baghdad] government our intention to meet our commitments in both West Qurna and in Kurdistan". Quoted in Ben Van Heuvelen, "Exxon pressing forward on KRG, Qurna deals", *Iraq Oil Report*, 9 March 2012. The only documentary evidence of ExxonMobil's signing with the KRG was its annual filing to the U.S. Securities and Exchange Commission in February 2012: "During 2011, production sharing contracts were negotiated with the regional government of Kurdistan". ExxonMobil's filing included the following statement: "The exploration term is for five years with the possibility of two-year extensions. The production period is 20 years with the right to extend for five years". Quoted in Ben Van Heuvelen, "Exxon confirms Kurdistan deals", *Iraq Oil Report*, 25 February 2012. Meanwhile, ExxonMobil has established offices

on a series of interviews with oil industry experts and government officials in the U.S., Europe and the Middle East in January-March 2012, it appears that ExxonMobil may have suffered from buyer's remorse after jumping into the south in 2009.⁷² Finding systemic infrastructural and bureaucratic obstacles there, it came to expect that the investment would yield much lower returns than it had anticipated when it signed the contracts with the federal oil ministry.⁷³

By contrast, the Kurdish region offered virginal territory with great hydrocarbons potential, as well as an inviting business climate. ExxonMobil and Shell, partners in developing the West Qurna I block in southern Iraq, jointly began exploring the Kurdish region for attractive opportunities in the first half of 2011. For both, there was the prospect of being the first major companies there, with resulting commercial advantages, much as BP had been in the south.⁷⁴ Both companies say they ideally would like to invest in all of Iraq, not just in any one part of it. However, realising that Baghdad would not budge in its objection to the companies' signing with the KRG, Shell pulled out of negotiations with Hawrami, the KRG natural resources minister, in September 2011 in order to protect its interests in the south, which it deemed sufficiently profitable to warrant staying on.⁷⁵

in Erbil and is making all the moves of an oil company primed to start operations. Sam Dagher, "Kurds seize on Iraqi crisis to advance bid for oil and disputed lands", *The Wall Street Journal*, 2 February 2012.

⁷² The discussion of ExxonMobil's business dealings is based on interviews in January-March 2012 with oil industry experts and government officials who had varying degrees of proximity to the events surrounding the signing of its contract with the KRG. Crisis Group sought to obtain ExxonMobil's views directly but was told by company representatives that no comment would be made.

⁷³ ExxonMobil signed a contract to develop the West Qurna I oil field and a separate contract to create the infrastructure to bring water from the Gulf for injection in the south's oil fields. An oil expert noted that the problem with international companies' contracts with Baghdad was that the "Iraqi" risks to the project (implementation and payment delays) "do not have adequate protection in the contract", and that this, "combined with very little possibility to recover earnings through access to the upside risk in the project" (ie, companies get nothing out of high oil prices or in making the projects more cost-efficient), adversely affects the companies' bottom line. Crisis Group email correspondence, 2 April 2012.

⁷⁴ An oil industry expert said, "ExxonMobil wants to do in the north what BP did in the south". Crisis Group interview, Erbil, December 2011.

⁷⁵ In September 2011, Shell, which has contracts for two oil fields in the south – West Qurna I and Majnoun – was also close to signing a major contract to capture and produce flared gas on all of Iraq's oil fields. Shell (in partnership with Iraq's South

ExxonMobil apparently reached a different conclusion. It presumably saw greater prospects for profitable business in the Kurdish region,⁷⁶ despite the absence of a secure export channel, a problem its decision to invest might conceivably help to overcome: it perhaps anticipates that escalating production will put sufficient pressure on Baghdad to allow the KRG to increase its exports commensurately or even to reach a compromise with the KRG over a federal hydrocarbons law.⁷⁷ Moreover, ExxonMobil may have hoped that its move northward would not cost it its investments in the south but have calculated that if the central government did seek to punish the company by removing it as operator on West Qurna I, Baghdad would be the party that broke the contract, thus giving ExxonMobil the possibility to pursue legal remedies.⁷⁸ ExxonMobil might also not mind losing that contract: so far it has sunk \$700 million into developing the field while receiving only a partial payment and having little prospect of seeing full reimbursement soon.⁷⁹

In a move that delighted Kurdish leaders while angering Baghdad, ExxonMobil took two blocks (Bashiqa and Qara Hanjir) that are entirely in disputed territories and a third (Al-Qosh) that edges across the Green Line.⁸⁰ Its reasoning

Gas Company and the Mitsubishi Corporation) signed the contract with the oil ministry in November. Its monopoly of gas development in the south is comparable to BP's advantage in oil there. By contrast, ExxonMobil had neither, which may have provided a powerful incentive to turn northward.

⁷⁶ A possible reason for ExxonMobil's interest in the Kurdish region may be that by signing a contract on six promising blocks it could have reasonable hopes to gain access to significant reserves to add to the company's balance sheet ("bookable reserves"). Like most oil companies, it is very important for ExxonMobil's long-term value to replace the barrels it has taken out of the ground through production each year with new resources. This has reportedly been an increasing concern for the firm over the last few years. Crisis Group interview, oil industry expert, Europe, March 2012.

⁷⁷ Moreover, ExxonMobil's contract could have a significant knock-on effect, as it has given a tremendous boost to other investors, both actual and potential, in the Kurdish region. Further investments would drive up production even more, creating additional pressures on Baghdad to open up its export pipeline to Kurdish crude.

⁷⁸ In January 2012, an international arbitration panel awarded ExxonMobil \$907 million in a similar contract dispute in Venezuela. "ICC awards ExxonMobil \$907 mil in Venezuela arbitration case", *Platts*, 2 January 2012.

⁷⁹ The government has been delayed in making payments to companies operating in the south. An oil industry expert termed ExxonMobil's deal a disaster, as "ExxonMobil is not a loss-leader", ie, a company that will agree to high up-front investments without a reasonable prospect of cost recovery. Crisis Group interview, Washington DC, February 2012.

⁸⁰ The Qara Hanjir block is located due east of Kirkuk city on the way to Suleimaniya, in an area of Kirkuk governorate that is almost exclusively Kurdish. The Bashiqa block is located di-

is not known. When ExxonMobil and Shell opened negotiations with the KRG, six blocks were on the table. In an apparent attempt to push the two companies into a decision, Hawrami removed two blocks (not in the disputed territories) from the deal in July 2011, awarding these to a New York-based company, Hess Corporation.⁸¹ He then replaced these with the two blocks in the disputed territories and offered them to ExxonMobil and Shell.⁸² Shortly afterward, Shell pulled out, and ExxonMobil signed a contract concerning all six blocks on 18 October. It is uncertain whether ExxonMobil fully appreciated the loaded nature of the deal.⁸³ It dramatically raised the value of real estate whose status is disputed, whose control by the KRG would provide a critical economic building block for Kurds' longed-for independent state, and whose ultimate disposition is subject to a process that ran aground years ago, leaving them under Baghdad's sovereignty by default.⁸⁴

Time will tell whether Baghdad will punish ExxonMobil. It is hard to see how Shahrstani could climb down from his public threats to remove the company from the south.⁸⁵

rectly east of Mosul in Ninewa governorate. It has a mixed population of Kurds, Arabs, Shabak, Yazidis and, especially, Chaldo-Assyrian Christians. It is an unstable area in which insurgents operate. Arab politicians in Ninewa immediately protested the deal when it became known. See Ben Van Heuvelen, "Exxon deal stokes territorial disputes", *Iraq Oil Report*, 22 December 2011.

⁸¹ Hess' two blocks are not in disputed territories.

⁸² The offer of these two blocks surprised many, as they did not appear on any maps showing blocks on offer by the KRG. Crisis Group interview, oil industry expert, Dubai, March 2012.

⁸³ It is very likely that ExxonMobil was attracted by the potential wealth of the Bashiqa and Qara Hanjir blocks. It is a mantra among oil companies in the Kurdish region that the closer you get to Kirkuk (ie, into disputed territories) the greater both the quality and the quantity of the oil present in the ground.

⁸⁴ It is possible that ExxonMobil executives, like many U.S. government officials, believe that since the Iraqi constitution provides for fair revenue sharing, a principle that all Iraqi parties have embraced, the location of individual blocks – in the south, in the Kurdish region or in disputed territories – is immaterial. This ignores the critical matter of Kurdish nationalism, however. If and when the Kurds push ahead with their aspiration to gain statehood, the location of oil fields would be vitally important, as the KRG would seek to incorporate as many as possible, just as the federal government would try to keep as many out of the Kurds' hands as it could. Crisis Group interview, oil industry expert, Europe, March 2012.

⁸⁵ Shahrstani accused ExxonMobil of breach of contract (Ben Van Heuvelen, "Q&A: Hussain al-Shahrstani", op. cit.), but reportedly agreed to postpone any decision for six months in order not to create difficulties during the U.S. troop withdrawal and the possible instability that operation might bring in its wake. Crisis Group interviews, U.S. officials, January 2012. It is doubtful that ExxonMobil's signing with the KRG amounts to a breach of its contract with the federal government, as that contract appears to have no clause prohibiting the company from separate dealings with the KRG. Indeed, for that reason, inter-

Already, the oil ministry informed it that it would not be permitted to participate in the fourth bid round,⁸⁶ in May 2012, although ExxonMobil in all likelihood would not consider this a punishment.⁸⁷ The government also removed ExxonMobil as lead operator for a large project to bring water from the Gulf to the oil fields for injection.⁸⁸ In March, ExxonMobil reportedly wrote the Maliki government that it would not start seismic testing, drilling and other operations in the Kurdish region until year's end. This may have bought the company time, though it was stating the obvious: it is in no position to start operations earlier.⁸⁹ But the move north appears to have left Baghdad with little choice on West Qurna I: as Shahrstani has noted, if it allows such a major firm to sign a separate deal with the KRG without negative consequence, others will follow swiftly.⁹⁰

Wise or not,⁹¹ deserved or not,⁹² ExxonMobil's move amounted in effect to an enormous vote of confidence in

national advisers to the oil ministry are suggesting making such a prohibition explicit in future oil contracts, such as the ones to be issued following the fourth bid round (tentatively scheduled for May 2012). Crisis Group interview, Ahmed Mousa Jiyad, Amman, 1 March 2012.

⁸⁶ Shahrstani said he was waiting for ExxonMobil's "final answer" before he would inform it of the government's "final decision", quoted in Reuters, 12 February 2012.

⁸⁷ Major oil companies have expressed dismay at the terms being mentioned for the fourth bid round, which will put up for auction potential fields for exploration. The round has been delayed on several occasions as the oil ministry and companies have haggled over the terms, which over time have been modified as a result but are still not to the companies' liking. Industry experts predicted that the outcome could be that only non-major companies, especially from Asia, will participate when the bid round is eventually held. Crisis Group interview, Dubai, March 2012.

⁸⁸ Reuters, 9 February 2012. For every barrel of oil pumped out of the ground, 1.5 to two barrels of water must be injected.

⁸⁹ Crisis Group, oil industry expert, Washington DC, 5 April 2012.

⁹⁰ Crisis Group interview, oil industry expert who met with Shahrstani, January 2012.

⁹¹ Commenting on the impact with respect to the Erbil-Baghdad conflict, a parliamentarian close to Maliki said, "[b]efore, there was a dispute just over land; now, it also becomes a dispute over wealth, over money – a dispute about land becomes a dispute about oil". Abbas al-Bayati quoted in Ben Van Heuvelen, "Exxon deal stokes territorial disputes", *Iraq Oil Report*, 22 December 2011.

⁹² The KRG is both repressive (eg, having committed serious human rights violations and forcefully cracked down on peaceful protesters in Suleimaniya in February-April 2011) and corrupt, the subject of ongoing Crisis Group research. The Iraqi federal government is equally repressive and corrupt. See, for example, Crisis Group Middle East Report N°113, *Failing Oversight: Iraq's Unchecked Government*, 26 September 2011.

both the Kurdish region's potential and its government,⁹³ an effect that will hardly be lessened in the unlikely event the company is forced to reconsider its decision due to Baghdad's unyielding stance. Cumulatively, growing investments by oil companies bolster the region's claim to separate status, be it autonomous or independent. They do not resolve the question of export, but allow for two scenarios: first, the potential of a million b/d of Kurdish oil would put tremendous pressure on Baghdad to open up the national pipeline, given the high revenues this would generate for the federal treasury; secondly, were Baghdad to block exports, Turkey would come under great pressure to allow for direct exports, especially if other factors led it to lose confidence in the Iraqi regime.

While Turkey has given no sign that it is moving in this direction or on the verge of giving up on Baghdad – most importantly, it has not begun to build either a dedicated pipeline or storage facilities that could accommodate Kurdish crude⁹⁴ – the July 2011 ministerial decree allowing oil and gas imports by road or rail from neighbouring states (when necessitated by Turkish national interest) is intriguing.⁹⁵ By its terms, the KRG natural resources ministry in principle could apply directly to Turkish customs to allow oil tankers to enter Turkey at the Khabour/Habur border crossing without asking Iraq's state marketing board for permission.⁹⁶ While trucking oil is not the most efficient way to convey crude from well to port, oil industry experts deem it acceptable in the absence of a pipeline;

producing companies could thus be paid for their efforts.⁹⁷ For companies in the Kurdish region, which mostly have not been paid since they initiated operations, this would be a godsend.⁹⁸ Moreover, Turkey's decision is an important precedent and provides a stopgap solution until such a time as direct exports by pipeline become politically and physically feasible.⁹⁹

B. APPLYING THE BRAKES: TURKEY

From the Kurdish perspective, the ExxonMobil deal, the Turkish export directive and other related developments are accelerating centrifugal forces that they hope will aid their quest for statehood. Witnessing the rebirth of Kurdistan – its initially slow (1992-2003), then rapid economic blossoming (post-2003, but especially post-2008)¹⁰⁰ – despite serious obstacles, it is easy to understand the Kurds' buoyancy. Yet, much stands in the way of realising their ultimate aspiration, independence, or even the lesser one, a strong autonomy based on unhindered oil exports through

⁹³ A Turkish investor in the Kurdish region said, "the ExxonMobil deal with the KRG means that our interests in Kurdistan are safer. It was an important breakthrough". Crisis Group interview, Ankara, March 2012.

⁹⁴ Change could be on the way. A Turkish newspaper reported in February 2012: "According to local daily *Zaman*, Ikideniz Petrol ve Gaz Sanayi, a Calik Group company, applied to the Turkish authorities to construct a 640-kilometre-long pipeline between Turkey and Iraq. The Silopi-Yumurtalik pipeline will carry oil from Iraq to the Turkish port of Ceyhan, on the Mediterranean coast. The planned pipeline will transfer daily one million barrels of oil". "Calik company Ikideniz plans oil pipeline between Turkey-Iraq", *Turkey Today*, 20 February 2012.

⁹⁵ "Decree No. 2011/2033 on the Transportation of Crude Oil and Jet Fuel over Turkey via Rail and Land Route", 18 July 2011, as published in the Official Gazette, 11 November 2011. Article 4 states: "LPG and fuel products stated in article 2 of Law no 5015 and crude oil shall not be transited, imported or exported via land route or rail from Turkey to another country, from another country to Turkey or to a third country over Turkey. However, when required by the national interest, transit via land route or rail of the product covered by this Decree may be permitted". While the decree does not specify the country of origin, a Turkish official indicated that it was issued specifically with Iraq's Kurdish region in mind. Crisis Group interview, 6 March 2012.

⁹⁶ Crisis Group interview, Turkish official, 6 March 2012.

⁹⁷ Turkey might also be interested in drawing Kurdish oil away from (smuggled) exports to Iran. As for road transportation, a truck can carry 400-500 barrels, so some 36 truckloads would be needed to transport a daily production of 15,000-18,000 barrels. Trucking ten times that volume would be possible but would place a huge stress on the Kurdish region's underdeveloped road system. Crisis Group interview, oil industry expert, Erbil, 13 December 2011.

⁹⁸ The Turkish government and Turkish Kurds would also see this as a godsend that could revive the booming crude trucking business that has been an economic mainstay in the south east since the 1980s. In April 2012, these exports by truck had not yet started, despite Turkish government encouragement, apparently because of political and bureaucratic delays, as well as the KRG's rotation of prime ministers (the new government was inaugurated on 5 April). For oil companies operating in the Kurdish region, the solution to the fact they have not been paid lies in either the KRG reaching a deal with Baghdad over a federal hydrocarbons law, or dealing bilaterally with Ankara. Either solution would be fine, they say, as long as both their costs and profits are paid. Even something less than a hydrocarbons law might suffice, for example a patchwork of laws and agreements. Crisis Group interviews, oil industry experts, Erbil, December 2011.

⁹⁹ Turkish officials have suggested that the next step could be the construction of a power plant on the border that would produce gas for Turkish consumption. One official hinted at further possibilities: "The Kurdish region produces more oil and gas than what Turkey produces. If there is still no federal hydrocarbons law after two years, then the logic suggests ... but I'm not making Turkish policy!" Crisis Group interview, Ankara, December 2011.

¹⁰⁰ The decisive factor was the 2003 U.S. invasion of Iraq, which re-linked the Kurdish region to the rest of Iraq, unlocking its economy, but the unexpected rapprochement between Ankara and Erbil that began in 2008 accelerated the Kurdish region's great strides forward.

the Iraqi pipeline. The Kurds are victims of their geography and of post-World War I political manipulations by the victorious powers, Britain and France, a legacy that could prove impossible to shake short of some border-shattering event.

Turkey has conflicting interests in Iraq. To preserve its own territorial integrity, it is determined to preserve that of neighbours possessing their own Kurdish populations: Iraq, Iran and Syria. Turkish officials are quick to repeat the old mantra that Iraq should remain united, and Kurds should remain an integral part of the country, lest Turkey's own Kurds get the idea that they, too, can move toward greater autonomy and eventually statehood, possibly in alliance with their brethren across the post-Ottoman borders. The spectre of a "Greater Kurdistan" is not one Turkey or Iraq's other neighbours (Iran and Syria) are willing to contemplate.

In the case of Iraq, Turkey is additionally motivated to encourage the presence of a strong Arab-controlled buffer against Iranian influence, based on the age-old, mostly peaceful competition between the Ottoman and Safavid Empires and their respective successor states, Turkey and Iran. The U.S. invasion of Iraq and the subsequent wholesale removal of its leadership, top management and security forces heightened Ankara's concern, as it saw Shiite Islamist parties, which some key officials deemed proxies for Iran, rise to power in the ensuing vacuum.¹⁰¹

In 2007, after the U.S. military launched a surge in Iraq that helped pacify areas wracked by insurgency and sectarian fighting and, more importantly in Ankara's eyes, recalibrated power in Baghdad to Iran's disadvantage by giving disenfranchised Sunni Arabs a seat at the table, the Turkish AKP-led government struck out on an Iraq policy that was meant to be "colour-blind": it reached out to Sunnis and Shiites, Arabs and Kurds without distinction. Encouraged by the Bush administration, it embarked unexpectedly on an unprecedented rapprochement with Iraqi Kurdish leaders – a thaw that led to spring and full-bloom summer. Rather than having to fight the PKK directly, Ankara thought that it could persuade the KRG with economic emoluments to contain and squeeze it, thereby removing the threat it posed and pushing it toward disarmament as part of a political solution.¹⁰²

Turkish businesses expanded their investments in the Kurdish region, building the Erbil and Suleimaniya airports, shopping malls and educational institutions. They also moved prominently in the hydrocarbons field: pri-

vately-owned Pet Oil and Genel Enerji were among the first oil companies making the plunge; Genel has become a main investor there, producing approximately 100,000 b/d at its Taq Taq field, about a third of which is for export, and being set to build the Kurdish strategic pipeline to Turkey.

Turkish diplomats say they are pursuing the Iraqi Kurdish region's "full economic integration" into Turkey, a scenario unthinkable a mere five years ago.¹⁰³ In addition to the economic benefits that flow from this relationship, Turkey's strong ties with the KRG and its investment in the region have given rise to a powerful Turkey-friendly buffer in northern Iraq against any future chaos or spread of pro-Iranian interests in Arab Iraq.

Rather than see the KRG as an ally against Baghdad, however, Ankara has sought to bring the two closer, as part of the imperative of preserving Iraq's territorial unity. Its chosen mechanism has been the unifying federal hydrocarbons legislation that the U.S. also has pushed. The perennial failure since 2006 of Baghdad and Erbil to agree on it¹⁰⁴ has generated enormous frustration in Ankara, prompting calls to circumvent Baghdad in the quest to satisfy Turkey's appetite for the Kurdish region's hydrocarbons wealth.¹⁰⁵ Energy-poor Turkey wants not only to buy Kurdish oil and gas for its own use but also to become a vital hydrocarbons transit corridor for Europe and the Middle East.¹⁰⁶ In particular, seeking to take advantage of Europe's desire to lessen dependence on Russian gas, it has participated in discussions on various gas pipeline options, including the stalled Nabucco project and the TransAnatolia pipeline, to deliver gas potentially from Azerbaijan, Turkmenistan, Iran and Iraq to European markets.¹⁰⁷ Turkey's pivotal

¹⁰³ Crisis Group interview, Turkish official, May 2010.

¹⁰⁴ The differences between the KRG and Baghdad government over the hydrocarbons law are deep, reflecting unresolved issues about the nature of federalism in Iraq. See Sean Kane, Joost R. Hiltermann and Raad Alkadiri, "Iraq's Federalism Quandary", *The National Interest*, March-April 2012, <http://nationalinterest.org/article/iraqs-federalism-quandary-6512>.

¹⁰⁵ Already in 2008 a Turkish official expressed frustration at Baghdad politics as an obstacle to progress on a federal hydrocarbons law: "Turkey and the Kurds are on a historic course of Turkish-Kurdish reconciliation. We need the KRG. We can't wait for the Iraqi government [to get its act together]. We can't wait ten years for it to pass a hydrocarbons law. By 2011 we will need lots of natural gas. If we have to, we'll make deals directly with the Kurds". Crisis Group interview, Ankara, November 2008.

¹⁰⁶ Ankara first outlined this vision in 2008, sometime before that same vision began to sour over obstacles in the way of bringing gas from Iran, Turkmenistan and Iraq to Turkey. Crisis Group interview, Murat Yetkin, Ankara editor of *Radikal* (Turkish daily), Ankara, 19 January 2009.

¹⁰⁷ Industry experts consider the Nabucco project to have failed due to structural and political obstacles (including fickleness of gas supplies from Turkmenistan, international sanctions on Iran

¹⁰¹ Crisis Group interviews, Turkish officials, Istanbul and Ankara, November 2008, January 2009 and July 2009.

¹⁰² See Crisis Group Middle East Report N°81, *Turkey and Iraqi Kurds: Conflict or Cooperation?*, 13 November 2008.

role would be diminished without a lasting Baghdad-Erbil agreement on oil and gas exports.

Besides encouraging Baghdad and Erbil to agree on an oil law, Turkey has also heavily invested in Arab Iraq, opening consulates in Basra, Mosul and Erbil, in addition to its Baghdad embassy; pressing Turkish businesses to trade and invest throughout the country; establishing a High-Level Strategic Cooperation Council (Iraqi and Turkish ministers) in 2008; and signing 48 agreements with the Maliki government in 2009 on energy, security and economic cooperation.¹⁰⁸ A Turkish official explained:

Our goals in Iraq are to establish a functioning system of government, increase our relations in the sphere of trade and investment and contribute to each other based on our mutual interest. Iraq needs a lot of infrastructure and has huge oil reserves. We believe we can play a moderating role in Iraq with our soft power.¹⁰⁹

Another official stressed that Turkey's number one priority in Iraq was its territorial integrity, followed by the acquisition of oil and gas, fostering of political interdependence between Turkey and Iraq (including via a north-south oil pipeline) and promotion of interdependence between Baghdad and Erbil (via a federal hydrocarbons law). He said that it was "not a Turkish interest to have political tensions between Erbil and Baghdad", that the Kurds "should want to be part of a strong Iraq", and that Turkey was mediating indirectly by pushing for "big win-win investment projects".¹¹⁰

When Prime Minister Erdoğan visited Iraq in March 2011, he made a point of including Najaf (where he met with Grand Ayatollah Ali al-Sistani) as a sign that Turkey wished

to maintain close ties with the country's Shiites.¹¹¹ And in a signal that Ankara was in no way contemplating dealing with the KRG separately, a statement released after the governments of Turkey and Iraq extended the Kirkuk-Ceyhan pipeline agreement for fifteen years in September 2010 expressly named the Iraqi State Oil Marketing Organisation (SOMO) as the sole agency authorised to approve Iraqi oil exports through that key artery.¹¹² This precluded any possible Turkish consideration to buy oil directly from the KRG, except by road or rail, as noted above. Kurdish leaders were not pleased.¹¹³

On the sensitive issue of Kirkuk, Turkish officials have long hewn to the position that its incorporation into the Kurdish region constitutes a red line. Ankara's preferred option for the province's permanent status is for it to become a stand-alone region (as envisioned by Iraq's 2004 interim constitution, but not its 2005 successor);¹¹⁴ it sees this as a way to protect the province's sizeable Turkoman population.¹¹⁵ It also sees Kirkuk's oil as an integral part

¹¹¹ He also made the first visit by a Turkish prime minister to Erbil, the Kurdish region's capital, meeting with President Barzani and other Kurdish officials.

¹¹² In a joint statement accompanying the signing of the lease agreement, the Turkish energy minister and Iraq's oil minister stated they "confirm their commitment that the sole sovereign authority for the exportation of Iraqi hydrocarbon resources is strictly channelled through the Iraqi Federal Ministry of Oil and Oil Marketing Co. (SOMO)". "Joint Declaration of Taner Yildiz ... and Hussain al-Shahristani ...", 19 September 2010. The Turkish energy minister, Taner Yildiz, said in an interview, "we agreed with the central government [in Baghdad], the treasure of Iraq belongs to all the people of Iraq. We can only accept northern Iraq's agreements if the central government accepts it", quoted in *Iraq Oil Report*, 21 September 2010. A Turkish official explained: "It was a technical issue. There was no other way but to mention SOMO. This was nothing new. We told the Kurds that this was nothing against them. Once there is a federal hydrocarbons law, we will accept whatever it says". Crisis Group interview, Ankara, September 2010.

¹¹³ Crisis Group interview, senior KRG official who termed the agreement "unconstitutional", Erbil, 21 September 2010.

¹¹⁴ A Turkish official explained that Turkey would prefer for Kirkuk to obtain a special status following a negotiated settlement and a confirmatory referendum. Moreover, he said, Masoud Barzani had told the Turkish leadership that he agreed to this during a visit to Ankara. Crisis Group interview, September 2010. This confirms information released by WikiLeaks that the Turkish ambassador in Baghdad informed U.S. diplomats in January 2010 that the KRG's interior minister, a close adviser to Barzani, had conveyed this position to Turkish leaders. "Turkish ambassador on Article 140 and Kirkuk", U.S. embassy Baghdad cable, 24 January 2010, published by WikiLeaks.

¹¹⁵ Kirkuk city used to be predominantly Turkoman, but with the advent of the oil industry in the 1940s and 1950s, Kurds moved into the city in greater numbers from the surrounding countryside as well as from Kurdish cities such as Dohuk, Erbil and Suleimaniya. From the 1960s onward, the Baath regime's

and the unresolved conflict between Erbil and Baghdad) that made it commercially unviable. They predict that alternatives will be pursued. Alan Riley, "There is life for the Southern Corridor after Nabucco", *European Energy Review*, 12 March 2012.

¹⁰⁸ In July 2008, Erdoğan and Maliki signed a "Joint Political Declaration on the Establishment of the High-Level Strategic Cooperation Council" between Turkey and Iraq, outlining their future relationship. The event marked the first visit by a Turkish leader to Baghdad in over twenty years. A year later, in June 2009, the two countries signed a military cooperation accord; four months later they signed 48 cooperation agreements. Shortly afterward, Turkey opened consulates in Basra and Erbil. Turkish officials now complain that Baghdad has not acted on the 48 agreements signed in 2009 and that by default most Turkish business has turned toward the Kurdish region, which accounts for 70 per cent of Turkish investments in Iraq. Crisis Group interviews, Ankara, March 2012.

¹⁰⁹ Crisis Group interview, Ankara, March 2012.

¹¹⁰ Crisis Group interview, Ankara, March 2010.

of Iraq's oil, though as a region with its own constitution, Kirkuk would potentially have a greater say in what happens with its hydrocarbons wealth than it does today.¹¹⁶ Moreover, the AKP government has actively promoted the Turkomans' political representation in Kirkuk, engineering a deal with the KRG in February 2011 that saw the appointment of a Turkoman as provincial council chairman.¹¹⁷ If Iraq generally becomes more decentralised, Turkey could deal more freely with the newly empowered governorates like Kirkuk but also Suleimaniya (which has a de facto autonomy from Erbil), as well as the Sunni Arab governorates of Ninewa, Salah al-Din and Anbar.¹¹⁸

It is almost impossible to conceive on what grounds Turkey would consider altering its stance toward Iraq and decide to deal directly with the KRG at Baghdad's expense – certainly not without a regional game-changing event, such as an Iran-U.S. war or the violent break-up of Syria, and perhaps not even with it. However frustrated Turkish leaders might be, and under however much pressure they might come from the KRG and its business and diplomatic allies in Turkey, it is in Ankara's overriding interest to overcome its distrust of Iraq's Shiite Islamist parties and the deep differences between Erbil and Baghdad and continue to strive for a united Iraq.

Yet Ankara faces serious obstacles, not in the least because of the spat between Maliki and Erdoğan in January 2012, in which Maliki accused Turkey of acting like the (Sunni) Ottoman Empire and Erdoğan compared Maliki to a figure from Islamic history hated by Shiites (see above). To put their relationship back on the 2007-2009 footing, the two would first have to mend their personal relationship and additionally overcome the sectarian divide that has opened up over the Syria crisis. One way forward would be to agree to put new energy into discussions to rebuild the strategic pipeline that would connect Iraq's southern oil fields to Turkey's Mediterranean ports. The

challenges are enormous, but both Baghdad and Ankara have a significant stake in the project's success.

Turkey's position is not the only factor determining the Kurds' future. So is that of the two other neighbours with significant Kurdish populations, Iran and Syria. Iran repeatedly has stated that it opposes Kirkuk's merger with the Kurdish region (as a stepping stone toward Kurdish independence) but has been content to let Turkey do the heavy diplomatic lifting vis-à-vis the KRG. Syria long was not a factor, and also was happy with Turkey's role. Despite the dramatically changed situation in that country, which has placed Iran and Syria at loggerheads with Turkey, none favours a strong Kurdish region in any of these countries. Whatever their differences – and there are many – Iran and Turkey have shown that if there is one objective on which they can agree, it is thwarting Kurdish aspirations.¹¹⁹

C. APPLYING THE BRAKES: BAGHDAD

While many Arab Iraqis are wont to state that the Kurds have a right to their independence, once they are pressed to explain their position it quickly becomes clear that they mean the Kurds within the Kurdish region, bounded by the Green Line. There is no political group that appears to support ceding any part of the disputed territories to the Kurds, least of all Kirkuk and its surrounding areas.¹²⁰ Whatever the remaining volume of the Kirkuk oil field – expert opinion is divided over how much the field has been depleted and whether new technology and better maintenance could slow down or even reverse the decline¹²¹ – the general perception seemingly is that Kirkuk will remain an important source of wealth to its occupants for the foreseeable future. In other words, Arab Iraq would countenance only a resource-poor independent Kurdistan, a non-starter for the Kurds.

Arabisation policies greatly increased the city's Arab population. As a result of these developments, the Turkoman population declined in relative terms, though it is unclear by how much, as a reliable breakdown of population figures on an ethnic basis does not exist. (The last reliable census was in 1957.)

¹¹⁶ Crisis Group interviews, Turkish officials, Ankara and Washington DC, 2011.

¹¹⁷ As part of the deal, which Ankara has not publicly acknowledged, the council chairman and the governor, both Kurds, were replaced with a new Kurdish governor and a Turkoman council chairman. Crisis Group interviews, Kirkuk, March 2001, and Ankara, December 2011. A Turkish official said that "the better Turkey's relationship with the Kurdish region, the better the KRG treats the Turkomans in Kirkuk". Crisis Group interview, Ankara, March 2012.

¹¹⁸ Crisis Group interview, Turkish officials, Ankara, December 2011.

¹¹⁹ Syria traditionally has shared this view. Today, the Assad regime appears less capable of acting on this inclination and may even be trying to appease Syrian Kurds as a way to divide the opposition.

¹²⁰ For example, a parliamentarian who belongs to Prime Minister Maliki's State of Law party said, "oil and gas belong to Iraq unless Kurdistan officially secedes. If that were to happen, Kirkuk won't be part of the area that splits off. Yes, the Kurds want that, but not everything you want, you get". Crisis Group interview, Shaker al-Daraji, Baghdad, 6 February 2012. Another State of Law legislator similarly declared: "Kirkuk will remain a disputed area, but even so it is going to stay within Iraq. Its resources will stay for Iraq, as its people represent the array of Iraqi people". Crisis Group interview, Husein al-Safi, member of parliament's legal committee, Baghdad, 6 February 2012.

¹²¹ Ashti Hawrami claims the field has only about eight billion to ten billion barrels left, with sixteen billion produced since 1928, "especially for Iraq's wars". Crisis Group interview, Erbil, 22 May 2010.

To solve the Kirkuk conundrum, Kurdish leaders have proposed to couple its integration into the Kurdish region with a national revenue-sharing arrangement that would allow each side a fair share of Iraq's oil income, including that generated by the Kirkuk field.¹²² Then, they argue, it would not matter whether Kirkuk is incorporated into their region, as income would still accrue to the federal treasury for distribution to all parts of Iraq through the annual budget.¹²³ Baghdad has not bought into this argument, however, realising that if the Kurds intend to use Kirkuk as their ticket to statehood, the issue of how national revenues are disposed would become moot the moment independence was declared, as the new state would naturally hold onto its own income from exports. The location of the fields – in Kirkuk and other disputed territories, as opposed to within the Green Line – is critical.

Holding the Kurds in its grip, Baghdad is not only preventing them from breaking away; it is also using its new oil-fuelled buoyancy to squeeze them. For example, Shahrastani, the architect of Baghdad's oil policy, repeatedly has stated that he deems the KRG's production-sharing contracts "illegitimate" and that, should it come to a deal between the two sides, the KRG would have to convert them into standard technical service agreements. That is something to which the companies might consent if they could still turn a profit, but that the KRG would oppose because it would limit its autonomy from the central government.¹²⁴

The problem is potentially worse for the Kurds. While Baghdad might be willing to accommodate some Kurdish oil in the national pipeline as long as its own fields yield insufficient revenue, if and when it can ramp up its production, it might decide it no longer needs Kurdish oil at all. This is because there is a limit on how much Iraq will

be permitted to produce by the Organization of Petroleum Exporting Countries (OPEC), of which it is a founding member. That cartel seeks to control the oil price by assigning each member a quota that caps its production.¹²⁵ Iraq has not had a quota since the beginning of the Iran-Iraq war, because it was producing so little, but once production again becomes substantial, OPEC can be expected to put a ceiling on it, especially because Iraq's most immediate competitors are oil-producing neighbours and OPEC members: Iran and Saudi Arabia.¹²⁶ If oil fields under Baghdad's direct control reached that limit without the Kurdish region's output, Baghdad could decide to choke off Kurdish exports in the absence of a healthy relationship with the KRG.¹²⁷ Short of an agreement, codified in a federal hydrocarbons law, this conflict will fester.

The Baghdad government also has taken steps to reconfirm its monopoly on the national pipeline. Apart from renewing the Kirkuk-Ceyhan pipeline lease agreement in September 2010, it issued a joint declaration with the European Union (EU) in May 2011, stating that the Iraqi government must approve all exports of Iraqi oil and gas.¹²⁸

¹²⁵ OPEC is not known to have a set formula for allocating production quotas to its twelve members; the decisions appear to be political, taken at the OPEC Conference. Quotas may or may not be calculated as a percentage of a member state's proven reserves. Iraq will claim that it lost three decades of optimal output, roughly equivalent to twelve billion barrels, due to war, sanctions and other turmoil. Presentation by Ibrahim Bahr Alolom, a former Iraqi oil minister, Washington DC, 1 November 2011. It is unlikely that Iran would look kindly at the "war" argument, however, as it was Iraq that initiated their conflict in 1980. The director of Iraq's State Oil Marketing Organisation suggested that Iraq will start discussions with other OPEC members over a quota in 2014, when it hopes to reach an output of 4.5 million b/d. "Amri: OPEC quota talks to begin", *Iraq Oil Report*, 19 December 2011.

¹²⁶ Iran, in particular, would feel threatened by an oil-fuelled, resurgent Iraq while it labours under tough international sanctions. The unanswered question is what level of Iraqi production it would tolerate in light of its own output of 3.5 million b/d. While it has various means to subvert Iraqi production – halting work on joint cross-border fields, choking off Iraq's narrow gateway to the Gulf, pipeline sabotage – its first step would likely be to get OPEC to re-impose a production quota.

¹²⁷ Ashti Hawrami said, "let's say Baghdad produces five million b/d and we produce one million b/d, and let's say that OPEC agrees to a ceiling of six million b/d. In that case, we would need a mini-internal OPEC for ourselves to fairly allocate production quotas. And we shouldn't just get 17 per cent. We should be allowed more if we are capable of producing more. Iraq's oil belongs to all of us". Crisis Group interview, Erbil, 22 May 2010.

¹²⁸ The declaration, signed by EU Energy Commissioner Günther Oettinger and Iraqi Deputy Prime Minister for Energy Hussain al-Shahrastani, included the following clause: "This [agreement] includes abiding by relevant legislation on any contract for export from, or development of, oil and gas fields in

¹²² "Revenue Sharing as the Key to Iraq's Problems", Power-Point slides of a presentation given by Ashti Hawrami at a conference in Istanbul, 15-16 May 2010. See also, Sean Kane, "Iraq's Oil Politics: Where Agreement Might Be Found", U.S. Institute of Peace, January 2010.

¹²³ Crisis Group interview, Ashti Hawrami, Salah al-Din, 22 May 2010.

¹²⁴ Crisis Group interview, Hussain al-Shahrastani, deputy prime minister for energy, Baghdad, 16 January 2011 (see extended quote in the text above). An independent oil adviser to the oil ministry, Ahmed Mousa Jiyad, has argued that production-sharing contracts can be converted to technical service contracts and that there is a precedent for this: the contract of the Chinese company CNPC for the Ahdab oil field, signed during the previous regime, was successfully converted in 2008. Crisis Group interview, Amman, 1 March 2012. An oil industry expert who works for a company that does not have a contract with the KRG called the KRG's contracts "not a lot better" than the federal government's and added that "the KRG has pretty tough terms as well. It's just that it is easier to operate in the Kurdish region". Crisis Group interview, Europe, March 2012.

Moreover, reports surfaced in March 2012 that BP was exploring options with Baghdad to develop the Kirkuk oil field. This reassertion of Baghdad's presence in Kirkuk would be a significant counterweight to the KRG's operations in the disputed territories (ExxonMobil's contract in particular), and the first attempt by the federal government to rehabilitate this major asset, which dominates exports through the Kirkuk-Ceyhan pipeline that the KRG also taps into. Kurdish leaders immediately denounced BP for meddling.¹²⁹ If the contract is signed, it would also raise questions about the KRG's role at Khurmala Dome, which geologically is an integral part of the Kirkuk oil field and of all the field's domes appears to have the largest remaining reserves.¹³⁰

Baghdad appears to have an ally in the U.S. government, which repeatedly has stated that the Kurds should remain within a united Iraq.¹³¹ In that context, Washington has been advising U.S. oil companies not to sign contracts with the KRG without the federal government's approval, because

Iraq approved by the Federal Iraqi Government". Quoted in Eric Watkins, "EU affirms authority of Iraq's central government over oil, gas exports", *Oil & Gas Journal*, 27 May 2011.

¹²⁹ The (Kurdish) deputy speaker of parliament, Aref Tayfour, accused British companies of "once again" creating tensions and problems, and called on them not to sign contracts with Baghdad in the disputed territories, statement, 11 March 2012, http://parliament.iq/Iraqi_Council_of_Representatives.php?name=articles_ajsdyawqwqdasdb46s7a98das6dasda7das4da6sd8asdsawewqeqw465e4qweq4wq6e4qw8eqwe4qw6eqwe4sadkj&file=showdetails&sid=6685. Clearly, this is a difficult position to maintain, given its flagrant inconsistency with the KRG's own record of signing oil contracts in the disputed territories and development of Khurmala Dome. The KRG refers to Khurmala Dome as a "non-producing field" at the time the constitution was ratified in 2005, which would mean that if it had been inside the Kurdish region, the KRG would have had sole authority over it. However, it lies in disputed territories (despite being in Erbil governorate) and is an integral part of the Kirkuk oil field, not a separate field in its own right; in 2005, the Kirkuk oil field was a producing field. A conflict likewise is looming over another part of the field, the Avana Dome, which also lies in a disputed section of Erbil governorate and which the KRG has said it will soon claim. "Natural Resources Ministry: Kirkuk oil field development requires approval of KRG and Kirkuk Governorate", www.krg.org, 26 March 2012.

¹³⁰ Khurmala Dome is estimated to be a five billion barrel reservoir, as compared to Avana and Baba, which jointly may have no more than four billion barrels. However, because of its particular geology, Khurmala allows for a flow rate of no more than 100,000 b/d. As an oil industry expert put it, "even huge finds [in the Kurdish region and disputed territories] will not always equal huge production". Crisis Group interview, Erbil, 21 May 2010.

¹³¹ A U.S. official repeated the oft-stated position that the U.S. has a special relationship with the Kurds but insists that they remain part of Iraq. Crisis Group interview, Washington DC, February 2012. See also the White House statement on 4 April 2012, cited above.

of the latter's control over the export channel,¹³² and it has warned them that signing contracts with the KRG for acreage in the disputed territories could raise difficult legal questions and precipitate political and even military conflict.¹³³ It appears that the U.S. was aware that ExxonMobil was considering investing in the Kurdish region but was caught by surprise by the actual signing of the contract and even more so by the location of two blocks and a part of the third in the disputed territories.¹³⁴ With its reduced leverage following the troop withdrawal, it does not seem to be actively pursuing a solution to the conflict between Erbil and Baghdad, or making any headway if it is.¹³⁵

¹³² A U.S. official said, "we discourage investments by international oil companies in oil and gas in the Kurdish region short of an agreement between Baghdad and Erbil, because it is risky. We will talk to companies if they call on us, but we will not seek them out". Crisis Group interview, Baghdad, January 2011. In a statement in late 2010, after Marathon Oil signed a contract with the KRG, the U.S. government stated: "The United States' position remains that it is in the interest of all Iraqi parties to enact a set of national laws to govern the development, management, and distribution of Iraq's hydrocarbons resources We have encouraged all companies, including Marathon, to refrain from signing deals with the KRG independent of the central government's approval We have consistently advised companies of the significant legal and financial risks they may incur by signing contracts with any party independent of the central government's approval", quoted in Ben Lando, "Baghdad silent, US pans new KRG deals with American oil firms", *Iraq Oil Report*, 3 November 2010.

¹³³ Crisis Group interviews, U.S. officials, Washington DC, January 2012.

¹³⁴ The Obama administration reportedly sent a high-level delegation to Baghdad shortly after the news of ExxonMobil's contract with the KRG broke to say it had not been aware that ExxonMobil would sign with the KRG and that, had it known, it would have advised against it. Crisis Group interview, oil industry expert, Middle East, March 2012. The Iraqi deputy prime minister for energy, Hussain al-Shahristani, asserted in an interview: "This contract that was signed by ExxonMobil will not undermine [the] Iraq-US relationship. Both countries have taken a very clear position that such contracts will have to be done with the approval of the central government, and we don't expect anything more than that from the US government. They have given the right advice to the companies". Ben Van Heuvelen, "Q&A: Hussain al-Shahristani", op. cit.

¹³⁵ U.S. officials often suggest that the administration is actively mediating intra-Iraqi disputes. Vice President Biden's security adviser, for example, declared in relation to the political crisis that erupted in Baghdad in late 2011: "During the most recent political standoff, the United States remained the indispensable honest broker and the only one trusted by, and in regular communication with, all of the leading blocs. Much of this engagement takes place quietly, unadvertised. But just because you don't see it and we don't say it, doesn't mean it's not happening". (Quoted in *USA Today*, 5 April 2012.) The problem with such a statement regarding the conflict between Baghdad and

Baghdad and Erbil are on diverging paths that, given the military and political equation, could lead to disaster if one side overreaches or signals are misread. The U.S. and Turkey, which other than Iran have the greatest interest and influence in Iraq, should step up efforts to reinforce Iraqi unity, while using inducements to make power-sharing work in the centre. This means supporting the early start of negotiations between the Iraqi government and the KRG on the status of disputed internal boundaries and a federal hydrocarbons law, including by providing full financial and diplomatic backing to UNAMI in mediating stakeholder talks.

The Obama administration should use military assistance (equipment and training) as leverage to press the two sides to refrain from unilateral steps in the disputed territories, including by army and Kurdish regional guard units or by issuing oil and gas contracts, and should work to strengthen mechanisms aimed at improving communications and security cooperation to reduce chances of violent conflict. The U.S. should also publicly announce and reaffirm its policy of advising international oil and gas companies not to sign contracts for acreage located in disputed territories, and persuade those that have signed such deals to suspend all operations in disputed territories until the status of internal disputed boundaries has been resolved. For its part, the Erdoğan government would do well to refrain from inflammatory rhetoric toward Maliki and his political allies, reaffirm Turkey's interest in the unity of Iraq and make a renewed approach to the Baghdad government to revive the 48 agreements on energy, security and economic cooperation signed in 2009.

Erbil is that whatever U.S. mediation may have taken place, the conflict has continued to escalate. Concerning the ExxonMobil question, Washington has been caught in the middle. A U.S. official said the government has no influence over a company as big as ExxonMobil but would be intensely embarrassed if Baghdad were to expel the company. Questions would then arise in the U.S. Congress as to why the U.S. went to war with Saddam Hussein if the net result was that Chinese and other foreign companies walked away with major business opportunities. Crisis Group interview, Washington DC, January 2012.

V. CONCLUSION

To break out of their predicament, Kurdish leaders are strengthening their position while hoping a game-changing crisis might break down post-Ottoman boundaries and dramatically alter state structures and politics in the Middle East.¹³⁶ Some have openly supported a U.S. attack on Iran, for example, not because they are especially worried about Iran's suspected potential nuclear weapons capability but because they see such a war as indirectly creating an opportunity for them to break free from Iraqi shackles.¹³⁷

Another potential event could be presenting itself in the evolving Syria crisis. If and when the Assad regime falls, Iraq's Sunnis might feel empowered vis-à-vis a Shiite Islamist-dominated government in Baghdad they despise, thus aggravating their already tense relationship. Moreover, having just seen the demise of a key Arab ally (the Assad regime) and, in the process, having lost easy access to another (Hizbollah), Iran might devote more resources to the Maliki government, which itself would feel threatened by a potentially Sunni Islamist-led Syria. This would further compound Iraq's internal crisis and raise the spectre of a return to the days of sectarian conflict.

The Kurds are divided over whether a Sunni-Shiite civil war in Iraq would benefit them: on the one hand, their issue with Baghdad is ethnic/national, not sectarian, and since they do not aim to gain control of the federal government and rule Iraq, they assume the Kurdish region will remain shielded from the worst of conflict. On the other hand, they rely on Baghdad for their budget and access to external markets; they might be politically autonomous, but they are economically and financially dependent. They still would need an independent export route for their oil and gas to realise their dream of independence.

¹³⁶ Some Kurdish leaders expected that the U.S. troop withdrawal could be such a game-changer. Crisis Group reported in 2009 that: "Fuad Hussein, chief of staff to the KRG president, offered [the following] proposal. Declaring that 'we don't want to be part of Turkey and Turkey doesn't want more Kurds', he indicated that Kurdish leaders were now convinced that the Obama administration indeed intends to leave by the timetable it has set and that Iraq, as a result, would collapse. This, he said, would leave the Kurds no choice but to ally themselves with Turkey, while remaining in what would be a highly dysfunctional Iraq, possibly racked by endemic war and regional intervention. In that case, he said, the Kurds would benefit from Turkish protection, and in exchange Turkey would gain direct access to the Kurdistan region's oil and gas, even the huge reserves of Kirkuk". Crisis Group Report, *Trouble Along the Trigger Line*, op. cit., pp. 25-26.

¹³⁷ A senior Kurdish leader suggested in the Bush administration's waning days, July 2008, that a U.S. attack on Iran (a topic of intense discussion in Washington at the time) was desirable, as it would allow the Kurds to press for independence. Crisis Group interview, Erbil, July 2008.

The question thus comes down to what Turkey might do under such a scenario and under what conditions it might agree to deal with the KRG separately even, at the cost of alienating Baghdad. To the Kurds, in other words, Turkey is the linchpin. Ankara's relations with Baghdad took a nosedive after it supported Iyad Allawi's Iraqiya coalition against Maliki's State of Law alliance in the 2010 parliamentary elections and Maliki prevailed. Its subsequent about-face on Syria encouraged Maliki's perception that Turkey remains at bottom the Sunni heir to the Sunni Ottoman Empire, a sectarian power seeking to use its economic weight to establish a new dominion in the Middle East.¹³⁸ Maliki has tried to replace some Turkish investors with Iranians since then – without too much success but signalling his profound mistrust of the northern neighbour.¹³⁹ The January 2012 public spat between Maliki and Erdoğan was emblematic of the growing divergence between the two governments, a far cry from 2009, when they signed a series of wide-ranging cooperation agreements.

A worsening Syria crisis that precipitates a new round of sectarian conflict in Iraq could tip the balance: chaos in the Iraqi heartland might deter Ankara from pursuing its investments there and would render realisation of what Ankara wants most from Iraq even more unlikely: a federal hydrocarbons law, a strategic pipeline connecting the two countries, close security cooperation (focused on the PKK) and free trade. Turkey's ill-fortune in Iraq thus could serve the Kurds, as they think it might persuade Ankara to give up its uncertain relationship with a dysfunctional and hostile Iraq for guaranteed access to Kurdish oil and gas and a stable and pliable Kurdish neighbour on its south-eastern border.¹⁴⁰ And they hope they could gain Kirkuk in the bargain.

¹³⁸ For example, a State of Law parliamentarian said, "Turkey is trying to extend its power in the region by dividing it. A strong Iraq may not present a threat to Turkey, but still Turkey doesn't like having a strong state in its neighbourhood, because it wants to realise its old dream and restore its empire, using new tools. We won't be surprised to learn that Turkey's policy is to divide Iraq". Crisis Group interview, Kamal al-Saadi, Baghdad, 6 February 2012.

¹³⁹ A Turkish government adviser said, "Iran's role in Iraq prevents Turkish entrepreneurs from investing in the south. Security conditions there are a problem for Turkish companies, and the political climate is also not very helpful. Maliki is indirectly creating obstacles to discourage our people". Crisis Group interview, Ankara, March 2012.

¹⁴⁰ A lawmaker of the (opposition) Iraqi Supreme Islamic Council, which is close to the Kurds politically, stated: "The Kurds are seeking good relations with Turkey so that they can prevail on a number of issues in Iraq, extend the power of their region and accomplish their project of establishing a home for the Kurds of Syria, Iran and Iraq. This is their long-term, strategic goal, anyway". Crisis Group interview, Ali Shubar, member of parliament's human rights committee, Baghdad, 16 February 2012.

Overall, the Kurds hope that by increasing the KRG's economic attractiveness to Turkey and threatening the federal government with eventual secession, they could push Ankara to their side. This might pay off, but more likely not. And it is a gamble that will have a cost if it fails: Kurdish leaders are supporting a scenario – growing, unmanaged tensions with Baghdad with the eventual goal of separation – that has existential implications for Iraq. There is every reason to believe the Maliki government will resist if it has the capability. Already, voices can be heard in Baghdad saying the Kurds are over-reaching by signing contracts with firms such as ExxonMobil and will suffer the consequences.¹⁴¹

Arab nationalism remains a powerful force, and resentment of "uppity" Kurds simmers just beneath the surface. A resurgent Iraq could try to suppress Kurdish aspirations by force. Maliki appears firmly in the saddle, having outmanoeuvred his rivals. His security forces are becoming more cohesive and better armed, including with U.S.-made battle tanks and fighter jets.¹⁴² The struggle over hydrocarbon-rich disputed territories could be particularly fierce. Masoud Barzani's strident tone in March 2012, reminiscent of a vituperative exchange with Maliki in 2008-2009, suggests a sharp deterioration in Erbil's relationship with Baghdad.¹⁴³ Yet, at the end of the day, if companies holding contracts with the KRG are not paid, they will have little choice but to pull out.

¹⁴¹ For example, a critic said, referring to the Kurds' autonomy as well as their presence in the most senior ranks of the federal government, "the Kurds are saying, 'What is mine is mine, and what is yours belongs to both of us'. Many Iraqis are complaining now that the Kurds are overreaching, and they shouldn't be doing this". Crisis Group interview, Amman, 2 March 2012. Ashti Hawrami's response to that sentiment was: "When Baghdad talks about power-sharing, it is saying, 'we have the power and we will share it'. That's unacceptable". Presentation, Istanbul, 1 October 2010.

¹⁴² Iraq's military resurgence is an obvious source of concern for the Kurds. In an interview with Al-Hurra, the U.S. government Arabic-language TV station, in April 2012, Masoud Barzani complained that senior Iraqi officials and military commanders had recently discussed pushing back against the Kurds, pending arrival of U.S. F-16 fighter planes; suggested that the Kurds had paid a heavy price defending their identity and existence and warned that there is no military solution to the Kurdish issue; pledged that the Kurds will not resort to violence to press their claim for independence; and ended the interview by saying he hoped it would not come to war between Baghdad and Erbil. Al-Hurra TV, 5 April 2012, www.youtube.com/watch?v=LBSS_4kFBPw (part 1) and www.youtube.com/watch?v=NPRCg70-W-U (part 2).

¹⁴³ Barzani made his comments in a speech on the occasion of Nowruz, the Kurdish New Year in March 2012, op. cit. For the earlier exchange with Maliki, see Crisis Group Report, *Trouble Along the Trigger Line*, op. cit., pp. 1-3.

As for Turkey, it would stand to lose more than it would gain from giving up on Baghdad. It would end up in the Kurds' favoured scenario, therefore, only if dragged into it by force of circumstance. It will do much to prevent reaching the tipping point, starting with making a genuine attempt to overcome its evident distaste for the Maliki government in order to hold Iraq together. Its reticence toward getting more deeply involved in Syria without full-throttle Western (U.S. and NATO) support – compared with the more militant approach that Saudi Arabia and some of the other Gulf states appear to be pursuing – could open the way for accommodation with Maliki in the future. Ankara would do well to be explicit about its objectives and redlines in Iraqi Kurdistan in order to restrain the Kurds' unrealistic ambitions, because whatever happens in Syria (or Iran), the end of Iraq may not be nigh, even if the country is likely to face some turbulent times.

**Baghdad/Erbil/Washington/Brussels,
19 April 2012**

APPENDIX A
MAP OF IRAQ



APPENDIX B

MAP OF KRG OIL AND GAS CONCESSIONS WITH LEAD OPERATORS, AND GREEN LINE



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.

APPENDIX C

MAP OF NORTHERN OIL AND GAS FIELDS, KRG OIL AND GAS CONCESSIONS, AND GREEN LINE



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.

APPENDIX D

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