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The Rt Hon Patricia Hewitt MP
SECRETARY OF STATE
FOR TRADE AND INDUSTRY

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See Matthew

IRAQ: UPDATE ON COMMERCIAL ISSUES

As discussed yesterday, I enclose a note for the Prime Minister on commercial issues on Iraq. The note outlines the approach TPUK has taken to date and some of the successes that UK firms have had. The note gives some statistics on contracts won, but we are unable to give a total figure for UK contracts because the CPA does not make this information publicly available.

*Yours,
Erica*

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IRAQ: UPDATE ON COMMERCIAL ISSUES

Our Strategy

TPUK's strategy for helping British companies win business in Iraq has been to position UK firms as best we can through the provision of information about contacts, procurement issues, etc, and to press the US authorities (and the CPA) to ensure a level playing field on which UK companies can compete. In response to the latter point the US authorities have consistently expressed a welcome for the participation of UK companies but have stressed that there is no "special deal".

2. TPUK set up an Industry Working Group on Iraq in April. It advises Government on Iraq reconstruction issues. It is chaired by Tony Allum, Chief Executive of Halcrows. It has set up six sector groups in key areas for reconstruction - power, water, oil & gas, health, education and telecommunications. A wide range of major UK companies in these sectors are represented on these groups. These sector groups are now looking at what initiatives they can take to promote UK sectoral expertise in Iraq. These efforts have been reinforced by the opening of a bilateral commercial section in the British Office in Baghdad staffed by two TPUK officials and an industry secondee (from AMEC) to provide project management and engineering advice and help focus the section's work on ensuring that the British private sector is able to meet the reconstruction needs of the CPA. Our efforts will also be reinforced by the appointment of Brian Wilson as the Prime Minister's Special Representative for British Business, with particular focus on Iraq reconstruction.

Security

3. Security is still the major constraint and a major inhibiting factor in UK companies becoming active in reconstruction. We have agreed with the FCO travel advice that allows "essential" travel to Iraq. But in practice security and insurance costs mean that only firms with contracts to work in Iraq can justify the expense of travelling there.

Sources of Funds for Reconstruction

4. Most visible funding for reconstruction in Iraq has come from the US Government. Although US development assistance is tied to US firms, Ministerial lobbying of the US Government shortly after the end of the

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conflict secured US agreement that sub-contracting would be untied. The USAID funded prime contract for reconstruction, which Bechtel initially won, has been a major focus for the UK private sector, though it is USAID policy to give preference to the Iraqi private sector.

5. Future sources of funding are likely to be split between the US Government and the international donor community. The US Government is seeking Congressional approval for an additional \$20 billion for the next stage of reconstruction. This funding (if agreed) is likely to be tied to US Federal procurement/tendering rules. This means that UK (and other foreign) companies will not be able to bid for main contracts but should (as with the Bechtel contract) be able to compete for sub-contract work. A second major source of funding will be through the Multi-Donor Trust Fund to be agreed at Madrid. UK companies should be well placed to compete for this work (and have a strong record in winning contracts from the IFIs and the UN).

Oil & Gas

6. The US Department of Defence is responsible for funding oil & gas work. Their contracting procedures are opaque, and not as open to non-American firms. A number of UK companies are bidding (with US partners) for oilfield development work in the north and south sectors.

7. The DTI has focused on two issues in dealing with Iraqi oil policy. Firstly to achieve sight of and influence over US/CPA short term actions or longer term policy on the Iraqi oil sector. This was consistently unsuccessful until five weeks ago when we inserted a senior representative, Terry Adams into the CPA oil team. This has improved our understanding to some extent, but Adams' access to information and decision making meetings appears to have been restricted by the CPA. It is important to continue to pursue this strategy with Washington as well as through Adams and through Iraq Rep in Baghdad.

8. The second strategy is to begin to build relationships directly with senior managers in the oil ministry and the national oil company. Adams is leading on this for us and is proving very effective. We have committed to two areas of action. Firstly we have offered to produce consultation/discussion papers written by the best UK sources on management and technical issues for use by the Iraqis. These will offer options and advice on subjects of the Iraqis choosing in an effort to bridge the skills/knowledge gap caused by years of isolation. We have £150k designated for this.

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9. The DTI is also using education through the Chevening scheme and through support for an Imperial College initiative as a non contentious way of offering UK plc an early role in Iraq. We have £25,000 reserved for this.

10. This work is vital in the commercial context: if we do not get the policy framework right and build strong relationships now, efforts to secure future oil contracts will be seriously hampered. The Prime Minister raising the issue with Bush in his VTC earlier this week was very much appreciated - we will need further assistance.

Our Concerns

11. Our major concern is lack of openness in the CPA's tendering/procurement procedures resulting in a possible bias towards US firms. This is particularly important when dealing with contracts financed through non-US Government funds. . Although the CPA does publish tender notices, it does not publish a list of contracts awarded or their value. We are pursuing this in Baghdad and in Washington. TPUK has also paid for a procurement consultant to work in the CPA Ministry of Finance to make procurement more transparent and ensure that UK firms are on the CPA's bidding lists. We shall also fund secondments to the proposed Project Management Office in Baghdad, which will be responsible for the disbursement of the additional \$20 billion, when approved by Congress.

How are UK Companies Doing?

12. Quite well given that most of the work so far is US funded. Up to 28 August, the breakdown of Bechtel sub-contracting by nationality places Iraqi firms first with 36%, US firms second with 28% and UK firms third with 16%. British firms have also won contracts in other areas. In financial services, De la Rue have been awarded the contract to print a new Iraqi currency. A consortium including Standard Chartered won a contract from the Coalition Provisional Authority to set up a Trade Bank for Iraq. UK firms dominate the private security sector. Erinsys have won a major contract to provide security in Iraq's oilfields. Olive Security has contracts with several USAID prime contractors, and Armor Group are providing additional security to Bechtel. Datasat has won a major contract to rebuild international telecommunications links. On power, Cummins, Aggreko and Siemens UK have all won contracts.

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Concerns of UK Companies

13. While some parts of UK industry would have preferred a specific commitment from the US on reconstruction contracts in the light of our contribution to the military campaign, most, including our own Working Group, accept that it is not realistic to demand equal access for British companies to US funded reconstruction work, or an inside track for contracts.
14. Companies remain concerned that the UK has untied its development assistance, which means that UK companies do not enjoy privileged access to UK development funds in the way that US companies do; that the current risks of doing business in Iraq mean that ECGD cover is not available (see below); and that HMG (unlike the US) has not made available funds for British business to become involved in reconstruction, and to establish a longer term presence in Iraq.
15. Relying aid is unrealistic. But the additional risk and difficulties in entering the Iraq market have led to a number of companies calling for some sort of business support fund from HMG, perhaps modelled on the Know How Fund set up for Central and Eastern Europe to help them manage the transition to a free market economy and to facilitate access for British business. TPUK's programme resources, even reallocated from lower priorities, allow only for small-scale, limited funding for initiatives (e.g. conferences, seminars, missions when safe to visit) aimed at positioning UK firms for contracts, but these sums are insignificant compared to the overall level of UK funding for Iraq and that available to foreign competitors, particularly the US.
16. We are also working closely with colleagues from across Whitehall. This includes ensuring that commercial interests are factored into economic policy on Iraq and helping DFID identify UK companies with equipment and/or resources to support the implementation of the CPA (South) Action Plan.
17. The British Embassies in Jordan and Kuwait are identifying local companies who can act as agents or business partners for British firms who want to trade with Iraq but do not have to travel there. This is primarily aimed at suppliers of goods into Iraq and at small and medium sized enterprises. There will be an Iraq focused trade mission to Jordan in December and we hope to organise a similar one to Kuwait early next year.

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ECGD

18. It will be some time before ECGD can consider support for normal Medium Term credit or Overseas Investment Insurance (OII) for Iraq. Notwithstanding Iraq's clear economic potential, both economic, security and political risks will remain high.

19. Furthermore, Ministers are not prepared to consider cover under 'Ministerial Instruction' on ECGD's Account 3.

20. However, ECGD is actively considering whether it could provide support for UK exports to Iraq on 180-360 days terms. ECGD is looking at whether it can provide 100% guarantees to banks opening letters of credit on behalf of the Trade Bank of Iraq to secure payments due under contracts placed with UK exporters. HM Treasury is currently considering these proposals.

21. In the longer term, as stability strengthens we would hope to see:

- The private market taking on credit insurance for short term business;
- ECGD moving to its more traditional role of supporting more project oriented business;
- Subject to a satisfactory security situation ECGD being able to consider cover for UK investments in Iraq.

Iraq Unit
Trade Partners UK

10 October 2003

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