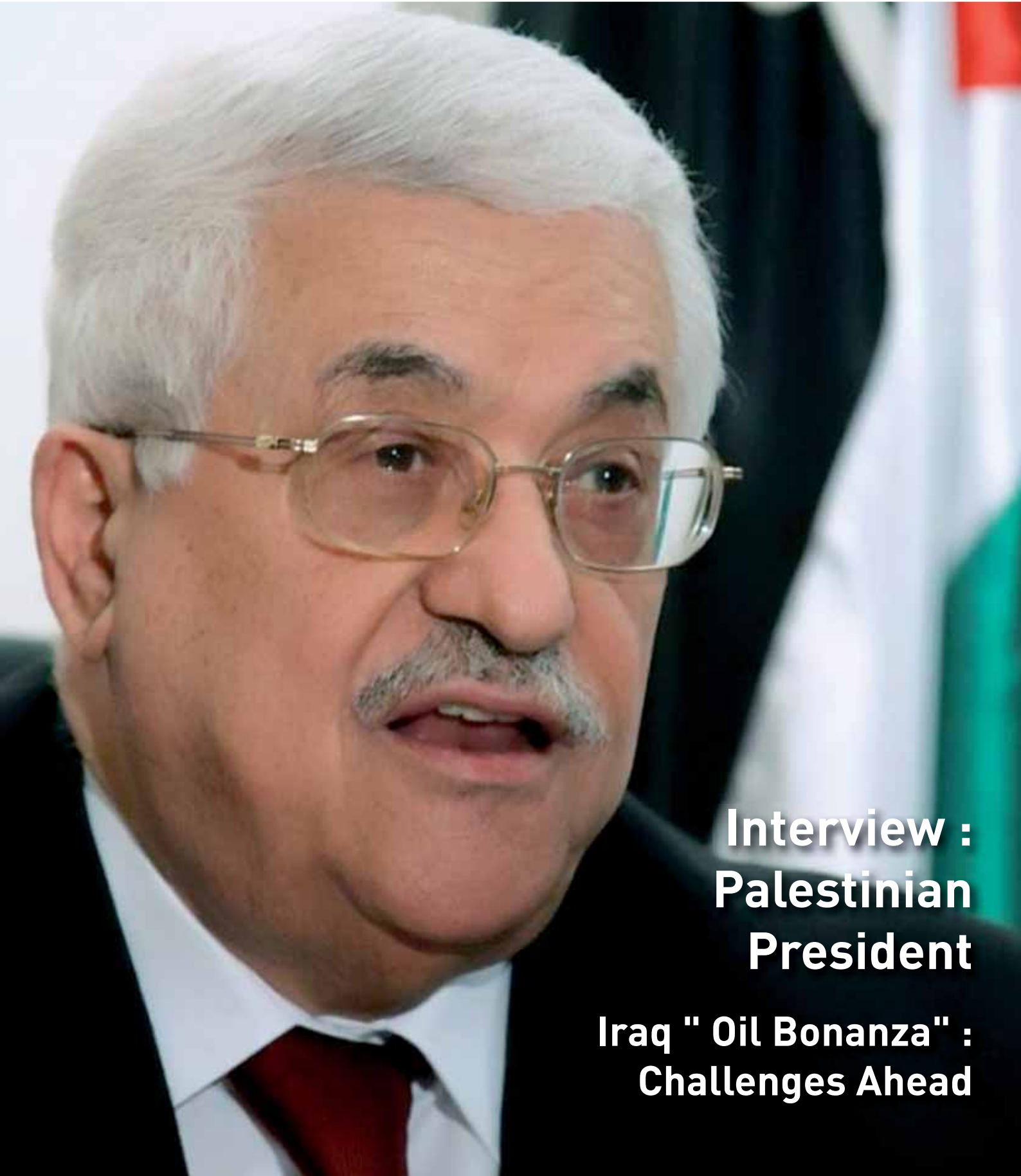


ENERGY & GEOPOLITICAL RISK

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**Interview :
Palestinian
President**

**Iraq " Oil Bonanza" :
Challenges Ahead**

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EDITORIAL

The Palestinian- Israeli conflict has been at the core of Middle East problems for over half-a-century, lacking a pragmatic and just resolution. The MEES interview with Palestinian State President Mahmoud Abbas (Abu Mazin) sheds light on the current state of the negotiations process, undertaken by the US, and the Palestinian position. President Abbas told MEES that the Palestinian aim and strategy is “the establishment of an independent state on the 1967 borders, that is the West Bank and the Gaza Strip, with East Jerusalem as its capital. We reject any solution based on a state with temporary borders.” Mr. Abbas added that the Palestinian adherence to peace is a strategic choice, and that they have welcomed President Barak Obama’s position on the two-state solution. However, the Palestinian President added, it is futile and meaningless to resume peace negotiations if the Israeli policy of building more settlements in East Jerusalem and the West Bank continues, “because this is a policy imposing a fait accompli and prejudging the results of future negotiations... Once Israel stops its settlement activities, particularly in East Jerusalem, and adheres to its Road Map commitments, we will be ready to resume negotiations.”

The next two articles, by Iraqi specialists, consider some of the challenges confronting the ambitious Iraqi oil plans to increase production capacity to 12mn b/d by 2017. The first article, by Tariq Alhaimus, formerly with the IBRD and the IMF, reviews the impact of the lack of governance and effective bureaucracy on the expected “oil bonanza.” Mr. Alhaimus , cautions observers of the Iraqi scene that they “should not underestimate the monumental and deeply entrenched obstacles and uncertainties” as a result of the lack of governance and deeply dysfunctional institutional structure of the country “that inhibits the carrying out of any credible economic transformation, and the now rampant corruption that provides a recipe for plundering future resources.” The author has been undertaking research on the subject for around two decades and recently published his research in a book published in Arabic. The second article by Zainab Al-Assam reviews the opaque condition of IOCs’ in Iraq’s Kurdistan Region, whereby the firms have contracts negotiated with the Kurdistan Regional Government (KRG) that entitles them to undertake E&P and development of fields but not export oil and gas through the federal pipeline grid. The author concludes that the problem is part of many differences between the KRG and the federal government in Baghdad over interpretation of the constitution as to the authorities of the federal and regional governments in the oil sector, and that the on-and-off again permits to export oil from the Kurdistan Region is no solution to the problem, which still awaits a global understanding between Irbil and Baghdad.

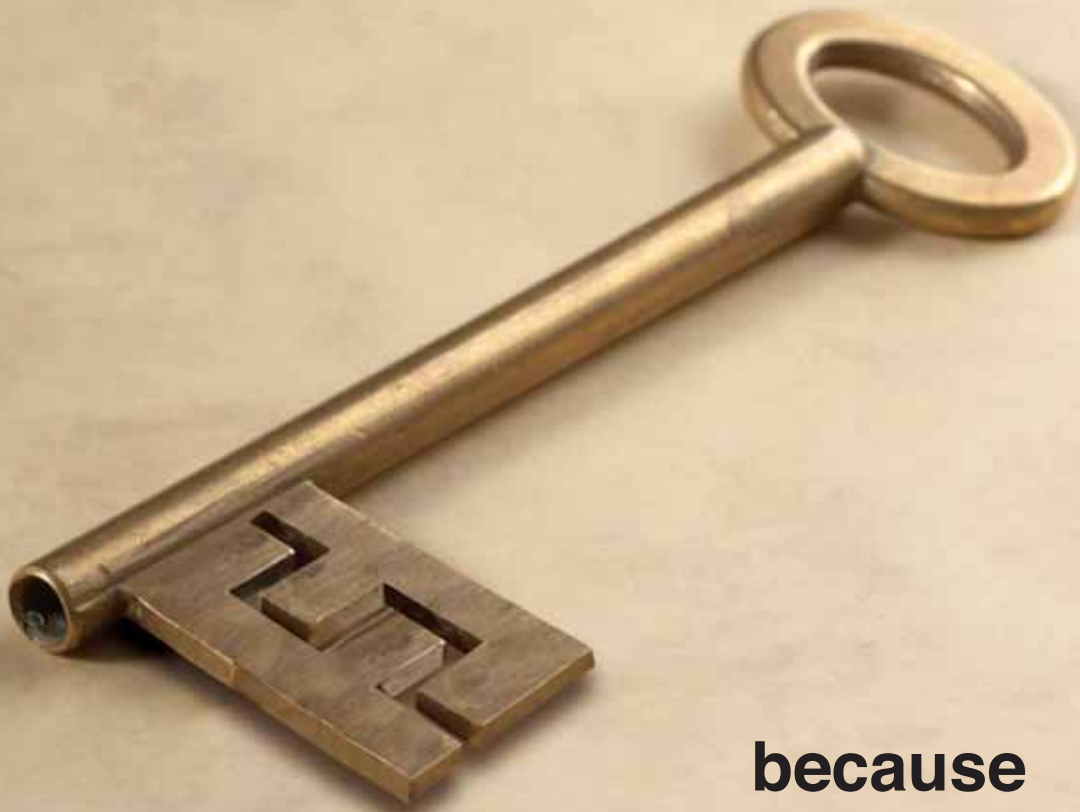
The last three items are about various regional water-related issues. The Nile River Basin Countries have failed once more to agree on a new Nile River Basin Framework. The differences are between Egypt and Sudan, on one hand, and the resource countries, on the other, according to Salah Nasrawi of the Associated Press reporting from Cairo in early April. A future meeting is planned, but the differences are substantive. Meanwhile, Qatar, similar to other GCC states, depends on constructing more desalination plants to meet the rising water consumption because of increasing population and rising standards of living in the country and the region as a whole. Finally, Professor David Holland, Director of the Center for Atmosphere-Ocean Science at New York University, told the Gulf News, during a lecture visit to Abu Dhabi that “the current sea rise projection need to be perfected, most importantly regarding the melting of the Greenland and Antarctica ice sheets,” adding that, since a modest sea level rise could spell trouble for low-lying cities such as Abu Dhabi.

Walid Khadduri



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INTERVIEW WITH PALESTINIAN PRESIDENT MAHMOUD ABBAS



Mr. President, how do you evaluate the results of the Arab summit in Libya?

It was a successful summit. The resolutions adopted are satisfactory to us, especially concerning financial and political support for Jerusalem. The Arab leaders decided to allocate a budget of 500 million dollars to Jerusalem, in order to support the steadfastness of our people in the Holy City against Israel's policy of land confiscation and house demolitions and its continuous attempts to change the city's Muslim and Christian character by building more and more Jewish settlements. We are satisfied with the Arab leaders' awareness of the necessity to bear their responsibility towards Jerusalem. We are hopeful that these resolutions will be implemented soon by the Arab League. On our part, we stressed that peace cannot be achieved unless the Israeli occupation of our land, including East Jerusalem, is terminated, and an independent Palestinian state is established on the 1967 borders, according to UN resolutions and international legitimacy.

Are you optimistic that the peace process can be resumed soon, given Israel's declared position on Jerusalem following the recent meeting between President Obama and Prime Minister Netanyahu?

We have repeatedly declared our adherence to peace as a strategic choice. We have welcomed President Obama's position on the two-state solution and his declared position against the illegal Israeli settlement activity in the West Bank and in East Jerusalem. We have also welcomed the Quartet's declaration in Moscow last March. And we are still faithful to the text and spirit of the Arab Peace Initiative. But we have made it clear to the international community that the resumption of negotiations is futile and meaningless if Israel continues its policy of building more and more settlements in East Jerusalem, because this is a policy of imposing a *fait accompli* and prejudging the results of future negotiations. Our position has been



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explained to, and accepted by, the international community. We have informed Mr. Obama's administration of our position on this matter, and we are waiting for a response in the near future. Once Israel stops its settlement activities, particularly in East Jerusalem, and adheres to its Road Map commitments, we will be ready to resume negotiations.

Will these be direct or indirect negotiations?

As you know, in early March the American administration presented a proposal for indirect negotiations for a period of four months. We took this proposal to the follow-up committee of the Arab League and it was accepted. But then the Israeli government announced a new plan to build 1600 housing units in a Jewish settlement in East Jerusalem. We rejected this decision and considered it a major obstacle to the resumption of negotiations. We conveyed our position to the international community and asked the Obama administration to intervene for the sake of the peace process. Once this decision is revoked by Israel, we are ready to engage in the rapprochement talks proposed by the US envoy, George Mitchell, who made it clear in his proposal that these negotiations will have a clear point of reference and a clear goal, as set by the international community, and will cover the final status issues. Mr. Mitchell also determined a period of 24 months during which all final status issues can be negotiated, beginning with the issue of borders, which can be concluded within four months.

What are your alternatives in case the status quo is prolonged by Israel's refusal to resume the peace process?

Our aims and strategy are clear and have been publicly declared. We seek the establishment of an independent Palestinian state on the 1967 borders, that is the West Bank and the Gaza Strip, with East Jerusalem as its capital. We reject any solution based on a state with temporary borders. We are in full coordination with our Arab brothers, and we have sought and achieved the direct engagement of the Arab League. We will make sure that any decision of ours will have the complete endorsement of the Arab League. We will ask the Arab League and the Islamic Conference Organization to resort to the UN Security Council and all other international forums to seek an international denunciation of Israel's unilateral measures.

There is considerable evidence that Israel is going full speed ahead in changing the nature of Jerusalem. What is your government doing about it before it becomes a fait accompli?

We are seeking international protection for Jerusalem's Arab character, particularly the preservation of its Muslim and Christian holy places. We are soliciting UNESCO's intervention against Israel's intention to declare more than 150 historic sites in the Palestinian territories as belonging to the Jewish heritage. If not reversed, and if such planned actions continue, I believe severe consequences may occur in the future.

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The systematic and gradual usurpation of Palestinian culture by Israeli governments and their military might is tantamount to daylight highway robbery. The planned cultural encroachment represents a criminal extension of land usurpation and ethnic cleansing by the occupying forces.

Do you expect violence to erupt?

Our people have a legitimate right to resist the Israeli occupation and seek their freedom and independence. This resistance can take many forms within the context of international legitimacy, among which is non-violent popular resistance. We have declared that in current conditions an armed confrontation with Israel does not serve our national interests – and this awareness is growing among all Palestinian factions - and we adhere by our commitments to a peaceful negotiated solution.

Are you optimistic about national reconciliation with Hamas?

National reconciliation is our top priority. We have responded positively to every relevant initiative from our Arab brothers on this issue, and we held endless sessions of talks with Hamas for many months under Egypt's auspices. We have displayed all good will. This situation is the result of the Hamas coup d'état in June of 2007, but it cannot and must not continue. We need to lift the illegal and inhuman siege imposed by Israel against our people in Gaza, and Israel has masterfully exploited the conditions created by that coup. As long as there is no retreat from that position I believe the unacceptable and inhumane conditions in Gaza will worsen. Our people everywhere deserve better. Egypt presented a written proposal, which was endorsed by the Arab League. I personally proposed to the Fatah Central Committee to accept this proposal, despite our reservations and remarks, and the Egyptian document was signed by Fatah upon my personal instructions. But Hamas is still refusing to sign. We call on Hamas to abandon serving regional agendas and to uphold the national interests of the Palestinian people. We do not want to resolve this crisis with Hamas by resorting to an armed confrontation, which will only weaken our national cause. We must resort to the people and let our people decide through democratic elections, so as to preserve our national unity. This division serves only Israel and gives its governments a breathing space to carry out their plans to prolong the occupation with all its painful impact on the Palestinian people, as well as to reinforce their presence in the remaining parts of Palestine. Our reconciliation despite our differences will boost our international efforts to promote our national goals and aspirations. Let us not fall in the quicksands of power where the more we struggle the deeper we sink, leaving the Palestinian people in a state of bewildered diaspora even in their own legitimate homeland.

What kind of a Palestinian state do you envisage?

Our vision is to establish an independent, viable and geographically connected sovereign state on the 1967 borders, that is in the West Bank and Gaza, with East Jerusalem as its capital. A just solution for the rights of Palestinian refugees according to international resolutions is part and parcel of our objective. Law and democracy will be the cornerstones of the state's constitution. The responsibility of its democratically elected government will be to protect all its citizens, irrespective of race, gender or faith, and ensure the development of their welfare within a system of law that is based on justice and equal rights for all citizens. A state that lives in peace and harmony with all its neighbors, Israel included. We have already taken important steps in building the institutions of our future state. Let me remind you that Palestine is not short of Palestinian brain power in all the fields necessary for the successful performance of the state and its institutions. This is to be found in the public as well as the private sector, in the communities under occupation as well as in the diaspora. The Palestinian National Authority has succeeded in improving the economy and establishing a satisfactory security situation, and is on the way towards establishing law and order despite the meager resources at its disposal and the immense obstacles contrived by successive Israeli governments. I am sure a future independent Palestine will score far better.

If a final settlement is negotiated what steps would you intend to take?

I reiterate that any final status agreement reached between us and Israel will not be implemented before being endorsed by our people through an open and democratic referendum. This has been my unwavering position. Any other way under my administration or under future ones would be fatal to the democratic process.

What are the risks if a satisfactory agreement with Israel is not reached?

I am an optimist by nature. I have confidence that the people of Israel will realize sooner rather than later that the option of peace will produce better results than any other alternative in the short as well as the long run.



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Palestine Overview

The following set of statistics is based on data obtained by MEES from the Palestine Authority, the Arab Monetary Fund in Abu Dhabi and the World Bank. (2008)

1. Total Area: 764 sq Km. West Bank 404 Km and Gaza 360 sq km. (Areas are “not linked due to occupation by Israel. The Question of Palestine is still outstanding since 1948).

2. Capital : under negotiations

3. Population: 3.72mn. (62.3% in the Occupied Territories of the West Bank of Palestine, and 37.7 in Gaza)

4. Concentration ratio: 626 per sq kilometre. (Gaza has the highest population concentration in the world)

5. Age structure :

Gaza:

0-14 years: 44.4% (male 353,489/ female 334,770)

15-64 years: 53% (male 420,618/ female 402,297)

65 years and over: 2.6% (male 16,483/female 24,202) (2009 est.)

West Bank:

0-14 years: 37.3% (male 470,735/ female 446,878)

15-64 years: 59.1% (male 744,822/ female 708,695)

65 years and over: 3.7% (male 37,471/female 52,666) (2009 est.)

6. Literacy rates:

Gaza:

Definition: age 15 and over can read and write Total population: 92.4%

Male: 96.7%

Female: 88% (2004 est.)

West Bank:

Definition: age 15 and over can read and write

Total population: 92.4%

Male: 96.7%

Female: 88% (2004 est.)

7. Declared labor force : 848500

8. Unemployment: 29%.

(Gaza unemployment rate is 49 %) the West Bank is a little more than 16%; (19% 2009 estimate)

9. Labor Force distribution : 13.4% (Agriculture); 12.1% (Industry);

10.9% (construction); 63.6% (Services)

10. GDP: 5.01bn\$.

11. GDP Per Capita : 1445 \$ (Current Prices)

12. GDP Per Capita : 1109 \$ (in 1997 Prices)

13. Economic Sectors Contribution to GDP :

4.6% (Agriculture); 13.6% (Industry); 4.9 % (Construction);

76.9% (Services)

14. Exports % of GDP: 14.5%

15. Imports % of GDP: 73.9% (close to 82.1 % are food and the balance is other consumption goods).

16. Trading partners : 93% of exports are to Israel; 97.5 of imports are from Israel

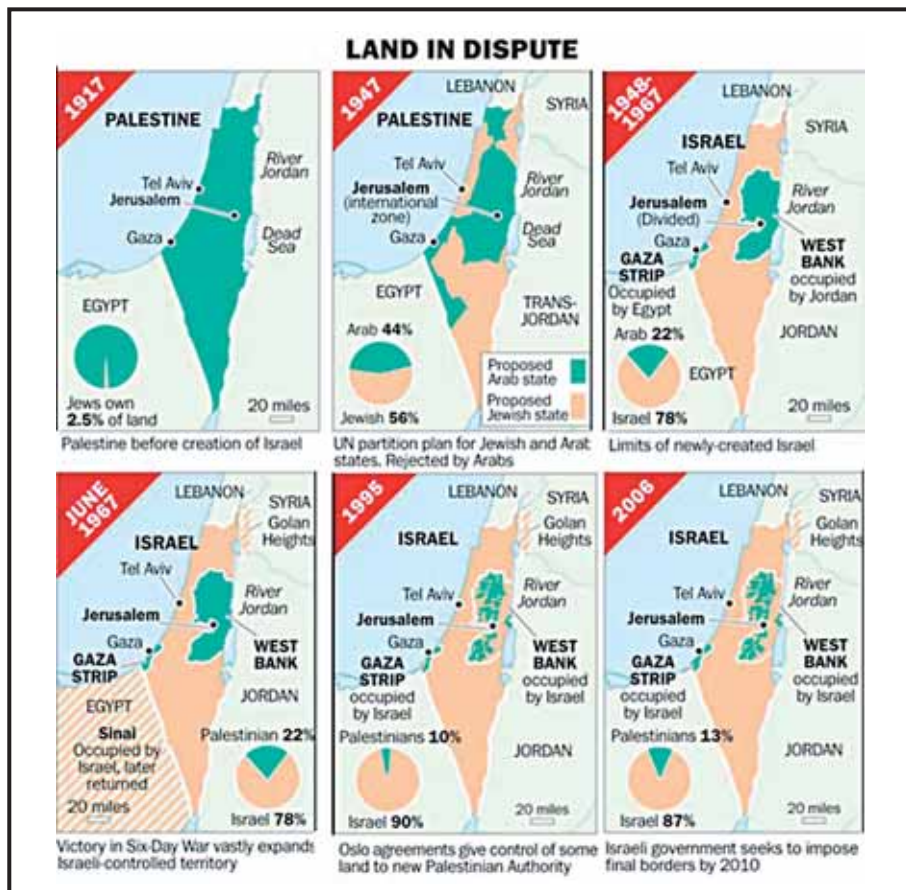
17. Investment Expenditure 310 mn\$ (250mn \$ from foreign donors)

18. Commercial Banks: 21 Banks. (Only one Swiss nationality and the rest are national or from neighboring Arab countries particularly Jordan).

19. Total Bank Assets : 7.6bn\$ (149.8% of GDP)

20. Total Deposits in the Banking System : 5.7bn\$, (111.6% of GDP)

21. Foreign Aid : 2 \$bn. (Arab countries 526 \$mn; Europe 651mn\$; World Bank 283 mn\$; USA 300mn\$; the rest is from other donors)



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Iraq Oil Bonanza: Challenges by Governance & Institutional Weaknesses

Tariq Alhaimus¹

Talk of a forthcoming Iraq oil bonanza spread almost instantly after the fall of the former regime, surfacing and vanishing with the turmoil intensity of the past seven years and recently climaxing with advent of the auctions of some world famous oil fields. Right from the start the oil industry was busy on calculations of potential lucrative returns in a country of abundant reserves and low cost. Alongside, this was echoed among the powers that be at the time by such predictions as the memorable assumption of Paul Wolfowitz of a country that can finance its reconstruction fairly soon, and reaching \$50-100bn oil revenues in three years. Inside the country the past few months also witnessed predictions from some senior politicians, reaching 12mn b/d in six years and approximate revenue of \$200bn, with reported applications for jobs starting to flow!

It is fair to say that there has always been skepticism, to say the least, of future prospects, citing fallacies and wishful thinking that underestimate the monumental and deeply entrenched obstacles and uncertainties. A lot of the recent exuberance has also been submerged by the harsh realities that came to the fore again in the run-up to the March election, reminding us once more that discord and confusion will remain for a long time to come, dimming the chances of meaningful development of the oil industry and making an effective use of this source to realize the illusive dream of solidly based economic and social development.

These hopes preoccupied generations of policymakers and researchers in the past decades, from the good old days of obsession with the beyond oil diversification, to the mystery of the oil curse! Readers of MEES don't need to be reminded of this and the first issue of its Geopolitical Reports included two timely contributions that sought to look ahead on the ever complex Iraqi prospects and opportunities in making use of a potential historic bonanza². What the following remarks suggest is that much more attention will hopefully be made to two specific factors that play a crucial part in determining the shape of prospects ahead. These are the dysfunctional institutional structure that inhibits the carrying out of any credible economic transformation, and the now rampant corruption that provides a recipe for plundering future resources.



A book on this subject which I had written many years ago but could not publish until recently *Kitabuna wa Kitabukym*, (Arabic), pleaded for more attention to both these factors³. It is mostly a collection of articles on public sector institutional management and mismanagement published in newspapers and periodicals in the seventies and somehow got censored in 1974 when a naive attempt was made to publish them in a book! They have now been "updated" with a chapter on the corruption aspect of governance as the country reached the bottom of the corruption index and the word "fasaad" (corruption) became one of the most prevalent in conversations, discussions and the airwaves. Researching the past shows that many of the issues remain the same as in three or four decades ago and institutional conditions worsened as expected following wars, sanctions, occupation and subsequent turmoil. The broad message conveyed is that with the gross institutional deterioration and deeper spread of "fasaad" into the political system and social norms, the prospects of the country will remain dim, to say the least, unless exceptional reform efforts are undertaken.

Messages from the past

Among the more specific potentially relevant messages was the clear warning signals conveyed as far back as six decades ago, and increasingly validated ever since, on the critical importance of the institutional structure and civil service capacity for any meaningful utilization of Iraq's new oil resources. A good number of consultant and experts reports underscored the same message, including the World Bank report on the a government's 1952-57 program concluding that the proposed ID168mn of expenditures could not be implemented without substantial effort to improve public



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sector management and institutions; a similar conclusion was reached by William Brownrigg's recommendations in 1954 for an effective civil service in Iraq painting a bleak picture of what he saw; in the same year the widely acclaimed Plan of Action for Iraq Development by Lord Salter concluded unequivocally that the main obstacle for the economic development of Iraq was the competency of the administrative system and not the shortage of resources or technical expertise; and finally even a Karl Everson's report on the monetary policy at the time could not avoid emphasizing that mismanagement can disrupt the productive system and the achievement of a fast pace of development. These are the warning signals that were visibly hoisted at the dawn of the country's earlier oil bonanza, coming interestingly at a time when the economic development state of the art was largely focusing on the factor of resource availability and foreign aid, a far cry from recent times when the institutional and governance factors have been assuming a center stage. A number of articles in Kitabuna, dating back to the late sixties and early seventies, tried to advocate the same message and sought to identify one area that could explain the lack of progress in facing this challenge: the absence of a credible plan for institutional improvement that should accompany new development plans and programs. The indispensability of such plans is the second specific message that comes out of the past decades and assumes a particular relevance now with the talk of a new development plan being formalized.

Attempts were made in the early seventies to put together a comprehensive administrative development plan, especially with new challenges of the post oil nationalization era, though no action materialized, leaving it to sporadic attempts, and gimmicks, in subsequent decades with widening of the gap between resource allocation and implementation that has now become a fact of life. Back in 1967 one article in Kitabuna ventured to underscore a link between the national development plan and an administrative development plan, something that has now unfortunately become even much more difficult with the prevailing environment of ambiguous "federalism" and weak coalition governments that has led and will likely lead national planning to take the back seat, unless an exceptional political commitment and consensus are mustered.

The third potentially relevant message from past experience is the host of challenges on civil service reform that have been attempted and remain grossly overdue aggravating the inefficiencies and poor capacity of government agencies. The critical salary structure was subject of a plan that got nowhere, prompting an article that tried to explain and call for at least modest steps towards a modern system based on job description. The incentive system was also subject of a haphazard attempt for change by transplanting a regime of East European "socialist contests", also covering the Basra oil employees, that quickly dissipated. Experience also showed the failure of the attempt to limit patronage by the establishment of a Civil Service Council, something recently advocated to avoid the misuse of powers of appointment of new 120,000 positions amid the unique Iraqi system of distribution favors called "muhasasa" (euphuism for sectarianism)! Past decades witnessed numerous failed approaches and what might provide a glimmer of hope now is that if there is a political will for civil service reform, so far in short supply, there are abundant successful international experience and much assistance from international institutions.

Increasing Corruption

The managerial and administrative dysfunction in Iraq, as in other developing countries, has been compounded by corruption, along with the other often cited components of governance including accountability, inclusiveness, government effectiveness, regulatory framework and the rule of law. Corruption in the country, however, has reached such abysmal proportions and pervasive impacts prompting a chapter in Kitabuna on the roots, current features and prospects. This comes at a time when there are already warning signals from institutions and experts on the vast new scope for massive corruption that might be made possible by the multi-billion new oil contracts and the huge oil industry service and related infrastructure needs that will inevitably have to be met by foreign contractors, with hardly any credible government's capacity to monitor despite the rhetoric⁴. Facing this challenge is a huge task, and the chapter is far from optimistic given the country's governance fundamentals and the now possible entry of powerful vested interests.

The chapter attempted to seek better understanding of the corruption phenomenon in the country, tracing its roots especially in the past several decades of the previous regime when the county's resources were systematically utilized to bolster regime control and came to full global view with the flagrant use of the Oil for Food program as detailed by the Volcker report and release of the oil coupons. With the fall of the regime this gave way overnight to chaos, intransigence of the new authorities, free grab of public assets by the new elite came to full view, an estimated nine billion dollars of Iraqi money that were unaccounted for, numerous cases of corruption in US funded works with lax controls and permissive



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contracts, and widespread stories that journalists reported of corruption in reconstruction contracts.

Further episodes of corruption ensued after the end of the formal occupation, spreading and deepening in subsequent years as manifested in several shapes and forms. This ranged from the huge opportunities made possible for granting contracts with hardly any system of controls culminating in the world class cases in the defense, electricity and trade ministries; the rampant oil smuggling and mysterious absence of oil metering, with full connivance of those in power and costing billions; and the almost total ineffectiveness of anti corruption integrity units that faced hostility from many of those in authority who also invoked and actively used the previous regime's law giving ministers authority to exempt whomever they deem fit from corruption investigations. Evidence of the pervasive level of corruption is manifested in what millions of people experience and talk about publically, and the more systematic evidence provided on the global ranking of Iraq prepared by Transparency International and the World Bank that put the country in the very bottom of the scale along with Somalia, Myanmar, and Afghanistan.

What this review tries to argue is that the various epochs in the past four decades, let alone the more distant past, has deepened the "culture" of corruption in the political system and social norms, leading to the conclusion that the prospects of at least bringing it to "normal" levels appears far from bright, especially now that much more lucrative bonanza opportunities lie ahead. This is due to several factors including the likely absence for the foreseeable future of a reasonably strong administration that can develop and build consensus on strategies and have the willingness and capacity for implementation as long as the factious and tenuous alliances continue; an elite that has squandered a historic opportunity following the fall of the old regime to put in place new values but reverted, instead, to the "now it is our turn" to compensate for past exclusion that set the tone for the new regime; lack of clear policies and strategies based on deep understanding of the complex corruption phenomenon and tinkering, instead, with the edges by sporadic investigations and litigations and signing conventions; going into the opposite direction in tolerating or turning a blind eye on mega cases of corruption involving members of the elite sending unmistakable negative signals and undermining respect for the country's leadership; and finally the lack, so far, of strong organized popular pressure with dedicated activists which in many cases may prove to be the only hope for forcing change.

The book hopes that this bleak view of prospects in dealing with corruption will not materialize and it certainly should not be seen as a lost cause, especially if the post 2010 parliamentary election era provides a more stable environment that allows benefitting from the abundant knowledge that

accumulated in the past decade, the readiness of international institutions to put together practical programs and the experience of many countries. Looking ahead it may very well be the case that no "master plan" can work in Iraq given the deeply entrenched and pervasive level of corruption and that more realistic approaches based on a series of incremental, but well-designed approaches, have a better chance of making inroads. Not all experiences and approaches are of course expected to fit Iraq's peculiar conditions as two examples relevant to the use of oil revenues show.

One is the current debate in Brazil on how to avoid mismanagement and corruption in the use of reported huge reserves off the southern coast that were seen as a "gift from God". Suggestions were made for establishing a fund for the expected new revenues, making use of the Norwegian model, to make good use of the new resources and escape the "oil curse". Some skepticism, however, was strongly voiced about the usefulness of this or indeed of any fund for this purpose. The one architect of Norway's energy policy, of Iraqi origin, in fact went as far as saying that the Norwegian model cannot even be adapted⁵. A different and quite interesting approach for dealing with corruption mentioned in Kitabuna is based on sector by sector analysis of risk points and laying down possible remedies and responses. This is the central theme of a fairly comprehensive book covering a good number of sectors, including the revenue and expenditure side of public finance, and has a particularly interesting chapter on 'Corruption in the Petroleum Sector' that tracks corruption vulnerabilities at various stages of the industry and among the main players and interestingly includes references to Iraq⁶. Country specific conditions certainly determine what works and what does not in these and other possible approaches and methodologies.

All this being said the issue still remains: just how much, if at all, the people of Iraq can expect from any new oil bonanza. The message that comes from country history and global experience is that this crucially depends on how far will there be efforts, already grossly overdue, to improve the capacity of country institutions to deliver; and how much political will and social consensus will there be to counter the corruption epidemic that risks plundering of resources and degenerate the social fabric. As of now only history can tell.

1. Tariq Alhaimus worked for the Central Bank of Iraq since the mid-sixties, and participated in the establishment of the OPEC Fund. OPEC Fund, taking part later in its Board meetings. . Since 1981 until recently he worked for the Boards of Directors of the IMF and the World Bank, Washington, D.C.
2. Articles by Thamer Ghadhban and Fadhil Mahdi: MEES: Energy & Geopolitical Risk, 2010
3. Kitabuna wa Kitabukum: (Our Memo, Your Memo!) It is a common reference widely used in Iraq to the bureaucracy's vicious circle of endless preoccupation with paper work and little action.
4. Timothy Williams: report in the New York Times, January 14, 2010
5. The Basel Institute on Governance website
6. J Edgardo Campos and Sanjay Pradhan (editors): The Many Faces of Corruption –Tracking Vulnerabilities at the Sector Level, 2007

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Iraq: Political Risks for Energy Companies in the Kurdistan Region

Zainab Al-Assam*

Despite Baghdad's acquiescence to exports from the Kurdistan Region that it regards as illegal, on-going disputes over the legality of the Region's contracts heighten risks.

The Iraqi government does not recognize any of the contracts that the Kurdistan Regional Government (KRG) has signed with foreign energy companies and regards as illegal those signed after August 2007 when the latter's own oil and gas law came into being. Until Baghdad recognizes these contracts, which would most likely necessitate the passage of its own hydrocarbons law, energy companies exporting oil from the Kurdistan Region face significant non-payment risks. Indeed, despite Baghdad's acquiescence to exports from the Kurdistan Region, a dispute between the federal government and the KRG over payment for oil exports is unlikely to be resolved soon. Meanwhile energy companies that have interests in the Kurdistan Region are at risk of being blacklisted from bidding for contracts elsewhere in Iraq.


In April 2006, the KRG based in Irbil formed its own Ministry of Natural Resources headed by Ashti Hawrami to facilitate the signing of energy contracts with international oil companies independently of Baghdad. Since 2003, the KRG has independently signed several deals for exploration and production as well as refinery projects. In contrast to the long-term technical service contracts signed by Baghdad, the KRG has signed several agreements on a production sharing basis whereby the companies receive a percentage of oil revenues, alleged to be up to 18%. The KRG has signed over 30 Production Sharing Contracts, mainly with small-medium sized companies that include DNO of Norway, Western Oil Sands and Heritage Energy Middle East Limited of Canada, General Enerji and PetOil of Turkey, Perenco S.A. of France, as well as the US' Hunt Oil. There is significant opposition to the model used by the KRG in Baghdad because it allows foreign oil companies exaggerated profits and would, if applied elsewhere in Iraq, result in a significant loss of revenue for the government; the KRG claims the opposite is true. Under a technical service contract, the oil company is paid a fixed fee for its services and receives no ownership of the country's oil, which would be the case under a Production Sharing Contract.

Iraq's Constitution does not clearly specify by which



authority energy resources in the Kurdistan region will be administered; it appears to endow both central and regional entities with licensing rights. In August 2007, the KRG passed its own oil and gas law giving it the authority to manage oil and gas fields in its region (comprising the three northernmost provinces of Sulaimaniyah, Irbil and Dahuk). According to Baghdad, this contradicts Article 108 of the Iraqi constitution that states 'the federal government with producing governorates and regional governments shall undertake the management of oil and gas extracted from current fields'. Iraqi oil minister Hussein al-Shahristani consequently asserted that all energy contracts signed by the KRG with foreign oil companies since the Kurdish oil and gas law came in to place were illegal and the President of the Kurdistan Region, Massoud Barzani, threatened to withdraw from al-Maliki's government in response. Separately, the KRG has claimed that the Iraqi government would violate the Constitution if it unilaterally made decisions over the controversial Kirkuk or Bay Hassan oil fields; according to the Iraqi Constitution, the KRG and the federal government have to consult each other on matters involving oil fields in these disputed areas.

Energy companies that have bypassed the central government and signed oil contracts with the KRG are likely to be threatened with exclusion from future deals elsewhere in the country, or with being awarded oil export contracts. Companies that have signed memorandums of understanding both with the Ministry of Oil in Baghdad and the KRG will be at greatest risk of being blacklisted. In October 2009, it emerged that China's Sinopec had been prevented from participating in an oil and gas bidding round



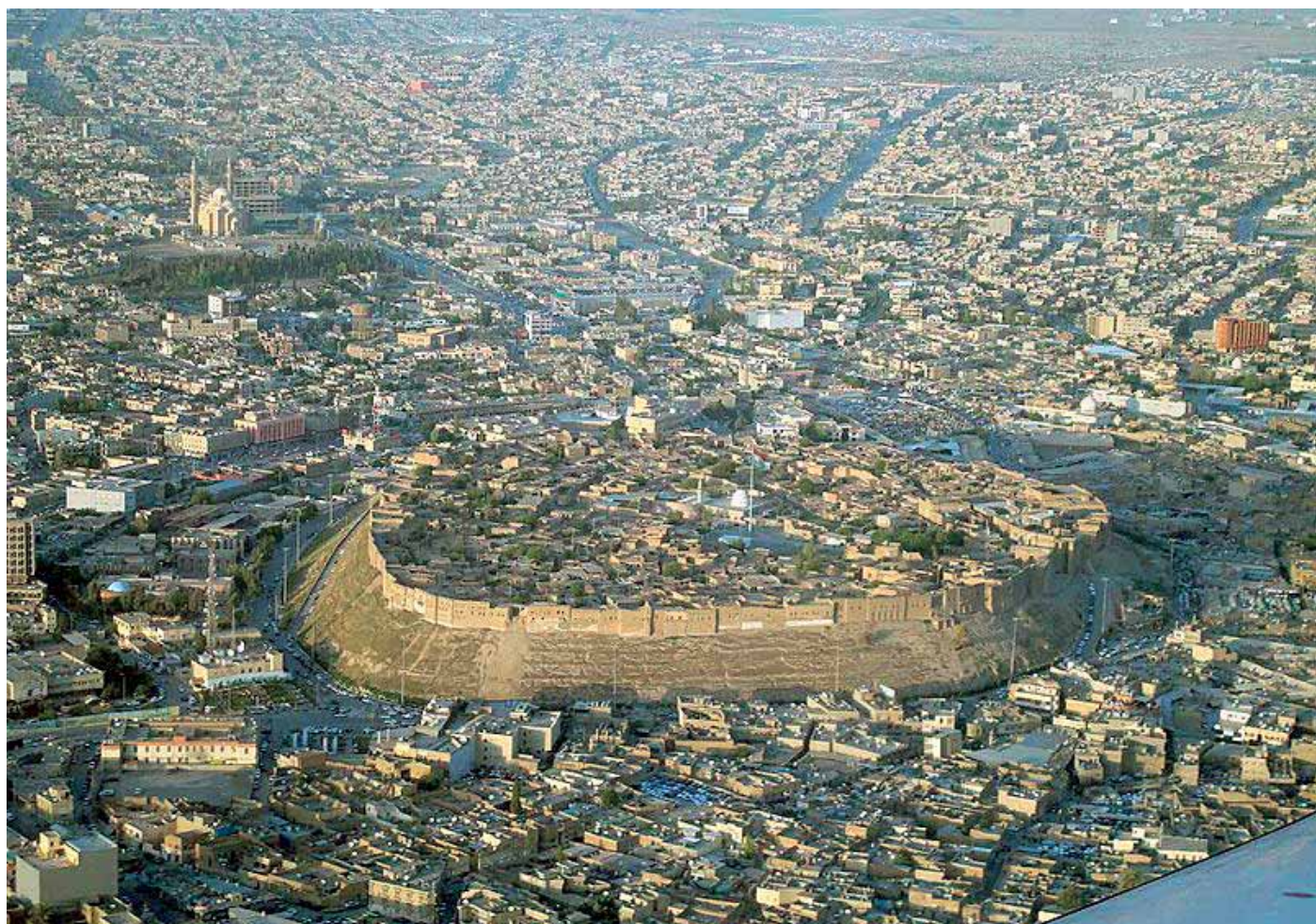
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held in December 2009 as a result of its purchase of Addax Petroleum, since the latter is one of several companies that have entered into PSCs with the KRG. Sinopec had been pre-qualified to bid for a number of projects including development of the Zubair, Maysan and Kirkuk fields. Prior to that, in December 2007, the Iraqi government said that it would halt exports to Korea unless a Korean consortium led by the Korea National Oil Corporation (KNOC) ceases its operations in the KRG-controlled Bazian Region.

Ahead of Iraq's legislative elections that were held on 7 March 2010, reconciliatory statements indicated a possible resolution of the dispute over oil contracts between the federal government in Baghdad, and the KRG. These statements most probably reflect political alliance building rather than an imminent resolution to disputes. Given that Shia and Kurdish parties will need to forge an alliance to form the new government, the uncompromising positions of both Baghdad and Erbil based-politicians is being replaced with hints of compromise. Minister of Oil al-Shahristani stated that exports from the Kurdistan Region via the federal Iraqi government-owned Ceyhan pipeline would resume soon (exports ceased in September 2009 amid a payment dispute). The Kurdish natural resources minister, Ashti Hawrami, for his part, stated that the KRG would make public the details of all 38 Production Sharing Contracts (PSCs) that it had signed with foreign oil companies, since an apparent lack of transparency had been one

of the federal government's grievances. However, on 14 February 2010, the KRG's natural resources minister admitted that the KRG had not yet received official written confirmation from Baghdad that its exports would be resumed from the Kurdistan Region. Furthermore, external financial regulators' increased scrutiny of possible insider share dealings within the KRG (and potentially implicating Hawrami) points to a lack of transparency which the Iraqi government in Baghdad can use against the KRG.

Even if an agreement is reached over the legality of some of the contracts the KRG has signed, this would not necessarily mean Baghdad would agree to pay oil companies involved in exporting oil from the Kurdistan Region's Tawke and Taq Taq fields (operated by Norwegian company DNO and Addax Petroleum respectively). Indeed, the federal government's position, stipulating that the KRG must pay oil companies from its 17% share of the Iraqi budget, is unlikely to change. On 1 June 2009, oil exports were launched from the Taq Taq and Tawke fields in the Kurdistan Region operated by Addax Petroleum (where it has a 45% interest and operatorship) and DNO respectively. Whilst the Iraqi government in Baghdad has repeatedly stated that all oil contracts signed by the Kurdish Region are illegal it appears to have made an exception to this deal on the grounds that the contracts were signed before the KRG oil law came into being in 2007. It is also likely that the Iraqi government accepted the deal under pressure to

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increase output amidst dwindling oil revenues and a lower oil price, which had resulted in revisions to 2009's budget. Iraq's oil exports in 2009 averaged around 2mn b/d. Given that Iraq possesses the third largest reserves in the world, this highlights the damage inflicted by decades of sanctions and armed conflicts. Furthermore, Iraq's antiquated downstream infrastructure, which currently offers a refining capacity of just 600,000b/d, means that one quarter of the refined petroleum used domestically must be imported.

In September 2009, after the KRG failed to make payments to DNO, the latter ceased drilling. The KRG has demanded that Baghdad pay DNO, as revenue from the project would go to the federal government. This is because the oil is dependent on export through the Ceyhan pipeline, which goes through Baghdad government-controlled territory. The Iraqi government, which still does not recognize DNO's PSC with the KRG, has refused to do so. As far as Baghdad is concerned, the oil that DNO produces for export through the Ceyhan pipeline belongs to the federal government. Accordingly, it expects that the KRG should pay DNO for its production from the 17% share it receives from Iraq's annual budget. However, Baghdad is currently in a stronger position vis-à-vis the KRG than when it agreed to allow the exports from the north, which makes an about-face on this issue even less likely now. Previously, whilst the KRG had signed dozens of PSCs, the federal government was unable even to hold a bidding round, cancelling such efforts in September 2008. By the end of 2009, however, the Iraqi government had concluded two successful bidding rounds, held in June and December, with the aim of maximizing oil production to 12 million bpd over the next decade.

The KRG has attempted to put pressure on the Iraqi government by threatening to withhold revenues from the oil it produces in the Kurdistan Region. On 10 November 2009, the president of the Kurdistan Region, Massoud Barzani, said that it would hold on to its revenues from the 100,000 oil barrels exported per day in lieu of the current arrangement whereby the Central Bank distributes 17% of total revenues to the region, claiming that it is being used as a political weapon by Baghdad. One key obstacle for the KRG would be the leverage Baghdad can bring to bear by preventing the latter from use of the Ceyhan pipeline to export oil from the Kurdistan Region to Turkey.

In addition to the opposition it faces from the federal government, Kurdish criticism of oil deals signed by its Natural Resource ministry has been increasingly vocal and has focused on the perceived corruption and lack of transparency accompanying certain deals and the limited economic benefits for the population of the Kurdish provinces; this was likely a key factor in the loss of support for the ruling KDP and PUK parties in July 2009's parliamentary elections and the rise of the opposition Goran (Change) party. The Goran list is led by Nawshiran

Mustafa, a former deputy leader of the PUK while the opposition Peshkawtin (Progress) Party is led by the brother-in-law of Iraq President and PUK leader Jalal Talabani, Dr Halo Ibrahim Ahmed. Just ahead of the Kurdistan Regional elections, Ahmed gave a press conference in which he apparently exposed financial corruption in relation to a contract signed with oil company Pet Prime International Company Ltd.

A more vocal opposition to the PUK and KDP in the Kurdistan Region may lead to greater pressure for transparency in oil deals. On 25 July 2009, Kurdish parliamentary and presidential elections were held in the Kurdistan Region; results for the parliamentary elections gave the KDP-PUK Kurdistan List 55 seats of the 111 seat parliament, down from 78, and gave the opposition Goran (Change) list 28 seats. The KDP and PUK parties, which are controlled by the Barzani and Talabani families respectively, have governed the Kurdistan Region since 1991 (since the establishment of a no-fly zone) and, following 2005 elections, agreed to distribute all the key positions amongst themselves cementing the two parties' control over decision-making.

The gains made by Goran mean that the KDP and PUK will face credible opposition in the Kurdistan Region for the first time. A strong opposition could potentially challenge Kurdish policy vis-à-vis Baghdad on the hydrocarbons law, a referendum on the status of oil-rich Kirkuk and the other disputed Arab-Kurd areas of northern Iraq, potentially making resolution of these more complex. However, given that many of the challengers to the Kurdistan List were previously PUK members who defected in protest at the excesses of the KDP and PUK and lack of reform, they are unlikely to differ radically in policy towards Baghdad. Instead a more vocal opposition is now likely to increase pressure within parliament for investigations into oil deals signed with foreign companies.

The future success of energy companies such as DNO in the Kurdistan Region will most likely depend on the passage of the National Hydrocarbons Law, as it would most likely legalize its contract. DNO was the first to sign a contract with the KRG in 2003, which puts it in a relatively favorable position compared to oil companies that entered the Kurdistan Region much later (i.e. before the KRG's own oil and gas law came into place). However a Hydrocarbons Law is unlikely in 2010 due to significant opposition in Parliament, regardless of the outcome of legislative elections. Furthermore, given that al-Shahristani's Oil Ministry recently ratified a number of contracts with international oil companies, including Shell, Sonangol and Petronas, there is less urgency, as far as the federal government is concerned, for the law's passage through Parliament.

**Head of Middle East and North Africa Forecasting at Exclusive Analysis, Ltd., London.*



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مَصْرَفُ لُبْنَانَ



Egypt says Nile sharing meeting fails

By SALAH NASRAWI (AP)



CAIRO — Egypt's state news agency reported Tuesday that 10 African nations have failed to conclude a long delayed new agreement for sharing water from the Nile and will call for closer cooperation instead.

The Nile basin nations have failed for years now to agree on the Nile River Cooperative Framework Agreement to administer the longest river in the world, which would reduce Egypt's share of the Nile water. Egypt has categorically refused to sign the agreement.

Ugandan Minister of Water and Environment Maria Mutagamba, in her opening speech at the meeting in the Sinai resort of Sharm al-Sheikh called on her counterparts to sign the agreement without further delay.

Ahead of the discussions, however, Egyptian Minister of Water Resources and Irrigation Mohammed Nasreddin Allam insisted that Egypt would maintain its share of 55.5 billion cubic meters of water from the river — more than half of the Nile's flow.

Egypt also wants veto power over any new irrigation projects undertaken by the other nine riparian states.

The Sub-Saharan African states have rejected the

clause and called for the signing of the agreement.

Egypt's claim to Nile water is based on a 1929 agreement between Egypt and Great Britain on behalf of Britain's colonies which gave Egypt the right to most of the more than 100 billion cubic meters of water that reaches the downstream countries annually.

Egypt, a country of some 80 million people says if Egypt's annual share of Nile water remains at 55.5 billion cubic meters, per capita water availability will stand at around 630 cubic meters in 2025, compared with 1,213 in 1990.

The agreement lays down principles of cooperative water resources management. If signed, the treaty would pave the way for the establishment of a permanent Nile River Basin Commission.

In addition to Egypt the group includes Burundi, Congo, Ethiopia, Eritrea, Kenya, Rwanda, Sudan, Tanzania and Uganda, which are calling for new allocations of Nile water to reflect their burgeoning populations and industrial capacity.

Source: <http://www.google.com/hostednews/ap/article/ALeqM5iaEErLsWyklylOK1-kIXxXfYJxOwD9F2BKNO0>

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Qatar Water Report Q2 2010



Qatar is a small country in terms of population, but it is one of the world's largest water consumers on a per capita basis. More than half of the country's water goes to the agricultural sector, but increasing demand is coming from the country's growing urban population.

It is a country with limited and declining groundwater resources, and the state is therefore investing heavily in desalination plants. It has one of the longest-standing desalination programmes in the Middle East and so has garnered much experience in the sector.

Much of the expansion in Qatar's desalination programme is being achieved through independent water and power projects (IWPPs). The largest of these is the Ras Girtas project currently under construction in the Ras Laffan industrial complex. A further IWPP is said to be under consideration, and the country is also widening its technological horizons, with a pilot reverse osmosis desalination plant due to be built and solar-powered desalination plans under consideration.

Qatar has been open to foreign investment for several years and is regarded as a relatively safe investment destination, with major international companies currently active in the sector. The US\$3.9bn Ras Girtas project managed to achieve its funding goals in mid-2008, despite the already rocky state of international capital markets, indicating investor confidence. The global economic downturn has hindered the pace of development since then to some extent, but signs of improvement in the regional investment climate will benefit the sector.

Qatar will need to build on this reputation to attract more funding and technical know-how, as it will need to expand its water supply, wastewater treatment and power capacity over the next five years if output is to keep ahead of growing demand. Water demand

in the summer months of 2009 rose 7% compared with the previous year.

The Qatar Electricity and Water Company (QEWC) is the state's main investment vehicle in the water and power sectors. The government holds a 43% stake in the company, with the rest held by private and public investors. It says its profits and revenues have been on the rise, as income from joint ventures feed through. QEWC is involved in many of the large projects taking place in the country and so is a key partner for other investors. It now owns and manages almost 1mn m³/d of water capacity and around 3 gigawatts (GW) of power output. It also has interests in IWPPs, producing some 750,000 m³/d of water and more than 6GW of power. When Ras Girtas becomes operational in 2011, the country will have around 1.4mn m³/d of desalinated water capacity, as well as power generating capacity of 9GW. The Public Works Authority, Ashghal, manages the development of wastewater and drainage projects in the country, and is responsible for contracting firms to work on its growing slate of projects. Ashghal is considering outsourcing the operation and maintenance of some elements of its wastewater network – the first time it has done this.

The water sector is regulated by the Qatar General Electricity and Water Corporation (Kahramaa), which was established in 2000 as an independent corporation operating on a commercial basis. Kahramaa also owns projects and develops strategy for the sector. Kahramaa is also responsible for setting water tariffs, which have been heavily subsidised for decades. There has been some talk of making them more representative of costs, but little action has been taken on this front yet.

Source: <http://www.companiesandmarkets.com/Summary-Market-Report/qatar-water-report-q2-2010-278209.asp>

Cities in region face floods if sea level rises modestly

Gulf News



The current sea level rise projections need to be perfected by collecting more information, most importantly regarding the melting of the Greenland and Antarctic ice sheets, according to Professor David Holland, Director of the Center for Atmosphere-Ocean Science at New York University.

By Rayeesa Absal, Staff Reporter

April 17, 2010

Abu Dhabi: Even a modest sea level rise could spell trouble for low-lying cities such as Abu Dhabi, an academician has warned.

"Abu Dhabi is vulnerable to any change in sea level. Even a modest rise in the sea level could potentially lead to perfect storm conditions," Professor David Holland, Director of the Center for Atmosphere-Ocean Science at New York University, said in an interview with Gulf News.

"At present there is, however, no credible projection of the sea level rise that could be expected and when," he added.

He was in the capital last Sunday to deliver a lecture, organized by his university on 'A Tale of Two Cities, and of Climate Change: Future Sea Level Projections in New York and Abu Dhabi'.

The current sea level rise projections need to be perfected by collecting more information, most importantly regarding the melting of the Greenland and Antarctic ice sheets, he said.

The UN's Intergovernmental Panel for Climate Change predicted a sea level rise of 0.37 to 0.59 meter by 2100 in its fourth assessment report in 2007.

But the report was criticized for not having included the impact of these two massive ice sheets.

Predicting the sea level rise could be based on a continuation of weather forecasts (which predicted a 30 cm rise at the turn of the century) on global warming due to increasing greenhouse gases (which predict a 20-60cm rise) or the melting of ice sheets,

he explained.

The most plausible cause of rising sea levels could be the melting of the ice sheets, Holland, like most climate scientists, believes.

"It is also the most uncertain number yet," said the expert, who has been researching these ice sheets for a long period.

At least ten years of data collection is required in order to make reliable computer simulation models. While Abu Dhabi is susceptible to flooding, it is no more vulnerable than other cities around the world located at sea level, such as New York, Holland said.

Up to 6% of UAE at risk

Abu Dhabi: As much as 6 per cent of the UAE's land area could be flooded by 2100 if the worst-case scenario of a nine-meter rise in the sea level comes true, according to a government study published in January.

The study titled 'Climate Change: Impacts, Vulnerability and Adaptation' was published by the Environment Agency - Abu Dhabi (EAD) with the help of researchers from the US-based Stockholm Environment Institute.

Significant built-up areas in coastal regions will be inundated, even if there is only a small rise of one meter, it says.

Since scientists are not certain of the rise in sea levels caused by continued melting of the glaciers, the study envisages two possible scenarios — a rise of two meters by 2100 if there is no accelerated ice cap melting, and a rise of nine meters if there is.

A two-meter rise would flood 1,155 square km, or 1 per cent of the land, while a nine-meter rise would inundate close to 5,000 square km, which is 6 per cent of the land.

Source: <http://gulfnews.com/news/gulf/uae/environment/cities-in-region-face-floods-if-sea-level-rises-modestly-1.613498>

Cultural Risk – A Subset Of Completion Risk In Middle East Project Finance

By Saleh S Jallad*

Engineering, procurement and construction (EPC) contracts typically account for up to 80% of the total cost of project finance deals, with development, finance and legal expenses comprising most of the remainder. Most project revenues are expected to be generated years after draw-down, and specifically after completion on time and within the bid price. Any slippage that is not promptly cured during the construction phase may have a detrimental impact on the entire project, its debt and debt service, its profitability and ultimately its economic viability. Notwithstanding the negative impact on the host government and its international credibility, the reputation of the EPC contractor, an important asset for its existence in the highly competitive construction industry, could be also drastically hurt.

Project finance lenders extend debt to projects, on the basis of an intricate and interdependent set of legal contracts and technical documents, way before the works commence. In most developing countries, lenders demand the clear legal and financial support of the host countries as part of a complex security package. Project assets rarely constitute significant collateral. Therefore it is incumbent on the EPC contractor, in conjunction with the operator, to utilize the right human resources and expertise, from the due diligence stage and throughout the negotiations phase with the potential clients and lenders. The need is more intense if they are also one of the sponsors of the project, regardless of the level of participation. Economic and technical feasibility studies, modeling, sensitivity analysis and a variety of examinations of legal and regulatory factors are among the factors to be seriously considered. But they may not be sufficient.

It should not surprise any party involved in project finance to discover on financial close that the project they conceived, and on which they had spent millions in various currencies, does not end up exactly as planned. Alterations are normally made and accepted by all parties at the negotiating table during the many months of negotiations. Compromises are often difficult, with contractors usually under considerable pressure from the client and project sponsors. Consequently, it is advisable to have sophisticated risk matrixes and related tools as a back-up during negotiations. The result is always the allocation of the identified commercial, financial and political risks and the corresponding cost, monetary or contractual, to the entity that is judged best able to manage them. Often, those legal, commercial, technical and political skills required during the



negotiations process are most critical in the final hours before signature.

Project Finance Defined

Based on my own experience in financing construction projects, the following new definition of project finance is more realistic, comprehensive and practical than the various definitions available in books or professional journals:

“Project finance is the art of understanding, negotiating, allocating and mitigating the risks inherent in economically viable projects, managed by creditworthy multinational consortia, for the purpose of efficiently raising long-term funds to develop, construct and operate profitably highly leveraged projects; with the proviso that the recourse of the debtors relies fundamentally on the cash flow generated by the project over the debt period, and not on the balance sheet of the sponsors.”

The literature and practice regarding identification, evaluation, pricing and mitigating the ever growing list of risks is growing continually. Though acknowledged by a few practitioners in the construction industry, the risk emanating from cultural differences among the participants, which we prefer to name ‘cultural risk’, is rarely or inadequately tackled on a formal basis, seriously investigated, priced or contractually mitigated as part of the overall risk evaluation at the development stage. It is most often realized only after its impact is felt, and that is usually too late. Cultural



risk is normally manifested in a detrimental impact on the profit and loss calculus of the contractors, as it has a direct but initially concealed impact on the completion obligation of the consortium, and probably on the economic viability of the overall project. As the risks inherent in a project increase, the financial and contractual liabilities normally deepen. It is more likely then that cultural differences become more significant under the project finance structure.

A review of the many projects developed recently by credible multinational consortia in the Middle East would indicate that the majority suffered considerable delays, cost overruns, and serious threats of abandonment or termination. Of course, the problems could be related to a number of material variables that can be easily observed and rationally explained. However, assuming, other things being equal, that all other risk factors are satisfactorily evaluated, priced, mitigated and contractually protected as per current methods, we still find an increasing number of projects failing to achieve their expected contractual and economic goals. Although we continue to observe success stories in the Middle East, the existence of both failure and success in the same 'business ecosystem' suggests that cultural risk may be evident as a significant subset of completion risk, particularly under project finance agreements.

Success Through Flexibility

Success in many projects can be attributed to some degree to the willingness and ability of a multinational management to incorporate in their cultural behavior a flexibility and sensitivity towards the other cultures involved. This style of management can help such companies to achieve higher levels of performance, but there is no magic formula or fixed set of rules that can guarantee mutually beneficial managerial compromises. Flexibility under the various business conditions in the Middle East has been a potent mechanism for success. Among the requirements for success are: entrepreneurial acumen; compassionate labor management to encourage long-term loyalty to the firm; in-house and outside professional

training and capacity building; closing the gap between productivity and pay; pursuit of long-term institution building and succession development; and augmenting the accountability of the management. The 'behavioral matrix' below (see table), is supported by personal experience and studies by the World Economic Forum findings published in The Arab World Competitive Report (2007), and demonstrates the hypothesis that cultural risk is a significant subset of the completion risk in project finance. The matrix is based on the findings of the Japanese authors, Kunshima, et al, of The Principles of Construction Management, and relevant material found in various editions of The International Construction Law Review, particularly Kris Nielson's Trends and Revolving Risks In Design – Build, BOT And BOOT Projects (Vol 14, Part 2, April 1997, pp 191-192). While the matrix can be modified in many ways, it will always show that different cultural behavior can have a significant effect on the management of projects that are led by multinational consortia.

The matrix assumes that each of the three regions – the Middle East, US and Japan – comprises a cultural unit, despite internal differences. Moreover, each has a distinct language system, a set of unique historical determinants, religious and ethic paradigms that combined to shape the social characteristics of their ecosystems and the traits of their people. Consequently it is imperative that consortia members ensure that their management representatives are aware from the outset of a spectrum of cultural differences, and are able and willing to employ their personal as well as their technical skills in such matters. Such skills and personal traits will assist in the collective management of the project. Serious and open discussions with respect to specific cultural issues should be conducted at the start of the project and also periodically, particularly when controversial issues appear to rise.

Project Managers' Roles

The roles of the project managers who are responsible for daily progress are critical. The multinational firms must, therefore, select them based on a careful assessment of their technical, managerial and personal skills in managing people of different cultures. Project managers are the link with the consortia management, and may find themselves reporting to boards composed of different nationalities, belonging to different political and social systems based on conflicting determinants, and probably with some history of national antagonism. Pricing under project finance is more expensive than under traditional contracting, as the risk level in general is higher. This is a well known and accepted reality. Therefore, it is a sensible precaution to increase the level of contingencies in projects to reflect the cultural risks that a multinational management has a high probability of having to face. The rate of risk is a question for the estimators to decide, based among other things on the intricacy of the projects, their location and the nationalities involved.

Cultural Risk: A Subset Of Completion Risk For Multinational EPC Consortia

	Factor	Middle East	US	Japan
1	Business ownership	Families	Numerous shareholders	Oligarchs
2	Business objectives	Continuity of family legacy	Profitability	Assertive enduring existence
3	Business principles	Rivalry	Fair competition	Shared competition
4	Entrepreneurship	Very high, based on the business acumen of the entrepreneur; strategic planning is secondary	Strictly limited by management strategic planning	Highly planned and long-term
5	Business Ethics	Uncontrolled; legally inadequate	Legally controlled and enforced	Legally and socially controlled and enforced
6	Business relationship behavior	Harmony with client, tendency to put 'Company' rather than 'Client' first	Short term relationship but with an eye on the long term; competition principle dominates company behavior with others, including clients	Long term and strong relationship with all entities; harmony standards dominate
7	Auditing and accounting standards	Poor, treated with suspicion	High	Very high
8	Decision process	Top to bottom, autocratic	Top to team	Top to bottom, hierarchical
9	Minority shareholder rights	Unprotected	Legally protected and enforced	Legally protected and enforced
10	Quality of board of management	Low accountability	High accountability	Very high accountability
11	Quality of top management	Family members control	Professional and skilled management	Management by seniority, through the ranks
12	Discipline	Low respect, haphazard enforcement	As per procedures; democratically enforced	Very high respect; hierarchical
13	Law and Order	Avoided if you can, no harsh consequences when enforced	Respected, with harsh consequences upon enforcement	Highly respected, with very harsh social consequences
14	Taxation	Not a serious matter, not treated with concern	Very serious, high priority	Very serious, treated with concern
15	Debt	Shunned and avoided whenever possible	Aggressively pursued; maximum leverage preferred	An important aspect of business
16	Delegation of authority	Poorly practiced wherever it exists	Highly practiced and a must in the firm; decentralized	Highly implemented with strict discipline; concentrated in the top echelon
	Factor	Middle East	US	Japan
17	Intellectual property	Low respect, unprotected by the law.	Protected by enforceable laws and respected	Protected by enforceable laws

	Factor	Middle East	US	Japan
18	Employment	Assumed by management as fixed assets; changing job is not frequent	Variable assets; high frequency of changing jobs, freedom to hire and fire	Lifetime
19	Wage and salary determination	Each company has its individual system; little relationship between job content and remuneration	Collective bargaining driven by market forces	Seniority
20	Pay and productivity	Poorly related to each other	Very important relationship; fair assessment	Important relationship; pay is more affected by seniority, productivity is related to job stability
21	Behavior of employees	Employing individuals, chauvinistic, favoritism, nepotism	Employing skills of individuals as long as they are useful	Employing individuals <i>per se</i>
22	Reward	Very small, very late if any	Big and prompt, normal practice for motivation	Small, in kind, with small bonus
23	Punishment	Benign neglect, relocation and slow dismissal; paternal behavior	Prompt dismissal, no second chance; rational	Relocation, rare dismissal
24	Labor-employee relations	Sense of injustice, fatalism and docility	Cooperative and dynamic; reflecting market conditions	Disciplined and authoritarian; long-term stability
25	Fundamental employee behavior	Passive attendance; minimum enhancement of learning and skills; when externally motivated, their behavior becomes highly individual and assertive	Actively participative; enhancement of learning and skills; highly individualistic; assertive	Actively listen, observe, learn, accumulate work knowledge and continue the hard work; harmony and team work.
26	Loyalty to firm	Very strong	Not so strong	Very strong
27	Interpersonal relationship	Warm and strong, collectively cordial	Individualistic and aloof	Individualistic and stratified
28	Quality of R&D	Poor; of secondary importance to firm	Very high; vital to firm and industry	Very high; vital to the firm
29	Expenditure of R&D	Insignificant assumed as cost only	Of primary importance; assumed as investment, profitability related	Of primary importance to increase their share in the market
30	Training and capacity building	Of secondary importance	Individual enhancement is encouraged	Important activity to the firm

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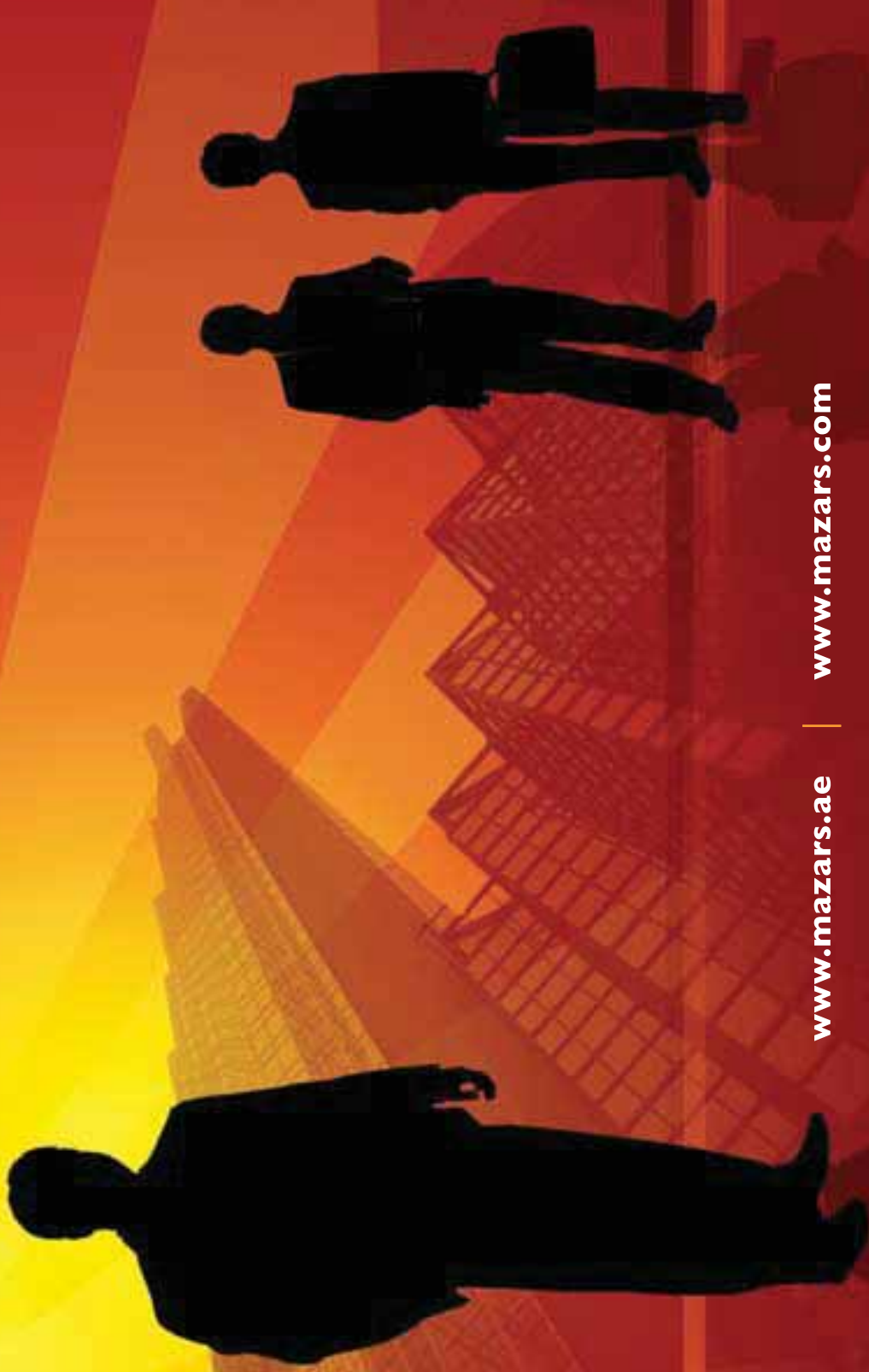
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