

## Executive Summary

Section 2207, as amended, of the Emergency Supplemental Appropriations Act for Defense and for the Reconstruction of Iraq and Afghanistan, 2004 (Public Law 108-106) requires the Secretary of State to submit a quarterly report to Congress outlining the current conditions for programs and initiatives supported by the specific appropriation(s) dedicated to the Iraq Relief and Reconstruction Fund (IRRF). The Office of Management and Budget (OMB) submitted the first financial report to Congress on January 5, 2004 and subsequent reports on April 5, 2004 and July 2, 2004. The Department of State submitted the October 5, 2004 report, which outlined significant changes in IRRF priorities, along with an update of ongoing IRRF programs and activities. This quarterly update for January 5, 2005, reviews progress in IRRF activities in the context of that reallocation, as well as the recent re-allocation of \$457 million in the IRRF to address near-term needs of the electricity sector and to expedite delivery of essential services to four key post-battle cities.

In addition to outlining the progress in each of the sectors funded by the IRRF, this report will describe specific challenges faced by the United States, its coalition partners, and allies in the Iraqi Interim Government (IIG) to carry out the strategic programs funded by the IRRF and its related spending plans.

As noted in last quarter's report, Iraqi President al-Yawer, Prime Minister Allawi and the IIG continue to demonstrate resolve, unity of purpose, and a clear commitment to furthering Iraq's transition to democracy. The IIG's invitation for all Iraqis to participate in the democratic political process remains open. Key members of the IIG continue to take important steps to strengthen Iraq's standing as a sovereign state, illustrated by Iraq's participation in the United Nations (UN) General Assembly and Prime Minister Allawi's historic address to a Joint Session of Congress on September 23, 2004. At Iraq's request, the Egyptian government hosted a regional conference in November 2004 that brought together Iraq's leaders, states within the region, G-8 representatives, and other international friends of Iraq. The leaders discussed security and other regional concerns, Iraq's upcoming elections, and economic issues central to the stability of the region. Iraqi officials have also made numerous trips to neighboring states for bilateral discussions.

These are challenging times for the people of Iraq and the Coalition Forces supporting them. As we have highlighted in previous quarterly reports, insurgents and infiltrators have stepped up their efforts to destabilize the government and undermine the January 30<sup>th</sup> national and governorate elections. These elections are a critical step in Iraq's transition to democracy and the efforts to support stability and security in Iraq. The Independent Electoral Commission of Iraq (IECI), with strong support from the U.S. and its coalition partners, is working closely with the UN to ensure the elections take place in a way that maximizes the participation of Iraqis from all parts of the country in the selection of a new transitional government.

The IECI has implemented a voter registration system, launched a public information campaign, and completed the formulation of election rules and procedures. Over 233 political entities and 33 coalitions registered and submitted broadly based election lists by the IECI's December 15<sup>th</sup> deadline. Given the ongoing insurgency, assuring security for the election presents the largest challenge, but the IIG and Multinational Forces-Iraq (MNF-I) are working on a security plan to create conditions that encourage the widest possible participation.

## **IRRF SPENDING PLAN REVIEW**

As reported in last quarter's submission, the Administration's strategic review of IRRF priorities was driven by the growing danger posed by the insurgency, preparations for the elections in January 2005, increasing capacity in the oil sector, and creating job opportunities for Iraqis. We reported the results of this strategic review to Congress in September 2004, and we appreciate Congressional support for the reallocation of IRRF priorities. The current report reviews progress across the board in IRRF programs, but it also highlights projects and activities undertaken as a result of the IRRF review. The report also reviews the \$457 million adjustment to IRRF spending that was made in late December to address critical near-term needs in the electricity sector and to restore essential services in the four key cities most affected by the insurgency.

## **Security and Law Enforcement Sector**

Insurgency and terrorism remain the most significant challenges to the reconstruction of Iraq. The United States Agency for International Development (USAID) and the Project and Contracting Office (PCO) report that intimidation of local workers has delayed projects, while the unsecure environment has driven away critically needed foreign technicians in the essential services sectors. As a result, security costs for private security forces protecting construction sites, workers, and convoys have increased dramatically, therefore significantly adding to reconstruction overhead costs. The success of our reconstruction efforts and the longer-term political and economic development of Iraq depend upon establishing a secure environment. The IIG, for its part, recognizes the need to devote additional Iraqi resources to the security sector, and in the Iraqi FY 2005 budget approved an increase of \$1.3 billion dollars for the Iraqi security forces. The process of improving the security will take time to complete.

Multinational Security Transition Command-Iraq (MNSTC-I) has assisted the Ministry of Interior to increase police training capacity, graduating nearly 3,000 police per month, and poised to graduate over 4,000 per month in the next 60 days. In addition, MNSTC-I is assisting in equipping and training the newly formed Police Commando Brigades (PCBs), while providing assistance to the Department of Border Enforcement (DBE) in the development of a coherent border strategy that includes the establishment of a centralized training program for qualified Iraqi personnel and the location requirements for various planned ports of entry and border forts.

Within the Ministry of Defence, all twenty-seven Regular Army and Intervention Force battalions will complete their initial training by the end of February.

In the last quarter, Iraqi Security forces (ISF) were tested in a number of ways. Police and military forces were committed to offensive counterinsurgency operations in Samarra, North Babil, Fallujah, Mosul, Baghdad and a host of other areas, often within weeks after completing initial training. At the same time, attacks against security forces have increased at all levels, with the targets ranging from ministerial directors to privates. Finally, and directly related to these attacks, anti-Iraqi forces (AIF) have increased the level of intimidation directed against ISF, making retention more difficult in some areas.

While Iraq's Security Forces have shown considerable progress during the last quarter, the overall performance of these forces has been mixed when put to test. Several conclusions from these experiences are clear. First, the overall performance and capabilities of ISF units are directly related to the strength of Iraqi leadership in the units. Second, the ability of Iraqi and Coalition forces to provide backup support when needed is of great importance. Third, the IIG intends to continue the employment of Iraq's Security Forces in offensive counterinsurgency operations. Fourth, these operational requirements, in turn, will require national, operational, and tactical level capabilities to reconstitute and regenerate forces that suffer casualties, injuries, or absentees. Fifth, these force deployments also require logistical capabilities that do not currently reside in military and police force structures. Finally, it is clear that the IIG will increasingly take the initiative in developing capabilities to combat insurgents.

### **Justice, Public Safety Infrastructure and Civil Society Sector**

The consolidated U.S. Government effort to strengthen Iraqi civil society, increase the capacity of the Iraqi justice system and improve the public safety infrastructure continued throughout the last quarter, despite difficulties presented by the insurgency. In an effort to accelerate delivery of assistance, U.S. implementing agencies have moved to contract directly with Iraqi firms for a variety of projects. Programs implemented during the 1<sup>st</sup> Quarter of FY 2005 include: (1) the creation of a witness protection program; (2) the establishment of a credible fire protection services, police training academies and associated facilities; (3) the training of an investigative staff of the Council of Judges that understands the legal aspects of evidence gathering, electronic surveillance, and human rights; (4) penal system improvements, including trained correction officers and acceptable detention centers; (5) humanitarian demining; (6) improvements to the judicial process and legal system with written code, statute and standard operating procedures; (7) the construction of new judicial facilities for the Council of Judges, Court of Cassation, and Central Criminal Court of Iraq; (8) the implementation of a financial management information system for Iraqi ministries coupled with a 2005 budget planning and reporting process; and (9) support for the election process, including technical assistance to the IECI and programs to enhance the capacity of local and provincial government.

Finally, the implementation of the Advanced First Responders Network (AFRN) will enable Iraqi police, fire, and emergency personnel to communicate effectively through

radio, secure voice, and data communications. Completion of this project is key to the establishment of an effective police force and for linking police with other security and government personnel, thereby facilitating a rapid reaction to local and regional emergencies. During this quarter, site assessments in Baghdad were completed, and construction began for a switching center, operations centers and 28 base stations.

### **Electric Sector**

The short-term foci in the electrical sector are generation capacity and necessary fuel availability. The Iraq Reconstruction Management Office (IRMO), in coordination with the Minister of Electricity, initiated a \$50 million "Rapid Recovery Program" to stabilize the generation crisis caused by insurgent activity, increasing consumer demand due to lack of tariffs, and high levels of unplanned outages at power plants. The goal is to increase generation so that Iraqis have more hours of available power prior to the January 30<sup>th</sup> elections, as compared to the average during this reporting period, when power supplies were low due to fall maintenance, and unscheduled maintenance, and fuel shortages resulting from the insurgency. Construction on generation, transmission, and distribution projects are progressing moderately across all governorates despite security problems in many locations. In response to recent insurgent attacks on electricity infrastructure, additional Electricity Security forces are being trained, and PCO has identified \$35 million to procure emergency spare parts. Due to interdictions at various pipelines, supplies of reserves are at all time lows. The Embassy, MNF-I, Iraq's Deputy Prime Minister and Minister of Electricity are working jointly to address the fuels shortage resulting from pipeline interdictions and intimidation campaigns and to ensure the necessary fuel inventories are stocked by mid-January 2005.

### **Oil Infrastructure Sector**

Iraqi oil production averaged 2.18 million barrels per day (mbpd) in the first quarter of 2005 (through December 31, 2004), with exports averaging 1.55 mbpd for the same period. While this does not mark a significant change from the previous quarter (in which production averaged 2.29 mbpd and exports averaged 1.39 mbpd), it is significant when compared to the 2.6 mpbd in production and 2.0 mpbd in exports Iraq can sustain when there are no attacks on pipelines and other oil facilities. In the first quarter of FY 2005 (through the week of December 10), Iraq lost an estimated \$887 million in export revenues due to attacks on oil infrastructure. The export and production numbers also do not reflect the apparent strategy by insurgents to disrupt fuel supplies to Baghdad, which has been evident since early November. There is a shortage of all refined petroleum products in Baghdad, causing the Ministry of Oil to divert more of its budget than normal from capital projects to the importation of refined products, repairs and the provision of additional security to repair teams, truck convoys and key infrastructure points. The Ministry has, nevertheless, moved forward on IRRF funded projects, including projects funded by the \$450 million reprogrammed in the first quarter.

Installation has begun on the Bai Hassan South Wet Crude Plant, and is scheduled for completion by end of January 2005. Seven of the ten remaining gas oil separation plants

(GOSPs) have been definitized and procurement activities continue. Additionally, a new task order for the Qarmat Ali Pressure Maintenance project has been approved using \$100 million in funding from the fuels fund transfer. The project to restore the Southern GOSPs has been definitized, and an additional GOSP restoration project can also be completed with remaining funds. The Ministry of Oil has expressed an interest in a National Energy Strategy Study, which would develop a linear programming equation to measure the effect of policy choices, and provide educational opportunities to Ministry leadership on oil strategy/policy development. The Oil Exploration Company has also used \$3.8 million to fund a database system project on geological and geophysical interpretation. In addition, as one element of a more comprehensive infrastructure security effort, \$50 million in IRRF is identified for expenditure on security and repair projects.

### **Water Resources and Sanitation Sector**

Consistent with the Administration's Strategic IRRF Review reallocation plan, the October 5<sup>th</sup> Report indicated a decrease in the allocation for potable water projects that were scheduled for later in the reconstruction process. In this quarter's report, we show an increase in funds devoted to potable water projects, reprogramming \$63 million from funds previously allocated for sewerage projects. This shift corresponds to a similar change in priorities by the Ministry of Municipalities and Public Works (MMPW).

### **Transportation and Telecommunications Sector**

New contracts were awarded in this quarter for continued airport rehabilitation in Baghdad, Basrah and Mosul, including air navigation equipment, visual aids, and Baghdad airport facilities. At Baghdad, commercial passenger charter and cargo flights have risen to an average of 1,000 per month, and Iraqi air controllers are now operating the tower. At the port of Umm Qasr, ship-loading equipment has arrived, renovation of the operations center is 75% complete, and designs for port warehouses and the Roll-on Roll-off berth were completed. Despite war wreckage and twenty years of silting, the two key ports of Umm Qasr and Khor Az Zubayr have recovered enough to permit between 30-50 vessels per month at Umm Qasr and 60 vessels per month at Khor Az Zubayr. In the railroad sector, 56 kilometers of track between Umm Qasr and Shoiba Junction were rehabilitated, spare parts were procured, and station rehabilitation has begun at 40 stations, including Baghdad. This rehabilitation continues despite the significant impact of the insurgency on the railroad sector.

In telecommunications, \$70 million was reprogrammed during the 1<sup>st</sup> quarter of FY 2005 to increase efficiencies among three separate fiber optic networks projects and combine them into a Consolidated Fiber Network (CFN). When completed, the CFN will provide a communications network that will support the electricity, railroad, and telecommunications sectors. Final design was completed for the Wireless Broadband Network that will support inter-ministry communications for the Iraqi government in Baghdad. The U.S. Government also provided equipment to improve postal operations at the Iraqi Telephone and Postal Company and to support spectrum management at the

telecommunications regulatory body, the National Communications and Media Commission (NCOM). The Embassy continues to provide technical assistance to the NCOM, which has overseen the growth of wireless services to over 1.3 million subscribers from the initial award of mobile licenses in late 2003.

### **Roads, Bridges and Construction Sector**

The prime design and build contractor for roads was demobilized in favor of direct local contracting program with Iraqi construction firms. This shift to using local contractors will decrease overall project costs, including security costs, and will make a more immediate and visible impact on local employment. \$56 million was made available to fund the Dora-Yousafiya expressway project. Depending on the Ministry of Housing and Construction's execution success with similar projects, this project may be given to the Ministry for implementation. Projects implemented by the Ministry of Housing and Construction will be appropriately monitored by PCO.

### **Health Care Sector**

This report outlines activities using the \$439 million allocated to rehabilitate maternity and children's hospitals and construct new primary healthcare centers (PHCs) throughout Iraq. Currently, there are 35 PHCs under construction and 16 hospitals under renovations. Construction began on the \$50 million National Children's Hospital in Basra on November 10<sup>th</sup>. The majority of construction and renovation projects are scheduled to be finished by November 2005.

### **Private Sector Development Sector**

Although the oil sector dominates the economy, its capital-intensive nature generates limited employment creation. To encourage economic reform, private sector development, and to create job opportunities, the Administration shifted \$380 million into this effort as part of the Strategic IRRF Review. These funds will be used to help increase employment and productivity in the private sector, which can more significantly generate employment. The implementation of business training programs in four business centers in the north has helped to spur employment and productivity, and the completion of a labor analysis survey will add knowledge on current labor market needs. The delivery of 14,000 tons of superior wheat seed increased agricultural production, and a joint venture between the Ministry of Agriculture, international firms and local companies is facilitating mechanization rehabilitation. At the same time, institutional, trade, and state owned enterprise reforms are underway that will help create conditions required for lasting employment.

In an effort to generate employment, stimulate economic growth, and provide immediate assistance to areas targeted by insurgents, the \$286 million was shifted in the October 5<sup>th</sup> Report to more labor-intensive, fast-disbursing assistance programs. USAID's Office of Transition Initiatives (OTI) and MNF-I are the implementing agencies for this funding. During this reporting period, USAID/OTI projects employed a peak of over 38,000 Iraqis

nationwide. These projects targeted the highest-risk communities – including Sadr City, Najaf, North Babil and Kirkuk – where creating short-term employment opportunities directly contributes to promoting stability.

### **Debt Relief**

The President and other G-8 leaders committed at the June 2004 Sea Island summit to provide debt reduction for Iraq in 2004 to relieve the new Iraqi government of the crushing burden of debt inherited from Saddam Hussein. With its friends and allies, the United States helped secure a deal at the Paris Club in November 2004, whereby Paris Club members agreed to forgive 80% of Iraq's debt. The IIG has taken the lead in seeking at least comparable debt reduction terms from its non-Paris Club creditors, a condition of the Paris Club agreement.

As part of the Strategic IRRF Review, \$360 million was reprogrammed to forgive 100% of Iraq's approximately \$4.1 billion debt to the United States. On December 17, in advance of the second U.S.-Iraq Joint Economic Commission meeting in Washington, Secretary Powell and Secretary Snow signed the formal agreement with the IIG to forgive Iraq's debt to the U.S.

### **Education, Refugees, Human Rights, and Governance Sector**

The Office of Foreign Disaster Assistance (OFDA) is partnering with the Ministry of Displacement and Migration (MoDM) to continue their efforts in expanding the size and scope of their primary program for Internally Displaced Persons (IDP), using the increase of \$70 million in funds noted in the October 5<sup>th</sup> Report. Emergency distributions of food and non-food items reached over 25,000 IDPs who left Fallujah in October and early November. A further distribution valued at \$1.1 million is on-going and will benefit another 190,000 persons who fled Fallujah during the weeks and days prior to the commencement of military operations. Additionally, distribution of winterization supplies is ongoing in 14 other governorates, and it is expected that these supplies will benefit over 350,000 IDPs.

### **Capacity Building**

To ensure proper operation, maintenance, and sustainability of IRRF-financed projects, PCO developed and approved a Capacity Development Plan that will:

- Develop transition/hand-over plans for projects to ensure sustainability for Iraqi operators and maintenance personnel.
- Convert PCO Logistics Infrastructure for Iraqi use as appropriate.
- Assist in establishment and enhancement of Iraqi engineering, construction, and professional organizations.
- Monitor progress of completed projects.
- Maximize transfer of program management techniques and methods.
- Promote employment opportunities for Iraqi citizens at all levels.

## **The Way Forward**

Given the continuing security constraints and the need to demonstrate visible reconstruction progress throughout Iraq, the Embassy conducted another review of IRRF funding priorities in December 2004, resulting in a recommendation to reprogram \$457 million. The Embassy has allocated \$211 million to the electricity sector for rapid-disbursing, high-visibility projects to address the near-term electric needs. The Embassy is also using \$246 million for smaller projects designed to provide immediate and visible essential services in four post battle cities—Fallujah, Samarra, Najaf and Thawra (Sadr City). The objective of this reprogramming is to gain support of the local population by complementing the efforts of the Coalition Forces and Iraqi Security Forces as they seek to stabilize the operating environment.

### **Commanders Humanitarian Relief and Reconstruction Projects (CHHRP)**

The October 5<sup>th</sup> Report allocated \$86 million for a new Commander's Humanitarian Relief and Reconstruction Projects (CHRRP), to be used on small-scale economic development projects in priority areas such as Baghdad, Samarra, Ramadi, North Babil, among other areas. \$30 million of the \$86 million has been obligated to 13 sewer and water projects. During this quarter, the IIG augmented this fund by matching the \$86 million. \$21 million of the matching funds have been obligated to fund electricity and water projects in Baghdad.

### **Commanders Emergency Response Program (CERP)**

All \$218 million of the initial CERP allocated to Iraq for FY 2005 has been made available. Of this, \$93 million is obligated to 1,121 projects (see chart below). Local commanders are planning more than 1,200 additional immediate infrastructure repair and post-combat reconstruction projects with a value estimated to be between \$450 million and \$500 million. In October 2004, the MNF-I commander requested that the IIG contribute \$218 million toward the additional projects. The IIG has provided \$50 million in response and indicates additional funds will be provided once the \$50 million is spent. These funds are in support of a concerted effort to fund 1,200 additional immediate infrastructure repair and post-combat relief and reconstruction projects for the benefit of the Iraqi people.

Status of CERP Projects Started in the 1<sup>st</sup> Quarter FY 2005:

<b>Project Type</b>	<b>Number of Projects</b>	<b>Amount Obligated</b>
Education	284	\$11.3
Electricity	43	\$1.2
Health	74	\$3.5
Private Sector Projects	225	\$23.5
Police/Security	92	\$3.5
Reconstruction	157	\$14.3
Rule of Law/Government	59	\$1.7
Transportation	28	\$2.2
Water/Sewer	159	\$31.8
<b>Total:</b>	<b>1,121</b>	<b>\$93.0</b>

(As of 20 Dec 2004)

### **The Development Fund for Iraq (DFI)**

Prior to transition, the Coalition Provincial Authority (CPA) created a sub-account (DFI) at the New York Federal Reserve Bank for the Central Bank of Iraq. This sub-account was to be used exclusively to pay outstanding, DFI-funded CPA contracts. The Iraq Ministry of Finance (MoF) has transferred funds into this sub-account on a routine basis in order to pay for outstanding liabilities.

PCO and IRMO are developing a detailed list of all outstanding contracts for the MNF-I in order to determine the remaining balance of outstanding liabilities. PCO and MNF-I personnel are assisting pertinent IIG officials on issues related to contracts designated by the IIG for modification. An overall plan is being developed to facilitate the transition of administration and payment of DFI liabilities to the Iraqis for final resolution by the IIG.

### **Accelerated Iraqi Reconstruction Program (AIRP)**

The AIRP, using DFI funds, continues to create jobs and build infrastructure that improves quality of life. The projects provide clean water, waste treatment facilities, roads, bridges, clinics, schools and infrastructure in eight key governorates. At this time, more than 360 projects valued at over \$324 million are under contract and are employing approximately 12,000 Iraqis. Of these, 172 projects valued at over \$26 million have been completed to date, with total work in place valued at over \$80 million. The majority of these projects are expected to be completed by late spring 2005, but several of the larger projects will not be completed until December 2005.

### **International Donor Assistance**

#### *International Resources for the Reconstruction of Iraq*

Over the past quarter, the United States has built on the success of the October 2003 Madrid Donors' Conference. At the Madrid Conference, donors other than the United States pledged over \$13.5 billion in assistance for the reconstruction of Iraq, including \$8

billion in assistance from foreign governments and \$5.5 billion in lending from the World Bank and International Monetary Fund. All of these funds are to be disbursed between 2004 and 2007. As of December 2004, over \$2.5 billion in non-U.S. assistance had been disbursed, either through bilateral projects or through the International Reconstruction Fund Facility for Iraq (IRFFI).

*The International Reconstruction Fund Facility for Iraq (IRFFI)*

The Madrid Conference authorized the establishment of the IRFFI, to give donors a multilateral channel for processing their assistance to Iraq over and above their own bilateral assistance activities. The IRFFI is a mechanism for the joint management of World Bank and United Nations reconstruction trust funds. In a manner similar to the bilateral assistance program, donations channeled through the IRFFI are funded out of donors' pledges at Madrid. Recent and upcoming IRFFI milestones include:

- The IRFFI Donors' Committee held its third meeting in Tokyo, Japan, on October 13-14, 2004. The Donor's Committee consists of 15 countries that have committed at least \$10 million each to the fund facility and two rotating representatives (currently Finland and Turkey) from countries that have committed less than \$10 million.
- At the Tokyo meeting, the IIG established its central role in soliciting international support for Iraqi reconstruction. It also presented its National Development Strategy. Following this successful presentation, donors reaffirmed their support for the Iraqi reconstruction effort.
- Current donor commitments to the IRFFI total about \$1.04 billion. Of this amount, \$490 million is from Japan; \$200 million from the European Commission; \$127 million from the UK; \$67 million from Canada; \$20 million from Spain; \$15 million from Australia; \$12.9 million from the Netherlands; \$12 million from Italy; \$10 million each from the United States, Belgium, India, Iran, Kuwait, Republic of Korea, Qatar, Norway, and Sweden. Finland, Greece, Iceland, Ireland, and Turkey are committing amounts less than \$10 million each.
- The next Donors' Committee meeting is tentatively scheduled for spring 2005 in Amman, Jordan

While recognizing the Iraqis are their own best advocates in seeking international assistance for reconstruction, the United States has been supporting Iraqi efforts to encourage other nations to contribute.