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## **Iraq: Recent Developments in Reconstruction Assistance**

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# Iraq: Recent Developments in Reconstruction Assistance

## Summary

Large-scale reconstruction assistance programs are being undertaken by the United States following the war with Iraq. To fund such programs, Congress approved on April 12, 2003, a \$2.48 billion Iraq Relief and Reconstruction Fund in the FY2003 Supplemental Appropriation. On November 6, 2003, the President signed into law P.L. 108-106, the FY2004 Emergency Supplemental Appropriation, providing \$18.4 billion for Iraq reconstruction. Contributions pledged at the October 24, 2003, Madrid donor conference by other donors amounted to roughly \$3.6 billion in grant aid and as much as \$13.3 billion in possible loans.

On June 28, 2004, the entity implementing assistance programs, the Coalition Provisional Authority (CPA), dissolved, and sovereignty was returned to Iraq. Security Council Resolution 1546 of June 8, 2004, returned control of assets held in the Development Fund for Iraq to the government of Iraq. U.S. assistance is now provided through the embassy of the United States under Ambassador John Negroponte.

Many reconstruction efforts on the ground are underway, but security concerns have slowed progress considerably. Most reconstruction funding is targeted at infrastructure projects — roads, sanitation, electric power, oil production, etc. Aid is also used to train and equip Iraqi security forces. A range of programs are in place to offer expert advice to the Iraqi government, establish business centers, rehabilitate schools and health clinics, provide school books and vaccinations, etc. However, of the \$18.4 billion appropriated by Congress in October 2003, only \$7.9 billion had been obligated and \$1.5 billion spent by mid-October 2004. Congress approved on September 29 an Administration-proposed re-allocation of \$3.5 billion in previously appropriated reconstruction funds to give greater emphasis to security, employment generation, and debt relief.

The report will be updated as events warrant. For discussion of the Iraq political situation, see CRS Report RL31339, *Iraq: U.S. Regime Change Efforts and Post-Saddam Governance*. See also CRS Report RL32229, *Iraq: Frequently Asked Questions About Contracting*.

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# Iraq: Recent Developments in Reconstruction Assistance

Large-scale reconstruction assistance programs are being undertaken by the United States in Iraq. This report describes recent developments in this assistance effort. The report will be updated as events warrant.<sup>1</sup>

## Funding for Reconstruction

Following years of authoritarian rule and economic sanctions, the United States and the international community agreed in the spring of 2003 that efforts should be made to introduce economic reform and democratic government to post-war Iraq. The best available estimates of the eventual cost of this Iraq reconstruction are provided in an October 2003 World Bank and U.N. Development Group needs assessment of 14 sectors of the Iraqi government and economy. Prepared for the benefit of the international donors conference held in Madrid on October 23-24, 2003, it established the targets by which the adequacy of available resources will be judged. The World Bank/U.N. assessments put the cost of reconstruction for the 14 sectors at \$36 billion over four years, a figure that does not include \$19.4 billion estimated by the Coalition Provisional Authority (CPA) for security, oil, and other sectors not covered by the Bank/U.N. assessments. Total World Bank/CPA projected reconstruction costs through 2007 amount to \$55 billion.<sup>2</sup>

Several potential “spigots” are available to fund Iraq reconstruction. U.S. foreign aid appropriations were provided in FY2003 and FY2004 in two emergency supplemental bills specifically for Iraq. International donors have also made aid contributions. Iraqi funds, mostly derived from oil export profits, have been employed largely to cover the “normal” operating costs of the Iraqi government, but, where sufficient amounts are available, have been used to address reconstruction needs. Additionally, the reduction or rescheduling of Iraqi debt repayments makes further resources available. These sources of reconstruction funding are discussed below.

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<sup>1</sup> For detailed discussion of the Iraq political situation, see CRS Report RL31339, *Iraq: U.S. Regime Change Efforts and Post-Saddam Governance*.

<sup>2</sup> For the full text of the report online, see the World Bank website at [<http://siteresources.worldbank.org/INTIRAQ/Overview/20147568/Joint%20Needs%20Assessment.pdf>].

## Funds Committed/Pledged to Iraq Relief and Reconstruction

(\$ millions)

United States Assistance	FY2003 Apps.	FY2004 Apps.	Total
<b>Iraq Relief and Reconstruction Fund</b>	<b>2,475.0</b> (of which 2,398.0 obligated as of 6/22/04)	<b>18,439.0</b> (of which 7,694.0 obligated as of 10/12/04)	<b>20,914.0</b>
DOD - Oil Repair	802.0	—	802.0
DOD - Iraq Army	51.2	—	51.2
DOD - CERP	—	140.0	140.0
Other Agency Funds	472.9	1.9	474.8
CPA Administration	698.0	983.0	1,681.0
<b>Total U.S. Assistance</b>	<b>4,499.1</b>	<b>19,563.9</b>	<b>24,063.3</b>

<b>Iraq Resources</b> (as of 6/28/04)	
U.S. Vested Funds	1,724.0
U.S. Seized Funds	927.0
Development Fund for Iraq (DFI)	20,706.0
<b>Total Iraq Resources</b>	<b>23,357.0</b> (of which, all expended or committed)

<b>Other Donors</b> (as of 6/6/04)	
Humanitarian Funds	849.0
Reconstruction Grants & Loans Pledged at Madrid Conference	13,535.0 (of which at least 9,000.0 are loans)
<b>Total Other Donor Grants &amp; Loans</b>	<b>14,384.0</b>

**Source:** Section 2207 Reports to Congress Pursuant to P.L. 108-106, July 2, 2004 and October 2004; CPA Inspector General Report to Congress Pursuant to P.L. 108-106, July 30, 2004; Coalition Provisional Authority, Development Fund for Iraq Spreadsheet, June 26, 2004; Department of State Working Papers: Iraq Weekly Status, October 13, 2004; and CRS calculations.

### U.S. Assistance

In the FY2003 Emergency Supplemental (P.L. 108-11, H.R. 1559/H.Rept. 108-76), signed on April 16, 2003, \$2.48 billion was appropriated for a special Iraq Relief and Reconstruction Fund (IRRF) for the purpose of aid efforts in a wide range of sectors, including water and sanitation, food, electricity, education, and rule of law. The legislation gave the President control over the Fund, and amounts could be

transferred only to the Department of State, the Agency for International Development (USAID), the Department of the Treasury, the Department of Defense, and the Department of Health and Human Services, subject to the usual notification procedures.

The FY2004 Emergency Supplemental (P.L. 108-106, H.R. 3289/H.Rept. 108-337), signed on November 6, added \$18.4 billion to the IRRF and allowed funds to go directly to the CPA in addition to the above named agencies. While earlier funds had been used to support a broad range of humanitarian and reconstruction efforts, the FY2004 appropriation was largely intended to have an immediate impact on the two greatest reconstruction concerns raised since the occupation of Iraq began — security and infrastructure.

The reconstruction funds were provided entirely as grants, after the Administration threatened to veto any measure that provided aid in the form of loans. The legislation established an Inspector General office to monitor the use of funds by the CPA, and included extensive reporting requirements regarding expenditures, projects, and other sources of revenue. The bill also provided \$983 million for operating expenses of the CPA. Exceptions to the rule of full and open competition for contracts have to be justified and notified to Congress.

On September 14, 2004, the Administration asked Congress to approve a significant re-allocation of \$3.46 billion of the \$18.4 billion (see Reconstruction Priorities below). Because the desired changes were greater than the supplemental's restriction on how much a specific sector — such as security or health — could be increased (no more than 20%) or decreased (no more than 10%) from the original congressional allocation, a simple notification to the appropriations committees was insufficient. Requiring legislative action in order to accommodate the President's re-allocation plan, Congress included such authority in the FY2005 Continuing Resolution (P.L. 108-309).

Administration officials have said that there will be no new funding request for Iraq reconstruction in calendar year 2004. A supplemental request is anticipated in early 2005.

Although the IRRF accounts for most U.S. reconstruction aid to Iraq, funds have been drawn from other accounts for related purposes. Department of Defense appropriations were used to cover the FY2003 operational expenses of the CPA and have gone to pay part of the costs for repair of Iraq's oil infrastructure, for training of the Iraqi army, and towards the Commanders Emergency Response Program (CERP). In addition to drawing from the IRRF, USAID has used its own funds to pay for humanitarian programs in Iraq. The FY2005 Defense Appropriations, signed into law (P.L. 108-287, H.R. 4613) on August 5 makes available up to \$300 million in additional funding for the CERP.

## **Oil Resources and Development Fund for Iraq**

Efforts are being made to restore Iraq's oil production capacity. Oil exporting resumed in mid-June 2003, but oil production has been slowed by looting and sabotage. Until the most recent destruction of a northern pipeline on September 3,

rates of production had reached a peak of 2.67 million barrels/day, compared with a pre-war rate of 2.5 million barrels/day and with a target of 2.8-3.0 million barrels/day by end of 2004.<sup>3</sup> The Administration's re-allocation of appropriations subtracts \$450 million from the emergency supply of oil to Iraqis and adds it to efforts to improve the oil production infrastructure.

Prior to the war, the Administration had expected that Iraq's oil reserves would help it "shoulder much of the burden for [its] own reconstruction."<sup>4</sup> The May 22, 2003, U.N. Resolution 1483 which ended sanctions permitted the occupying coalition to use oil reserves for more long-term reconstruction purposes. The resolution shifted responsibility for oil profits and their disbursal from the U.N. to the United States and its allies by establishing a Development Fund for Iraq (DFI) held by the Central Bank of Iraq and into which oil profits and other Iraqi assets would be deposited. Under Security Council Resolution 1546, adopted on June 8, 2004, the transitional government of sovereign Iraq now has control over use of DFI funds.

As of June 28, total DFI deposits amounted to about \$20.7 billion in oil proceeds and other repatriated funds. In addition to the Oil for Food Program's monthly food baskets, responsibility for which was transferred to the coalition on November 22, 2003, DFI funds have been used to support a wide range of reconstruction activities, including the currency exchange program, oil and electricity infrastructure repair, and purchase of firefighting equipment. Up to the transition at the end of June, roughly \$14 billion in DFI resources had been expended and \$6.6 billion remained in the DFI, but virtually all of it was committed to supporting the 2004 Iraqi budget.<sup>5</sup>

Many questions have been raised regarding the CPA's use and monitoring of DFI funds. Security Council Resolution 1483 (May 2003) required that an international advisory board to monitor the sale and use of oil be established, but at first the CPA opposed international institution efforts to create a system of "special audits" that would allow the board to look at any issue. CPA failure to establish the board led to international criticism, and Security Council Resolution 1511 (October 2003) recommended that the board be established as a priority and that the DFI should be "used in a transparent manner."<sup>6</sup> On October 21, 2003, the CPA announced that it would allow the advisory board to go forward and the first meeting of the International Advisory and Monitoring Board (IAMB) was held on December 5. However, a delay in appointing accountants by the CPA continued to prevent work up to early February 2004. On March 24, the IAMB recommended installation

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<sup>3</sup> Department of State, Iraq Status Weekly Working Papers, October 13, 2004.

<sup>4</sup> Ari Fleisher, White House, February 18, 2003. *90 Day Update Report to Congress Pursuant to Sec. 1506 of Emergency Wartime Supplemental*, page. 4, July 14, 2003.

<sup>5</sup> CPA Inspector General Report to Congress, July 30, 2004. Some news reports suggested that \$900 million was uncommitted by the time of the transition. "U.S. Funds for Iraq Are Largely Unspent," *Washington Post*, July 4, 2004.

<sup>6</sup> Security Council Resolution 1511, October 16, 2003, paragraph 23. "Oil to Come Under Iraqi Control as U.S. Fails to Form Advisory Board," *Financial Times*, August 19, 2003. "Annan Deals a Blow to U.S. Draft Resolution," *Financial Times*, October 3, 2003.

of a metering system for oil extraction to prevent diversion, and criticized the use of non-competitive bidding for contracts funded by the DFI.<sup>7</sup> Security Council Resolution 1546 (June 2004) determined that the IAMB should continue to exist after the turn-over of sovereignty with the addition of an Iraqi government-appointed full voting member.<sup>8</sup>

The CPA established a Program Review Board in June 2003 to prioritize and recommend how DFI resources are used. Although composed of coalition, multilateral bank, and U.N. officials, the multilateral bank members had no vote and the U.N. official served only as an observer. The Program Review Board published brief minutes of its meetings, but little detailed information regarding the nearly 2,000 contracts it awarded utilizing Iraqi funds. Reportedly, U.S. contractors received as much as \$1.9 billion of DFI funds, of which Halliburton subsidiary Kellogg Brown & Root was awarded \$1.7 billion.<sup>9</sup>

In its June audit, KPMG, the accounting firm designated by the IAMB to audit the DFI, noted the CPA's inadequate accounting systems and records and lack of controls over ministry spending of DFI resources, opening the door for corruption. KPMG also pointed out the use of non-competitive bidding for some contracts funded by the DFI.<sup>10</sup> A representative on the IAMB has accused the Administration of withholding information on non-competitive contracts, and repeated requests to U.S. agencies for information on sole-sourced contracts funded by the DFI have not been answered.<sup>11</sup> The organization Christian Aid has accused the CPA of being "in flagrant breach of the U.N. resolution" giving it use of DFI funds. "Last minute" spending by the CPA of \$2.5 billion in DFI resources in the weeks prior to the turn-over of sovereignty has also drawn critical attention. Among other things, the spending has gone for equipment for security forces, vocational training, and oil and electric infrastructure, and local projects. Iraqi officials have been critical of the contrast between the slow spending of U.S. funds and the rapid drawdown of the DFI.<sup>12</sup>

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<sup>7</sup> IAMB website is at [<http://www.iamb.info/>]. IAMB, Press Release, March 24, 2004. "Monitoring Panel for Iraq Spending Yet to Start Work," *Financial Times*, February 5, 2004.

<sup>8</sup> Security Council Resolution 1546, June 8, 2004, paragraph 24.

<sup>9</sup> "\$1.9 Billion of Iraq's Money Goes to U.S. Contractors," *Washington Post*, August 4, 2004.

<sup>10</sup> KPMG Audit dated June 29, 2004 available on-line at IAMB website.

<sup>11</sup> Press Release, "Statement by the International Advisory and Monitoring Board on Iraq," September 8, 2004. "U.S. Won't Turn Over Data for Iraq Audits," *Washington Post*, July 16, 2004.

<sup>12</sup> Christian Aid, *Fuelling Suspicion: the Coalition and Iraq's Oil Billions*, June 2004. "U.S. is Quietly Spending \$2.5 Billion from Iraqi Oil Revenue to Pay for Iraqi Projects," *New York Times*, June 21, 2004. Section 2207 Report, OMB, July 2, 2004. "U.S. Funds for Iraq are Largely Unspent," *Washington Post*, July 4, 2004.



## Debts and Assets

The United States has sought to obtain support from creditors for Iraq debt relief. Debt estimates vary widely; some in the Administration have put it at as much as \$200 billion, others at \$120 billion.<sup>13</sup> The Paris Club of government creditors has estimated Iraq's debt to its members at \$41 billion, including both principal and interest. Of this amount, the United States is owed \$2.1 billion in principal alone.<sup>14</sup> Including arrears and contingent liabilities, the total Iraq debt owed the United States totals about \$4 billion. The London Club of commercial creditors, multilateral banks, and the Gulf States are owed substantial additional sums.

On December 5, 2003, President Bush appointed former Secretary of State James Baker III as his personal envoy responsible for seeking a reduction in debt owed by Iraq. In spring 2003, creditors had agreed to suspend repayment of debt until the end of 2004. But the United States has argued that any new Iraqi government should not be burdened with debts associated with the policies of its previous ruler.<sup>15</sup> Some large holders of Iraqi debt have been more inclined to reschedule debt than to forgive it. Prior to the October donor conference, both Germany and Russia indicated they wished to have their debts repaid. Following a meeting with Baker on December 16, the leaders of Germany and France announced their support for debt reduction (more recently, French President Chirac indicated that a 50% reduction was his limit). Italy and Britain have also expressed support. Russia has indicated its willingness to participate in debt relief talks, but wants the status of its companies pre-war contracts with Iraq to be considered. Japan announced that it would be willing to forgive the majority of its roughly \$7 billion debt, if other Paris Club countries do the same. Secretary Baker met with Arab country leaders in the Gulf states on January 19-22, 2004, on the debt issue, obtaining from them pledges to reduce Iraqi debt.<sup>16</sup>

Iraqi sovereignty is expected to facilitate the resolution of outstanding debt. A sovereign government can negotiate with creditors. On September 22, 2004, Iraq cleared its overdue financial obligations to the IMF and within one week, gained access to \$436 million in IMF Emergency Post Conflict Assistance. This could make it easier for Iraq to reach agreement with private and government creditors. As part of the Administration's re-allocation proposal, Congress approved in P.L. 108-309 \$360 million to cover the costs of cancelling the roughly \$4 billion Iraqi debt obligation owed the United States.

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<sup>13</sup> Paul Bremer, Testimony, House Foreign Operations Subcommittee, September 24, 2003. "G8 Tensions Underlie Iraq Debt Reduction," *Financial Times*, June 9, 2004.

<sup>14</sup> "Stand-off Ended Over Relief of Iraqi Debt," *Financial Times*, December 17, 2003.

<sup>15</sup> "G-7 Agrees that Iraq Needs Help with Debt," *Washington Post*, April 13, 2003. "Restructuring, not Forgiveness," *Financial Times*, April 15, 2003.

<sup>16</sup> "Chirac Avoids Criticizing U.S. on Iraq," *New York Times*, August 28, 2004. "Japan Says it Will Forgive Most of Debt Owed by Iraq," *New York Times*, December 30, 2003. "4 Arab Nations Agree to Reduce Debt Owed by Iraq," *New York Times*, January 22, 2004. "Russia Agrees to Discuss Debt Relief for Iraq," *New York Times*, December 19, 2003.

On March 20, 2003, President Bush issued an executive order confiscating non-diplomatic Iraqi assets held in the United States. Of the total assets seized, an estimated \$1.74 billion worth were available for reconstruction purposes. Another \$926 million in assets located by the United States in Iraq were also used for these purposes. In addition, foreign governments were reported to hold an estimated \$3.7 billion in seized or frozen assets, of which \$847 million has been deposited in the DFI.<sup>17</sup> Security Council Resolution 1511 urges member states to deposit seized assets in the DFI immediately.

## Other Donors

Since March 2003, U.N. appeals for postwar humanitarian relief to Iraq have been met with \$849 million in donations from non-U.S. donors.<sup>18</sup> The Madrid donor conference, held on October 23-24, produced roughly \$3.6 billion in pledges of grant reconstruction aid from other donors, including \$1.4 billion by Japan, \$452 million (in new funds) by the United Kingdom, \$220 million by Spain, \$236 million by the European Union (EU), \$200 million by South Korea, and \$236 million by Italy. In some cases, announced amounts include funds previously contributed. Additionally, between \$9.6 and \$13.3 billion in loans were offered, including \$3.5 billion by Japan, between \$3.0 and \$5.0 billion by the World Bank, between \$2.6 and \$4.3 billion by the IMF, and \$500 million by Saudi Arabia.<sup>19</sup> Of the roughly \$13 billion (low-end figure) pledged, \$1.2 billion had been disbursed through June 2004.<sup>20</sup>

During much of the occupation, donors had been reluctant to contribute to reconstruction because they had no say in where the funds are to be allocated.<sup>21</sup> To deal with this concern, a multi-donor trust fund, the International Reconstruction Fund Facility for Iraq (IRFFI), was established on December 11. It would encourage contributions by keeping them outside the control of the United States, but would support needs identified in the World Bank needs assessment. The Facility has two windows, one run by the Bank (the World Bank Iraq Trust Fund) and one by the United Nations (UNDG Iraq Trust Fund). As of May 25, donors had committed about \$1 billion of already pledged assistance to the Facility, \$849 million of which was already deposited. To date, the World Bank Fund has financed textbooks, school

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<sup>17</sup> CPA Inspector General Report to Congress, July 30, 2004.

<sup>18</sup> As of April 5, 2004. Includes appeal and outside-appeal aid from all donor countries, except United States. U.N. Office for the Coordination of Humanitarian Affairs. *Total Humanitarian Assistance for Iraq Crisis 2003*. April 5, 2004, [<http://www.reliefweb.int/w/rwb.nsf>].

<sup>19</sup> See conference website at [[http://www.comisionadoiraq.org/donors/index\\_ing.htm](http://www.comisionadoiraq.org/donors/index_ing.htm)]. "Iraq Pledges Roll In," BBC News, October 24, 2003.

<sup>20</sup> CPA Inspector General Report to Congress, July 30, 2004, page 68.

<sup>21</sup> "U.S. Seeks Help With Iraq Costs, But Donors Want a Larger Say," *New York Times*, July 14, 2003. "Bush's Plea for Iraq Aid Falls on Deaf Ears," *Financial Times*, September 25, 2003.

rehabilitation, and water and sanitation infrastructure, and has provided hundreds of Iraqi civil servants with management training.<sup>22</sup>

## **U.S. Aid Policy Structure on Iraq**

On June 28, 2004, the Coalition Provisional Authority (CPA), the agency established to temporarily rule Iraq and implement assistance programs, was dissolved as Iraq regained its sovereignty. The United States will continue to provide an assistance program and, to the extent possible, policy guidance to the Iraqi government through its U.S. embassy under Ambassador John Negroponte. The embassy is expected to employ about 1,000 U.S. and 700 Iraqi staff. A temporary Iraq Reconstruction Management Office (IRMO) has been created within the U.S. embassy to supplant CPA assistance efforts. It is being headed by Ambassador William B. Taylor, Jr., the former Coordinator of U.S. Assistance to Afghanistan and, before that, Europe and Eurasia. The CPA's Program Management Office (PMO), although changing its name to the Project and Contracting Office (PCO), continues to be responsible for program management and contracts and remains within the Department of Defense, but will report to the Department of State as well as to the Department of the Army. It is now headed by Charles Hess, the former PCO deputy.<sup>23</sup>

Immediate overall responsibility for management of U.S. military activity in Iraq belongs to General George Casey, Jr.. As commander of the multinational forces in Iraq, Casey is responsible for establishing a new relationship between coalition forces and the new Iraqi government and providing training and support to Iraqi security forces. He also serves as principal military adviser to the U.S. Ambassador.

With the dissolution of the CPA which was under the Secretary of Defense, the Secretary of State assumes responsibility for assistance. Within the State Department, Robin Raphel is the coordinator for Iraq reconstruction.

Under the FY2004 Emergency Supplemental legislation, the post of CPA Inspector General, currently occupied by Stuart Bowen, Jr., continues for six months after dissolution. The CPA-IG office has about 104 employees examining a range of issues, including the extent and use of competition in contracting; efficient and effective contract management practices; and the impact of security costs on the reconstruction program. The CPA IG issued his first report to Congress on March 30, 2004.<sup>24</sup> The State Department reportedly wanted to make the CPA Inspector General part of its existing IG office in the Department. H.R. 4818, the FY2005 foreign aid bill (sec. 573) approved by the House, would absorb it into the

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<sup>22</sup> CPA Inspector General Report to Congress, Appendix H, July 30, 2004.

<sup>23</sup> The PCO and IRMO were established by a National Security Presidential Directive of May 11, 2004. PCO website at [[http://www.rebuilding-iraq.net/portal/page?\\_pageid=35,62867&\\_dad=portal&\\_schema=PORTAL](http://www.rebuilding-iraq.net/portal/page?_pageid=35,62867&_dad=portal&_schema=PORTAL)] .

<sup>24</sup> See [<http://www.cpa-ig.org/>] for a copy and for subsequent reports. CPA Inspector General Report to Congress, July 30, 2004.

Department as a separate office.<sup>25</sup> Meanwhile, the enacted DOD Authorization for FY2005 (Sec. 1059B of H.R. 4200) extends the CPA-IG beyond its late-December 2004 expiration by re-designating the office as the Special Inspector General for Iraq Reconstruction and granting operational authority until 10 months after 80% of the reconstruction funds have been obligated.

## Security Concerns

The successful conduct of much reconstruction work is contingent on an environment of order and stability. More than a year since Operation Iraqi Freedom was launched, violence persists against both U.S. forces and Iraqis in the transition government. Among the effects of the continued instability has been an increase in reconstruction costs. For example, the value of proposed U.S. contracts in the oil sector was doubled in late October 2003 to accommodate the anticipated rise in costs, partly due to sabotage. A telephone exchange in Baghdad, repaired for \$50 million, was bombed in March 2004. Major pipelines were sabotaged in June, shutting down oil exports. In the past year, power was cut to more than 100 electrical lines, and nearly 1,200 electrical towers have been felled. Ensuring security for project personnel has reportedly accounted for as much as 10-25% to the cost of reconstruction activities, draining funds from the purposes for which they were intended.<sup>26</sup>

The instability has delayed implementation of reconstruction projects. Fearing for their safety, many aid implementors have been withdrawn from the country. U.N. and bilateral aid donors have been reluctant to initiate projects of their own; many, including the U.N., are running programs from Jordan or Kuwait utilizing Iraqi personnel to the extent possible. World Bank loans are unlikely to be made until its staff can safely visit project sites.<sup>27</sup>

The quality of aid has likely been negatively affected as implementors cannot meet with local people and design and monitor projects as they would in other countries. The pool of foreign expertise available to advise the government and NGOs is restricted to those few willing to endure the country's hardships. In a broader sense, prolonged insecurity has undermined the trust of the Iraqi people in

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<sup>25</sup> "State Department Wants to Absorb Watchdog," *Washington Post*, June 18, 2004.

<sup>26</sup> CPA Inspector General, Report to Congress, March 30, 2004. "Security Companies: Shadow Soldiers in Iraq," *New York Times*, April 19, 2004. "Two Pipeline Blasts Halt Oil Exports at Top Iraq Port," *New York Times*, June 16, 2004. "Violence in Iraq Curbs Work of 2 Big Contractors," *New York Times*, April 22, 2004. "Saboteur Attacks Iraqi Phone Center," *Washington Post*, March 4, 2004. "In Iraq, Contractors' Security Costs Rise," *Washington Post*, February 18, 2004. "Sabotage Cuts Power to More Than 100 Electrical Lines," *New York Times*, June 11, 2004.

<sup>27</sup> CPA Inspector General Report to Congress, July 30, 2004, p. 69. "Security Conditions Continue to Hamper U.N. in Iraq," *Washington File*, August 11, 2004. "Charities Get Ready to Leave," *London Times*, September 9, 2004.

U.S. leadership to bring about a democratic and economic transformation in Iraq, opening the door to further political discontent and opposition.<sup>28</sup>

Throughout the year, as security concerns continued to dominate the attention of policymakers, efforts have been made to encourage other countries to provide peacekeeping forces. However, participation of other countries has been hindered by previous opposition to the war and other factors. In the wake of recent violence and hostage-taking, the Philippines, Honduras, and others withdrew their forces. President Bush's request that NATO provide forces was rejected at the G-8 summit in June, but NATO has agreed to help train Iraqi troops.<sup>29</sup>

The number of U.S. troops is currently estimated at roughly 140,000; earlier plans to draw down to 110,000 by late spring were cancelled.<sup>30</sup> Deputy Defense Secretary Wolfowitz recently testified that U.S. troops could be stationed in Iraq for years.<sup>31</sup> There are also about 24,000 troops from 31 other nations. In addition, there are an estimated 22,000 private security contract workers in Iraq, many guarding U.S. civilian reconstruction personnel.

Since October, the United States has accelerated efforts to use Iraqis for security purposes. According to the State Department, in mid-September there were about 85,000 conventional Iraqi police, compared with the 37,000 reported in September 2003. Only 41% of the police force had received any form of coalition-sponsored training. In addition, there were 41,461 Iraqi National Guard (formerly Civil Defense Corps) personnel patrolling with coalition forces, 74,000 Facilities Protection Service guards protecting buildings and civilian personnel, and 16,798 customs/border police. A 12,699-member Iraqi army conventional force, less than half of whom have completed training, is expected to increase to 27,000 over time.<sup>32</sup>

During the past year, efforts to increase security forces were troubled by a spate of resignations in the army attributed to low pay; salaries have since been raised. Reports of poorly trained and equipped security forces, dismissals of police for criminal behavior, bribe taking by border police, and thousands of no-shows by Facilities Protection Service personnel also threatened U.S. plans to increase security using Iraqi personnel. During the April confrontation in Fallujah, as many as 20 to 25% of the security forces quit, changed sides, or did not perform duties.<sup>33</sup> A dispute

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<sup>28</sup> "As Violence Deepens, So Does Pessimism," *Washington Post*, May 18, 2004. "Fueling Anger in Iraq," *Washington Post*, December 9, 2003.

<sup>29</sup> "Powell Urges U.S. Allies to Stay Steadfast in Iraq," *Washington Post*, July 28, 2004. "Leaders Dispute NATO Role in Iraq," *Washington Post*, June 10, 2004. "NATO Ready to Help Train Iraqi Forces," *New York Times*, July 31, 2004.

<sup>30</sup> *Iraq Index*, Brookings Institution, [<http://www.brookings.edu/iraqindex>], August 11, 2004. "Under Fire, Security Firms Form an Alliance," *Washington Post*, April 8, 2004.

<sup>31</sup> "Wolfowitz Says Iraq Stay Could Last Years," *Washington Post*, June 23, 2004.

<sup>32</sup> Department of State, Working Papers: Iraq Weekly Status, September 15, 2004.

<sup>33</sup> "Iraqi Security Has Come Far, With Far to Go," *Washington Post*, August 1, 2004. "Wanted: Police Academy ASAP," *Washington Post*, May 16, 2004. "Iraqi Battalion (continued...)"

— now resolved — over a contract to equip Iraqi forces led to a lengthy delay in provision of radios, body armor, and vehicles. It has been reported that in some cases, U.S. commanders drew on their discretionary funds to meet these needs, thereby limiting availability of funds for community goodwill purposes.<sup>34</sup> Statistics show that as of July 13, most security forces had substantially less than the number of weapons, vehicles, communications equipment, and body armor required, but equipment is now reportedly arriving “in large quantities.”<sup>35</sup> Major General David H. Petraeus was sent to Iraq in mid-April to oversee the organization and training of all Iraqi security forces.<sup>36</sup>

More than half of the Administration’s September 2004 re-allocation of supplemental appropriations resulting from a recent U.S. embassy review of priorities and needs would go toward greater spending on security. Among other items, the total increase of \$1.8 billion over the previously allocated level of \$3.2 billion for security will be used to train and equip 45,000 new police, 16,000 new border enforcement personnel, and 20 additional Iraqi National Guard battalions.

## The Role of the United Nations

In what has been perceived by analysts as an about-face in policy, the Bush Administration began in early January to press the U.N. to return to Iraq and play an active role in the political transition. Although France, Germany, and Russia, among others, had long been urging the United Nations to assume a more active role in Iraq, especially in assisting the political transition, U.N. Secretary General Kofi Annan had been unwilling, since the dual bomb attacks in August and September, to approve a renewed U.N. presence. Annan had said that the U.N. would not return unless security was assured, its role was well-defined, and that the role was commensurate with the risks involved.<sup>37</sup> On January 27, he approved a “technical” mission, headed by U.N. Iraq envoy Lakhdar Brahimi to evaluate the political situation in the country. After repeated visits, Brahimi proposed a plan to appoint a transition government which was accepted by the United States and the Governing Council.<sup>38</sup>

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<sup>33</sup> (...continued)

Refuses to ‘Fight Iraqis’,” *Washington Post*, April 11, 2004. “Iraqi Police Suspected in Slaying of Americans,” *Washington Post*, March 13, 2004. “Recruits Abandon Iraqi Army,” *Washington Post*, December 13, 2003.

<sup>34</sup> “Delivery Delays Hurt U.S. Effort to Equip Iraqis,” *New York Times*, March 22, 2004.

<sup>35</sup> Department of Defense, Working Papers: Iraq Update, July 13, 2004, pages 24-25. Department of State, Working Papers: Iraq Weekly Status, August 18, 2004, p. 21.

<sup>36</sup> “Biggest Task for U.S. General is Training Iraqis to Fight Iraqis,” *New York Times*, June 27, 2004. “U.S. Needs More Time to Train and Equip Iraqis,” *New York Times*, May 24, 2004.

<sup>37</sup> “Wary Annan Set to Discuss a Possible U.N. Role in Iraq,” *Washington Post*, January 19, 2004.

<sup>38</sup> “Envoy Urges U.N.-Chosen Iraqi Government,” *Washington Post*, April 15, 2004.  
(continued...)

At the same time that envoy Brahimi was negotiating the transition to sovereignty, a U.N. team headed by Carina Perelli has worked on assisting the Iraqi Electoral Commission with the implementation of elections for a 275-member National Assembly by January 31, 2005. Some analysts have criticized the form of elections chosen by Ms. Perelli — party slates instead of single-member constituencies.<sup>39</sup> The U.N. continues to work on preparations for those elections, including the national conference held on August 13-18, but security concerns could impede progress. Currently, most U.N. work is being conducted from outside Iraq, with about 600 Iraqi employees implementing activities.

The appointment on July 12 of Ashraf Jehangir Qazi as the new U.N. Special Representative to Iraq suggests a growing U.N. presence and activity in Iraq itself. On August 12, the U.N. Security Council approved Resolution 1557 extending the U.N. Mission for Iraq (UNAMI) for another year, but Secretary Annan cautioned that continuing violence will prevent it from undertaking a wide-ranging assistance program. Mr. Qazi has recently indicated that security was the “key operating principle.”<sup>40</sup> U.S. policy is to encourage U.N. involvement, and the United States supports and is currently discussing with U.N. members establishing a 4,000 to 5,000 member force to protect U.N. workers.<sup>41</sup>

On June 8, 2004, Security Council Resolution 1546 was approved. In addition to endorsing the occupation’s end, Iraqi sovereignty, and the timetable leading to democratic government, it affirms a leading U.N. role in assisting Iraq toward representative government. It affirms the “importance of international assistance in reconstruction,” and calls on all nations and international financial institutions to assist Iraq. It hands control of the DFI to the transition government, recognizes the role of the multinational force in building Iraqi security forces, recognizes the Iraqi government as the primary coordinator of international assistance, and welcomes international contributions of aid to rebuild Iraq’s administrative capacity and develop the Iraqi economy. It temporarily continues the role of the IAMB in monitoring and auditing use of the DFI and repeats calls from an earlier resolution that nations should transfer frozen Iraqi assets to the DFI. The Resolution welcomes efforts to reduce Iraqi debt.<sup>42</sup>

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<sup>38</sup> (...continued)

“Administration Split Over Role of U.N.,” *Washington Post*, February 18, 2004. “Annan Sets Conditions for Sending U.N. Team to Iraq,” *Washington Post*, January 22, 2004. “U.N. to Send Expert Team to Help in Iraq, Annan Says,” *New York Times*, January 28, 2004.

<sup>39</sup> “The Wrong Elections for Iraq,” *Washington Post*, June 19, 2004.

<sup>40</sup> “‘Vicious Cycle of Violence’ Undermining U.N. Efforts to Rebuild Iraq,” *UN News Service*, September 14, 2004.

<sup>41</sup> U.N. Security Council Votes to Extend Mandate in Iraq,” *Washington Post*, August 13, 2004. “Security Fears are Slowing U.N. Return to Baghdad,” *New York Times*, August 6, 2004.

<sup>42</sup> U.N. Security Council Resolution 1546, June 8, 2004.

## U.S. Reconstruction Assistance

Among the key policy objectives laid out by the Bush Administration in conjunction with the war in Iraq was the economic and political reconstruction of the country. Discussion and debate within the United States government and abroad have been ongoing regarding the strategy to reach these ends utilizing reconstruction aid funds and the effectiveness of aid implementation.

With the dissolution of the CPA, U.S. influence in post-occupation Iraq will no longer be based on dictate, but on persuasion by Ambassador Negroponte with leverage provided by the security support of the U.S. military and billions of dollars in reconstruction aid. U.S. efforts to “remake” Iraq have been facilitated in part by the presence of U.S. advisers attached to each of the Iraqi ministries to provide technical expertise. With ministries now sovereign, U.S. advisers, in the words of one Iraqi government official, have become “consultants.” Reportedly, about 150 Americans remain attached to Iraqi ministries.<sup>43</sup>

### Reconstruction Priorities

Reconstruction priorities have changed over time. The CPA’s reconstruction priorities were reflected in the FY2004 supplemental appropriation approved by Congress in October 2003. By the time of the transition, about 23% of total funds were targeted on improving the security capabilities of the Iraqi government, including training and equipment for police, army, customs, and fire personnel. About 71% of funds were aimed at improvements in infrastructure — including electricity, oil production, water and sewerage, transportation, and telecommunications — in order to stabilize the country by creating jobs and stimulating the economy. Technical assistance and small-scale grants in such areas as democratization, civil society, microenterprise, education, economic policy, and health account for the remainder of the appropriated FY2004 funds (about 5%).

The November 2003 agreement to accelerate the hand-over of sovereignty to Iraqis led the Administration to revise plans in January 2004 for the use of appropriations. With the exception of the oil sector where emergency supply efforts were cut by nearly \$200 million, the broad categories of assistance were largely unaffected. However, a number of funding changes were made within sectors. The most significant change was an increase in the democratization effort — from \$100 million to \$458 million — reflecting the more intensive plan to prepare Iraqis to take-over. Increases were made as well in funding for border enforcement (from \$150 to \$300 million) and the civil defense corps (from \$76 to \$200 million). In addition, roughly a third of the total appropriation — \$5.8 billion, mostly intended for electric power and water and sanitation rehabilitation — was extended out to FY2005. By April 2004, the CPA had slightly revised its allocations, including adding \$184 million for administrative expenses for operating costs of the post-June 28 U.S. Mission in Iraq (taken from the water resources sector) and estimating a more rapid

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<sup>43</sup> “Iraqis Start to Exercise Power Even Before Date for Turnover,” *New York Times*, June 13, 2004. “U.S. Has Leverage, But Wants to Show Iraqis are in Charge,” *New York Times*, June 29, 2004.



spending plan, now leaving \$4.6 billion for FY2005. The main July 2004 allocation is a restoration of some water funding, and a decision to prorate all sectors equally to derive funding to cover each agency's program implementation costs. Under this allocation, \$4.5 billion is expected to remain unobligated until FY2005.<sup>44</sup>

**Iraq Relief and Reconstruction Fund: FY2004 Supplemental**  
(in \$ millions)

Sector	P.L. 108-106	Prior Allocation	Obligations as of 10/12/04	Exp.	Re-Allocation
Security and Law Enforcement	3,243	3,235	2,235	826	5,045
Justice, Public Safety, and Democracy	1,318	1,484	908	134	1,953
Electricity	5,560	5,465	2,184	340	4,350
Oil Infrastructure	1,890	1,701	723	50	1,701
Water and Sanitation	4,332	4,246	752	24	2,311
Transport and Telecommunications	500	500	173	13	499
Roads, Bridges, and Construction	370	368	145	15	359
Health	793	786	453	4	786
Private Sector	153	183	140	47	843
Education, Refugees, Human Rights	280	259	137	28	379
Administrative Expenses	0	213	29	26	213
<b>Total</b>	<b>18,439</b>	<b>18,439</b>	<b>7,879</b>	<b>1,507</b>	<b>18,439</b>

**Source:** Section 2207 Report, October 2004. Department of State, Working Papers: Iraq Weekly Status, October 13, 2004.

The September 14, 2004 Administration proposed re-allocation of resources, approved by Congress on September 29 in P.L. 108-309, reflects a review conducted by the Iraq Reconstruction and Management Office and the U.S. Embassy country team after the State Department took charge of Iraq non-military policy on June 28. The review identified security needs, increased oil production, greater employment, and democracy as the highest priorities, while suggesting that many large-scale infrastructure projects were too slow and dependent on an improved security situation to have an immediate impact. Security — mostly training and equipping Iraqi forces — increases by \$1.8 billion. Efforts to increase oil production capacity gains \$450 million. Employment creation — a combination of USAID labor-intensive projects and increased funding for the CERP — receives an additional \$280 million.

<sup>44</sup> See Section 2207 Report, OMB, July 2, 2004 for details.

Democracy programs geared toward assisting the pending elections grow by \$180 million. General development programs — mostly conducted by USAID in the areas of economic reform, private sector development, and agriculture — increase by \$380 million. Presumably to demonstrate U.S. commitment to debt reduction prior to a Paris Club discussion of the Iraq issue, the re-allocation draws on \$360 million to subsidize U.S. forgiveness of as much as \$4 billion in bilateral Iraqi debt to the United States.

In all, these sectors gained \$3.46 billion of the \$18.44 billion FY2004 supplemental appropriation. That amount was drawn from three sectors to which the funds had originally been allocated — purchases of already refined imported oil (-\$450 million), water and sewerage (-\$1.935 billion), and electricity (-\$1.074 billion). Most of the re-allocated funds — \$2.7 billion — came out of amounts that had been set aside for obligation in FY2005. Therefore, most existing contracts are not affected by the re-allocation.

Following this re-allocation, reconstruction aid priorities in Iraq, as determined by the State Department, puts 32% of total FY2004 funds into security (versus 22% previously), 12% into democratization and traditional development (9% before), and 56% into economic infrastructure (69%).

## Reconstruction Programs

A wide range of reconstruction project work is underway, although many employing Iraqi, rather than U.S., funds. For a variety of reasons, not least of which is the poor security situation, these reconstruction efforts have produced a somewhat mixed picture. The Iraqi government appears to be a functioning concern, with ministries restocked with equipment following the massive looting that occurred after the initial invasion. Health clinics are being rehabilitated, healthcare providers trained, and children immunized. Neighborhood councils have been established in 445 locations throughout the country. Most of the 1,485 grassroots projects conducted through USAID grants (\$78 million) provided to 670 community action groups have been completed. School materials have been provided, schools inventoried, and thousands of schools renovated. A broad range of economic policy reform efforts were launched, including the introduction of a new currency. Business centers have been set up throughout the country and a micro-loan program established.<sup>45</sup>

The more positive claims made by the CPA during the past year for the success of their reconstruction programs have been countered by reports of slow and ineffective implementation. Few, if any, of the 2,300 construction projects identified by the Project and Contracting Office appear to have been completed. Objectives in critical sectors, such as oil production and electric power generation, have not been met. Electric power in early October was at 100,375 Megawatt Hours compared to 95,600 MW before the war — the goal is 120,000. Oil production reached a post-war peak in late September at 2.67 million barrels/day — 2.5 million barrels/day is

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<sup>45</sup> Department of State, Working Papers: Iraq Status, August 4, 2004. *Iraq Reconstruction and Humanitarian Relief*, Weekly Update #44, USAID, August 11, 2004.

the rate before the war — and the goal is 2.8-3.0 million by December. Most of the Iraqi police have not yet been trained.<sup>46</sup>

A particular congressional concern is the rate of implementation.<sup>47</sup> One Administration argument for the \$18.4 billion appropriated in November was the need to demonstrate progress so as to employ Iraqis and win their hearts and minds. However, as of end of March, only about \$2.2 billion of that \$18.4 billion had been obligated, let alone expended. As of October 12, \$7.9 billion had been obligated, and \$1.5 billion expended.<sup>48</sup> Among reasons for the slow progress were pressures to employ open and competitive bidding for most of the new reconstruction contracts and inter-agency disputes over control of the funds. Security concerns, exacerbated in April, have been chiefly responsible for delaying reconstruction further. In practice, this means that, assuming diminishing levels of violence, it may be early autumn before significant activity occurs on the ground as a consequence of the \$18.4 billion. To speed up the reconstruction process, in April CPA Ambassador Bremer initiated the Accelerated Iraqi Reconstruction Program (AIRP) which utilizes Iraqi DFI funds (\$300 million by July 4) to get work underway in ten cities. The AIRP effort is coordinated with the use of CERP funds (see below).<sup>49</sup> The State Department's re-allocation of reconstruction funds is, in part, reportedly intended to speed up implementation, including the expanded use of smaller projects.<sup>50</sup>

While most reconstruction activities provide needed infrastructure and services, some far-reaching economic and political policy reforms promoted by the CPA stirred controversy in Iraq, especially as they were viewed as imposed by an occupying administration. For example, in a move to establish an open and free market economy and obtain revenue to meet development needs, Ambassador

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<sup>46</sup> Department of State, Working Papers: Iraq Status, October 13, 2004. Anthony Cordesman, "Figures Indicate Challenging Transition Ahead in Iraq," Scholar Statement, June 25, 2004, and "Cleaning up the Mess," July 7, 2004, Center for Strategic and International Studies. "U.S. Handing Over An Unfulfilled Iraq," *Chicago Tribune*, June 27, 2004. "Reality Intrudes on Promises in Rebuilding of Iraq," *New York Times*, June 30, 2004. "Death Stalks an Experiment in Democracy," *Washington Post*, June 22, 2004. "An Educator Learns the Hard Way," *Washington Post*, June 21, 2004. "In Race to Give Power to Iraqis, Electricity Lags," *New York Times*, June 14, 2004. "To Many, Mission Not Accomplished," *Washington Post*, June 3, 2004.

<sup>47</sup> For example, see hearing on security assistance by House Foreign Operations Subcommittee, Committee on Appropriations, April 29, 2004 and hearing on reconstruction assistance, Senate Foreign Relations Committee, September 15, 2004. "Rebuilding Aid Unspent, Tapped to Pay Expenses," *Washington Post*, April 30, 2004.

<sup>48</sup> Department of State, Working Papers: Iraq Status, October 13, 2004. Of the original \$2.475 billion appropriated for the Iraq Relief and Reconstruction Fund in April 2003, only \$1.504 billion, or 61%, had been disbursed by end of February 2004. The same percentage had been expended (\$1.522 billion) by June 30. Nearly all had been obligated. [CPA Inspector General Report to Congress, July 30, 2004.]

<sup>49</sup> "Accelerated Iraq Reconstruction Effort Exceeds Goals and Schedules," PCO, Iraq, July 4, 2004.

<sup>50</sup> "U.S. Seeks to Provide More Jobs and Speed Rebuilding in Iraq," *New York Times*, July 27, 2004.

Bremer approved new laws in September 2003 abolishing all curbs on foreign direct investment except in natural resources. According to the *Financial Times*, the reforms were “near universally unpopular,” Iraqi businessmen and unions fearing they would be unable to compete.<sup>51</sup> Such laws and regulations could face resistance and reversal under the new sovereign government, although the interim constitution requires approval of a majority of the government’s ministers, president, and vice-presidents to overturn existing laws. According to the press, CPA Administrator Bremer issued 97 legal orders in the last two weeks of the occupation.<sup>52</sup>

On the other hand, as a result of the year-long continuing instability and the accelerated agreement to turn over sovereignty, some controversial positions which were favored by Ambassador Bremer and his staff — privatization of state-owned business, elimination of crop subsidies, and an end to the Oil for Food program’s free food baskets — were put off entirely. Iraqi government officials would, reportedly, have preferred that the CPA bear the burden of such potentially destabilizing decisions rather than leave them to a new Iraqi government.<sup>53</sup>

**Commanders Emergency Response Program (CERP).** Drawn from DFI Iraqi seized assets and oil profits and Department of Defense operational funds rather than reconstruction appropriations, the CERP contributes to the reconstruction effort by providing “walking around money” for the roughly 1,600 U.S. military civil affairs officers throughout Iraq. Until the recent FY2005 DOD appropriation of up to \$300 million in additional funds for the CERP, roughly \$680 million — \$540 million from Iraqi resources — had been made available for this purpose. Provided in the form of small grants — over 27,600 such projects totaling \$364.6 million as of end of June — the CERP supports a wide variety of reconstruction activities at the village level from renovating health clinics to digging wells to painting schools. In lieu of civilian government or NGO aid personnel, who are not present in most of the country, commanders identify local needs and dispense aid with few bureaucratic encumbrances. The grants have been credited with helping the military better exercise their security missions, while at the same time meeting immediate neighborhood development needs.<sup>54</sup> In an effort to stimulate employment, the State Department re-allocation of assistance increases CERP funding by \$86 million.

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<sup>51</sup> “Free-Market Iraq? Not So Fast,” *New York Times*, January 10, 2004. “Business Deals May be Invalid, Experts Say,” *Financial Times*, October 29, 2003. “Governing Council Hits at Minister Over Business Reform,” *Financial Times*, September 25, 2003. “Iraq Offering Laws to Spur Investment From Abroad,” *New York Times*, September 21, 2003. “Economic Overhaul for Iraq,” *Washington Post*, September 22, 2003.

<sup>52</sup> “U.S. Edicts Curb Power of Iraq’s Leadership,” *Washington Post*, June 27, 2004.

<sup>53</sup> “Attacks Force Retreat From Wide-Ranging Plans for Iraq,” *Washington Post*, December 28, 2003. “Iraqis Face Tough Transition to Market-Based Agriculture,” *Washington Post*, January 22, 2004. “Iraq Privatization Postponed for Now,” *Dow Jones Newswires*, October 27, 2003.

<sup>54</sup> OMB, Section 2207 Report, July 2, 2004. “Soldiering On to Rebuild Iraq,” *Washington Post*, February 21, 2004. “The GI’s Weapon of Choice in Iraq: Dollars,” *Christian Science Monitor*, January 29, 2004. “\$126 Million Spent So Far by U.S. Military on Iraq Reconstruction,” Department of Defense Transcript, CPA Briefing, January 14, 2004. “A Different Street Fight in Iraq,” *Washington Post*, May 27, 2004.

**Reconstruction Contract Issues.**<sup>55</sup> Dozens of U.S. and international companies and NGOs are participating in the reconstruction of Iraq.<sup>56</sup> (Many contractors are also participating in military support operations — these are not discussed in this report). In connection with implementation of the FY2004 Supplemental, the CPA set up an Iraq Program Management Office (PMO). In post-occupation Iraq, it is now called the Project and Contracting Office (PCO). The PCO coordinates infrastructure construction and monitors contracting and expenditures in six sectors — transport and communications; electricity; buildings/health; security/justice; public works/water resources; and oil. It more generally manages and oversees use of the non-construction funds as well. At present, contracts potentially worth about \$8.5 billion of the \$12.6 billion in FY2004 supplemental funding set aside for infrastructure have been awarded. Roughly \$5.8 billion in non-construction projects is expected to be conducted with FY2004 funds.

The PCO has largely supplanted government agencies traditionally responsible for reconstruction program contracting as it implements the bulk of the FY2004-funded programs. The main contracting agencies implementing FY2003 programs are the Army Corps of Engineers, responsible for oil well repair and maintenance; the Department of State, handling police training; and the Agency for International Development (USAID), managing the widest range of economic, social, and political development programs. Using FY2003 funds, USAID has awarded \$1.8 billion in contracts and grants in seaport and airport administration, capital construction, theater logistical support, public health, primary and secondary education, personnel support, local governance, agricultural development, and higher education. Utilizing FY2004 funding, it is responsible for \$2.3 billion to date, including a \$1.8 billion construction project contracted to Bechtel. USAID will continue to be responsible for most activities related to social services, civil society, and policy reform.

Continuing security concerns in the unpredictable Iraqi environment pose problems for firms interested in reconstruction work. A firm's security plans are a factor in awarding contracts. As noted earlier, a substantial proportion of contract costs are being diverted to providing security to employees. One recent concern of contractors has been the legal status of workers in the post-occupation period, especially with regard to efforts to protect themselves from attack. Prior to the turn-over of sovereignty, CPA Administrator Bremer signed an order providing legal

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<sup>55</sup> For further discussion on contract issues, see CRS Report RL32229, *Iraq: Frequently Asked Questions About Contracting*.

<sup>56</sup> For information on contract awards and solicitations, and business opportunities in Iraq, see the following websites: the Iraq Project and Contracting Office [[http://www.rebuilding-iraq.net/portal/page?\\_pageid=33,30990&\\_dad=portal&\\_schema=PORTAL](http://www.rebuilding-iraq.net/portal/page?_pageid=33,30990&_dad=portal&_schema=PORTAL)]; USAID's Iraq Reconstruction effort [<http://www.usaid.gov/iraq/activities.html>]; the Department of Commerce (DOC) Iraq Reconstruction Task Force [<http://www.export.gov/iraq/>]; the U.S. Army Corps of Engineers [<http://www.hq.usace.army.mil/cepa/iraq/iraq.htm>]; and the site for recruiting of police trainers under the State Department-managed, DynCorp-implemented project [<http://www.policemission.com>]. Companies interested in sub-contracting under any projects should contact the winner of the award.

immunity to contractors while they are in the course of performing work in support of Iraq reconstruction efforts.<sup>57</sup>

Seeking to encourage economic growth and decrease unemployment, the CPA made special efforts to insure that Iraqi business had an opportunity to participate in contracts, including putting contract solicitations on its website and appointing business liaison representatives. The extent to which firms plan to utilize Iraqi services has been a factor in the awarding of new contracts. Although U.S. government requirements could be waived for Iraqi contractors, most work for Iraqi business is expected to come in the form of subcontracts. The PCO claims that over 315 Iraqi firms are currently working on U.S.-funded reconstruction projects, and that roughly 111,000 Iraqis are employed.<sup>58</sup>

An Administration decision applied to the FY2003 reconstruction contracts to waive the normal competitive bidding requirements and request bids from specific companies which were seen to have preexisting qualifications received considerable attention by the business community. U.S. officials explained that only a few select firms possessed the particular skills that would qualify them for the job specifications for Iraq reconstruction, and that time and security clearances were also critical factors. Other U.S. firms and foreign entities potentially excluded by “buy America” provisions of law, they noted, could participate as sub-contractors to the selected American firms.

Most FY2004 contracts are being competitively solicited, and the FY2004 supplemental contains a provision requiring notification and justification to Congress of any waiver of competitive rules. On December 5, 2003, Deputy Secretary of Defense Paul Wolfowitz issued a determination and findings report, essentially limiting eligibility for prime contracts using FY2004 funds to U.S. firms and those of 62 countries — including Iraq, coalition partner, and force contributing nations. His rationale for barring other countries’ firms, including Germany and France, was that it was “necessary for the protection of the essential security interests of the United States.” Countries excluded from prime contracts could still participate as sub-contractors. Administration officials have indicated that the limitation on country eligibility will be reversed in the near future. The action may be interpreted as an effort to gain greater international cooperation on Iraq as well as a mark of State Department control over Iraq policy following the June 28 transition.<sup>59</sup>

The closed bidding and lack of transparency in early contracting and later reports suggesting that U.S. and Iraqi funds are being squandered disturbed a number

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<sup>57</sup> “Immunity Provision Extended for U.S. Firms with Reconstruction Contracts,” *Washington Post*, June 29, 2004.

<sup>58</sup> PCO website and Department of State, Working Papers: Iraq Weekly Status, September 8, 2004.

<sup>59</sup> “U.S. to End Ban on War Opponents From Getting Iraq Contracts,” *Bloomberg*, September 8, 2004. “Wider Support Prompts U.S. Rethink on Contracts,” *Financial Times*, July 21, 2004. “Pentagon Bars Three Nations From Iraqi Bids,” *New York Times*, December 10, 2003. “U.S. Pressed Over Iraq Contracts Ban,” *Financial Times*, December 12, 2003. “Iraq Contracts Open to Canadians,” *Washington Post*, January 14, 2004.

of legislators.<sup>60</sup> The FY2004 supplemental established an Inspector General for the CPA, a position scheduled to expire at the end of 2004. Sec. 1059B of H.R. 4200, the Defense Authorization Act for FY2005, extends the CPA-IG by re-designating the office as the Special Inspector General for Iraq Reconstruction and granting operational authority until 10 months after 80% of the reconstruction funds have been obligated. The CPA Inspector General has issued a number of audits and launched dozens of investigations.<sup>61</sup>

In particular, it was the sole source contract for oil well repair (“Restore Iraqi Oil” — RIO project) provided to Kellogg Brown and Root (KBR), a subsidiary of Halliburton, whose former chief executive is Vice-President Cheney, that was and continues to be the focus of media attention, raising concerns of favoritism and reinforcing suspicions that the war was fought for oil. The repair work for this contract, conducted by KBR for the Army Corps of Engineers, has been valued at \$2.5 billion to March 2004.<sup>62</sup> In summer 2003, the Corps announced that remaining oil repair work would be competitively bid. However, KBR continued to carry out work orders on a non-competitive basis pending a decision, finally reached on January 16, 2004, on two new contracts collectively worth up to \$2.0 billion.<sup>63</sup> One of the new contracts — worth up to \$1.2 billion — was awarded to KBR.

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<sup>60</sup> For example, a cement plant’s renovation, estimated to cost \$15 million by U.S. engineers, was repaired by Iraqis for \$80,000. [Rep. Henry Waxman, letter to Joshua Bolten, Director of OMB, September 26, 2003.] The Governing Council questioned a decision by the CPA to spend \$1.2 billion training 35,000 police in Jordan rather than in Iraq at, in its view, “a fraction of the cost.” [“Iraqis Say U.S. Occupation Authority Misspends Million in its Awarding of Contracts,” *New York Times*, October 4, 2003.] Press reports suggest that ministry equipment is sold on the streets and reconstruction subcontracts are delivered for bribes. [“Spoils of War,” National Public Radio, April 21-23, 2004.] The Department of Defense Inspector General found numerous “irregularities” in contracting procedures followed by DOD acquisition support for the CPA and its predecessor through August 2003. Department of Defense Inspector General — Audit, Contracts Awarded for the Coalition Provisional Authority by the Defense Contracting Command, Report No. D-2004-057, March 18, 2004.

<sup>61</sup> CPA Inspector General Report to Congress, July 30, 2004. See CPA-IG website [<http://www.cpa-ig.org/>] for audit reports to date.

<sup>62</sup> \$815 million of this sum is Iraqi resources; \$1.7 billion is from U.S. appropriations. The figure does not include its profit margin of between 2% and 7%. U.S. Army Corps of Engineers, March 2003 Contract Obligation Status, [<http://www.hq.usace.army.mil/cepa/iraq/oilfires.htm>].

<sup>63</sup> Jane Mayer, “Contract Sport,” *The New Yorker*, February 16, 2004. “Iraq Contract Award Delayed Again,” *Houston Chronicle*, December 2, 2003. “U.S. Delays Awarding 2 Iraq Repair Contracts,” *Washington Post*, October 30, 2003. “Bush Seeks \$2.1 Billion More for Iraqi Oil Industry,” *New York Times*, September 13, 2003. “Halliburton’s Deals Greater Than Thought,” *Washington Post*, August 28, 2003. “Halliburton’s Iraq Role is Expanded to Oil Products Distribution,” *Financial Times*, May 8, 2003, “Halliburton Contracts Total \$50 million,” *Financial Times*, April 12, 2003, “U.S. to Request Bids for Work on Oil Fields,” *Washington Post*, April 15, 2003. “Halliburton’s Links Sharpen Bids Dispute,” *Financial Times*, March 27, 2003

KBR has also been the focus of two DOD audits — one related to its work providing logistics support to the U.S. military under its competitively-bid LOGCAP contract and the other for the importation of fuel for use by Iraqis under the RIO project. In the latter case, KBR is suspected of overcharging by \$61 million.<sup>64</sup> Recently, former KBR staff have come forward with accusations of wasteful spending.<sup>65</sup>

**Recent Assessments of Reconstruction.** There have been dozens of reports and articles during the past year that have sought to analyze, criticize, and recommend action regarding the progress of reconstruction aid. Two of the most recent ones are indicative of the others. *Reconstructing Iraq*, a September 2004 report from the International Crisis Group, examines the gamut of mistakes that many agree were made prior to and during the occupation. These include the lack of a reconstruction plan; the failure to adequately fund reconstruction early on; unrealistic application of U.S. views to Iraqi conditions by, for example, emphasizing privatization policy; the organizational incompetence of the CPA; shifting deadlines, such as the November decision to end the occupation seven months later; and the inadequate utilization of Iraqis both in making policy and in implementing reconstruction projects. The report draws on these failures to inform its recommendations for the future. Recommendations for the U.S. government include the suggestion that staff with expertise in post-conflict situations be utilized and encouraged to serve in Iraq longer than six months; that Iraqis representing a range of views participate in design and implementation of U.S. reconstruction projects; that development of the Iraqi private sector be emphasized through greater use of Iraqis as subcontractors; and that prime contractors be required to employ Iraqis as much as possible.<sup>66</sup>

*Progress or Peril? Measuring Iraq's Reconstruction* from the Center for Strategic and International Studies uses polling to attempt to measure the status of reconstruction from the Iraqi point of view. It finds that security is the predominant issue in Iraqi minds, and that governance is a largely negative picture. It suggests that U.S. efforts are too focused on national level politics and that efforts to support local political bodies are not backed by sufficient funding. A lack of economic opportunity fuels anger and security problems, and the level of social services is also undermining public confidence. An improvement in social well-being — health and education — may be the only bright spot that the report highlights. Recommendations include accelerating training of security forces, increasing more direct assistance to Iraqis, giving priority to Iraq's employment crisis, supporting the return of the U.N. to provide election assistance, giving precedence to aid for Iraq's judicial sector, supporting the development of more responsive Kurdish regional

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<sup>64</sup> In the former case, Halliburton is repaying the government \$27.4 million in overcharges. "Halliburton Will Repay U.S. Excess Charges for Troops' Meals," *New York Times*, February 3, 2004. "Pentagon Asks for Probe of KBR Oil Deal," *Washington Post*, January 16, 2004.

<sup>65</sup> "Halliburton Staff Called to Testify on Wasteful Spending," *Financial Times*, June 16, 2004.

<sup>66</sup> International Crisis Group, *Reconstructing Iraq*, September 2, 2004.



governments, mobilizing the Iraqi silent majority to counter the insurgents, and giving Iraqis a stake in the country's oil wealth.<sup>67</sup>

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<sup>67</sup> Center for Strategic and International Studies, Post-Conflict Reconstruction Project, Frederick Barton and Bathsheba Crocker, Co-Directors, *Progress or Peril? Measuring Iraq's Reconstruction*, September 2004.