



Audit Report



OIG-06-029

INTERNATIONAL ASSISTANCE PROGRAMS: Review of Treasury Activities for Iraq Reconstruction

March 23, 2006

Office of
Inspector General

Department of the Treasury

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Abbreviations

ACH	Automated Clearing House
CBI	Central Bank of Iraq
CPA	Coalition Provisional Authority
IFC	International Finance Corporation
IFTF	Iraq Financial Task Force
IRRF	Iraq Relief and Reconstruction Fund
OIG	Office of Inspector General
OMB	Office of Management and Budget
OTA	Office of Technical Assistance
PSD	Treasury Departmental Offices’ Procurement Services Division
RTGS	Real Time Gross Settlement
SIGIR	Special Inspector General for Iraq Reconstruction
Treasury	United States Department of the Treasury
U.S.	United States

*The Department of the Treasury
Office of Inspector General*

March 23, 2006

Van B. Jorstad
Director, Office of Technical Assistance
Office of International Affairs

This report provides the results of our review of the Department of the Treasury's (Treasury) activities for Iraq Reconstruction, in which the Office of Technical Assistance (OTA) plays a central role. Our objectives were to (1) identify Treasury activities and funding involving Iraq relief and reconstruction and (2) determine the completeness and accuracy of the information provided by OTA in its reports to the Special Inspector General for Iraq Reconstruction (SIGIR) regarding its activities for Iraq reconstruction.

Treasury's Iraq reconstruction activities have been funded by two Iraq Relief and Reconstruction Funds (IRRF)—IRRF 1 and IRRF 2. We identified two OTA-administered reconstruction programs and found that as of August 31, 2005, approximately \$29.4 million had been obligated out of \$35.1 million apportioned for the programs and about \$23.2 million had been disbursed.¹

We reviewed selected contracts and related documentation to verify the fund-use status statement through August 31, 2005, provided to SIGIR, which is included in Appendix 2.

A more-detailed description of our objectives, scope, and methodology is included in Appendix 1.

We found that the fund-use status statement fairly presented the financial status of the contractual obligations and disbursements through August 31, 2005. In its March 20, 2006, response to our draft report, OTA management concurred with our findings. See Appendix 3 for a copy of the management response.

¹ As of February 28, 2006, about \$32.9 million had been obligated and about \$26.3 million had been disbursed.

Background

Office of Technical Assistance

OTA provides technical assistance to countries with transitional or developing economies. OTA is under the supervision of the Deputy Assistant Secretary for Technical Assistance Policy, who is 1 of the 6 deputies supporting the Assistant Secretary for International Affairs. The Deputy Assistant Secretary for Technical Assistance Policy develops, evaluates, and implements Treasury policies and positions on economic and financial assistance to countries with transitional or developing economies.

Since 1990, OTA has provided advisory services to governments in Central and Eastern Europe and the former Soviet Union to assist in their transitions to market economies. Typically, a Treasury advisor, with the support of short-term experts and technicians, advises a senior finance ministry or central bank counterpart. More recently, as countries in Eastern Europe and the former Soviet Union have made progress in their transitions, OTA has addressed challenges in other parts of the world, such as South Africa, Haiti, and Indonesia.

In Iraq, Treasury's primary reconstruction efforts are focused on establishing modern central bank functions and a nationwide payment system among local banks and the central bank. OTA has been administering the banking sector establishment program by awarding contracts and conducting procurement activities under six major projects. OTA is the only Treasury office whose works have been funded through the IRRFs.

Iraq Financial Task Force

To coordinate and support Treasury's reconstruction efforts, in March 2003 the Under Secretary for International Affairs created the Iraq Financial Task Force (IFTF) within the Office of International Affairs. The Director of International Affairs' Office of Middle East and South Asian Nations at that time was appointed to lead the task force.

The task of IFTF was to coordinate the planning and execution of Treasury's role in the post-war stabilization, administration, and reconstruction of Iraq. The staff of the task force was composed of officials of Treasury's Office of International Affairs, the Federal Reserve Bank of New York, Treasury's Office of the Fiscal Assistant Secretary, and a few detailed officials from the Department of the State and the United States (U.S.) Agency for International Development. At its heights, the task force had approximately a dozen staff members. IFTF and its function were folded into the Office of Middle East and South Asian Nations in August 2005.

IFTF served as liaison among Treasury and various organizations involved in the post-conflict reconstruction, such as the International Monetary Fund; the World Bank; Iraqi exiles, some of whom later became officials in Iraq; as well as the U.S. agencies involved in the reconstruction. Because Treasury's involvement was focused on the financial sector, IFTF's role was also focused on that sector.

In particular, IFTF was involved in discussing and planning the printing and delivery of the new Iraqi currency (the dinar); sought expertise from the Federal Reserve System, the Office of the Comptroller of the Currency, and the International Monetary Fund in formulating macroeconomic, monetary, banking and exchange rate policies to stabilize the economy; and coordinated the debt relief efforts with the members of the Paris Club,² working closely with the Treasury Office of International Debt Policy. As OTA was involved in technical assistance to Iraqi financial institutions, IFTF was actively engaged in its mission, providing support to the OTA advisors working in Iraq. The IFTF's work and the salaries of its staff were not funded by the IRRFs.³

² The Paris Club is an informal group of official creditors whose role is to find coordinated and sustainable solutions to the payment difficulties experienced by debtor nations. The first meeting was held in 1956 when Argentina agreed to meet its public creditors in Paris. There are currently 19 permanent members, including the United States. Iraq's external debt was estimated to be around \$120 billion, of which the Paris Club members were owed roughly \$40 billion. The rest of Iraq's debt was held by non-Paris Club governments, chiefly the Gulf States.

³ They were assigned to the task and thus compensated by their respective agencies.

Iraq Relief and Reconstruction Funds

On May 22, 2003, President Bush issued Executive Order 13303 to protect the Development Fund for Iraq⁴ and the proceeds from the sales of Iraqi petroleum and petroleum products to assure an orderly reconstruction of Iraq. This fund and dozens of others constitute the funding sources for Iraq relief and reconstruction. Among them are two appropriated funds⁵—commonly referred to as IRRF 1 and IRRF 2.

IRRF 1 was established by Public Law 108-11 in April 2003 for necessary expenses for humanitarian assistance, rehabilitation, and reconstruction in Iraq. Congress appropriated a total of \$2.475 billion for IRRF 1, and the Office of Management and Budget (OMB) allocated this amount among the U.S. Agency for International Development, the Department of Defense, the Department of State, and Treasury. The apportionment for Treasury was \$6.0 million.

IRRF 2 was established by Public Law 108-106 in November 2003 for the defense and reconstruction of Iraq and Afghanistan. Congress appropriated \$18.4 billion for IRRF 2, which OMB also allocated among the U.S. Agency for International Development, the Department of Defense, the Department of State, and Treasury. The original apportionment for Treasury was \$39.1 million, of which \$10.0 million⁶ was transferred to the International Finance Corporation (IFC), a member of the World Bank Group, under an agreement between the U.S. Government and IFC dated April 2, 2004. Therefore, the remaining two programs represent Treasury's actual reconstruction activities, for which \$35.1 million was funded by IRRF 1 and IRRF 2.

⁴ The Development Fund for Iraq is a fund established in May 2003 on the books of the Central Bank of Iraq by the Administrator of the Coalition Provisional Authority. This fund consists of the proceeds from the export sales of Iraq's oil as well as the funds remaining from the United Nation Oil-for-Food Program and other assets seized from the defunct regime.

⁵ An appropriated fund is one that receives appropriations from Congress.

⁶ Initially, \$10.0 million was allocated for Treasury to fund the Micro, Small, and Medium Enterprise Development Program.

Office of the Special Inspector General for Iraq Reconstruction

The Office of the SIGIR, formerly the Coalition Provisional Authority (CPA) Office of Inspector General, is charged with independently and objectively conducting and supervising audits and investigations relating to programs and operations funded by the IRRFs. The SIGIR, who reports to the Secretary of State and the Secretary of Defense, works closely with other agencies, inspectors general, and non-governmental entities to ensure that reconstruction funds for Iraq are handled effectively and without waste, fraud, or abuse.

The SIGIR submits quarterly reports to Congress outlining the key findings and progress related to Iraq reconstruction programs, as well as deficiencies and the corrective actions taken to improve the programs. IRRF-funded agencies are required to report their quarterly fund-use status to the SIGIR. Each quarter, the Treasury Office of Inspector General (OIG) reviews OTA's fund-use status statements as well as the SIGIR's quarterly reports to ensure the accuracy and completeness of the information relating to the Treasury's reconstruction efforts. OIG also coordinates the SIGIR's audit efforts pertinent to the functions of the Treasury.

Findings

Treasury Provides Technical Assistance and Support to Modernize the Iraqi Banking System

Under IRRF 1 and IRRF 2, Treasury was allocated funds for two Iraq reconstruction programs:

1. The Technical Assistance Program (IRRF 1, \$6.0 million)
2. The Banking System Modernization Program (IRRF 2, \$29.1 million)

The Technical Assistance Program provides advisory services to Iraqi officials in administering the economic, fiscal, and financial sectors. The funds allocated to the program have been used for various operating expenses and the provision of security for civilian

advisors and consultants, working for the economic, fiscal, and financial sector reconstruction in Iraq. The personnel included, but were not limited to, the Treasury officials who had expertise in bank regulation and resolution, tax and budget administration, and the formulation of economic and financial institution policies. As of June 5, 2003, 25 personnel were deployed in Iraq in four separate phases.

Assigned mostly in the Iraqi Ministry of Finance and the Central Bank of Iraq (CBI), the deployed personnel advised Iraqi officials on overall debt policy, budget and tax policies and administration, and bank operations. By the end of August 2005, Treasury had obligated the full \$6.0 million allocated under IRRF 1 for this program and had disbursed about \$4.7 million.

The purpose of the Banking System Modernization Program is to modernize the Iraqi banking system. OTA has been administering the program under six major projects.⁷ The projects are primarily to build financial sector infrastructure, purchase bank equipment, implement the core functions of CBI, train CBI staff, and establish security for CBI personnel and others involved in implementing the program.

To implement the core functions of CBI, OTA awarded contracts for planning, acquisition, installation, and initial operation of two essential components of a nationwide payment system for CBI. The two components are a Real Time Gross Settlement (RTGS) system, for making inter-bank payments with immediate finality across the books of the CBI; and an Automated Clearing House (ACH) system, for processing files of payment instructions, both debits and credits, and settling on a net basis across the books of CBI. The initial operation also included training of CBI staff and staff from other participant banks so that operational responsibility for the nationwide payment system can be transferred to CBI.

Also included in the program is an establishment of a Visa-based interim bank branch payments and clearing system. This project

⁷ Some of the major projects break down to several sub-projects with different contracts.

refers to the payments of the membership fees to Visa International Service Association on behalf of the Iraqi banks.

Typically, a contract is awarded by a contracting officer of the Treasury Departmental Offices' Procurement Services Division (PSD) at OTA's request. PSD monitors the execution of the contract and keeps the records. When an invoice arrives at OTA, an OTA official reviews and certifies it, and sends the invoice to PSD. PSD reviews the invoice and approves the payment. OTA then sends a payment notice to the Treasury Departmental Offices' Office of Financial Management. Upon receiving the notice, the Office of Financial Management pays the invoice.

The Banking System Modernization Program was funded through IRRF 2. Of the \$29.1 million apportioned for the program, Treasury had obligated about \$23.4 million and disbursed about \$18.4 million by the end of August 2005.⁸ In summary, from the total of \$35.1 million that Treasury received through IRRF 1 and IRRF 2 to execute the two programs, about \$29.4 million had been obligated and about \$23.2 million had been disbursed through August 31, 2005. As a result, \$5.7 million remained as the available, unobligated balance at the end of August 2005.⁹

The Financial Information Provided by OTA Fairly Presented the Fund-Use Status of Treasury's Iraq Reconstruction Activities

As required, OTA has provided the quarterly fund-use status statements to the Office of the SIGIR.¹⁰ To obtain evidence about the accuracy of this information, we selected a sample of four major obligations under the six major projects¹¹ to review the

⁸ By the end of February 2006, for the Banking System Modernization Program about \$26.9 million had been obligated and about \$21.4 million had been disbursed.

⁹ By the end of February 2006, a total of \$32.9 million had been obligated and \$26.3 million had been disbursed. As a result, about \$2.2 million remained as the available balance.

¹⁰ Currently, OTA sends monthly fund-use status statements to the SIGIR to provide more timely information.

¹¹ The contracts under these projects ranged in value from \$85,300 to \$8,835,037.

statements of work for the related contracts, funds obligated, and progress on the work. These obligations, described below, totaled approximately \$17.5 million, which is approximately 60 percent of the \$29.1 million allocated to Treasury for reconstruction projects under IRRF 2.

Description of Sample Projects

1. Financial Sector Senior Advisors and Consultants: Protective Services Transportation

This project provides secure transportation of senior advisors and consultants who are working to facilitate the program in Iraq. The services refer mainly to armored-vehicle transportation of the personnel. For the Protective Services Transportation project, \$4,770,951 was obligated as of August 31, 2005.

2. Essential Office Equipment for Banks

This project involves two contracts made through PSD. The first contract, awarded for \$1,065,335 in May 2004, procured laser printers, cartridges, batteries, computers, monitors, and other peripherals. The second contract, awarded for \$1,763,783 in June 2004, procured similar items. The total obligation for the two procurement contracts was \$2,829,118.

3. Visa-Based Interim Bank Branch Payments and Clearing System

As mentioned earlier, this project refers to the payments of the membership fees to Visa International Service Association on behalf of the Iraqi banks to establish an interim automated payment system. This project was approved by the CPA, and a memorandum for the obligation and disbursement was issued by the member of the CPA responsible for the project; hence, no further contract administration was required by OTA for the transaction. A total of \$1,134,000 was obligated as of August 31, 2005.

4. National Payment System (RTGS and ACH)

This project is an essential part of the banking system modernization program. As previously described, this project refers to an installation of two core bank payment systems – the RTGS and ACH systems. OTA awarded a single contract to execute the project. The amount of the contract, which was awarded in April 2005, was \$8,835,037. The contract line items included software for the RTGS and ACH systems, equipment and operating software, program management, training and technical support. Nearly a half of the contract amount was for the cost of the software for the RTGS and ACH systems.

The contract amounts of the four sample projects were captured in the worksheet that OTA used to list the projects and tally the contract amounts. OTA summed up the contract amounts and reported the sum as the obligation in its fund-use status statement to SIGIR.

To verify the accuracy of the contract amounts of the sample projects listed in the worksheet, we obtained the copies of the sample contract documents from PSD. We found that the obligations in the worksheet correctly reflected the contract amounts recorded in the contract documents. Therefore, we determined that the contract amounts were correctly captured in the fund-use status statement.

We also considered the manner in which OTA compiles the disbursement data for its reports to SIGIR and reviewed the support for the disbursement amounts for the four sample projects. We found that the disbursements of the four sample projects totaled \$12.9 million by the end of August 2005.

We found that the disbursements were made properly following the due process of certification, approval, and documentation, after confirmation of the receipt of goods and services in accordance with the agreement set forth in the contracts.

Based on our review, we concluded that the financial information that OTA reported to the SIGIR fairly presented the fund-use status of Treasury's Iraq reconstruction activities through August 31, 2005.

* * * * *

We would like to extend our appreciation to the Associate Director, Operations and his staff for the cooperation and courtesies extended to our staff during the review. If you have any questions, please contact me at (202) 927-6512 or Myung Han, Management Analyst, the major contributor to this report, at (202) 927-4878.

/s/
Donald R. Kassel
Director, Fiscal Service Audits

Our objectives were to (1) identify Treasury activities and funding involving Iraq relief and reconstruction and (2) determine the completeness and accuracy of the information that OTA provided in its reports to the SIGIR on Treasury's Iraq reconstruction activities.

We reviewed the SIGIR's initial report to Congress, dated January 30, 2005, and updated reports thereafter. We reviewed the relevant laws that appropriated funds for Treasury's Iraq reconstruction activities. We visited OTA and interviewed the Associate Director, Operations, and the Operations Manager. We also spoke with the Chief of the Internal Programs Contracts Branch of Treasury's Procurement Services Division.

We performed certain tests of the fund-use status statement that OTA provided to the SIGIR for the month of August 2005. Specifically, we reviewed the list of contracts awarded by OTA to execute Iraq reconstruction program activities, which was provided by OTA's Associate Director, Operations, and tested a sample of contractual obligations against the contract data obtained from Procurement Services Division personnel to ensure that the obligated amounts were correctly captured in the report. We also reviewed the disbursement documents provided by OTA's financial manager.

We conducted our field work from August 2005 to October 2005 in accordance with generally accepted government auditing standards.

Appendix 2
OTA IRRF Fund-Use Statement

**Iraq Relief and Reconstruction Funds
Treasury Office of Technical Assistance
Status through 08/31/2005**

	FY 2003	FY 2003	FY 2004	TOTAL
Fund Title	Iraq Relief & Reconstruction Fund	International Affairs Technical Assistance	IRRF2 PC 08000	
Fund Symbol	20-113/41096	113/41045	20-114/61096	
Amount Received	3,750,000	2,250,000	29,100,000	\$35,100,000
Obligations in FY 2003	520,001	2,250,000		\$2,770,001
Balance from previous report	0	0	7,011,411	\$7,011,411
Project	0	0	6,233,748	
Operating	0	0	777,663	
Received/Recoveries	0	0	0	
Project	0	0	0	
Operating	0	0	0	
Total Resources	0	0	7,011,411	\$7,011,411
Project	0	0	6,233,748	
Operating	0	0	777,663	
Obligations	0	0	1,308,788	\$1,308,788
Project	0	0	531,125	
Operating	0	0	777,663	
Available Balance	0	0	5,702,623	\$5,702,623
Project	0	0	5,702,623	
Operating	0	0	0	
Disbursements/Outlays(Total)	2,972,091	1,765,722	18,444,653	\$23,182,466
Project			16,602,855	
Operating			1,841,798	

Note: The total obligation through the end of 08/31/2005 can be derived by subtracting the available balance (\$5,702,623) from the total amount received (\$35,100,000). Hence, it is \$29,397,377.



DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

March 20, 2006

MEMORANDUM FOR DONALD R. KASSEL
DIRECTOR OF FISCAL SERVICE AUDITS
OFFICE OF INSPECTOR GENERAL

FROM:

Van B. Jorstad
Director
Office of Technical Assistance

A handwritten signature in black ink, appearing to read "Van B. Jorstad", written over the printed name and title.

SUBJECT:

Comments on Draft Report – Review of Treasury Activities for
Iraq Reconstruction

I concur with your description of Treasury activities and use of funds involving Iraq relief and reconstruction. I am pleased that the Office of Technical Assistance was able to help you meet your responsibilities for this audit and to note that your findings do not include any recommendations to change or correct our procedures.

Treasury Office of Technical Assistance will continue to report regularly, as required, on the status of Iraq relief and reconstructions funds and to provide copies of those reports to your office.

Department of the Treasury

Deputy Assistant Secretary for Technical Assistance
Associate Director, Operations, Office of Technical Assistance
Office of Strategic Planning and Performance Management
Office of Accounting and Internal Control

Office of Management and Budget

OIG Budget Examiner

Office of the Special Inspector General for Iraq Reconstruction