

The seal of the Office of the Special Inspector General for Iraq Reconstruction is a large, circular emblem in the background. It features a central eagle with wings spread, holding an olive branch and arrows. Above the eagle is a shield with vertical stripes and a central star. The eagle is surrounded by a wreath. The outer ring of the seal contains the text "OFFICE OF THE SPECIAL INSPECTOR GENERAL FOR IRAQ RECONSTRUCTION" in English and Arabic. The Arabic text at the top reads "المفتش العام" and at the bottom "مجمع إعادة إعمار العراق".

**LESSONS LEARNED FROM U.S.
AGENCIES' MANAGEMENT OF IRAQI
FUNDS FOR RELIEF AND
RECONSTRUCTION**

**SIGIR 13-004
JANUARY 22, 2013**



SPECIAL INSPECTOR GENERAL FOR IRAQ RECONSTRUCTION

January 22, 2013

MEMORANDUM FOR U.S. SECRETARY OF DEFENSE
U.S. SECRETARY OF STATE

SUBJECT: Lessons Learned from U.S. Agencies' Management of Iraqi Funds for Relief and Reconstruction (SIGIR 13-004)

We are providing this audit report for your information and use. The report summarizes key lessons learned based on reports the Special Inspector General for Iraq Reconstruction (SIGIR) issued which addressed the U.S. government's management and oversight of Iraqi funds for relief and reconstruction activities. We performed this review in accordance with our statutory responsibilities contained in Public Law 108-106, as amended, which also incorporates the duties and responsibilities of inspectors general under the Inspector General Act of 1978. This law provides for independent and objective audits of programs and operations funded with amounts appropriated or otherwise made available for the reconstruction of Iraq, and for recommendations on related policies designed to promote economy, efficiency, and effectiveness and to prevent and detect fraud, waste, and abuse.

We received technical comments from the Office of the Under Secretary of Defense (Comptroller), which we incorporated as appropriate. The Office of the Under Secretary of Defense (Comptroller) also noted that it agreed with the opportunities highlighted within the four broad lessons learned areas presented in the report. The Office further stated that the information provided in our reports and the corrective actions taken on the Development Fund for Iraq, affirm what can be accomplished through a collaborative effort between agency management and the audit community. We addressed this last comment in our concluding observations. The Office's statements are presented in their entirety in Appendix E.



SPECIAL INSPECTOR GENERAL FOR IRAQ RECONSTRUCTION

We appreciate the courtesies extended to the SIGIR staff. For additional information on the report, please contact F. James Shafer, Assistant Inspector General for Audits (Washington D.C.) (703) 604-0894/ fred.j.shafer.civ@mail.mil, or Tinh Nguyen, Principal Deputy Assistant Inspector General for Audits (Washington, D.C.), (703) 604-0545/ tinh.t.nguyen4.civ@mail.mil.

A handwritten signature in black ink, appearing to read "Stuart W. Bowen, Jr." followed by a period.

Stuart W. Bowen, Jr.
Inspector General

cc: Commander, U.S. Central Command
Office of the Secretary of Defense (Comptroller)
Commanding General, U.S. Army Corps of Engineers
Director, Defense Contract Audit Agency
U.S. Ambassador to Iraq

Table of Contents

Background	1
The Coalition Provisional Authority’s Oversight of Iraqi Funds	2
The U.S. Department of Defense’s Oversight of Iraqi Funds	3
Objective	4
Lessons Learned from Auditing U.S. Agencies’ Management of Iraqi Funds for Relief and Reconstruction	5
Sound Program Management That Provides Effective Guidance, Direction, and Oversight Is Critical for Consistency and Success	5
Strong Internal Controls Are Essential to Deter Fraud, Waste, and Abuse	8
Good Records Management Is Important to Facilitate Audits and Investigations	11
Close Working Relationships between Involved Parties Is Needed to Help Ensure Success of Relief and Reconstruction Programs	12
SIGIR Observations	14
Appendix A—Scope and Methodology	16
Appendix B—SIGIR Audit Reports Involving Iraqi Funds	17
Appendix C—Acronyms	19
Appendix D—Audit Team Members	20
Appendix E—Office of the Under Secretary of Defense (Comptroller) Comments	21
Appendix F—SIGIR Mission and Contact Information	22



Lessons Learned from U.S. Agencies' Management of Iraqi Funds for Relief and Reconstruction

SIGIR 13-004

January 22, 2013

Background

U.S. reconstruction assistance to Iraq began in May 2003, after the end of U.S. combat operations. Early that month, the Coalition Provisional Authority (CPA) was created to plan and initiate reconstruction activities in Iraq. For about 14 months thereafter, the CPA acted as the managing body for the governance and reconstruction of Iraq.

Following the CPA's dissolution on June 28, 2004, the Interim Iraqi Government granted the U.S. Department of Defense (DoD) limited authority for administering contracts previously awarded by the CPA.

Together, the CPA and DoD had access to about \$26.7 billion in Iraqi funds for relief and reconstruction activities.¹ The two sources for these Iraqi funds were the Development Fund for Iraq (DFI) (\$24 billion) and vested and seized assets (\$2.7 billion).²

United Nations Security Council Resolution 1483 created the DFI in May 2003 and assigned the CPA the responsibility for its management. The DFI account at the Federal Reserve Bank of New York contained revenues from sales of Iraqi oil and gas, certain remaining deposits from the Oil for Food program, and repatriated national assets. Resolution 1483 specified that these funds be used for the benefit of the Iraqi people, including financing reconstruction, civil-administration programs, and humanitarian initiatives.

During the CPA's tenure, its Administrator intermittently directed bulk shipments of the DFI, in the form of U.S. currency, be flown to Baghdad (or ordered electronic fund transfer payments executed) to reimburse vendors for reconstruction projects and for other purposes benefitting the Iraqi people. The CPA established guidance for shipping DFI funds from the Federal Reserve to Baghdad and their deposit into the Central Bank of Iraq. Some DFI funds were also held in the Republican Palace vault in Baghdad.³

In separate decisions made between March 20, 2003 and April 30, 2003, pursuant to Executive Order 13290: "Confiscating and Vesting Certain Iraqi Property," DoD was assigned responsibility for planning and accounting for the use of vested and seized Iraqi funds.

¹ In addition, DoD had access to billions of dollars of U.S. appropriated funds for reconstruction.

² In response to a draft of this report, DoD noted that it did not have direct access to any of the Iraqi bank accounts including the DFI accounts. However, SIGIR notes that the funds used to make payments for relief and reconstruction activities, with proper Iraqi authorization, came out of these accounts.

³ Saddam Hussein's Republican Palace in Baghdad became the CPA's headquarters and was used to store cash needed by the CPA.

According to presidential direction, these funds were to be used to assist the Iraqi people and to support the reconstruction of Iraq.

Vested assets entailed Iraqi funds that had been frozen in U.S. bank accounts since the first Gulf War. Seized assets entailed Iraqi assets obtained from non-U.S. banks and from certain Iraqi state or regime-owned property confiscated by Coalition forces and transferred to U.S. government accounts.

The Coalition Provisional Authority’s Oversight of Iraqi Funds

During its roughly 14-month tenure, the CPA had access to about \$23.4 billion in Iraqi funds: \$20.7 billion of which were in DFI funds and another \$2.7 billion in Iraqi vested and seized asset funds. It directed expenditures of \$14.1 billion in DFI funds, mostly to Iraqi ministries for salaries, pensions, and operating costs.

The CPA had \$6.6 billion in DFI funds remaining when its mission ended on June 28, 2004. We previously reported that the CPA Administrator transferred full and legal control over almost all of the \$6.6 billion to the Central Bank of Iraq.⁴ SIGIR also reported that DoD assumed control of the \$217.7 million in cash that remained in the Republican Palace vault. Table 1 provides a matrix showing DFI revenues and expenditures during the CPA’s existence.

Table 1—DFI Revenues and Expenditures during the CPA’s Existence

Revenues	Oil for Food	\$8,100,000,000
	Proceeds from Oil Exports	\$11,362,662,000
	Repatriated Funds	\$1,039,805,000
	Interest from U.S. Treasury Bills	\$33,495,000
	Other ¹	\$170,433,000
	Total	\$20,706,395,000
Expenditures	Disbursements for Ministries	\$10,430,426,000
	Project Disbursements	\$3,628,232,000
	Total	\$14,058,658,000
Remaining Fund Balance		\$6,647,737,000

Source: SIGIR’s analysis of CPA financial matrix, as of June 28, 2004.

Note:

¹ Interest income from overnight deposits, sale of smuggler boats, donations, United Nations World Food Program, and vested assets.

In May 2003, the Deputy Secretary of Defense delegated the authorities that DoD had been granted for administering and accounting for \$2.7 billion in vested and seized assets to the CPA

⁴ *Development Fund for Iraq: The Coalition Provisional Authority Transferred Control over Most of the Remaining DFI Funds to the Central Bank of Iraq*, SIGIR 12-001, 10/26/2011.

Administrator for a one-year period. In May 2004, DoD resumed its responsibilities for administering these funds. About \$2.4 billion, or 89%, of the vested and seized asset funds had been spent by the time the CPA's mission ended on June 28, 2004.

In October 2010, SIGIR reported that at least \$47.4 million in vested and seized asset funds remained in U.S. government accounts and that DoD needed to develop a policy on the disposition of those funds.⁵ DoD is currently using some of the funds to pay DFI invoices that contractors submitted to the Government of Iraq (GOI) for which they never received payment. In April 2010, SIGIR reported that about \$32.2 million in invoices remained unpaid, including \$24.4 million owed to 11 U.S. contractors, more than two years after they had been submitted to the GOI.⁶ DoD is reviewing each invoice and determining whether all required supporting documentation exists before making a final decision on whether to pay it. In response to a draft of this report, the Office of the Under Secretary of Defense (Comptroller) noted that final decisions have been made for all but \$2 million of the unpaid invoices.

The U.S. Department of Defense's Oversight of Iraqi Funds

After the CPA dissolved, the Iraqi Minister of Finance granted DoD limited authority to use DFI funds to pay invoices on contracts that the CPA awarded prior to its dissolution. Within DoD, the Joint Area Support Group–Central was responsible for accounting for DFI funds. This organization's first Comptroller, who held the position from mid-July through mid-November 2004, established internal processes and controls to account for DFI payments and report them to the Iraqi Minister of Finance.

From July through December 2004, the Minister of Finance transferred a total of \$2.8 billion in DFI funds from the main account into a newly established DFI sub-account at the Federal Reserve Bank of New York to which DoD had access for invoice payment. DoD also had access to the \$217.7 million in cash remaining in the Republican Palace vault.

DoD used these funds to make payments on contracts the CPA awarded prior to its dissolution. The Minister directed DoD to submit monthly reports, as well as a final report, documenting all expenditures of DFI funds made from the DFI sub-account. The Minister withdrew DoD's authority to administer DFI funds on December 31, 2007.⁷

In April 2008, four months after DoD's management of Iraqi funds ended, the GOI transferred \$270 million from the DFI main account to support the Iraq Commander's Emergency Response Program (I-CERP). The GOI directed that DoD use these funds for urgent reconstruction projects to aid citizens in the 15 Iraqi provinces not under the Kurdish Regional Government. The agreement with the GOI stated that I-CERP funds were to be managed and accounted for under the same process already in place for the Commander's Emergency Response Program, a similar program funded mostly by U.S.-appropriated funds.

⁵ *Guidance Needed for Use of Residual Iraqi Vested and Seized Asset Funds*, SIGIR 11-002, 10/15/2010.

⁶ *Process for Continuing Invoice Payment for the Development Fund for Iraq Needs Attention*, SIGIR 10-014, 4/27/2010.

⁷ The Minister of Finance extended the date twice for closing out DFI-funded work and returning any unused DFI funds. The initial date for these actions was December 31, 2005, and the final date was December 31, 2007.

Objective

This report summarizes lessons learned from our previous work on U.S. use of the DFI and other Iraqi funds that could improve management and oversight of other countries' funds, should the United States be granted authority for managing such in the future.

Lessons Learned from Auditing U.S. Agencies' Management of Iraqi Funds for Relief and Reconstruction

In an April 2012 meeting, the Prime Minister of Iraq told the Inspector General that adequate oversight of Iraqi funds had been weak, particularly in the early years of the reconstruction effort. Our work on the DFI bears out his conclusion.

From July 2004 through October 2012, SIGIR issued 30 audit reports focusing on various aspects of the CPA's and DoD's accounting for and use of Iraqi funds. Our earlier reports focused on controls over cash and the CPA's administration and management of specific contracts and grants, while the later ones examined DoD's accounting for and use of Iraqi funds and the availability of documentation supporting payments made using those funds.

SIGIR's lessons learned from its body of work on U.S. agencies' management of the DFI and other Iraqi funds fall into four broad areas—the need for:

- 1) sound program management,
- 2) strong internal controls,
- 3) good records management, and
- 4) a close working relationship with the host government.

Sound Program Management That Provides Effective Guidance, Direction, and Oversight Is Critical for Consistency and Success

DoD did not establish a central organization to manage and oversee the DFI which led to fragmented management among the nine Defense organizations involved in DFI-funded reconstruction activities. To illustrate, DoD never provided participating Defense organizations necessary policies, guidance, and oversight to ensure program uniformity and effectiveness, and to minimize the potential for fraud, waste, and abuse.

Defense organizations were mostly left to their own discretion to determine how best to manage and oversee DFI funds and, although intentions were good, there was little uniformity among them or even within the same organization. Sound program management and uniform guidance are needed to ensure consistency and success, especially when multiple entities are involved in reconstruction activities, as was the case with the DFI. The lack of these best practices caused unnecessary waste, the consequences of which are still being dealt with today. This waste could have been avoided had there been a central authority managing the DFI.

Good Program Management and Oversight Are Necessary When Multiple Agencies Are Involved

Our prior audits found numerous situations where the lack of centralized management and oversight led to inconsistencies in the way Defense agencies managed, controlled, and reported on DFI funds. Inadequate oversight resulted in the expenditure of U.S. appropriated funds when, by regulation, Iraqi funds should have been used.

The absence of a centralized management office limited DoD's ability to provide assurances to the GOI that the funds it provided for relief and reconstruction activities were effectively used in accordance with its expectations. SIGIR reports bear this out:

- In October 2012, SIGIR reported that, five years after the GOI directed DoD to close out DFI contracts and return unused funds, some contracts remained open. As a result, it was unknown whether there were still funds that should be returned to the GOI.⁸ Due to the absence of central management, the GOI's close-out directive was not disseminated to all DoD organizations involved with the DFI. SIGIR found inconsistencies with how units within the same DoD organization implemented the close-out process. For instance, one unit negotiated contract closeouts immediately, while another unit within the same organization did not take similar action and its contracts still remain open.
- In July 2010, SIGIR reported that the lack of a centralized management organization resulted in inconsistent contracting practices.⁹ Most notably, some Defense organizations contracted on behalf of the GOI, others on behalf of the U.S. government. Contracting on behalf of the GOI was preferred, but it was never communicated to all participating Defense organizations. As a result, organizations that contracted on behalf of the U.S. government were not in a position to terminate those contracts and return unused DFI funds when the GOI directed them to do so. SIGIR reported that, due to a lack of communication, DoD organizations continued to issue new contracts and to spend DFI funds after the GOI directed that neither of these actions should take place.
- In October 2009, SIGIR reported that, due to insufficient program oversight as well as unclear and incomplete guidance on document requirements, I-CERP project files lacked critical internal control documentation.¹⁰ In July 2011, SIGIR reported continuing problems with I-CERP project documentation, but, more significantly, reported on U.S.-funded Commander's Emergency Response Program projects that, based on regulations, should have been funded with Iraqi funds. In response, DoD conducted a review and identified 267 Commander's Emergency Response Program projects for 2011, totaling \$2.1 million, which should have been funded with Iraqi versus U.S. appropriated funds.

⁸ *Development Fund for Iraq: U.S. Army Corps of Engineers Has Missing Receiving Reports and Open Task Orders*, SIGIR 13-003, 10/26/2012.

⁹ *Development Fund for Iraq: Department of Defense Needs to Improve Financial and Management Controls*, SIGIR 10-020, 7/27/2010.

¹⁰ *Iraq Commander's Emergency Response Program Generally Managed Well, but Project Documentation and Oversight Can Be Improved*, SIGIR 10-003, 10/27/2009.

Better oversight of the two programs would have allowed U.S. funds to be put to better use.¹¹

We believe that the lack of a centralized organization within DoD to oversee the use of and accounting for DFI funds caused many deficiencies. In response to a July 2010 SIGIR report on this matter, the Office of the Under Secretary of Defense (Comptroller) concurred, stating that it would collaborate with other Defense organizations to update the *DoD Financial Management Regulation* to include requiring the designation of an executive agent for establishing and overseeing policy on the use of non-U.S. government funds in future contingencies. The estimated date for completion was November 2010, but SIGIR has learned that DoD is still reviewing how best to implement the requirement.

Transparency Is Important to Good Stewardship

Transparency involves the full and accurate disclosure of information, which can help prevent fraud, waste, and abuse of funds. United Nations Security Council Resolution 1483 specified that DFI funds were to be used in a transparent manner, and Iraqi officials often reiterated the need for transparency.

Iraqi officials stated that decisions on the purpose, use, and reporting of the DFI should be made in an open forum which would provide them with good visibility over the funds. While the CPA publicized decisions outlining the purpose of individual DFI project funding, SIGIR found that it generally did not report on how the funds were distributed and used, and, therefore, did not meet the transparency requirement.

The CPA supported many reconstruction projects, as well as government operations, with Iraqi funds. Instead of using a transaction-based accounting system to record payment activity, the CPA created a very basic Excel-based spreadsheet approach, similar to a single-entry checkbook style register, to monitor and account for DFI funds.

DoD continued this approach after the CPA dissolved, which created difficulties when the Interim Iraqi Government asked it to provide an aggregate value of all DFI-funded contracts. Two years after the request, DoD still could not identify the value of the obligations, payments, and unpaid obligations for each of the contracts which raised questions about transparency and accountability.

- In October 2009, SIGIR reported that DoD should improve the thoroughness of quarterly reporting for I-CERP projects valued at \$50,000 or more.¹² SIGIR found that, for 141 of 347 projects or 40.6%, either the reports were not sent or, if sent, were missing critical information. The GOI needed these reports to validate project location and completion, and to ensure that the funds were spent to benefit the Iraqi people. In July 2011, SIGIR found that the problems with missing or incomplete reports continued.

¹¹ *Management of the Iraq Commander's Emergency Response Program Needs To Be Improved*, SIGIR 11-021, 7/29/2011.

¹² *Iraq Commander's Emergency Response Program Generally Managed Well, but Project Documentation and Oversight Can Be Improved*, SIGIR 10-003, 10/27/2009.

- In October 2009, SIGIR reported that, after some delay, one DoD organization provided a listing of DFI-funded contracts totaling \$2.4 billion, a substantial increase from its initial tally showing \$127.8 million in contracts.¹³ We found that this organization and one of its contractors were holding unused DFI funds in suspense accounts; however, the amounts were not readily transparent. Officials attributed these situations to the lack of a transaction based accounting system for their reconstruction activities and the absence of a single accounting code to clearly segment DFI from other funding sources.
- In January 2005, SIGIR reported that the CPA established a process whereby Iraqi ministry budgets were prepared in a transparent manner.¹⁴ However, the CPA did not implement sufficient financial controls over the \$8.8 billion in DFI funds provided to the ministries and, as a result, there were no assurances that the funds were used for their intended purpose. We also reported on a U.S. government agency's review of one Iraqi ministry which concluded that internal controls over its \$435 million budget were weak or non-existent, which could lead to fraud, kickbacks, and misappropriation of funds.

Strong Internal Controls Are Essential to Deter Fraud, Waste, and Abuse

Management is responsible for developing and maintaining effective internal controls that serve as the first line of defense in safeguarding assets and preventing and detecting fraud, waste, and abuse. But it should not only ensure that internal controls are a top priority; it should also evaluate their effectiveness on an on-going basis.

Iraq's environment of corruption, combined with huge shipments of cash from the DFI, and the purchase of high-risk commodities such as fuel and vehicles, required the most stringent controls possible to minimize the potential for fraud and theft. SIGIR audits repeatedly identified weak controls over the expenditure of DFI funds for reconstruction activities.

In our earlier audits, we found insufficient numbers of and inadequately trained oversight staff, poor inventory controls, high staff turnover, poor recordkeeping, and weak oversight of cash disbursements. In our later audits, we found key financial supporting documentation missing for DFI payments.

SIGIR also found that separate deposit fund accounts and related accounting codes were not always established for Iraqi funds to oversee and report on the status of these monies. Our audits showed that stronger internal controls could have provided better stewardship of Iraqi funds.

Strong Internal Controls Are Essential to Demonstrating Good Stewardship

Maintaining strong internal controls over another country's money is not only a prerequisite for financial accountability, but it also relieves the host government of concerns that its funds could be misused. These controls must include maintaining adequate financial supporting documentation—public vouchers, material inspection and receiving reports, and vendor

¹³ *Development Fund for Iraq: Policy Guidance Needed to Enhance Accountability of USACE-Managed Funds*, SIGIR 10-006, 10/29/2009.

¹⁴ *Oversight of Funds Provided to Iraqi Ministries through the National Budget Process*, SIGIR 05-004, 1/30/2005.

invoices—to show how the funds were used and that the products or services paid for were received.

The receiving report, which verifies the government’s inspection and receipt of a product or service, is key. Without it, there is no way to match product delivery with the vendor invoice, prior to making the payment. On multiple occasions, we highlighted that, due to the absence of supporting documentation, we could not conclude that the products and services paid for with DFI funds were actually received.

SIGIR audits revealed that, in too many cases, the CPA and DoD failed to maintain adequate supporting documentation for products or services, including products highly vulnerable to fraud and theft, such as fuel and vehicles, paid for with Iraqi funds. The absence of such documentation raised concerns within the GOI that the U.S. government was not a good steward of its money and that funds provided for reconstruction efforts may have been lost or stolen.

More than 20 SIGIR reports identified internal control weaknesses in the CPA’s and DoD’s management and control of Iraqi funds:

- In October 2012, we reported that one DoD organization did not establish effective internal controls to document the receipt of \$1.3 billion in fuel deliveries.¹⁵ We found that the responsible organization did not use material inspection and receiving reports, but instead, according to agency officials, recorded fuel deliveries in a logbook which DoD could not locate. We did not conclude that fraud or theft occurred, but the absence of both receiving reports and the logbook raised serious accountability questions.
- In April 2012, we reported on \$5.9 billion in electronic fund transfer payments the CPA made with DFI funds.¹⁶ We found the accounting records for 2003 were good, but the records for 2004 were often missing key financial documentation. For instance, there was almost a complete absence of records relating to \$44 million in electronic fund transfer payments that allegedly financed some Iraqi Haj pilgrimages.¹⁷ As a result, we could not determine what, if any, services were received for those expenditures.
- In October 2005, we reported that CPA personnel in the South-Central Region distributed about \$23 million in DFI cash, but project files only contained documentation supporting the receipt of \$300,000 by grantees.¹⁸ Similarly, in January 2006, SIGIR reported that South-Central Region personnel spent \$3.3 million for vehicles, but project files did not contain evidence that the vehicles had been received. We considered these shortcomings as “material management control weaknesses” and, due to possible fraud, transferred information to our Investigations Directorate for further review.¹⁹

¹⁵ *Development Fund for Iraq: U.S. Army Corps of Engineers Has Missing Receiving Reports and Open Task Orders*, SIGIR 13-003, 10/26/2012.

¹⁶ *Development Fund for Iraq: The Coalition Provisional Authority’s Financial Controls for Electronic Fund Transfer Payments Diminished Over Time*, SIGIR 12-013, 4/30/2012.

¹⁷ Haj is a pilgrimage to Mecca in Saudi Arabia. One of a Muslim’s duties is to go on a Haj, if in good health and with the means to do so, at least once during his or her lifetime.

¹⁸ *Management of Rapid Regional Response Program Grants in South-Central Iraq*, SIGIR 05-015, 10/25/2005.

¹⁹ *Management of Rapid Regional Response Program Contracts in South-Central Iraq*, SIGIR 05-023, 1/23/2006.

- In July 2004, we reported that the CPA created policies that, although well-intended, did not establish effective funds control and accountability over \$600 million in DFI cash being held for disbursement—\$200 million by the Comptroller and \$400 million by pay agents.²⁰ We found: (1) proper cash accountability was not maintained, (2) physical security was inadequate, (3) pay agent records were incomplete, and (4) fund managers' responsibilities were not properly assigned. Although no loss of cash was identified, SIGIR concluded that the funds were susceptible to fraud and theft.

Our reports noted that improvements could be made in overall control and accountability for contracts, grants, and cash transactions using the DFI, and SIGIR made recommendations for improvements. For instance, in 2005, we recommended that DoD develop standard procedures, controls, and organizational functions needed to maintain DFI records, paying close attention to the controls needed to effectively monitor DFI funded contracts. In most cases, DoD concurred and, if it had not begun making improvements during the audits, generally did so following them.

More recent SIGIR reports determined that DoD often did not have financial documentation to support receipt of goods and services the DFI paid for between 2003 and 2005. We concluded the absence of these documents raised serious accountability questions. We generally did not make recommendations to address the problems because these were old cases, but DoD attempted to find supporting documentation through file searches and by contacting former CPA and DoD officials involved with DFI activities.

Establishing a Separate Deposit Fund Account Is Not only Required but Critical in Ensuring Money Is Effectively Managed

U.S. government agencies are required to establish separate deposit fund accounts to hold non-U.S. government funds when they are acting as a fiscal agent for those funds. SIGIR found that DoD established these accounts for vested and seized assets as well as for DFI funds received for the I-CERP, but did not do so for other DFI funds. The absence of deposit fund accounts contributed to the CPA's and DoD's inability to readily determine the amount of DFI funds received, obligated, expended, and remaining.

Our audit reports revealed an inconsistent approach to establishing accounts for the various categories of Iraqi funds:

- In January 2012, we reported that DoD did not establish the required deposit fund account for \$217.7 million in cash that remained in the Republican Palace vault when the CPA dissolved.²¹ Although DoD established its own internal processes to account for the funds, it could only provide supporting documentation for \$73.9 million of the \$193.3 million spent. Similarly, in October 2012, SIGIR reported that DoD did not establish

²⁰ *Coalition Provisional Authority Comptroller Cash Management Controls Over the Development Fund for Iraq*, SIGIR 04-009, 7/28/2004.

²¹ *Development Fund for Iraq: Department of Defense Cannot Fully Account for the Funds it Used after the Coalition Provisional Authority Dissolved*, SIGIR 12-008, 1/27/2012.

deposit fund accounts for 13 advance DFI payments it received, with a combined value of \$233.2 million, from May 2004 through April 2005.²²

- In October 2010, we reported that as a result of establishing deposit fund accounts in 2003, DoD generally maintained an accurate accounting for vested and seized asset funds in terms of receipt, obligation, expenditure, and amount of remaining funds.²³
- In July 2010, we reported that the responsible DoD organization established a deposit fund account in 2004, when it received DFI funds for the Commander's Emergency Response Program. Then, in 2008, when the GOI provided \$270 million in DFI funds for the I-CERP, this DoD organization managed the funds as a separate budget line in the original deposit fund account. As a result, it was readily able to provide SIGIR with a full accounting of the I-CERP obligations, expenditures, and remaining balances.²⁴

Good Records Management Is Important to Facilitate Audits and Investigations

SIGIR audits found that DoD had policies and procedures for maintaining Iraq reconstruction records, but they were not fully implemented. Records management can be divided into two parts: (1) maintaining required contractual and financial documents in individual contract files, and (2) cataloging and permanently storing those records. Maintaining good program and financial records is important to facilitate audits and investigations of potential fraud and theft, as well as for preservation for the historical record.

We found DFI financial records to be incomplete and not always managed to ensure their availability. In some cases, we questioned whether certain documents ever existed, and in other cases where there were indications the documents existed, DoD could not locate them.

DoD officials stated they provided reports on DFI reconstruction activities to Iraqi officials, but did not make copies of those reports. Because records were not properly maintained or available, including problems retrieving records sent to storage, SIGIR could not always be assured that products or services paid for with Iraqi funds were actually provided. In a 2010 internal study, DoD identified significant problems with all phases of records management in Iraq.

SIGIR also found the following relevant to poor recordkeeping:

- In January 2012, we reported that DoD could not locate most of the monthly reports or the final report that the Iraqi Minister of Finance directed it to provide covering DFI sub-account payments.²⁵ Although we found evidence indicating the reports were sent, DoD

²² *Development Fund for Iraq: U.S. Army Corps of Engineers Has Missing Receiving Reports and Open Task Orders*, SIGIR 13-003, 10/26/2012.

²³ *Guidance Needed for Use of Residual Iraqi Vested and Seized Asset Funds*, SIGIR 11-002, 10/15/2010.

²⁴ *Development Fund for Iraq: Department of Defense Needs to Improve Financial and Management Controls*, SIGIR 10-020, 7/27/2010.

²⁵ *Development Fund for Iraq: The Department of Defense Cannot Fully Account for the Funds It Used After the Coalition Provisional Authority Dissolved*, SIGIR 12-008, 1/27/2012.

could locate only four of the 42 required monthly reports. As a result, DoD lacked comprehensive evidence to support its use of \$1.7 billion from the DFI sub-account and \$119.4 million in DFI cash from the Republican Palace vault.

- In July 2005, we reported that DoD could not locate 21 of 69 contract data files, or 30.4%, that we selected for review during the audit.²⁶ As a result, SIGIR could not fully address the audit's objective, which was to determine whether DFI funds were inappropriately used to award new contracts after the CPA dissolved.

Close Working Relationships between Involved Parties Is Needed to Help Ensure Success of Relief and Reconstruction Programs

The CPA's governance of Iraq, as well as DoD's administration of the DFI at the Interim Iraqi Government's request, required close coordination and good working relationships with Iraqi officials. The CPA had advisors in the Iraqi ministries and DoD worked closely with the Interim Iraqi Government and, when formed, the permanent GOI. U.S. and Iraqi officials also worked together on the review board responsible for approving and establishing dollar limits for DFI-funded projects, and in authorizing DFI payments.²⁷

While the mechanisms used to accomplish close working relationships developed over time, breakdowns occurred that left DFI funds vulnerable to fraud, waste, and abuse. Our audits also showed that Iraqi directives were not always communicated to participating DoD organizations which, at times, strained relationships:

- In July 2010, we reported that the GOI had terminated the U.S. government's authority to administer and spend DFI funds effective December 31, 2007.²⁸ It directed that all active DFI contracts should be closed, no new contracts awarded, and remaining DFI funds returned to them. However, DoD failed to disseminate this information to all participating Defense organizations and new contracting and spending continued after the designated date. DFI contracts remain open today and it is unknown whether there are still funds that need to be returned to the GOI.
- In April 2010, we reported that \$32.3 million worth of unpaid invoices for work completed in 2004 and 2005 using DFI funds were still outstanding.²⁹ DoD provided the required documentation to the GOI to pay the invoices, but they claimed that it was either lost or never received. DoD resubmitted the documentation on several occasions but the GOI never responded. DoD is currently reviewing all supporting documentation and has decided to pay valid claims with remaining vested and seized asset funds.

²⁶ *Reconciliation of Reporting Differences of the Source of Funds Used on Contracts After June 28, 2004*, SIGIR 05-009, 7/8/2005.

²⁷ The Program Review Board, established by the CPA Administrator, was responsible for reviewing and recommending expenditures of resources from the DFI.

²⁸ *Development Fund for Iraq: Department of Defense Needs to Improve Financial and Management Controls*, SIGIR 10-020, 7/27/2010.

²⁹ *Process for Continuing Invoice Payment for the Development Fund for Iraq Needs Attention*, SIGIR 10-014, 4/27/2010.

- In October 2009, we reported that U.S. government contracting officials were required to obtain letters signed by GOI officials agreeing to accept and maintain completed I-CERP projects.³⁰ However, it was never clearly established which GOI officials were responsible for signing the sustainment letters. SIGIR found sustainment letters that were missing signatures and, as a result, it has limited the U.S. government's ability to support the claim that the GOI agreed to accept and maintain completed I-CERP projects.

³⁰ *Iraq Commander's Emergency Response Program Generally Managed Well, but Project Documentation and Oversight Can Be Improved*, SIGIR 10-003, 10/27/2009.

SIGIR Observations

As the Iraq rebuilding experience made clear, contingency relief and reconstruction operations are inherently complicated. During contingency operations, regulations and controls that would normally be followed are sometimes pushed aside in the interest of getting things done quickly.

The CPA and DoD had adequate regulations to effectively guide their management and accounting of Iraqi funds used for reconstruction activities. Had those regulations been followed more closely, many of the deficiencies that SIGIR identified would not have occurred.

Most significantly, internal control weaknesses including, in some cases, the complete absence of supporting documentation, left no less than \$11.7 billion, or more than half of all Iraqi funds spent, vulnerable to fraud, waste, and abuse. Such a situation is not only unacceptable but it also raises questions as to whether those involved fulfilled their fiduciary responsibilities.

The United States could be called upon in a future contingency to manage another country's funds, as was the case in Iraq. Challenges exist when operating in an unstable environment such as existed in Iraq and those challenges have been well documented. Nonetheless, there are certain principles that despite the situation should not be compromised, including the need to be good stewards when spending another country's money. Transparency is paramount to achieving good stewardship, as is demonstrating efficient and effective use of funds, proper accounting for funds, and establishing mechanisms for reporting the use of funds to the host government.

SIGIR's in-depth study, entitled *Hard Lessons: The Iraq Reconstruction Experience* (February 2, 2009), laid out the challenges the United States faced during the relief and reconstruction of Iraq. The difficulties experienced with managing and overseeing the use of Iraqi funds are analogous in scope to other challenges the U.S. government faced, such as security, personnel turnover, and sustainability. The CPA and DoD acted with good intentions in overseeing Iraqi funds. Although intentions were good, execution was inadequate. Weaknesses clearly existed in the CPA's and DoD's management controls.

DoD made a genuine and concerted effort during the reconstruction process to implement SIGIR's recommendations to strengthen the mechanisms to better manage and control Iraqi funds. This effort is best revealed in the way DoD worked with SIGIR during recent DFI audits. Following a 2010 SIGIR report, DoD established an internal team to address issues about missing documentation and the accounting for Iraqi funds provided to DoD organizations for reconstruction activities. The team retrieved hundreds of boxes of data from storage, reviewed their contents, made multiple requests to defense agencies for information on DFI receipts and expenditures, and contacted former CPA and DoD personnel to document Iraqi funded activities. SIGIR auditors and DoD team members held numerous discussions and exchanged data, and DoD answered many of the questions raised in SIGIR reports. In commenting on a SIGIR draft report entitled "Development Fund for Iraq: The Coalition Provisional Authority's Financial Controls for Electronic Fund Transfer Payments Diminished Over Time" (SIGIR 12-013, 4/30/2012), the Office of the Under Secretary of Defense (Comptroller) stated:

I appreciate the collaborative effort extended by your team throughout the series of audits on the Development Fund for Iraq. Through this collaborative effort, DoD obtained CPA records from the U.S. National Archives that included information about the Haj-related payments to Iraqi officials highlighted in the draft report. The Department will continue to support SIGIR audit efforts to ensure transparency and proper accountability.

SIGIR believes this collaborative effort is also an important lesson learned. Due to the close working relationship that evolved, when deficiencies were identified the common goal became identifying what needed to be done to correct them and determining how the two organizations could work together to implement a corrective plan. The objective was to ensure that proper policies and procedures would be in place should the U.S. government be called upon in a future contingency to manage funds belonging to another country.

Appendix A—Scope and Methodology

Scope and Methodology

In September 2012, the Special Inspector General for Iraq Reconstruction (SIGIR) initiated Project 1301 to identify lessons learned based on the U.S. government’s management and oversight of Iraqi funds for relief and reconstruction. Based on our review and evaluation of 30 audit reports published from July 2004 through October 2012, we identified common themes that emerged from the U.S. government’s use of Iraqi funds for relief and reconstruction efforts. It was not SIGIR’s objective to re-audit the subject matter of the original audit reports, but rather to rely on previous audit work.

This work was performed by SIGIR under the authority of Public Law 108-106, as amended, which also incorporates the duties and responsibilities of inspectors general under the Inspector General Act of 1978. SIGIR conducted its work on this project from September through December 2012, in Arlington, Virginia.

Use of Computer-processed Data

In performing this audit, SIGIR did not rely on data from computer-based systems. Our audit focused on published SIGIR audit reports whose data originated in various DoD accounting systems. To achieve the original audit assignment’s objective, we examined and reported as appropriate on computer-processed data contained in those databases.

Internal Controls

Because we are commenting on prior audit reports, we did not independently assess or re-assess the overall systems of management controls but relied on previous assessments discussed in the original audits. Those audit reports more fully explain the significant internal controls assessed, the scope of the assessment work, and any significant deficiencies found during the reviews. Further, the issued reports identify management control weaknesses and make recommendations or highlight lessons learned that would improve the management control problems.

Appendix B—SIGIR Audit Reports Involving Iraqi Funds

From July 2004 through October 2012, the Special Inspector General for Iraq Reconstruction (SIGIR) issued 30 audit reports focusing on various aspects of the Coalition Provisional Authority's and Department of Defense's accounting for and use of Iraqi funds. Following is a listing of those reports.

Development Fund for Iraq: U.S. Army Corps of Engineers Has Missing Receiving Reports and Open Task Orders, SIGIR 13-003, 10/26/2012.

Development Fund for Iraq: The Coalition Provisional Authority's Financial Controls for Electronic Fund Transfer Payments Diminished over Time, SIGIR 12-013, 4/30/2012.

Development Funds for Iraq Returned to the Central Bank of Iraq, SIGIR 12-012, 1/13/2012.

Development Fund for Iraq: Department of Defense Cannot Fully Account for the Funds It Used after the Coalition Provisional Authority Dissolved, SIGIR 12-008, 1/27/2012.

Development Fund for Iraq: The Coalition Provisional Authority Transferred Control over Most of the Remaining DFI Funds to the Central Bank of Iraq, SIGIR 12-001, 10/26/2011.

Management of the Iraq Commander's Emergency Response Program Needs to be Improved (Interim Report), SIGIR 11-021, 7/29/2011.

Guidance Needed for Use of Residual Iraqi Vested and Seized Asset Funds, SIGIR 11-002, 10/15/2010.

Development Fund for Iraq: Department of Defense Needs to Improve Financial and Management Controls, SIGIR 10-020, 7/27/2010.

Process for Continuing Invoice Payment for the Development Fund for Iraq Needs Attention, SIGIR 10-014, 4/27/2010.

Development Fund for Iraq: Policy Guidance Needed To Enhance Accountability of USACE-Managed Funds, SIGIR 10-006, 10/29/2009.

Iraq Commander's Emergency Response Program Generally Managed Well, but Project Documentation and Oversight Can Be Improved, SIGIR 10-003, 10/27/2009.

Cost, Outcome, and Oversight of Iraq Oil Reconstruction Contract with Kellogg Brown & Root Services, Inc., SIGIR 09-008, 1/13/2009.

Attestation to Development Fund for Iraq Cash in the Possession of the Joint Area Support Group-Central, SIGIR 08-012, 4/13/2008.

Follow-up on SIGIR Recommendations Concerning the Development Fund for Iraq (DFI), SIGIR 06-036, 1/29/2007.

Iraqi Armed Forces Seized Assets Fund: Review of Contracts and Financial Documents, SIGIR 06-015, 4/28/2006.

Briefing to the International Advisory and Monitoring Board for Iraq: Management Controls Over the Development Fund for Iraq, SIGIR 06-013, 4/28/2006.

Development Fund for Iraq Cash Accountability Review: Joint Area Support Group-Central/Falluja, SIGIR 06-012, 4/28/2006.

Review of the Multi-National Security Transition Command-Iraq Reconciliation of the Iraqi Armed Forces Seized Assets Fund, SIGIR 06-010, 4/28/2006.

Development Fund for Iraq-Cash Accountability Review: Joint Area Support Group-Central, SIGIR 06-008, 4/28/2006.

Follow-up on Recommendations Made in SIGIR Audit Reports Related to Management and Control of the Development Fund for Iraq, SIGIR 06-005, 4/28/2006.

Management of Rapid Regional Response Program Contracts in South-Central Iraq, SIGIR 05-023, 1/23/2006.

Management of the Contracts, Grants, and Micro-Purchases Used to Rehabilitate the Karbala Library, SIGIR 05-020, 10/25/2005.

Management of the Contracts and Grants Used To Construct and Operate the Babylon Police Academy, SIGIR 05-016, 10/26/2005.

Management of Rapid Regional Response Program Grants in South-Central Iraq, SIGIR 05-015, 10/26/2005.

Reconciliation of Reporting Differences of the Source of Funds Used on Contracts After June 28, 2004, SIGIR 05-009, 7/8/2005.

Administration of Contracts Funded by the Development Fund for Iraq, SIGIR 05-008, 4/30/2005.

Control of Cash Provided to South-Central Iraq, SIGIR 05-006, 4/30/2005.

Oversight of Funds Provided to Iraqi Ministries through the National Budget Process, SIGIR 05-004, 1/30/2005.

Coalition Provisional Authority Comptroller Cash Management Controls Over Development Fund for Iraq, SIGIR 04-009, 7/28/2004.

Coalition Provisional Authority Control Over Seized and Vested Assets, SIGIR 04-008, 7/30/2004.

Appendix C—Acronyms

Acronym	Description
CPA	Coalition Provisional Authority
DFI	Development Fund for Iraq
DoD	Department of Defense
GOI	Government of Iraq
I-CERP	Iraq-Commander's Emergency Response Program
SIGIR	Special Inspector General for Iraq Reconstruction
USACE	U.S. Army Corps of Engineers

Appendix D—Audit Team Members

This report was prepared and the audit conducted under the direction of James Shafer, Assistant Inspector General for Audits, Office of the Special Inspector General for Iraq Reconstruction.

The staff members who conducted the audit and contributed to the report include:

Benjamin H. Comfort

M. Glenn Knoepfle

L. Michael Welsh

Appendix E—Office of the Under Secretary of Defense (Comptroller) Comments



COMPTROLLER

OFFICE OF THE UNDER SECRETARY OF DEFENSE
1 100 DEFENSE PENTAGON
WASHINGTON, DC 20301-1100

JAN 16 2013

MEMORANDUM FOR ASSISTANT INSPECTOR GENERAL FOR AUDITS, OFFICE OF
THE SPECIAL INSPECTOR GENERAL FOR IRAQ
RECONSTRUCTION

SUBJECT: Special Inspector General for Iraq Reconstruction 13-004 Draft Audit Report,
“Lessons Learned from U.S. Agencies Management of Iraqi Funds for Relief and
Reconstruction”

We received your January 3, 2013, draft report and appreciate the opportunity to offer comments. Consistent with our responses to recommendations contained in past reports on this subject, the following input is provided for your consideration to ensure an accurate and complete context for lessons learned:

- Of the reported Coalition Provisional Authority and Department of Defense (DoD) combined access to \$24 billion in Development Fund for Iraq (DFI) funds, DoD access was limited to \$217.7 million that remained in the presidential palace vault; and DoD was accountable to the Government of Iraq (GOI) for its usage. As verified by the Federal Reserve Bank, the Department did not have access to any Iraqi bank accounts including the DFI accounts.
- The reported \$32.2 million in unpaid DFI invoices is now \$2 million. As indicated in the subject report, these invoices were submitted to the GOI for payment multiple times without response. To resolve the issue, DoD conducted reviews to determine validity, paid valid invoices using Seized/Vested funds, and closed the related DFI contracts. Approximately \$2 million in unpaid DFI invoices remain under review.
- DoD conducted a data call and identified \$8.5 million in DFI funds that remained in the possession of DoD agencies. The Department provided written notification of the results to the GOI, contacted the Governor, Central Bank of Iraq, for remittance information, and returned the funds.

We also agree with the opportunities highlighted within the four broad areas presented. The DFI information revealed in your reports and the corrective actions taken, where applicable, affirm what can be accomplished through a collaborative effort between management and the audit community.

My staff point of contact is Ms. Charlotte Beacham. She can be reached at charlotte.beacham@osd.mil or 703-602-0371.

Mark E. Easton
Deputy Chief Financial Officer



Appendix F—SIGIR Mission and Contact Information

SIGIR’s Mission

Regarding the U.S. reconstruction plans, programs, and operations in Iraq, the Special Inspector General for Iraq Reconstruction provides independent and objective:

- oversight and review through comprehensive audits, inspections, and investigations
- advice and recommendations on policies to promote economy, efficiency, and effectiveness
- deterrence of malfeasance through the prevention and detection of fraud, waste, and abuse
- information and analysis to the Secretary of State, the Secretary of Defense, the Congress, and the American people through Quarterly Reports

Obtaining Copies of SIGIR Reports and Testimonies

To obtain copies of SIGIR documents at no cost, go to SIGIR’s Web site (www.sigir.mil).

To Report Fraud, Waste, and Abuse in Iraq Relief and Reconstruction Programs

Help prevent fraud, waste, and abuse by reporting suspicious or illegal activities to the SIGIR Hotline:

- Web: www.sigir.mil/submit_fraud.html
- Phone: 703-602-4063
- Toll Free: 866-301-2003

Congressional and Public Affairs

Hillel Weinberg
Assistant Inspector General for Congressional Affairs

Mail: Office of the Special Inspector General
for Iraq Reconstruction
2530 Crystal Drive
Arlington, VA 22202-3940

Phone: 703-428-1059

Email: hillel.weinberg.civ@mail.mil
