OPEC ON THE MARCH

Why Iraq still sells its oil à la cartel

By Greg Palast

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Two years and $154 billion into the war in Iraq, the United States has at least one significant new asset to show for it: effective membership, through our control of Iraq's energy policy, in the Organization of the Petroleum Exporting Countries (OPEC), the Arab-dominated oil cartel.

Just what to do with this proxy power has been, almost since President Bush's first inaugural, the cause of a pitched battle between neoconservatives at the Pentagon, on the one hand, and the State Department and the oil industry, on the other. At issue is whether Iraq will remain a member in good standing of OPEC, upholding production limits and thereby high prices, or a mutinous spoiler that could topple the Arab oligopoly.

According to insiders and to documents obtained from the State Department, the neocons, once in command, are now in full retreat. As of today, Iraq's system of oil production, after a year of failed free-market experimentation, is being re-created almost entirely on the lines originally laid out by Saddam Hussein. Even Hussein's Baathist technocrats are back at the helm of the Ministry of Oil and the State Oil Marketing Organization.

Under the quiet direction of U.S. oil company executives working with the State Department, the Iraqis have discarded the neocon vision of a laissez faire, privatized oil operation in favor of one shackled to quotas set by OPEC, which have been key to the 121 percent rise in oil prices since the beginning of 2002. This rise is estimated to have cost the U.S. economy 1.2 percent of its GOP, or a fourth of its total growth during that period.

Given this economic blow, and given that OPEC states account for 46 percent of America's oil imports, it may seem odd that the United States' "remaking" of Iraq would allow for a national oil company that props up OPEC's price gouging. And in fact the original scheme for reconstruction, at least the one favored by neoconservatives, was to privatize Iraq's oil entirely and thereby undermine the oil cartel.

One intellectual godfather of this strategy was Ariel Cohen of the Heritage Foundation, who in September 2002 published (with Gerald P. O'Driscoll, Jr.) a post-invasion plan, "The Road to Economic Prosperity for a Post-Saddam Iraq," that put forward the idea of using Iraq to smash OPEC. Cohen recently explained to me how such an extraordinary geopolitical feat might be accomplished.

OPEC maintains high oil prices by suppressing production through a quota system effectively imposed on each member by Saudi Arabia, which reigns by dint of its overwhelming reserves.

The Saudis, to maintain their control on pricing, must keep a lid on production from other members-particularly Iraq, which has the second greatest proven reserves. Under Saddam Hussein, Iraq adhered to the OPEC quota limit (historically set to equal Iran's, now 3.96 million barrels a day) via state ownership of all fields. Cohen reasoned that if Iraq's fields were broken up and sold off, a dozen competing operators would quickly crank up production from their individual patches to the maximum possible, swiftly raising Iraq's total output to 6 million barrels a day. This extra crude would flood world petroleum markets, OPEC would devolve into mass cheating and overproduction, oil prices would fall over a cliff, and Saudi Arabia-both economically and politically-would fall to its knees.

By February 2003, Cohen's position had been enshrined as official policy, in the form of a hundred-page blueprint for the occupied nation titled, "Moving the Iraqi Economy from Recovery to Sustainable Growth"-a plan that generally embodied the principles for postwar Iraq favored by Defense Secretary Donald Rumsfeld, Deputy Secretary Paul Wolfowitz, and the Iran-Contra figure Elliott Abrams, now Deputy National Security Adviser.

Nominally written by a committee of Defense, State, and Treasury officials, the blueprint was in fact the brainchild of a platoon of corporate lobbyists, chief among them the flat tax fanatic Grover Norquist. From overhauling tax rates to rewriting copyright law, the document mapped out a radical makeover of Iraq as a free-market Xanadu-a sort of Chile on the Tigris-including, on page 73, the selloff of the nation's crown jewels: "privatization ... [of] the oil and supporting industries."!

Following the U.S. military's swift advance to Baghdad, those skeptical of the neocon plan were summarily brushed aside. Chief among the castoffs was General Jay Garner, the short-lived occupation viceroy who on the very night he arrived in Baghdad from Kuwait received a call from Rumsfeld informing him of his dismissal. When I met with Garner last March at the Washington offices of Sy Coleman, the giant security firm he now heads, he told me that he had resisted imposing on Iraqis the plan's sell-off of assets, especially the oil. "That's just one fight you don't have to take on right now," he said. "You don't want to end the day with more enemies than you started with."

In plotting the destruction of OPEC, the neocons failed to predict the virulent resistance of insurgent forces: the U.S. oil industry itself.

From the outset of the planning for war, U.S. oil executives had thrown in their lot with the pragmatists at the State Department and the National Security Council. Within weeks of the first inaugural, prominent Iraqi expatriates- many with ties to U.S. industry- were invited to secret discussions directed by Pamela Quanrud, an NSC economics expert now employed at State. "It quickly became an oil group," one participant, Falah Aljibury, told me. Aljibury, an adviser to Amerada Hess's oil trading arm and to investment banking giant Goldman Sachs, who once served as a back channel between the United States and Iraq during the Reagan and George H. W. Bush administrations, cut ties to the Hussein regime following the invasion of Kuwait.

The working group's ideas about the war had been far less starry-eyed than those of the neocons. "The petroleum industry, the chemical industry, the banking industry-they'd hoped that Iraq would go for a revolution like in the past and government was shut down for two or three days," Aljibury told me. "You have a martial law ... and say Iraq is being liberated and everybody stay where they are ... *Everything as is."* On this plan, Hussein would simply have been replaced by some former Baathist general.

One candidate was General Nizar Khazraji, Saddam's former army chief of staff, who at the time was under house arrest in Denmark pending charges for war crimes. (Khazraji was seen in Iraq a month after the U.S. invasion, but he soon disappeared and has not been heard from since.) Roughly six months before the invasion, the Bush Administration designated Philip Carroll to advise the Iraqi Oil Ministry once U.S. tanks entered Baghdad. Carroll had been CEO of both Fluor Corporation, now a major contractor in Iraq, and, earlier, of Royal Dutch/Shell's U.S. division. In May 2003, a month after his arrival in Iraq, Carroll made headlines when he told the *Washingron Post* that Iraq might break with OPEC: "[Iraqis] have from time to time, because of compelling national interest, elected to opt out of the quota system and pursue their own path .... They may elect to do that same thing. To me, it's a very important national question." Carroll later told me, though, that he personally would not have been supportive of privatizing oil fields. "Nobody in their right mind would have thought of doing that," he said.

Soon after Carroll resigned his post in September 2003, the new provisional government appointed an oil minister, Ibrahim Bahr al-Ulourn. Uloum (who had been maneuvered into the job by then-neocon favorite Ahmad Chalabi) quickly fired Muhammad al-Jiburi, chief of Iraq's State Oil Marketing Organization, and Thamer Ghadhban, the expert in charge of the southern oil fields, both of whom had been trusted by the Western oil industry.

Production faltered from a combination of incompetence, wholesale theft (Iraq's oil was unmetered), sabotage, and corruption that one oil man told me was "rampant," with "direct payoffs to government officials by commercial operators."

With pipelines exploding daily, the fantasy of remaking Iraq's oil industry also went up in flames. Carroll was replaced by another Houston oil chieftain, Rob McKee, a former executive vice-president of ConocoPhillips and currently the chairman-even during his tenure in Baghdad-of Enventure, an oil-drilling supply subsidiary of the Halliburton Corporation. McKee had little tolerance for the neocons' threat to privatize the oil fields. A close associate of McKee's and the executive adviser to Hess's trading arm, Ed Morse, told me that "Rob was very promotive of putting in place a really strong oil company," even if he had to act over the objections of the Iraqi Governing Council. Morse, who says he takes as many as six calls a day from the Bush Administration regarding Iraq, is one of the men to whom Washington turns to obtain the views of Big Oil. Like Carroll and McKee, Morse sneers at what he calls "the obsession of neo-conservative writers on ways to undermine OPEC." Iraqis, says Morse, know that if they pump 6 million barrels a day, i.e., 2 million above their expected OPEC quota, "they will crash the oil market" and bring down their own economy.

In November 2003, McKee quietly ordered up a new plan for Iraq's oil. The drafting would be overseen by a "senior adviser," Amy Jaffe, who had worked for Morse when he held the formidable title of Chairman of the Council on Foreign Relations-James Baker III Institute Joint Committee on Petroleum Security. Jaffe now works for Baker, the former Secretary of State, whose law firm serves as counsel to both Exxon-Mobil and the defense minister of Saudi Arabia. The plan, nominally written by State Department contractor BearingPoint, was guided, says Jaffe, by a handful of oil industry consultants and executives.

For months, the State Department officially denied the existence of this 323-page plan for Iraq's oil, but when I identified the document's title from my sources and threatened legal action, I was able to obtain the complete report, dated December 2003 and entitled *Options far Developing a Long Term Sustainable Iraqi Oil Industry.* The multi-volume document describes seven possible models of oil production for Iraq, each one merely a different flavor of a single option: the creation of a state-owned oil company.

The seven options ranged from the Saudi Aramco model, in which the government owns the whole operation from reserves to pipelines, to the Azerbaijan model, in which the state-owned assets are operated almost entirely by "IOCs" (International Oil Companies).

The drafters had little regard for the "self-financing" system, such as Saudi Arabia's, which bars IOCs from the fields; they prefer the production-sharing agreement (PSA) model, under which the state maintains official title to the reserves but operation and control are given to foreign oil companies.

These companies then manage, fund, and equip crude extraction in exchange for a percentage of sales receipts. While promoting IOC control of the fields, the authors take care to warn the Iraqi government against attempting to squeeze IOC profits: "Countries that do not offer risk-adjusted rates of return equal to or above other nations will be unlikely to achieve significant levels of investment, regardless of the richness of their geology." Indeed, to outbid other nations for Big Oil's favor will require Iraq to turn over quite a large share of profits, especially when· competing against countries such as Azerbaijan that have given away the store. The Azeri government, notes the report, has "been able to partially overcome their risk profile and attract billions of dollars of investment by offering a contractual balance of commercial interests within the risk contract." This refers to the fact that Azerbaijan, despite its poor oil quality and poor location, drew in the IOCs via scandalous splits of revenue allowed by the nation's corrupt government.

Given how easily the interests of OPEC and those of the IOCs can be aligned, it is certainly understandable why smashing the oil cartel would not strike oilmen as a good idea. In 2004, with oil approaching the $50- a-barrel mark all year, the major U. S. oil companies posted record or near record profits. ConocoPhillips, Rob McKee's company, this February reported a doubling of its quarterly profits from the previous year, which itself had been a company record; Carroll's former employer, Shell, posted a record-breaking $4.48 billion in fourth-quarter earnings.

ExxonMobil last year reported the largest one-year operating profit of any corporation in U.S. history.

When I talked to Ariel Cohen at Heritage, his dream of smashing OPEC in shambles, he blamed the State Department for acquiescing to the Saudis and to Russia, which also benefits from selling oil at high OPEC prices.

The poisonous policies were influenced, he said, by "Arab economists hired by the State Department who are basically supporting the witches' brew of the Saudi royal family and the Soviet *ostblock* ... because the Saudis are interested in maximizing their market share and they're not interested in fast growth of the Iraqi output."

According to Morse, the switch to an OPEC-friendly policy for Iraq was driven by Dick Cheney himself. 'The person who is most influential in running American energy policy is the Vice President," who, says Morse, "thinks that security begins by ... letting prices follow wherever they may."

Even, I asked, if those are artificially high prices, set by OPEC? "The VP's office [has] not pursued a policy in Iraq that would lead to a rapid opening of the Iraqi energy sector ... so they have not done anything, either with producers or energy policy, that would put us on a track to say, 'We're going to put a squeeze on OPEC.'"

Today, the old interim oil minister, Uloum, has been replaced by the very men he removed: Muhammad al-Jiburi, now minister of trade, and Thamer Ghadhban, now oil minister.

And Dick Cheney, far from "putting the squeeze on OPEC," has taken a de facto seat there, allowing the cartel to maintain its own, suffocating grip on the U.S. economy.