PLANNING FOR THE IRAQI PETROLEUM INFRASTRUCTURE:

Briefing for the Secretary of Defense

11 January 2003

Prepared by Energy Infrastructure Planning Group

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</tbody>
</table>
Guiding Principles

Certain principles should guide any temporary US/coalition administration of Iraqi petroleum resources, including:

- *Iraq's oil resources are an asset that belongs to all the Iraqi people.*
- *Any temporary administration of Iraqi oil production and marketing:*
  - Will seek to minimize disruptions and promote confidence and stability in world markets;
  - Should involve existing Iraqi personnel and organizations whenever possible to ease future transition;
  - Should work with the international community to build support for our policies;
  - Will respect Iraqi contracts previously approved by the United Nations (NB: Just service contracts, no development contracts);
  - Will be conducted transparently and accountably, in accordance with applicable legal norms and prudent industry practices, for the benefit of the Iraqi people;
  - Will prepare for the return of production and marketing responsibility to a stable Iraqi authority as soon as practicable.
- *The initial goal should be to bring Iraqi petroleum production up to pre-hostility capacity of about 3.1 million barrels/day, consistent with sound business considerations.*
- *Any increase in production levels and capacity should serve the interest of maximizing revenues for the people of Iraq.*
Public Diplomacy--Main Themes

- Iraqi petroleum resources are a national asset of all the Iraqi people, i.e., the nation as a whole, and not of any regional entity.
- We want to work with the Iraqis themselves and the international community in administering petroleum proceeds for the benefit of the Iraqi people.
- Interim administration decisions will be based on prudent, accountable, best practices to prepare for the return of the sector and its management to responsible Iraqi authorities.
- We will act, through our administration, so as not to prejudice Iraq's future decisions regarding:
  - Its oil development policies.
  - Its relations with international organizations.
  - The future ownership structure of the its oil industry.
- US/Coalition will fulfill its responsibility to the Iraqi people to create conditions of stability and well-being for the people of Iraq, but we will not administer oil assets on a long-term basis.
- Petroleum proceeds will be handled transparently and used for the benefit of the Iraqi people.
- We will respect the legitimate interests of all countries in the reconstruction period.
- We will respect Iraqi contracts previously approved by the United Nations.
Contingency Plans for Repair

- OUSD(P)/Energy Infrastructure Planning Group ("EIPG") manages planning.
- EIPG guidance to the Army contractor:
  - Plan for full range of damage scenarios: Little or no damage, to major disabling damage by Iraqi forces to key choke points (e.g., gas and oil separation plants, marine terminals, pumping stations).
  - Fight over 1,000 well fires, if necessary.
  - Repair priorities:
    - First, restore current production of about 2.4 million barrels per day as soon as conditions permit.
    - Second, restore current capacity of about 3.1 million barrels per day.
- Plan (draft) calls for modular components for major facilities (e.g., gas-oil separators, pumping stations) wherever needed, to restore production ASAP.
- "Best case" = No infrastructure damage, just safety repairs needed.
  - 6 mos. to 2.4 million b/d, 9 mos. to 3.1 million b/d.
  - Cost: approx. $0.8 Billion.
- "Worst case" = Major, disabling damage throughout infrastructure.
  - 20 mos. to 2.4, 30+ mos. to 3.1.
  - Cost: $7 to $8 Billion (oil only). Refineries and gas plants add another $4-5 Billion.
Contingency Plans for Production and Sale

- **Production priorities:**
  - First, crude oil.
  - Second, natural gas to support electrical grid.
  - Third, refined products (import during interim if necessary).

- **Build on “modular” approach.**
  - Pre-conflict: Profile all fields and facilities.
  - Post-conflict:
    - Rapidly assess production level achievable with whatever still works.
    - Assemble building-blocks of a functioning system with whatever still works.
    - Use all functioning production facilities to extent safe and cost effective.

- **Produce first where damage is least, to maximize early output.**

- **Sales:**
  - New USG-created organization to manage Iraqi oil assets (acronym: “IOTA”) uses personnel from Iraq’s State Oil Marketing Organization (SOMO) to extent available and reliable -- supplement with other nationals as needed.
  - IOTA approves terms and conditions of sales, within policies set by higher authority.
  - “Good Title”: SOMO and Iraqi Central Bank currently co-sign all oil sales contracts.
    - Standard terms include warranty of title.
    - Suggests need to maintain existence and operations of Iraqi Central Bank and SOMO.
      - Would continue to warrant good title to buyers.
      - Would help reassure markets, reduce likelihood of later disputes about validity of sales.
Organization and Management

- Deputies agreed to recommend establishing an organization dedicated solely to managing Iraqi petroleum industry.
  - Corporate organizational model ("Iraqi Oil Temporary Administration" -- "IOTA") drawing on current Iraqi Oil Ministry structure.
- To "internationalize," appoint:
  - Chairman
    - American.
    - Current or former statesman.
  - Chief Executive Officer.
    - British or other international.
    - Former chairman or CEO of oil company.
  - Vice Presidents for each functional sector within current Ministry.
    - Preferably Iraqis.
  - Board of Advisors.
    - Advisory only, non-binding on management.
    - Half composed of Iraqis, the rest could be international figures.

**Issues for Decision: Appointment, Reporting, Removal of Chairman, CEO.**
- Candidates vetted by PCC will go to Deputies/Principals for consideration (see Back Up Slide).
- Chairman, CEO will recommend to USG the candidates for Board of Advisors.
- **Recommend:** SecDef appoints and removes Chairman, CEO (with White House coordination).
- **Recommend:** Chairman reports to top civil administrator; CEO reports to Chairman.
- **Recommend:** Chairman hires/fires anyone below CEO, in consultation with top civil administrator.

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Petroleum Proceeds: Possible Uses and Availability

- Figures below exclude high end range of humanitarian needs and unaddressed Gulf War claims. When possible, (average) annual numbers are provided.
- Humanitarian aid, military campaign and occupation costs -- about 1 year; others vary from about 2 to 10 years or more.
- **Bottom Line:** Demands on petroleum revenue will likely exceed available funds for foreseeable future.

<table>
<thead>
<tr>
<th>RANGE OF POTENTIAL FINANCIAL DEMANDS (in $ billions)</th>
<th>Low</th>
<th>High</th>
</tr>
</thead>
<tbody>
<tr>
<td>Humanitarian Aid (minimum) -- Humanitarian Planning Group</td>
<td>16</td>
<td>16</td>
</tr>
<tr>
<td>Reconstruction of War-Damaged Eco. (annual avg) -- CIA</td>
<td>3</td>
<td>4</td>
</tr>
<tr>
<td>Restore prewar oil production capacity (initial) -- CIA/Industry</td>
<td>1</td>
<td>8</td>
</tr>
<tr>
<td>Expand oil capacity to 3.6 million b/d (additional) -- CIA/Industry</td>
<td>3</td>
<td>5</td>
</tr>
<tr>
<td>Expand oil capacity to 5-8 million b/d (annual avg) -- CIA/Industry</td>
<td>1</td>
<td>4</td>
</tr>
<tr>
<td>Foreign Debt Payment (annual) -- CIA</td>
<td>7</td>
<td>15</td>
</tr>
<tr>
<td>Gulf War Claims (annual) -- CIA/State</td>
<td>5</td>
<td>7</td>
</tr>
<tr>
<td>Costs of Occupation (annual) -- CBO</td>
<td>48</td>
<td>48</td>
</tr>
<tr>
<td>Costs of Military Campaign (total) -- CBO/House Budget Comm., Dem staff</td>
<td>30</td>
<td>60</td>
</tr>
<tr>
<td><strong>TOTAL DEMAND</strong></td>
<td><strong>114</strong></td>
<td><strong>167</strong></td>
</tr>
</tbody>
</table>

**TOTAL ANNUAL PETROLEUM PRODUCTION REVENUE**

<table>
<thead>
<tr>
<th>Low</th>
<th>High</th>
</tr>
</thead>
<tbody>
<tr>
<td>16</td>
<td>25</td>
</tr>
</tbody>
</table>

**BALANCE**

<p>| | |</p>
<table>
<thead>
<tr>
<th></th>
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</tr>
</thead>
<tbody>
<tr>
<td>-98</td>
<td>-142</td>
</tr>
</tbody>
</table>

* Based on 2.4 million b/d of oil production and an $18-28/bbl average price
Funding Enhancement: Borrow Against Future Oil Revenues?

- Major issues:
  - Recent Iraqi oil revenues may not support major loans (i.e., billions of dollars) without new development contracts in place to back them up.
  - Who would borrower be during temporary administration? Iraqi Central Bank? Would it still exist and function?
  - New lender(s) likely to demand subordination of pre-existing debt and third-party guarantors (other governments?).
  - Likely to require rescheduling Iraq's existing foreign debt (about $82 billion at end 2002 assuming 6% interest rate).
  - Iraq also owes $27 billion in unpaid claims awarded by UN Compensation Commission for Gulf War damages.
Iraqi Production Goals: Initial Objective

Bring production up to prewar capacity level of about 3.1 million barrels/day (b/d).

We have contingency plans to do this (see Slides 5 and 6).

- Current actual production: 2.4 million b/d.
  - Annual revenue with $18-28/barrel average price range: $16-25 B.

- Current production capacity: 3.1 million b/d (CIA).
  - Some in private sector say sustainable capacity closer to 2.8 million barrels/day (b/d), with significant rehabilitation needed to reach 3.1.
  - Investment needed to sustain: $1-8 B over 6-20 months, depending on damage level (based on CIA and industry estimate).

- Iraq a member of OPEC but has not been in quota system since Gulf War.
Enable Iraq to regain its historical capacity.

- 3.6 million b/d.
  - Likely to require high repair, maintenance and upgrade of existing fields, possible development of new fields.
  - Reachable about one year after obtaining 3.1 million b/d.
  - Cost: additional $3-5 billion over 3.1 million b/d level (industry estimate).
Iraqi Production: Long-Term Objective

Allow Iraq to achieve economically reasonable increase in capacity.

- Would exceed 5 million b/d.
  - Requires development of new fields.
  - About 5 million b/d reachable within 3-5 years with investments of around $30 B (CIA and industry estimate).
Increasing Iraqi Production: Considerations

Advantages

- Speeds Iraqi rehabilitation and stability.
- Supported by many in Iraqi opposition.
- Puts long-term downward pressure on price.
- Helps consumers.
- Diversifies/increases global oil supply and spare production capacity in long-term, if no price war.
  - Strengthens global economic security.
  - Only 3.7 million b/d of global spare capacity (CIA), or 5% of demand.
  - Saudis have 2/3 of global spare capacity.

Disadvantages

- Politically controversial, especially if new fields are developed.
- Might trigger a price war, which would likely decrease Iraqi oil revenues and could drive out higher-cost producers, thus reducing diversity of supply.
- Some would argue that new Iraqi government should decide.
Contract Policy

- **Existing deals:** IOTA should observe contracts previously approved by UN. **Query whether should observe those made in hopes sanctions eventually would be lifted?**
  - Four "fee-for-service" maintenance contracts (three Russian companies, one Turkish) currently approved by UN under OFF. (See Back Up Slide).
  - Iraq has signed about four capacity expansion contracts (Chinese CNPC, Petro Vietnam, Tunisian ETAP, maybe Syrian Oil Co.), which await lifting of UN sanctions.
    - French Total Fina Elf initialed but reportedly not yet signed.
    - Iraq recently abrogated Russia's Lukoil contract.
  - Over 60 foreign companies pursued various stages of oil negotiations since sanctions were imposed.
  - Iraqi opposition opposed to honoring deals made by Saddam unless clearly in Iraqi interests.
    - Better to defer these for new Iraqi government to decide.
  - US and British companies were not allowed to do this.

- **New deals:** *As a rule, should be based only on economic return, open competition, and sound business practices.*
  - IOTA will likely need to contract with foreign companies -- whether to expand production capacity or to maintain existing capacity.
    - Repairs from war damage, safety upgrades, normal operations and maintenance.
  - Should be governed by sound business decisions unless compelling reasons otherwise.
  - *Generally let IOTA management run it like a business.*

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Next Steps

- Brief DC next week, PC soon thereafter.
- Promptly appoint management of IOTA.
- Proposal early next week that you appoint Army as Executive Agent.
- Proposal to you next week for pre-positioning assessment teams, fire-fighting and other critical equipment.
- Within 2 weeks present final draft of detailed continuity-of-oil operations plans for your review.
Back Up
**Prep Task: Pre-position Contractor Equipment and Personnel, Sustain Planning**

### Costs of Prep Task

<table>
<thead>
<tr>
<th>Item</th>
<th>$ Millions</th>
</tr>
</thead>
<tbody>
<tr>
<td>Firefighting (4 sets) &amp; Well Testing Equipment</td>
<td>23.3</td>
</tr>
<tr>
<td>Planning Sustainment/Advance Party</td>
<td>3.3</td>
</tr>
<tr>
<td>Assessment Teams (Hire, Train &amp; Move)</td>
<td>4.1</td>
</tr>
<tr>
<td>Firefighting Teams Movement</td>
<td>0.4</td>
</tr>
<tr>
<td>Firefighting &amp; Oil Spill LNO's with CENTCOM</td>
<td>0.6</td>
</tr>
<tr>
<td>Engineering of long lead items (GOSP's &amp; pipeline pumps)</td>
<td>2.0</td>
</tr>
<tr>
<td>Freight/Insurance</td>
<td>3.8</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>37.5</strong></td>
</tr>
</tbody>
</table>

- Pre-position firefighting and well testing equipment.
- Rapid damage assessment from maritime and river oil spills and remediation plan development.
- Rapid deployment of facility assessment teams.
- Rapid deployment of wellhead assessment equipment.
- Sustain ongoing planning effort.
- Pre-position personnel and equipment to support rapid deployment.
Iraq's Share of OPEC Production

- IRAQ'S SHARE OF OPEC PRODUCTION 2002
  - IRAQ
  - 9%
  - REST OF OPEC
  - 91%

- IRAQ'S SHARE OF OPEC PRODUCTION 1990
  - IRAQ
  - 15%
  - REST OF OPEC
  - 85%

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## Awarded Contracts

<table>
<thead>
<tr>
<th>Country/Company</th>
<th>Oilfield(s) (potential production)</th>
<th>Type of Contract</th>
<th>Status</th>
<th>Details</th>
<th>Voidable</th>
</tr>
</thead>
<tbody>
<tr>
<td>Russia</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Lukoil Consortium</td>
<td>West Qurnah Phase 2 (600,000 b/d)</td>
<td>Production Sharing</td>
<td>Signed in 1997; Unilaterally cancelled by Iraq on 02 Dec</td>
<td>Consortium includes Lukoil (majority holder), Mashinomreport, and Zarubezhneft</td>
<td>Voided</td>
</tr>
<tr>
<td>Talnait</td>
<td>Say Hassan (90,000 b/d)</td>
<td>Service Contract</td>
<td>Approved by UN</td>
<td>Service contract to drill wells; employees on the ground as of October 2002</td>
<td>Difficult</td>
</tr>
<tr>
<td>Saddam</td>
<td>Saddam (300,000 b/d)</td>
<td>Service Contract</td>
<td>Approved by UN</td>
<td>Service contract to drill wells; employees on the ground as of October 2002</td>
<td>Difficult</td>
</tr>
<tr>
<td>&quot;South of Basrah&quot;</td>
<td>Service Contract</td>
<td>Unclear if submitted to UN</td>
<td>Service contract to drill 15 wells signed; could be referring to Az Zubair or possibly West Qurnah</td>
<td>Unclear</td>
<td></td>
</tr>
<tr>
<td>Zarubezhneft</td>
<td>Karkuk - Khurmala Dorte (120,000 b/d)</td>
<td>Service Contract</td>
<td>Unclear if submitted to UN</td>
<td>Service contract to drill 45 wells signed</td>
<td>Unclear</td>
</tr>
<tr>
<td>Zangas</td>
<td>West Qurnah Phase 1 (300,000 b/d)</td>
<td>Service Contract</td>
<td>Approved by UN</td>
<td>Service contract for water injection</td>
<td>Difficult</td>
</tr>
<tr>
<td>China</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>China National Petroleum Corp (CNPC)</td>
<td>Production Sharing</td>
<td>Signed in 1998; No indication of work in progress</td>
<td>NFI</td>
<td>Unclear</td>
<td></td>
</tr>
</tbody>
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## Awarded Contracts (cont.)

<table>
<thead>
<tr>
<th>Country</th>
<th>Company</th>
<th>Description</th>
<th>Details</th>
</tr>
</thead>
<tbody>
<tr>
<td>Syria</td>
<td>Syrian Petroleum</td>
<td>Development Contract (Noor)</td>
<td>Unclear; Conflicting reports in late 2001; Initial contract cancelled by Iraq, according to Sept. 2001 Humint reports, new contract drafted, set to be notarized, according to Sep./Dec. 2001 Humint reports</td>
</tr>
<tr>
<td>Tunisia</td>
<td>ETAP (Enterprise</td>
<td>Kabb (40,000 b/d) Development Contract</td>
<td>Contract signed, according to Iraqi media; NFI; Unclear.</td>
</tr>
<tr>
<td></td>
<td>Tunisienne</td>
<td>Actuelle Petroleum)</td>
<td></td>
</tr>
<tr>
<td>Turkey</td>
<td>TPAO</td>
<td>Karbala - Khurmulti Service Contrack</td>
<td>Approved by UN; Service contract to drill 22 wells; Difficult</td>
</tr>
<tr>
<td>Vietnam</td>
<td>PetroVietnam</td>
<td>Amara Service Contract (50,000 b/d)</td>
<td>Contract signed, according to Iraqi media; NFI; Unclear</td>
</tr>
<tr>
<td>France</td>
<td>Total Fire St.</td>
<td>Nam, Umar (440,000 b/d) Development Contrack</td>
<td>Contract reportedly initiated but not signed; Reports: Terms not competitive, TEP would get unusually high rate of return; Unclear</td>
</tr>
</tbody>
</table>

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