



# SIGIR Observations

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## THE YEAR OF TRANSITION ENTERS THE FOURTH QUARTER

This 11th Quarterly Report from the Special Inspector General for Iraq Reconstruction (SIGIR) covers a period of significant activity fraught with challenge and filled with transitional events.

The quarter's most notable transitional event was the U.S. government's effort to ensure that the money remaining in the Iraq Relief and Reconstruction Fund (IRRF) was fully obligated by the statutory deadline of September 30, 2006. During an early August hearing on U.S. contracting in Iraq, Senate Committee on Homeland Security and Governmental Affairs Chairman Susan Collins raised concerns with SIGIR about potential waste in the "race to obligate." Thus, SIGIR monitored this process

throughout the quarter, issuing a quick reaction audit on improper IRRF obligations in late September. For an executive summary of this audit, see Section 3.

As of October 18, 2006, most U.S. agencies had not yet provided SIGIR with complete data on the status of IRRF obligations. The Joint Contracting Command-Iraq/Afghanistan, however, reported that it effectively had executed its plan to obligate the IRRF within its purview by the September 30, 2006 deadline. Some flexibility remains with regard to IRRF funds. They can still be de-obligated from one project and re-obligated to another, as necessary, until the end of FY 2007.

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## CHALLENGES CONFRONTING TRANSITION

Reaching the IRRF obligation deadline emphasizes that the U.S.-funded phase of Iraq's relief and reconstruction has entered its concluding stages. The Government of Iraq's (GOI) success in building on the foundation established by the U.S. relief and reconstruction program will now depend in part on the GOI's ability to attract more support from other donors and the private sector.

In the last Quarterly Report, SIGIR termed the next phase of the reconstruction program the "multilateral phase." To that end, negotia-

tions continue on the International Compact for Iraq, which will generate more financial support from and active participation by the broader international community.

For transition to succeed, the GOI must improve security, especially in Baghdad. GOI progress on national reconciliation and strengthening its rule-of-law system are essential elements to resolving the serious and continuing security crisis that plagues Iraq. With respect to reconciliation and rule of law, there exists a particular problem in Baghdad:

all local government offices are held by members of Shia political parties. This means that the Sunnis have virtually no voice in Baghdad's governance.

Some of the obstacles to a successful transition include:

- the deteriorating security situation across Iraq
- poor capital budget execution by the GOI
- corruption within certain Iraqi ministries
- breakdowns in the transfer of IRRF assets to Iraq

## Security Situation

The deteriorating security situation across Iraq continues to impede progress in the reconstruction program, causing project delays, preventing travel to many sites, increasing security costs, and endangering contractors' lives. This situation directly affected SIGIR's operations during this quarter: SIGIR inspectors canceled or altered a number of visits to sites across Iraq because of security threats.

The security problems in Iraq are fueled by several groups seeking to undermine the country's government, including Al Qaeda, sectarian militias, and criminal gangs. The lethality of the threat generated by these groups was especially acute this quarter in Baghdad. Moreover, October 2006 was the deadliest month for U.S. forces since January 2005: 98 soldiers had been killed as of October 29, 2006.

Major General William Caldwell alluded to the security crisis in Baghdad when he reported in mid-October that Operation

Forward Together II had "not met our overall expectations of sustaining a reduction in the levels of violence... We are working very closely with the government of Iraq to determine how best to refocus our efforts." Decisions regarding this strategic refocusing are expected to be made public soon.

Sabotage of Iraq's infrastructure, particularly in the electricity sector, hindered reconstruction efforts this quarter. On October 20, 2006, a series of attacks on power lines providing electricity to Baghdad isolated the city from the national power grid, leaving only about 800 megawatts of power available within the "Baghdad Ring" (the grid supporting the capital). There was thus only enough power that day to generate a few hours of electricity for Baghdad's 7 million inhabitants.

The power problem in Iraq is compounded by the fact that repairing power lines is nearly impossible because of sniper attacks and death threats to repair crews. As Iraq's Minister of Electricity reported to SIGIR:

Every day I send repair teams [to repair power lines], but they can't get to the area: there are too many insurgents...I've spoken to [everyone]...no one can help.

To address the power lines' vulnerability, the U.S. Army Corps of Engineers Gulf Region Division (GRD) has ordered 25 Lindsey Towers—temporary towers that can be used for rapid repair efforts. GRD also has a program to reinforce the existing towers so that they can better survive attacks.

Security threats across Iraq inhibited progress by the Provincial Reconstruction Teams (PRTs), which comprise the most important U.S. capacity-building initiative at the local government level. During this quarter, SIGIR visited seven of the ten PRTs. For details on the challenges that this program faces, particularly with respect to security and resources, see the summary of SIGIR's PRT audit in Section 3.

### **GOI Budget Execution**

Although Iraq's Unity Government has been in power since May 2006, Iraq's ministries still struggle with capital budget execution as they have since the first sovereign government took office in mid-2004. The GOI's capital budget is estimated at \$6 billion, which is nearly 20% of the total budget. Part of the problem reportedly arises from bureaucratic resistance within the Ministry of Finance, which traditionally has been slow to provide funds. Iraqi ministries generally can pay salaries and execute administrative budgets, but many—in particular, the Ministry of Oil—have difficulty executing their capital budget programs.

The U.S. government is working intensively with the GOI to help resolve the budget execution problem. However, unless GOI ministries execute their 2006 capital budgets, international donors will likely be reluctant to provide new funds to Iraq in 2007.

### **Transparency and the Fight Against Corruption**

Corruption afflicts a number of GOI ministries. Building capacity within the GOI's transparency institutions—the Board of Supreme Audit, the Commission on Public Integrity, and the ministry inspectors general—is the most important initiative in the fight against corruption.

During his seven-week visit to Iraq this quarter, the SIGIR met with all the Iraqi inspectors general, the President of the Board of Supreme Audit, and the Commissioner of Public Integrity. Significantly, in a meeting with the SIGIR and the Iraqi inspectors general, Prime Minister Nouri al Maliki pledged his strong support for the Iraqi inspector general system.

The SIGIR and the Department of State Inspector General met in Baghdad with the Iraqi inspectors general to advise them on strategies for training and structuring their respective departmental organizations. The SIGIR also met with the Minister of Defense and his IG, and found that the current condition of the oversight program at that ministry is excellent.

The U.S. Embassy's Anticorruption Working Group became more active during this quarter. In conjunction with that development, SIGIR worked with the Embassy to build more support for the Board of Supreme Audit and the Iraqi inspectors general: these organizations will now have a specially designated U.S. senior consultant advising them. The Commission on Public Integrity already has a senior consul-

tant advising it. Additionally, the Embassy designated a new transparency coordinator to ensure that Embassy programs supporting GOI transparency efforts complement one another.

SIGIR remains concerned about challenges confronting the fight against corruption within the GOI. This concern stems from a number of issues, including:

- The Ministry of Finance has explored the possibility of moving its foreign exchange accounts from the New York Federal Reserve Bank to other foreign banks, which may cause concern within the international community about the continuing transparency of these accounts.
- The mandate of the International Advisory and Monitoring Board (IAMB), created by UN Security Council Resolution 1483, expires at the end of 2006, ending the independent and external oversight of Iraqi oil revenues.
- The Council of Representatives has passed a resolution asking the Prime Minister of Iraq to close the two largest media outlets in Iraq because of their coverage of the new law on regionalization.
- International contractors still working on Coalition Provisional Authority-era (CPA) contracts funded by the Development Fund

for Iraq have indicated that, if these contracts are turned over to the GOI, they will ask for termination for convenience because they do not have confidence that they will continue to be paid for their services.

- Iraq ranks 137th of the 158 countries in Transparency International's 2005 Corruption Perception Index.

### **Incomplete Transfer of U.S. Assets to Iraqi Ministries**

The asset recognition and transfer process, begun in 2005 to catalogue and transfer IRRF assets to the GOI, appears to have broken down. The Ministry of Finance is not processing the data, as required by the agreed-upon procedures, and some data in the U.S.-developed Iraq Reconstruction Management System is incomplete or inaccurate.

The GOI is currently re-evaluating the overall asset transfer process, while the Iraq Reconstruction Management Office (IRMO) is intensifying efforts to develop a complete and accurate record of U.S. assets. The GOI must commit to taking appropriate measures that will ensure successful completion of the asset transfer process and thus secure the continuing operation and management of IRRF facilities and inventories.

## THE NEED FOR CONTINUED U.S. ASSISTANCE

Although more U.S. aid to Iraq will inevitably be necessary, SIGIR believes that future relief and reconstruction funding should be tied to specific actions by the GOI. That is, the Iraqi government should meet concrete milestones and political and economic benchmarks as a condition of future aid. One approach to consider toward achieving these goals is to provide new U.S. reconstruction assistance through conditional loans.

SIGIR believes that the U.S. government should pursue these important relief and reconstruction initiatives and issues:

- Engage the Department of Justice (DoJ) more fully in supporting the development of effective rule of law in Iraq.
- Finalize the memorandum of agreement between the Department of State (DoS) and the Department of Defense (DoD) on the PRT program.
- Invest more in building the operational and administrative capacities of the Iraqi ministries.
- Promote the International Compact for Iraq as the catalyst for the next phase of Iraq's relief and reconstruction.

### Expand Rule-of-law Efforts

U.S. government support to the GOI on rule-of-law reform has been fragmented because of poor coordination and insufficient definition of various agency responsibilities.

During the course of the IRRF program, the

U.S. government channeled much of the rule-of-law funding through the DoS Bureau for International Narcotics and Law Enforcement Affairs (INL), which had hundreds of contractors in Iraq but relatively few U.S. government personnel in actual operational control. The Multi-National Security Transition Command–Iraq (MNSTC-I), which was given the lead on police training in October 2005, used significant IRRF funding to support training and equipping Iraqi police.

The DoJ has significant inherent capability in criminal law, civil law, prosecutorial development, judicial training, and police training, but it received limited IRRF funding and thus has played a relatively minor role in the rule-of-law program. Because of its expertise, DoJ should play a larger role in defining and coordinating the strategic approach to the rule-of-law mission. Thus, the Embassy should consider appointing a senior rule-of-law coordinator from DoJ to bring the wide array of rule-of-law programs in Iraq under one umbrella. The new coordinator initially should execute an assessment of the entire program.

### Provide the PRTs More Personnel and Resources

The PRTs were created to help build local governance capacity in Iraq's provinces and to help Provincial Reconstruction and Development Councils identify, prioritize, and implement

U.S.-funded projects.

Four concerns about the PRT program emerged from SIGIR's audit of it this quarter:

1. DoD and DoS should more clearly define the allocation of responsibilities between them with respect to the PRT mission. Specifically, the memorandum of understanding between the two agencies addressing these key issues must be immediately finalized.
2. The PRTs need to be more consistently resourced and provided with the appropriate personnel to execute their mission.
3. Security concerns continue to inhibit the work of most PRTs, especially those not located with Regional Embassy Offices.
4. The PRTs should be funded for a sufficient period to ensure that their mandate is fulfilled. SIGIR strongly supports increasing the funding and extending the time for the PRTs.

For an executive summary of this audit, see Section 3.

## **Build Capacity in the Iraqi Ministries**

SIGIR continues to raise concerns about the capacity of Iraqi ministries to operate effectively. The current U.S. capacity-building efforts are relatively modest in scope and may not ensure that IRRF-funded infrastructure will be adequately managed and maintained after transfer. A core concern is the current inability of some ministries to take responsibility for managing IRRF facilities.

There is no generally agreed-on baseline for the capacity of the Iraqi ministries; thus, it is difficult to measure the results of U.S.-funded programs. Several ministries—oil, electricity, water, and defense—appear to have benefited from U.S. efforts to build capacity, but it remains unclear whether the GOI will commit the resources necessary to ensure the sustainment of IRRF projects and programs.

SIGIR raised concerns this quarter about the need for a revised strategic plan to better guide capacity building within the GOI. The current approach relies heavily on contractors to implement capacity-building programs, and the overall program does not have a single U.S. government official providing comprehensive operational direction.

IRMO has a \$65 million program for capacity building, but the list of needs is so long that this program will meet only a few of them. The U.S. Agency for International Development (USAID) has focused its capacity-building efforts on establishing a training school for Iraqi government technocrats. The two programs should be better coordinated. Both the Government Accountability Office (GAO) and SIGIR are conducting audits on capacity-building programs in Iraq.

## **Promote the International Compact for Iraq**

The International Compact for Iraq, currently under negotiation and expected to be completed soon, is designed to create a new partnership between the Iraqi government and the international community. It will also provide

a framework for further multilateral engagement on economic, political, and security issues in Iraq.

The Compact requires the GOI to commit to specific reforms, milestones, and benchmarks. Critical among these is the passage of a comprehensive hydrocarbon law. The international community concomitantly will commit to supporting Iraq's reform program, particularly the GOI's goal of financial self-sufficiency within five years.

From a financial perspective, the Compact is expected to galvanize international donors to:

- provide funds already pledged
- increase pledges to Iraq over the next several years

To ensure coordination of expanded donor programs and to avoid duplication of effort, the Compact is expected to use the existing Donor Committee and other coordinative mechanisms created in connection with the 2003 Madrid Donors Conference.

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## NOTABLE SIGIR ACTIVITIES THIS QUARTER

In executing its oversight mission this quarter, SIGIR issued 8 audits, which made 29 recommendations; and SIGIR's 9 project assessments presented many construction-related findings. SIGIR opened 20 new investigations this quarter, most arising from allegations of fraud, waste, and abuse in U.S. spending on Iraq's reconstruction.

Appendix A cross-references the pages and content of this Report that relate to SIGIR's statutory reporting requirements.

### Audits

The 8 final audit reports produced this quarter bring the total number of completed SIGIR audits to 73. SIGIR also issued 2 draft reports

and has 16 ongoing audits. Eight new audits are planned for next quarter.

SIGIR completed two audits this quarter that were requested by the Chairman of the Senate Armed Services Committee:

- Iraqi Security Forces: Review of Plans to Implement Logistics Capabilities (SIGIR-06-032)
- Iraqi Security Forces: Weapons Provided by the U.S. Department of Defense Using the Iraq Relief and Reconstruction Fund (SIGIR-06-033)

These two reports present nine recommendations to improve planning, accountability, capacity development, and resource manage-

ment of the Ministries of Defense and Interior. The two reviews were coordinated with GAO, the DoD Office of Inspector General, and the Under Secretary of Defense for Acquisition, Logistics, and Technology.

SIGIR also completed an audit of the overhead costs of the largest IRRF contractors. These costs, which were charged through “administrative task orders,” were very high in 2004 when little reconstruction work was getting done.

In conjunction with the DoS Office of Inspector General, SIGIR is conducting a review of an INL contract supporting the Iraqi police training program. SIGIR is also coordinating several oversight efforts with GAO and other accountability organizations.

## Inspections

SIGIR’s 9 project assessments completed this quarter brings the total number of project assessments completed to 65. Since the beginning of the program, SIGIR has completed 96 limited on-site inspections and 220 aerial assessments.

Most IRRF projects that SIGIR visited this quarter met contractual specifications. Quality control (QC) and quality assurance (QA) programs were essential to ensuring that contract specifications were met. Contractor performance and weak quality assurance programs were issues at a few of the project sites SIGIR visited.

SIGIR found some projects with design and construction deficiencies, including:

- At the Baghdad Police College, the contractor installed inferior wastewater piping and

joined it together improperly. The resulting wastewater leakage in the newly constructed buildings on the campus caused severe damage to the facilities and may pose serious health risks.

- At the Ninewa Provincial Police Headquarters in Mosul, the GRD terminated the contract because the work by an Iraqi contractor was substandard. The deficiencies involved the guard house, roof, air-conditioning units, water supply and distribution system, wall construction, bathrooms, generator installation, septic and sewer system, and electrical wiring.

At most of the other sites that SIGIR assessed this quarter, the government QA programs were effective in monitoring the contractor’s construction progress and workmanship.

## Investigations

SIGIR continues to field the largest number of U.S. criminal fraud investigators in Iraq. They are supported by staff at SIGIR headquarters in Arlington, Virginia.

During this quarter, SIGIR Investigations opened 20 new cases and closed 10 cases. To date, SIGIR has opened 256 cases and has either referred or unsubstantiated 164. Currently, SIGIR has 92 open cases; 25 of those cases are at DoJ, many in the final stages of prosecution. Four cases have resulted in convictions and are currently pending sentence.

This quarter, two SIGIR targets were convicted: Faheem Salam and LTC Bruce Hopfgardner, USAR. Faheem Salam pled guilty to

one count of a violation of the Foreign Corrupt Practices Act of 1997; he will be sentenced on November 3, 2006. Hopfengardner pled guilty to two conspiracy charges in a scheme to defraud the CPA in Hilla, Iraq. For details on these and other cases, see Section 3.

SIGIR formed a new task force this quarter to investigate contract fraud in Iraq. The members of this task force include:

- U.S. Agency for International Development Office of the Inspector General

- U.S. Army Criminal Investigations Division Major Procurement Fraud Unit
- Department of Defense Criminal Investigative Service
- Department of State Office of the Inspector General
- Federal Bureau of Investigation

On October 2, 2006, the task force's Joint Operations Center opened at SIGIR headquarters.

## FINANCIAL IMPACT OF SIGIR OPERATIONS

SIGIR oversight continues to produce tangible financial benefits. To date, SIGIR audits have saved \$10.9 million, recovered \$1.4 million, and improved the use of \$20.6 million. SIGIR auditors have challenged payments of \$306.9 million, which include possible duplicate payments, overpayments, payments for ghost workers, and work that was not completed. SIGIR also has made recommendations that improved property accountability valued at

\$65.3 million. The net potential beneficial impact of SIGIR audits is approximately \$405.1 million, as of September 30, 2006.

SIGIR inspections have produced recommendations that could potentially increase Iraq's annual oil revenues by \$1.278 billion.

SIGIR investigations have seized or recovered \$11.69 million in cash and assets in the course of SIGIR investigations. For the data supporting these benefits, see Appendix B.

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## THE HUMAN TOLL

The human toll in Iraq reveals the risks that confront the men and women working to promote Iraq's rehabilitation and transition to a fully democratic society. Recently described by the UN Secretary General's Special Representative as one of the most violent conflict areas in the world,<sup>1</sup> Iraq faces an increasingly complex and dangerous series of challenges to maintaining a safe and secure environment.

Evidence of the human toll is greatest among Iraqi civilians who continue to be killed, wounded, or displaced from their homes:

- The Iraqi Ministry of Health reported that more than 2,600 civilians were killed in September 2006, adding to the total of more than 6,600 civilians killed in July and August.<sup>2</sup> The UN estimated that more than 8,100 persons were wounded in July and August 2006 combined.
- Many Iraqis have been forced or have chosen (for security reasons) to leave their homes. The number of internally displaced persons<sup>3</sup> in Iraq is estimated at 1.3 million.

More than 300,000 of those have been displaced since the early February 2006 attack on the Golden Mosque in Samarra.

Contractors and civilians working in Iraq continue to be victimized by violence:

- Since the beginning of the Iraq reconstruction effort, 646 death claims for civilian contractors working on U.S.-funded projects in Iraq have been filed. In the quarter ending September 30, 2006, the Department of Labor reported 68 new death claims.
- DoS reports that eight U.S. civilians died in Iraq this quarter. Since the beginning of the U.S. reconstruction effort, there have been 196 U.S. civilian deaths in Iraq.
- Since March 2003, 85 journalists and 35 media support workers have been killed, according to the Committee To Protect Journalists. In the most recent quarter, 10 media-affiliated professionals were killed.