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THE YEAR OF TRANSFER TO DATE

SIGIR's January Report designated 2008 as the "Year of Transfer" in Iraq relief and reconstruction, defining three measures to assess performance: transfer of reconstruction funding responsibility, transfer of U.S.-funded assets, and transfer of security responsibilities. Progress was achieved on each of these during this reporting quarter.

Completing Iraq's relief and reconstruction is now an Iraqi-led mission driven by Iraqi-developed and Iraqi-funded solutions. The management responsibilities for moving forward on national recovery have shifted into the hands of Iraq's national and local authorities, with the United States and the international community providing targeted support.

TRANSFER OF RECONSTRUCTION FUNDING RESPONSIBILITY

In January of 2004, the U.S. government estimated that between \$50 and \$100 billion would

be needed to rebuild Iraq.¹ To date, \$118 billion in U.S., Iraqi, and international funds has been committed to the program. The Government of Iraq's (GOI) share of the investment for relief and reconstruction reached \$50 billion this quarter, equaling the cumulative U.S. investment. As Table 1.1 reveals, Iraq's current investment in relief and reconstruction is more than three times current U.S. investment.

IRAQ'S CONTINUING INVESTMENT GROWTH

In a recent review of progress, conducted pursuant to the requirements of the *International Compact for Iraq* (Compact), the GOI noted that "Iraq is a rich country with skills and the wealth of its natural resources. Rather than aid, Iraq is looking for partnership and cooperation that will help it unlock its own resources."²

Deputy Prime Minister Barham Salih recently echoed the Compact's conclusion, noting that

U.S./GOI FUNDING FOR IRAQ RECONSTRUCTION, BY CALENDAR YEAR (\$ BILLIONS)

	2003/2004	2005	2006	2007	2008/2009
United States	\$23.07	\$6.61	\$7.28	\$9.33	\$4.17
GOI	\$16.00	\$5.03	\$6.18	\$10.06	\$13.06
Total	\$38.06	\$11.61	\$13.15	\$18.60	\$17.43

Sources: GOI, *Republic of Iraq: Budget Revenues and Expenses 2003, July–December*; Presidency of the Iraqi Interim National Assembly: *The State General Budget for 2005*; GOI 2006 Budget (as approved by TNA and written into law December 2005); U.S. Treasury, response to SIGIR data call (10/15/2007, 1/4/2008); GOI Budget 2008: Overview of Revenue and Expenditure, 2007–2008; Ministry of Finance, "Iraqi Federal Budget 2008," provided by the U.S. Treasury (6/29/2008).

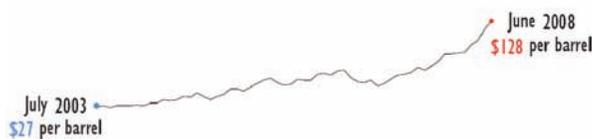
Note: Numbers are affected by rounding. U.S. appropriations shown reflect cumulative totals of funds enacted in each calendar year.

TABLE 1.1

“Iraq does not need financial assistance.” The recent Compact review also highlighted areas of progress in Iraq, including the issuance of more than 2,000 licenses to establish new private sector businesses in 2007.³

Oil Windfall

Unlike Afghanistan, Iraq has abundant financial resources to fund relief and reconstruction projects. Last November, the GOI estimated that oil income in 2008 would amount to \$35 billion. But with oil now hovering around \$125 per barrel—about five times what it was five years ago—and Iraq’s oil production at record levels, SIGIR estimates that oil revenues for 2008 could exceed \$70 billion.



Along with Iraq’s burgeoning oil revenues, significant amounts of unspent money from the 2006 and 2007 Iraqi budgets remain available for further infrastructure investment by the GOI.

Budget Execution

Notwithstanding its significant fiscal resources, Iraq continues to struggle to execute its capital budgets. In 2006, the GOI reported that it executed 22% of its capital budget. That rate notably increased to 63% in 2007, but execution rates of provincial capital budgets continue to be low. As

of March 2008, only 2.7% of the cumulative capital budgets allocated to the provinces (excluding the Kurdistan Regional Government) for 2008 had been expended.⁴

To address budget execution problems, the GOI raised limits on contract authorization at the ministry level to \$50 million for key ministries and to \$10 million for the provinces. The GOI also eliminated the Central Contracts Committee, which had been attached to the Economic Affairs Committee of the Council of Ministers, replacing it with contract committees within ministries.

The Procurement Assistance Centers continue to support national and provincial training efforts and guided technical assistance projects to improve budget execution. But continued slow progress on implementing the new Iraqi Financial Management Information System (IFMIS) limits the transparency and efficiency of Iraq’s budgeting system.

THE FUTURE OF U.S. INVESTMENT

On June 30, 2008, the President signed into law the Supplemental Appropriations Act, 2008 (the Supplemental), which includes conditions-based restrictions on the use of certain appropriated U.S. funds for Iraq. The most significant new condition requires that U.S. reconstruction funds be made available only to the extent that the GOI matches them on a dollar-for-dollar basis. This provision applies to new U.S. assistance provided through the Department of State and the U.S.

Agency for International Development. Additionally, the Congress implemented these other conditions:

- the submission of new anticorruption strategies
- the development of more detailed plans for future Provincial Reconstruction Team (PRT) activities
- the execution of an asset-transfer agreement between the United States and Iraq
- a prohibition on new prison construction

SIGIR previously highlighted the problems with prison construction in Iraq. Those problems are most acutely reflected in this quarter's inspection of the failed Kahn Bani Sa'ad Correctional Facility project. See *SIGIR Inspections* in Section 3.

The Supplemental contained approximately \$4.2 billion in new funds for Iraq's relief and reconstruction, appropriated through the Iraq Security Forces Fund (ISFF), Economic Support Fund (ESF), Commander's Emergency Response Program (CERP), and International Narcotics Control and Law Enforcement Affairs Fund (INCLE).

With its passage, U.S. investment in Iraq's reconstruction achieved these milestones:

- **ISFF.** Total appropriations for the ISFF reached \$17.9 billion, almost equaling the \$18.4 billion appropriated to the Iraq Relief and Reconstruction Fund 2. Total U.S. funding for Iraq security now stands at \$27 billion,⁵ equaling about \$56,000 per Iraqi police officer, soldier, and security officer.⁶
- **CERP.** New appropriations of \$800 million for the CERP pushed total appropriations to \$3.5 billion, almost equaling the total amount appropriated to the ESF, which has received \$3.7 billion. Since 2004, CERP funding has increased by 80%. The Congress has raised concerns about risks arising from weak metrics for measuring CERP performance.
- **ESF.** ESF received a total of \$527 million in FY 2008 supplemental and FY 2009 bridge funding, increasing total U.S. appropriations to the fund by over 16%.

Although the Supplemental provides new funding for Iraq's relief and reconstruction, significant amounts of unobligated funds from prior-year appropriations await execution. For the status of major U.S. funding accounts, see Table 1.2.

TRANSFER OF ASSETS

The transfer and sustainment of U.S.-funded assets to the GOI continues to be a key challenge. As SIGIR previously reported, there exists a continuing need for a new and definitive asset-transfer agreement between the United States and the GOI. The lack of such an agreement has resulted in the unilateral transfer of many projects to the GOI without formal acceptance, increasing the risk that the U.S. investment in Iraq will be wasted. SIGIR currently is executing another review of the asset-transfer process, which will appear in the next Quarterly Report.

STATUS OF MAJOR U.S. RECONSTRUCTION ACCOUNTS (\$ BILLIONS)

U.S. FUND	APPROPRIATED	OBLIGATED	% OBLIGATED	EXPENDED	% EXPENDED
IRRF 2	\$18.39	\$17.82	97%	\$17.13	93%
ISFF	\$17.94	\$12.61	70%	\$9.93	55%
ESF	\$3.74	\$2.62	70%	\$1.53	41%
CERP	\$3.49	\$2.88	83%	\$2.40	69%
TOTAL	\$43.56	\$35.93	82%	\$30.99	71%

IRRF 2: DoS, *Iraq Weekly Status*, July 2, 2008. ISFF: OSD, response to SIGIR data call, July 9, 2008. ESF: DoS, *Section 2207 Report*, October 2007; ITAO, responses to SIGIR data call, January 4, June 29, and July 7, 2008; GRD, response to SIGIR data call, July 2, 2008; USAID, responses to SIGIR data call, June 29, July 1, July 15, and July 17, 2008; ITAO, *Essential Indicators Report*, July 10, 2008; OMB, response to SIGIR data call, January 2, 2008. CERP: OSD, response to SIGIR data call, July 18, 2008; INL, response to SIGIR data call, July 2, 2008.

Note: Numbers are affected by rounding.

TABLE 1.2

TRANSFER OF SECURITY

The last of the five U.S. Surge brigades redeployed out of Iraq in July. The Commanding General in Iraq, General David Petraeus, is now in the midst of a 45-day evaluation period, and he will make further recommendations on troop levels by September.

The surge is partially responsible for the drop in the total number of security incidents to 2004 levels.⁷ Iraqi civilian deaths are 75% lower than July 2007 levels, which was the high point of violence in Iraq.⁸



Key developments in the security sector this quarter notably include successful operations by Iraqi Security Forces in Basrah, Sadr City, Mosul, and Amara. The Sons of Iraq program—which employs Sunnis in the security sector—now has more than 100,000 members; a new Daughters of Iraq component also has been established.

PROVINCIAL IRAQI CONTROL

After a seven-month lull in the process, another province was transferred to Provincial Iraqi Control (PIC) this quarter. With the transfer of Qadissiya, 10 of 18 provinces (comprising 42% of the population) have now been turned over to Iraqi security control. Anbar is scheduled to transfer next. The GOI has stated that it could assume full security responsibility of all provinces by the end of 2008, although the scheduled PIC process extends into 2009.⁹

FUNDING FOR THE IRAQI SECURITY FORCES

A new SIGIR review of ISFF funding revealed that \$4.7 billion, or approximately one-third of all ISFF funding, has been programmed for infrastructure. Unobligated balances for infrastructure projects amount to more than \$1 billion, which means that ISFF-supported security construction projects could continue into 2010. See *SIGIR Audits* in Section 3.

CONTRACTOR IMMUNITY

Negotiations continue between the United States and the GOI on a strategic framework governing

the U.S. presence in Iraq beyond the end of 2008. From a relief and reconstruction perspective, one of the most critical issues under discussion is contractor immunity. Existing agreements provide U.S. contractors in Iraq with blanket immunity from prosecution under Iraqi law. But the GOI is seeking to modify, if not eliminate, that immunity. Such action would acutely affect

the status of private security contractors in Iraq. SIGIR estimates that about 70 private security companies have operated in country since 2003, with cumulative contract values totaling approximately \$4.5 billion. The removal of immunity could lead to a contractor exodus, which would impose significant limitations on U.S. relief and reconstruction operations.

NATIONWIDE RECONSTRUCTION

The U.S. reconstruction program continues to assist the GOI to improve the delivery of basic services, to promote stable governance, and to foster economic development. Section 2b of this Report examines how the United States is working to help Iraq achieve these goals through reconstruction and capacity-development initiatives.

Essential services in Iraq improved this quarter, but they remain uneven and are not adequate to meet current demand. Improved security across the country has helped reduce attacks on oil pipelines, and the electricity sector's expanded operations and maintenance programs have helped push grid production up. The GOI still struggles to develop effective water and sewer services; emblematic of this struggle is the fact that two-thirds of the raw sewage produced in Baghdad flows untreated into rivers and waterways.¹⁰

GOI PURCHASE OF U.S. PRODUCTS

The GOI has significantly increased spending on U.S.-made products, funding more than \$8 billion in procurements, including a nearly \$5 billion order for Boeing aircraft and a \$500 million order for General Electric power-generation equipment. Iraq made progress this quarter in its U.S. Foreign Military Sales (FMS) program, through which it uses its money to purchase defense equipment from the United States using U.S. procurement processes. The GOI has already committed \$2.5 billion of the \$2.9 billion set aside for the program.

U.S. EFFORTS BUILD IRAQI BUSINESS CAPABILITIES

The Iraqi-based Industrial Zone (I-BIZ) initiative is a new DoD innovation that is building Iraqi capacity. Through I-BIZ, the U.S. military establishes secure centers next to Coalition bases where privately owned small and medium-sized Iraqi businesses can operate.¹¹



Pipeline Exclusion Zone in Kirkuk: A success story in the resurgence of Iraq's oil industry.

The Iraqi First program continues to help grow the Iraqi economy by emphasizing the award of U.S.-funded reconstruction contracts to Iraqi firms. This quarter, five of the six project sites visited by SIGIR inspectors were awarded to local contractors. For executive summaries of these and other inspections, see *SIGIR Inspections* in Section 3.

Iraq's Electronic Funds Transfer (EFT) system expanded this quarter. Catalyzed by investment from the Joint Contracting Command-Iraq/Afghanistan, which has used the system to transmit more than \$100 million in contract payments, the EFT program now reaches bank branches in many Iraqi provinces. Implementing EFT is key to cutting down on corruption in the banking and contracting systems.

The GOI has reportedly committed to spend \$400 million to restart its state-owned enterprises (SOEs); \$50 million in U.S. funds has already been appropriated to support 34 restarted factories, reportedly creating 25,000 new jobs. SIGIR's new overview of this U.S. program is in Section 3.

OIL PRODUCTION RECORD

Iraqi oil production this quarter reached 2.43 million barrels per day, the highest quarterly

average since the 2003 invasion. This increase stems in part from improved security across Iraq and the success of the Pipeline Exclusion Zone (PEZ) program. The \$34 million Kirkuk-to-Baiji PEZ segment is a system of ditches, berms, fences, and concertina wire protecting oil pipelines, which are secured by Iraqi security forces. The success of the program is evident in the fact that there have been no successful attacks on northern oil lines this year.

SIGIR conducted an inspection of the PEZ segment from Kirkuk to Baiji this quarter. A summary of the report is in Section 3. Work also began this quarter on the next leg of the PEZ, which will extend from Baiji south to Baghdad.

ELECTRICITY CAPACITY GROWING

Growth continues in Iraq's electricity sector. On July 8, 2008, peak generation reached 5,615 MW,¹² and substantial increases in generation capacity are expected as projects come online toward the end of this year, which could add up to 1,600 MW to the grid. Publicly available power—which is provided virtually without fees—meets approximately 55%¹³ of demand. Private generators make up for much of the shortfall.

GOVERNANCE

The GOI faces several important governance hurdles that it must address this year to promote political reconciliation.

KEY LEGISLATION STILL STALLED

As SIGIR previously reported, there remains a critical need for new provincial elections. Such elections are an essential element to achieving political reconciliation across Iraq.

The **Provincial Powers Law**, which came into effect in February, provided that provincial elections should occur in October 2008, but further supporting legislation is needed before these elections can occur. It does not appear that the GOI will approve and implement the legislation necessary to hold provincial elections this year.

Progress remains stalled on the **Hydrocarbon Laws**. The primary points of disagreement continue to be disputes over control of the Kirkuk oil fields and the level of management authority vested in the central government.

The GOI has implemented several other laws, including the **Amnesty Law** and the **Justice and Accountability (De-Ba'athification) Law**. The Amnesty Law resulted in the release of 79% of the prisoners held by the GOI.¹⁴ The successful reconciling effects of these two laws was evidenced recently when the Sunni political bloc (Tawafiq) ended its boycott of the Council of Ministers.

NORMALIZING INTERNATIONAL RELATIONS

This quarter, the United Arab Emirates (UAE) and Kuwait appointed ambassadors to Iraq, the first Gulf States to do so. Normalizing relations with its neighboring Gulf nations is essential for Iraq to stabilize. Similarly, continued progress on reducing Iraq's international debt will promote stability. In this regard, UAE recently announced that it will forgive the Iraqi debt it holds, totaling about \$7 billion.¹⁵

REBUILDING THE PROVINCES

The responsibility for moving forward on reconstruction in Iraq has shifted to Iraqi national and local authorities, with the U.S. and the international community playing important supporting roles. Provincial Reconstruction Teams, which lead Coalition support at the local level, are increasingly moving into provinces that they previously had not reached. Section 2c of this Report reviews progress in the 18 Iraqi provinces, providing snapshots of the ongoing reconstruction activities within each of them.

This quarter, SIGIR notes these important developments in the provinces:

- **Two New PRTs in Kerbala and Najaf.** Two U.S. PRT teams—Najaf and Kerbala—have moved out into provinces without U.S. military presence. This is a significant milestone in

this evolving program because the U.S. teams are located on bases of the Iraqi Army Eighth Infantry Division.¹⁶

- **First ATM in Diyala.** This quarter, the first automatic teller machine opened in Baquba, the capital of Diyala.

During a visit to Diyala province this quarter, SIGIR learned that PRT officials in that province are assisting the provincial government with expenditure of its 2006 budget—which is still just 85% expended. Moreover, Diyala has yet to spend its 2007 or 2008 budgets, and when asked to submit a request for supplemental funds in 2008, the Provincial Council declined.¹⁷

SIGIR OVERSIGHT

AUDITS AND INSPECTIONS

This quarter, SIGIR issued two capping reports assessing and analyzing SIGIR's previous audits and inspections. The audit capping report identified four key contributing causes to program deficiencies:

- the need to better understand the potential impact of an unstable security environment on contingency reconstruction efforts
- the need for an integrated organizational management structure that provides effective

interagency coordination and program accountability

- the need to attract, develop, and retain qualified program and contract management personnel who can effectively implement reconstruction programs
- the need to work closely with host-country government officials to develop reconstruction projects and programs that they want and that will be maintained



Kahn Bani Sa'ad Correctional Facility: A \$40 million project, incomplete and abandoned.

The inspections capping report found similar patterns caused by these shortfalls:

- poorly trained or unqualified contractor personnel
- the use of inferior or inadequate construction materials
- weak government quality assurance programs

Of the 115 projects assessed by SIGIR to date, 41 were found to have no deficiencies. Successful projects were chiefly due to effective quality control management by the contractor and good quality assurance programs by the government.

SIGIR has now completed seven focused contract reviews of the largest IRRF contractors, with two issued this quarter. The new review of task orders valued at \$367 million awarded to Parsons Delaware, Inc., for security and justice projects, found that only one-third of the original projects were completed. Moreover, more than \$140 million of the contract funds were paid for projects that were either terminated or canceled. The most egregious failure was the Kahn Bani Sa'ad Correctional Facility in Diyala province, a \$40 million structure that was eventually abandoned

by U.S. reconstruction managers along with over a million dollars worth of material and equipment left onsite.

A SIGIR inspection of Kahn Bani Sa'ad this quarter found that, although security concerns affected the project, the quality of construction was so poor that some sections need to be demolished and reconstructed.

SIGIR's focused contract review of work in the water sector by FluorAMEC revealed that half of the planned work was canceled due to sector funding constraints. Most of the canceled projects were terminated before substantial costs were incurred. The work that FluorAMEC did complete, however, was generally well done.

A SIGIR audit this quarter found that the Iraq Reconstruction Management System (IRMS), the system created by the U.S. government to keep track of projects, is not being properly used. Although the majority of expensive infrastructure projects are now complete, hundreds of significant projects are still ongoing, and IRMS should be the basis for keeping track of them.

INVESTIGATIONS

As of June 30, 2008, the work of SIGIR investigators has resulted in 16 arrests, 17 indictments, 8 convictions, and more than \$17 million in fines, forfeitures, recoveries, and restitutions. Five defendants are pending trial in September 2008, and an additional four defendants await the scheduling of trial dates.

Since SIGIR's last Quarterly Report, the

Procurement Fraud Branch suspended 19 more individuals and companies, bringing the total suspensions to date to 77. In addition, 8 individuals and companies have been proposed for debarment by the Army, bringing the total proposed debarments to 43. Total debarments remain at 25. For more on SIGIR's investigative work, see *SIGIR Investigations* in Section 3.

THE HUMAN TOLL

Attacks on the International Zone, which spiked in March and early April, tapered off significantly as the GOI gradually reasserted its control over Sadr City. Nonetheless, violence continues to pose a deadly threat to personnel involved in reconstruction activities.

CASUALTIES

The United States lost several citizens serving the reconstruction program in Iraq:

- On June 24, Steve Farley, a DoS employee serving on the ePRT for the Sadr City and Adhamiyah districts of Baghdad, was killed when a bomb exploded at a local council meeting in Sadr City.¹⁸ Two U.S. Army soldiers and two DoD civilian employees also died in this attack. This bombing occurred the day after a similar incident in a town southeast of Baghdad, in which a local politician opened fire on U.S. troops as they were about to enter a city council building near Salman Pak. At least two U.S. soldiers were killed in this attack.¹⁹

- This quarter, the Department of Labor (DoL) reported 48 new death claims for civilian contractors working on U.S.-funded projects in Iraq. Since 2003, 1,229 death claims have been filed with DoL.
- DoS reported that 15 U.S. civilians died in Iraq this quarter. Since the beginning of the U.S. reconstruction effort, 271 U.S. civilians have died in Iraq.
- Two journalists were killed in Iraq this quarter. According to the Committee to Protect Journalists, 129 journalists and 50 media support personnel have been killed in Iraq since March 2003.²⁰

This quarter, U.S. Embassy personnel began moving into the \$788 million New Embassy Compound,²¹ and the hardening of housing for U.S. mission personnel at selected sites in the International Zone is underway. Also, in June 2008, the World Health Organization (WHO) established a permanent office in Baghdad. The

Special Representative for Iraq of the United Nations Secretary General stated that WHO's decision demonstrates the UN's intention to render increased assistance to the people of Iraq.²²

REFUGEES

Effective July 7, 2008, a new immigrant visa will allow up to 5,000 Iraqi contractors and their families to enter the United States as immigrants each year for the next five years.²³ Iraqi citizens who were employed by the U.S. government or U.S. government contractors in Iraq on or after March 2003 for at least one year are eligible for this special visa. The worker must have provided "faithful and invaluable" service to the U.S. government.