July 13, 2016

To: USAID – Iraq
Tarabot (USAID) Management

From: Michael Schaeffer
Miraq Aljubouri

**Re: Brief Iraq Public Financial Management (Legal) Comments**

The Public Management (PFM) Team engaged in a cursory review of current Iraqi budget and public financial management legislation (Budget Laws and CPA 95). Upon completion of this review the PFM team's observations and recommendations are provided in Tables 1 and 2 (below). PFM's general observations include the following:

**Ministry of Finance (Treasury):** The discussion of the functions of the Ministry of Finance (Treasury) should be clarified with respect to the custodianship of real and financial assets.

**Roles and Responsibilities (Accounting/Budget) Officers:** The current legislation should be revised to confer broader responsibilities to accounting officers and accounting authorities (governing bodies of government entities), including establishment and operation of basic financial management system (including internal controls). These sections should consider the following headings:

- General responsibilities of accounting officers
- Budgetary control responsibilities
- Reporting responsibilities
- Responsibilities for assets and liabilities transferred to a public entity or another level of government
- Responsibilities in relation to budget reallocation and virements
- Responsibilities in relation to revenue and debtor management.

Reporting of **Accounting/Budget Officers should include the following:** i) This must specify the timetable and financial statements that should be prepared by the Accounting Officers; ii) These financial statements should comply with IPSAS accounting standards; iii) There should be a stipulation in the financial statements produced, prepared and submitted by the accounting officers should contain/accompany an annual report of non-financial performance information; the calendar should be stipulated.

**Principles of Public Finance -** The guiding principles, as outlined under the current legislation, speak to annual budgets rather than multi-year budgets or program budgets (which are multi-year in nature). Any future revisions in the Budget Law/Public Financial Management Act should be future proofed to include multi-year budgets.

**Fiscal Responsibility Principles -** There needs to be greater clarity on the definition of subnational government revenues. Do these revenues include national transfers, development grants, equalization grants etc.

**Reallocation of Government Funds –** Any public financial management act (Budget Law) should include provisions that no transfer of funds between item control totals within a given program may be made without the approval of MoF, which may subject to certain constraints approve such transfers. There are two types of item transfers within programs which Treasury should not be authorized by the Parliament to approve. The first of these is transfers *to* personnel expenses from any other item control total. The second is transfers *away from* capital expenditure to any other item control total. The ban on transfers to personnel expenses means that each ministry must respect absolutely the upper limit imposed by the Parliament on personnel expenses in the budget estimates. The reason for this is that hiring additional staff usually creates expenditure obligations not only in the financial year when those staff are hired, but in future financial years. Maintaining control of expenditure therefore requires firm control of staffing decisions. This firm control will continue to be supported by the requirement of Public Service Commission approval of ministry staffing levels. The ban on transfers away from capital expenditure is designed to prevent ministries from inappropriately sacrificing capital expenditure, which builds assets and infrastructure for the future, in order to increase current expenditure. It may be prudent to allow for a Cabinet Secretary to authorize reallocations outside these limits in extraordinary situations.

**Contingencies Fund** Contingencies Fund should be viewed as an unassigned budget category that can be accessed under urgent and unforeseen circumstances, whereby the mechanism for releasing the contingencies fund is through budget reallocation. This should be clearly designated in any future public financial management legislation.

**Supplementary Appropriations for National Government -** The current provision allows for approval of expenditure that has not been appropriated subject to several conditions. We would recommend that this state that it is inappropriate to spend without any budget appropriations.

**National Government Reporting:** The law should: i) Make clear reference to International Public Sector Accounting Standards; ii) Specifically list responsibilities of the Inspector /Accountant General in relation to producing consolidated statements and setting standards; and, iii) Should stipulate a formal oversight report adoption by Parliament regarding annual financial statements.

**Table 1: Public Financial Management Law/Budget Law Recommendations**

| Area | | Recommendations |
|---|---|---|
| **Macro-Economic and Fiscal Policy** | **1.1** | PFM Act to contain fiscal principles including fiscal policy, fiscal objectives, targets to guide annual budget |
| | **1.2** | PFM Act to include fiscal rules limiting debt (e.g., total debt as a percentage of GDP) |
| | **1.3** | PFM Act to include debt ceiling applied to each level of government (e.g, % internally generated funds and transfers) |
| | **1.4** | PFM Act to include power to set numerical fiscal rules by regulation |
| | **1.5** | PFM Act to define minimum contents Budget Policy Statement (BPS) (Fiscal – Strategy Document) |
| | **1.6** | Subnational governments to be involved in MTBF, Annual Division and Allocation of Revenue Bill, Integrated PFM Act and regulations / instructions issued. |
| | **1.7** | PFM Act should define Parliament role development/approval of BPS |
| | **1.8** | PFM Act should establish requirements for reporting requirements (for monthly, quarterly, other reports) |
| | **1.9** | PFM Act should establish requirements for pre-election report (e.g. include macroeconomic / fiscal forecasts /as full report against BPS). |
| | **1.10** | PFM Act to establish publication requirements for all documents (e.g, timing and form) |
| | **1.11** | PFM Act to include set of sanctions to deal with breaches of fiscal responsibility provisions (e.g, automatic sanctions) |
| **Budget Preparation and Execution** | **2.1** | PFM Act to empower Ministry of Finance to prescribe the manner of budget preparation, execution, performance reporting, and in-year reporting requirements for National, Subnational and other government entities. |
| | **2.2** | PFM Act to designate Ministry of Finance with authority to develop/ issue instructions regarding unified classifications to be applied across the general government in the preparation, execution, and accounting of the budget |
| | **2.3** | PFM Act to provide virement rules: no virement between ministries; some virement between programs; some virement between broad economic categories. |
| | **2.4** | PFM Act to include provision for carryover with strict rules and procedures |
| | **2.5** | PFM Act to provide that preparation/approval / execution of a supplementary budget governed by same principles and rules applicable to the approval and execution of the annual budget |
| | **2.6** | PFM Act to provide for Contingencies Fund (unforeseeable, unabsorbable, unavoidable) |
| | **2.7** | PFM Act to provide procedures to report to Controller of Budget and Parliament on Contingencies Fund |

**Table 1: Public Financial Management Law/Budget Law Recommendations**

| Area | | Recommendations |
|---|---|---|
| **Treasury and Cash Management** | **3.1** | PFM Act to reflect budget execution controls, cash management responsibilities, and the financial control responsibilities of the Ministry of Finance (Treasury). |
| | **3.2** | PFM Act to prescribe treasury single account (TSA) approach for all government banking arrangements. PFM Act to prescribe a Subnational Government (TSA) approach from onset (to be defined in Treasury issued regulations) |
| | **3.3** | PFM Act to require treasury to provide regulations on: the collection, management, and reporting of non-tax revenues on a gross basis; (donor funds reflected in the budget if applicable), in the in-year reports, and in the accounts; and the collection, processing, and reporting of earmarked taxes. |
| **Borrowing Guarantees and Management** | **4.1** | PFM Act to provide relevant provisions governing the principles, control and oversight of public debt and debt management. |
| | **4.2** | PFM Act to include clear definitions of the concepts of 'borrowing' and "guarantees. |
| | **4.3** | PFM Act to include provisions strengthening Treasury's authority to oversee and control borrowing & guarantees. |
| | **4.4** | PFM Act to include provisions/rules for borrowing by Subnational Governments and State-owned operations; rules regarding government guarantees to be specified; and, rules regarding borrowing by public agencies and funds should be established. |
| | **4.5** | PFM Act to provide for combining g loan guarantees with all other sources of contingent liabilities to assist more effective fiscal risk management. |
| | **4.6** | PFM Act to establish basis for implementing fiscal rules on public debt and guarantees under which, parliament should set annual limits (cap)(e.g, including by sub-national governments and SOEs). |
| | **4.7** | PFM Act should provide that the Treasury is the only body allowed to contract debt in foreign currency. |
| | **4.8** | PFM Act should provide for: strengthening Treasury's access to bank account data (balances and flows) for projects; strengthen regular and timely reporting projects; and, establish a framework to agree on specific arrangements for donors who have multiple projects. |
| **Accounting and Audit** | **5.1** | PFM Act should provide guidelines to establishing international accepted accounting standards to be reported by all Government Entities. |
| | **5.2** | PFM Act should stipulate roles, responsibilities for Internal Auditing and financial reporting, External Auditing by Inspector General, and special provisional reporting. |
| | **5.3** | PFM Act should stipulate additional role for value for money audits. |

**Table 1: Public Financial Management Law/Budget Law Recommendations**

| Area | | Recommendations |
|---|---|---|
| **Intergovernmental Fiscal Relations** | **6.1** | PFM Act to specify appropriate assignment of roles and responsibilities for subnational government as well as national government. |
| | **6.2** | PFM Act to include subnational governments in the entities covered by the comprehensive public financial management requirements. |
| | **6.3** | PFM Act to establish requirements relating to the process for determining the funding for subnational governments including alignment of subnational government and national budget calendars. |
| | **6.4** | PFM Act to set out requirements relating to the disbursement of funding to subnational governments including the criteria to be applied for disrupting disbursements. |
| | **6.5** | PFM Act should establish requirements relating to the role of Ministry of Finance (Treasury) in collecting, consolidating, dispersing, and publishing subnational government level financial and non-financial performance information. |
| | **6.6** | PFM Act should establish requirements for annual budgets and appropriations for subnational governments including: Plans and budget documents; strategy and compliance with fiscal responsibility requirements; Form of appropriations and requirements relating to the Appropriation Bill; Key dates and actions for the budget cycle; Consultation requirements; and, power for Ministry of Finance (Treasury) to issue instructions relating to these documents and processes. |
| | **6.7** | PFM Act should include accountability mechanisms for subnational government performance (e.g. performance specification, agreements, reporting, monitoring, review, and rights to follow up on performance issues). |
| | **6.8** | PFM Act to include criteria for issuing guarantees for subnational government debt; and, right of Ministry of Finance to obtain information relating to the financial viability of the subnational government. |
| **Agencies, Funds and Enterprises** | **7.1** | PFM Act to contain definitions, differentiation and criteria for agencies, funds, enterprises. |
| | **7.2** | PFM Act to specify what PFM rules apply to agencies, funds and enterprises. |
| | **7.3** | PFM Act to prescribe specific reporting obligations of entities to be reflected in the budget documents, fiscal reports and annual accounts. |
| | **7.4** | PFM Act to establish a clear and comprehensive framework governing entity financing arrangements. |
| | **7.5** | PFM Act to specify circumstances that sub-national government's right to establish and terminate entities. |
| | **7.6** | PFM Act to specify provisions regarding PFM standards applicable to these agencies and funds consistent with |

**Table 1: Public Financial Management Law/Budget Law Recommendations**

| Area | | Recommendations |
|---|---|---|
| | | the standards applicable to the government. |
| | **7.7** | PFM Act to prescribe rules governing the fiscal relations of the government with enterprises. |
| | **7.8** | PFM Act to include roles and responsibilities of the MoF in monitoring State Owned Enterprises (SOEs') transactions and operations for potential contingent liabilities. |
| | **7.9** | PFM Act to consider specific rules for oversight and monitoring of other government's investments (e.g. Public, Private, Partnership (PPP)). |
| **Sanctions, Transitional Arrangements** | **8.1** | Design a new sanctions regime, with its corresponding enforcement mechanisms, to be included in the Integrated PFM Act. |
| | **8.2** | Sanctions regime in PFM Act should be comprehensive applicable to all public officials and entities for of all levels of government (including subnational government structures). |
| | **8.3** | Sanctions regime to be included in PFM Act should contain, at a minimum, the following elements: specific description of the types of actions or omissions that will be considered misconducts, infringements; clear and specific description of the types of sanctions that will apply; personal and institutional sanctions; and, Administrative, disciplinary, civil and criminal sanctions. |
| | **8.4** | PFM act should provide for the person(s) or entity(ies) that will be charged with the responsibility of enforcing the sanctions regime under the PFM Act. |
| | **8.5** | PFM Act should provide that the person or entity responsible for enforcement shall select clear and prominent cases of noncompliance or contravention and publicize them, stressing the action or omission that triggered the application of the procedures under this regime and the corresponding sanction that was applied. |
| | **8.6** | PFM Act should provide that the sanctions regime include as a criminal offence the failure by a public officer to report to the relevant authority the existence of a contravention or infringement of the law, when that public officer has knowledge of such actions. |

## Table 2: Definitions for Consideration

| Term | Recommendation |
|---|---|
| **Accounting standard(s)** | Accounting standards means principles that governs current accounting practice and that is used as a reference to determine the appropriate treatment of financial transactions as approved by the Ministry of Finance (Treasury). Should include Internationally Accepted Accounting Standards. |
| **Accounting /budget officer** | Accounting/budget officer" means:<br>(a) a person who by any law, regulation or appointment is charged with the duty of collecting or receiving, or who actually collects or receives, or who is charged with the duty of disbursing, or who actually disburses, any public money,<br>(b) a person who by any law, regulation or appointment is authorized to commit or incur the expenditure of public money,<br>(c) a person who by any law, regulation or appointment is charged with a duty relating to the keeping of accounts with respect to public money, or<br>(d) a person who by any law, regulation or appointment is charged with a duty relating to the purchase, receipt, issue, sale, custody, control, management or disposal of, or the accounting for, public property or who actually purchases, receives, issues, sells, keeps in custody, controls, manages, disposes of, or accounts for, public property. |

## I. NEAR TERM ACTION PLAN

**14. The process of drafting the new Integrated PFM Act should be guided by the principles of transparency and inclusiveness.** For this purpose, Treasury should take into account the following steps:

- Ensure that all key stakeholders shall be effectively involved in the process;
- Ensure that the views and recommendations of all stakeholders involved are heard and taken into consideration as appropriate in the decision making process; And,
- Ensure that the design of the new Integrated PFM Act takes into account current and, future needs, goals and relative capacities.

**15.** The process for drafting, submitting and approving the new Act requires careful consideration of the necessary steps required to allow all stakeholders to internalize that the reform is needed and to generate a "political consensus" that it is in the best interest of Kenya. In order to accomplish the task of completing and meeting Parliamentary approval deadlines, the mission recommends:

- Treasury name a drafting team with the specific Terms of Reference to write, define, and complete a draft Integrated PFM Act by April 30, 2011
- This small PFM Act drafting team should include persons familiar with: 1) Public Financial Management and knowledge of treasury, budgeting and other aspects of Intergovernmental Fiscal, 2) have legal drafting skills, and be able to organize and draft sections of the PFM law on a fast-track schedule.
- Any public sector official should be excused from his/her day-to-day responsibilities and be seconded exclusively to this task.
- The draft Integrated PFM Act should be developed in modular form, with newly completed sections undergoing a formal review/vetting process with relevant stakeholders. As such, a formal review process should be established with regular reporting requirements and deadlines.
- AFE (IMF) will be able to provide six weeks of international consultancy assistance (through April), plus additional assistance from AFE's regional PFM advisors to assist in defining and refining the organic budget law. AFE will review whether additional resource requirements are needed after April 30, 2011.
- FAD (IMF) will provide headquarter support on refining the draft integrated PFM Act as required.

East AFRITAC
INTERNATIONAL MONETARY FUND
REGIONAL TECHNICAL
ASSISTANCE CENTER

June 2, 2011

To: Dr. Thugge
Dr. G. Mwau

From: East AFRITAC PFM Advisors (Michael Schaeffer/Guy Anderson/Onesmus Ayaya) and Mario Gutierrez (Fiscal Policy Advisor)

**Re: Comments to Integrated PFM Act – May 2011**

East AFRITAC (IMF) has provided comments on earlier working drafts of this Integrated PFM law. We are pleased to find that some of our earlier suggestions have been incorporated. Upon reading the document in its entirety our general commentary is: 1) the draft integrated PFM law has come a long way from its inception phase but still needs refinement; and, 2) this draft is somewhat prescriptive and some of the detail could best be relegated to forthcoming financial regulations rather than being embedded directly into this law.

**Part I – Preliminary**
Several definitions provided in Part 1-Preliminary (e.g., expenses) provide for a definition '*in accordance with generally accepted accounting principles'*. These definitions should be succinctly provided in this section rather than referencing GAAP or IAS standard principles (See Table 1, below).

**Part II – Responsibilities and Powers in Relation to Public Finances**

**Section 22 - National Treasury:** The discussion of the functions of the National Treasury should be clarified with respect to the custodianship of real and financial assets. Under the new Constitutional environment accounting officers would be responsible for resources including assets assigned to the various Votes. National Treasury would issue policy and guidelines for management of assets, rather than being the custodian of these (real, financial) assets.

**Section 24- County Treasury:** The establishment of county treasuries and their role and functions has been provided for in the draft legislation albeit in a somewhat unclear manner. Specific sections that have been devoted to county financial matters are located within the

intergovernmental fiscal framework. These should be brought forward to the responsibilities section. Other issues: It is not clear who should head the country treasury?; Some of the duties of a county treasury should be to exercise control over budget implementation, comply with CRA provisions, monitor implementation of norms and standards, and intervene in cases of serious breaches of this Integrated Public Financial Management Law. Further, in contradiction to Section (j), asset management in a budgetary body is the responsibility of the accounting officer.

**Section 26 - Controller of the Budget:** The Constitution provides for the Controller of the Budget to submit reports every four months. Section 26.1.c provides for quarterly report submissions. Further, Section 26.1.d.i provides that the Controller of the Budget submit *'non-financial performance reports'*. Non-financial performance reports should be submitted by the Accounting Officers of the Governing Bodies of Public Entities.

**Section 27- Auditor General:** Under section 27.1.g the public debt - shouldn't this already be part of the national consolidated accounts?

**Section 30 – Commission on Revenue Allocation:** The description of the duties and functions is well documented. However, some of this discussion (processes) may actually be more suited to the section on intergovernmental fiscal relations?

**Sections 33-34 – Accounting Officers:** The draft legislation should confer broader responsibilities to accounting officers and accounting authorities (governing bodies of government entities), including establishment and operation of basic financial management system (including internal controls). These sections should consider the following headings:

- General responsibilities of accounting officers
- Budgetary control responsibilities
- Reporting responsibilities
- Responsibilities for assets and liabilities transferred to a public entity or another level of government
- Responsibilities in relation to submission of information to AG, NT, NA, and Cabinet secretary
- Responsibilities in relation to budget reallocation and virements
- Responsibilities in relation to revenue and debtor management.

**Section 35 – Discipline, Reporting of Government Officers:** We recommend as part of the definition of improper behavior to include Section 35.2.d fails to collect or account for revenues due.

**Sections 37 to 39:** These provisions should be located under accounting officers responsibilities' for revenue and debtor management. Proceed to provide clause that empowers accounting officers to delegate to other public officials

**Part 3-Fiscal Responsibility**

**Section 42 (h) Principles of Public Finance -** The guiding principles speak to annual budgets rather than multi-year budgets or program budgets (which are multi-year in nature). Does the Law need to be future proofed to include multi-year budgets?

**Section 42.2 Fiscal Responsibility Principles -** There needs to be greater clarity on the definition of county revenues. Does it include national transfers, development grants, equalization grants etc.

**Section 50.2 County Government Economic and Fiscal Update -** Clarity is needed with respect to the nature of the election. Do the drafters mean a county election? A by-election?

**Section 50.2.a.ii County Government Economic and Fiscal Update -** Does this imply that all police and security budget allocations for that election year are indirect expenses? This section needs to concentrate on election related activity budgets only.

**Part 4- Intergovernmental Fiscal Relations**

**Section 53 (1) Funding County Governments -** This section should clearly define all County Government revenue sources. What is meant by own revenue?

**Section 56 - Unconditional Grants:** The draft law defines that unconditional funds are spent without conditions. As such, Section (2) then goes on to provide conditions. Section (2) should be removed.

**Section 59 – Loans and External Grant:** It is understood, that loans, grants and own-source revenues etc. make up the general sources of funding for country government. What is unclear is what is meant by '*external grants shall be as negotiated with the development part'*. Further, to what extent can counties negotiate directly with development partners?

**Section 61 – Assessing Revenue Raising Capacity by Counties:** It is not clear how the Commission of Revenue allocation would under Section 61 a) and b) would 1) impose financial penalties for counties which fail to adequately support or suppress revenue raising capacity; and 2) how the Commission of Revenue allocation would actually determine whether there is a deliberate attempt to suppress revenue enhancing by sub national governments?

**Sections 66-71 Government Budget and Economic Council and County Government and Economic Forum -** These two sections are mirror images of each other. However, it is not clear what their functions and relationships are to the national and county budget processes. Further, how do these bodies relate to each other? What are these organizations expected to produce? What are they expected to do?

**Part 5- National Budget**

**Section 80 (b) iv National Budget Document.** Budget Presentation should include programs (and outputs) rather than just recurrent and development expenditure.

**Section 80.1.e. National Budget Document -** This section provides for a ***Treasury Memorandum*** being submitted as part of the budget documents. As such, this appears to be out of place with other requirements in terms of national budget submission.

**Section 81 (a) National Budget Approval Section 81 a -** Any increase in expenditure in a proposed appropriation is to be balanced by a reduction in expenditure in one or more proposed appropriations. This does not apply when talking of natural disasters or state of emergency. Should this be stated as exception?

**Section 82 Deferred Approval of Division of Revenue Bill and County Allocation of Revenue Bill** March 15th, appears to be very late in the budget cycle to pass a revenue bill as such it would be difficult for county governments to develop a budget. Perhaps, moving this deadline up by 1 or 2 months would be appropriate. Further, what happens if no bill is proposed by March 15th? Are there any contingency plans provided for?

**Section 84 – Reallocations Between Programmes or Sub-votes -** This section should include a provision that no transfer of funds between item control totals within a given program may be made without the approval of Treasury, which may subject to certain constraints approve such transfers. There are two types of item transfers within programs which Treasury should not be authorized by the Parliament to approve. The first of these is transfers *to* personnel expenses from any other item control total. The second is transfers *away from* capital expenditure to any other item control total. The ban on transfers to personnel expenses means that each ministry must respect absolutely the upper limit imposed by the Parliament on personnel expenses in the budget estimates. The reason for this is that hiring additional staff usually creates expenditure obligations not only in the financial year when those staff are hired, but in future financial years. Maintaining control of expenditure therefore requires firm control of staffing decisions. This firm control will continue to be supported by the requirement of Public Service Commission approval of ministry staffing levels. The ban on transfers away from capital expenditure is designed to prevent ministries from inappropriately sacrificing capital expenditure, which builds assets and infrastructure for the future, in order to increase current expenditure. *It may be prudent to allow for the Cabinet Secretary to authorize reallocations outside these limits in extraordinary situations.*

**Section 85 Contingencies Fund** Under the current description it is not clear how the Contingencies Fund will actually work. It is our recommendation that the Contingencies Fund be viewed as an unassigned budget category that can be accessed under urgent and unforeseen circumstances, whereby the mechanism for releasing the contingencies fund is through budget reallocation.

**Section 86 Supplementary Appropriations for National Government -** The current provision allows for approval of expenditure that has not been appropriated subject to several conditions. AFE (PFM) would simply state that it is inappropriate to spend without any budget appropriations. This section should be revised to meet that condition. The Contingencies Fund (see Section 85, above) should be sufficient to cover most urgent, unforeseen activities. AFE

(PFM) stands by its earlier recommendations that supplemental budgets should be approved by Parliament as part of the mid-year assessment review. Supplementary estimates can be positive or negative.

**Section 89 Expiry of Appropriation -** The Government should consider a mechanism for unused, committed development budgets to be rolled-over/carried-forward.

**Part 6- County Government Budgets**

**Section 93 - County Budget Process -** It is unclear how a Governor of a County can produce a Fiscal Strategy?

**Section 96 - Consultation** Section 96.1 should indicate that there shall be a consultation process with the public; Section 96.2 should define a method and time table for the consultative process.

**Section 97.1.e. County Budget Document -** This section provides for a ***Treasury Memorandum*** being submitted as part of the budget documents. As such, this appears to be out of place with other requirements in terms of county budget submission.

**Section 98 County Government Approvals -** What happens when the county is not approved by the start of the financial year?

**Section 100 – Reallocations between programmes or Sub-votes -** See comment for Section 84 (above) for national budget.

**Part 7 – National Government Reporting**

**AFE (PFM) would suggest reversing the order of Annual Reporting by National Treasury (Sections 101-106) and Annual Reporting by Accounting Officers (Sections 107-108)**

**Section 107 Annual Reporting by National Treasury-** This section should:

- Make clear reference to International Public Sector Accounting Standards.
- Specifically list responsibilities of the Accountant General in relation to producing consolidated statements and setting standards.
- There should be a stipulation of a formal oversight report adoption by Parliament regarding annual financial statements.

**Section 101** should be reorganized to discuss the reporting by **Accounting Officers** first and consolidation second in the process.

- With respect to the section on Accounting Officers - this must specify the timetable and financial statements that should be prepared by the Accounting Officers.
- These financial statements should comply with IPSAS accounting standards.

- There should be a stipulation in the financial statements produced, prepared and submitted by the accounting officers should contain/accompany an annual report of non-financial performance information.
- The calendar should be stipulated: Financial statements submitted for audit no later than 31 August and should be audited by 31 October.
- Consolidated financial statements should be started in parallel. So as to have the consolidated financial statements audited by December 31.

**Section 101.1.a** As financial statements are based on a comprehensive financial system and not just bank accounts, the reference to exchequer accounts should be removed.

**Section 108 -** If sections 33-34 are revised as indicated above, then there is no need to incorporate section 108.

**Section 109 - Reporting on other Public Funds -** Unless a distinction is drawn between entities in line ministries and public entities this section will be difficult to implement. This section should be revisited after drawing a clear distinction between funds within line ministries and other public entities.

**Section 110.1 - Periodic Reports for National Government** - This section should be eliminated because it is already dealt with under the revised sections 33-34.

**Section 112 Debt Reporting -** This section should be retained under a separate Public Debt Management and Reporting section.

**Part 8 - County Government Reporting**
Section 8 - County Government reporting is a mirror image of national government reporting. As such, we recommend the same treatment as provided for in Part 7, above. In addition, provision should be made for time frames for submission of financial statements, preparation and adoption of an annual report, formats and contents of financial statements and annual reports, disclosure of intergovernmental allocations, submission and tabling of annual reports to county assemblies, oversight reports by county assemblies, auditing of financial statements, and compliance of financial standards with International Accounting Standards.

**Part 9-Treasury Management**
**Sections 124-128 Prohibitions -** The law should provide for the roles and responsibilities of Accounting Officers and Cabinet Secretaries. As a result, this list of prohibitions is redundant, not necessary and should be removed.

**Part 10 -Special Provisions**

## Table 1: Revising Definitions for Consideration

| Term | Definition as Provided in Current Draft Law | Recommendation |
|---|---|---|
| **Accounting standard(s)** | Accounting standards means authoritative statements of how particular types of transactions and other events should be reflected in the accounts as approved by the National Treasury. | Accounting standards means principles that governs current accounting practice and that is used as a reference to determine the appropriate treatment of financial transactions as approved by the National Treasury. |
| **Accounting officer** | Accounting officer means a person designated to be an accounting officer within the meaning of the constitution or any person designated by the Cabinet Secretary responsible for Finance, who is charged with the duty of accounting for any service in respect of which money has been appropriated by Parliament or any person to whom issues are made from the consolidate or county revenue fund. | Accounting officer" means:<br>(a) a person who by any law, regulation or appointment is charged with the duty of collecting or receiving, or who actually collects or receives, or who is charged with the duty of disbursing, or who actually disburses, any public money,<br>(b) a person who by any law, regulation or appointment is authorized to commit or incur the expenditure of public money,<br>(c) a person who by any law, regulation or appointment is charged with a duty relating to the keeping of accounts with respect to public money, or<br>(d) a person who by any law, regulation or appointment is charged with a duty relating to the purchase, receipt, issue, sale, custody, control, management or disposal of, or the accounting for, public property or who actually purchases, receives, issues, sells, keeps in custody, controls, manages, disposes of, or accounts for, public property. |

| Area | | Recommendations |
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| **Macro-Economic and Fiscal Policy** | **1.1** | PFM Act to contain fiscal principles including fiscal policy, fiscal objectives, targets to guide annual budget |
| | **1.2** | PFM Act to include fiscal rules limiting debt (e.g., total debt as a percentage of GDP) |
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| **Budget Preparation and Execution** | **2.1** | PFM Act to empower Ministry of Finance to prescribe the manner of budget preparation, execution, performance reporting, and in-year reporting requirements for National, Subnational and other government entities. |
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| | **2.4** | PFM Act to include provision for carryover with strict rules and procedures |
| | **2.5** | PFM Act should include a provision for Vote on Account in the eventuality that a budget is not approved in a timely manner. |
| | **2.6** | PFM Act to provide that preparation/approval / execution of a supplementary budget governed by same principles and rules applicable to the approval and execution of the annual budget |
| | **2.7** | PFM Act to provide for Contingencies Fund (unforeseeable, unabsorbable, unavoidable) |
| | **2.8** | PFM Act to provide procedures to report to Controller of Budget and Parliament on Contingencies Fund |
| **Treasury and Cash Management** | **3.1** | PFM Act to reflect budget execution controls, cash management responsibilities, and the financial control responsibilities of the Ministry of Finance (Treasury). |

| Area | | Recommendations |
|---|---|---|
| | **3.2** | PFM Act to prescribe treasury single account (TSA) approach for all government banking arrangements. PFM Act to prescribe a Subnational Government (TSA) approach from onset (to be defined in Treasury issued regulations) |
| | **3.3** | PFM Act to require treasury to provide regulations on: the collection, management, and reporting of non-tax revenues on a gross basis; (donor funds reflected in the budget if applicable), in the in-year reports, and in the accounts; and the collection, processing, and reporting of earmarked taxes. |
| **Borrowing Guarantees and Management** | **4.1** | PFM Act to provide relevant provisions governing the principles, control and oversight of public debt and debt management. |
| | **4.2** | PFM Act to include clear definitions of the concepts of 'borrowing' and "guarantees. |
| | **4.3** | PFM Act to include provisions strengthening Treasury's authority to oversee and control borrowing & guarantees. |
| | **4.4** | PFM Act to include provisions/rules for borrowing by Subnational Governments and State-owned operations; rules regarding government guarantees to be specified; and, rules regarding borrowing by public agencies and funds should be established. |
| | **4.5** | PFM Act to provide for combining g loan guarantees with all other sources of contingent liabilities to assist more effective fiscal risk management. |
| | **4.6** | PFM Act to establish basis for implementing fiscal rules on public debt and guarantees under which, parliament should set annual limits (cap)(e.g, including by sub-national governments and SOEs). |
| | **4.7** | PFM Act should provide that the Treasury is the only body allowed to contract debt in foreign currency. |
| | **4.8** | PFM Act should provide for: strengthening Treasury's access to bank account data (balances and flows) for projects; strengthen regular and timely reporting projects; and, establish a framework to agree on specific arrangements for donors who have multiple projects. |
| **Accounting and Audit** | **5.1** | PFM Act should provide guidelines to establishing international accepted accounting standards to be reported by all Government Entities. |
| | **5.2** | PFM Act should stipulate roles, responsibilities for Internal Auditing and financial reporting, External Auditing by Inspector General, and special provisional reporting. |
| | **5.3** | PFM Act should stipulate additional role for value for money audits. |
| **Intergovernmental Fiscal Relations** | **6.1** | PFM Act to specify appropriate assignment of roles and responsibilities for subnational government as well as national government. |
| | **6.2** | PFM Act to include subnational governments in the entities covered by the comprehensive public financial management requirements. |
| | **6.3** | PFM Act to establish requirements relating to the process for determining the funding for subnational governments including alignment of subnational government and national budget calendars. |

| Area | | Recommendations |
|---|---|---|
| | **6.4** | PFM Act to set out requirements relating to the disbursement of funding to subnational governments including the criteria to be applied for disrupting disbursements. |
| | **6.5** | PFM Act should establish requirements relating to the role of Treasury in collecting, consolidating, dispersing, and publishing subnational government level financial and non financial performance information. |
| | **6.6** | PFM Act should establish requirements for annual budgets and appropriations for subnational governments including: Plans and budget documents; strategy and compliance with fiscal responsibility requirements; Form of appropriations and requirements relating to the Appropriation Bill; Key dates and actions for the budget cycle; Consultation requirements; and, power for Ministry of Finance (Treasury) to issue instructions relating to these documents and processes. |
| | **6.7** | PFM Act should include accountability mechanisms for subnational government performance (e.g. performance specification, agreements, reporting, monitoring, review, and rights to follow up on performance issues). |
| | **6.8** | PFM Act to include criteria for issuing guarantees for subnational government debt; and, right of Ministry of Finance to obtain information relating to the financial viability of the subnational government. |
| **Agencies, Funds and Enterprises** | **7.1** | PFM Act to contain definitions, differentiation and criteria for agencies, funds, enterprises. |
| | **7.2** | PFM Act to specify what PFM rules apply to agencies, funds and enterprises. |
| | **7.3** | PFM Act to prescribe specific reporting obligations of entities to be reflected in the budget documents, fiscal reports and annual accounts. |
| | **7.4** | PFM Act to establish a clear and comprehensive framework governing entity financing arrangements. |
| | **7.5** | PFM Act to specify circumstances that sub-national governments right to establish and terminate entities. |
| | **7.6** | PFM Act to specify provisions regarding PFM standards applicable to these agencies and funds consistent with the standards applicable to the government. |
| | **7.7** | PFM Act to prescribe rules governing the fiscal relations of the government with enterprises. |
| | **7.8** | PFM Act to include roles and responsibilities of the MoF in monitoring SOEs' transactions and operations for potential contingent liabilities. |
| | **7.9** | PFM Act to consider specific rules for oversight and monitoring of other government's investments (e.g. PPP). |
| **Sanctions, Transitional Arrangements** | **8.1** | Design a new sanctions regime, with its corresponding enforcement mechanisms, to be included in the Integrated PFM Act. |
| | **8.2** | Sanctions regime in PFM Act should be comprehensive applicable to all public officials and entities for of all levels of government (including subnational government structures). |
| | **8.3** | Sanctions regime to be included in PFM Act should contain, at a minimum, the following elements: specific description of the types of actions or omissions that will be considered misconducts, infringements; clear and |

| Area | | Recommendations |
|---|---|---|
| | | specific description of the types of sanctions that will apply; personal and institutional sanctions; and, Administrative, disciplinary, civil and criminal sanctions. |
| | **8.4** | PFM act should provide for the person(s) or entity(ies) that will be charged with the responsibility of enforcing the sanctions regime under the PFM Act. |
| | **8.5** | PFM Act should provide that the person or entity responsible for enforcement shall select clear and prominent cases of noncompliance or contravention and publicize them, stressing the action or omission that triggered the application of the procedures under this regime and the corresponding sanction that was applied. |
| | **8.6** | PFM Act should provide that the sanctions regime include as a criminal offence the failure by a public officer to report to the relevant authority the existence of a contravention or infringement of the law, when that public officer has knowledge of such actions. |

East AFRITAC
INTERNATIONAL MONETARY FUND
REGIONAL TECHNICAL
ASSISTANCE CENTER

June 30, 2011

To: Dr. Kamau Thugge (MOF)
Haron Sirima (MOF)

From: FAD (IMF) and East AFRITAC (AFE-IMF) PFM Advisors

Cc: S. Flynn (IMF FAD)
R. Gudmundsson (IMF Resident Representative)
X. Maret (East AFRITAC, Coordinator)

## Re: Comments to the June 15th, Integrated PFM Bill

FAD (IMF) and East AFRITAC (IMF) would like to raise the following concerns, some of which were conveyed in previous comments, regarding the current June 15 draft of the PFM law, as well as issues raised during the CIC forum on June 27, 2011.

## 1. Clarity of roles and responsibilities

1.1 **The roles and responsibilities in Part II do not adequately cover all key actors** - Public Accounts Committee, National Assembly, Senate, Principal Secretaries, County Secretaries for Finance, and County Secretaries generally are missing. Each of these requires specific responsibilities to be spelt out avoiding any overlapping responsibilities.

1.2 **The coverage of the Parliament in particular seems skewed**. There is mention of the Budget Committee but not the Public Accounts Committee, and there is no mention of the National Assembly or the Senate.

1.3 Also the **inclusion of the Parliamentary Budget Office is unorthodox** (this is usually an internal matter of the Parliament) - the background of the 2009 Fiscal Management Act which set up the Office is of course understood. Since it is a transitional arrangement (article 5 of the Second Schedule – Section 100) pending the establishment of the Parliamentary Services Commission, it should not appear in Part II (or any other part) of the law (otherwise the law itself will need to be amended when the PSC comes to its own decision on the matter.

1.4 The law should be **very clear on the roles and responsibilities of the Controller of the Budget**. According to the Constitution it has an ex-ante pre-audit compliance role, culminating in fiduciary assurance reporting to Parliament. It has no role in policy, and should not conflict/overlap in any way with the role of the ex-post audit function of the Auditor General. The current draft has the ***Controller of the Budget as member of the National Budget and***

***Economic Council***, which is a *policy formulation body*. Other assigned responsibilities should be carefully reviewed to ensure coherence with the above role of the Controller of the Budget.

1.5 **The law should provide for delegation of assigned roles and responsibilities** in the relevant sections of Part II, with the caveat that delegation of responsibilities does not abrogate accountability. For example, the responsibilities related to the design and control of the public financial management system vested in the Cabinet Secretary for Finance should be delegated to the Permanent Secretary for Treasury.

1.6 **The draft integrated PFM law is largely silent on the responsibilities of the Members of the County Executive**.

1.7 **The roles and responsibilities of Accounting Officers and other accounting authorities (governing bodies of state corporations), should be fully spelt out in <u>regulations</u> issued by the Treasury.** These regulations should provide detailed guidance in the following areas:

- General responsibilities of accounting officers;
- Establishment and operation of basic financial management systems;
- Budgetary and other internal control responsibilities;
- Reporting responsibilities, both internal and external;
- Responsibilities for assets and liabilities, including those transferred to a public entity or another level of government;
- Responsibilities in relation to submission of information to National Treasury, Controller of the Budget, Auditor General, and National Assembly;
- Responsibilities in relation to budget reallocation and virements; and,
- Responsibilities in relation to revenue collection and debtor management.

## 2. Budget issues

2.1 The **link between planning** (from Vision 2030 to line ministry strategic plans) **and budgeting could be addressed in the law**. While the detailed instructions would be in regulations and circulars, the law could establish the principle of linkage between planning and budgeting. For Accounting Officers, this could be done by adding a responsibility to "prepare strategic plans for the entity he/she is responsible for which are in conformity with the medium-term fiscal framework and national policy objectives" before part (h) of Section 17 (2), and by adding the phrase "that are in conformity with strategic plans" after "estimates of expenditure" in part (h) of same Section.

2.1 As commented in earlier FAD and AFE submissions, **appropriations (section 37) should be moved to the program level** (program budgeting is advanced and failure to do this would be an inhibiting factor). This should be similarly envisaged for county budgets (section 46), although this may require delayed implementation pending roll-out of program budgeting to Counties.

2.2 **Related to this is the need to move reallocation limits (section 40) to the program level** rather than the ministry level, coupled with restrictions on reallocations to wages items and away from capital items. Same should apply to county budgets (sections 49). More detailed reallocation rules should be prescribed in regulations.

2.3 In line with the spirit and letter of the Constitution, the Law should explicitly provide for **public consultation at key stages of budget formulation**. The law could provide for public

consultation during the preparation of the Budget Policy Statement (section 24), as well as the County Fiscal Strategy Papers (section 29). The National Budget and Economic Council the County Budget and Economic Forums could also be required to invite civil society representatives from time to time (Section 32 (5) and Section 32 (5)), rather than leaving it to the discretion of these entities.

## 3. Annual reporting

3.1 As commented in earlier FAD and AFE submissions, **the law should require accounting standards and financial statements (section 11) to follow international standards**, with preference for an explicit reference to **IPSAS**. It should also specify how these standards are to be formulated and prescribed, with preference given to a joint effort between Accountant General and Auditor General (the option of a Standards Board may not be available/appropriate at this time in Kenya).

3.2 The law should have a provision (either explicit or through regulation) for **prescribing the contents of annual reports prepared by the Treasuries**. The contents could include: a statement of cash receipts and payments; a statement of comparison of budget to the outturn; a statement of financial position; and, a report on intergovernmental fiscal transfers.

3.3 **There is no provision for adoption by Parliament of the audit report, an essential oversight element, nor any provision for the treasury memorandum**. Both of these require specific deadlines (the first is actually in the Constitution - 229(8)).

3.4 **Reference to exchequer bank accounts under Section 52 is out of place for two reasons**: (a) Counties do not have exchequer accounts; and (b) annual accounts and financial statements should be comprehensive, covering all government funds, some of which may be managed outside the exchequer bank account (e.g. Contingencies Fund, Judicial Fund, etc...). Also there is a need to clarify the difference between the exchequer account (defined in Part I) and the treasury single account (defined in section 70).

## 4. Resolution of financial problems

4.1 **Resolution of financial problems in county government is a key aspect of co-operative governance.** The Constitution of Kenya provides for national government intervention in County affairs in cases of material breeches of county government obligations and responsibilities (Section 72). The PFM law should provide for the resolution of financial problems, types of national government intervention, criteria for determining serious financial problems, preparation of recovery plans, and implementation of recovery plans.

## 5. Improved clarity of financial provisions for State Corporations

5.1 **Part VIII remains inadequate and does not address issues raised on several occasions by FAD and AFE**, including:

- It fails to distinguish between State Owned Enterprises (SOEs) and Semi-Autonomous/Autonomous Agencies and Extra-Budgetary Funds (SAGAs/AGAs/EBFs), or to differentiate their treatment vis-a-vis the budget;
- It does not recognize the possibility of such entities at the County Government level;
- It does not prescribe any in-year reporting and the role of the governing bodies;
- It does not provide for policy and financial coordination during budget preparation;

- It does not give the Treasury any authority to establish rules and procedures and issue regulations for State Corporations; and,
- It is not clear why the annual information gathered by the Treasury should be submitted to the Controller of Budget.

5.2 **The law, as currently written, does not state that its provisions override the State Corporations Law** and other specific laws that created some of these entities. Of particular concern is the current inclusion of Local Authorities as entities governed under the State Corporations Act – these should be removed as they will now be part of devolved county governments.

5.3 **Two schedules listing current entities covered by the State Corporation Act should be attached to the law**, one for SOEs, the other for SAGAs/AGAs/EBFs.

5.4 **Financial management and reporting responsibilities**, which should be clearly spelt out in the PFM law, should be **assigned to each entity's Chief Executive Officer** under the supervision of its relevant governing body.

5.5 **The Chief Executive Officer of these entities should account to Parliament or County Assemblies** through the relevant accounting authorities (governing bodies) in the same way accounting officers of line ministries can account to parliament through the relevant cabinet secretaries in order to conform to the existing codes of good corporate governance.

## 6. Responses to other issues raised during the CIC forum

6.1 **Removing accounting and reporting responsibilities from MoF is not appropriate**. There are sufficient checks in place, both ex-ante (Controller of the Budget) and ex-post (Auditor General).

6.2 The **establishment of a loans and grants board is not necessary.** there are sufficient provisions in the law to address all issues arising from borrowing and receipt of grants, which should be vested in the Treasury as part of its overall responsibility of sustainable macro-fiscal management and financial control.

# DRAFT FEDERAL BUDGET LAW

Behalf of the people
The Presidency of Republic

Resolution No. (  )

As approved by the House of Representatives and in accordance with the provisions of paragraph (First) of Article (61) of the Constitution

The President of the Republic decided on  /  /2010
the issuance of the following law:

No. (  ) for the year / 2011

**General Federal Budget Law of the Republic of Iraq for the fiscal year / 2011**

((Chapter I))

## Revenue

Article 1 (First): A - Estimated revenues of the federal budget for the fiscal year / 2011
Amount of 78705237500 thousand dinars (eight and seventy thousand
Seven hundred and five billion two hundred and thirty-seven million five hundred thousand dinars), as shown in (Table / according to a revenue accounts attached to this law.

B - Calculation of income resulting from export of crude oil based on the average price of 73 dollars per barrel and the

rate of export of (2.25 million) barrels per day (two million two hundred and fifty thousand barrels per day) of (150000) barrels per day (one hundred and fifty thousand barrels per day) for revenue resulting from the export of crude oil through the territory of Kurdistan and to commit the province to transfer revenues from that to fund of reconstruction of Iraq DFI after deducting a percentage of (5%) of compensation for the Kuwait war, or any percentage determined by the Security Council and paid to the United Nations and at the non-payment will be deducted amounts of the region's share of 17%.

Second: Ministries and non-associated departments to be committed to register all amounts of cash grants that obtained under agreements with governments or foreign institutions' revenues "ultimate" to the public treasury and the Federal Ministry of Finance re-allocated for the purposes given for it and in coordination with the Federal Ministry of Planning.

Third: All amounts of cash contributions received by the ministries and non-associated departments with the Ministry and governorates not organized into a region after its acceptance by the Cabinet if it is from foreign sources and from the Federal Minister of Finance whether the sources of national revenue "ultimate" for the treasury of the federal public, the Federal Minister of Finance to allocate of funds to the ministry or organization that is not related to the Ministry in accordance with the purposes for which given.

Fourth: Restrict all grants and contributions in-kind received by the ministries and non-associated departments with the Ministry and governorates after the approval of the Cabinet if it is from foreign sources and of the Federal Minister of Finance if it is from national sources in the records of the ministry or organization that is not related to the Ministry or province to take over the use and for the purposes which they were given.

Fifth: To obtain approval from the Federal Minister of Finance to accept grants or donations from governments and foreign institutions to the ministries and departments, non-associated with the Ministry in the form of technical assistance and preparation of

studies or designs and others that are under speculative costs in the records of the ministry or organization is not related to the Ministry or conservative relationship.

((Chapter II))

**Expenditure and Deficit**

Article 2 (First) - **Expenditure**:

The sum of 92980582970 dinars (ninety-two thousand nine hundred and eighty billion, five hundred and eighty-two million nine hundred and seventy thousand dinars) for the expenses of the financial year / 2011 distributed according to (Table / 3 of total expenditure) (Table / b expenditure by ministries) attached to this law.

A sum of 28957957804 dinars (Twenty-eight thousand nine hundred and fifty-seven billion, nine hundred and fifty-seven million and four thousand dinars)

Expenditures for investment projects distributed according to (Table / 2 expenditure of investment projects) of the (Table / b expenditure by ministries) attached to this law.

The amount of 64022625166 dinars (Four thousand and twenty-two billion, six hundred and twenty five million, one hundred and sixty-six thousand dinars) for current expenditures in the following manner:

Defense and security spending 13520645222 dinars (thirteen thousand five hundred and twenty billion, six hundred and forty-five million two hundred and twenty-two thousand dinars)

Compensation expenses and debt 6484152315 dinars (six thousand four hundred and eighty-four billion one hundred and fifty-two million and three hundred and fifteen thousand dinars)

A - Support the expenses of the social strata 12562258720 dinars (twelve thousand five hundred and sixty-two billion two hundred and fifty-eight million seven hundred and twenty thousand dinars)

B - Support the expenses of public companies and self-funded entities, 2485669374 dinars (two thousand four hundred and eighty-five billion six hundred and sixty-nine million three hundred and seventy-four thousand dinars)
Sector expenditure:

1 - Agricultural, 493 861 096 dinars (four hundred and ninety-three billion, eight hundred and Sixty-one million and ninety six thousand dinars).

2 - Industrial and Energy, 3642287836 dinars (three thousand, six hundred and forty-two billion two hundred and eighty seven million, eight hundred and thirty-six thousand dinars).

3 - Transport and Communications, 234 263 055 dinars (two hundred and thirty-four billion two hundred and sixty three million and fifty-five thousand dinars).
4 - Construction, housing and services, 2111323907 dinars (Two thousand one hundred and eleven billion, three hundred and twenty-three million nine hundred and seven thousand dinars).
5 - Education, 7879075180 dinars (seven thousand eight hundred and seventy-nine billion and seventy-five million one hundred and eighty thousand dinars).

Expenses of ministries and other public administrations.

14609088461 dinars (fourteen thousand, six hundred and nine billion and eighty-eight million four hundred and sixty-one thousand dinars).

According to details provided in accordance with (Table 1 / operating expenses) of the (Table / b expenditure by ministries) attached to this law.

C - The sum of 250000000 dinars (two hundred and fifty billion dinars) in the contingency reserve funds to offset other expenses and the Federal Ministry of Finance out of the customizations listed in paragraph (first b) expenditures referred to above.

D - Allocate an amount of 2657256000 dinars (two thousand six hundred and fifty-seven billion, two hundred and fifty-six thousand dinars (the reconstruction and development projects, regions and provinces, including Kurdistan) out of assignments referred to in paragraph (first a) above is distributed as follows:

A - According to the population of each province.

B - According to the level of deprivation when preparing the Federal Ministry of Planning and criteria for such and implemented as follows:

1- Introduces the conservative plan of reconstruction of the province, districts and areas affiliated ratified by the provincial council to the Ministry of Planning for the purpose of the study and validation that take into account the worst-hit areas "within the province".

2- Carries conservative implementation of the reconstruction plan approved by the Cabinet to maintain responsibility for overseeing implementation.

E - The sum of 1633788000 (one thousand six hundred and thirty-three billion seven hundred and eighty-eight million dinars) to province an equivalent to (1) a dollar for every barrel of crude oil producer in the province, and (1) dollars for every barrel of crude oil refined in refineries maintain and (1) a dollar for every (150) cubic meters of natural gas producer in the province is distributed according to the production of each province and that the accounting adjustments are made after being examined by the Office of Financial Supervision.

**Deficit**

A - The total planned deficit for the federal public budget for the financial year / 2011 14275345470 dinars (fourteen thousand two hundred and seventy-five billion three hundred and forty-five million four hundred and seventy thousand dinars) covers the shortfall of cash retained from the Federal budget for the year April 2010 and internal and external borrowing.

B - Authorizes the Federal Minister of Finance the power to continue to borrow from the International Monetary Fund which complements the sum of 4.5 billion dollars (four billion five hundred million dollars) and the World Bank, complementing the 2 billion dollars (two billion U.S. dollars) during the year / 2011, using Special Drawing Rights up to SDR, 1.8 billion dollars to cover the projected shortfall in the federal budget in addition to the domestic borrowing by the treasury transfers.

C - Finance the deficit of the loan amount of 500 million dollars (five hundred million dollars) granted to the Oil Ministry by the British Oil Company.

((Chapter III))

**General and Final Provisions**

Article 3 limits the exchange of key appropriations accounts (grants, subsidies, other expenses, and expenses of capital projects) approved in the general budget of the Federal Republic of Iraq by the competent minister or head of the entity is related to the Ministry and the provinces and provincial councils are not related to province, per allocations in the annual budget .

Article 4 of the Federal Minister of Finance the power to make transfers between appropriation budget of the Federal Republic of Iraq ratified in the general budget of the Federal annual and supplementary funds and the main accounts and sub has authorized

ministers and heads of departments not related to the Ministry, governors and heads of provincial councils is associated with the province the power to make transfers between appropriation the federal budget of the Republic of Iraq ratified in the federal budget the annual or supplementary rate not to exceed (10%) of the unit of exchange for the unification of other exchange that is reducing the allocations with the exception of appropriation of investment projects, taking into account the provisions of paragraph (8) of section (9) of the Financial Administration Act and General Debts (No. 95) for the year April 2004 to be done exclusively for transfers of allocations of the expenses of capital projects to operating expenses and allocations done exclusively of non-financial assets to the substance of salaries and operating expenses.

Article 5 of the Cabinet, amounts approved for use (contingency reserve), as set forth in item (I "c) of Article (2) of this Act for the payment of incidental expenses and unexpected after the depletion of the law, if there is an urgent need for domestic spending and the absence of the allocation to cover this need.

Article 6 (First): The usage of approved appropriations in this Act to 31 / December of the fiscal year / 2011 and an affiliate income earned up to 12/31/2011 and received revenue after the end of the fiscal year / 2011 "for the federal public budget for fiscal year 2012.

Article 7 is calculated by amount of grants and subsidies are not used funds allocated to government departments and public sector companies to end by the fiscal year / 2010 in accordance with Accounting Standards are used to calculate the final exchange and the amounts paid in excess along these lines as down payment at the expense of the grant allocated to the department or unit in the fiscal year / 2011.

Article 8 of the competent federal minister and heads of departments not related to the Ministry and the provincial governors and heads of the power exchange per approved allocations within the annual budget and authorize the heads of departments of his ministry or organization that is not related to the Ministry the partial or the full authority of disbursement, according to the following:

First: The disbursement to conducted according to the appropriation approved in the federal budget and the annual or supplementary purposes specified.
Second: The usage of funds allocated in the Federal Budget under the spending plan approved by the Federal Minister of Finance.

Third: Compliance with the appropriations allocated in the federal budget and can not be in effect into a commitment as intended in the federal budget:

First, Article 9: The ministries and government departments all Federal accounts monthly (model budget) at a date not to exceed duration (10 days) from the end of each month to the Federal Ministry of Finance and Accounting Service.
Second: It is not permitted to make any transfers within the allocations (reconstruction and development projects, regions and provinces) between the provinces.

Article 10 of the Federal Minister of Finance in coordination with the Minister of Planning Federal transfers approved allocations for investment projects contained in the federal budget for the year April 2011 have not been implemented, (25%) of the allocations for each project within six months from the adoption of the budget that do not affect the obligations of the executed contract, and conversion to other projects with the exception of projects that did not start the execution of the imperative reasons of security.

Article 11, First: "When an employee get re-assigned from the Department of State services that either centrally funded or self-funded to the private sector, the Federal Ministry of Finance is to bear half of his/her salary transferred to them to two years as the date of re-assignment in relationship to his final constituency.

Article 12: Authorizes the Minister of Municipalities and Public Works, the federal authority to make transfers between budget allocations by the self-financing municipal to maintain one entity to deliver the required services.

Article 13, First: Set quotas of governorates that not related to a district in proportion to population of the total expenditures shown in (Table / d expenditures ruling) attached to this law, after excluding the Kurdistan region's share of (17%).

Second: the share of the Kurdistan region (17%) of the total expenditures shown in (Table / d expenditures) attached to this law that are not taken to dispose of these shares for longer consultation and coordination between the concerned ministry in the federal government and the concerned ministry in the province of Kurdistan.

Third: The proportion (17%) Seventeen percent of the total operating expenses and expenses of the investment projects of the general budget of the Federal Republic of Iraq ratified the Kurdistan region after excluding expenses of the sovereign (the House of Representatives, the Presidency, the Council of Ministers, Ministry of Foreign Affairs, the Ministry of Defence), and legal claims for debts, costs to be audited and followed-up and the pursuit of money overseas, costs for auditing firm (Ernest & Young) and the Committee of Financial Experts, contribute to the cost of producing crude oil source, including contracts for foreign companies executing the Kurdistan Region, the benefits of foreign loans, interests, money orders in the public treasury, and benefits to write-off the external debt of the private sector, the amounts of contributions of Arab and international levels, amounts of compensation the Kuwait war, the operational expenses of travel and the Nationality Directorate and the leadership of the border forces, debt settlement abroad, the benefits of the restructuring of foreign debt under the Paris Club countries and countries outside the Paris Club, and the fees of the transfer of crude oil exported via Turkey, premiums bilateral agreements with Paris Club countries and countries outside the Paris Club and the investment projects of foreign oil companies).

Fourth: Once an increase or decrease occurred in the total expenses of the federal budget, added or reduced in the share of the Kurdistan region proportionally with the increase and decrease in the budget of the Kurdistan region, taking into account the provisions of item (II) of this article amendments to the sovereign

expenditure from the transfer of sovereign expenditure to public expenditure, the same proportion mentioned above.

Fifth: The Prime Minister agreed with the Federal President of the Kurdistan region on expenses (salaries, armament, and equipment) for the Regional Guard forces in line with the Constitution and to agree to cover pending advanced payments and the issuance of a law that regulates benefits and pay.

Article 14, First:

A - The Office of Federal Financial Supervision to coordinate and cooperate with the Office of Region Financial Regulatory to calculate and determine the Federal income obtained in the region this year and the Ministry of Finance in the region by referring to the Federal Ministry of Finance every month.

B - The settlement of dues between the Kurdistan region and the federal government for the years (2004 to 2010) and subsequent years to be audited by the Office of Financial Supervision Federal to coordinate and cooperate with the Office of Financial Supervision of the Kurdistan region.

Second: Unpaid federal income withdrawn to the Public Treasury and the Federal Ministry of Finance to deduct the federal quota under paragraph (a) of item (I) of this article, revenues planned in the federal budget and settlement calculations are to be conducted later.

Third: The Ministry of Finance to deduct the federal amounts of damage caused by the region or province as a result of not allowing the use of airspace of the Republic of Iraq for the benefit of mobile phone companies approved by the Federal Government share of the region or province and funding, specifically from revenue derived from licenses and fees for mobile phone.

Fourth: The Federal Oil Ministry to identify the damage caused by any act on the result of crude oil extracted for the purpose of export and domestic consumption.

Article 15: Re-examined the share of the Kurdistan region and governorates of provinces in the federal budget for the year April 2011 and onwards in the light of the results of the census and the census for the year April 2010 and that is in the determination of the amount to the real share of the region or province is regular province in the federal budget for the year / 2011 and display the difference on the Federal Cabinet for settlement.

Article 16, First: All revenue departments centrally funded "ultimate revenue" to the public treasury of the State and Federal is stated in the balance of the audit.
Second: Notwithstanding the provisions of paragraph (First), Federal Minister of Finance of sums add monthly revenue generated by departments and the Federal Ministry of Health budget to the Ministry.

Article 17: The transition at all income Communications and Media Authority to the Federal Treasury Account of the State and the Ministry of Finance.

Article 18: The federal ministries and non-associated with the Ministry to be committed to (Table / c) on the number of manpower for the ministries and departments centrally funded for the year / 2011 attached to this law and the Federal Minister of Finance the authority of the development of grades and adjusting staffing resulting from the introduction of grades to re-separated politicians and the integration of the militias and transport companies of public sector or self-funded departments to centrally funded and the development of scores of new formations.

Article 19: Taking into account the equitable distribution of loans provided to the Federal Government to the regions and governorates of Iraq and in proportion to its population, after taking into account the strategic projects funded by these loans exclusively.

Article 20, First: The ministries and departments not associated with the Ministry prior coordination with the provincial councils and the selection of projects.

Second: The Federal Ministry mandated to maintain the implementation of investment projects allocated in the budget belonging to that province.

Third: To maintain the mandate of any of the ministries or by the Federal jurisdiction for the implementation of investment projects in that province at the expense of allocations (reconstruction and development of the regions and provinces) allocated to them.

Article 21: The three presidencies (Presidency of the Council of Representatives and the Presidency of the Republic and the Presidency of the Cabinet) controls for the disbursement of social benefits in coordination with the Federal Ministry of Finance and the Office of Financial Supervision Federal and that being the exchange in accordance with the provisions of Article (29) of the Code of Federal budget for the financial year / 2008 (20) for the year April 2008 to when to issue such regulations and approved by the Cabinet.

Article 22, First: Federal Minister of Finance ensure financial allocations for employees in companies and self-funded public entities to develop grades as a result of the transfer of services to the staffing services that centrally funded in accordance with Article (18) of this law to cover the needs of staff.

Second: The federal ministries to stop appointments within the staffing profiles of its public corporations and self-funded entities which receive a grant from the Treasury, Federal Public of the State or loans from government banks to delete the grades within staffing agencies throughout the search when it became vacant due to transport or referral to retirement, resignation or death.

Article 23, First: The deduction of the proportion (20%) twenty percent of the salaries of the Spokesperson and his deputies and

the President of the Republic and his deputies and the Prime Minister and his deputies.

Second: The deduction of the proportion (10%) ten percent of the salaries (Chairman of the Supreme Council of Justice and his deputies and members of the House of Representatives, and receive a salary of the Secretary and who are the rank of Deputy Minister and advisers and those with special grades and general managers and workers in the House of Representatives and the Presidency and the Cabinet (Prime Minister / Cabinet Secretariat / National Security Council / Office of the Adjutant General of the Armed Forces / Iraqi National Intelligence Service / National Authority for Investment).

Article 24, First: The ministries and government departments all Federal accounts monthly to refer to the Federal Ministry of Finance and Accounting Service at a date not to exceed duration (10 days) from the end of each month.

Second: It is not permitted to make any transfers within the allocations (reconstruction and development projects, regions and provinces) between the provinces.

Article 25, First: The Federal Minister of Finance to re-allocate of the approved amounts in the federal budget for the year April 2010 for the purposes of investment projects of the ministries and departments not associated with the Ministry and development projects and accelerate the reconstruction of the provinces, Marshes revival projects and projects of Petro-Dollars and non-disbursed to the allocations of the beneficiary exclusively for disbursement during the year / 2011 to the completion of projects investment exception from the provisions of (Section IV - P / 1) of the Financial Administration Act and the public debt, number / 95 for the year 2004.

Second: The Federal Minister of Finance allocations on the quantities of (1) a dollar for every barrel of crude oil producer in the province, or (1) dollars for every barrel of crude oil refined in the refineries to maintain and (1) a dollar for every (150) cubic meters

a product of natural gas in the province for conservation benefits for the year / 2010, which was not included in the above-mentioned year's budget due to delays sending new projects by the province concerned to the Ministry of Planning as the rights acquired.

Article 26: The Cabinet's law that regulates the number of staff and salaries of employees of the House of Representatives and the Presidency of the Republic and the prime minister.

Article 27: The prevention of private aircraft rental to be absolutely at the expense of the state of all contacts with the exception of the three presidencies (Presidency of the Council of Representatives and the Presidency of the Republic and the Presidency of the Cabinet).

Article 28: Not to exceed the monetary rewards or in-kind granted to staff, a million dinars a year, per person to meet the service rendered to the ministry or organizations that not related to the Ministry and within the approved budget allocations and competent in accordance with instructions issued by the Federal Ministry of Finance.

Article 29: To be referred to the head of the spending unit to investigate according to legal rules and regulations in force in cases of failure to submit the final bills for the year April 2010 to the constituency after exceeding the date specified in the law of financial management and public debt (No. 95) for the year April 2004.

Article 30, First: Decisions that contrary to the law are not to be considered and the federal treasury to tolerate any financial burdens of this decision unless they acquire the legitimacy of legal and approved by the House of Representatives.

Second: The provision of financial bills by the Cabinet to the House of Representatives, are not implemented retroactively.

Article 31: Companies of public sector are committed to take into account the provisions of section (8) of the Financial Administration Act and the public debt (No. 95) for the year / 2004.

Article 32: Obliges the ministries of electricity and telecommunications, municipalities, and public works and Baghdad Municipality and the municipalities in the provinces to activate the collection of wages, electricity and telephone, water and sewage from citizens and business owners, factories, government agencies and the public sector and others for the purpose of increasing their own resources and reduce dependence on the federal budget.

Article 33: All federal ministries and departments not associated with the Ministry and the provinces to buy from the public sector the need equipment and materials manufactured in the public sector taking into account the competition in price and quality as well as dealing with the Ministry of Transport and the national carrier.

Article 34: Public companies that self-funded by the federal budget, and the possibility of the companies mentioned, borrowing from government banks in accordance with the Companies Act No. 22 of 1997, after submission of feasibility studies with the exception of the directorates of the Ministry of the Federal Electricity companies and Federal Ministry of Agriculture and military manufacturing companies that was attached to the Ministries of Defence and industry and the General Company for Railways of the Iraqi Ministry of Transport.

Article 35: The indeterminacy in any leadership positions (general manager and above) unless there is a degree in law or the ministry of the organizational structure according to the law ministry or organization.

Article 36: The concerned minister or the President responsible on the assignment of related Ministries' staff redundant who have a service pension of not less than 15 years nor less than the age of fifty years to retirement.

Article 37: Obliges ministries and departments not associated with the Ministry and all other official entities not afford to send their members to attend conferences, seminars, workshops and meetings in accordance with instructions issued by the Cabinet at the

suggestion of the Ministry of Finance and the Secretariat of the Cabinet.

Article 38, First: Duties of all goods and imported goods by government departments and for the benefit of the public sector are exempted.

Second: The above exemption of goods and imported goods to government departments and public sector institutions, governments or donors.

Article 39: The Iraqi Central Bank to provide loan of 5 billion (five billion U.S. dollars) to support programs and projects of the federal budget for the year / 2011 in accordance with the terms and schedule determined by the Bank mentioned in coordination with the Cabinet for the purpose of payment and that the Cabinet to add the equivalent of the projects and programs within the federal budget for the year / 2011.

Article 40: Ministers and heads of departments not related to the Ministry, governors and heads of local councils, municipalities and concerned to implement this law

Article 41: The Federal Minister of Finance to issue the necessary instructions to facilitate the implementation of the provisions of this law.

Article 42: This law shall be published in the Official magazine and implemented with effect by January 1 / 2011.

President of the Republic

# COALITION PROVISIONAL AUTHORITY ORDER NUMBER 87

# PUBLIC CONTRACTS

*Pursuant* to my authority as Administrator of the Coalition Provisional Authority (CPA), and under the laws and usages of war, and consistent with relevant U.N. Security Council resolutions, including Resolutions 1483 and 1511 (2003),

*Recognizing* that public contracts laws should conform to international standards of transparency, predictability, fairness of treatment; provide for dispute resolution mechanisms; be free from corruption and undue influence; and create a system to procure goods and services at the best possible value for the government,

*Noting* that the concept of full, fair and open competition is of critical importance to the economy of Iraq and the goal of free trade among nations,

*Building on* the existing Iraqi laws in the field, including administrative instructions, and modernizing them in accordance with best international practice,

I hereby promulgate the following:

## Section 1
## Principles of Government Public Procurement

1) This Order applies to all procurements of goods, services, and construction services by the State of Iraq acting through Ministries or other federal agencies (collectively "agencies"); or governmental units including Regions; Governorates; and all other subdivisions of the State of Iraq (collectively "governmental units") that may commit public funds. Procurement is the acquiring by contract with public funds of goods, services or construction services by and for the use of the government through purchase or lease. The State of Iraq through Ministries or other federal agencies; Regions; Governorates; and all other subdivisions of the State of Iraq shall commit public funds in accordance with the following basic principles:

    a) To the maximum extent practicable, full, fair and open competitive public bidding procedures, including, but not limited to: effective tender publication; objective bid evaluation criteria; public bid opening; and, the use of electronic commerce methods.

    b) International standards of transparency, predictability, fairness and equality of treatment;

c) Procurement process integrity, minimum ethical standards and non-conflict of interest;

d) Offeror's right to file tender protests and related appeals;

e) Tender dispute resolution mechanisms and the timely resolution of such disputes.

## Section 2
## Office of Government Public Contract Policy

1) Establishment and Responsibilities

a) There shall be established, within the Ministry of Planning and Development Cooperation, an Office of Government Public Contract Policy. The head of this Office shall report directly to the Minister of Planning.

b) The Office of Government Public Contract Policy shall have responsibility for:

i) Coordination of government public contract policy for all ministries and public entities of the government, including, but not limited to, the issuance, after appropriate provision for notice to and comment by interested parties, of implementing regulations and administrative instructions in the Arabic and Kurdish languages, and such other languages as appropriate, in furtherance of this Order;

ii) Establishment and adoption of rules for an independent Administrative Tribunal to have jurisdiction over complaints and disputes arising under or relating to the award of public contracts by the government;

iii) Recommendations for amendments to this Order and related Iraqi laws, regulations and administrative instructions;

iv) Development and adoption of standard government public contract provisions; and

v) Training of government public contracting personnel for the proper application of this Order and its implementing regulations and administrative instructions.

2) Application

a) Every governmental unit or agency described in Section 1.1 "government" shall designate a contracting office that shall be responsible for the contracting activities of the governmental unit or agency. For reasons of administrative convenience, a

governmental unit or agency may agree with another governmental unit or agency that the latter will be responsible for the contracting activities of the former.

b) In addition to the standard contract provisions adopted for all governmental units or agencies, each individual governmental unit or agency, after concurrence by the Office of Government Public Contract Policy, may include standard contract provisions that are necessary for the particular objectives of said governmental unit or agency.

c) This Order applies to Iraqi state-owned enterprises when awarding public contracts for the procurement of goods, services or construction services that are directly financed by government funds.

## Section 3
## Contracting Authority

1) The authority to obligate government funds, award and sign government public contracts, enter into and authorize material modifications to such contracts, and authorize the payment of invoices and claims, shall rest solely with a qualified government agency or a committee within each governmental unit or agency, duly appointed under the authority of this Order.

   a) Agency and committee members shall not be political appointees or members of the office within the governmental unit or agency that requires or benefits from the contractor's performance under the contract to be awarded. Political appointees are Governing Council members and their deputies; ministers and deputy ministers; governors; judges; members of national commissions, deputy commissioners of such commissions, directors and equivalent officials within Iraqi commissions, boards or similar organizations; all elected members of the Iraqi Interim Government or Iraqi Transitional Government, including the national executive; and those individuals appointed by the public officials listed in this Section to advise them.

   b) The individuals vested with the authority described in this Section shall not directly report to the official or office requiring or benefiting from the contractor's performance under the contract.

2) In all public contracts, there shall be a standard provision advising contractors of the public agency or committee that shall have this authority and the full scope of that authority. Included in that provision, there shall be reference to the fact that direction from the government to the contractor that affects the rights and liabilities of the parties to the contract from anyone other than the designated responsible public official shall not be authorized and shall not have any effect.

## Section 4
## Full and Open Competition

To the maximum extent practicable, government public contracts shall be awarded on a competitive basis. Prior to the competitive award of public contracts, the Contracting Authority, vested with the authority pursuant to Section 3 of this Order, shall state in writing the awarded contract price to be fair and reasonable under the prevailing facts and circumstances.

1) Exceptions – Public contracts may be awarded using other than full and open competitive public contracting procedures under the following conditions:

   a) When, for technical or artistic reasons, or for reasons connected with the protection of exclusive rights, the goods or services to be purchased under the contract may only be manufactured or supplied by a particular entity or otherwise is available from a very limited number of entities.

   b) When for reasons of extreme urgency brought about by events not attributable to the Contracting Authority, the public interest does not permit award on a fully competitive basis.

   c) When the goods to be purchased are:

      i) Required as a partial replacement for or addition to goods purchased under an existing or previous contract; or

      ii) Required to be compatible or interchangeable with existing goods purchased from the original source who supplied the existing goods.

   d) When the use of other than full and open competitive public contracting procedures is necessary to promote economic or institutional development among certain population sectors or geographic regions of the State of Iraq or of Iraqi state-owned enterprises. These regulations shall also indicate the circumstances where the use of other than full and open competitive public contracting procedures may be used to promote economic or institutional development among certain population sectors or geographic regions of the State of Iraq or of Iraqi state-owned enterprises.

   e) When international agreements (bilateral, plurilateral, or multilateral) or treaties to which the State of Iraq is a party require the use of other than full and open competitive public contracting procedures, either by their explicit terms or by implication.

f) If the anticipated value of the public contract is below certain monetary thresholds, as determined by regulations issued in accordance with Section 2, a streamlined procedure for the procurement of lower priced goods and services shall be used.

g) The Office of Government Public Contract Policy shall issue implementing regulations indicating, among other matters, those circumstances permitting other than full and open competition and specifying the streamlined procedures for awarding public contracts using other than full and open competitive public contracting procedures. These regulations shall require documentation previous to every occasion where other than full and open competitive public contracting procedures are used.

2) Prequalification - Prequalification of offerors, including required deposits or bonds, shall be implemented in such a manner that does not unreasonably limit competition. If a deposit is required as a condition for participating in a competitive tender, such deposit shall be reasonable in amount, based upon the value of the contract, and returned to an unsuccessful offeror. The use of bonds, as opposed to deposits, is encouraged.

3) Notice of Tenders - The Office of Government Public Contract Policy shall issue implementing regulations that address, but are not limited to, the following:

a) The notice of tenders shall provide the maximum possible exposure of the proposed public procurement action. Notices shall be published at a minimum in the Arabic and Kurdish languages, as well as such other language as may be appropriate where it is anticipated that offers will be made from entities or individuals outside the State of Iraq.

b) The notice shall provide potential offerors with sufficient information, including but not limited to, standard terms and conditions, the statement of work and a delivery schedule, to reasonably respond to the tender. In this regard, all tenders shall also contain the factors upon which offerors shall be evaluated, and the failure of the government to evaluate an offer against the stated evaluation factors in the notice shall be a basis for filing a tender protest pursuant to this Order.

c) The notice shall provide potential offerors with sufficient time to reasonably respond.

d) The notice shall provide potential offerors the opportunity to request clarifications about the tender and for extensions of time to respond to the tender, if necessary.

e) The notice shall provide a date by which responses to tenders shall be due, and provide those specific instances where late offers can be accepted.

f) The implementing regulations to this Order shall provide for exceptional circumstances when the notice is not required.

## Section 5
## Negotiated Contracts

1) Authorization - Although competitive bidding is preferred in general, competitive negotiated contracts that comply with this Order are hereby specifically authorized and should be employed whenever the interests of the governmental unit or agency concerned will best be served by awarding the contract on a basis other than the lowest price.

2) Process

   a) Tender notices for negotiated contracts shall specifically indicate that the contract shall be awarded on a basis other than the lowest price.

   b) The notice shall state those factors, in addition to price, that will be evaluated and the relative importance of each of these factors (this is not an exhaustive list, and all of these factors, except price or cost, may not necessarily be required on all procurements):

      i) The merit of the technical solution proposed to meet the government's requirements;

      ii) The risk associated with the offeror's proposed approach as it relates to accomplishing the requirements of the tender;

      iii) Past performance on recent and relevant government and commercial efforts;

      iv) Experience of key personnel; and/or

      v) Management structure.

   c) The notice shall state the relationship between the price and the non-price factors in making an award (e.g., are the non-price factors more important, less important, or of equal importance to price).

   d) The government shall have the right to enter into direct negotiations with offerors after their written response to the tender has been received by the government.

The purpose of entering into direct negotiations is to clarify offers, respond to questions, and negotiate price. At no time during the negotiation process (and after award) shall information, including price, about proposals from other offerors be discussed or made public. The price of the awarded contract shall be made public.

e) If requested, offerors shall have the right to amend their offers after negotiations and prior to final evaluations.

f) All members of procurement evaluation teams shall be bound by the principles stated in Section 8 of this Order on "Procurement Integrity and Conflicts of Interest".

## Section 6
## Standard Public Contract Provisions

1) The Office of Government Public Contract Policy shall issue and publish implementing regulations that include standard public contract provisions. These provisions may include additional conditions not specifically required by, but otherwise consistent with this Order. These regulations may provide that certain conditions apply or do not apply depending on the value or type of the public contract.

2) The Office shall, in preparing the implementing regulations required by this Order, be guided by recognized and accepted international standards and best practices, such as those contained in the United Nations Commission on International Trade Law (UNCITRAL), "Model Law for Procurement of Goods, Construction, and Services", Directives of the European Union, and the World Trade Organization Agreement on Government Procurement. Where appropriate, these regulations shall also apply generally accepted international commercial practices.

## Section 7
## Statements of Work, Contract Specifications, and Contract Types

1) Statements of Work and contract specifications must accurately reflect the government's needs and must be written in such a way that they do not unduly restrict competition.

2) Proprietary features or brand names shall be avoided. If a brand name or proprietary feature is included in a specification, offerors must be notified of the features of the brand name and be advised that they may offer an equivalent or equal product.

3) The contract type has a direct effect on risk allocation in public contracts. Fixed-priced contracts are generally preferred over cost contracts, especially where a

reasonable price estimate can be made by the government and the contract anticipates a specific deliverable.

a) A fixed-price contract provides for a price that is not subject to adjustment on the basis of the contractor's costs incurred in performing the contract. A fixed-price contract places upon the contractor maximum risk and full responsibility for all costs and resulting profit or loss.

b) A Cost-reimbursement contract provides for payment of allowable incurred costs, to the extent prescribed in the contract. These contracts establish an estimate of total cost for the purpose of committing funds and establishing a ceiling that the contractor may not exceed (except at its own risk) without the approval of the contracting officer.

## Section 8
## Procurement Integrity and Conflicts of Interest

1) The Office of Government Public Contract Policy shall issue and publish implementing regulations that implement, at a minimum, the following ethical standards:

2) No minister, official or consultant under contract to support the governmental unit or agency involved in any tender shall have a financial interest in the outcome of the tender.

   a) All proprietary or competition sensitive information received by ministers, officials, or contractors during the tender process shall remain confidential.

   b) The post-government employment of ministers and officials substantially involved in the government procurement process shall be restricted for a reasonable period of time in accordance with this Section. Those ministers and officials substantially involved in the following activities shall not seek nor accept employment with the offeror awarded the contract:

      i) A particular tender;

      ii) The administration of the contract awarded subsequent to a particular tender; or

      iii) The surveillance of the work performed under a particular contract.

   c) No offeror shall have a business interest that is in conflict with its ability to use its best efforts to satisfy the requirements of the contract.

## Section 9
## Exclusions from Participation

1) To ensure the integrity of the procurement process, entities and individuals may be excluded from competing for government public contracts in accordance with the following provisions.

   a) As defined in the implementing regulations issued under the authority of this Order, misconduct, including but not limited to the following, shall be the basis for exclusion:

      i) Willful violations of this Order or the implementing regulations issued under the authority of this Order;

      ii) Willful failure to perform in accordance with one or more material terms of a public contract;

      iii) Conviction of a criminal offense; or

      iv) Other misconduct indicating a lack of business integrity or business honesty that seriously and directly affects the ability of the contractor to perform.

   b) Responsibilities for ensuring the integrity of the procurement process shall be carried out by the Office of Government Public Contract Policy which shall issue implementing regulations that shall, at a minimum:

      i) Provide standards for exclusion;

      ii) Provide a fair, equitable and expeditious process with an opportunity to be heard before a determination for exclusion is made;

      iii) Provide a method by which an excluded entity may apply for re-instatement; and

      iv) Provide that a public record be maintained and published of all excluded individuals and entities.

## Section 10
## Financial Requirements

1) No tender notice shall be published, nor any tender commenced, prior to a certification by the senior financial officer, or his official designee, of the

governmental unit or agency offering the tender that there are funds available sufficient to satisfy the government's estimated cost of any resulting contract.

2) No contract shall be awarded without a certification that sufficient funds are available and dedicated (i.e., may not be used for any other purpose) to the contract in an amount equal to the full contract price.

3) Regulations shall be issued and published providing for the right of any governmental unit or agency awarding a public contract to have access to and have the authority to audit a contractor's financial records related to the public contract that was awarded. This right to audit, together with any additional oversight responsibilities, shall be exercised by an office that is not responsible for tender issuance. The Office of Government Public Contract Policy may establish a central agency for public procurement audit services.

## Section 11
## Termination for the Convenience of the Government

1) The right of the government, acting through the Contracting Authority vested with the authority described in Section 3 of this Order, to terminate public contracts entered into under the authority of this Order, in whole or in part, when it is in the government's best interest, may be included in contracts awarded by the government.

2) If a contract is terminated for the convenience of the government, the rights, duties, and obligations of the parties, including compensation to the contractor, shall be in accordance with the procedures set forth in Section 12 of this Order on "Dispute Resolution".

3) The Office of Government Public Contract Policy shall issue implementing regulations describing the circumstances under which the government can terminate public contracts pursuant to the authority of this Order.

## Section 12
## Dispute Resolution

All interested parties, as defined below, to a government public contract tender process and those entities and individuals that have been awarded government public contracts have certain rights against the government that may include the ability to seek and obtain monetary relief against the government.

1) Tender Protests

a) Right to File - Any offeror deemed to be an interested party, that believes it has not received fair treatment in the award of a government public contract, or believes that the provisions of a tender unfairly restrict full and open competition in a manner that inappropriately excludes it from competing, may file a tender protest with the Administrative Tribunal established pursuant to the authority of this Order.

   i) An interested party is an actual or prospective bidder or offeror that has a reasonable chance for award and whose direct economic interest would be affected by the award of a public contract or by the failure to award such a contract.

   ii) The Tribunal shall rule on the protest within the shortest period of time practicable and may, among other reasonable remedies, direct the contracting authority to take corrective action, including but not limited to, terminating the awarded contract, resoliciting tenders, reevaluating tenders received for consideration, award reasonable tender preparation costs, or take other actions necessary to comply with this Order and the implementing regulations promulgated under the authority of this Order.

b) Results of Filing - Upon the filing of a tender protest after award, the governmental unit or agency that awarded the public contract shall immediately order the awarded contractor to cease working on the contract.

   i) If a minister or the senior official responsible for contracting within governmental unit or agency awarding the contract determines the requirement being satisfied by the contract is of such importance to the public interest that ceasing work will unduly harm the public interest, such minister or official may, by written determination of such undue harm, and after notice to the Tribunal, order the governmental unit or agency to notify the contractor to proceed with the contract.

   ii) The minister or official, in making this determination, shall also consider the likelihood of success of the protest.

c) Effect of Grant of Protest - If the Tribunal sustains the tender protest and either directs the contracting authority to award the contract to the protestor or directs the contracting agency to take corrective action consistent with this Order or the regulations promulgated under the authority of this Order, the governmental unit or agency shall immediately terminate the contract with the originally awarded contractor, if that contractor is not selected for award following the corrective action ordered by the Tribunal. Such contractor may have certain rights against the government as discussed in Subsection 2 below.

d) Additional Rights of Unsuccessful Offerors - There shall be notices published of all public contract awards. All unsuccessful offerors in a government public contract competition shall be notified by the authority offering the tender, and such unsuccessful offerors shall be entitled to receive a written explanation of the factors upon which it was not successful. Such explanations shall be provided promptly and with full consideration to the proprietary nature of the information provided to the government by the other offerors, including the awardee, of the tender. Decisions of the Tribunal may be appealed by either party to the appropriate Court with jurisdiction over the procurement.

e) Implementing Regulations - The Office of Government Public Contract Policy shall issue implementing regulations published in conjunction with this provision that address, but are not limited to, the following:

i) The establishment of the independent Administrative Tribunal referred to in Section 2.1(b)(ii) of this Order;

ii) The rules of the Tribunal, including time and place requirements for filing protests, both before and after public contract award (including the effect on such time requirements if a request for explanation is made), and for issuing decisions;

iii) The time requirements for an unsuccessful offeror to request an explanation of the governmental unit or agency decision and for the governmental unit or agency to respond to that request;

iv) The nature of the relief that may be granted by the Tribunal; and

v) The legal bases upon which a tender protest may be filed.

2) <u>Claims</u>

a) Right to File - A contractor has a right to make a claim to the authority awarding the public contract that a condition of the contract has not been followed or that it has otherwise been treated in an unfair way. This right to make a claim shall also apply to a contractor whose contract has been terminated as a result of a decision by the Tribunal hearing a tender protest to terminate its contract where it believes it is entitled to additional compensation for work under its terminated contract, but not yet paid.

b) Process - A contractor seeking to exercise its rights under this Subsection must first seek a final written decision on the merits of its claim from the governmental

unit or agency that awarded the contract by submitting a written request to the contracting authority for that governmental unit or agency. This request shall specify that amount that the contractor believes it is owed and the basis for the request. This final decision must be prepared by the contracting authority and it must be issued within a reasonable period of time. If after a reasonable period of time, the contractor does not receive a final written decision from the appropriate authority, the contractor may deem this lack of a response as a denial of its claim.

c) Appeal - If the contractor is dissatisfied with the final written decision of the governmental unit or agency, it shall have the right to file an appeal with the court having jurisdiction over disputes between the government and private parties (or such other Court granted jurisdiction to hear such cases), which shall render its decision within a reasonable period of time.

d) Regulations - The Office of Government Public Contract Policy shall issue regulations in coordination with the Ministry of Justice implementing the claims process described in this subsection. The regulations shall include the following subjects and may include other subjects:

   i) The office within the governmental unit or agency where claims may be filed;

   ii) The time for filing claims with the governmental unit or agency and for its decision;

   iii) The time for filing appeals and for decisions on such appeals;

   iv) The scope of review, including but not limited to, whether to completely review all of the facts and circumstances of the claim or to review a narrow point of law, or whether a rational basis exists to support the contracting authority's decision;

   v) The responsibility of the contractor to continue prosecuting the work under the contract while a claim or appeal is pending;

   vi) The legal bases upon which claims may be filed including, but not limited to, claims concerning contract modifications and terminations; and

   vii) Such additional rules and procedures consistent with the responsibilities and jurisdiction granted by this Order.

e) The State of Iraq, acting through the Contracting Authority vested with the authority described in Section 3 of this Order, shall be able to make a claim in a court of proper jurisdiction against the contractor to enforce the government's

rights under the contract. The State of Iraq shall be represented in the court of proper jurisdiction by a representative designated by the Ministry of Justice.

f) Alternative Dispute Resolution - In resolving all such disputes (i.e., whether they are tender protests or claims during administration of a public contract), principles of alternative dispute resolution shall be used to the maximum extent possible, so long as both parties agree.

## Section 13
## Effect on Present Iraqi Law

1) Tenders instructions (Outfitting and Buying) for State Agencies and the Social Sector, issued by the Legal Department/Planning Organization/Council of Ministers/Republic of Iraq, 2001 (Tender Instructions) are hereby suspended.

2) Instructions for Implementation and Follow up of Projects and Works of National Development Plan. Issued by the Legal Department/Ministry of Planning/Republic of Iraq, 1988 (Implementation Instructions) are hereby suspended.

3) Any provision of Iraqi law, including but not limited to, statutes, decrees, regulations, and instructions, that is inconsistent with this Order is hereby suspended to the extent of such inconsistency.

## Section 14
## Implementation

1) The Minister of Planning, through the Office of Government Public Contract Policy shall issue Administrative Instructions and regulations to implement this Order.

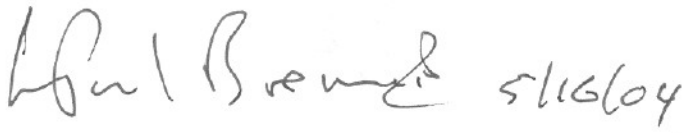
2) Until such time as regulations are promulgated by the Ministry of Planning and Development Cooperation under the authority of this Order, Coalition Provisional Authority Memorandum Number Four and its appendices, dated 19 August 2003 (CPA/MEM/19 August 2003/04) ("Memorandum Four"), shall serve as the implementing regulation for this Order.

3) In the event of an inconsistency between Memorandum Four and this Order, Memorandum Four shall be interpreted in a manner that is consistent with this Order.

4) Except as otherwise specifically provided by Coalition Provisional Authority Order Number 71, Local Governmental Powers, dated 6 April 2004 (CPA/ORD/6 April 2004/71), or other law or regulation, including other Coalition Provisional Authority orders, this Order shall apply to the federal and regional governments, Governorates, and municipal and local governments.

**Section 15**
**Entry into Force**

This Order shall enter into force upon signature.



L. Paul Bremer, Administrator
Coalition Provisional Authority

# COALITION PROVISIONAL AUTHORITY ORDER NUMBER 95

## FINANCIAL MANAGEMENT LAW AND PUBLIC DEBT LAW

*Pursuant* to my authority as Administrator of the Coalition Provisional Authority (CPA) and under the laws and usages of war, and consistent with relevant U.N. Security Council resolutions, including Resolutions 1483 and 1511(2003),

*Having* worked closely with the Governing Council to ensure that economic change occurs in a manner acceptable to the people of Iraq,

*Acknowledging* the Governing Council's desire to bring about significant change to the Iraqi economic system,

*Determined* to improve the conditions of life, and opportunities for all Iraqis and to fight unemployment with its associated deleterious effect on public security through stable financial markets,

*Recognizing* that Iraq needs laws concerning the issuance and payment of public debt to assist in financing the Government and to promote confidence in the country's economic system,

*Further recognizing* the CPA's obligation to provide for the effective administration of Iraq,

*Recalling* that U.N. Security Council Resolution 1483 (2003) called upon the CPA to promote economic reconstruction and the conditions for sustainable development,

*Acting* in a manner consistent with the Report of the Secretary General to the Security Council of July 17, 2003, concerning the need for the development of Iraq and the need to enact institutional and legal reforms to give it effect,

I hereby promulgate the following:

### Section 1
### Purpose

1) This Order promulgates the Financial Management Law, which establishes a comprehensive framework for the conduct of fiscal and budgetary policy in line with international best practices, by setting a structured process for

the formulation of the federal budget and a number of reporting requirements aimed at increasing the accountability and transparency of the budgeting process.

2) This Order promulgates the Public Debt Law, which authorizes the Ministry of Finance to issue and pay debt securities guaranteed by the Government, and establishes certain related authorities and duties, for the purposes of financing Government operations and promoting a stable Iraqi economy.

## Section 2
## Financial Management Law

The Financial Management Law attached to this Order as Annex A shall have the full force and effect of law.

## Section 3
## Public Debt Law

The Public Debt Law attached to this Order as Annex B shall have the full force and effect of law.

## Section 4
## General Provisions

1) Prior to the transfer of governance authority to the Iraqi Interim Government in accordance with Article (2)(B)(1) of the Law of the Administration for the State of Iraq for the Transitional Period, the powers and responsibilities assigned to the Prime Minister and Council of Ministers by the Financial Management Law and the Public Debt Law shall be exercised by the Administrator.

2) Until such time as the Iraqi Interim Government assumes full governance authority in accordance with Article (2)(B)(1) of the Law of the Administration for the State of Iraq for the Transitional Period, the Ministry of Finance is prohibited from issuing new debt securities if the issuance of such securities would increase the total level of Iraq's public debt, including obligations to the Central Bank, beyond the current level of such debt**.**

3) Notwithstanding any provision of the Financial Management Law to the contrary, spending units shall submit requests for allocation of funds for the budget for fiscal year 2005 to the Ministry of Finance not later than 15 June 2004.

**Section 5**
**Inconsistent Legislation**

Any provision of Iraqi law that was enacted prior to the effective date of this Order, Annex A, or Annex B is hereby suspended to the extent of such inconsistency.

**Section 6**
**Entry into Force**

This Order shall enter into force on the date of signature

L. Paul Bremer, Administrator
Coalition Provisional Authority

ANNEX A

# IRAQ

# FINANCIAL MANAGEMENT LAW OF 2004

## Section 1
## Purpose

This Law shall regulate the arrangements governing the preparation, adoption, recording, management, execution, and reporting of the federal budget of Iraq and related issues including public borrowing and guarantees, internal control, accounting, and auditing. The principles of transparency, comprehensiveness, and unity shall be of fundamental importance in the preparation and execution of the federal budget of Iraq, and in related issues.

*The principle of transparency* requires that budget information be classified according to accepted international standards and presented in a way that facilitates policy analysis and promotes accountability.

*The principle of comprehensiveness* requires that the budget cover all government agencies and institutions undertaking government operations, so that the budget presents a consolidated and complete view of these operations and is voted on, as a whole, by the body vested with national legislative authority.

The principle of *unity* requires that all government resources be directed to a common pool to be allocated and used for public expenditure according to the priorities of the government.

## Section 2
## Definitions for the Purposes of this Law

1) "*Budget appropriation*" is the legal authorization given to the government to spend public money over the fiscal year for specified purposes.

2) "*Authorized person*" is a person delegated authority in writing by the Minister of Finance to manage public money.

3) "*Borrowings*" are funds received in return for a legally binding agreement to repay.

4) "*Budget*" is a financial program based on annual estimates of government cash receipts and payments, transfers, and transactions in kind.

5) "*Budget executor*" is an authorized person, or person delegated authority by the budget executor, responsible for the execution of the budget.

6) "*Capital expenditures*" are the use of funds to acquire or upgrade capital assets, such as buildings, structures, machinery, and equipment, and financial assets.

7) "*Cash payments"* are any monetary transactions resulting in a reduction in the balance of a bank account or cash balance.

8) "*Chart of accounts"* is a structured list of accounting codes used to classify and record budget revenue and expenditure transactions.

9) "*Commitment"* is an undertaking to make an expenditure following the conclusion of a binding agreement that will result in a payment.

10) "*Contingency reserves"* are funds allocated to the Ministry of Finance in the annual budget law or supplementary budget laws for the purpose of making expenditures that are urgent and unforeseen at the time of passage of the annual budget law.

11) "*Council of Ministers"* is the Council of Ministers described in the Law of Administration for the State of Iraq for the Transitional Period (the "Transitional Administration Law" or "TAL").

12) "*Current expenditures"* are expenditures which are not capital expenditures, such as salaries, supplies, services, and fuel.

13) "*Economic classification"* is a systematic arrangement of budget revenue and expenditure items by type for the purposes of financial statistical reporting and analysis.

14) "*Financial assets*" include foreign or domestic cash, deposits, loans, bonds, financial derivatives, accounts receivable, other types of claims, monetary gold, special drawing rights (SDRs), treasury bills, and shares.

15) "*Fiscal year"* is the general government's accounting period, which begins on January 1st and ends on December 31st.

16) "*Federal budget"* is the estimate of the total annual receipts and payments as approved by the Federal Government.

17) "*Federal government"* is the Iraqi Interim Government, the Iraqi Transitional Government, or the Government to be elected pursuant to a permanent constitution, as set forth in Article 61 of the Law of Administration for the State of Iraq for the Transitional Period (the "Transitional Administration Law" or "TAL").

18) "*Federal government bank account"* is a bank account for the receipt, payment, or transfer of public money belonging to the federal government.

19) "*Functional classification system*" means the array of budget authority, expenditures, and other budget data according to the major purpose served—for example, agriculture, national defense, and transportation.

20) *"General government"* comprises all government units primarily engaged in non-market operations, including the federal government, regional governments, governorates, municipal and local governments.

21) *"Government debt securities"* are debt securities issued by the Ministry of Finance, including debt securities lawfully issued prior to the effective date of the Public Debt Law promulgated in 2004.

22) *"Governorates' budgets"* are the estimates of annual receipts and payments of the governorates.

23) *"Governorate Councils"* are the Governorate Councils described in Section 2 of CPA Order Number 71, Local Governmental Powers (the "Local Governmental Powers Law").

24) *"Line items*" are the payments specifically itemized in the budget law.

25) *"In kind"* means a transfer or exchange in which payment takes the form of tangible property, intangible property, or services rather than cash.

26) *"Liability*" is a present obligation arising from past events, the settlement of which is expected to result in a future payment in cash or in kind.

27) *"Outlay"* means a payment to liquidate an obligation other than borrowing.

28) *"Payment arrears"* arise when a payment is not made by its due-for-payment date.

29) *"Petroleum"* means hydrocarbons, including, but not limited to, crude oil, natural gas, and natural gas liquids and refined petroleum products.

30) *"Petroleum revenue account"* means the Development Fund for Iraq (DFI) account as described in United Nations Security Council Resolution 1483 (2003) or any successor account to the DFI.

31) *"Public money"* means cash and bank deposits within the custody and control of the federal government.

32) *"Public corporations"* are -

(1) State companies, as defined in Law Number 22 of 1997 on State Companies; and

(2) any other juridical person or unit that is owned or controlled by the federal government, and produces goods or services for the market and, in the case of a unit which is not a juridical person, functions independently and is capable of maintaining separate accounting.

33) *"Special budgetary funds"* are special funds whose sources, uses, and purposes are established by law.

34) *"Spending units"* are the ministries of the federal government and the administrative bodies of the federal and regional governments, governorates, and municipal and local governments, to which funding is allocated in the annual budget law.

35) *"Reallocate,"* in relation to a budget appropriation, means to move budgetary resources from one budget account, unit, or line item to another.

36) *"Transfers"* are the provision of goods and services, assets (including financial assets), or labor that do not require the recipient to provide a good, service, payment, or payment-in-kind in return.

37) *"Treasury Consolidated Account"* is a system managed by the Ministry of Finance for consolidating the balances of the cash accounts of the federal government for the purpose of efficient cash management.

38) *"Treasury general ledger"* is a system, based on double entry principles, of accounting for, executing, and reporting the budget.

39) "*Treasury Single Account*" is a bank account, or a set of linked bank accounts, of the government through which all government receipts and payments are channeled. It is controlled by the Ministry of Finance and is maintained at the Central Bank.

40) *"Government"* is the public authorities and agencies of Iraq, which are entities established through political processes, and that exercise legislative, judicial or executive authority within the territory of Iraq. Government does not include public corporations.

41) *"Government debt"* consists of all liabilities of the government that require payment or payments of interest and/or principal by the borrower to the lender at a date or dates in the future.

42) *"Petroleum revenue"* is petroleum export revenue, non-tax revenue earned from the sale of petroleum to domestic buyers (collectively, petroleum non-tax revenue), and tax revenue levied on petroleum (petroleum tax revenue).

43) *"Petroleum export revenue"* is non-tax revenue earned from the sale of petroleum to foreign buyers.

44) "*Publicly available"* means that information is available for ready access by any member of the public. This includes, but is not limited to, publication in the *Official Gazette*, on an unrestricted website, or in widely available public newspapers.

## Section 3
## Exercise and Delegation of Authority

1) The Minister of Finance may issue regulations, instructions, guidelines or directions as necessary to give effect to and implement this Law.

2) The Minister of Finance may delegate to officials within the Ministry of Finance who are authorized persons those authorities that are conferred upon him under this Order, except the authority to waive the right of the federal government to collect amounts owing, to submit the draft annual federal budget to the Council of Ministers, and to sign borrowing and guarantee contracts of the federal government.

## Section 4
## General Provisions

1) The budget is adopted for the fiscal year and shall be valid during the year for which it is passed. Unspent appropriations will lapse at the end of the fiscal year for which they have been approved, except to the extent that goods and services have been validly ordered and received.

2) The draft annual budget law will be determined by the Council of Ministers and will be submitted by the Minister of Finance by October 10th to the body vested with national legislative authority for approval or adjustment pursuant to Article 33(C) of the TAL.

3) Pursuant to Article 25 of the TAL, the federal government has exclusive competence in drawing up the federal budget of Iraq. The Governorate Council, pursuant to Section 2 of the Local Governmental Powers Law, possesses the limited amendment authority to amend the budget plan of a ministry with regard to a specific project. Individual governorates' budgets for the fiscal year shall be passed by the Governorate Councils. Individual regions' budgets for the fiscal year shall be passed by the regional governments.

4) The annual federal budget shall comprise:
   a) the receipts and payments in cash or in kind of all government ministries, organizations, and agencies of the federal government; and

   b) transfers, including to regional governments, governorates, and municipal and local governments, including special budgetary funds.

5) The source of all receipts shall be specifically identified in the budget. All payments for the budget year and commitments for future years shall be disclosed in the budget, and the nature and duration of these commitments shall be limited as specified in the annual budget laws.

6) The difference between receipts (excluding borrowings) and payments (excluding repayments of debt principal) is the budget surplus (if positive) or the budget deficit (if negative).

7) Receipts consist of:

    a) Tax revenues:
        1. Petroleum tax revenues;

        2. Non-petroleum tax revenues;

    b) Non-tax revenues:
        1. Petroleum non-tax revenues;

        2. Non-petroleum non-tax revenues;
            1) Social security contributions;
            2) External grants;
            3) Others;

    c) Domestic and external borrowing;

    d) Repayment of government lending;

    e) Proceeds from asset transfers;

    f) Transfers of surplus profits from the Central Bank of Iraq in accordance with the relevant provisions of the Central Bank Law;

    g) Transfers from public corporations;

    h) Transfers from regional governments, governorates, and municipal and local governments, including special budgetary funds.

8) Payments consist of:

    a) Current expenditures, including for salaries and other allowances, outlays for goods and services, current transfers, including pensions and social security payments, that are paid in cash or have been issued in kind, interest payments and transfers in kind;

    b) Capital expenditures for purchase of fixed assets, inventories, intangible assets, financial assets, capital transfers that are paid in cash or have been issued in kind, and grants;

    c) Gross lending;

    d) Repayment of external and domestic debt;

    e) Other payments in accordance with the laws of the federal government;

f) Transfers to the Central Bank of Iraq in accordance with the relevant provisions of the Central Bank Law;

g) Transfers to public corporations;

h) Transfers to regional governments, governorates, and municipal and local governments, including special budgetary funds.

9) A Treasury Consolidated Account shall be established and maintained within the Ministry of Finance. Subject to the transition provisions in Section 15, all receipts shall be credited to the Treasury Consolidated Account and paid into the Treasury Single Account, and all payments shall be debited to the Treasury Consolidated Account and withdrawn from the Treasury Single Account. All federal budget receipts, commitments, expenditures, and other payment transactions shall be entered into the Treasury's General Ledger.

10) The Minister of Finance shall issue orders to open bank accounts and such accounts must have a title that includes the words "federal government." An authorized person may dispose of federal government money only in accordance with this law and with regulations properly promulgated by the Minister of Finance. An authorized person must not misapply, improperly dispose of, or improperly use federal government money in contravention of this Law. Violations of this Law are subject to applicable administrative and criminal penalties under the legislation of Iraq, including Article 2(g) of Law Number 7 of 1958, Wastage of Natural Resources and Squandering of Public Assets and Funds, and applicable provisions of Law Number 111 of 1969, as amended, including provisions relating to bribery by public officials, embezzlement by public officials, and officials who overstep the bounds of their duty.

11) Subject to the monetary limits established by the Council of Ministers, the Minister of Finance may waive the right of the federal government to collect an amount owing, postpone the time of payment, or allow payment by installment only under the conditions and procedures provided by law.

12) The Minister of Finance shall report each and every such written-off sum or postponement to the Council of Ministers with the explanation for the write-off. This report shall be submitted quarterly with a final summary report to be submitted with the annual final accounts of the federal budget. These reports will be made publicly available.

13) The annual federal budget shall stipulate the use of the budget surplus or the means of financing the budget deficit.

14) The budget deficit shall be financed by cash balances of the federal government, short-term borrowings, domestic and external loans, or by the issuance of government debt securities. Short-term borrowings may be used for the purpose of ensuring liquidity during a period no longer than six months.

15) The annual federal budget shall be accompanied by documents that shall state the objectives and operating rules for fiscal policy, including constraints on borrowing and federal government debt, in accordance with the principles stated in Section 1 and with the provisions in Section 6(1) of this law and following Section 7(1), and will report on progress against these objectives.

## Section 5
## Management of Petroleum Revenues

1) All proceeds from the sale of petroleum or otherwise derived from current and prospective petroleum extraction, including from the federal government's production shares and royalties, and from the amount paid in respect of a right to explore for petroleum resources, and any amount derived from the investment of amounts in the petroleum revenue account, shall accrue to the budget. Except as provided in paragraph 2 of this section, below, or as may otherwise be required by applicable United Nations Security Council Resolutions (UNSCRs), the receipts from the export of petroleum shall be deposited into the Development Fund for Iraq (DFI) account to be held in the name of the Central Bank of Iraq, or a successor account to the DFI, hereafter generically referred to as the petroleum revenue account, and reflected accordingly as receipts and transfers to and from the budget.

2) Pursuant to United Nations Security Council Resolution 1483 (2003), and subsequent related UNSCRs, five percent (or such other percentage as may be determined by the United Nations Security Council or jointly by the internationally recognized, representative government of Iraq and the Governing Council of the United Nations Compensation Commission in accordance with UNSCR 1483) of the receipts from the export of petroleum shall be transferred to the Compensation Fund established in accordance with UNSCR 687 (1991) and subsequent relevant UNSCRs and the balance of receipts from the export of petroleum shall be deposited into the petroleum revenue account. These transfers to the Compensation Fund will be shown in the budget.

3) Disbursements from the petroleum revenue account shall be restricted to disbursements necessary to finance the budget, which shall include adequate provision for the government's obligations under any relevant UNSCRs or international law.

4) In the event that a successor account to the original DFI is established or the original DFI is continued beyond the date of the transfer of governance authority to the Iraqi Interim Government, the following will apply:

   a) Operational responsibility for the petroleum revenue account will be with the Minister of Finance, reporting to the Council of Ministers, which shall take advice from the Governor of the Central Bank and such other individuals as the Council may deem appropriate. The Council, in its discretion, may delegate responsibility for oversight of the operation of the petroleum revenue account to a committee, which shall be composed of such individuals as the Council may determine, and shall include, as a minimum, the Minister of Finance, the Minister of Oil and the Governor of the Central Bank in an advisory capacity.

b) Disbursements from the petroleum revenue account require the authorizing signature of at least two authorized persons, one of whom is an official in the offices supporting the Prime Minister or Council of Ministers and reporting to the Prime Minister and the other a permanent employee of the Ministry of Finance, designated by the Prime Minister and the Minister of Finance, respectively. The persons to whom authority has been delegated may not delegate to another person.

c) Any positive balance in the petroleum revenue account may be invested by the Minister of Finance with the written consent of the Council of Ministers or the committee mentioned in section 5(4)(a) of this law. Any amount so invested shall at all times remain the property of the Government of Iraq. No contract or agreement that purports to encumber the assets of the petroleum revenue account shall be enforceable, and the assets shall continue to enjoy all privileges and immunities to the extent provided by UNSCR 1483, or as otherwise decided by the UN Security Council.

d) The activities of the petroleum revenue account shall be subject to external audit conducted under the oversight of the Board of Supreme Audit, which shall act in accordance with Law Number 6 of 1990 as amended by CPA Order Number 77 (CPA/ORD/18 April 2004/77), except as otherwise provided by relevant UN Security Council Resolution.

5) The Minister of Finance shall make publicly available details of the petroleum revenue account; including opening and closing balance, underlying assets, and summary of movements, within three weeks of the end of each month. The Minister of Finance will authorize a quarterly review of the investment position, and by the end of the month following the end of each quarter submit a report on the results of the review to the Council of Ministers or the committee mentioned in section 5(4)(a) of this law. The final report for each year will detail each investment and enumerate the changes in the portfolio over the year and will be made publicly available.

## Section 6
## Budget Preparation

1) The preparation of the federal budget shall be based on the projections of economic development, the pursuit of macroeconomic stability, economic policy, and applicable laws and regulations, and shall be prepared with due regard to the desirability of ensuring the sustainability of Iraq's fiscal position, minimizing fluctuations in government spending, and achieving efficient revenue collection. In particular, the preparation of the federal budget will be based upon prudent and conservative forecasts for petroleum prices, petroleum production, and tax and customs revenue. The projections shall be prepared by the Ministry of Finance in consultation with the Central Bank and other Ministries in their respective areas of expertise.

2) During the month of May of each year, the Minister of Finance, shall issue a report on the priorities for fiscal policy for the next fiscal year, including the proposed total limit on spending and the limits for each individual spending unit, and submit it to the Council of Ministers for approval, together with the Final Accounts of the Federal Budget as submitted to the Board of Supreme Audit according to section 11(6) of this law, and an update on progress in execution of the budget in the current fiscal year. The Minister of Finance shall consult with the Minister of Planning and Development Cooperation on priorities, estimates of total funding, and procedures for preparing the capital spending plan and current budgetary implications of capital expenditures, including those to be implemented or financed by external sources.

3) In the month of June of each year, the Minister of Finance, in consultation with the Minister of Planning and Development Cooperation, and based on the priorities for fiscal policy established by the Council of Ministers, shall issue a circular setting guidelines and objectives of fiscal policy for spending units for the preparation of their budgets. The circular shall include key economic parameters, based on the macroeconomic framework referred to in Section 7(1), the procedures and timetable for budget preparation, as well as total levels of expenditure for each spending unit. This will serve as the basis for the spending unit to prepare its budget request.

4) In the month of July of each year, spending units will submit requests, including the information prescribed below, to the Minister of Finance for the allocation of funds. Copies of requests for the capital portion of the budget will also be submitted to the Ministry of Planning and Development Cooperation. Each request shall include:

a) The expenditure estimates for the budget year as prescribed in the economic and functional classification systems determined by the Minister of Finance in accordance with international accounting standards, including the value of outstanding commitments for the current or prior year;

b) Consistent with the guidelines issued by the Minister of Finance, the expenditure estimates for the year following the budget year (the “upcoming fiscal year”) and to the extent permissible given conditions prevailing in Iraq, for the two fiscal years following the upcoming fiscal year as prescribed in the economic and functional classification system determined by the Minister of Finance, in accordance with international accounting standards;

c) Estimates of personnel requirements for which budgetary funds are required;

d) Estimates of the requirements for other operating costs;

e) Multi-year commitments or multi-year payments, along with separately prepared capital expenditures; and

f) Estimates of receipts from the core activities of spending units.

g) Estimates of the proportion of expenditures that would be due in foreign currency.

5) The Minister of Finance may determine more specific requirements for the content and format of the request.

6) The Minister of Finance, in consultation with the Minister of Planning and Development Cooperation shall, on the basis of the estimates of revenue and submitted budget proposals for the allocation of budget funds, and in the light of discussions with proposing Ministers, determine estimated payments for spending units for the budget, as well as any amounts to be included in the contingency reserve.

7) In the event of an irreconcilable disagreement during discussions on the draft annual federal budget between the Minister of Finance and the Ministers responsible for spending units, the Minister of Finance will note the disagreement and explain his proposed solution in his submission of the draft annual federal budget. In determining the proposed solution, the Ministry of Finance may consult with the Ministry of Planning and Development Cooperation regarding the prioritization of capital expenditures. The Council of Ministers may, within the agreed aggregate limit, adjust appropriations in accordance with their collective priorities. Any increase in the aggregate spending limit must be based on a proposal submitted by the Minister of Finance and approved by the Council of Ministers.

8) In the month of September of each year, the Minister of Finance shall prepare the draft annual federal budget and submit it to the Council of Ministers for approval. The Minister of Finance shall submit the budget by October 10th to the body vested with the national legislative authority for approval.

## Section 7
## Budget Law

1) In preparing the draft annual budget law the following shall be taken into account, disclosed to the body vested with national legislative authority, and made publicly available in the documents accompanying the budget law:

a) A statement of the objectives and operating rules for fiscal policy in accordance with the principles stated in this law, and an explanation of how these objectives relate to provisions in the annual budget law.

b) A comprehensive and consistent quantitative macroeconomic framework, and the main assumptions underlying the budget, including the assumptions for oil prices and oil production. To the extent permissible given conditions prevailing in Iraq, the macroeconomic framework shall cover the budget year and the subsequent three years;

c) New policies being introduced in the annual budget and their quantified fiscal impact;

d) Major fiscal risks, quantified where possible, including variations in economic assumptions and the uncertain costs of specific expenditure commitments, including financial restructuring;

2) The draft annual budget law shall include:

a) The estimation of receipts in cash and in kind in accordance with economic classification;

b) The estimation of payments in cash and in kind in accordance with economic, organizational, and functional classifications;

c) The use of any surplus, and the financing of any deficit;

d) The contingency reserve, which shall be no greater than 5% of the non-interest expenditures of the federal budget;

e) Clear specification of the rules for authorization of expenditure and limits to expenditure. Limits on borrowing, issuance of government debt securities, change in stocks of government debt securities, and guarantees consistent with the Public Debt Law, and the authority granted to the Minister of Finance to buy, redeem, or refund outstanding government debt securities;

and the draft budget law shall be accompanied by a report on the economic and financial situation, including the assumptions, methods, and outcomes of the economic projections on the basis of which the draft annual Federal budget law is established, including actual revenues, expenditures, balance and total debt of the general government for the past two years.

3) The body having national legislative authority has the right to reallocate proposed spending and to reduce the total amounts in the federal budget. It also has the right to propose an increase in the overall amount of expenditures to the Council of Ministers if necessary, and provide notice of this proposal to the Minister of Finance. The Minister of Finance will make a nonbinding recommendation to the Council of Ministers with respect to this proposal.

4) If the federal budget is not approved by the body vested with national legislative authority by December 31st, the Minister of Finance will, on a monthly basis, approve funds for spending units up to 1/12 (one twelfth) of appropriations of the previous fiscal year until a budget is approved. The funds so provided for can be used only for liquidation of existing commitments, salaries, pensions, social security payments, and debt service.

5) The annual federal budget may be amended through a supplementary budget only on the basis of a significant and unexpected change in economic circumstances or national priorities. The supplementary budget must be determined by the Council of Ministers on recommendation

of the Minister of Finance and approved by the body vested with national legislative authority. Should the Minister of Finance conclude that a supplementary budget is required, he shall make appropriate recommendations, including on proposed total receipts and payments, to the Council of Ministers. The Minister of Finance shall, within eight weeks after recommending that the Council of Ministers adopt a supplementary budget, submit details of the draft supplementary budget to the Council of Ministers for approval. The Council of Ministers shall approve such recommendations, with any appropriate modifications, within two weeks of receiving them. The draft supplementary budget, as approved by the Council of Ministers, shall be submitted to the body vested with national legislative authority within one week of such approval. The Minister of Finance shall issue regulations and guidelines for the procedures to be followed in preparing the supplementary budget.

6) The revenues and expenditures of special budgetary funds are to be reflected in the annual budget law.

7) The approved federal annual and supplementary budgets shall be published in the *Official Gazette* and made publicly available in other media, as appropriate.

## Section 8
## Public Corporations

1) Each public corporation shall prepare its budget proposal, and after approval by its directors and the competent minister, submit it to the Minister of Finance for review and final approval. The budget should, among other things, show budgeted revenues, expenses, profits or loss, capital expenditure, cash flows, borrowings, grants, transfers, contingent liabilities including guarantees, and balance sheet. Any amendments to the budget shall also be submitted to the Minister for Finance for review and approval**.** The Minister of Finance shall respect the operational independence of public corporations.

2) The budgets of public corporations are not incorporated into the federal government budget and are not incorporated into the budgets of any other level of government.

3) Public corporations shall submit by August 31st estimates of total loans and short-term borrowings to be raised in the forthcoming fiscal year for approval by the Minister of Finance. Public corporations will report monthly to the Minister of Finance on the amount of loans and short term borrowings raised. Guarantees given by the federal government in respect of public corporations borrowings shall be in accordance with law, and shall be disclosed in the final accounts of the federal government.

4) All public corporations shall submit their monthly accounts to the competent ministry 10 days following the end of each month. All public corporations shall submit semi-annual accounts to the Minister of Finance no later than July 15th. Each public company shall submit its audited final accounts to the Minister of Finance no later than March 31st of the year following the fiscal year ended. The final accounts shall include balance sheet, profit and loss statement, cash flow statement, and notes to the final accounts covering, among other things,

accounting policies, revenues and expenses, assets and liabilities including borrowings, commitments, and contingent liabilities. The final accounts shall be prepared in accordance with international standards and shall be audited by an independent auditor.

## Section 9
## Budget Execution

1) The Minister of Finance is responsible for the execution of the federal budget**.**

2) No payments will be made from the Treasury Consolidated Account except under an appropriation made in the annual budget or supplementary budget law, under a standing appropriation of another Law, or to make an investment in terms of Section 5(4)(c) of this Law**.**

3) Spending units will use the funds determined in the federal budget in accordance with a spending plan that has been approved by the Minister of Finance.

4) Spending units may not commit to making expenditures that exceed the amounts allocated to them, unless otherwise provided by the budget law.

5) Budget executors are responsible for ensuring that allocated funds within their spending units are used for lawful purposes.

6) Appropriations for contingency reserve funds may be used for payments that are urgent and that were unforeseen at the time the annual budget law was passed, if approved by the Council of Ministers and the Minister of Finance. The Minister of Finance shall propose the criteria for using reserve funds for approval by the Council of Ministers. All expenditures from the reserve will be reported to the body vested with national legislative authority.

7) In accordance with regulations prescribed by the Minister of Finance, the spending units, governorates, and special budgetary funds shall submit reports on realized receipts and executed payments to the Minister of Finance within 30 days following the end of each month. By the 15$^{th}$ of the subsequent month, the Ministry of Finance shall compile a consolidated report on realized receipts and executed payments on the basis of the reports submitted, and make it publicly available in the *Official Gazette* and other media, as appropriate.

8) The Ministry of Finance can authorize the responsible Minister or Ministers, subject to the provision below, to reallocate the approved budget appropriations from one spending unit to another up to a limit of five per cent of the amount approved by the annual or supplementary budget law for the spending unit that is to have its appropriation reduced. The following restrictions apply:

a) No funds can be reallocated between a current expenditure of one spending unit and the capital expenditures of another or between transfer payments of one spending unit

and other items, including salaries, goods, and services or capital expenditures, of another.

b) Spending units may, with the approval of the Minister of Finance, reallocate their approved funds between line items by up to 5% of the total amount of funds approved provided that no funds can be reallocated from capital to current expenditures or between transfer payments and other current expenditures, including salaries, goods and services. Virement from salaries or current spending to capital spending of up to 5% may be permitted with the approval of the Minster of Finance.

c) A report of these transfers shall be prepared by Ministry of Finance and submitted on a quarterly basis to the body vested with national legislative authority. A copy of such report will be forwarded to the Minister of Planning and Development Cooperation.

9) Funds approved for spending units may be used only until the December 31st of the fiscal year, except to the extent that goods and services have been validly ordered and received. Receipts received after the end of a fiscal year will be recorded as receipts of the next fiscal year budget.

## Section 10
## Borrowings and Guarantees

1) Federal government debt may be in the form of domestic and foreign loans, short-term borrowings, and securities issues. The issue and redemption of securities shall be managed by the Central Bank of Iraq as the agent for the federal government. The Ministry of Finance and the Central Bank shall share information on government cash and borrowing needs and current monetary conditions in order to ensure effective coordination of monetary and budgetary policy.

2) Governorates and regional governments may, upon notification to the Minister of Finance, raise funds through borrowings, and issue loan guarantees subject to the debt limit set in the annual budget law, and to the specific debt limit set for each entity under the apportionment approved by the Council of Ministers on a recommendation of the Minister of Finance. Regional governments and governorates shall submit by August 31st estimates of total outstanding borrowings, and borrowings to be raised in the forthcoming fiscal year for review and for approval by the Minister of Finance. Regional governments and governorates will report to the Minister of Finance monthly on the amount of outstanding borrowings raised and loan guarantees issued.

3) The Ministry of Finance shall submit to the Council of Ministers for approval with the draft annual budget law, the financial plan on loans, short-term borrowing, and the issuing of guarantees by the federal government, governorates regional governments. In addition, the Ministry will submit to the Council of Ministers a report any time that the plan must be changed. Such changes must remain within the limits set by the budget. The Ministry of

Finance shall have the right, upon notification to the affected governorate or regional government, to adjust the timing of the issuance of governorate or regional government debt approved in the plan on the basis of macroeconomic and debt policy considerations.

4) The annual budget law shall determine the terms, conditions, and the limit on the annual increase in the total existing federal government, regional government and governorate and public corporation debt, and shall establish the total amount of guarantees to be issued by the federal government, regional governments, governorates, and public corporations.

5) The federal government shall set limits for guarantees issued by regional governments and governorates, but shall not guarantee them, unless explicitly provided in law.

6) The Minister of Finance shall sign the borrowing and guarantee contracts of the federal government, and shall enter into a contract with the Central Bank for services required in implementing all decisions on issues of securities.

7) The Minister of Finance shall maintain a record of all federal government debt. The authorized body within the regional governments and governorates shall maintain a record of existing regional government and governorate debt, loans granted, short-term borrowings, and issued guarantees, and shall provide the Ministry of Finance with an updated record of this information within 30 days of the end of each month.

8) The Minister of Finance shall prepare a consolidated report on all government debt within 90 days of the end of each fiscal year and shall make this report available to the public.

## Section 11
## Internal Control and Accounting

1) Budget executors shall be responsible for the accounting and internal control of transactions related to receipts, commitments, and payments of spending units and sub-units falling within their jurisdiction.

2) The Minister of Finance shall, on behalf of the federal government, have responsibility for the accounting, internal control, borrowing, and debt transactions associated with the budget.

3) The Minister of Finance shall prescribe internal control arrangements, accounting procedures and standards, submission of reports on the usage of budget funds, and the manner of recording receipts, payments, and commitments.

4) The Minister of Finance may issue special orders to spending units, governorates, municipal and local governments, and other budget entities for their submission of financial reports and shall prescribe the submission of the Final Accounts of spending units, including regional governments, governorates, municipal and local governments, and other budget entities.

5) The Minister of Finance shall submit to the body vested with national legislative authority by May 31st and November 30th, quarterly reports on the execution of budget revenue, expenditures, and financing for the quarters ending March 31st and September 30th, respectively. This report will include the execution of budget revenue, expenditures and financing of the federal budget. The Minister of Finance shall also submit to the body vested with national legislative authority by August 31st of each year a mid-year report on execution of budget revenue, expenditures, and financing for the half year ending June 30th. This report will include detailed information on the execution of budget revenue, expenditures and financing of the budget.

6) The Minister of Finance shall, by April 15th of the succeeding year, prepare the annual final accounts of the federal budget, including special budgetary funds, and submit it to the Board of Supreme Audit. The Board of Supreme Audit will provide an audit report on the final accounts by June 15th. The Council of Ministers will submit final accounts and the related audit report to the body vested with national legislative authority by June 30th.

7) The final accounts of the federal budget must be in accordance with the content and classifications of the budget and international accounting standards, and shall include the following:

a) An external audit report from the Board of Supreme Audit in accordance with the Board of Supreme Audit Law, as amended, and its established procedures;

b) The initial and final balance of the Treasury Consolidated Account and a summary of movements for the year;

c) A report on differences between budgeted and executed receipts and payments and on the financing of any deficit or the use of any surplus;

d) A report of all federal government borrowings for the year, and the total debt outstanding, including any payment arrears;

e) A report of spending from the budget contingency reserves;

f) A report on federal government guarantees issued during the fiscal year;

g) The Minister of Finance shall prepare a report of all borrowings by regional governments and governorates;

h) Outstanding amounts on capital contracts;

i) Retentions due on contracts;

j) Letters of credit entered into for which funds have been placed but for which goods have not been received;

k) The Minister of Finance shall prepare a report on all guarantees by regional governments and governorates.

8) Following approval of the final accounts of the annual federal budget by the body vested with national legislative authority, the final account shall be published in the *Official Gazette* and made publicly available.

**Section 12**
**Ministry of Finance Functions**

1) The Ministry of Finance shall be responsible for, but is not limited to, conducting the following treasury functions:

a) Executing all cash and non-cash payments on the basis of documentation and data supplied manually or electronically by spending units, in accordance with this Law;

b) Maintaining the Treasury general ledger and subsidiary accounts;

c) Processing budget allocations to spending units;

d) Preparing the federal government's final accounts;

e) Ensuring that no budget executor can exceed his annual appropriation;

f) Developing and managing the federal government's accounting and financial information system;

g) Providing regular financial reports as required;

h) Supporting analysis and improvements to the federal government's financial systems;

i) Making payments from the current and permanent reserves;

i) Managing the cash balances of the Treasury Consolidated Account and the investment of the federal government's surplus cash balances;

j) Managing the recording of domestic and external debt;

k) Managing the recording of international grants, assistance, and loans;

l) Preparing government accounting and financial management standards, regulations, and related legislation;

m) Managing the opening, recording, and reconciliation of government bank accounts; and

n) Managing the operations of the Regional Treasury Offices.

2) The Ministry of Finance shall be responsible for, but is not limited to, the following budget formulation functions:

a) Managing the process of budget preparation, planning and development, including the preparation of macroeconomic and other economic advice;

b) Proposing guidelines for the preparation, planning, execution, revision, and evaluation of budgets;

c) Preparing the annual budget law, any supplementary budget laws, and making them publicly available;

d) Monitoring receipts and execution of payments, including petroleum revenues;

e) Preparing cash flow forecasts;

f) Providing advice to the Council of Ministers on requests by spending units for the reallocation of appropriations and implementing decisions on reallocations;

g) Making payments from the current and permanent reserves.

h) Providing advisory support on budgetary issues to all spending units; and

i) Preparing reports on budget preparation and budget execution for international economic organizations.

j) Preparing regulations, instructions, guidelines and directions under this Law and on amendments to this Law.

## Section 13
## Internal Audit

1) The Minister of Finance shall prescribe the manner and procedures by which Ministries, spending units, and public corporations will undertake internal audits, and is responsible for ensuring that the internal audit process is conducted in accordance with these rules and procedures.

2) Internal Audit performance consists of the following:

a) Providing regular assessments of the adequacy and effectiveness of the Ministries' decision-making processes, minimization of risk, and internal control;

b) Reporting significant internal control issues and improving the control processes and information system in order to minimize risk in the decision-making process;

c) Reviewing the efficiency and effectiveness of the use of existing services, and proposing more efficient ways of providing these services;

d) Liaising with the external audit agency; and

e) Providing periodically information on the status of the execution of the annual audit plan.

**Section 14**
**External Audit**

1) The federal budget and any supplementary budget shall be subject to annual audits by the Board of Supreme Audit, according to the law.

2) In order to facilitate this audit, the Minister of Finance shall make available to the Board of Supreme Audit:

a) The approved federal budget and any supplementary budgets, and any accompanying documents;

b) The reported results of all internal audits;

c) The quarterly and annual reports on loans, borrowings, guarantees, and debt;

d) Final accounts of public corporations and the results of all audits;

e) Documents discussed by the Council of Ministers its role of oversight of operations for any successor to the DFI, or by any committee delegated with this role according to section 5(4) of this Law, as well as the results of any internal audits; and

f) Any other documents, information and explanation requested by the Board of Supreme Audit in connection with the performance of its audit functions.

## Section 15
## Transitional Arrangements

1) To the extent that this Law is inconsistent with existing laws, the provisions of this Law shall prevail.

2) Regulations implementing this Law shall be approved within 12 months from the day of enactment of this Law. Until these regulations are approved, existing regulations shall continue to apply, to the extent consistent with this Law.

3) In transitioning to the Treasury Single Account, the Minister of Finance is hereby authorized to close the accounts of the federal government Budget Accounts opened at the Central Bank or in any other banks. Resources remaining in Federal Budget user accounts are to be transferred to the Treasury Single Account and reflected in the Treasury Consolidated Account. Until the closure of the existing bank accounts is completed and the Treasury Single Account is fully established, the Minister of Finance is authorized to operate the existing bank accounts on a zero-balance basis under which balances of these accounts will be transferred to the Treasury Single Account on a daily basis. Should circumstances make daily transfers impracticable, the Minister of Finance shall institute transfers as frequently as practicable.

4) Law Number 107 of 1985 on Consolidated Government Budget (as amended by Law Number 48 of 1990), and Law Number 20 of 1940 on General Accounting Principles shall not have effect for the fiscal year 2005 and subsequent years.

5) The Minister of Finance is authorized to promulgate rules that will facilitate accurate financial reporting during the period in which Iraq is undergoing the transition to international accounting standards ("interim standards"). These interim standards shall apply only for the fiscal year with respect to which they are promulgated. Reports prepared for these periods that are otherwise required to comply with international accounting standards may comply with either the interim standards or international accounting standards.

6) Unless otherwise provided by relevant UNSCR and the Transitional Administration Law, including its Annex, prior to the establishment of a national legislature, the Council of Ministers shall serve as the final approval authority for the federal budget, subject to the approval of the Presidency. During such period, if the federal budget is not approved by the Presidency and the Council of Ministers, the Minister of Finance will, on a monthly basis, approve funds for spending units up to 1/12th one twelfth of appropriations of the previous fiscal year until the budget is approved.

7) To the extent that the relevant UNSCR and the Transitional Administration Law, including its Annex, attributes executive power to a body or person different than the Council of Ministers, powers and responsibilities delegated to the Council of Ministers by this Law shall be delegated instead to the executive body or person so identified in the relevant UNSCR or the Transitional Administration Law.

8) Upon the transfer of governmental authority to the Iraqi Interim Government, the Program Review Board established pursuant to Coalition Provisional Authority Regulation Number 3 (CPA/REG/18 June 2003/3) shall cease to perform budgetary functions for Iraq and shall dissolve.

## Section 16
## Entry into Force

This Law shall enter into force on the same date that the Order authorizing this law enters into force. It shall apply to the budget of the fiscal year 2005 and subsequent years, and additionally, following the transfer of governance authority to the Iraqi Interim Government, shall apply to any supplementary budgets for fiscal year 2004.

ANNEX B

# IRAQ

# PUBLIC DEBT LAW

## Section I Definitions

For the purposes of this law, the terms below are defined as follows:

"*Bank*" means a bank as defined under the Banking Law.

*"Government"* means the entity exercising temporary governmental authority in Iraq on the date this law enters into force and then the transitional Iraqi administration upon the transfer to it of full governmental authority and the recognition of the sovereignty of that administration by the CPA, and then the internationally recognized representative government of Iraq once it assumes the responsibilities of such authority.

"*Government Debt Security*" means a debt security issued by the Ministry of Finance, including debt securities lawfully issued prior to the effective date of this Law. The term "debt security" shall have the same meaning assigned to it in the Banking Law.

"*Minister*" means the Minister of Finance acting in an official capacity.

"*Official Publication*" means the *Official Gazette* or such other general publication of wide circulation as specified by the Council of Ministers or its delegee.

"*Owner*" means the person registered as the owner of a Government Debt Security on the books of the government securities registrar.

## Section II Authorities and Duties Pertaining to the Issuance of Government Debt Securities

1. The Minister shall have authority to issue Government Debt Securities as an obligation guaranteed by the Government only in amounts reasonably necessary for expenditures authorized by law and in amounts necessary to buy, redeem, or refund outstanding Government Debt Securities.

2. The issue and redemption of Government Debt Securities shall be managed by the Central Bank of Iraq as the agent for the Government.

3. The Minister shall have authority to set the terms and conditions for Government Debt Securities before they are issued, such as:

(a) the date of maturity;

(b) the offering price and interest rate;

(c) the method of computing the interest rate;

(d) the dates for paying principal and interest;

(e) whether a debt security is to be issued on an interest-bearing basis, a discount basis, or an interest-bearing and discount basis;

(f) the form of the security;

(g) the currency in which the debt is issued; and

(h ) any other condition not prohibited by law.

4. The Minister shall have authority to determine how it will offer Government Debt Securities for sale, such as by competitive auction and by subscription.

5. The Minister shall have authority to offer Government Debt Securities for sale to any person.

6. The Minister shall deposit without delay all proceeds from the sale of Government Debt Securities into the public treasury or an authorized depositary.

**Section III Authorities and Duties Pertaining to Outstanding Debt Securities**

1. The Minister shall have authority to buy, redeem, or refund Government Debt Securities in accordance with their terms and conditions using public funds.

2. The Minister shall have authority to give relief to owners of lost, defaced, or destroyed Government Debt Securities in accordance with regulations issued by the Minister.

3. The Minister shall pay principal and interest in legal tender when due, or earlier in his discretion, in accordance with the terms and conditions of the Government Debt Security.

4. The Minister shall have a permanent and indefinite appropriation of public funds for the purpose of buying, redeeming, or refunding Government Debt Securities and for the purpose of paying interest on those securities.

**Section IV Authorities Pertaining to Fiscal Agents and Depositaries**

1. The Minister shall have authority to engage the Central Bank of Iraq, and any other Bank, as a fiscal agent for the purpose of carrying out any function authorized by this Law.

2. The Minister shall have authority to designate Banks that are eligible to act as depositaries for any part of the proceeds from the issuance of Government Debt Securities. The Minister shall have authority to prescribe conditions for the deposit of public money, including the interest rate on amounts deposited.

3. The Minister shall have authority to transfer public money in a depositary's possession to the public treasury, and to transfer public money between depositaries.

4. The Minister shall have the authority to require his fiscal agent and depositaries to provide him with any information about their activities under this Law.

**Section V Administrative Authorities and Duties**

1. The Minister shall have authority to issue regulations, prescribe policies, and issue announcements for the purpose of implementing this Law and carrying out the Minister's functions under this Law.

2. The Minister shall have authority to delegate his duties and functions under this Law, except the power to delegate, to any person within the Ministry of Finance.

3. The Minister shall publish all regulations issued under this Law in the Official Publication.

4. Prior to any sale, the Minister shall list the terms and conditions applying to a Government Debt Security in a regulation or an offering announcement. An offering announcement shall be publicized in a manner that ensures wide circulation among potential buyers.

5. If the Minister proposes to issue a regulation pursuant to this Law, he shall publish a draft of the proposed regulation in the Official Publication. Along with the proposed regulation, the Minister shall publish an explanation of the regulation and provide at least thirty days after publication for the public to submit comments. The Minister shall consider all comments received. If the Minister determines that a final regulation is appropriate, the Minister shall issue the regulation accompanied by a general description of the comments and his response to those comments. The Minister may issue a final regulation without publishing a draft or considering public comment if the Minister determines that the delay involved would be a serious threat to the interests of the financial system or hinder the effective conduct of monetary policy. In such an event, the Minister shall publish an explanation of his decision to depart from the procedures in this paragraph in the Official Publication.

6. The Minister shall maintain a system of books and records

(a) describing all issued Government Debt Securities;

(b) identifying the dates when outstanding obligations come due; and

(c) stating all amounts of principal and interest paid on Government debt securities.

7. The Minister shall make all its books and records pertaining to Government Debt Securities available for inspection upon request by the Prime Minister and Council of Ministers or its delegee.

8. On or before the end of the fiscal year, the Minister shall submit a report to the Prime Minister and Council of Ministers on the public debt activities of the Ministry of Finance. The report shall include, at a minimum:

(a) A table showing the public debt from all outstanding Government Debt Securities as of the date of the report, the interest cost for that debt in the current year, and the projected interest cost for government debt over the next five fiscal years, taking into account projections for the budget.

(b) A table showing the maturity distribution of the public debt from all Government Debt Securities outstanding as of the date of the report.

(c) An explanation of the overall financing strategy used in determining the distribution of maturities and interest rates for Government Debt Securities issued during the current fiscal year.

## Section VI Final Provisions

1. Any provision of Iraqi law that was enacted prior to the effective date of this Law and that is inconsistent with this Law is hereby superseded.

2. This Law shall enter into force on the same date that the Order authorizing this Law enters into force.

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FROM THE AMERICAN PEOPLE

# LAW OF GOVERNORATES NOT INCORPORATED INTO A REGION

## As Amended by Law 15 of 2010 and Footnoted

**MARCH 2011**

**Volume I**
**Version I**

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*RTI International is a trade name for Research Triangle Institute.

## TABLE OF AUTHORITIES FOR OTHER APPLICABLE LAWS

In numerous instances throughout the text, Law 21 mentions the Iraqi Constitution and other applicable law as binding on the provinces. Such other law would include the following.

| Law No. | Date | Central Government Body | Title |
|---|---|---|---|
| 24 | 1960 | COR | Civil Service Act, Law No. 24 of 1960 |
| 130 | 1963 | COR | Municipality Revenues Law No. 130 of 1963 |
| 165 | 1964 | COR | Municipal Administrative Law No. 165 of 1964 |
| 159 | 1969 | COR | Decentralization Law No. 159 of 1969 |
| 25 | 1995 | COR | Law of Popular Councils, Law No. 25 of 1995 |
| 71 | 2004 | CPA | Order 71 (abrogated by Law 21 of 2008, upon seating of Provincial Councils in April of 2009) |
| 95 | 2004 | CPA | Order 95, Financial Management and Public Debt Law |
| 39 | 1971 | COR | National Retirement Law |
| 27 | 2006 | COR | Unified Retirement Law |
| 69 | 2007 | COR | First Amendment of the Unified Retirement Law |
| 36 | 2008 | COR | Law of Electing Provincial, Qada'a, and Nahiya Councils |
| 44 | 2008 | COR | Amendment of Law of Electing Provincial, Qada'a, and Nahiya Councils |
| 37 | 2005 | COR | Forming the National Ministries |
| 16 | 1933 | COR | Elections Law |
| 36/44 | 2008 | COR | Law of Election of Provincial and Local Councils |
| 10 | 2008 | COR | Accountability and Justice Commission Law |
| 22 | 2008 | COR | Law of Public Sector Salaries |

Note: COR = Council of Representatives; CPA = Coalition Provisional Authority

## INTRODUCTORY NOTE

This document is a product of the Iraq Local Governance Program – Phase III (LGP III), funded by the United States Agency for International Development (USAID).

On the following pages, the text of Law 21 of 2008, entitled the *Law of Governorates Not Incorporated into a Region, As Amended by Law 15 of 2010*, is reproduced. Relying on the original Arabic text, this footnoted version of Law 21 updates and replaces a prior publication entitled *Law of Governorates Not Incorporated into a Region: An Annotated Text*. Published in July 2008, that pocket-sized edition anticipated how the law would (or ought to) be implemented. Although, by its own terms, Law 21 was then "in force," it did not begin to be implemented until late spring 2009, after provincial elections had been held and some disputes surrounding their outcome had been settled.

Once the law began to be implemented, differing opinions emerged as to how it should be interpreted. Because governorate (provincial) and lower level councils are not organized under a Ministry of Local Government as is common in neighboring Arab countries (and the Minister of State for Provincial Affairs lacks rule-making authority), these differences are not capable of being resolved via administrative regulations. Instead, the provincial (governorate) councils have largely been left alone, to interpret as well as they could those laws that are binding on them.

Of course, the laws binding on them include more than just the Constitution of 2005 and Law 21 itself, and this document includes a Table of Authorities and relevant citations to some of that other law applicable to the provinces. The footnotes in this volume, therefore, strive to show how the law is being interpreted with reference to the Constitution and other applicable law, as well as actual practice. The notes attempt to be neutral and to avoid advocacy of how the law should be interpreted; instead, they explain how a footnoted word, phrase, or paragraph has come to be understood after almost two years of implementation.

The Law of Governorates itself applies to only 14 of Iraq's 18 provinces. The Iraqi Constitution of 2005 recognized three provinces in the north of the country as being incorporated into the Kurdistan Regional Government (KRG). Law 21 has, therefore, never applied to those three provinces. It also does not presently apply to Kirkuk (Ta'meem) province because of an unresolved constitutional question of whether all or part of that province will be incorporated into the KRG.

The text of Law 21 and its amendment in Law 15 was originally written in Arabic. The English translation used here is the official translation of the U.S. Embassy in Iraq. In case of differences between the English translation and the Arabic original, the Arabic text governs. To encourage an appreciation of the sometimes very great differences between Arabic and English terms for governance concepts, and to encourage correct pronunciation of relevant words, a glossary of Arabic Terminology is also included with this document.

For more detailed information about the law in force in the provinces, please visit www.iraq-lg-law.org. For information on the Local Governance Program, please visit www.lgp-iraq.org.

March 2011

## ABBREVIATIONS

| | |
|---|---|
| **ARDP** | Accelerated Reconstruction and Development Program |
| **COMSEC** | Council of Ministers Secretariat |
| **COR** | Council of Representatives or national parliament |
| **CPA** | Coalition Provisional Authority (April 2003–June 2004) |
| **DG** | Director General |
| **GO** | Governor's Office |
| **HCCP** | High Commission for Coordination between Provinces (cf. Article 45) |
| **IHEC** | Independent High Electoral Commission |
| **ILGA** | Iraqi Local Government Association |
| **KRG** | Kurdistan Regional Government |
| **LGP III** | [Iraq] Local Governance Program–Phase III |
| **MMPW** | Ministry of Municipalities and Public Works |
| **MOF** | Ministry of Finance |
| **MOLSA** | Ministry of Labor and Social Affairs |
| **MOP** | Ministry of Planning |
| **O&M** | operations and maintenance |
| **PDP** | Provincial Development Plan (1-year plan) |
| **PDS** | Provincial Development Strategy (5-year plan) |
| **PPA** | Provincial Powers Act, a misnomer for the Law of Governorates Not Incorporated into a Region, Law 21 of 2008 |
| **PPL** | Prioritized Projects List/Proposed Projects List |
| **PPL** | Provincial Powers Law, another misnomer for Law 21 |
| **SAB** | Supreme Audit Board |
| **SMS** | short message service |
| **U.S.** | United States |
| **USAID** | United States Agency for International Development |
| **USD** | United States dollars |

## ARABIC TERMINOLOGY

The translation of Arabic governance terminology into English has confused what is already a challenging enough system. Therefore, the following list is intended to remove some of that confusion. It includes a few key Arabic terms as they appear in the Iraqi law/s. When appropriate, both the singular and plural form of nouns is given because plurals in Arabic are much more irregular than English nouns. Both singular and plural Arabic words are also shown with their vowel and diacritical markings to aid English readers, who are familiar with the Arabic script in the proper pronunciation. For English readers unfamiliar with the Arabic alphabet or its orthography, both the singular and the plural form of each word is spelled in Latin characters (i.e., transliterated). This transliteration is intended to help readers understand the proper pronunciation of the words. The phonetic spelling below includes elided definite articles indicated with hyphens, syllables differentiated by spaces, long vowels represented by doubled letters, and emphatic consonants represented by capitalized ones. Because this document is in the English language, the words are ordered alphabetically by their approximate English translation. They are translated only, however; they are not defined, because it is seldom possible to capture all the complex associations of such terms when translating from one language to another. Thus, this list of common governance terms is far from complete but is intended to increase understanding, both of the terms themselves and of their underlying meaning. To emphasize the uniqueness of that meaning and of the function of Iraqi institutions of government, terms in the Arabic language are, therefore, preferred to either the anglicized or the translated ones in the English text of the law and footnotes that follow.

**Table 1: Key Iraqi Governance Terminology**

| English | Arabic | Transliteration |
|---|---|---|
| alderman (or neighborhood sheikh) | مُخْتارْ | mukh tar |
| authority/ies | سُلْطة / سُلُطاتْ | sul Ta / su lu Taat |
| Baghdad Amanat | أمانة بغداد | a maa nat Bagh dad |
| budget | الْموازنة | al-mu wa za na |
| Cabinet of Ministers | مَجلسْ الوزراء | maj lis al-wu za ra'a |
| central | مَرْكزية | mar ka zee yah |
| central government | الحُكومة المَركزية | al-hu koo ma al-mar ka zee yah |
| city-center | مَركزْ المدينة | mar kaz al-ma dee nah |
| commission/s | هَيئة / هيئآت | ha ya'a / ha ya'aat |
| constitution/s | دُسْتور / دَساتير | dus toor / da saa teer |
| consultation | تَشاورْ | ta shaa ur |
| Council of Representatives | مجلسْ النواب | maj lis an-nu waab |
| decision/s | قرار / قراراتْ | qarar / qa-ra-rat |
| department/s | قِسْم/أقسام | qism / aq saam |

| English | Arabic | Transliteration |
|---|---|---|
| deputy/s | نائِبْ / نوّابْ | naa ’eb / nu waab |
| director/s | مُديرْ / مُدراءْ | mu deer / mu da raa’a |
| directorate/s | دائرة / دَوائِرْ | daa ’era / da waa ’er |
| district administration/s | قائمقامية / قائمقاميات | qaa ’im ma qaa mee yah /<br>qaa ’im ma qaa mee yaat |
| district administrator/s | قائم مَقام / قائم مقامين | qaa ’im ma qam / qaa ’im ma qaa meen |
| district council/s | مجلسْ القضاء | maj lis al-qa daa ’a |
| district/s | قَضاء / أقضية | qa Daa ’a / aq Dee yah |
| endowment/s | وقف / اوقاف | waqf / aw qaaf |
| federal parliament | البرلمان الإتحادي | al-bar la maan al-i ti haa dee |
| general director/s | مُديرْ عام / مُدراء عامين | mu deer a’am / mu da ra’a a’amin |
| general directorate/s | مُديرية / مُديرياتْ | mu dee ree yah / mu dee ree yaat |
| government/s | حُكومة / حُكومات | hu koo ma / hu koo maat |
| governor (old usage) | متَّصرّفْ | mu ta ser rif |
| governor/s | مُحافِظْ / مُحافظين | mu haa fiTH / mu haa fi THeen |
| identity card/s | جِنسيّات / جِنسّية | jin see yah / jin see yaat |
| inspection | تَفتيشْ | tef teesh |
| lease of government property | مُساطَحة | mu saa Ta ha |
| legislation | التَشريع | at-tash ree ’a |
| local government/s | الحُكومة المحلّية/ الحُكومات المحلية | al-hu koo mat / al-hu koo maat al-mahaliya |
| ministers/s | وَزير / وزراءْ | wa zeer / wu za ra’a |
| ministry/ies | وزارة / وزاراتْ | wa zaa ra / wa zaa rat |
| monitoring | *الرقابة* / مُرَاقبة | ar-ri qaa ba / mu raa qa ba |
| municipal council/s | المجلسْ البلدي/ المَجالسْ البلدية | al-maj lis al-ba la dee / al-majaalis al-baladeeyah |
| municipality/ies | بَلدية / بَلديات | ba la dee yah / ba la dee yaat |
| national budget | الموازنة الوطنية | al-mu wa za na al-wa Ta nee yah |
| national government | الحُكومة الإتحادية | al-hu koo mat al-i ti haa dee yah |
| national parliament | البرلمان الوطني | al-bar la maan al-wa Ta nee |
| neighborhood/s | حَي / أحياء | hay / ah ya’a |
| opinion/s | رأي/آراء | ra ai / araa |
| overseer/s | مُرَاقب / مَشرفْ | mu raa qib / mu shrif |

| English | Arabic | Transliteration |
|---|---|---|
| oversight | إشرافْ | ish raff |
| planning | التخطيط | at-taKH TeeT |
| province/s or governorate/s | مُحافظة / مُحافظاتْ | mu haa fa THa / mu haa fa THat |
| provincial council/s | مجلسْ المحافظة / مَجالسْ المحافظات | maj lis al-mu haa fa THa /<br>ma jaa lis al-mu haa fa THat |
| Shura Council | مجلسْ الشُورى/ مَجالسْ الشورى. | maj lis ash-shu ra |
| subdistrict administrator/s | مُدير ناحية/ مُدراء نواحي | mu deer naa hee yah / mu da r'aa na waa hee |
| subdistrict council/s | مَجلسْ الناحية / مَجالسْ النواحي | maj lis an-naa hee yah / ma jaa lis an-na waa hee |
| subdistrict/s | ناحية / نواحي | na hee yah / na waa hee |
| Supreme Court | المحكمة العُليا | al-mah ka ma al-'u lee yah |

## LAW NO. 21 OF 2008

June 1, 2008

In the name of the People[1]
The Presidency Council

Based on the approval of the Council of Representatives in accordance with the provisions of Article 61, "First," of the *Constitution*, and due to the elapsing of legal duration of time stipulated in Article 138, "Fifth-A," of the *Constitution*, the following Law was issued on March 19, 2008.[2]

Law of Governorates Not Incorporated into a Region[3]
No. 21 of 2008
Amended by Law No. 15 of 2010, approved by the Presidency Council on February 16, 2010.

1 Although most documents in the Muslim world begin with the formula "In the name of God, the merciful, the compassionate," Law 21 begins with a different formulation. This assertion that the law has been passed in the name of the people connects Law 21 to the idea of popular sovereignty intimated by some of the articles in the Constitution of 2005. The Iraqi Constitution, however, begins with the traditional Muslim formula: "In the name of God."

2 In Article 54, Law 21 expected the Council of Representatives (COR) to call provincial elections within 90 days of its passage. It also tried to enforce that timeline by imposing a deadline for elections to be held no later than October 1, 2008. However, elections were delayed until January 2009 and still have not been conducted for councils at the district or subdistrict level.

3 Article 116 of the Constitution describes the federal system as being composed of a capital, regions, and governorates, and Article 117 states that when the Constitution comes into force, the Kurdish provinces will constitute their own region. Article 119 further provides that one or more governorates shall have the right to organize into a region. At the present time, there is only one region within Iraq—the KRG. However, on September 7, 2010, Basrah's provincial council passed a resolution seeking to become a region of its own. Until such time as a referendum can be organized and the population can vote on its status, Basrah remains subject to Law 21. Kirkuk (Ta'meem) is the only province outside the KRG that is not currently subject to the law. It remains to be seen whether it will be joined to the Kurdish region or given the full status of a province. For the time being, Law 21 does not apply to Kirkuk, but still applies to Basrah.

## PREAMBLE

### ARTICLE 1:

The following terms shall have the meaning indicated opposite to each for the purposes of this law wherever they appear:

**The Law:** Law of Governorates Not Incorporated into a Region.[4]

**Council of Representatives:** Iraqi Council of Representatives.

**Governorate:** An administrative unit in its geographic boundaries consisting of *qada'as* (districts), *nahiyas* (subdistricts), and villages.[5]

**Council:** Governorate Council.

**Local Council:** qada'a council, nahiya council.

**Councils:** governorate councils, qada'a councils, nahiya councils.

**Administrative unit:** governorate, qada'a, nahiya.

**Head of an administrative unit:** governor, qada'a administrator (*qa'im maqam*), and nahiya administrator.

**Senior positions:** directors general and heads of security agencies, except university chancellors, judges, and army commanders.

**Absolute majority:** achieved with half plus one of the members.[6]

**Simple majority:** achieved with half plus one of the members present after a quorum is made.[7]

4 Although most commonly referred to in Arabic as Law 21, this law has been known by other, and sometimes confusing, names, such as the Provincial Powers Act (PPA) and the Provincial Powers Law (PPL). Both of these names can be misleading in that neither the words "province" nor "power" appear in the Arabic original. In addition, PPL is also a common name for the Prioritized Project Lists that are required by the Ministry of Planning (MOP) for investment projects requested from the Accelerated Reconstruction and Development Program (ARDP) fund.

5 The word "governorate," rather than the word "province," is a more accurate translation of the Arabic original محافظة (*muhaafatha*). The word is a derivative of the word محافظ (*muhaafath*), which is the person of the governor, and is itself derived from the root حفظ (*hafatha*), which means to preserve. The sense of the word is that a territory and the peace in that territory are being preserved by an executive officer, a notion supported by the reflection of the governor's traditional function of keeping the peace, found in Article 31, *Tenth*. Use of the word "province" with its associations as an administrative unit in the Roman Empire connotes far more autonomy from the center than does the word *muhaafatha*. Either word, "governorate" or "province," however, is preferable to the word "state," because that connotes a degree of sovereignty not enjoyed by the governorates in Iraq.

6 Absolute in this case means *all members*; therefore, an absolute majority is half of the total members of the council plus one.

7 A simple majority, in contrast, is half plus one of the *members present*, not of the total number of councilors. However, the members present must at least equal a quorum. The number constituting a quorum, although usually half of the total members plus one, must be a reasonable number and is decided upon by the council members and stated in each council's bylaws. For example, Ninawa's provincial council has a total of 37 members; however, 12 members do not attend, leaving only 25 members who attend on a regular basis.

# PART I
# THE COUNCILS[8] AND PROCEDURES FOR THEIR FORMATION

## ARTICLE 2:

**First:** The governorate council is the highest legislative[9] and oversight[10] authority within the administrative boundaries of the governorate[11] and shall have the right to issue local legislation within the boundaries of the governorate so that it can carry out its affairs on the basis of the principle of administrative decentralization and in a manner that would not contradict the *Constitution* and federal laws.[12]

**Second:** The governorate council and the local councils are subject to monitoring by the Council of Representatives.

## ARTICLE 3:

**First:**

1. The governorate council shall comprise 25 seats with the addition of one seat for every 200,000 inhabitants, if the number of the governorate's inhabitants exceeds 500,000.[13]
2. The qada'a council shall comprise 10 seats with the addition of one seat for every 50,000 inhabitants.
3. The nahiya council shall comprise seven seats with the addition of one seat for every 25,000 inhabitants.
4. Members of the council shall be elected by direct secret ballot in accordance with the election law for councils.

8 Law 21 has several antecedents, including laws formally abrogated by the passage and coming into force of this law. The most obvious of those laws include Law 159 of 1969 and the Coalition Provisional Authority (CPA) Order 71.

9 Notwithstanding the specific provisions of Law 21, the authority of provincial councils to legislate is a matter of keen debate. See Note 26, *infra*.

10 Although the governorate council is given authority to oversee and monitor—Article 7, *Sixth*—the governor is given authority to oversee and inspect. Article 31, *Fourth*. Compare Notes 30 and 58

11 The governorate council is one of several government actors operating "within the administrative boundaries of the governorate" as described by Law 21, Article 2, First. The existence of other actors within a governorate's boundaries requires a distinction between two types of government power: territorial and subject matter jurisdiction. Territorial jurisdiction is the power that a governing body has over a discrete geographical area. Subject matter jurisdiction is the power of a governing body over a particular responsibility of government or over another governmental department, possibly within the same geographical area. What is true of the departments is also true of the governorate council. It is only one of several government bodies operating "within the administrative boundaries" of a governorate, and at the present time, although the territorial jurisdiction of the council is identical to that of most of the departments, its subject matter jurisdiction is not.

12 This formula appears throughout Law 21. Governorate councils and their decisions are subordinate to the Constitution and central government law. This "other law" presumably includes decisions of the Supreme Court, the Council of Ministers, the Presidency Council, the Prime Minister, and most difficult for provincial councils to accept, the regulations and instructions of central government ministries.

13 The base number for each governorate is 25 seats. An additional seat will be added for every 200,000 inhabitants that exceed the base of 500,000. The eligibility for the additional seat can be established when a governorate proves through official census or other required methods (such as ration cards, Ministry of Planning records, or others) that its inhabitants exceed 500,000.

For example, if a governorate has 700,000 inhabitants, it would be eligible for one additional seat. Currently, the population of Baghdad is estimated at 6.5 million, which means the governorate council should have 25 (base) plus 33 (additional) seats, for a total of 58 seats; currently, Baghdad has 51 seats. With the exception of Baghdad, the other 14 governorates may have less than the 41 seats currently allocated to every governorate.

**Second:** The latest official census[14] shall be adopted to specify the number of seats to be added pursuant to Paragraph "First" of this Article.

**ARTICLE 4:**

The electoral term of the councils shall be four calendar years commencing with its first session.[15]

## Chapter 1
## Membership Requirements and Termination

### SECTION ONE
### MEMBERSHIP REQUIREMENTS

**ARTICLE 5:**

The candidates for the council membership shall meet the following:

**First:** Be an Iraqi citizen, fully eligible, and have attained 30 years of age at the time of candidacy.

**Second:** Hold, at the minimum, a secondary school certificate or its equivalent.[16]

**Third:** Be of good moral reputation and conduct and have not been convicted of a crime involving moral turpitude.[17]

14 Although the 2010 census was scheduled for October 24, it was postponed indefinitely. Among the reasons given for its postponement were a higher priority by the caretaker administration at the time in resolving the stalemate that had resulted from the national election held on March 7, 2010, and the formation of the government. Another issue of major concern was the status of Kirkuk (Ta'meem) province. It was expected that census takers in Kirkuk (Ta'meem) would possibly face armed opposition to getting an accurate count of the number of Kurds in the province, as that would likely determine whether the province would be divided or joined to the KRG. See Note 20, *infra*. As a consequence, elections in Iraq continue to be based on out-of-date census figures from before 2003.

15 The drafters of Law 21 required the national parliament to call for elections by no later than October of the year in which the law was passed (2008). However, the election for provincial councils was not held until January 2009, and the original Article 54 that called for elections within six months of passage of Law 21 was removed by amendment in 2010 (Law 15).

16 The Ministry of Higher Education and Scientific Research certifies academic credentials. Falsified credentials, nevertheless, remain a common accusation between political opponents; the lack of verifiable credentials was one of the major complaints against Salah ad Din province's first governorate council chairman, Ahmed Abdullah Abed al Jiboori (aka Abu Mazin). See Note 33 *infra*.

17 The second part of this provision connects moral reputation and conduct to court orders and convictions. According to the Iraqi Penal Code, dishonorable offenses are defined as follows:

Article 21–(1) (a): "Dishonorable offenses such as theft, embezzlement, forgery, breach of trust, fraud, bribery, and rape."

Article 23: "There are three categories of criminal offense: felony, misdemeanor, and infraction."

Article 25: "A felony is an offense punishable by one of the following penalties:

(1) Death
(2) Life imprisonment
(3) Five to 15 years imprisonment."

Article 26: "A misdemeanor is an offense punishable by one of the following penalties:

(1) Detention with hard labor or ordinary detention for a period of between three months and five years
(2) A fine."

Largely, the court record will be the basis for demonstrating good moral reputation and conduct.

**Fourth:** Be from the governorate according to the Civil Status Register,[18] or if originating from elsewhere, be a permanent resident therein for an uninterrupted[19] period not less than 10 years, provided that his residence is not for purposes of demographic change.[20]

**Fifth:** Not be a member of the security agencies or the armed forces at the time of his candidacy.

**Sixth:** Not be covered by the De-Ba'athification provisions and procedures or any other laws that replace them.[21]

**Seventh:** Not have illegally accumulated wealth at the expense of the national and public funds, according to a judicial decision.

## SECTION TWO
## TERMINATION OF MEMBERSHIP

### ARTICLE 6:

**First:** The membership of the councils shall terminate with the expiration of the electoral term or under the following conditions:

1. Death of the member, or his permanent disability, or a disability or a serious disease that prevents him from carrying out his responsibilities as a member, based on a decision from a specialized medical committee.
2. Resignation:
   A. The council member or the local council member may submit his resignation from the respective councils in writing to the council head [chairman]; the latter shall present it at the next session so that the council may decide on it.
   B. The resignation shall be considered accepted only if approved by the absolute majority of the council members or when he insists on his resignation even if the council rejects it by an absolute majority.
3. The member shall be considered removed if he fails to attend four successive sessions or a quarter of the total number of council sessions within a period of four months without legitimate reasons. In such cases, the council shall invite him to a hearing to be held at least seven days from the date of notification of the hearing. The council may consider him to be removed upon a decision taken by an absolute majority of the council members.

18 In reality, the جنسّية (*jinsiya*) or national identity card is the accepted evidence of residency. Birthplace in the governorate must be demonstrated and approved by the Civil Status Registry, or a candidate must demonstrate that he/she has lived in the governorate for a period of 10 years. The status can be confirmed through certification by the qada'a and nahiya councils, the current governorate council, or the مُختارْ (*mukhtar*) or alderman, as well as through the Civil Status Registry, which shows changes of physical location.

19 Citizens with dual nationalities cannot assume high profile positions, according to the Constitution, Article 18, *Fourth*.

20 "Demographic change" refers primarily to Kirkuk (Ta'meem) (see Article 140, *Second*, of the Constitution).The article states that there must be a normalization and census, concluding with a referendum in Kirkuk and other disputed territories to determine the will of their citizens, by a date not to exceed the 31st of December 2007. To date, the census in Kirkuk has not been taken, and therefore, no referendum has taken place.

21 De-Ba'athification of Iraqi Society (CPA Order 1 of May 2003), later annulled by the Accountability and Justice Commission Law 10 of 2008. The de-Ba'athification order was one of the grounds for removal in September 2009 of the first governor of Salah ad Din, Mutashar Hussein al Sammara'ee, who had been elected after implementation of Law 21.

Although individuals sentenced under the De-Ba'athification Law (CPA Order 1 of May 2003), or covered by the procedures before reaching a verdict, may have their sentences reduced or changed, they remain ineligible for election to councils.

If a candidate is covered by the De-Ba'athification Law, but was not sentenced or had not started the procedures before the dismissal of the law, then he/she is eligible for membership in the council.

4. The council may terminate the membership by an absolute majority if any of the conditions stated in Article 7, "Eighth," of this Law is met.
5. If he ceases to possess any of the membership requirements.

**Second:** The replacement upon the termination of the membership under conditions stipulated in this Article shall be from the same list,[22] if the elections are conducted in accordance with the list system, or by the candidate who obtains most of the votes in compliance with the applicable system of election.

**Third:** A member of the council may contest the membership termination decision before the Administrative Causes Court[23] within (15) days from his notification. The court shall decide on his challenge within 30 days from its filing with the court. The court decision shall be final.[24]

**Fourth:** The provisions of membership termination stipulated in this Article shall be applicable to the local councils.

## Chapter 2
## Competencies of the Governorate Council and the Local Councils

### SECTION ONE
### COMPETENCIES OF THE GOVERNORATE COUNCIL

#### ARTICLE 7:

The governorate council shall assume the following functions:

**First:** Elect the council head and his deputy by an absolute majority of the council members at the first session of the council called for by the governor within 15 days from the date of the certification of the election results. The session shall be chaired by the oldest member.

**Second:** Remove, upon the request of one third of the members, the council head or the deputy by an absolute majority of the council members in cases where one of the conditions stipulated in Paragraph "Eighth" of this Article has been met.

22 Two rounds of elections for provincial councils have taken place. The first round was held in January 2006, shortly after the 2005 adoption of the Iraqi Constitution, and well before the passage of Law 21 in 2008. Because of the level of violence at the time, candidates for elective office did not feel comfortable revealing their identities. As a result, most if not all candidates ran on so-called closed party lists. A party was assigned a number by the Independent High Electoral Commission (IHEC), and it was that number that appeared on campaign posters, in campaign advertising, and ultimately the ballot. After people went to the polls and the ballots were tabulated, the seats of a council were distributed based on the relative strength of the parties' showing. In other words, those parties that received the most votes were allowed to choose the most members from their party lists. This allowed party leaders to choose individuals from the top or the bottom of the list, as they felt necessary, because there were no individual candidates.

In contrast, Law 36 of 2008, the Provincial Councils Election Law, permitted a hybrid method of voting in which both open and closed lists were possible, and individual candidates felt comfortable enough to show their faces and their names in campaign posters. As a result, voters went to the polls and voted for individuals, along with, and maybe in addition to, numbered parties. This limited some of the discretion of party leaders in assigning individuals because the votes were tabulated by candidate as well as by party. This reference in Law 21 to "party list" requires that in the event a council member resigns or is removed, the individual who received the next most votes on the departing member's party list should fill the vacancy. This procedure is typical of a parliamentary system and preserves the relative party strength on a council by keeping constant the number of seats won at the general election.

23 Not the Federal Supreme Court.

24 Before being amended by Article 8 of Law No. 15 of 2010, Law 21 gave members 30 days to challenge their removal and left open the number of days allowed the court to issue a decision. The Article 8 amendment has decreased the number of days council members are allotted to object to their removal, and imposed a deadline on the court for the issuance of a ruling, presumably to increase certainty and discourage protracted removal disputes.

**Third:** Issue local laws, instructions, bylaws[25], and regulations[26] to organize the administrative and financial affairs so that it can conduct its affairs based upon the principle of administrative decentralization[27] in a manner that does not contradict the provisions of the *Constitution* and federal laws.[28]

25 On January 26, 2010, the Shura Council issued model bylaws for adoption by provincial councils. By that time, however, all provincial councils had bylaws of their own as required by this paragraph. Although cautioning the provincial councils that they are "subject to the Council of Representatives' monitoring," the Shura Council stated in Chapter VI, Article 34, of their model bylaws that standing committees shall "develop local legislation, decisions, and administrative orders" in apparent contradiction to their opinion of September 2009, stating that provincial councils lacked the authority to legislate because the word "legislation" was omitted from the notice requirement of council "opinions" and "decisions" in Article 12 of Law 21. See Note 26, *infra*.

26 The authority of provincial councils to issue legislation is in dispute. Although Article 2, *First*, of Law 21 declares the councils to be "the highest legislative . . . authority" and affords them "the right to issue local legislation" (provided that legislation does not "contradict the Constitution and federal laws"), the exercise of this legislative authority has been challenged. In September 2009, for instance, the Shura Council offered its opinion that provincial councils had no authority to legislate because Article 12 of Law 21 only obligated them to publish their opinions and decisions in a provincial gazette. Because the text of the law did not include an explicit mention of "legislation" along with "opinions" and "decisions," the Shura Council concluded that the councils lacked that authority. The opinion did not mention or distinguish Article 2, *First*, or Article 7, *Third*, which each suggest that provincial councils are empowered to issue local laws. On June 21, 2010, the legal committee of the Council of Ministers issued their own opinion, arguing that the provincial councils had not been given the authority to issue legislation, citing the Constitution and concluding: "Article 61, *First*, of the Iraqi Constitution defines the COR as the party in charge of enacting laws and legislation. This power also has been given to the regional authorities as stated in Article 121, *First*, but has never been given to authorities of provinces not incorporated into a region."

27 Article 116 of the Constitution describes the regions and provinces as being "decentralized," but Article 122, *Second*, qualifies the kind of decentralization in Iraq as "administrative."

Because the drafters of Law 21 qualified the type of decentralization, it can be concluded that they intentionally used the word "administrative" before the word "decentralization." Especially considering that each of the two references in the law occurs before a reiteration of the supremacy of (1) the Constitution and (2) Federal Law, "administrative" decentralization would be correctly understood as subordination of governmental bodies in the provinces to the central government.

That subordination is a starting point, however, and as Article 122, *Second* of the Constitution states that the provinces shall be regulated by law, the national government could alter or expand the authorities of the provincial councils, change their jurisdiction, and ultimately change the character of the decentralization they enjoy by changing the law. Such changes appeared to be happening in 2010.

On January 25, 2010, the Presidency Council approved Law 20 of 2010 that purported to devolve the Ministry of Municipalities and Public Works (MMPW) and transfer its staff, property, budget, and responsibilities to provincial governors. Then on February 16, 2010, the Presidency Council likewise approved Law 18 of 2010 that purported to dissociate the social affairs responsibilities of the Ministry of Labor and Social Affairs (MOLSA) and transfer them to the governors as well. Each of these two laws was identical in that each obligated the provincial councils to write local ordinances that reorganized the former ministry staff of the dissociated and devolved departments as now being under the jurisdiction of the governor's office. On May 25, 2010, Karbala province succeeded in completing a new, provincial structure for its department of Public Works, but on June 14 of the same year, the Supreme Court "froze" further implementation of Laws 18 and 20, and on July 15, 2010, declared both laws to be unconstitutional.

In holdings Number 43 and 44 of 2010, the Supreme Court concluded that the laws were unconstitutional because they originated in the national parliament (COR) itself and not with the Council of Ministers. In reaching his conclusion, Chief Justice Medhat al Mahmood repeated a distinction the Constitution makes between "draft" and "proposed" laws in Article 60. On his reading, the national parliament may "propose" but may not "draft" laws, and because Laws 18 and 20 had been drafted by the COR, rather than drafted by the Council of Ministers, the laws were void. Although his opinion left open the possibility that, once formed, a new government (i.e., a new Council of Ministers) could draft new "decentralization" legislation and introduce it to the parliament for passage, the ruling ended expansion of the jurisdiction of provincial elected officials for the time being.

28 Because Iraq's system of government is fundamentally a ministerial one, there is scarcely any aspect of life that is not the subject of a central government ministry and covered by a ministerial regulation. Such regulations can severely restrict the provincial councils and governors from exercising their authority. Recognizing this conflict between the competencies given to them by Law 21 and the apparently contradictory authority maintained by the central ministries, the Dhi Qar provincial council in southern Iraq submitted the issue to the highest ranking judicial authority for the resolution of constitutional disputes, the Shura Council. Unfortunately for the province, the Shura Council refused to hear their claim on the grounds that (essentially) the provincial council lacked "standing" to sue.

The Shura Council is a deliberative body within the Ministry of Justice, created by Law 65 of 1979, to resolve disputes of a constitutional nature between governmental entities. Although provincial and subprovincial councils existed at the time of the law's passage (such councils having been created by a law dating from 1969), they were not explicitly mentioned as within the Shura Council's jurisdiction in the 1979 law. Instead, the Shura Council was created to resolve

**Fourth:** Outline, in the development of the plans for the governorate, the general policies in coordination with the competent ministries.

**Fifth:**

1. Prepare the council budget to be included in the general budget of the governorate.
2. Approve the governorate draft general budget plan referred to the council by the governor, and transfer funds between its chapters with the approval of the absolute majority of the council members,[29] provided that the constitutional criteria shall be observed, and submit to the Ministry of Finance of the federal government to ensure its uniformity with the federal budget.

**Sixth:** Monitor all the activities of the local executive authority excluding the courts, military units, colleges, and institutes in order to ensure its good performance with the exception of offices under federal jurisdiction.[30]

**Seventh:**

1. Elect the governor and his two deputies by an absolute majority of the members within a maximum of 30 days from the date of its first session.[31]

disputes between governmental entities in which a ministry was a party. The law creating the Shura Council did not give it jurisdiction over the provincial councils at that time, and although the character of those councils has changed since ratification of the 2005 Constitution and Law 21, the law determining the jurisdiction of the Shura Council has not. In addition to lacking standing, the Dhi Qar provincial council also lacked a dispute. They were asking the Shura Council for an advisory opinion, not a ruling.

According to the jurisdiction statute of the Federal Supreme Court, Law No. 30 of 2005, it is the Supreme Court that is empowered to resolve conflicts "between the federal government, regional governments, provincial governments, municipalities, and local administrations." Raising doubt as to whether the provincial council is equivalent to the "provincial government" described in the Supreme Court's statute of jurisdiction, between August 16 and September 1, 2010, the Court refused to hear cases number 39, 54, 57, 58, 61, and 63, submitted to them by various provincial councils, encouraging the litigants to inquire of the Shura Council instead.

29 Law 21 gives the governorate council the authority to review, change, and transfer funds among chapters of the draft governorate general budget. The draft general budget includes budgets of the مُحافظة (*muhaafatha*) or governorate council, قضاء (*qada'a*) or district and ناحية (*nahiya*) or subdistrict councils, governor's office, and offices of heads of administrative units, قائم مقامين (*qa'im maqameen*). These are operating budgets only. Operating and capital budgets of the provincial level departments of the central government, such as the Ministry of Municipalities and Public Works (MMPW), are not included in the governorate general budget.

30 Because Article 24 describes the governor as "the highest ranking executive officer in the governorate," the power given to the governorate council in Article 2, *Sixth*, to "[m]onitor all the activities of the local executive authority," certainly includes the governor. That power is even more certain given its placement before paragraphs *Seventh*—"elect the governor" and *Eighth*—"question the governor," "remove" him, and "elect a new governor." But the councils' power over other executives outside of the governor's office—specifically the staff of central government ministries working in the same province—is less certain. While Article 2, *Sixth*, sounds comprehensive, the power it grants to monitor all executive activities comes with an exception.

"[O]ffices under federal jurisdiction" are specifically excepted from the councils' power to monitor. Although Law 21 does not make it clear, practice suggests that offices engaged in one of the exclusive powers of the central government, as defined in Article 110 of the Constitution, are excluded from scrutiny by the provincial councils. Offices engaged in activities described in Article 114 of the Constitution as "shared" with the central government may be subject to council scrutiny, and in practice, the councils' power to "[a]pprove the nomination of three" candidates for "senior positions" proposed by the governor and "relieve . . . senior officials" from their departments supports this interpretation.

31 Although Article 47 of the Iraqi Constitution makes reference to "the principle of separation of powers," the "branches" of government are not co-equal. In reality, the system of government described by the Iraqi Constitution is parliamentary or ministerial; it is not presidential. This means that (1) the executive branch is lead by a Prime Minister, who forms "the government" by choosing ministers with the consent of the national parliament, and that (2) the Prime Minister is himself selected from the membership of the national parliament.

Governors, like the Prime Minister, are chosen by the members of a council and not elected directly by the people, but the analogy ends there. Unlike a Prime Minister, a governor does not form a "government" for the province by nominating directors to head the provincial level departments of central government ministries (the way a Prime Minister chooses ministers). Instead, directors are appointed by the ministries and have "subject matter" jurisdiction separate from that of either the provincial council or the governor. See Note 11, *supra*.

2. If any of the candidates to these offices fails to win the absolute majority of the members, the candidates with the highest number of votes shall compete in a run-off ballot, and the candidate who wins the highest number of votes then shall be elected to the office.

**Eighth:**

1. Question the governor or one of his two deputies based upon a request from one third of the members. In case the simple majority is not satisfied with his answers, then his removal is put to vote at another session and he is deemed removed with the consent of the absolute majority of the council members. The request to remove or recommend his removal shall be based on one of the following exclusive causes:
   A. Lack of integrity or abuse of position
   B. Causing waste of public funds
   C. Loss of one of the membership requirements
   D. Willful negligence and dereliction of his duties.
2. The Council of Representatives may remove the governor by the absolute majority[32] of its members upon the proposal of the prime minister for the above stated reasons.
3. The governor shall be considered to be removed if he ceases to possess any of the requirements stipulated in Article 5 of this Law.
4. The governor may object to his removal decision before the Administrative Causes Court within 15 days from the notification of his removal. The court shall decide on his objection within one month from the date of its filing with the court. In such case, he shall continue to conduct the daily affairs of the governorate until his objection is decided.[33]
5. The governorate council shall, at the end of the challenge period referred to in Paragraph "Fourth" of this Article or when the removal decision is upheld by the competent court, elect a new governor within a period not exceeding 15 days.[34]

**Ninth:**

1. Approve the nomination of three out of at least five candidates proposed by the governor for the senior positions in the governorate by the absolute majority of the council members and the competent minister shall [appoint] one of them.

32 Since provincial councils elected governors by the terms of Law 21 in the late spring of 2009, removal proceedings have been started in Babil, Basrah, Muthanna, Ninawa, Salah ad Din, and Wasit, and the governors of Salah ad Din (September 2009 and again in October 2010), Wasit (September 2010), and Muthanna (January 2011) were removed from office. In the southern provinces, in every province except Basrah, the proceedings were initiated by Sadrist party council members against governors thought to be allied with the Law and State (old Dawa'a) party of Prime Minister, Nouri al-Maliki. In Basrah, the struggle was between members of the State of Law party. That most of these attempted removals had to do with national politics is proven by the fact that all of them were dismissed, and the governor of Wasit restored to his office after appeal to the Administrative Tribunal, once it was clear that Maliki would secure a second term as Prime Minister. On October 31, the Administrative Tribunal passed a verdict on the appeal made by the Wasit governor about his September 7, 2010, removal. The Administrative Tribunal ruled in favor of the governor and stated that the decision of the Wasit provincial council to remove the governor was illegal; they also stated that the corruption, cited by the provincial council as one reason for the removal, had occurred prior to the governor's term in office. Law 15 of 2010 (an amendment to Law 21 of 2008) states that the Administrative Tribunal has the power to rule on such cases and not the Federal Supreme Court (as originally stated in Law 21, 2008).

In Salah ad Din, however, the council has so far successfully removed two governors. The first governor of Salah ad Din province elected under Law 21 was Mutashar Hussein al Samara'ee of the al-Tawafeq party, and the first chairman of the provincial council was Ahmed Abdullah Abed al-Jiboori of the Iraqiya party. In September 2009, the council voted to remove Governor Mutashar and replaced him with a compromise candidate, Khalid ad Daraji, who was neither affiliated with one of the two major party lists, nor with the dominant al Jiboori tribe. He remained five months in office until November 2010, when Governor Khalid was also removed and, after a protracted dispute, replaced by Ahmed Abdullah Abed al-Jiboori (aka Abu Mazin).

33 Amended by Law 15 of 2010. In the 2008 version of the law, a governor challenged his removal by a governorate council before the Federal Supreme Court.

34 Added by Law 15 of 2010.

2. Relieve, by the absolute majority of its members, senior officials[35] in the governorate from their duties upon the request of one fifth of the council members or the governor in accordance with Paragraph "Eighth" of this Article. The Council of Ministers may also relieve the senior officials upon a proposal from the competent minister.

**Tenth:** Approve the local security plans submitted by the security agencies in the governorate through the governor in coordination with the federal security agencies with due consideration of their security plans.

**Eleventh:** Approve by absolute majority, upon the proposal of the governor, administrative changes to the qada'as, nahiyas, and villages[36] in terms of merger, creation and renaming, including the name of the center, and the consequential administrative formations within the boundaries of the governorate upon the request of the governor or one third of the council members.

**Twelfth:** Issue a gazette wherein the council's decisions and orders shall be published.[37]

**Thirteenth:** Select a logo for the governorate embodying its cultural and historical heritage.

**Fourteenth:** Approve a bylaw for the council within one month from the date of the first session.[38] The bylaw shall be approved by the absolute majority.

35 Senior officials are defined in Article 1 of Law 21 as "directors general and heads of security agencies, except university chancellors, judges, and army commanders."

Iraq's security agencies are: the National Intelligence Service (administered by the Council of Ministers), the military (administered by the Ministry of Defense), and the police (administered by the Ministry of Interior). Intelligence and the military are the exclusive jurisdiction of the federal government (Constitution, Article 110), and provincial authorities are explicitly excluded (Constitution, Article 31, *Tenth*, 1, and throughout Law 21). Therefore, "heads of security agencies" likely means only chiefs of police.

36 In parallel to the national parliament's authority to redraw the boundaries of provinces (Law 159 of 1969), this paragraph gives to governorate councils a similar authority to redraw the boundaries of the administrative units, (أقضية [*aqdiyah*] or districts and نواحي [*nawahi*] or subdistricts) within that province. They do not have any incentive, however, because council members are not elected from geographic constituencies. Without a political need to win votes, no direct jurisdiction over service delivery, and a limited ability to direct resources to the districts or subdistricts (via ARDP monies), councils are not very likely to change the administrative boundaries in their province any time soon.

The one major exception is Baghdad. Article 124, *Second*, of the Constitution obligated the national government to give the capital city a separate, legal character. A committee, under the direction of the Shura Council, has collected four competing versions of a capital law, but the differences between them remain unresolved. Although, like in other provinces, council members of the Baghdad governorate council are not elected from districts or subdistricts, the issue bearing on the delay in adopting a capital law is the question of where the geographical lines will be drawn between Baghdad city and Baghdad province. Unique in Iraq, Baghdad is the one city that has a separate government entity (in addition to the governor and governorate council) with its Amanat. The Baghdad Amanat, distinct from a provincial council, does exercise direct jurisdiction over basic services delivery—water, wastewater, garbage—within the territory of the city. Therefore, the crux of the dispute between the governor, the Baghdad governorate council, and the Amanat is where the territorial boundaries of that city will be drawn, or in the language of Article 124, *First*, "its municipal borders."

37 In September of 2009, the Shura Council issued an advisory opinion in which they concluded that because Article 12 of Law 21 imposed a notice requirement on governorate councils to publish their *ara'a* (opinions) and *qararat* (decisions), but did not explicitly reference nor include the word التَشريع *at-tashree'a* (legislation), that governorate councils, therefore, enjoyed no authority whatsoever to legislate. The notice requirement is for decisions and opinions, only. See Note 26, *supra*.

38 Bylaws are internal council regulations that are intended to help councils organize the work of the provincial council and its members' roles. Bylaws are frequently supplemented by detailed procedures and possibly bylaws of individual standing or ad hoc committees. The point of all these internal regulations is order and transparency, in that it makes the business of the council more conspicuous and better organized, given all the members know and follow the rules. Councils have made immense strides in improving the quality of official proceedings, in part due to the adoption of bylaws, and in large part due to experience. The often chaotic early meetings have become calm as council members have grown more secure in their positions and more certain of how business should be conducted.

**Fifteenth:** Identify the governorate's priorities in all fields and outline its policies and strategic development plans[39] in a manner that does not contradict with the overall national development.

**Sixteenth:** Approve by an absolute majority of the council members the acceptance or rejection of donations and gifts received by the governorate.

**Seventeenth:** Exercise any other competences stipulated in the *Constitution* or applicable laws.[40]

## SECTION TWO
## COMPETENCIES OF LOCAL COUNCILS[41]

### FIRST: Competencies of the Qada'a Council[42]

### ARTICLE 8:

**First:** Elect the head of the qada'a council by the absolute majority of the members of the council at the first session called for by the qada'a administrator within 15 days from the date of the certification of the elections results. The session shall be chaired by the oldest member.

**Second:** Remove the head of the qada'a council by the absolute majority of the members upon the request of one third of the members if one of the conditions stated in Paragraph "Eighth" of Article 7 of this Law is met.

39 The language of the law that requires a strategic plan for the province is general. In most provinces, however, "provincial development strategy" has come to mean a process and a document. The Provincial Development Strategy (PDS) process consists of three main phases: Phase 1: Formulation, Phase 2: Implementation, and Phase 3: Institutionalization. Each phase consists of several steps with specific outcomes. The PDS document articulates a community vision, priorities, objectives, and strategies to guide the planning and development of projects, programs, and other investments within the governorate. The PDS is *not* a list of specific projects or financial plans. The projects are developed subsequently during Phase 2: Implementation. To ensure Phase 3: Institutionalization, the process needs to continue with a functional analysis. It would determine required functions and corresponding units that need to be established within each branch, with clear roles and responsibilities to conduct, on a continuous basis, the required tasks for formulation, review, and implementation of the PDS. The Ministry of Planning supported the use of the PDS methodology, and the Ministry of Finance, in its 2007 budget circular, required the completion of PDS documents by all governorates. Although instructions issued by the ministries in subsequent years have not made the process mandatory, it has come to be the practice in all governorates, except Ninawa, which began working on a 20-year plan in 2010 that it has yet to finish.

40 Article 61 of the Iraqi Constitution states that the provinces shall be regulated by a law. That article expressly acknowledges the COR responsibility to regulate the provinces. The Constitution gives to the national parliament latitude to expand or contract the authorities of the provinces, and of course as the national parliament enjoys both territorial and subject matter jurisdiction over the provinces, they can change, amend, update, revise, or repeal the laws applicable to them. This is in conformity to the hierarchy of the laws established by the Constitution and the subordination of subnational administrative units to national ones.

41 Although there have been two rounds of elections for provincial councils and two rounds of national elections since the adoption of the 2005 Constitution, elections for district or subdistrict councils have never been held. This is in spite of a separation of provincial and subprovincial council elections into two stages by Article 6 of the Law on Provincial Elections of September 24, 2008: "Provincial council elections shall be held in the first stage, and district and subdistrict council elections shall be held in a second stage within six months after the date of holding the first-stage elections." Because provincial council elections were held in January 2009, district and subdistrict council elections should have been held by August of the same year, but they were not; elections for councils below the provincial level are not expected any time soon.

42 One of the more peculiar debates since the adoption of Law 21 has been whether it applied to district and subdistrict councils. The source of the difficulty was a line in the original Article 55, *First*, which provided that the law "shall be applicable . . . after the conducting of the next council elections." Because the drafter did not specify which council's elections, it was widely asserted that Law 21 only applied to provincial councils, because only provincial council members had been chosen by election in January 2009. According to this reasoning, CPA Order 71 still applied to the district and subdistrict councils. This reading fails to take into consideration that Article 53 of Law 21 "abrogates" prior law, and the *Fourth* paragraph specifically names CPA Order 71. Synonyms for "abrogate" are "annul," "officially abolish," and "repeal." Article 53 entirely abolished CPA Order 71. It ceased to exist, and not only for provincial councils but for all councils, whether or not elections are ever held. Therefore, in all 14 governorates not incorporated into a region, and not otherwise subject to a constitutional dispute (e.g., Kirkuk [Ta'meem]), Law 21 applies to provincial, district, and subdistrict councils. If that were not enough, Law 15 of 2010, the first amendment to Law 21, completely replaced the language of the original Article 55, but left the abrogation of CPA Order 71 in Article 53 intact.

**Third:**

1. Elect the qada'a administrator by the absolute majority of the members, and if any of the candidates fails to win the required majority, the candidates with the highest number of votes shall compete in the second ballot, and the candidate who wins the highest number of votes then shall be elected to the office.
2. Remove the qada'a administrator by the absolute majority of the members upon the request of either one third of the members or the governor based on any of the reasons stated in Paragraph "Eighth" of Article 7.

**Fourth:** Monitor the progress of the work of the local administration in the qada'a.

Local administration includes nahiya and beladiya councils; heads of local administration units include qa'im maqams and mudeers.

**Fifth:**

1. Prepare the qada'a council's draft budget.
2. Approve the budget plans of the qada'a offices and refer them to the governor.

**Sixth:** Approve naming of streets and planning of roads.

**Seventh:** Approve the basic designs of the qada'a in coordination with the governorate council and consistent with the general plans of the federal government.

**Eighth:** Monitor and evaluate the educational activities within the boundaries of the qada'a and submit relevant recommendations through the governorate council.

**Ninth:** Monitor and organize the utilization of public lands within the geographic location of the qada'a and endeavor to develop agriculture and irrigation.

**Tenth:** Approve the security plan presented by the heads of the local security agencies through the qada'a administrator.

**Eleventh:** Any other competencies delegated by the governorate council that would not contradict applicable laws.

**Twelfth:** Draft the bylaw of the qada'a council.

### ARTICLE 9:

The qada'a council, for successful performance, shall:

**First:** Present scientific studies and research for the development of the qada'a, and refer them to the governorate council.

**Second:** Cooperate and consult with the nahiya councils of the qada'a so as to ensure the welfare of the community.

### ARTICLE 10:

The heads of the administrative unit, heads of the security agencies, and the directors of offices shall have the right to attend the council's ordinary meetings as nonvoting members at the invitation of the council.

### ARTICLE 11:

In the event that the qada'a council's decisions are contrary to the governorate council's decisions, priority shall be given to the latter if the decision concerns the governorate in general.

**SECOND: Competencies of the Nahiya Councils**

**ARTICLE 12:**

The nahiya council shall assume the following functions:

**First:** Elect the head of the nahiya council by the absolute majority of the members at the council's first session called for by the nahiya administrator within 15 days from the date of the certification of the elections results. The session shall be chaired by the oldest member.

**Second:** Remove the head of the nahiya council by the absolute majority of the members upon the request of one third of the members if one of the conditions stated in Article 7, Paragraph "Eighth," of this law is met.

**Third**:

1. Elect the nahiya administrator by the absolute majority of the members, and if any of the candidates fails to win the required majority, the candidates with the highest number of votes shall compete in the second ballot, and the candidate who wins the highest number of votes then shall be elected to the office.
2. Remove the nahiya administrator by the absolute majority of the members upon the request of either one fifth of the members or the qada'a administrator based on any of the reasons stated in Paragraph "Eighth" of Article 7.

**Fourth:** Monitor the work of the local administration in the nahiya.

**Fifth**: Monitor the local offices and forward the necessary recommendations in this regard to the qada'a council.

**Sixth:**

1. Prepare the nahiya council's draft budget.
2. Approve the budget plans of the nahiya's offices and refer them to the qada'a council.

**Seventh:** Approve the local security plan submitted by the nahiya police through the nahiya administrator.

**Eighth:** Present scientific studies and research for the development of the nahiya, and refer them to the qada'a council.

**Ninth:** Cooperate and consult with the other nahiya councils of the qada'a so as to ensure the welfare of the community.

**Tenth:** Draft the bylaw of the nahiya council.

**Eleventh:** The governorate or the qada'a council may delegate any other competencies to the nahiya council in a manner that would not contradict applicable laws.

**ARTICLE 13:**

The nahiya administrator shall have the right to attend the nahiya council's ordinary meetings at the invitation of the latter, as a nonvoting member.

**ARTICLE 14:**

In the event that the nahiya council's decisions are contrary to the qada'a council's decisions, priority shall be given to the latter if the decision concerns the qada'a in general.

## SECTION THREE
## RIGHTS AND PRIVILEGES

### ARTICLE 15:

1. The members of the councils shall be free to express their opinions in the deliberations.
2. The councils may decide, by a majority of the members present, to deny a member from attending one or more sessions if his conduct in the council or his general conduct has brought discredit to the council in which he is a member.

### ARTICLE 16:

During their membership tenure, council and local council members shall be deemed members of the public service and are subject to the Penal Code.

### ARTICLE 17:

**First:** In return for his service in the council, the member of the council shall receive a monthly remuneration and allowances equivalent to that of a director general.

**Second:** In return for his service in the council, the member of the local council shall receive a monthly remuneration and allowances equivalent to a deputy director general.

**Third:** The provisions of this Article shall be applicable to the members of the councils who took up their positions after April 9, 2003.[43]

### ARTICLE 18:

**First:** The members of the council shall not be permitted to combine their council membership with any other official position, and shall have the right to resume their original employment upon the termination of their membership. The competent authorities shall facilitate the approval of the full-time service of the member to the council and his resumption of the original position upon the termination of his tenure of membership.

**Second:** The duration of the service in the council of a member shall be taken into account for the purposes of increment, promotion, and retirement.

**Third:**

1.
   A. Members of the councils, heads of the administrative units, and the two governor's deputies who took up their positions after April 9, 2003, shall be paid pensions no less than 80% of the monthly remuneration prescribed under this Law provided that the active service be no less than six months[44] or in the event they suffer a disability that prevents them from discharging their duties during their membership tenure.

43 According to this article, all individuals who have served on a council during the CPA administration, the Interim Iraqi Government, or subsequent governments for a period of six months shall receive pension benefits and allowances equivalent to 80% of their salary as a council member. See Note 84 *infra*

44 Amended by Law 15 of 2010. The period of service was originally "one year" but was reduced to "six months" by amendment and applies retroactively.

Following are the qualifying criteria for a pension (80% of the monthly remuneration prescribed under the Law of Governorates):

- Be a council member
- Be a head of an administrative unit (governor, qa'im maqam, mudeer nahiya)
- Be a deputy governor
- Serve at least a six-month employment term
- Took up the position after April 9, 2003
- Served at least a year or suffered a disability during the period less than a year.

Articles 17, "Third," and Article 18, "Third" (A), take effect immediately. All other provisions of the Law of Governorates are not in effect until governorate and local elections are held.

B. Members of the councils, heads of the administrative units and the two governor's deputies who assume their positions in accordance with this Law shall be paid pensions no less than 80% of the monthly remuneration prescribed under this Law after the termination of the electoral term or if they suffer a disability that prevents them from discharging their duties during their tenure.

2. The legal heirs of the members of the councils, heads of the administrative units, and the two governor's deputies, according to the *Unified Retirement Law*, shall receive the pension of the member in the event of his death or martyrdom during his membership tenure.

**ARTICLE 19:**

**First:** The quorum for sessions of the councils shall be met with the attendance of the absolute majority of the council's members.

**Second:** The decisions shall be taken at the sessions of the governorate council and the local councils by a simple majority unless otherwise stated.

**ARTICLE 20:**

**First:** The council and local councils shall be dissolved by an absolute majority of the members based upon a request of one third of the members under the following conditions:

1. Gross dereliction of duties and functions assigned to them
2. Contradicting the *Constitution* and laws.
3. If one third of the members no longer meet the membership requirements.

**Second:**

a. The Council of Representatives may object to a decision issued by the Governorate Council if it contradicts the Constitution or applicable laws. If the violation is not removed, the Council of Representatives may cancel the decision by a simple majority vote.

b. The Council of Representatives may dissolve the council by an absolute majority of its members based upon the request of the governor or one third of the governorate council members if one of the conditions stipulated above is met.[45]

45 Amended by Law 15 of 2010. The previous version allowed the COR to dissolve a governorate council. This version requires a two-step process in which the COR first objects and gives the council an opportunity to cure its objection before cancelling the decision. In this respect, it parallels the "veto" power afforded to the governor in Article 31, *Eleventh*. The grounds for objection—contravening the Constitution or other applicable laws—are also parallel.

**Third:**

1. The governorate council may dissolve a local council by an absolute majority of its members upon a request from the qada'a administrator, as regards the qada'a council, or the nahiya administrator, as regards the nahiya council, or one third of the local council members if one of the conditions stipulated above is met.
2. The dissolved council or one third of its members may contest the dissolution decision before the Federal Supreme Court within 15 days from the date of its issuance. The court shall decide on the challenge within 30 days from the date of receiving it.

**ARTICLE 21:**

**First:** In case the decision to dissolve the council is approved or the legal period of the contest expires, the governor shall call for the governorate council to conduct elections.

**Second:** The work of the council shall terminate on the date the competent court approves the decision of dissolution or the challenge period has elapsed and no challenge to the decision has been mounted. The head of the administrative unit shall conduct the daily affairs of the governorate until a new council is elected.[46]

**Third:** The provisions of this Article are applicable to the local councils provided that the call for new elections for the qada'a councils shall be made by the qada'a administrator and the call for the elections for the nahiyas shall be made by the nahiya administrator.

46 Amended by Law 15 of 2010. Although the Arabic original does not use the word "governor," the head of the administrative unit in this instance would be the governor, because the section concerns the dissolution of a governorate council.

# PART II
# HEADS OF ADMINISTRATIVE UNITS

### ARTICLE 22:

Each administrative unit shall have a juridical character[47] and financial and administrative independence. In the performance of its functions, it may:

**First:** Collect taxes, duties, and fees in accordance with the federal laws.[48]

**Second:** Exercise the competencies granted to it in accordance with the *Constitution*.

**Third:** Fulfill the duties and functions it is entrusted with in accordance with the laws and in a manner that will not contradict the *Constitution*.

### ARTICLE 23:

The governor and the qada'a and nahiya administrators are the highest executive employees in their respective administrative units and shall have authority over staff of each, and subject to the *Civil Service Law*[49] in terms of their rights and employment in a manner that would not contradict this law.

## Chapter I
## The Governor

### ARTICLE 24:

The governor shall be considered the highest-ranking executive officer in the governorate at the rank of a deputy minister as regards rights and service.

### ARTICLE 25:

1. The candidates for the position of the governor shall meet the requirements stipulated for membership of the governorate council and shall hold a university degree or its equivalent.
2. The requirement referred to in Paragraph "First" of this Article shall be applicable to the two deputy governors.

47 The legal personality afforded to the administrative unit of a province does not appear to be identical to that of a provincial council. In other words, provincial councils have not been recognized as provincial governments. Instead, they appear to be treated as one of several governmental bodies operating in the territory of a province. Their territorial jurisdiction may be the same, but the subject matter jurisdiction of those bodies remains separate. See Note 11, *supra*. This distinction explains why the Federal Supreme Court could refuse to hear cases from provincial councils between August and September of 2010, despite a grant of authority to resolve disputes between the "central" and "provincial governments" in its statute of jurisdiction, Law 30 of 2005. See Note 29 *supra*. It also explains why the Nongovernmental Organization Bureau could refuse to recognize the Iraqi Local Government Association (ILGA) as a parastatal organization, because its constituent members, the provincial councils themselves, were deemed to lack legal personality and, therefore, the legal capacity to constitute an organization. So, while the Supreme Court recognizes the legal personality of the provincial council because it is one of the several government bodies operating in the territory of the province, the Court does not consider the provincial council to be an aspect of or an equivalent of the provincial government.

48 Whatever the drafters of Law 21 anticipated as being the authority of provincial councils to collect taxes, the central government has consistently denied provincial councils that ability. Since the restoration of sovereignty in 2004, each Prime Minister has denied provinces the authority to collect taxes. In addition, in July 2010, the Council of Ministers' legal committee stated that Basrah provincial council was not within its rights in attempting to impose a surcharge on the issuance of passports and national identity cards because the Constitution, in Article 28, *First*, states that no such tax shall be imposed "except by law." The denial of taxation by successive Prime Ministers and the Council of Ministers Secretariat (COMSEC) notwithstanding, shortly after Law 21 had been adopted but before it had been implemented, the Supreme Court issued an advisory opinion, No. 16, recognizing the authority of provincial councils to raise local revenues. It is perhaps significant that the question was presented to the court by Najaf province, where at least one form of tax seems to be imposed without central government challenge. That is a pilgrims' tax on religious tourists, something formally recognized in Article 2, *Second*, of the annual, national budget law, No. 10 of 2010. A similar provision is to be found in the draft budget law for 2011.

49 Law No. 24 of 1960, as amended.

**ARTICLE 26:**

**First:** The appointment of the governor shall be under a republican decree[50] issued within 15 days from the date of his election, and he shall commence his duties from the moment of his appointment.

**Second:** The governorate council may elect the governor from within or outside the council.[51]

**ARTICLE 27:**

**First:** Each governor shall have two deputies[52] elected by the council. Their orders of appointment shall be issued by the governor within 15 days from the date of their election by the council. Each of the deputy governors shall hold the rank of director general and they may be elected from within or outside the council.

**Second:** Each deputy shall be required to meet the requirements for membership of the governorate council stipulated in Article 5 of this Law and shall hold a university degree.

**ARTICLE 28:**

If the governor fails to fulfill his duties for reasons of health for a period exceeding three months, he shall be superannuated and the council shall elect a new governor pursuant to Paragraph "Seventh" of Article 7 of this Law, and the governor's first deputy shall be the acting governor until such election is conducted.

50 Law 159 of 1969 granted the provinces extensive authorities, including security, public services, the protection of freedoms and properties, and even controlling the borders and the agreements related to them, because the governor used to bear the title of مُتَصرّفْ (*mutaserrif*). The term *mutaserrif*, current until 1969 and the implementation of Law 159, was an approximate synonym of the term governor, our current term. According to the Provinces Administration Law No 58 of 1927, the *mutaserrif* was in charge of various affairs in the province. During the era of dictatorship, however, the central government gradually began to take away the provincial powers until the governor was merely an employee who followed the orders and prohibitions of the central government with regard to provincial affairs. After the fall of the regime in 2003, the demands for decentralization, and the desire to award the provinces with extensive authorities, returned to the political forefront. Provincial council elections were held, and it was intended for those councils to handle the function legally entrusted to them and according to the Constitution

51 Law 21 required that the provincial councils choose a governor within 30 days of their first session. Due to the number of challenges to the results of the elections in January 2009, several councils were not finally seated until April, resulting in the process of governor selection not being concluded until May.

52 Although the law authorizes the governor to have two deputies, it does not designate the priority relationship between them. In other words, the law does not specify that one is to be the "first deputy" and the other the "second deputy." More than just a problem of semantics or of status, this absence of distinction opens the way to a succession crisis if a governor is incapacitated.

On December 30, 2009, a car bomb exploded near the police station and government building in Ramadi, the provincial seat of Anbar province. Following the blasts, the governor, his top security advisor, and several provincial council members went outside the building to inspect the site of the blast. A man in a uniform walked up to them and detonated a concealed suicide vest. The second blast killed the security chief and one provincial council member and caused serious injury to the governor himself. The governor was medevaced out and surgery performed to try to save his hand, but in his absence, the law left it unclear who was to rule. Although the governor of Anbar had two deputies, each had the same status as the other, leaving it to the provincial council to decide which of the two men should temporarily assume the duties of governor, and possibly the full responsibilities should the governor die or not be able to return to work. Although the council and deputies reached an amicable solution, with the Deputy for Technical Affairs becoming acting governor rather than his colleague, the Deputy for Administrative Affairs, the absence of a clear order of succession forced the issue to be resolved by a political process rather than a legal process. Had the province been experiencing a widespread security crisis, for instance, or had the two deputies been political rivals, the succession question could have destabilized the province.

**ARTICLE 29:**

The heads of administrative units, the two deputy governors, and the head and members of local councils shall take the following oath before the highest provincial judiciary authority before assuming their duties: "I swear by Allah the Almighty to sincerely safeguard the federal republican system, guard the public interest and the safety of the homeland, uphold the Constitution and the law, and discharge my duties sincerely, faithfully, and impartially, and may Allah be my witness."[53]

**ARTICLE 30:**

The governor, his two deputies, and the heads of the administrative units shall continue to discharge their daily responsibilities after the expiration of the electoral term of the councils until their respective successors are elected by the new councils.[54]

**ARTICLE 31:**

The governor shall exercise the following powers:

**First:** Draft the general budget of the governorate[55] in accordance with the constitutional standards, except for those which fall within the jurisdiction of the federal government, and submit the budget to the governorate council.

**Second:** Execute the decisions of the governorate council[56] as long as they are consistent with the applicable laws and the provisions of the *Constitution*.

**Third:** Execute federal general policy within the boundaries of the governorate.[57]

53 (Amended by Law 15 of 2010.) As in Article 21, the use of "head of the administrative unit" here refers to the governor. Although the text of the oath prescribed was not changed, the number of elected officials expected to take it expanded from just the governor and his two deputies to include all council members and their corresponding executives, the مُديرْ ناحية (*mudeer nahiya*), and the قائم مقام (*qa'im maqam*).

54 Legally, a province can have only one governor at a time. Since coming into force, Law 21 has been tested on this principle in three different ways. The first way this principle was tested, in the spring of 2009, was after the last round of provincial elections, when outgoing governors continued in office until the new councils could choose new ones. This is remarkable, given an average turnover rate of over 80% of council members. The second test occurred as a result of the incapacitation of the governor of Anbar by a would-be assassin in December 2009. That attempt on the governor's life sent him to the hospital and put the province into a brief succession crisis until one of the two deputy governors could be elevated by the provincial council. See Note 52 *supra*. Following the governor's convalescence, however, he returned to his duties and the deputy to his, without controversy. The third way the principle has been tested involved removal proceedings. The most complicated of these proceedings took place in Salah ad Din province. Here, one governor, who had been formally removed by the council but had appealed; a replacement governor, designated by the governorate council; and eventually a military officer sent from Baghdad, all claimed the governor's office at the same time.

55 The law gives the governor responsibility for preparing the general budget and for submitting it to the provincial council. The above suggests that the governorate is one government body with jurisdiction over the entire province, but the budget that the governor prepares is only the operations budget for the provincial council and the governor's office (GO), plus a so-called capital budget or investment budget used for mini projects executed by the GO and known as the Accelerated Reconstruction and Development Program (ARDP).

56 Article 2 gives the provincial council the authority to legislate and "issue" local laws. Article 12 obligates the provincial council to publish its "decisions" and "opinions" in a provincial gazette. See Note 26, *supra*. Article 31 only obligates the governor to enforce the decisions of the council and makes no mention of either "legislation" or "opinions." The qualification on the governor's obligation to execute decisions of the council—that they are consistent with the Constitution and other applicable laws—is consistent with the supremacy clause of the Iraqi Constitution—Article 13, *First*—as well as with the council's obligation to conform to higher order laws in Article 2, *First*, and the Council of Ministers' authority to object to decisions of the provincial council in Article 2, *Second*.

57 This obligation extends from the era of Ba'athist control in which the governor bore overall responsibility for central government policies and execution of decisions within the province.

**Fourth:** Oversee and inspect[58] public facilities in the governorate except for courts, military units, universities, colleges, and institutions.

**Fifth:** Represent the governorate at the conferences, symposia, and general forums to which he is invited and which are relevant to the governorate affairs and local administrations. He may delegate any of the governorate employees to carry out these functions in accordance with the law and applicable rules and regulations.

**Sixth:** Establish universities, colleges, and institutes in the governorate in coordination with the Ministry of Higher Education and Scientific Research within the governorate budget and with the approval of the council by an absolute majority of the council members.

**Seventh:**

1. Issue official letters of appointment for local employees in the governorate from grade 5 and below[59] in the employment scale stated in the *Federal Civil Service Law* upon the recommendations of the offices concerned and in accordance with the staffing plan approved by the council.
2. Appoint local employees in the governorate on a permanent basis from grade 4 upward in the employment scale stated in the *Federal Civil Service Law* except for the senior positions upon the recommendations of the offices concerned and in accordance with the guidelines prepared by the council.

**Eighth:** Take legal and administrative measures against the directors general and employees[60] in the governorate with the approval of the council by a simple majority.

**Ninth:**

The governor may:

1. Order the police to investigate the crimes that take place within the administrative boundaries of the governorate according to the law and to present the investigation reports to the concerned judge, provided that the governor has been informed of the investigation outcome.
2. Establish or abolish police stations with the approval of the council by the absolute majority of the council members in accordance with the relevant laws and guidelines of the Ministry of Interior.

**Tenth:**

1. The governor shall have direct authority over the local security agencies and all authorities tasked with protection duties relating to peace and order within the governorate, except for the armed forces (army units).
2. If the governor is convinced that the security agencies in the governorate are unable to fulfill their duties in maintaining peace and order on account of insufficient numbers, he shall promptly inform the Minister of Interior with a recommendation as to the size of the numbers required to fulfill their responsibilities.

58 In this paragraph the governor is given arguably more power over public facilities than the provincial council. The council is instructed by the law to "monitor," and the local executive, according to Article 76—the governor—is given the authority to "oversee and inspect." In practice, provincial councils have exercised an authority to inspect, frequently paying visits to the locations of investment projects. Complicating matters, the Arabic terms for monitoring and oversight (الرقابة [*riqaba*] and إشراف [*ishraff*]) are not clearly distinguished in meaning. What appears clear, however, is that the governor, as chief executive, inherently bears responsibility for ensuring that both the decisions of the provincial council and the decisions of the central government are enforced, and that enforcement implies a responsibility to inspect.

59 Law of Public Sector Salaries, No. 22 of 2008, rescinded CPA Order 30 of 2003, and included a revised schedule of grades.

60 At the provincial level, several government bodies are operating with concurrent territorial jurisdiction but separate subject matter jurisdiction.

**Eleventh:**

1. The governor shall have the right to object[61] to the decisions of the governorate council or the local council in the following cases:
   A. If they contradict the Constitution or applicable laws
   B. If they are not within the competence of the council
   C. If they contradict the general plan of the federal government or the budget.
2. The governor shall communicate to the council concerning the reasons for his objection together with the decision of the council within 15 days of the notification of the decision.
3. If the council concerned affirms its decision or amends it without removing the violation communicated by the governor, the matter shall be referred to the Federal Supreme Court for conclusive decision.

## ARTICLE 32:

The ministries and offices not affiliated with ministries shall notify the governor of their correspondence with their offices and public utilities within the governorate so that the governor may monitor the implementation of the instructions in such correspondence. The heads of the offices and public utilities in the governorate shall abide by the following:

**First:** Notify[62] the governor of official correspondence with their respective offices.

**Second:** File reports to the governor on matters that he has referred to them.

**Third:** Notify the governor of their activity on matters that relate to security and important issues as well as on matters that relate to more than one office within the governorate or the conduct of their personnel.

**Fourth:** Notify the governor when they commence and end their work.

**Fifth:** Fulfill the functions that the governor assigns and the work of the committees that the governor requires to be formed.

## ARTICLE 33:

**First:** The governor shall have a maximum of five assistants[63] for administrative and technical affairs and they shall fulfill the tasks assigned by the governor and work under his supervision and guidance.

**Second:** The assistants shall have at least 10 years of experience in their specialization and shall meet the requirements stipulated for deputy governors.

**Third:** The assistants shall hold the rank of deputy director general.

61 Though given responsibility to execute the decisions of the provincial council by Article 31, *Second*, the governor retains discretion to exercise his best judgment and can object to decisions that he finds violate the Constitution or other applicable laws, or are outside the subject matter jurisdiction of the council. Interestingly, only the decisions of the council are referenced. Notwithstanding, this paragraph has been understood by provincial councils to outline a legislative process in which the governor either approves of legislation or essentially vetoes it by filing his objections, thereby setting in motion a process by which the council can amend their legislation to conform to the governor's objections, or in the absence of resolution, refer the matter to the Supreme Court.

62 This paragraph imposes a notice requirement on ministerial departments in the provinces over the performance of their duties, but does not involve submitting to the governor's jurisdiction. Presumably, routine correspondence within the department or between a department head and his superiors in Baghdad would not be shared with the governor, only notice of the communication would be. To obtain detailed information as to department business, the law places an affirmative obligation on the governor to request it.

63 Law 21 provides for a staff of five assistants for administrative and technical support, without specifying their expertise.

**ARTICLE 34:**

**First:** An advisory board consisting of not more than seven advisors[64] specialized in legal, technical, and financial affairs chosen by the governor shall be formed in each governorate. The advisory board shall report directly to the governor and shall function under his supervision and guidance.

**Second:** The advisors shall have 10 years of experience in the areas of their specialization. Each of them shall hold the rank of assistant director general.

Third: The board referred to in Paragraph "First" of this Article shall assume the responsibility of studying matters referred to it by the governor, each according to his area of specialization, and shall submit relevant written recommendations.

**ARTICLE 35:**

The governor may delegate some of his powers to his deputies and assistants. The governor shall not delegate powers exclusively vested in him.

**ARTICLE 36:**

The services of the governor's experts of the advisory board, assistants, and heads of administrative units who are permanent public employees shall be transferred to the staff of the administrative units in which they are elected or appointed for such positions for the duration of their tenure.

**ARTICLE 37:**

First: The governor, his two deputies, and heads of administrative units may submit their resignation to the councils that elected them. The resignations are deemed accepted as of the date of their submission.[65]

**Second:** Their replacements shall be elected pursuant to the procedures stipulated in this Law.

These procedures are stipulated in the following articles of the Law of Governorates:

- Article 5
- Article 8, "Third"
- Article 12
- Article 25
- Article 26.

**ARTICLE 38:**

The provisions for removing the governor stipulated in this Law shall be applicable to the two deputies of the governor.

64 In addition to the five assistants accorded to the governor, he may also appoint up to seven advisors, specialized in areas of the governor's choosing. This advisory board can change composition and specialties as required. Both the assistants of Article 33 and the advisors in Article 34 must be included in the governor's operations and maintenance budget to be paid. Because the operations and maintenance (O&M) budget was due to the Ministry of Finance shortly after councils were seated and governors selected in 2009, very few governors' offices had a full complement of assistants and advisors in 2010 because they had not been included in the budget.

65 Three southern provinces of Iraq have recently experienced political turmoil, two of them directly as a result of recent political demonstrations, which have been popularly described as "Days of Rage." The three governorates are Babil, Basrah, and Wasit. In each governorate, the governor has been replaced or is in the process of being replaced.

## Chapter 2
## Qada'a and Nahiya Administrators

### ARTICLE 39:

**First:** The qada'a and nahiya administrators are the highest executive employees in their administrative units to be elected in accordance with Paragraph 3 of Articles 8 and 12 of this Law.

**Second:** The qada'a and nahiya administrators are required to meet the conditions stipulated for the governorate council member in Article 5 of this Law and hold a university degree.

**Third:** The governor shall issue an official letter of appointment to the qada'a and nahiya administrators, who shall be under his guidance and supervision.

**Fourth:** The qada'a administrator holds the rank of director general and the nahiya administrator holds the rank of deputy director general.

### ARTICLE 40:

**First:** In the absence of the qada'a administrator, the governor shall assign the administrator of a nahiya affiliated to the qada'a to function in his place.

**Second:** In the absence of a nahiya administrator, the qada'a administrator shall assign the administrator of a nahiya affiliated to the qada'a to function in his place.

**Third:** The qada'a administrator shall notify the governor and the nahiya administrator shall notify the qada'a administrator of their absence sufficiently in advance so that the governor may appoint a replacement for the duration.

### SECTION ONE
### POWERS OF THE QADA'A ADMINISTRATOR

### ARTICLE 41:

The qada'a administrator shall exercise the following powers:

**First:** Execute the decisions of the qada'a council that are consistent with the Constitution and applicable laws.

**Second:**

1. Directly supervise and inspect the public offices in the qada'a and their employees excluding the army, courts, universities, and institutes and to impose legally sanctioned punishments on the violators with the approval of the qada'a council.
2. The qada'a administrator may order the police to investigate the crimes that take place within the boundaries of the qada'a and to present the investigation reports to the investigative judge concerned, and must be informed about the investigation outcome.

**Third:**

1. Maintain security and order and protect citizen's rights, lives, and property.
2. Preserve the rights and public property and collect the revenues in accordance with the law.

**Fourth:** Prepare the draft budget of the qada'a and submit it to the qada'a council.

**Fifth:** When necessary, the qada'a administrator may order police patrols and posts to be established on a temporary basis within the qada'a in order to maintain security.

**ARTICLE 42:**

The heads of government offices within the governorate shall submit to the qada'a administrator, where they are relevant to the qada'a concerned, copies of their communications and decisions to their respective branch offices so that the qada'a administrator may follow up on the actions taken.

## SECTION TWO
## POWERS OF THE NAHIYA ADMINISTRATOR

**ARTICLE 43:**

The nahiya administrator shall exercise the following powers:

**First:**

1. Directly supervise and inspect the public offices in the nahiya and their employees, but excluding the army, courts, universities, and institutes.
2. The nahiya administrator may order the police to investigate the crimes that take place within the boundaries of the nahiya and to present the investigation reports to the investigative judge concerned. The nahiya administrator shall be informed of the investigation findings.

**Second:**

1. Maintain security and order within the boundaries of the nahiya.
2. Preserve the rights and public property and collect the revenues in accordance with the law.

# PART III
# FINANCIAL RESOURCES

## ARTICLE 44:

The financial resources of the governorate shall consist of the following:

**First:** The budget transfers to the governorate from the federal government[66] in accordance with the constitutional criteria prepared by the Ministry of Finance and approved by the Council of Representatives.[67]

**Second:** Revenues[68] generated from the governorate services and investment projects.

**Third:** Proceeds[69] from taxes, duties, and local fines in accordance with the Constitution and the applicable federal laws.

66 Almost all the money received by a provincial council and provincial governor comes from the central Ministry of Finance, from the federal government.

67 Article 80, *Fourth*, of the Constitution obligates the Council of Ministers to introduce a draft budget to the national parliament, and Article 57 requires the parliament to pass a budget before it can recess its second of two annual sessions. In reality, the draft budget is prepared by the Ministry of Finance, and rather than form a permanent "ways and means" committee, the national parliament forms an ad hoc committee to review and comment on the draft. The chairman of the Ad Hoc Committee reviewing the 2011 budget is Sheikh Khalid al Atiyah of Diwaniyah. The process of preparation and review is set out in CPA Order 95, one of the very few U.S.-era laws not to have been replaced with Iraqi legislation. Even though Order 95 requires budgets for the following year to be passed before the end of the current one, in practice, this deadline has never been met. Instead, annual budget laws are usually passed sometime within the first quarter of the budget year (although they have been as late as the second quarter). In the period of deliberations over the budget, government expenses are paid on the basis of a "continuing resolution" or 1/12 of the prior year's budget, in order to maintain salaries and basic operating expenses. Once passed, the approved annual budget is elaborated with instructions published by the Ministry of Finance, usually within the second quarter of the budget year. Both the budget law and the ministry's instructions are binding on the provinces and provincial councils, but the most pressing obligation for elected officials at the provincial level is the deadline for submission of their O&M budgets. It bears repeating that the provincial councils and governors are each responsible for preparing an operating budget, which mostly comprises salaries. They do not prepare the budgets for ministerial departments operating in the provinces. In each of the years since Law 21 has been in force, the deadline published by the Ministry of Finance for preparation and submission of O&M budgets has been short. In the summer of 2009, it was literally 24 hours; on June 17, 2010, the ministry issued instructions for the implementation of the 2010 budget law, setting June 30 as the deadline for submissions from the provinces. Because budget formulation is a process, councils should know to begin preparing their budgets for the subsequent year as soon as they have closed the books on the one just concluded. For instance, the 2010 final reconciliation is due to the ministry by January 31, 2011. From February 2011, a council should be at work preparing its submission for 2012.

68 Although the law contemplates resources coming into the provinces from both central and local sources, the overwhelming majority of money spent on operations and capital projects comes through the central government budget.

69 Despite the clear grant of authority to receive proceeds from taxes, duties, or fines, to date, provincial councils and governors have been prevented from officially collecting them. Despite an advisory opinion of the Supreme Court, Number 16 of 2008, which interpreted the law as allowing provincial councils to impose taxes, that anticipated power has been consistently denied by Prime Ministers and the Ministry of Finance since the implementation of Law 21 and since sovereignty was returned in 2004. Consequently, there is no clear procedure for how to impose, collect, or spend local revenues. Moreover, the Ministry of Finance has placed impediments in the way of provinces that attempt to open provincial bank accounts.

The appointment of a special commission is called for in the Constitution, Article 106: "A public commission shall be established by a law to audit and appropriate federal revenues. The commission shall be composed of experts from the federal government, the regions, the governorates, and its representatives." That commission has not yet been appointed. Further legislation detailing revenue is likely to be required. Currently, numerous provinces generate revenue on their own through fees for services and other transactions, such as the revenue generated from religious tourism in Najaf. In addition, annual budget laws, such as those of 2010 and the draft 2011 budget law, have provided for additional revenues, including formally approving the religious tourism tax for any province affected by such tourism, and shares of oil revenues for provinces where oil is produced and refined.

**Fourth:** Donations and gifts[70] that may be received by the governorate in a manner that would not contradict the Constitution and the applicable federal laws.

**Fifth:** Proceeds from the sale and lease of public movable[71] and immovable assets in accordance with the Law on Sale and Lease of Public Properties and other applicable laws.

70 Revenues from holy shrines and other endowed properties stay with the shrines' trustees (not in the federal treasury). These endowments are known as أوقاف (*awqaaf*). However, donations and gifts that each province collects are transferred to the federal treasury, according to Budget Law Number 10, Articles 1 and 3 (2010).

71 A major question of title stands before the provincial councils in the exercise of this paragraph. Because the governor was formerly an employee of the Ministry of Interior, government properties that were controlled by the governor may still belong to that ministry. Sales and property laws are governed by Law 32 of 1986.

## PART IV
## FINAL PROVISIONS

### ARTICLE 45:

**First:** A high commission for coordination between the governorates[72] headed by the Prime Minister shall be formed and shall include as members the governors. This commission shall specialize in reviewing the affairs of the governorates, their local administrations and means of coordination between them, and shall address problems, obstacles that it faces, and common issues between the governorates.

**Second:** The commission shall meet at the invitation of its head every 60 days or when necessary.

**Third:** The head may invite those whose presence is required and necessary for the commission meetings.

### ARTICLE 46:

The governorate council and administration shall adopt recognized accounting systems.[73]

### ARTICLE 47:

The governorate offices and councils shall together be subject to monitoring and auditing of the Supreme Audit Board and branches of the independent commissions formed in accordance with the constitutional provisions.[74]

### ARTICLE 48:

The period of real service of the governor, his two deputies, his assistants, his advisors, and the heads of the administrative units shall be taken into consideration for the purposes of increment, promotion, and retirement.

### ARTICLE 49:

Rescinded[75]

72 The commission contemplated by the drafters of Law 21 would operate like a governors' club under the direction of the Prime Minister. Although the law anticipates periodic meetings every 60 days, in practice, the commission has met whenever the Prime Minister has decided it was necessary. Since 2009, there have been three such meetings. The first was an informal governors' meeting held in July 2009, to take steps towards organizing the commission and a Secretariat. The subsequent organization conference was then held in January 2010 in Wasit, during which the commission was formally announced and the Minister of State for Provincial Affairs at the time, Khulood al Majoon, was designated as its head. The commission never met again in 2010. After a new government was formed in December 2010, however, a new Minister was named: Turhan Abdullah, a Turkoman member of the Kirkuk (Ta'meem) provincial council. Although the Minister of State for Provincial Affairs currently has no rule-making authority and an inadequate professional staff, he may perhaps be able to revive the commission and realize its purpose under Article 45. Hopes were raised when the Commission met again in January 2011.

73 The Ministry of Finance specifies what constitutes recognized accounting systems.

74 According to Article 100, *First* and *Second* of the Iraqi Constitution, the Supreme Audit Board (SAB) is an independent federal entity under the national parliament (or Council of Representatives). The amended Board Law 6 of 1990 organizes its functions of auditing the legitimacy of public spending and evaluating the performance of public administrations, including the ministries' departments in the provinces. Provincial councils have no power over the SAB, and they cannot interfere with its audit plans and programs. After conducting audits, the SAB submits reports with their findings to their president.

75 Previously, Article 49 obligated council members and the corresponding executives of the *qada'a* and *nahiya* councils to take the same oath as prescribed for the governor and his two deputies in Article 29. Law 15 of 2010 amended Article 29 to include all in the same article, removing the necessity of a separate requirement in Article 49.

**ARTICLE 50:**

The council and the local councils shall authenticate the membership[76] in the respective councils by absolute majority of the members within 30 days of the date of the first session.

**ARTICLE 51:**

Every removal or relieving of duties referred in this Law shall be preceded by a hearing[77] for the individual concerned.

**ARTICLE 52:**

The budget allocated to the governorate[78] from the federal budget shall be submitted directly to the governorate by the Ministry of Finance after subtracting the strategic expenditures.[79]

**ARTICLE 53:**

The following shall be abrogated:[80]

**First:** The Governorates Law No. 159 of 1969 as amended.

**Second:** The Law on Peoples' Councils No. 25 of 1995 as amended.

**Third:** References to the formation and competencies of the municipal councils in the revised Law of the Municipalities Administration No. 165 of 1964.[81]

**Fourth:** Coalition Provisional Authority Order No. 71 of April 6, 2004, as amended.

**Fifth:** Laws, regulations, and decisions that contradict with the provisions of this Law.

76 Usually, the authentication (eligibility for the position) should be completed by the Independent High Electoral Commission (IHEC) during the election process. In their first meeting, the council members are to vote for the member's authentication.

77 In the summer of 2010, Article 51 was cited in the Basrah provincial council's questioning of the chief of police there. Although the chief of police insisted that the council had no jurisdiction in the case because he works directly under the Ministry of the Interior, he eventually agreed to attend a hearing where he was questioned for over seven hours by the provincial council about bombings in the province. To date, further action has not been taken to remove him.

78 Article 31 obligates the governor to draft a general budget for the province and submit it to the scrutiny of the provincial council. Article 44 mentions transfers to the governor from the federal government. This paragraph suggests that the total amount allocated is to be transferred to the control of an unnamed authority within the province, most likely the governor. This article could not be implemented prior to the summer of 2010, when provincial councils or governors were not authorized to open a bank account in the name of the province. Although the Ministry of Finance (MOF) eventually relented and allowed the opening of bank accounts in the provinces, it still requires that all provinces follow a standard chart of accounts, limiting their ability to move money between chapters or to create different chapters.

79 Almost all the money received by a provincial council and governor come from the central Ministry of Finance (MOF). An important distinction needs to be made between "allocations" as mentioned in Article 52 and "transfers" as mentioned in Article 44. An allocation is an amount budgeted, whereas the amount transferred is the amount received.

80 When the provincial councils, which were elected in the spring of 2009, were finally seated, Law 21 came into effect. At that time, a number of laws that formerly defined the relationship between the provinces and the central government went out of existence. The laws abrogated or voided by Article 53 continue in influence, however. In the first and most obvious way, many of the concepts (and in fact, in some instances also the language) of those prior laws were copied into Law 21. Two examples include (1) the governor's power over security and his responsibility to the Ministry of Interior in Article 31 and (2) the repetition of the phrase "administrative decentralization" in Article 2, *First* and Article 7, *Third*. In a second and more broad way, Law 21 does not exist in a political and legal vacuum, but in a legal and political context. The words of the law will be interpreted in light of that context, meaning that how government functioned in the past may be the strongest predictor of how it functions in the present.

81 Other than the section/chapter on the formation and competencies of the municipal councils, the rest of the Law of the Municipalities Administration No. 165 of 1964 remains in effect.

**ARTICLE 54:**

Villages and neighborhoods shall be run by a Nahiya council[82] and Administrator through an alderman (Mukhtar) who exercises his work according to the law.[83]

**ARTICLE 55:**

**First:** The provisions of the positions and rights to pension cited in this Law are applied to heads of administrative units, the two governor's deputies, and heads and members of councils and shall come into effect as of April 9, 2003.[84]

**Second:** Members of Municipality councils assumed office after April 9, 2003 shall enjoy the same rights to pension of that of a Nahiya council member under the same terms.

**Third:** Heads of administrative units and heads and members of local council shall resume duties until replacement are chosen according to the law.[85]

Justifying Reasons

This Law has been enacted pursuant to the scope of the competencies and powers granted by the *Constitution of the Republic of Iraq* to the governorates and their administrations and for the purpose of organizing these competencies and powers in a manner that is in harmony with the new state that is based on the federal and decentralized system, and taking into account the fact that existing legislation is inadequate.[86]

82 Since the adoption of Law 21 in the spring of 2008, the question of which law applies to district and subdistrict councils has been frequently debated. Although district and subdistrict councils existed prior to the events of 2003, they, like the provincial councils themselves, were subject to the oversight of the Ministry of Interior. After the U.S. entered Iraq, the character of these councils was changed to become representative bodies. Their membership was selected, in some instances by Army commanders, or informally elected by hastily assembled groups of concerned citizens.

Despite the fact that provincial elections have been conducted twice since adoption of the Iraqi Constitution of 2005, there has never been a formal, High Electoral Commission-conducted election for district or subdistrict councils. It is this absence of elections that has been the issue for those who look at Law 21 and conclude that it does not apply to the district or subdistrict councils. See Note 15 *supra*. Not being elected has also negatively affected subprovincial councils' legitimacy.

83 This has been amended by Law 15 of 2010, Article 8. The previous article obligated the national parliament to organize elections and was the source of confusion as to whether Law 21 could apply to district or subdistrict councils until elections had been held there. See Note 42 *supra*.

84 April 9 is the date that U.S.-led forces entered Baghdad. The capital city was under U.S. control on April 13. This provision rewards council members at the provincial, district, and subdistrict level, regardless of how they came to serve, with a pension equivalent to 80% of their salary while they were council members, provided they served at least six months of the term (in conformity with the amendment to the law, No. 15 of 2010). As a practical matter, this temporary incentive to public service will become a major burden on future administrations, because the number of persons who have served on councils is likely to increase, and with it the rolls of pensioners. This administrative burden would have been one of the complications shed by the central government had the Social Affairs department of the Ministry of Labor been devolved to the governors, as attempted in Law 18 of 2010, but it was held unconstitutional by the Supreme Court in its Holding No. 44 of 2010.

85 This has been amended by Law 15 of 2010. The previous article stated that Law 21 came "into force" from the date of its publication, but would only be applicable to the governorates after the election.

86 The justification for the amendment was given as: "This Law has been enacted to address problems that have emerged during the implementation of Law 21 related to challenges against the termination of council membership, to ensure the accuracy of council decisions, and to extend the right to a pension to members of councils formed after April 9, 2003."

# Government and Public Sector Employees Salaries Law No.22 - 2008

in

- Federal
- Civil Services

**Law / Document Number (ID) :** 22

**Type of Law:** Law

**Date Issued:** 4 May 2008

**Date Published:** 12 May 2008

**Status:** In force

**Summary :** This law is enacted for the purpose of supporting government and public sector employees by giving them salaries and privileges and to ensure better standards of living.

GOVERNMENT AND PUBLIC SECTOR EMPLOYEE SALARIES LAW

Based upon the decision of the Council of Representatives according to the provisions of article (61/first) of the Constitution and according to the provisions of paragraph (5/a) of article (138) of the Constitution.
The Presidency Council decided in its meeting held on 4/5/2008 to decree the following law:

Article 1

This law aims to modify salaries for those covered by its provisions to ensure a better standard of living taking into account academic credentials, job title, geographic location, job-related dangers, years of service, and marital status.

Article 2

The provisions of this law shall apply to first-degree employee and lower according to the salary and annual allowance schedule attached to this law.

Article 3

First- Ranks of employees, their annual allowances, and length of time before becoming eligible for promotion shall be as stated in the salary and annual allowance schedule attached to this law.
Second- The Council of Ministers may modify salary amounts stated in the salary schedule attached to this law in light of inflation to minimize its effect on employee standards of living.
Third- Modification of salaries as stated in paragraph (second) of this article shall be calculated using a base year and the effective date of this law shall be the first base year.

Article 4

First- Taking into account the provisions relating to job descriptions, the following persons that hold degrees shall be appointed according to the salary and annual allowance schedule attached to this law.
A- A person who does not hold a certificate shall be appointed in first rank of tenth grade of salary (140) thousand dinar.
B- A person who holds elementary school certificate shall be appointed in fourth rank of tenth grade of salary (152) thousand dinar.
C- A person who holds middle school certificate shall be appointed in first rank of ninth degree of salary (185) thousand dinar.
D- A person who holds middle school certificate in all its branches including the vocational branch shall be appointed in first rank of eighth grade of salary (240) thousand dinar.
E- A person who holds an institution degree the required duration of study for which is (2) years after

middle school and teachers institutions the required duration of study for which is (5) years after middle school study shall be appointed in fifth rank of eighth degree of salary (260) thousand dinar.
F- A person who holds first university degree (bachelor) shall be appointed in first rank of seventh grade of salary (296) thousand dinar.
G- A person who holds first university degree in pharmacy or dentistry or veterinary medicine or engineering or its equivalent the required duration of study for which is at least (5) years after middle school shall be appointed in first rank of sixth degree of salary (362) thousand dinar.
H- A person who holds a masters degree or its equivalent and a degree from the Iraqi medical University or its equivalent the required duration of study for which is at least (6) years after middle school shall be appointed in the third rank of sixth degree of salary (374) thousand dinar.
I- A person who holds a doctorate degree the required duration of study for which is at least (3) after obtaining a first university degree shall be appointed in first rank of fifth degree of salary (429) thousand dinar.
Second- Any additional years after obtaining the certificates and degrees as stated in paragraph (first) of this article shall be counted by adding an annual allowance for each year.

Article 5

An annual allowance shall be granted for an employee who completes (1) year in service taking into account the provisions of article (9) of this law.

Article 6

First: Promotion is the transfer of an employee from a job position he/she fills to a job a degree higher in the organizational structure.
Second: For promotion the following conditions must be fulfilled:
A- Availability of a vacant position in the higher degree to his/her degree within the relevant department.
B- Completing the period designated for promotion as stated in the schedule annexed to this law.
C- The employee must meet the conditions and required qualifications to occupy the position to which he/she would be promoted.
D- Proof of ability and effectiveness of the employee in meeting the requirements of the position for which he/she is a candidate based upon a recommendation from his/her direct manager and as approved by the higher authority.

Article 7

First- A committee shall be formed based on an order by the minister or head of an entity not associated with a ministry or any authorized person. The committee shall be headed by an employee whose job shall be no less than assistant director general and membership of two persons whose job shall be no less than a manager. The committee shall select candidates for promotion after meeting the required conditions for promotion as stated in paragraph (second) in article (6) of this law.
Second- A promotion decision shall be issued by the competent minister or head of an entity not associated with a ministry and the promotion decision shall be effective from the date of issuance.

Article 8

First- If the salary of the promoted employee is the same as the salary of the rank from which he/she was promoted then he/she shall be given salary of the next rank.
Second- If the salary of a promoted employee is located between two ranks then he/she shall be given salary of the higher rank.

Article 9

First- If it proves impossible to promote an employee to the next rank or to give him/her an annual allowance to the highest limit of his/her salary then it is permissible to continue to provide him/her with the annual allowance for the next rank.
Second- Granting an employee of the eleventh rank of the first grade his/her annual allowance shall be permitted provided that the minimum salary for the highest rank (B) shall not be exceeded.

Article 10

Allowances for a position shall be given as per the following percentages:
First- (30%) of the salary for a person who fills the position of director general’s deputy included in the organizational structure of the department.
Second- (25%) of the salary for specialized supervisors and educational supervisors and headmasters of schools and vocational institutions.
Third- (25%) of the salary for an employee who fills the position of an organizational administrator included in the organizational structure of the department.
Fourth- (20%) of the salary for an employee who fills the position of head of department.

Fifth- (15%) of the salary for an employee who fills the position of assistants for schools masters and vocational institutions as stated in paragraphs (third) and (fourth) of this article and heads of sections.

Article 11

First- Degree allowances shall be given per the following percentages:
A- (100%) of the salary for a PhD holder or its equivalent.
B- (75%) of the salary for a masters degree holder or its equivalent.
C- (55%) of the salary for a high diploma holder requiring at least (1) year of study after university.
D- (45%) of the salary for bachelors degree holder.
E- (35%) of the salary for vocational diploma holders and teachers not having any of degree stated in paragraphs (A), (B), (C), and (D) of this article.
F- (25%) of the salary for holders of middle school certificates in any one of its branches, including those that are vocational.
Second- Vocational allowances of (15%) of the salary shall be given for those who do not hold any of the degrees stated in item first of this article.

Article 12

Geographical location allowances shall be given as follows:
First- (60) thousand dinar for a person who works in a remote area.
Second- (50) thousand dinar for a person who works in a rural area.
Third- (40) thousand dinar for a person who works in district areas except in districts located in the centre of the governorates.
Fourth- (30) thousand dinar for a person who works in a Qada'a except those who work in Qada’a’s of governorates.
Fifth- (20) thousand diner for a person who works in a governorate centre not covered by free transportation.

Article 13

The minister or head of an entity not associated with a ministry shall grant danger allowances of between (20%) and (30%) of the salary per instructions issued by the Minister of Finance.

Article 14

First- A- A married employee shall be given support allowance of (50) thousand dinar when a husband and wife receive a salary or pension.
B- An employee whose husband or wife has passed away or has a disease that makes him/her incapable of work shall receive the allowances stated in paragraph (first) of this item if that person does not receive a pension.
Second-A- A married employee shall receive child allowances of (10) thousand dinar for each child up to a maximum of (4) children.
B- Child allowances shall continue to be granted until the child reaches (18) years of age or when he/she leaves school and obtains a private income.

Article 15

The Council of Ministers may grant allowances not exceeding (50%) of the salary in addition to the allowances stated in this law for treatment of any condition or circumstances of a special nature.

Article 16

The allowances stated in this law shall be calculated based on the salary and annual allowance schedule annexed to this law, and shall continue to enjoy hazard allowances granted according to the Order No. (30) of 2003 provided that the total allowances granted according to this law or any other law shall not exceed (200%) of the salary with the exception of the allowances stated in articles (14) and (15) of this law.

Article 17

The minister or head of an entity not associated with a ministry or any authorized person may demand that an employee works extra hours (not to exceed (3) hours daily) and grant them wages for their work according to instructions issued by the Minister of Finance and these wages shall not be counted in the limit determined in article (16) of this law.

Article 18

Employees of ministries and entities not associated with a ministry covered by special service laws shall receive the allowances granted to them according to those laws taking into account the provisions of article (16) of this law.

Article 19

Employees of the three presidential entities (Council of Representatives, Presidency of the Republic,

and Council of Ministers) and employees of the Ministry of Defense and Ministry of Interior or military personnel shall continue to receive their current allowances instead of the allowances stated in this law until the issuance of their service laws.

Article 20

Articles (3) and (4) of the Civil Service Law No. 24 of 1960 shall be repealed.

Article 21

The Order of the Coalition Provisional Authority (dissolved) No. 30 of 2003 shall be repealed.

Article 22

The Minister of Finance shall issue the necessary instructions to facilitate the execution of the provisions of this law.

Article 23

This law shall be published in the official gazette and be effective as of 1/1/2008.

**Tareq Al-Hashemi**
Vice President of the Republic

**Adel Abdul-Mahdi**
Vice President of the Republic

**Jalal Talbani**
President of the Republic

**Justification**

This law is enacted for the purpose of supporting government and public sector employees by giving them salaries and privileges and to ensure better standards of living.

Salary and Annual Allowance Schedule (1,000s of ID)

| High Grades | Service Years | | | | | | | | | | | Annual Allowance |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| High Grade (A) jobs with spec | 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 | 11 | 83 |

| | | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| ial grades | 241 3 | 249 6 | 257 9 | 266 2 | 274 5 | 282 8 | 291 1 | 299 4 | 307 7 | 316 0 | 324 3 | |
| High Grade (B) General Director | 150 0 | 158 3 | 166 6 | 174 9 | 183 2 | 191 5 | 199 8 | 208 1 | 216 4 | 224 7 | 233 0 | 83 |

| Job grade | Service Years | | | | | | | | | | | | Annual Allowance | Years before Promotion |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 | 11 | | | |
| 1 | 948 | 968 | 988 | 1008 | 1028 | 1048 | 1068 | 1088 | 1108 | 1128 | 1148 | | 20 | / |
| 2 | 758 | 775 | 792 | 809 | 826 | 843 | 860 | 877 | 894 | 911 | 928 | | 17 | 5 |
| 3 | 621 | 634 | 647 | 659 | 669 | 681 | 693 | 705 | 717 | 729 | 741 | | 12 | 5 |
| 4 | 509 | 519 | 529 | 539 | 549 | 559 | 569 | 579 | 589 | 599 | 609 | | 10 | 5 |

| | | | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| 5 | 429 | 436 | 443 | 450 | 457 | 464 | 471 | 478 | 485 | 492 | 499 | 7 | 5 |
| 6 | 362 | 368 | 374 | 380 | 386 | 392 | 398 | 404 | 410 | 416 | 422 | 6 | 4 |
| 7 | 296 | 302 | 308 | 314 | 320 | 326 | 332 | 338 | 344 | 350 | 356 | 6 | 4 |
| 8 | 240 | 245 | 250 | 255 | 260 | 265 | 270 | 275 | 280 | 285 | 290 | 5 | 4 |
| 9 | 185 | 190 | 195 | 200 | 205 | 210 | 215 | 220 | 225 | 230 | 235 | 5 | 4 |
| 10 | 140 | 144 | 148 | 152 | 156 | 160 | 164 | 168 | 172 | 176 | 180 | 4 | 4 |

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# IRAQI

# CONSTITUTION

# The Preamble

*In the name of God, the Most merciful, the Most compassionate*

{**We have honored the sons of Adam**}

We, the people of Mesopotamia, the homeland of the apostles and prophets, resting place of the virtuous imams, cradle of civilization, crafters of writing, and home of numeration. Upon our land the first law made by man was passed, and the oldest pact of just governance was inscribed, and upon our soil the saints and companions of the Prophet prayed, philosophers and scientists theorized, and writers and poets excelled;

Acknowledging God's right over us, and in fulfillment of the call of our homeland and citizens, and in a response to the call of our religious and national leaderships and the determination of our great authorities and of our leaders and politicians, and in the midst of international support from our friends and those who love us, marched for the first time in our history towards the ballot boxes by the millions, men and women, young and old, on the thirtieth of January 2005, invoking the pains of sectarian oppression inflicted by the autocratic clique and inspired by the tragedies of Iraq's martyrs, Shiite and Sunni, Arabs and Kurds and Turkmen and from all other components of the people, and recollecting the darkness of the ravage of the holy cities and the South in the Sha'abaniyya uprising and burnt by the flames of grief of the mass graves, the marshes, Al-Dujail and others and articulating the sufferings of racial oppression in the massacres of Halabcha, Barzan, Anfal and the Fayli Kurds and inspired by the ordeals of the Turkmen in Bashir and the sufferings of the people of the western region, as is the case in the remaining areas of Iraq where the people suffered from the liquidation of their leaders, symbols, and Sheiks and from the displacement of their skilled individuals and from drying out of its cultural and intellectual wells, so we sought hand in hand and shoulder to shoulder to create our new Iraq, the Iraq of the future, free from sectarianism, racism, complex of regional attachment, discrimination, and exclusion.

Accusations of being infidels, and terrorism did not stop us from marching forward to build a nation of law. Sectarianism and racism have not stopped us from marching together to strengthen our national unity, following the path of peaceful transfer of power, adopting the course of just distribution of resources, and providing equal opportunity for all.

We, the people of Iraq, who have just risen from our stumble, and who are looking with confidence to the future through a republican, federal, democratic, pluralistic system, have resolved with the determination of our men, women, elderly, and youth to respect the rule of law, to establish justice and equality, to cast aside the politics of aggression, to pay attention to women and their rights, the elderly and their concerns, and children and their affairs, to spread the culture of diversity, and to defuse terrorism.

We, the people of Iraq, of all components and across the spectrum, have taken upon ourselves to decide freely and by choice to unite our future, to take lessons from yesterday for tomorrow, and to enact this permanent Constitution, through the values and ideals of the heavenly messages and the findings of science and man's civilization. The adherence to this Constitution preserves for Iraq its free union of people, of land, and of sovereignty.

# Section One

## Fundamental Principles

Article 1:

The Republic of Iraq is a single federal, independent and fully sovereign state in which the system of government is republican, representative, parliamentary, and democratic, and this Constitution is a guarantor of the unity of Iraq.

Article 2:

First: Islam is the official religion of the State and is a foundation source of legislation:

A. No law may be enacted that contradicts the established provisions of Islam
B. No law may be enacted that contradicts the principles of democracy.
C. No law may be enacted that contradicts the rights and basic freedoms stipulated in this Constitution.

Second: This Constitution guarantees the Islamic identity of the majority of the Iraqi people and guarantees the full religious rights to freedom of religious belief and practice of all individuals such as Christians, Yazidis, and Mandean Sabeans.

Article 3:

Iraq is a country of multiple nationalities, religions, and sects. It is a founding and active member in the Arab League and is committed to its charter, and it is part of the Islamic world.

Article 4:

First: The Arabic language and the Kurdish language are the two official languages of Iraq. The right of Iraqis to educate their children in their mother tongue, such as Turkmen, Syriac, and Armenian shall be guaranteed in government educational institutions in accordance with educational guidelines, or in any other language in private educational institutions.

Second: The scope of the term "official language" and the means of applying the provisions of this article shall be defined by a law and shall include:

A. Publication of the Official Gazette, in the two languages;

B. Speech, conversation, and expression in official domains, such as the Council of Representatives, the Council of Ministers, courts, and official conferences, in either of the two languages;

C. Recognition and publication of official documents and correspondence in the two languages;

D. Opening schools that teach the two languages, in accordance with the educational guidelines;

E. Use of both languages in any matter enjoined by the principle of equality such as bank notes, passports, and stamps.

Third: The federal and official institutions and agencies in the Kurdistan region shall use both languages.

Fourth: The Turkomen language and the Syriac language are two other official languages in the administrative units in which they constitute density of population.

Fifth: Each region or governorate may adopt any other local language as an additional official language if the majority of its population so decides in a general referendum.

Article 5:
The law is sovereign. The people are the source of authority and legitimacy, which they shall exercise in a direct, general, secret ballot and through their constitutional institutions.

Article 6:
Transfer of authority shall be made peacefully through democratic means as stipulated in this Constitution.

Article 7:

First: Any entity or program that adopts, incites, facilitates, glorifies, promotes, or justifies racism or terrorism or accusations of being an infidel (takfir) or ethnic cleansing, especially the Saddamist Ba'ath in Iraq and its symbols, under any name whatsoever, shall be prohibited. Such entities may not be part of political pluralism in Iraq. This shall be regulated by law.

Second: The State shall undertake to combat terrorism in all its forms, and shall work to protect its territories from being a base, pathway, or field for terrorist activities.

Article 8:

Iraq shall observe the principles of good neighborliness, adhere to the principle of non-interference in the internal affairs of other states, seek to settle disputes by peaceful means, establish relations on the basis of mutual interests and reciprocity, and respect its international obligations.

Article 9:

First:

A- The Iraqi armed forces and security services will be composed of the components of the Iraqi people with due consideration given to their balance and representation without discrimination or exclusion. They shall be subject to the control of the civilian authority, shall defend Iraq, shall not be used as an instrument to oppress the Iraqi people, shall not interfere in the political affairs, and shall have no role in the transfer of authority.

B- The formation of military militias outside the framework of the armed forces is prohibited.

C- The Iraqi armed forces and their personnel, including military personnel working in the Ministry of Defense or any subordinate departments or organizations, may not stand for election to political office, campaign for candidates, or participate in other activities prohibited by Ministry of Defense regulations. This ban includes the activities of the personnel mentioned above acting in their personal or professional capacities, but shall not infringe upon the right of these personnel to cast their vote in the elections.

D- The Iraqi National Intelligence Service shall collect information, assess threats to national security, and advise the Iraqi government. This Service shall be under civilian control, shall be subject to legislative oversight, and shall operate in accordance with the law and pursuant to the recognized principles of human rights.

E- The Iraqi Government shall respect and implement Iraq's international obligations regarding the non-proliferation, non-development, non-production, and non-use of nuclear, chemical, and biological weapons, and shall prohibit associated equipment, materiel, technologies, and delivery systems for use in the development, manufacture, production, and use of such weapons.

Second: Military service shall be regulated by law.

Article 10:

The holy shrines and religious sites in Iraq are religious and civilizational entities. The State is committed to assuring and maintaining their sanctity, and to guaranteeing the free practice of rituals in them.

Article 11:
Baghdad is the capital of the Republic of Iraq.

Article 12:

First: The flag, national anthem, and emblem of Iraq shall be regulated by law in a way that symbolizes the components of the Iraqi people.

Second: A law shall regulate honors, official holidays, religious and national occasions and the Hijri and Gregorian calendar.

Article 13:

First: This Constitution is the preeminent and supreme law in Iraq and shall be binding in all parts of Iraq without exception.

Second: No law that contradicts this Constitution shall be enacted. Any text in any regional constitutions or any other legal text that contradicts this Constitution shall be considered void.

# Section Two

# Rights and Liberties

## Chapter One
## [Rights]

### First: Civil and Political Rights

Article 14:
Iraqis are equal before the law without discrimination based on gender, race, ethnicity, nationality, origin, color, religion, sect, belief or opinion, or economic or social status.

Article 15:
Every individual has the right to enjoy life, security and liberty. Deprivation or restriction of these rights is prohibited except in accordance with the law and based on a decision issued by a competent judicial authority.

Article 16:
Equal opportunities shall be guaranteed to all Iraqis, and the state shall ensure that the necessary measures to achieve this are taken.

Article 17:

First: Every individual shall have the right to personal privacy so long as it does not contradict the rights of others and public morals.

Second: The sanctity of the homes shall be protected. Homes may not be entered, searched, or violated, except by a judicial decision in accordance with the law.

Article 18:

First: Iraqi citizenship is a right for every Iraqi and is the basis of his nationality.

Second: Anyone who is born to an Iraqi father or to an Iraqi mother shall be considered an Iraqi. This shall be regulated by law.

Third:

A. An Iraqi citizen by birth may not have his citizenship withdrawn for any reason. Any person who had his citizenship withdrawn shall have the right to demand its reinstatement. This shall be regulated by a law.
B. Iraqi citizenship shall be withdrawn from naturalized citizens in cases regulated by law.

Fourth: An Iraqi may have multiple citizenships. Everyone who assumes a senior, security or sovereign position must abandon any other acquired citizenship. This shall be regulated by law.

Fifth: Iraqi citizenship shall not be granted for the purposes of the policy of population settlement that disrupts the demographic composition of Iraq.

Sixth: Citizenship provisions shall be regulated by law. The competent courts shall consider the suits arising from those provisions.

Article 19:

First: The judiciary is independent and no power is above the judiciary except the law.

Second: There is no crime or punishment except by law. The punishment shall only be for an act that the law considers a crime when perpetrated. A harsher punishment than the applicable punishment at the time of the offense may not be imposed.

Third: Litigation shall be a protected and guaranteed right for all.

Fourth: The right to a defense shall be sacred and guaranteed in all phases of investigation and the trial.

Fifth: The accused is innocent until proven guilty in a fair legal trial. The accused may not be tried for the same crime for a second time after acquittal unless new evidence is produced.

Sixth: Every person shall have the right to be treated with justice in judicial and administrative proceedings.

Seventh: The proceedings of a trial are public unless the court decides to make it secret.

Eighth: Punishment shall be personal.

Ninth: Laws shall not have retroactive effect unless stipulated otherwise. This exclusion shall not include laws on taxes and fees.

Tenth: Criminal laws shall not have retroactive effect, unless it is to the benefit of the accused.

Eleventh: The court shall appoint a lawyer at the expense of the state for an accused of a felony or misdemeanor who does not have a defense lawyer.

Twelfth:

A. Unlawful detention shall be prohibited.
B. Imprisonment or detention shall be prohibited in places not designed for these purposes, pursuant to prison laws covering health and social care, and subject to the authorities of the State.

Thirteenth: The preliminary investigative documents shall be submitted to the competent judge in a period not to exceed twenty-four hours from the time of the arrest of the accused, which may be extended only once and for the same period.

Article 20:
Iraqi citizens, men and women, shall have the right to participate in public affairs and to enjoy political rights including the right to vote, elect, and run for office.

Article 21:

First: No Iraqi shall be surrendered to foreign entities and authorities.

Second: A law shall regulate the right of political asylum in Iraq. No political refugee shall be surrendered to a foreign entity or returned forcibly to the country from which he fled.

Third: Political asylum shall not be granted to a person accused of committing international or terrorist crimes or to any person who inflicted damage on Iraq.

## Second: Economic, Social and Cultural Liberties

Article 22:

First: Work is a right for all Iraqis in a way that guarantees a dignified life for them.

Second: The law shall regulate the relationship between employees and employers on economic bases and while observing the rules of social justice.

Third: The State shall guarantee the right to form and join unions and professional associations, and this shall be regulated by law.

Article 23:

First: Private property is protected. The owner shall have the right to benefit, exploit and dispose of private property within the limits of the law.

Second: Expropriation is not permissible except for the purposes of public benefit in return for just compensation, and this shall be regulated by law.

Third:

A. Every Iraqi shall have the right to own property anywhere in Iraq. No others may possess immovable assets, except as exempted by law.
B. Ownership of property for the purposes of demographic change is prohibited.

Article 24:
The State shall guarantee freedom of movement of Iraqi manpower, goods, and capital between regions and governorates, and this shall be regulated by law.

Article 25:
The State shall guarantee the reform of the Iraqi economy in accordance with modern economic principles to insure the full investment of its resources, diversification of its sources, and the encouragement and development of the private sector.

Article 26:
The State shall guarantee the encouragement of investment in the various sectors, and this shall be regulated by law.

Article 27:

First: Public assets are sacrosanct, and their protection is the duty of each citizen.

Second: The provisions related to the preservation of State properties, their management, the conditions for their disposal, and the limits for these assets not to be relinquished shall all be regulated by law.

Article 28:

First: No taxes or fees shall be levied, amended, collected, or exempted, except by law.

Second: Low income earners shall be exempted from taxes in a way that guarantees the preservation of the minimum income required for living. This shall be regulated by law.

Article 29:

First:

A. The family is the foundation of society; the State shall preserve it and its religious, moral, and national values.

B. The State shall guarantee the protection of motherhood, childhood and old age, shall care for children and youth, and shall provide them with the appropriate conditions to develop their talents and abilities.

Second: Children have the right to upbringing, care and education from their parents. Parents have the right to respect and care from their children, especially in times of need, disability, and old age.

Third: Economic exploitation of children in all of its forms shall be prohibited, and the State shall take the necessary measures for their protection.

Fourth: All forms of violence and abuse in the family, school, and society shall be prohibited.

Article 30:

First: The State shall guarantee to the individual and the family - especially children and women – social and health security, the basic requirements for living a free and decent life, and shall secure for them suitable income and appropriate housing.

Second: The State shall guarantee social and health security to Iraqis in cases of old age, sickness, employment disability, homelessness, orphanhood, or unemployment, shall work to protect them from ignorance, fear and poverty, and shall provide them housing and special programs of care and rehabilitation, and this shall be regulated by law.

Article 31:

First: Every citizen has the right to health care. The State shall maintain public health and provide the means of prevention and treatment by building different types of hospitals and health institutions.

Second: Individuals and entities have the right to build hospitals, clinics, or private health care centers under the supervision of the State, and this shall be regulated by law.

Article 32:

The State shall care for the handicapped and those with special needs, and shall ensure their rehabilitation in order to reintegrate them into society, and this shall be regulated by law.

Article 33:

First: Every individual has the right to live in safe environmental conditions.

Second: The State shall undertake the protection and preservation of the environment and its biological diversity.

Article 34:

First: Education is a fundamental factor for the progress of society and is a right guaranteed by the state. Primary education is mandatory and the state guarantees that it shall combat illiteracy.

Second: Free education in all its stages is a right for all Iraqis.

Third: The State shall encourage scientific research for peaceful purposes that serve humanity and shall support excellence, creativity, invention, and different aspects of ingenuity.

Fourth: Private and public education shall be guaranteed, and this shall be regulated by law.

Article 35:

The state shall promote cultural activities and institutions in a manner that befits the civilizational and cultural history of Iraq, and it shall seek to support indigenous Iraqi cultural orientations.

Article 36:

Practicing sports is a right of every Iraqi and the state shall encourage and care for such activities and shall provide for their requirements.

## Chapter Two
## [Liberties]

Article 37:

First:

A. The liberty and dignity of man shall be protected.

B. No person may be kept in custody or investigated except according to a judicial decision.

C. All forms of psychological and physical torture and inhumane treatment are prohibited. Any confession made under force, threat, or torture shall

not be relied on, and the victim shall have the right to seek compensation for material and moral damages incurred in accordance with the law.

Second: The State shall guarantee protection of the individual from intellectual, political and religious coercion.

Third: Forced labor, slavery, slave trade, trafficking in women or children, and sex trade shall be prohibited.

Article 38:
The State shall guarantee in a way that does not violate public order and morality:

A. Freedom of expression using all means.
B. Freedom of press, printing, advertisement, media and publication.
C. Freedom of assembly and peaceful demonstration, and this shall be regulated by law.

Article 39:

First: The freedom to form and join associations and political parties shall be guaranteed, and this shall be regulated by law.

Second: It is not permissible to force any person to join any party, society, or political entity, or force him to continue his membership in it.

Article 40:
The freedom of communication and correspondence, postal, telegraphic, electronic, and telephonic, shall be guaranteed and may not be monitored, wiretapped, or disclosed except for legal and security necessity and by a judicial decision.

Article 41:
Iraqis are free in their commitment to their personal status according to their religions, sects, beliefs, or choices, and this shall be regulated by law.

Article 42:
Each individual shall have the freedom of thought, conscience, and belief.

Article 43:

First: The followers of all religions and sects are free in the:

A- Practice of religious rites, including the Husseini rituals.
B- Management of religious endowments (waqf), their affairs, and their religious institutions, and this shall be regulated by law.

Second: The State shall guarantee freedom of worship and the protection of places of worship.

Article 44:

First: Each Iraqi has freedom of movement, travel, and residence inside and outside Iraq.

Second: No Iraqi may be exiled, displaced, or deprived from returning to the homeland.

Article 45:

First: The State shall seek to strengthen the role of civil society institutions, and to support, develop and preserve their independence in a way that is consistent with peaceful means to achieve their legitimate goals, and this shall be regulated by law.

Second: The State shall seek the advancement of the Iraqi clans and tribes, shall attend to their affairs in a manner that is consistent with religion and the law, and shall uphold their noble human values in a way that contributes to the development of society. The State shall prohibit the tribal traditions that are in contradiction with human rights.

Article 46:

Restricting or limiting the practice of any of the rights or liberties stipulated in this Constitution is prohibited, except by a law or on the basis of a law, and insofar as that limitation or restriction does not violate the essence of the right or freedom.

# Section Three

# Federal Powers

Article 47:
The federal powers shall consist of the legislative, executive, and judicial powers, and they shall exercise their competencies and tasks on the basis of the principle of separation of powers.

## Chapter one
## [The Legislative Power]

Article 48:
The federal legislative power shall consist of the Council of Representatives and the Federation Council.

### First: The Council of Representatives

Article 49:

First: The Council of Representatives shall consist of a number of members, at a ratio of one seat per 100,000 Iraqi persons representing the entire Iraqi people. They shall be elected through a direct secret general ballot. The representation of all components of the people shall be upheld in it.

Second: A candidate to the Council of Representatives must be a fully qualified Iraqi.

Third: A law shall regulate the requirements for the candidate, the voter, and all that is related to the elections.

Fourth: The elections law shall aim to achieve a percentage of representation for women of not less than one-quarter of the members of the Council of Representatives.

Fifth: The Council of Representatives shall promulgate a law dealing with the replacement of its members on resignation, dismissal, or death.

Sixth: It is not permissible to combine membership in the Council of Representatives with any work or other official position.

Article 50:
Each member of the Council of Representatives shall take the following constitutional oath before the Council prior to assuming his duties:

**"I swear by God Almighty to carry out my legal duties and responsibilities with devotion and integrity and preserve the independence and sovereignty of Iraq, and safeguard the interests of its people, and ensure the safety of its land, sky, water, wealth, and federal democratic system, and I shall endeavor to protect public and private liberties, the independence of the judiciary, and pledge to implement legislation faithfully and neutrally. God is my witness."**

Article 51:
The Council of Representatives shall establish its bylaws to regulate its work.

Article 52:

First: The Council of Representatives shall decide, by a two-thirds majority, the authenticity of membership of its member within thirty days from the date of filing an objection.

Second: The decision of the Council of Representatives may be appealed before the Federal Supreme Court within thirty days from the date of its issuance.

Article 53:

First: Sessions of the Council of Representatives shall be public unless, for reasons of necessity, the Council decides otherwise.

Second: Minutes of the sessions shall be published by means considered appropriate by the Council.

Article 54:
The President of the Republic shall call upon the Council of Representatives to convene by a presidential decree within fifteen days from the date of the ratification of the general election results. Its eldest member shall chair the first session to elect the speaker of the Council and his two deputies. This period may not be extended by more than the aforementioned period.

Article 55:
The Council of Representatives shall elect in its first session its speaker, then his first deputy and second deputy, by an absolute majority of the total number of the Council members by direct secret ballot.

Article 56:

First: The electoral term of the Council of Representatives shall be four calendar years, starting with its first session and ending with the conclusion of the fourth year.

Second: The new Council of Representatives shall be elected forty-five days before the conclusion of the preceding electoral term.

Article 57:

The Council of Representatives shall have one annual term, with two legislative sessions, lasting eight months. The bylaws shall define the method to convene the sessions. The session in which the general budget is being presented shall not end until approval of the budget.

Article 58:

First: The President of the Republic, the Prime Minister, the Speaker of the Council of Representatives, or fifty members of the Council of Representatives may call the Council to an extraordinary session. The session shall be restricted to the topics that necessitated the call for the session.

Second: The legislative session of the Council of Representatives may be extended for no more than 30 days to complete the tasks that require the extension, based on a request from the President of the Republic, the Prime Minister, the Speaker of the Council, or fifty members of the Council of Representatives.

Article 59:

First:

The Council of Representatives quorum shall be achieved by an absolute majority of its members.

Second:

Decisions in the sessions of the Council of Representatives shall be made by a simple majority after quorum is achieved, unless otherwise stipulated.

Article 60:

First:

Draft laws shall be presented by the President of the Republic and the Council of Ministers.

Second;

Proposed laws shall be presented by ten members of the Council of Representatives or by one of its specialized committees.

Article 61:

The Council of Representatives shall be competent in the following:

First: Enacting federal laws.

Second: Monitoring the performance of the executive authority.

Third: Electing the President of the Republic.

Fourth: Regulating the ratification process of international treaties and agreements by a law, to be enacted by a two-thirds majority of the members of the Council of Representatives.

Fifth: Approving the appointment of the following:

A. The President and members of the Federal Court of Cassation, the Chief Public Prosecutor, and the President of Judicial Oversight Commission by an absolute majority, based on a proposal from the Higher Juridical Council.
B. Ambassadors and those with special grades, based on a proposal from the Council of Ministers.
C. The Iraqi Army Chief of Staff, his assistants, those of the rank of division commander and above, and the director of the intelligence service, based on a proposal from the Council of Ministers.

Sixth:

A. Questioning the President of the Republic, based on a petition with cause, by an absolute majority of the members of the Council of Representatives.

B. Relieving the President of the Republic by an absolute majority of the Council of Representatives after being convicted by the Federal Supreme Court in one of the following cases:
   1- Perjury of the constitutional oath.
   2- Violating the Constitution.
   3- High treason.

Seventh:

A. A member of the Council of Representatives may direct questions to the Prime Minister and the Ministers on any subject within their specialty and each of them shall answer the members' questions. Only the member who has asked the question shall have the right to comment on the answer.

B. At least twenty-five members of the Council of Representatives may raise a general issue for discussion in order to inquire about a policy and the performance of the Council of Ministers or one of the Ministries and it shall be submitted to the Speaker of the Council of Representatives, and

the Prime Minister or the Ministers shall specify a date to come before the Council of Representatives to discuss it.

C. A member of the Council of Representatives, with the agreement of twenty-five members, may direct an inquiry to the Prime Minister or the Ministers to call them to account on the issues within their authority. The debate shall not be held on the inquiry except after at least seven days from the date of submission of the inquiry.

Eighth:

A. The Council of Representatives may withdraw confidence from one of the Ministers by an absolute majority and he shall be considered resigned from the date of the decision of withdrawal of confidence. A vote of no confidence in a Minister may not be held except upon his request or on the basis of a request signed by fifty members after the Minister has appeared for questioning before the Council. The Council shall not issue its decision regarding the request except after at least seven days from the date of its submission.

B.

1- The President of the Republic may submit a request to the Council of Representatives to withdraw confidence from the Prime Minister.
2- The Council of Representatives may withdraw confidence from the Prime Minister based on the request of one-fifth of its members. This request shall not be submitted except after an inquiry directed at the Prime Minister and after at least seven days from the date of submitting the request.
3- The Council of Representatives may decide to withdraw confidence from the Prime Minister by an absolute majority of the number of its members.

C. The Government is deemed resigned in case of withdrawal of confidence from the Prime Minister.

D. In case of a vote of withdrawal of confidence in the Council of Ministers as a whole, the Prime Minister and the Ministers continue in their positions to run everyday business for a period not to exceed thirty days until a new Council of Ministers is formed in accordance with the provisions of Article 76 of this Constitution.

E. The Council of Representatives may question independent commission heads in accordance with the same procedures related to the Ministers. The Council shall have the right to relieve them by absolute majority.

Ninth:

A. To consent to the declaration of war and the state of emergency by a two-thirds majority based on a joint request from the President of the Republic and the Prime Minister.

B. The state of emergency shall be declared for a period of thirty days, which can be extended after approval each time.

C. The Prime Minister shall be delegated the necessary powers which enable him to manage the affairs of the country during the period of the declaration of war and the state of emergency. These powers shall be regulated by a law in a way that does not contradict the Constitution.

D. The Prime Minister shall present to the Council of Representatives the measures taken and the results during the period of the declaration of war and the state of emergency within 15 days from the date of its end.

Article 62:

First: The Council of Ministers shall submit the draft general budget bill and the closing account to the Council of Representatives for approval.

Second: The Council of Representatives may conduct transfers between the sections and chapters of the general budget and reduce the total of its sums, and it may suggest to the Council of Ministers that they increase the total expenses, when necessary.

Article 63:

First: A law shall regulate the rights and privileges of the speaker of the Council of Representatives, his two deputies, and the members of the Council of Representatives.

Second:

A. A member of the Council of Representatives shall enjoy immunity for statements made while the Council is in session, and the member may not be prosecuted before the courts for such.

B. A Council of Representatives member may not be placed under arrest during the legislative term of the Council of Representatives, unless the member is accused of a felony and the Council of Representatives members consent by an absolute majority to lift his immunity or if he is caught *in flagrante delicto* in the commission of a felony.

C. A Council of Representatives member may not be arrested after the legislative term of the Council of Representatives, unless the member is accused of a felony and with the consent of the speaker of the Council of

Representatives to lift his immunity or if he is caught *in flagrante delicto* in the commission of a felony.

Article 64:

First: The Council of Representatives may be dissolved by an absolute majority of the number of its members, or upon the request of one-third of its members by the Prime Minister with the consent of the President of the Republic. The Council shall not be dissolved during the period in which the Prime Minister is being questioned.

Second: Upon the dissolution of the Council of Representatives, the President of the Republic shall call for general elections in the country within a period not to exceed sixty days from the date of its dissolution. The Council of Ministers in this case is deemed resigned and continues to run everyday business.

## Second: The Federation Council

Article 65:

A legislative council shall be established named the "Federation Council," to include representatives from the regions and the governorates that are not organized in a region. A law, enacted by a two-thirds majority of the members of the Council of Representatives, shall regulate the formation of the Federation Council, its membership conditions, its competencies, and all that is connected with it.

## Chapter Two
## [The Executive Power]

Article 66:

The federal executive power shall consist of the President of the Republic and the Council of Ministers and shall exercise its powers in accordance with the Constitution and the law.

## First: The President of the Republic

Article 67:

The President of the Republic is the Head of the State and a symbol of the unity of the country and represents the sovereignty of the country. He shall guarantee the commitment to the Constitution and the preservation of Iraq's independence, sovereignty,

unity, and the safety of its territories, in accordance with the provisions of the Constitution.

Article 68:
A nominee to the Presidency of the Republic must be:

First: An Iraqi by birth, born to Iraqi parents.

Second: Fully qualified and must be over forty years of age.

Third: Of good reputation and political experience, known for his integrity, uprightness, fairness, and loyalty to the homeland.

Fourth: Free of any conviction of a crime involving moral turpitude.

Article 69:

First: The provisions for nomination to the office of the President of the Republic shall be regulated by law.

Second: The provisions for nomination to the office of one or more Vice Presidents of the Republic shall be regulated by law.

Article 70:

First: The Council of Representatives shall elect a President of the Republic from among the candidates by a two-thirds majority of the number of its members.

Second: If none of the candidates receive the required majority vote then the two candidates who received the highest number of votes shall compete and the one who receives the majority of votes in the second election shall be declared President.

Article 71:
The President shall take the constitutional oath before the Council of Representatives according to the language stipulated in Article 50 of the Constitution.

Article 72:

First: The President of the Republic's term in office shall be limited to four years. He may be re-elected for a second time only.

Second:
A- The President of the Republic's term in office shall end with the end of the term of the Council of Representatives.

B- The President of the Republic shall continue to exercise his duties until after the end of the election and the meeting of the new Council of Representatives, provided that a new President of the Republic is elected within thirty days from the date of its first convening.
C- In case the position of the President of the Republic becomes vacant for any reason, a new President shall be elected to complete the remaining period of the President's term.

Article 73:
The President of the Republic shall assume the following powers:

First: To issue a special pardon on the recommendation of the Prime Minister, except for anything concerning a private claim and for those who have been convicted of committing international crimes, terrorism, or financial and administrative corruption.

Second: To ratify international treaties and agreements after the approval by the Council of Representatives. Such international treaties and agreements are considered ratified after fifteen days from the date of receipt by the President.

Third: To ratify and issue the laws enacted by the Council of Representatives. Such laws are considered ratified after fifteen days from the date of receipt by the President.

Fourth: To call the elected Council of Representatives to convene during a period not to exceed fifteen days from the date of approval of the election results and in the other cases stipulated in the Constitution.

Fifth: To award medals and decorations on the recommendation of the Prime Minister in accordance with the law.

Sixth: To accredit ambassadors.

Seventh: To issue Presidential decrees.

Eighth: To ratify death sentences issued by the competent courts.

Ninth: To perform the duty of the High Command of the armed forces for ceremonial and honorary purposes.

Tenth: To exercise any other presidential powers stipulated in this Constitution.

Article 74:
A law shall fix the salary and the allowances of the President of the Republic.

Article 75:

First: The President of the Republic shall have the right to submit his resignation in writing to the Speaker of the Council of Representatives, and it shall be considered effective after seven days from the date of its submission to the Council of Representatives.

Second: The Vice President shall replace the President in case of his absence.

Third: The Vice President shall replace the President of the Republic in the event that the post of the President becomes vacant for any reason whatsoever. The Council of Representatives must elect a new President within a period not to exceed thirty days from the date of the vacancy.

Fourth: In case the post of the President of the Republic becomes vacant, the Speaker of the Council of Representatives shall replace the President of the Republic in case he does not have a Vice President, on the condition that a new President is elected during a period not to exceed thirty days from the date of the vacancy and in accordance with the provisions of this Constitution.

## Second: Council of Ministers

Article 76:

First: The President of the Republic shall charge the nominee of the largest Council of Representatives bloc with the formation of the Council of Ministers within fifteen days from the date of the election of the President of the Republic.

Second: The Prime Minister-designate shall undertake the naming of the members of his Council of Ministers within a period not to exceed thirty days from the date of his designation.

Third: If the Prime Minister-designate fails to form the Council of Ministers during the period specified in clause "Second," the President of the Republic shall charge a new nominee for the post of Prime Minister within fifteen days.

Fourth: The Prime Minister-designate shall present the names of his members of the Council of Ministers and the ministerial program to the Council of Representatives. He is deemed to have gained its confidence upon the approval, by an absolute majority of the Council of Representatives, of the individual Ministers and the ministerial program.

Fifth: The President of the Republic shall charge another nominee to form the Council of Ministers within fifteen days in case the Council of Ministers did not win the vote of confidence.

Article 77:

First: The conditions for assuming the post of the Prime Minister shall be the same as those for the President of the Republic, provided that he has a college degree or its equivalent and is over thirty-five years of age.

Second: The conditions for assuming the post of Minister shall be the same as those for members of the Council of Representatives, provided that he holds a college degree or its equivalent.

Article 78:

The Prime Minister is the direct executive authority responsible for the general policy of the State and the commander-in-chief of the armed forces. He directs the Council of Ministers, presides over its meetings, and has the right to dismiss the Ministers, with the consent of the Council of Representatives.

Article 79:

The Prime Minister and members of the Council of Ministers shall take the constitutional oath before the Council of Representatives according to the language stipulated in Article 50 of the Constitution.

Article 80:

The Council of Ministers shall exercise the following powers:

First: To plan and execute the general policy and general plans of the State and oversee the work of the ministries and departments not associated with a ministry.

Second: To propose bills.

Third: To issue rules, instructions, and decisions for the purpose of implementing the law.

Fourth: To prepare the draft of the general budget, the closing account, and the development plans.

Fifth: To recommend to the Council of Representatives that it approve the appointment of undersecretaries, ambassadors, state senior officials, the Chief of Staff of the Armed Forces and his deputies, division commanders or higher, the Director of the National Intelligence Service, and heads of security institutions.

Sixth: To negotiate and sign international agreements and treaties, or designate any person to do so.

Article 81:

First: The President of the Republic shall take up the office of the Prime Minister in the event the post becomes vacant for any reason whatsoever.

Second: If the event mentioned in “First” of this Article occurs, the President shall charge another nominee to form the Council of Ministers within a period not to exceed fifteen days in accordance with the provisions of Article 76 of this Constitution.

Article 82:

A law shall regulate the salaries and allowances of the Prime Minister and Ministers, and anyone of their grade.

Article 83:

The responsibility of the Prime Minister and the Ministers before the Council of Representatives is of a joint and personal nature.

Article 84:

First: A law shall regulate the work and define the duties and authorities of the security institutions and the National Intelligence Service, which shall operate in accordance with the principles of human rights and shall be subject to the oversight of the Council of Representatives.

Second: The National Intelligence Service shall be attached to the Council of Ministers.

Article 85:

The Council of Ministers shall establish internal bylaws to organize the work therein.

Article 86:

A law shall regulate the formation of ministries, their functions, and their specializations, and the authorities of the minister.

## Chapter Three
## [The Judicial Power]

Article 87:

The judicial power is independent. The courts, in their various types and levels, shall assume this power and issue decisions in accordance with the law.

Article 88:
Judges are independent, and there is no authority over them except that of the law. No power shall have the right to interfere in the judiciary and the affairs of justice.

Article 89:
The federal judicial power is comprised of the Higher Juridical Council, the Federal Supreme Court, the Federal Court of Cassation, the Public Prosecution Department, the Judiciary Oversight Commission, and other federal courts that are regulated in accordance with the law.

## First: Higher Juridical Council

Article 90:
The Higher Juridical Council shall oversee the affairs of the judicial committees. The law shall specify the method of its establishment, its authorities, and the rules of its operation.

Article 91:
The Higher Juridical Council shall exercise the following authorities:

First: To manage the affairs of the judiciary and supervise the federal judiciary.

Second: To nominate the Chief Justice and members of the Federal Court of Cassation, the Chief Public Prosecutor, and the Chief Justice of the Judiciary Oversight Commission, and to present those nominations to the Council of Representatives to approve their appointment.

Third: To propose the draft of the annual budget of the federal judicial authority, and to present it to the Council of Representatives for approval.

## Second: Federal Supreme Court

Article 92:

First: The Federal Supreme Court is an independent judicial body, financially and administratively.

Second: The Federal Supreme Court shall be made up of a number of judges, experts in Islamic jurisprudence, and legal scholars, whose number, the method of their selection, and the work of the Court shall be determined by a law enacted by a two-thirds majority of the members of the Council of Representatives.

Article 93:
The Federal Supreme Court shall have jurisdiction over the following:

First: Overseeing the constitutionality of laws and regulations in effect.

Second: Interpreting the provisions of the Constitution.

Third: Settling matters that arise from the application of the federal laws, decisions, regulations, instructions, and procedures issued by the federal authority. The law shall guarantee the right of direct appeal to the Court to the Council of Ministers, those concerned individuals, and others.

Fourth: Settling disputes that arise between the federal government and the governments of the regions and governorates, municipalities, and local administrations.

Fifth: Settling disputes that arise between the governments of the regions and governments of the governorates.

Sixth: Settling accusations directed against the President, the Prime Minister and the Ministers, and this shall be regulated by law.

Seventh: Ratifying the final results of the general elections for membership in the Council of Representatives.

Eight:

A. Settling competency disputes between the federal judiciary and the judicial institutions of the regions and governorates that are not organized in a region.
B. Settling competency disputes between judicial institutions of the regions or governorates that are not organized in a region.

Article 94:
Decisions of the Federal Supreme Court are final and binding for all authorities.

## Third: General Provisions

Article 95:
The establishment of special or extraordinary courts is prohibited.

Article 96:
The law shall regulate the establishment of courts, their types, levels, and jurisdiction, and the method of appointing and the terms of service of judges and public prosecutors, their discipline, and their retirement.

Article 97:
Judges may not be removed except in cases specified by law. Such law will determine the particular provisions related to them and shall regulate their disciplinary measures.

Article 98:
A judge or public prosecutor is prohibited from the following:

First: Combining a judicial position with legislative and executive positions and any other employment.

Second: Joining any party or political organization or performing any political activity.

Article 99:
A law shall regulate the military judiciary and shall specify the jurisdiction of military courts, which are limited to crimes of a military nature committed by members of the armed forces and security forces, and within the limits established by law.

Article 100:
It is prohibited to stipulate in the law the immunity from appeal for any administrative action or decision.

Article 101:
A State Council may be established, specialized in functions of the administrative judiciary, issuing opinions, drafting, and representing the State and various public commissions before the courts except those exempted by law.

## Chapter Four
## [Independent Commissions]

Article 102:

The High Commission for Human Rights, the Independent Electoral Commission, and the Commission on Public Integrity are considered independent commissions subject to monitoring by the Council of Representatives, and their functions shall be regulated by law.

Article 103:

First: The Central Bank of Iraq, the Board of Supreme Audit, the Communication and Media Commission, and the Endowment Commissions are financially and administratively independent institutions, and the work of each of these institutions shall be regulated by law.

Second: The Central Bank of Iraq is responsible before the Council of Representatives. The Board of Supreme Audit and the Communication and Media Commission shall be attached to the Council of Representatives.

Third: The Endowment Commissions shall be attached to the Council of Ministers.

Article 104:

A commission named The Martyrs' Foundation shall be established and attached to the Council of Ministers, and its functions and competencies shall be regulated by law.

Article 105:

A public commission shall be established to guarantee the rights of the regions and governorates that are not organized in a region to ensure their fair participation in managing the various state federal institutions, missions, fellowships, delegations, and regional and international conferences. The commission shall be comprised of representatives of the federal government and representatives of the regions and governorates that are not organized in a region, and shall be regulated by a law.

Article 106:

A public commission shall be established by a law to audit and appropriate federal revenues. The commission shall be comprised of experts from the federal government, the regions, the governorates, and its representatives, and shall assume the following responsibilities:

First: To verify the fair distribution of grants, aid, and international loans pursuant to the entitlement of the regions and governorates that are not organized in a region.

Second: To verify the ideal use and division of the federal financial resources.

Third: To guarantee transparency and justice in appropriating funds to the governments of the regions and governorates that are not organized in a region in accordance with the established percentages.

Article 107:
A council named the Federal Public Service Council shall be established and shall regulate the affairs of the federal public service, including appointments and promotions, and its formation and competencies shall be regulated by law.

Article 108:
Other independent commissions may be established by law, according to need and necessity.

## Section Four

## Powers of the Federal Government

Article 109:
The federal authorities shall preserve the unity, integrity, independence, and sovereignty of Iraq and its federal democratic system.

Article 110:
The federal government shall have exclusive authorities in the following matters:

First: Formulating foreign policy and diplomatic representation; negotiating, signing, and ratifying international treaties and agreements; negotiating, signing, and ratifying debt policies and formulating foreign sovereign economic and trade policy.

Second: Formulating and executing national security policy, including establishing and managing armed forces to secure the protection and guarantee the security of Iraq's borders and to defend Iraq.

Third: Formulating fiscal and customs policy; issuing currency; regulating commercial policy across regional and governorate boundaries in Iraq; drawing up the national budget of the State; formulating monetary policy; and establishing and administering a central bank.

Fourth: Regulating standards, weights, and measures.

Fifth: Regulating issues of citizenship, naturalization, residency, and the right to apply for political asylum.

Sixth: Regulating the policies of broadcast frequencies and mail.

Seventh: Drawing up the general and investment budget bill.

Eighth: Planning policies relating to water sources from outside Iraq and guaranteeing the rate of water flow to Iraq and its just distribution inside Iraq in accordance with international laws and conventions.

Ninth: General population statistics and census.

Article 111:
Oil and gas are owned by all the people of Iraq in all the regions and governorates.

Article 112:

First: The federal government, with the producing governorates and regional governments, shall undertake the management of oil and gas extracted from present fields, provided that it distributes its revenues in a fair manner in proportion to the population distribution in all parts of the country, specifying an allotment for a specified period for the damaged regions which were unjustly deprived of them by the former regime, and the regions that were damaged afterwards in a way that ensures balanced development in different areas of the country, and this shall be regulated by a law.

Second: The federal government, with the producing regional and governorate governments, shall together formulate the necessary strategic policies to develop the oil and gas wealth in a way that achieves the highest benefit to the Iraqi people using the most advanced techniques of the market principles and encouraging investment.

Article 113:

Antiquities, archeological sites, cultural buildings, manuscripts, and coins shall be considered national treasures under the jurisdiction of the federal authorities, and shall be managed in cooperation with the regions and governorates, and this shall be regulated by law.

Article 114:

The following competencies shall be shared between the federal authorities and regional authorities:

First**:** To manage customs, in coordination with the governments of the regions and governorates that are not organized in a region, and this shall be regulated by a law.

Second: To regulate the main sources of electric energy and its distribution.

Third: To formulate environmental policy to ensure the protection of the environment from pollution and to preserve its cleanliness, in cooperation with the regions and governorates that are not organized in a region.

Fourth: To formulate development and general planning policies.

Fifth**:** To formulate public health policy, in cooperation with the regions and governorates that are not organized in a region.

Sixth**:** To formulate the public educational and instructional policy, in consultation with the regions and governorates that are not organized in a region.

Seventh**:** To formulate and regulate the internal water resources policy in a way that guarantees their just distribution, and this shall be regulated by a law.

Article 115:

All powers not stipulated in the exclusive powers of the federal government belong to the authorities of the regions and governorates that are not organized in a region. With regard to other powers shared between the federal government and the regional government, priority shall be given to the law of the regions and governorates not organized in a region in case of dispute.

# Section Five

# Powers of the Regions

## Chapter One
## [Regions]

Article 116:
The federal system in the Republic of Iraq is made up of a decentralized capital, regions, and governorates, as well as local administrations.

Article 117:

First: This Constitution, upon coming into force, shall recognize the region of Kurdistan, along with its existing authorities, as a federal region.

Second: This Constitution shall affirm new regions established in accordance with its provisions.

Article 118:
The Council of Representatives shall enact, in a period not to exceed six months from the date of its first session, a law that defines the executive procedures to form regions, by a simple majority of the members present.

Article 119:
One or more governorates shall have the right to organize into a region based on a request to be voted on in a referendum submitted in one of the following two methods:

First: A request by one-third of the council members of each governorate intending to form a region.

Second: A request by one-tenth of the voters in each of the governorates intending to form a region.

Article 120:
Each region shall adopt a constitution of its own that defines the structure of powers of the region, its authorities, and the mechanisms for exercising such authorities, provided that it does not contradict this Constitution.

Article 121:

First: The regional powers shall have the right to exercise executive, legislative, and judicial powers in accordance with this Constitution, except for those authorities stipulated in the exclusive authorities of the federal government.

Second: In case of a contradiction between regional and national legislation in respect to a matter outside the exclusive authorities of the federal government, the regional power shall have the right to amend the application of the national legislation within that region.

Third: Regions and governorates shall be allocated an equitable share of the national revenues sufficient to discharge their responsibilities and duties, but having regard to their resources, needs, and the percentage of their population.

Fourth: Offices for the regions and governorates shall be established in embassies and diplomatic missions, in order to follow cultural, social, and developmental affairs.

Fifth: The regional government shall be responsible for all the administrative requirements of the region, particularly the establishment and organization of the internal security forces for the region such as police, security forces, and guards of the region.

## Chapter Two
## [Governorates that are not incorporated in a region]

Article 122:

First: The governorates shall be made up of a number of districts, sub-districts, and villages.

Second: Governorates that are not incorporated in a region shall be granted broad administrative and financial authorities to enable them to manage their affairs in accordance with the principle of decentralized administration, and this shall be regulated by law.

Third: The governor, who is elected by the Governorate Council, is deemed the highest executive official in the governorate to practice his powers authorized by the Council.

Fourth: A law shall regulate the election of the Governorate Council, the governor, and their powers.

Fifth: The Governorate Council shall not be subject to the control or supervision of any ministry or any institution not linked to a ministry. The Governorate Council shall have independent finances.

Article 123:
Powers exercised by the federal government can be delegated to the governorates or vice versa, with the consent of both governments, and this shall be regulated by law.

## Chapter Three
## [The Capital]

Article 124:
First: Baghdad in its municipal borders is the capital of the Republic of Iraq and shall constitute, in its administrative borders, the governorate of Baghdad.

Second: This shall be regulated by a law.

Third: The capital may not merge with a region.

## Chapter Four
## [The Local Administrations]

Article 125:
This Constitution shall guarantee the administrative, political, cultural, and educational rights of the various nationalities, such as Turkomen, Chaldeans, Assyrians, and all other constituents, and this shall be regulated by law.

# Section Six

# Final and Transitional Provisions

## Chapter One
## [Final Provisions]

Article 126:

First: The President of the Republic and the Council of the Ministers collectively, or one-fifth of the Council of Representatives members, may propose to amend the Constitution.

Second: The fundamental principles mentioned in Section One and the rights and liberties mentioned in Section Two of the Constitution may not be amended except after two successive electoral terms, with the approval of two-thirds of the members of the Council of Representatives, the approval of the people in a general referendum, and the ratification by the President of the Republic within seven days.

Third: Other articles not stipulated in clause "Second" of this Article may not be amended, except with the approval of two-thirds of the members of the Council of Representatives, the approval of the people in a general referendum, and the ratification by the President of the Republic within seven days.

Fourth: Articles of the Constitution may not be amended if such amendment takes away from the powers of the regions that are not within the exclusive powers of the federal authorities, except by the approval of the legislative authority of the concerned region and the approval of the majority of its citizens in a general referendum.

Fifth:

A- An amendment is considered ratified by the President of the Republic after the expiration of the period stipulated in clauses "Second" and "Third" of this Article, in case he does not ratify it.

B- An amendment shall enter into force on the date of its publication in the Official Gazette.

Article 127:

The President of the Republic, the Prime Minister, members of the Council of Ministers, the Speaker of the Council of Representatives, his two Deputies, members of the Council of Representatives, members of the Judicial Authority, and people of special grades may not use their influence to buy or rent any state properties, to rent or sell any of their assets

to the state, to sue the state for these assets, or to conclude a contract with the state under the pretense of being building contractors, suppliers, or concessionaires.

Article 128:
The laws and judicial judgments shall be issued in the name of the people.

Article 129:
Laws shall be published in the Official Gazette and shall take effect on the date of their publication, unless stipulated otherwise.

Article 130:
Existing laws shall remain in force, unless annulled or amended in accordance with the provisions of this Constitution.

Article 131:
Every referendum mentioned in this Constitution is deemed successful with the approval of the majority of the voters unless otherwise stipulated.

## Chapter Two
## [Transitional Provisions]

Article 132:

First: The State shall guarantee care for the families of the martyrs, political prisoners, and victims of the oppressive practices of the defunct dictatorial regime.

Second: The State shall guarantee compensation to the families of the martyrs and the injured as a result of terrorist acts.

Third: A law shall regulate matters mentioned in clauses “First” and “Second” of this Article.

Article 133:
The Council of Representatives shall adopt in its first session the bylaws of the Transitional National Assembly until it adopts its own bylaws.

Article 134:

The Iraqi High Tribunal shall continue its duties as an independent judicial body, in examining the crimes of the defunct dictatorial regime and its symbols. The Council of Representatives shall have the right to dissolve it by law after the completion of its work.

Article 135:

First: The High Commission for De-Ba'athification shall continue its functions as an independent commission, in coordination with the judicial authority and the executive institutions within the framework of the laws regulating its functions. The Commission shall be attached to the Council of Representatives.

Second: The Council of Representatives shall have the right to dissolve this Commission by an absolute majority after the completion of its function.

Third: A nominee to the positions of the President of the Republic, the Prime Minister, the members of the Council of Ministers, the Speaker, the members of the Council of Representatives, the President, members of the Federation Council, their counterparts in the regions, or members of the judicial commissions and other positions covered by de-Ba'athification statutes pursuant to the law may not be subject to the provisions of de-Ba'athification.

Fourth: The conditions stated in clause "Third" of this Article shall remain in force unless the Commission stated in item "First" of this Article is dissolved.

Fifth: Mere membership in the dissolved Ba'ath party shall not be considered a sufficient basis for referral to court, and a member shall enjoy equality before the law and protection unless covered by the provisions of De-Ba'athification and the directives issued according to it.

Sixth: The Council of Representatives shall form a parliamentary committee from among its members to monitor and review the executive procedures of the Higher Commission for De-Ba'athification and state institutions to guarantee justice, objectivity, and transparency and to examine their consistency with the laws. The committee's decisions shall be subject to the approval of the Council of Representatives.

Article 136:

First: The Property Claims Commission shall continue its functions as an independent commission in coordination with the judicial authority and the executive institutions in accordance with the law. The Property Claims Commission shall be attached to the Council of Representatives.

Second: The Council of Representatives shall have the right to dissolve the Commission by a two-thirds majority vote of its members.

Article 137:
Application of the provisions of the articles related to the Federation Council, wherever it may be cited in this Constitution, shall be postponed until the Council of Representatives issues a decision by a two-thirds majority vote in its second electoral term that is held after this Constitution comes into force.

Article 138:

First: The expression "the Presidency Council" shall replace the expression "the President of the Republic" wherever the latter is mentioned in this Constitution. The provisions related to the President of the Republic shall be reactivated one successive term after this Constitution comes into force.

Second:

A. The Council of Representatives shall elect the President of the State and two Vice Presidents who shall form a Council called the "Presidency Council," which shall be elected by one list and with a two-thirds majority.

B. The provisions to remove the President of the Republic present in this Constitution shall apply to the President and members of the Presidency Council.

C. The Council of Representatives may remove a member of the Presidency Council with a three-fourths majority of the number of its members for reasons of incompetence and dishonesty.

D. In the event of a vacant seat in the Presidency Council, the Council of Representatives shall elect a replacement by a two-thirds majority vote of its members.

Third: Members of the Presidency Council shall be subject to the same conditions as a member of the Council of Representatives and must:

A. Be over forty years of age.
B. Enjoy good reputation, integrity and uprightness.
C. Have quit the dissolved (Ba'ath) Party ten years prior to its fall, in case he was a member of it.
D. Have not participated in suppressing the 1991 and Al-Anfal uprisings. He must not have committed a crime against the Iraqi people.

Fourth: The Presidency Council shall issue its decisions unanimously and any member may delegate to one of the two other members to take his place.

Fifth:

A- Legislation and decisions enacted by the Council of Representatives shall be forwarded to the Presidency Council for their unanimous approval and for its issuance within ten days from the date of delivery to the Presidency Council, except the stipulations of Articles 118 and 119 that pertain to the formation of regions.

B- In the event the Presidency Council does not approve, legislation and decisions shall be sent back to the Council of Representatives to reexamine the disputed issues and to vote on them by the majority of its members and then shall be sent for the second time to the Presidency Council for approval.

C- In the event the Presidency Council does not approve the legislation and decisions for the second time within ten days of receipt, the legislation and decisions are sent back to the Council of Representatives, which has the right to adopt it by three-fifths majority of its members, which may not be challenged, and the legislation or decision shall be considered ratified.

Sixth: The Presidency Council shall exercise the powers of the President of the Republic stipulated in this Constitution.

Article 139:

The Prime Minister shall have two deputies in the first electoral term.

Article 140:

First: The executive authority shall undertake the necessary steps to complete the implementation of the requirements of all subparagraphs of Article 58 of the Transitional Administrative Law.

Second: The responsibility placed upon the executive branch of the Iraqi Transitional Government stipulated in Article 58 of the Transitional Administrative Law shall extend and continue to the executive authority elected in accordance with this Constitution, provided that it accomplishes completely (normalization and census and concludes with a referendum in Kirkuk and other disputed territories to determine the will of their citizens), by a date not to exceed the 31st of December 2007.

Article 141:

Legislation enacted in the region of Kurdistan since 1992 shall remain in force, and decisions issued by the government of the region of Kurdistan, including court decisions and contracts, shall be considered valid unless they are amended or annulled pursuant to the laws of the region of Kurdistan by the competent entity in the region, provided that they do not contradict with the Constitution.

Article 142:

First: The Council of Representatives shall form at the beginning of its work a committee from its members representing the principal components of the Iraqi society with the mission of presenting to the Council of Representatives, within a period not to exceed four months, a report that contains recommendations of the necessary amendments that could be made to the Constitution, and the committee shall be dissolved after a decision is made regarding its proposals.

Second: The proposed amendments shall be presented to the Council of Representatives all at once for a vote upon them, and shall be deemed approved with the agreement of the absolute majority of the members of the Council.

Third: The articles amended by the Council of Representatives pursuant to item "Second" of this Article shall be presented to the people for voting on them in a referendum within a period not exceeding two months from the date of their approval by the Council of Representatives.

Fourth: The referendum on the amended Articles shall be successful if approved by the majority of the voters, and if not rejected by two-thirds of the voters in three or more governorates.

Fifth: Article 126 of the Constitution (concerning amending the Constitution) shall be suspended, and shall return into force after the amendments stipulated in this Article have been decided upon.

Article 143:
The Transitional Administrative Law and its Annex shall be annulled on the seating of the new government, except for the stipulations of Article 53(A) and Article 58 of the Transitional Administrative Law.

Article 144:
This Constitution shall come into force after the approval of the people thereon in a general referendum, its publication in the Official Gazette, and the seating of the government that is formed pursuant to this Constitution.

# Regulations for Implementing Government Contracts

في

- الاقتصاد
- اتحادي

**قانون رقم الوثيقه- الهويه التعريفيه-:** 1

**نوع القانون:** تنظيمات

**تاريخ الاصدار:** 1 May 2008

**تاريخ النشر:** 19 May 2008

**حاله:** نافذ المفعول

**خلاصه:** According to the provisions of paragraph 1 of Section 14 of the Order of the Coalition Provisional Authority (dissolved) No. 87 of 2008 We issue the following regulations.

According to the provisions of paragraph 1 of Section 14 of the Order of the Coalition Provisional Authority (dissolved) No. 87 of 2008
We issue the following regulations:
No. 1 of 2008
Regulations for Implementing Government Contracts
Article 1
These regulations are to clarify the general principles for implementing government contracts that state bodies and the public sector conclude in the areas of public tenders, supply of goods and services, and consultant contracts with Iraqi and non-Iraqi parties. These regulations shall set the implementation methods of tenders, determine the duly authorized bodies for opening tenders and bids, determine methods of appeal in its decisions before the administrative court and provide that contracting procedures shall be characterized by transparency, predictability and fairness in competition.
Article 2
First- The provisions of these regulations shall cover all contracts concluded by state bodies (state entities and public sector) as represented by ministries, entities not related to a ministry, regions and governorates with Iraqi and non-Iraqi parties in order to implement public projects contracts, consultation contracts or for the supply of products and services.
Second- These regulations shall apply for state projects and contracts financed by international or regional organizations according to agreements or special protocols concluded with Iraqi parties for this purpose. It shall be permissible to use what is stated in these regulations as guidance for what is not stipulated in the text of applicable contract agreements, or protocols, and in a manner not inconsistent with the rules and regulations approved by these organizations.
Article 3
The text of No. 3 of paragraph (D) of item First of Article 3 of the Regulations Implementing Government Contracts No. 1 of 2008 was repealed.
According to the first amendment of the Regulations Implementing Government Contracts No. 2 of 2010:
First- The contracting parties in ministries and entities not associated with a ministry and regions and governorates not organized into a region shall meet the following requirements before preparing tender and bid documents:
A- A previous approval from the Ministry of Planning and Development Cooperation regarding a technical and economic feasibility study regarding the projects by the authorized parties accompanied with an application for project (application for follow-up of implementing investment

projects), when discussing the project in order to enlist it within the plan in accordance with the regulations No.1 of 1984, and its amendments, issued by the disbanded Planning Council.
B- An updated study regarding the project’s estimated cost for the required work in order to use it as a measure for analyzing bids and implementing contracts provided that confidentiality is maintained.
C- The availability of allocated amounts within the federal general budget as supported by the competent authorities for the implementation of the contract. There should be within the bidding documents an indication as to the special classification of the project within the plan.
D- All terms, specifications, quantity schedules, maps and other aspects that are necessary for implementation shall be prepared in a way to avoid any changes during implementation, or additions during implementation, taking into account the following:
1- Duly authorized financial authorities to decide the subject stated in Special Federal Budget Law.
2- Special rules for implementing projects through completion in the regulations of investment projects for the general federal budget.
3- Head of the contracting entity may make changes by adding volumes for supplies contracts, and consultation services, not exceeding 20% of the value of the contract when funds are available.
4. Rules and procedures for examining contractors' compensation requests as a result of increase in prices and which are issued by the Ministry of Planning and Development Cooperation in this regard.
E. An approval by the related parties as to the site and the land for the project or for the works when implementing public works contracts.
F- All legal and financial problems at the work site, if any, including procedures for site possession, shall be addressed when implementing public works tenders.
G- The site shall be prepared to start work, totally or partially, within the time schedule.
H- Taking any necessary procedures that may be needed according to the nature of the required project or contract.
Second- The value of one set of general and limited contract documents and tenders is estimated through two stages by a price in accordance with its relative importance and cost of establishing the project and shall ensure participation in the project and the contractor who has previously participated in the re-announced tender, has the right to submit the previous purchase receipt, for participation, accompanied with the bid documents. In case of amending the purchase prices of tender documents then the participating party shall cover the difference between the two prices and shall accompany his tender with the first and second receipts.
Third- A- The announcement shall be published in at least three official newspapers, taking into consideration that the newspaper published by the Ministry of Finance shall be one of these newspapers. If the Ministry of Finance newspaper ceases to exist then the announcement shall be published in widely distributed newspapers provided that the winner of the bid shall pay for the expenses of publication and last announcement. The import of foodstuff and medicine shall be exempt from this request taking into account the provisions (1) of Paragraph (C) of Item First of Article 5 of these regulations.
B- The tender announcement shall be issued on the Ministry's website and on the Ministry’s bulletin board, and also with the commercial attachés of the Iraqi Embassies and the site of United Nations for Business Development and DGMARKET regarding international general tenders.

Article 4

The text of Paragraph (A) of Item Four and the text of Item Five of Article 4 according to Article 2 of Item First and Second of the first amendment of Regulations Implementing Government Contracts No. 1 of 2010 were repealed, and replaced with the following:
The contracting party may use the following tender methods when implementing budget projects or general contracts of all kinds.
First- General Tender: This shall be either national or international determined per the authorities granted to the head of the contracting party and taking into account the nature of the contract and its value. This tender shall be conducted through an announced invitation for those who have the desire to participate in implementing projects with values not less than 50,000,000 Iraqi Dinar or any other amount determined by the concerned parties taking into consideration that procedures shall be conducted in a manner that is open to the public and competition is fair.
Second- Limited Tender: This is conducted by an announced invitation to all those who have the desire and qualifications to participate in contracts with values not less than 50,000,000 Iraqi Dinar, or any other amount determined by the competent authorities, and includes two phases:
A- Phase One: It includes submitting special documents concerning the qualifications of participants in the tender and according to the applicable legal documents relevant to the topic. These documents are evaluated so as to select contractors that are qualified to participate in the second

phase.
B- Phase Two: An invitation (free of charges) for not less than six qualified contractors to participate in the tender in order to evaluate their technical and financial abilities in relation to their bids.
Third-Tender in two stages:
A- The head of the contracting party or any duly authorized person may use tender of two stages to determine the best way to meet the contractual needs. This method shall be used for contracts of complicated technical descriptions, or when it is necessary to apply descriptions, but not necessary to draft details of the technical descriptions, to determine characteristics or features accurately for the goods, or works, in the case of services.
B- It may be permissible to start the process of submitting bids during the pre-qualification stage as stated in Item Second of this Article. For the purpose of implementing this method the following shall be taken into account:
1- Stage One: An invitation shall be submitted for bidders to submit their technical bids first based upon initial design and effectiveness to the head of the contracting party who may amend the estimated value when necessary.
2- Stage Two: Invitation of those winning bidders according to the technical specifications in Stage One to submit their financial bids according to stipulations determined by the contracting party.
Fourth- Direct Invitation-
A- This is conducted through an invitation for not less than three contractors and/or companies and/or other agencies that have the technical and financial capability to implement the contracts according to the following:
1) If bidders decline to participate in the announced tenders for the first time.
2) If the contract is a consulting contract.
3) If the contract is of a special nature and for reasons of maintaining secrecy in the implementation, or speed in completion, or for security reasons.
4) If the purpose is to achieve speed and efficiency in implementation in cases of emergency and natural disasters, preparing medicines or life saving tools.
B- Supplying contractors and consultants the bidding documents free of charge.
C- Those who submit bids based upon direct invitation shall be exempted from providing security deposits.
D- Financial consideration shall be taken into account when referrals are delivered based upon this method.
Fifth: Single Bid Method- Free invitation from the contracting parties to one bidder regarding single source contracts to provide supplies, execute works, special consulting or manufacturing when it is necessary and when there is a justifications taking into account the following procedures:
A- Informing the Central Contracts Committee in the General Secretary of the Council of Ministers for the purpose of implementing the contract using these methods accompanied with justification provided that this document is submitted by the contracting parties in ministries and entities not related to the ministry and regions and governorates not organized into a region.
B- Financial authorities approved by the contracting parties in implementing public works and the central contracting committee of the Council of Ministers shall be informed of this for the purpose of approving the recommendations of bidding committees when the contracting authority falls outside the jurisdiction of the head of the contracting party.
C- In case the central contracting committee does not decide or approve the applications submitted by the contracting parties within a period of not more than fourteen days from date of registration before said committee, then the approval shall be assumed and the contracting parties shall maintain secrecy in the process of awarding a contract and its implementation.
D- The entity that receives the invitation shall be exempted from depositing securities.
Sixth- Purchasing Committees:This method is conducted in respect to commodities and services whose values are less than 50,000,000 Iraqi Dinar, or any other amount determined in the current budget, taking into consideration the special regulations issued by the Ministry of Planning and Development Cooperation in coordination with relevant parties to the subject.
Article 5
The text of paragraph (C) of Item One and Item Four of Article 5 according to Article 3 of Items First and Second were repealed, and replaced with the following:
First- The following procedures shall be followed when advertising for the general bidding:
A- Name of tender, its number, address and the category listed in the budget.
B- A brief description of the project or contract along with details of the required goods and

services.

C- The announcement period for the tender or for the direct invitation as follows:

1) Period of 1-60 days shall be determined according to the importance of the contract and assessment of the head of the contracting party and shall start from the date of last announcement in the newspaper.

2) Contracts for supplying foodstuffs and medicines shall be excluded from item 1 of this paragraph.

3) Period of submitting bids for direct invitation and single tender shall be determined according to the estimate of the head of the contracting party.

D- Specify the date and the place for submitting bids, the expiration period and the place and date of selling tender documents.

E- Determination of preliminary security deposits of submitted tenders.

F- The tender's closing date.

G- The price of tender documents is non-refundable.

H- The contracting party website and email address for the administrative entity responsible for tenders.

Second- The information for those who submit tenders (public works, consulting services and supplies) shall include:

A- General principles of the contract to be signed, method of wages, or agreed upon amounts as a percentage or lump sum, or paid expenses and other means, taking into account the provisions related to the subject in regard to the federal general state budget.

B- Specify government ownership of the designs, maps and the specifications prepared by the party to which invitation was submitted directly when contracting with it, except in special cases based upon the approval of the relevant minister. These parties shall prevent disclosure of any information regarding the nature of the contract, unless there is specific authorization from the relevant ministry.

C- The bidders shall attach other bids of similar works, if they have any, as verification of qualification.

D- Specifying the date and place for opening bids.

E- The contractors shall clarify capabilities of their technical staff and specialized full-time and the part-time employees during the implementation of different projects or consulting contracts.

F- Contractors shall submit an implementation plan for the required work.

G- Determine the meeting date of a special conference regarding issues raised by participants in the tender, which shall be on a date within seven days before the closing date of the tender, with the exception of bids for supplying foodstuffs.

H- The grade and classification of the required Iraqi contractor as related to the public works project contracts to be implemented. The foundation certificate and the professional practice certificate as regards the companies and officially licensed offices.

I- The cost price for the supply contracts is determined in light of the place of arrival (CIP, CFR, CIF, FOB and others).

J- Determining late penalties in light of the contracting provisions (shipping delay penalties, delivery delay penalties).

K- The contracting party shall not be obliged to accept the lowest bids.

L- The state contracting party may cancel the bid without compensation and purchase cost of tender documents shall be reimbursed.

M- Include other information for contractors, or documents needed according to the nature of the work being implemented or materials needed or any consultations which need to be submitted.

N- Recording bid prices in writing or in numbers.

O- It shall not be permissible for the contractors to cancel any item of the tender documents or any procedures whatever its nature.

P- The tender documents shall include the approved mechanism for calculating the preponderance of winning used in analyzing bids.

Q- It shall not be permissible for those employed by the state or the public sector to participate in bids either directly or indirectly.

R- Request from those contractors submitting bids to provide their website address, email address and address of the person in charge for follow-up questions regarding the tender in their tender documents.

Third- the contracting party may extend the announcement period for the tender one time when necessary and taking into account the following:

A- Approval of the head of the contracting agency or any duly authorized person taking into account the financial authorities for contracting purposes.

B- Issuance of an annex announced in the same newspaper where the announcement was published and a copy shall be sent to all participants in the tender. Before the last date to accept the bids.

Fourth- If the bid exceeds 25% of the estimated budget, the head of the contracting party or any duly authorized person may accept the bid and analyze it provided there are sufficient funds within the total cost of the project and on the condition that the Ministry of Planning is informed.

Fifth- There shall be a re-announcement of bids in one of the following cases:

A- If bids are not submitted within the period of the announcement or in case of submittal of only one bid within this period taking into account that in case of submittal of more than one bid, and one of them is acceptable technically and commercially, then it shall be accepted and the process of analyzing and assigning the bids shall be performed.

B- If the amount of the best bid for those contractors exceeds the percentage determined in item Fourth of this article when analyzing the estimated cost for the purpose of contracting for implementing projects or listed work in the budget.

C- The head of the contracting party, or any authorized person, may accept a bid and analyze it if it exceeds the estimated costs for purposes of contracting by no more than 30%, provided there are sufficient funds and within the total cost of the project. The central contracting committee of the general secretariat of the prime ministry shall be informed of the justification in order to obtain approval of the award of the contract. The committee shall make the appropriate decision within a period of 14 working days from date of registering the request by the contracting party. Approval shall be presumed if there is no answer taking into account the authority stated in item Fourth of this article.

Sixth- The following procedures shall be followed in case of re-announcement:

A- Getting the approval of the concerned minister or the head of the agency which is not connected to any ministry or by any authorized person while informing the Ministry of Planning and Development Cooperation of this and determining the period of announcement in accordance with the provisions of paragraph C of item First of Article 5 of these regulations.

B- Informing the contractors who have participated in the past tender of the re-announcement.

C- The same serial number of the past tender shall be adopted for the new tender and that is to be mentioned in the new announcement.

D- Informing the concerned parties of the re-announcement.

E- Investigation of the reasons for lack of participation in the first announcement of the bid.

F- In case of re-announcement for the second time a single-tender bid shall be acceptable upon the following basis:

1. The cost of tender shall be within the estimated cost taking into account item Fourth and paragraph C of item Fifth of this article for the purpose of allocating the project funds or contract implementation.
2. The tender shall meet the technical specifications or the required conditions in the tender announcement.
3. In case that the price of the best bid after the second announcement occurred is more than the estimated cost stated in item Fourth and paragraph C of item Fifth of this article for the purpose of contracting to implement the project or the work, the Ministry of Planning and Development Cooperation shall be informed to take one of the following procedures:,

A- Postponement of implementing the project to the next year.

B- Benefiting of the amount allocated for implementing other projects.

C- Increase of the total cost for purpose of contracting within the total cost of the project in the plan.

4. In the case where no acceptable bid is submitted in the second announcement then the head of the contracting agency either may choose to make a third and last announcement or do whatever is necessary to change the method of implementing the contract taking into account the means approved in this regard.

The provisions of items First, Second, Third, Fourth, Fifth and Sixth of this article shall apply to construction contracts for civil, electrical, mechanical, and chemical engineering and preparing contract and consulting services contracts.

Article 6

Formations of the Bid Opening and Divisions and its Tasks

First- A Central Bid Opening Committee, or more than one, is to be formed in each ministry or any

agency not related to a ministry, for the opening of bids. This Committee is to be headed by an employee whose grade is not less than a general director, with members representing the legal and finance directorates of the contracting party, in addition to an employee with an engineer title and a secretary whose job title is not less than superintendent.

Second- It is permissible to form a Bid Opening Committee within the structure of a related ministry or the other agencies that are not related to a ministry. Each of these committees is formed as it is stipulated in the first section of this article.

Third- A Bid Opening Committee shall be formed in each region, or governorates not organized into a region, headed by the head of the contracting party or any duly authorized person and memberships of two persons having specializations (legal, financial, technical, and the contracting party), and a representative of the governorate council whose job title is not less than a superintendent. Its duty is to open the bids that are announced within the region or the governorate.

Fourth-A Bid Opening Committee may be formed within the departments of any region or governorate. Such committees will be formed on a similar basis as that mentioned in the third section of this article.

Fifth- Bid Opening Committees shall follow the following procedures when carrying out its duties:

A- The bids are to be kept in a special box of the concerned department backed by a receipt prepared in two copies. One receipt copy is given to the contractor whereas the second copy is to be kept with concerned department. In addition, the following information will be recorded in a special register:

1. Name and number of the tender as mentioned in its documents.
2. Name of the contractor and contractor’s official representative with full address inside or outside Iraq.
3. Name of the officially authorized bearer of the tender, address and signature.
4. Time and date of submitting the bid.
5. Additional attachments included with the bid, if any.
6. Bids may be sent by secure mail service (registered mail) and received before the closing date of the tender. The secretary of the Committee must register these tenders upon receipt.
7. It shall not be permissible to give any information to any un-related entity regarding the names and addresses of the bidders or their representatives during the period of the announcement to maintain the confidentiality of procedures.

B- The head of Bids Opening Committee shall assure the presence of committee members and in case some of them are absent then employees of similar specializations shall replace them as determined by the head of the contracting party or any duly authorized person.

C- The Bids Opening Committee shall meet directly after the ending of the identified closing date of the tender or at the beginning of the official starting hour of the next day. The Committee opens the bids publicly with the attendance of the contractor’s representatives, in a previously specified place. This is to be recorded in official minutes wherein the following should be specified:

1. Verify presence of stamps over bid covers.
2. Bids that are not accompanied by the primary prepaid bond amounts.
3. Bids that are based upon the reduction of a certain percentage rate or a fixed amount, out of the other bids that are being submitted for this tender.
4. The amendment of previous tender offers, whether technically or financially, and the bids which were presented during the announcement period shall be excluded. Old bids shall be returned to their owners.
5. Number of the pages that each bid is composed of.
6. Put a clear mark around each mark, erasure, addition or correction that appeared in the priced bill of quantity schedule, with the signature of the head and members of the Committee.
7. Put a horizontal line beside each paragraph, which is not priced within the priced bill of quantity schedule with the signature of the head and the members of the Committee.
8. Verify that the person who handed over the bid has signed all the pages of the priced bill of quantity schedule and attachments.

D. It shall be pointed out in the Committee’s report the remarks or their reservations related to issues shown in the bid and the attachments.

E- Mark all the pages of the bid with the Committee’s stamp and mark all of the priced bill of quantity schedule with the signature of all Committee members.

F- Marking all pages of the bid with the signing of the seal of the Commission members on all pages of the bidder’s price chart.

G- Point out clearly any information or details that are not given with the bid, and that they shall

have to be given in accordance with tender instructions.
H- After opening of all bids as specified within these regulations, the head of the Bid Opening Committee will carry out the following:
1. Post the contractor’s prices on the announcement bill board as they are mentioned in their bids, emphasizing that the declared prices are subject to audit and analysis.
2. The Committee report is prepared and signed by the chairman, members and the representatives of the contractors with clarifying any notices about the committee’s work, if any.
I- Bids and their attachments are sent to the Bid Evaluation Committee through a special report.
Article 7
Formation of Bid Analysis and Evaluating Committees and their Tasks:
A Bid Analyzing and Evaluating Committee is to be formed in each directorate according to its needs for the studying and analyzing of the technical and financial aspects of a bid. The Committee is headed by a specialized and experienced employee whose job title shall be not less than a director general or chief engineer. The members of this Committee shall be specialized technicians including legal and financial persons. The Committee has the right to ask for help from other specialized parties who are experienced with the nature of the bid. All recommendations of this Committee shall be approved by the contracting party or any duly authorized person. The Bid Analysis and Evaluation Committee shall analyze bids by the following procedures:
First- Exclude bids that are not accompanied by the primary required prepaid bond amount.
Second- Exclude bids that are based on the reduction of a certain percentage or fixed amount out of any other submitted bids in this tender, and to refuse any reduction in the price submitted after the closing date of the tender.
Third- The process of analyzing the bids shall be carried out secretly. The final report shall be presented to the responsible authority of assignment within the period determined by the head of the contracting agency taking into account the award deadline for those who submitted bids.
Fourth- It shall not be permissible to send the bids outside Iraq to analyze them. But the consultants who are located outside Iraq shall send their representatives to Iraq to carry out the required analysis, unless the nature of the work requires otherwise, taking into consideration the approval of the concerned minister or head of the agency not related to the ministry or head of the contracting parties in the regions, and governorates not organized into a region or the central contracting committee of the Council of Ministers in accordance with the approved authorization. The original document may be kept by the contracting agency.
Fifth- In case there are certain deductions with certain rates or fixed amounts, the reserve amounts being shown within the quantitative schedule shall be offset as to the contractor’s prices for the purpose of comparison and analysis.
Sixth- Any reserve amounts of money in the price list of the bidders shall be excluded as well as not needed amounts from the bid documents when comparing and analyzing.
Seventh- Prices of all bids shall be calculated on a uniform basis. This shall be stipulated within the tender documents.
Eighth- The price that is taken into consideration is that which is mentioned in writing when it differs with that which is written in numerals and also the price of a unit is to be taken into consideration in case of error in the bid.
Ninth- If items are not priced within the submitted contract then the cost of this item or items will nonetheless be considered within the total cost of the bid.
Tenth- The following criteria will be followed to determine the best bid:
A. Reject bids which do not meet the required technical specifications, even if it is the lowest in cost.
B. Reject bids of contractors which do not show evidence of experience with previous contracts of similar work. This shall apply to contractors and consultants.
C. Consider the financial efficiency of the contractor through submitting final accounts certified by a chartered accountant for the previous year.
D. Volume of financial obligations of the contractor during the year.
E. The ability of the contractor to meet the completion dates and final acceptance.
F. The contractor should provide a listing of past works performed.
G. Availability of technical and skill capabilities for the implementation of the contract (engineering, technical staff, and special equipment). A list of the accomplished works or similar works if any.
Eleventh- If so indicated in the tender document, a priority rate is given to the bid offer in order to take into account the financial and technical aspects of the tender when nominated for the referral.

Twelfth- If a disagreement occurs among the Bid Analysis and Evaluation Committee members then this difference in opinions shall be written in the final report and the matter shall be decided by the head of the contracting agency.

Thirteenth- After the end of the analysis process a table shall be prepared of all bids with related details and shortcomings (if any) and make a comparison from technical, legal, and financial aspects.

Fourteenth- The final report shall include a special field indicating the recommendation of the Bid Analysis and Evaluation Committee stating the name of the nominated name to win the tender, his nationality according to the attached schedule, amount of tender, its currency, period of implementation, the principles referred to by the Committee in making this recommendation, and the amount of bid within the acceptable limits of estimated cost. The report shall be stamped with date after signature by the head and members of the Committee.

Fifteenth- It is not permissible to negotiate prices with the nominees.

Sixteenth- The Bid Analysis and Evaluation Committee may supplement the bid for short-listed contractors, as to missing data of minor importance.

Seventeenth- The contracting parties may request the release of the prepaid bond submitted with the bid before the end of the bidding analysis period or before the awarding of the tender to a contractor. It is done only upon the request of the contractor who does not expect the tender to be awarded to them, but in all cases such amounts are kept for the first three nominated contractors.

Eighteenth- Verifying the personal information required in the tender documents from the concerned parties before referral including documentary credits.

Nineteenth- The Bid Analysis and Evaluation Committee shall submit its recommendation of the referral to the head of the contracting agency for finalization according to the authorities given to him for the purpose of contracting.

Twentieth-

A- Financial considerations of contracts shall be taken into account and in case of exceeding the authority in contracting then the head of the contracting agency shall inform the central contracting authority of the Council of Ministers to obtain the necessary approvals for the purposes of contracting within a period not exceeding 14 days from the date of submission. Approval shall be presumed when it is not decided within the specified period of time.

B- Referral decisions shall be effective from the date of notification and signature of the contract within a period not exceeding 14 days from the date of notification after approval of the head of the contracting agency and informing the other bidders of the referral decision.

C- If the winning bidder refuses to sign the contract within the period stated in paragraph (B) of this item then the contracting agency shall issue a warning of the necessity to sign within 15 days from the date of notification and, in case of refusal, the contracting agency shall take the necessary procedures stated in item First of Article 16 of these regulations.

Article 8

Preparing Contract Formation:

First- All ministries and agencies not connected to a ministry shall organize their contracts in coordination with technical and financial departments and the beneficiary agencies and shall include provisions related to tender conditions or invitation adding any additional conditions agreed upon by the parties that guarantee safety of implementation according to model contracts issued by public contracts department in the Ministry of Planning and Development Cooperation.

Second- Public contracts should include  text to collect government debts according to the Law for Collecting Government Debts No. 56 of 1977.

Third- Contracts shall include names and addresses of parties authorized to sign contracts and delegation documents according to the procedures followed provided that these procedures shall be effective at the time of contracting and issued before signature of the contract for a period of no more than 3 months.

Fourth- The contractor may assign part of the contract to sub-contractors with the approval of the contracting agency provided that contractual responsibility shall remain with the principal contractor for the implementation of the contract. It shall not be permissible to relinquish piece-work to a sub-contractor.

Fifth- The contracting agencies in the ministries and entities not associated with the ministry and regions and governorates not organized into a region shall inform the Ministry of Planning and Development Cooperation, Ministry of Labor and Social Affairs, Iraq Central Bank and Central Statistics Department of the name of the contractor, his nationality, amount of contract and duration.

Sixth- If the contract calls for payment as an advance after the contractor signs the contract, then the contracting agency may require all contractors to submit a letter of credit issued by a trusted bank in Iraq taking into account the procedures followed according to the provisions of the General Federal Budget Law.

Seventh-

A. Contracts shall be written in Arabic, Kurdish and English language whenever possible.

B. The tender document shall determine the prevailing version in case of difference in interpretation.

Article 9

Letters of Credit

The following procedures shall be taken into account when opening letters of credit to cover foreign purchase contracts (supply of materials, work implementation, and service purchase) when contracting with foreign and Arab companies:

First- The concerned ministry (or entity not associated with the ministry or region or governorate not organized into a region) after awarding the contract, and duly signing the contract, shall obtain the performance bond by taking the necessary procedures to open the irrevocable letter of credit.

Second- Opening of an irrevocable letter of credit shall be made according to international customs and rules for letters of credits through one of the reliable Iraqi banks in accordance with the special banking certificate, whereby the certificate should include all the financial provisions related to the procurement and supply process and other conditions agreed upon between the two contracting parties (seller and buyer).

Third- The process of opening a letter of credit shall abide by the following:

A. Determination of the name of the beneficiary (seller) and his full address.

B. Description of the needed goods in addition to the number and date of the contract.

C. Type of commercial sale according to international trade rules (Incoterms) which is determined on the basis of (FOB, CIF, CFR and CIP) or others and according to contract conditions.

D. Determine the method of shipping (land, air, sea or other) and final destination.

E. Determine partial shipment or not so as to receive the goods in several parts or at once taking into account that paid financial dues are balanced with the received shipments.

F. Statement to use more than one transshipment or not.

G. Stating the duration of the letter of credit in accordance with the contract terms.

H. Determination of the delivery time as agreed upon.

I. In case it is necessary to extend the letter of credit then the period of bonds or guarantees shall be taken into account.

J. It shall not be permitted to make any changes or extensions regarding the irrevocable letter of credit, unless after securing the agreement of both contracted parties.

K. It is not permitted to revoke the irrevocable letter of credit unless it is done by a written request through the client himself on condition that the beneficiary (the seller) agrees, or it is done by a request from the correspondent bank to revoke the letter of credit based on the beneficiary’s demand after taking into consideration the approval of the purchaser.

L. In the case of an advance payment, the irrevocable letter of credit shall be received with same amount and similar currency, which shall cover the advanced payment in condition that the letter of credit has been issued through a reliable Iraqi bank.

M. In case the seller insists to open irrevocable and confirmed letter of credit then the confirmation charges shall be paid by him.

1- All special expenses arising from the opening an irrevocable letter of credit inside Iraq shall be covered by the buyer who asked to open the letter of credit.

2- All expenses and interests arising from opening the letter of credit (outside the country) shall be covered by the buyer (the beneficiary).

3- It is required when contracting that seller shall pay these expenses and shall be confirmed in the text of the letter of credit.

N. The bond shall cover all risks and the letter of credit shall state whether insurance is covered by the seller or buyer and on the basis of CIF or CIP.

O. Determination of the conditions of payment and how to release these payments based on the contract between the parties (seller and buyer). The method of releasing payment shall be determined accurately and by determining the type of documents to be presented by the seller in order to receive his financial rights.

Fourth- Determining the required documents and papers for letter of credit, its approval, and negotiation according to the rules and international customs (UEP 600).

Fifth- The import license provisions for the materials, or the equipments that are to be imported in

accordance with the law, shall be attached.
Sixth- The concerned ministry, or entity not associated with the ministry or regions or governorates not organized into a region shall follow up the shipping process and receipt of the seller's notice that details shipment of goods taking into account the following:
A. Complete customs clearance procedures for equipments or received materials in order to ease the arrival at storage houses.
B. Complete the special procedures for clearance and loading as soon as possible within the specified areas to avoid paying fines for late delivery of goods to the airport or customs.
the unloading process as soon as possible within the specified areas and unload the C. Complete demurrage.ships to avoid
Seventh- Preparing equipments and usage tools in storage units for the purpose of completing the demurrage procedures and initial receipt of received goods without delay taking into account the status of received goods for the purpose of securing insurance rights.
Eighth- Follow up with completing engineering inspection procedures for received items and issue of inspection certificate within the period determined in the contract and date of receiving the materials.
Ninth
Defects, loss, and damages
A. In the cases whereby the items received are defective, or do not meet the technical specification as requested, then a certificate shall be issued for the difference by an Acceptance and Inspection Committee formed by the contracting agency. And the seller shall be notified without delay to replaces these items.
B- In case of missing items or presence of damage in all or part of these items then a report shall be issued by the Acceptance and Inspection Committee and the seller shall be notified of the missing items and damages for compensation when sale is based upon CIF or CIP as the insurance is covered by the seller.
C- In case insurance is covered by the buyer and there are missing items or damages then a report shall be issued for the difference, and the national insurance company shall be informed for purposes of compensation.
Tenth- The procedures issued by the Council of Ministers regarding opening letters of credit and methods of implementation shall be followed.
Eleventh
Other directions:
A. The conditions determined by the buyer to the bank issuing the letter of credit shall be clear, accurate, and transparent.
B- It shall not be acceptable to open a transferable letter of credit with the exception of assignment to manufacturing entities as stipulated in the contract.
C- In case of advance payment of a certain percentage out of the total amount of the letter of credit, then the advance payment shall not be made to the seller until the receipt of a bank guarantee of the value of advance payment and in the same currency provided the guarantee is unconditional on demand so that the buyer can withdraw that guarantee without the need of notice or judicial order.
D- It is not preferable to load goods on deck.
E- A follow-up of bank receipt for open letters of credit through the opening bank shall be made for the purpose of knowing the movement of credits and relevant costs and financial settlements.
F- The contracting agency shall monitor the open account of foreign currency so that the financial account shall suffice to cover the value of the letter of credit which is opened for implementing a certain supply contract, and not give any contractual obligation for a foreign entity unless there is proof of sufficient funds in foreign currency to cover the value of the letter of credit which was opened to fulfill this obligation.
G- In case of contracting with foreign parties to implement a certain work, supply (equipments, materials, tools) or purchase of service, this requires opening irrevocable letters of credit to cover the value of the contract after study of the special conditions of the letters of credit according to the rules and international principles of letters of credit before approval of the contract.
H- In case of supply of tools or equipments or any goods that need guarantee for use or maintenance, then the percentage of the letter of credit shall be kept for the purpose of covering the needs, provided that it is referred to in the special payment conditions of the letter of credit.
I. When the parties agree to modify the contract, then the bank that opened the letter of credit shall be notified to take necessary measures.
Article 10

Mechanics of settling Disputes

First- Disputes shall be settled before contracting as follows:

A- A central committee shall be formed in each ministry or any other agency that is not related to the ministry including the governorates to look into objections and contractual complaints. The committee shall be under the direction of the concerned minister or governor or any duly authorized person. Its members are a group of experts and specialists and the secretary of the committee shall be no less than a superintendent.

B- The duty of this committee is to study the appeals and the complaints that are submitted by bidders, or their official agents, of those who did not request withdrawal of preliminary guarantees as stated in item Seventeenth of Article 7 of these regulations, to the concerned contracting party within 7 days upon the date of the issuance of the transferring letter (assignment); and to give its recommendation to the concerned minister or head of the entity not associated with the ministry, head of the contracting agency in the regions or governorates not organized into a region within a period not exceeding 15 days as of the date of registering the complaints with the minister’s office. The concerned minister shall issue a decision within 7 days from the date of receiving the report of the committee.

C- The contracting parties in ministries and entities not associated with the ministry, regions, and governorates not associated with the ministry shall be patient in signing contracts until the dispute is resolved by the concerned minister or governor taking into account the special legal time limits for examining appeals stated in paragraph B of item First of this article provided that the appellant shall submit a formal undertaking to pay damages for the contracting party for delay in signing the contract if his claim is malicious or unjustified.

Second- A- special tribunal is to be formed by a decision of the Minister of Planning and Development Cooperation for dispute resolution. The Tribunal will be specialized as to government contracts. It shall be chaired by a judge named by the Supreme Council of Judges with members representing the Ministry of Planning and Development Cooperation whose post shall be equivalent to a Director General and a representative of the Iraqi Contractors Union and union of chambers of commerce..

B-The Tribunal shall have a secretary whose title is not less than a superintendent.

Third- Contractors shall submit their complaints (objections) to the administrative tribunal formed at the Ministry of Planning and Development Cooperation stated in item Second of this article within 7 days upon the date of the issuance of the transferring letter by the ministries, entities not associated with the ministry, regions and governorates not organized into a region, and to give its recommendation to the concerned minister.

Fourth- The tribunal shall issue its decisions to solve the dispute during a period not to exceed 120 days upon the date of paying the legal fee.

Fifth- The tribunal decision shall be final when not appealed to the court within 30 days of the next day from the date of notification.

Sixth- The duties assigned to the tribunal shall be practiced by it in accordance with CPA Order No. 87–2004 which was issued by the Coalition Provisional Authority (dissolved). The tribunal shall be guided by the Civil Code Procedure No. 83–1969 in whatever is not stipulated in these regulations.

Seventh- The general contracts directorate in the Ministry of Planning and Development Cooperation shall follow the decisions issued by the court in coordination with the concerned entities.

Article 11

Settling Disputes after Signing the Contract:

First- Disputes shall be resolved after signing public contracts of all kinds by using one of the following means:

A. Conciliation: By forming a combined committee by the disputing parties (the contracting party, contractors, or consultants) to study the subject and agree to deal with it according to the effective laws and regulations regarding the subject of the dispute.

B- Arbitration- By selecting an arbitrator by each party who shall have experience and knowledge of the dispute and the two arbitrators shall select a third one as head of the arbitration committee. In case this is not applicable, then the court shall select the third arbitrator. The arbitration committee shall study the subject and all its details and the committee shall issue its final decision for settling the dispute. The losing party shall pay the arbitration expenses and the decision of the committee shall be binding after approval by the court according to the law.

C- Referring the dispute to the courts to issue a decision taking into account the relevant law to settle disputes.

D- The contracting agency may select international arbitration to settle disputes provided that the contract shall provide for this facility and when one of the parties is a foreigner taking into account

the procedural mechanism agreed upon in the contract when using this method and one of the international arbitration associations shall be selected to settle the dispute.
Second- The contracting parties shall select the best method to settle disputes as a result of implementing the contract as stated in item First of this article according to the contractual conditions agreed upon.
Article 12
Duties of the General Formations of Contracts Office:
The General Formations of Contracts Office in each ministry or entity not associated with the ministry or region or governorate not organized into a region as they are stipulated in section (2/1/A) of CPA Order No 87–2004 to take over the process of following up the implementation procedures of the public contracts that are being contracted for with these parties. These departments practice their duties according to the contract law issued by CPA Order No. 87–2004. They shall coordinate work with the Inspector General Directorate of the concerned ministry, or that of the region or the appointed governorates. They shall follow up the adopted measures of the Governmental Contract Directorate in the Ministry of Planning and Development Cooperation regarding these cases.
Article 13
Compliancewith lawsand regulations:
All contracted parties or any other persons who have participated in the contract process shall be prohibited from disclosing information to any person who does not have any relation with the contract.
Article 14
Contract term and extension:
The contracting agencies shall follow procedures when extending contracts:
First- The contractor shall implement the contract within the contractual period provided that the period shall start from date of starting work, signing the contract or any other date stated in the contract conditions. When extending contracts the following shall be taken into account:
A-If there is any increase or change in works for different contractors or required materials quality or quantity which affects the course implementation so that it is impossible to complete the work within the period agreed upon in the original contract.
B- If delay in the performance of contract relates to reasons or procedures of the contracting agency or any authorized entity or any reason related to the other contractors used by the contracting agency (the employer).
C- If there are exceptional circumstances outside the control of the contractors that cannot be avoided when contracting and shall lead to delay in completing works or preparing required materials according to the contract.
Second- When applying the provisions of item First of this article, the contractor shall submit a written application to the contracting agency or any authorized person within 15 days for supply contracts, and 30 days for consulting contracts, from the date of the reason for which the application is submitted, requesting extension and detailing all matters regarding the extension. The contracting agency shall decide the matter within a period not exceeding 30 days for all kinds of contracts starting from the date of receipt of the application. No applications shall be accepted after issuance of first receipts stated in the conditions of the contract.
Article 15
Changing works and additional works:
First- It shall not be permissible to order changes in the works agreed upon or to make any additional works, or new materials, unless it is necessary and the change shall occur in a limited manner when one of the following occurs:
A- If no change or addition would cause delay for the work or huge damage from a technical and economic perspective.
B- If no change or no addition would cause unnecessary contractual works.
C- If the change or addition would saving work or project cost.
D- If the change or addition would not cause material alteration in the service or production capabilities for the project or work.
E- If the change would shorten the contract period provided that it does not lead to lowering of the technical standards of the work or project.
Second- All correspondences regarding orders of changes and additional works shall be expedited and the contracting agency shall finalize such orders within the period stated in item Second of Article 14 of these regulations.
Third- Additional works and orders of changes shall not be implemented unless there is a written

order (change order) issued by the contracting agency according to the contract term that includes a description of the work, amounts, prices, and additional period (if any) which is added to the period of the contract. In case there is no need for any extension then this shall be stated clearly in the order.

Fourth- The contracting agency shall determine the changes or required additions needed in the contract as early as possible in a manner not affecting the work progress according to the agreed upon timetable.

Fifth- Additional works and orders shall be priced according to the terms of the contract and in case of adding new items that have no equivalent or similar items in the contract, then the prevalent market price shall be adopted as the basis for pricing, in addition to administrative expenses and profits.

Sixth- It shall not be permissible that the cost of change orders and additional works exceed the authorities given to the concerned minister or governor taking into account the provisions of the general federal budget.

Article 16

Bonds, delay fines, and administrative costs

First- Legal Bonds

A. The primary prepaid bonds that are submitted by the participants in the tenders are not accepted unless they take the form of a letter of credit, certified check, bank guarantee, or security bond issued by the government of Iraq.

B. The bidders shall submit preliminary guarantees to prove the seriousness of their participation in the tender, for all kinds of contracts, at the rate of 1% of the contract price, from a recognized bank according to a statement made by the Iraq central bank regarding financial capabilities of the bank.

C- Preliminary guarantees or bonds shall be confiscated from the winner when, after notification, he declines to sign the contract and all the legal procedures stated in these regulations shall be taken against him.

D. The final bond guarantees for the full implementation shall be at the rate of 5% of the contract price and issued by a trusted bank in Iraq. This amount will not be released until the issuance of the final approval certificate and the clearance of final accounts.

F- State and public sector companies shall be exempted from presenting preliminary and final guarantee bonds stated in this article for a period of three years starting from the effective date of these regulations. The Ministry of Planning and Development Cooperation shall re-examine this exemption after passage of this period and in coordination with the Council of Ministers/Economic Affairs Committee.

Second- Delay Fines- The maximum limit for delay fines is limited by the implementing party at a rate of 10% of the contract or tender value. The implementing party shall state this rate within the contracting provisions, the tender documents, and the regulations to the bidders. The implementing party shall take the necessary measures to speed up the completion of the work before exceeding 25% of the time allowed for the work. These measures include the formation of a committee, consisting of experienced people, to speed up the time in which the contractor shall supply the remaining works, or the work may be withdrawn in accordance with contract provisions.

The following method shall be followed when calculating the penalty:

× 10%= penalty for every day

The amount of the contract

---

The period of implementation

Third- Delay fines may be reduced according to the percentage of completion of contracted works as determined in the timetable of the contract. The work, supplied good or required service shall be implemented according to the qualifications stipulated in the contract terms.

Fourth- The contracted party, based upon a reasoned decision, shall impose the delay fines upon the contractor or withdraw the work from him.

Fifth- The administrative cost rate is limited and not to exceed 20% of the actual implementation cost of the concerned obligation. This rate is adopted when the contracted party takes over by itself or through another party the implementation of the contractor’s obligations. The contracted party

shall state said conditions within the contracting provisions and tender documents.

Article 17

Legal Effects resulting from breach of contractual obligations:

First- The following procedures shall be followed when the legal effects for the breach arise before signing the contract in case the winner refuses to sign the contract and following formal notification to sign the contract within 15 days:

A. Confiscation of preliminary guarantee bonds in case of full refusal.

B. Refer the bid to the next bidder and the bidder who refused shall bear the difference between the two bids in addition to confiscation of preliminary bonds.

C- In case the first and second contractors refuse to sign the contract and/or submit the letter of guarantee, then the contracting agency may award the tender to a third contractor and in this case the first and second contractors shall bear the difference in addition to confiscation of preliminary bonds.

D- Those breaching contractors shall be subject to the procedures stated in paragraphs (A), (B), and (C) of this item in case of breach during implementation of their bids.

Second- Legal effects arising after signing the contract:

A. Confiscation of, or keeping, final guarantee bonds.

B. Implementing the contract through a committee by a representative of the breaching party and in case of refusal then a judicial order shall be obtained from court to implement the work at his expense and taking possession of the equipment and tools for the purposes of liquidation. Delay penalties and administrative burdens at a rate of 20% of the total amount and other financial obligations shall be applied and if found after final accounts that the account is in credit, then this credit shall not be returned to the party in breach. If the breaching party’s account is found to be in debt, then compensation shall be demanded.

C- It shall be permissible for the contracting agency to assign the contract to another contractor if the first contractor breaches his contractual obligation and the breaching contractor shall bear the difference between the two bids when implementing the contract in addition to confiscation of his bonds related to best performance and the proper procedures.

Article 18

Contract Prohibition:

The contracting parties in ministries and entities not associated with the ministry and regions and governorates not organized into a region may list those contractors that breach their contracts on a blacklist taking into account the following:

First- Listing of Iraqi contractors in the blacklist shall be made according to the regulations for registration and classification of Iraqi contractors issued by the Ministry of Planning and Development Cooperation No. 1 of 2005.

Second- Listing of contractors and consultants (non-Iraqis) based upon the mechanism stated in the regulations issued for this purpose.

Article 19

Preliminary and working advances:

First- The special provisions for granting preliminary advances for contracts shall be taken into account as stated in the General Federal Budget Law and by providing special guarantees before approval.

Second- Advances shall be paid to contractors according to the progress of work, within a period not less than 30 days and in light of the general conditions of the contract terms stated in the tender documents.

Article 20

Ministries and agencies that are not associated with a ministry, the regions and the governorates shall comply with the following:

First- All general public works contracts shall include obligatory rules within the contract provisions for civil, electrical, mechanical and chemical engineering work. These rules are adopted by the Ministry of Planning and Development Cooperation and are followed inside Iraq. These rules shall be considered an integral part of the contract when no wording is included in the contract.

Second-Take into consideration the provisions of the concerned valid laws related to general contracts and directions of the Ministry of Planning and Development Cooperation and regulations of the high authorities.

Article 21

First- All ministers and agencies not connected to a ministry shall require all the contracting parties related to them to organize their contracting plans with the Office of Government Public Contract

Policy within the Ministry of Planning and Development Cooperation and supply it with the required information.

Second-All ministries and agencies not related to a ministry shall abide by the investment budgets information issued by the Ministry of Planning and Development Cooperation or any other regulations issued by the Ministry of Finance regarding financial authorities for general contracts of the governmental directorates and the public sector, along with the mandatory power authorized to the concerned parties, when implementing the projects that are included within the state budget.

Article 22

The Office of Government Public Contracts in the Ministry of Planning and Development Cooperation shall take over the following:

First- Exercising the authorities given to it in accordance with the Public Contracts Law which was issued by the CPA (dissolved) in Order No. 87-2004.

Second- Issuing regulations that organize contractual relations between the state and those who contract with it, including the consequences of a contractor's violation of its contractual duties.

Third- Issuing and amending general contract provisions and goods and services supply provisions.

Fourth- Evaluating the duties and the procedures of the Bid Opening and Bid Evaluation Committees within state agencies and changing them whenever needed.

Fifth- Answering the questions of all state offices and other contracted parties and any other cases related to its duties.

Sixth- Providing training and development to improve the skills of employees working in the contracting parties in ministries and entities not associated with the ministry, regions, and governorates not organized into a region.

Seventh- Technical supervision of the general structures of contracts in the ministries, regions, and governorates not organized into a region.

Article 23

It shall be permissible to entrust companies of the Ministry of Industry and Minerals to manufacture equipments and internal materials in the work of productions for other ministries, when capable, as an exception to the provisions of these regulations.

Article 24

General contracts covered by these regulations shall be subject to Iraqi laws and Iraqi law court jurisdiction according to applicable procedures.

Article 25

Regulations of Implementing Government Contracts No. 1 of 2007 shall be cancelled.

Article 26

These regulations shall be implemented as of the date of publication in the official gazette.

Ali Ghaleb Baban

Minister of Planning and Development Cooperation

للطباعة

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**صورة التشريع الاصلي:** تعليمات تنفيذ العقود الحكومية رقم 1 لسنة 2008

- الاقتصاد
- الحادي

# IRAQ

## Subnational Public Financial Management: A Diagnostic Report

**November 26, 2007**

Social and Economic Development Group
Middle East and North Africa Region
The World Bank

**Document of the World Bank**

## CURRENCY EQUIVALENTS

(Exchange Rate Effective September 2007)

| | *2003* | *2004* | *2005* | *2006* | *2007* |
|---|---|---|---|---|---|
| Iraqi Dinar (ID) per US$1, period average | 1,957 | 1,455 | 1,467 | 1,432 | 1234 |

## FISCAL YEAR

January 1 – December 31

## WEIGHT AND MEASURES

Metric System

## ACRONYMS AND ABBREVIATIONS

| | |
|---|---|
| ARDP | Accelerated Reconstruction and Development Program |
| BCC | Budget Call Circular |
| BSA | Board of Supreme Audit |
| CBI | Central Bank of Iraq |
| CoR | Council of Representatives |
| COSIT | Center of Statistics and Information Technology of Iraq |
| CPA | Coalition Provisional Authority |
| CPI | Commission on Public Integrity |
| DFI | Development Fund for Iraq |
| DfiD | Department for International Development |
| DG | Directorate General |
| DTOs | District Treasury Offices |
| FMIS | Financial management information system |
| FML | Financial management Law and Public Debt Law (CPA Order/95) |
| GC | Governorate Councils |
| GDP | Gross Domestic Product |
| GFS 2001 | Government Financial Statistics (IMF) 2001 |
| GoI | Government of Iraq |
| GNIRs | Governorates Not Incorporated in Regions |
| GTO | Governorate Treasury Office (Ministry of Finance) |
| IAMB | International Advisory and Monitoring Board |
| IG | Inspector General |
| INTOSAI | International Organization of Supreme Audit Institutions |
| KRG | Kurdistan Regional Government |
| mbpd | million barrels per day |
| MoE | Ministry of Education |
| MoF | Ministry of Finance |
| MoI | Ministry of the Interior |
| MoMPW | Ministry of Municipalities and Public Works |
| MoPDC | Ministry of Planning and Development Cooperation |
| PEFA | Public Expenditure and Financial Accountability |
| PFM | Public Financial Management |
| SDTO | Subdistrict Treasury Offices |
| SOE | State-Owned Enterprise |

| | |
|---|---|
| Vice President: | Daniel Gressani |
| Country Director: | Joseph P. Saba |
| Sector Director: | Mustapha K. Nabli |
| Sector Manager: | Farrukh Iqbal |
| Task Team Leader: | Monali Chowdhurie-Aziz |

## ACKNOWLEDGMENTS

This report was written by a core team of staff from the World Bank, the United Kingdom's Department for International Development (DfiD) and United States Agency for International Development (USAID). The core team consisted of Monali Chowdhurie-Aziz, Kai Kaiser, Rima Das Pradhan, Jeff Rinne (World Bank), Farooq Khan (Adam Smith International/DfiD), and Ricardo Silva-Morales (USAID). Production support was provided by Muna Abeid Salim. The report benefited from extensive comments provided by Farrukh Iqbal, Pierre Messali and Dave Biggs (World Bank). The peer reviewers were Serdar Yilmaz and Vivek Srivastava. Comments were also provided by Joseph Saba and Kathryn Funk (World Bank). The team benefited from previous workshops held in Dubai with members of the Board of Supreme Audit (BSA) and the Commission on Public Integrity (CPI) by the Bank and workshops in Amman held by DfiD. In addition, the core team also undertook two missions to Kurdistan (from September 13th to 21st, 2006 and January 28th to February 1st, 2007) where they visited ministries, departments and agencies involved in budget implementation. Follow-up work was undertaken in Baghdad by DfiD staff and in the provinces by USAID staff. Input was also provided by donors actively involved in this area including the US Treasury.

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Achmad Majeed, Governor; As Sulaymaniyah; Chief of the Bureau of Supreme Audit, As Sulaymaniyah; Shawnem, Director General, Ministry of Electricity; Karzan Hama, Director, Oncology and Radiotherapy; Tariq Rafiq Rauf; Manager, Turbine Department, Engineer.

Delegates to the Joint Institutional and Policy Capacity Building Workshop, January 2007, Erbil
Special thanks to the Steering Committee for the Joint Institutional Capacity Building Workshop, Erbil January 2007: Hoger Shalli, Senior Consultant, Council of Ministers; Ezzat Isa, General Director of Administration and Financial Affairs; Nisar Talabany, Assistant Director, Council of Ministers; and Howar Talabany.

150 delegates from around the Kurdistan Region of Iraq attended the five-day workshop. 10 delegates from the Governorates outside the Kurdistan Region of Iraq, and the central ministries of Finance and Planning also attended to provide comparative information. These delegates also provided in-depth information during the Planning Focus Group meeting for the Sub-national Public Financial Management Workshop in Beirut, May 2007.

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# IRAQ
# Subnational Public Financial Management
# A Diagnostic Report

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## EXECUTIVE SUMMARY

i. **This report assesses public financial management at the subnational level in Iraq**. The assessment is based on information gathered through consultations with Iraqi policy makers at the national and subnational levels *and* officials and experts from international development partners engaged in capacity building for Iraq in this area.[1] The main methodological tool used by the report is the Public Expenditure and Financial Accountability (PEFA) framework which covers: (i) budget credibility, comprehensiveness and transparency (ii) policy-based budgeting (iii) predictability and control in the budget and (iv) accounting/reporting and external scrutiny and audit.[2]

ii. The report describes subnational public financial management (SPFM) arrangements as prescribed by laws and regulations (*de jure*) as well the actual practices that prevail on the ground (*de facto*). It distinguishes between Kurdistan and Governorates not incorporated as regions (GNIRs) because the former operates with much greater autonomy than the latter. Within GNIRs, the report further identifies differences between public financial management (PFM) processes associated with Governorate Councils/Governorate offices and those associated with deconcentrated line agencies. Governorate Councils are sub-national legislative cum executive bodies that were first introduced in Iraq through direct elections in 2005.

iii. Prevailing and prospective intergovernmental arrangements are relevant to the assessment of SPFM practices. In recent years, the legal and operational bases of relations between central and sub-national governments in Iraq have undergone tremendous change. The removal of the centralized government of Iraq (in 2003) allowed significant legislative changes to be brought about, first by the occupation authority (the CPA) and then by the elected government. The process has not yet come to a stable conclusion. The form and substance of intergovernmental arrangements continue to be discussed by the Iraqi Parliament and new or modified legislation will undoubtedly affect SPFM practices in the future. In particular, the following aspects will be relevant: (a) whether or not some Governorates will be incorporated into regions *à la* Kurdistan; (b) what consensus will be arrived at regarding the sharing of oil revenues among Iraq's Governorates and the federal as well as regional government(s); and (c) whether or not central line ministries will hand over to sub-national units responsibilities for service delivery in key areas like education and health.

iv. The Constitution specifies a federal form of government and broadly sets forth roles, responsibilities, and likely financing for the country's regions and Governorates. Regions, of which only one has been formed so far, Kurdistan, are invested with significant levels of autonomy. But financing realities tilt the balance to the center. With 95 percent of revenues coming from oil, all public spending in Iraq is dependent on a revenue stream that is controlled by the center. At the level of the Governorate, funds made available for projects and reconstruction and the small, recurrent allocations that the Governorate Councils receive from the center are devolved expenditures. In contrast, the budgets of the line agencies are deconcentrated, but the

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[1] Two extended workshops were, in particular, instrumental in generating the information that is reflected in this report. The first was held in Kurdistan in September 2006 and the second in Beirut in February 2007. The workshops facilitated interaction and exchange of information not only between Iraqi officials and foreign experts but also among officials from the Governorates, central ministries and Kurdistan.

[2] The PEFA framework has been applied in over three dozen national and sub-national contexts.

agencies continue to report directly to the ministries in Baghdad. Neither the Governorates nor Kurdistan have as yet been subject to administrative decentralization, save for the somewhat more autonomous status of Governors. Civil servants in the Governorates remain employed almost exclusively by central line agencies. Line agencies in the Governorates are subject to some accountability to Governorate Councils and Governors' offices. However, it is not clear whether these lines of accountability—or those to Baghdad—predominate.

v. Governorate Councils and Governors' offices represent a nascent form of devolved subnational government but their direct role is limited**.** While the goal of devolution is repeatedly stated in interim administration laws and the Constitution, the only subnational governmental units that have been given executive authority over service provision are the Governorate Councils. Moreover, policy- and decision-making authority remains centralized with their operating budgets controlled by the central government, and the financing for service administration going through the line ministries. So far their role is largely limited to prioritizing and implementing a multisectoral capital grant, in the case of Kurdistan, and spending ARDP grants, in the case of the 15 other Governorates. The Governorate Councils and Governors' offices also play a role in coordinating, prioritizing, and monitoring deconcentrated expenditures by the central line agencies (education, health, municipalities, and public works).

### *Key issues related to the new legal framework*

vi. **Consistency of practice.** Prior to 2003, Iraq's PFM system was highly centralized, with all policy and budget decisions made at the center. Implementation was conducted largely by provincial directorates of the central line ministries and accountability was enforced from the top. The CPA introduced a variety of new laws as well as amended existing laws in a short period of time from May 2003 till June 2004, starting with the transitional and administrative law and culminating with the Financial Management and Public Debt Law (June, 2004). New institutions were also created, such as the Commission for Public Integrity (CPI) and the Inspector General's Office while others, such as the Board of Supreme Audit (BSA), were rejuvenated. *While the new legal and institutional framework has many advantages, key weaknesses include insufficient connection with the (legacy) framework that preceded it, overlapping mandates in some areas and regulatory gaps in others.* This has led to two types of dysfunctions. First, not everyone interprets the new laws and regulations the same way and hence there is inconsistency of practice across Governorates and line agencies. Second, when faced with overlapping mandates (e.g. across the CPI and BSA) or situations where there is a lack of clarity regarding roles and functions and no arm of government -executive, legislature or judiciary– is in a position to arbitrate, PFM practitioners frequently avoid taking any decision.

vii. In Kurdistan, which functions with substantial autonomy, questions remain as to the extent to which federal or regional laws will prevail in matters relating to external audit, civil service management, and accounting and reporting. Practices in Kurdistan broadly follow national arrangements and guidelines, but with a series of important modifications and amendments. For example, Kurdistan is not subject to external audit from the federal Board of Supreme Audit; instead, it has its own structure.

viii. **Capacity weaknesses**. The pace of change in SPFM regulations and responsibilities has been too fast to allow subnational units to develop the capacity to plan and manage their own finances. Variations in capacity are another cause of inconsistent practice across the line ministries, the GNIRs and Kurdistan. Until significant capacity enhancement takes place at all levels of government, recent changes to the legal and institutional framework for SPFM will continue to impede smooth functioning. For example, at the level of the Governorate and regional

treasuries, accounting and financial staff have not been provided adequate training regarding the new instructions and regulations. As a result, treasury staff finds it difficult to discuss relevant matters with local level staff when spending is in process.

***Key issues related to budget formulation***

ix. **Selection of capital projects.** Although subnational units have been given a role in the capital budgeting process, several problems have emerged in practice. At the Governorate level, development projects are picked in a seemingly random manner with little regard for local capacity to implement. Governorate Councils frequently select projects that are best handled centrally. This is mostly due to the relative inexperience of the Governorate Councils and poor coordination between the councils and line ministries. It is also due to the lack of clarity in expenditure assignments across different levels of government. As a result, the Ministry of Planning and Development Cooperation (MOPDC) has to spend resources on weeding out central projects rather than on evaluating and supporting the selection of well-designed projects. Also, the projects that form regional development programs in each Governorate are generally picked without a clear link with national policy objectives specified through multi-year plans or fiscal commitments. Finally, many projects are chosen without adequate consultation with intended beneficiaries or adequate local input. Where local capacity is available and input is sought, results are often better. For example, Governorate Councils in locations such as Najaf have effectively utilized their knowledge of local conditions to propose projects with a high and immediate benefit to local populations.

x. **Realism of spending plans**. For Kurdistan, the realism issue is related to the fact that they get a fixed proportion (around 18 percent) of a volatile revenue stream tied to oil prices. Depending on where the average price of oil settles for the year, revenues owed to Kurdistan can be quite different at the end of the year than at the beginning. At present, there is no mutually satisfactory arrangement in place to smooth out revenue flows between the center and Kurdistan, something that would help the latter prepare more realistic budgets. For the other Governorates, the realism issue is somewhat different**.** Local government units and de-concentrated line ministry staff are not provided clear budget ceilings. Accordingly, there is a tendency to ask for more funds than can be realistically spent. In recent years, this has been highlighted by the fact that capital spending has been less than 50 percent of that budgeted. In part, this was due to the difficult security environment prevailing in Iraq. In part also, this was due to unrealistic estimates of what could be spent with the staff capacity at hand and lack of familiarity with the new PFM rules and regulations. Another factor has been the fear of being the object of allegations of corruption.

xi. **Transition to new classification system.** A new GFS 2001 based classification system was used for the preparation of the 2007 budget together with a new chart of accounts. This report does not comment on the quality of New Classification System being adopted by GoI. However, staffs in the subnational units and line ministries have yet to receive training or guidance on how to move from the previous chart of accounts to the new one. Furthermore, the new chart of accounts has yet to be adopted at all levels of government including in Kurdistan and the GNIRs.

***Key issues related to budget execution***

xii. **Monitoring and evaluation.** The budget law for 2007 specifies that the Governor should execute the approved plan of construction in a Governorate while the Provincial Council should monitor the execution process. However, in reality monitoring and evaluation are undertaken by the central and line ministries in part because of lack of capacity in the devolved structures and in

part because of legacy of past practice. Given the fact that the implementing agencies are the deconcentrated arms of the line ministries, it is unclear as to what actual authority the Governorates offices have in fulfilling their mandated role.

xiii. **Cash availability.** Neither Kurdistan nor the GNIRs seem reasonably assured that their capital projects will be funded continuously by the center. As a result they sign contracts only when the cash is at hand, resulting in an erratic pattern of spending or, in some cases, no implementation at all. For example, in 2006, some key projects in Dhi Qar were not undertaken because Governorate officials were unsure whether allocations would be made and cash provided to complete them in the following years.

xiv. **Source of funding**. The office of the Governorate treasury maintains a single bank account with two sources of funding: (i) Baghdad and (ii) security deposits and trust funds. Receipts from both these sources form part of the funds available to finance Governorate spending needs. As a result, security deposits and trust funds, which are actually liabilities of the state, are used to finance normal budgetary operations although they should be kept separate.

xv. **Procurement.** Procurement procedures in Iraq have a number of features that are not in line with generally accepted standards of sound practice. These range from inadequate requirements for registration of suppliers and contractors and absence of adequate national bidding documents to insufficiently transparent bid submission, opening and evaluation procedures, and contract award procedures as well as lack of effective bid protest mechanisms and publicity on contract awards. These issues apply both at the federal and at the subnational levels and affect budget execution at both levels as well.

xvi. **Quality of internal auditing.** There is no systematic internal auditing system process at the central level, let alone at the subnational level. With low capacity at the center and even less elsewhere, establishing controls and audit functions at the subnational level is of critical importance. So far in Iraq—because of a lack of independence as well as political capture, security concerns, and low capacity—few inspectors general (IGs) have added value to the work of their ministries. Because the IGs were appointed with little attention to capacity or training, they are not clear about their scope and mandate. Methodologies for audit and investigation are not consistent, and there is no common procedure set out for the IGs to fulfill their duties.

xvii. **Weaknesses in financial reporting.** At both the central and subnational levels, there are no standard reports for budget variance, cash flows, bank reconciliation, or fixed assets. Reporting is limited to production of periodic trial balances. This results in the accounting system being unable to provide full or timely information on budget performance. Furthermore, Governorate Councils are not in the information loop on this: the financial reports go from subnational treasuries directly to the Ministry of Finance.

xviii. **Weaknesses in external audit and public accountability.** In the governorates, public accountability and external scrutiny is undermined by the failure of subnational government agencies to understand the role of external audit and to accept and act upon audit findings. In Kurdistan there are two separate BSAs both of which suffer from severe capacity limitations and in some instances from the denial of access to government financial records. Reporting arrangements in Kurdistan are inappropriate and inconsistent in that the BSA in As Sulaymaniyah reports to the Council of Ministers whereas the BSA in Erbil reports to the President of KRG. It is expected that on unification the BSA in Kurdistan will report to Parliament in line with practice at the national level. Moreover there is very little transparency in public spending due to the non publication of audit reports.

# I. IRAQ'S EVOLVING FISCAL DECENTRALIZATION

## A. Fiscal federalism and the current of decentralization in Iraq

1. **The 2005 Constitution of Iraq envisages a federal form of government but this is evolving slowly**. Some steps have already been taken towards this objective**,** such as the formation of Governorate Councils, elections at Governorate levels, and the de facto autonomy provided to Kurdistan. While the 2005 Constitution sets out a federal vision, this is evolving slowly. The Constitution sets forth roles, responsibilities, and likely financing for the country's regions and Governorates. Regions, in particular, are invested with significant levels of autonomy from the central government. To date, however, only Kurdistan enjoys regional status, and the creation of new regions has been deferred until April 2008.However, the structures that supported the former wholly centralized state are yet to be dismantled. Thus funding remains largely controlled by central sources. While Governorate Councils (GCs) have been provided with a separate source of financing - an annual block grant from development and reconstruction funds – this still amounts to just 5 percent of total expenditures. The Governorates have not been subject to administrative decentralization, save for the somewhat more autonomous status of Governors. Civil servants in the Governorates remain employed almost exclusively by central line agencies. Line agencies in the Governorates are subject to some accountability to Governorate Councils and Governors' offices. It is not clear whether these lines of accountability—or those to Baghdad—predominate. Finally, while the law is in place, many implementing rules and regulations are still required. The overlay of various institutional arrangements dating from the prewar period, the CPA period, and recent reforms means that in many respects the system of subnational public finance remains inchoate.

2. **Administrative decentralization is presently characterized by both deconcentration and devolution.** Some public spending agencies are devolved while others are deconcentrated (see Box I.1 for definitions). Funds made available under the ARDP and the small, recurrent allocations that the Governorate Councils receive from the center are devolved expenditures. In contrast, the budgets of the line agencies are deconcentrated, but the agencies continue to report directly to the ministries in Baghdad. Expenditures by Governors' offices are mixed, as are their roles. Until 2006, their operating budget fell under the Ministry of Municipalities and Public Works (MoMPW). As of 2007 each Governor's office has its own budget. The Governor has a coordination and oversight role vis-à-vis the directors of the (deconcentrated) line agencies in the Governorates. But the exact balance of this accountability relationship (to line agencies in Baghdad or to the Governor) is not always clear in practice and differs from Governorate to Governorate.

3. **While the Governorate Councils and Governors' offices represent a nascent form of devolved subnational government[3], their direct role is limited**. Thus while the goal of devolving authority to subnational governmental structures is stated throughout the interim administration laws and the Constitution, the only subnational governmental units that have been given executive authority over service provision are the Governorate Councils. Moreover, policy- and decision-making authority remains centralized with their operating budgets controlled by the central government, and the financing for service administration going through the line ministries. So far their role is largely limited to prioritizing and implementing a multisectoral capital grant, in the case of Kurdistan, and spending ARDP grants, in the case of the 15 other Governorates. The

[3] These arrangements were initiated under the Coalition Provisional Authority (CPA).

Governorate Councils and Governors' offices also play a role in coordinating, prioritizing, and monitoring deconcentrated expenditures by the central line agencies (education, health, municipalities, and public works). Traditionally, municipal administrations have operated as self-financing deconcentrated entities under the MoMPW and are, to some degree, accountable to elected Municipal Councils.

4. **Governorate Councils receive some recurrent funds for sitting fees and technical support, but they do not formally employ staff.** Governors' offices employ civil servants. Until 2006, these were under the MoMPW. In the 2007 budget, for the first time, they were, like the Governorate Councils, non–line ministry line agencies. Recurrent funds are allocated separately to Governorate Councils and Governors' offices. While Governorate Councils are expected to prioritize what have to date been known as the ARDP funds, the Governors' offices are expected to play a significant role in the implementation of these funds.

5. **Most of Iraq's civil servants remain on central government payrolls.** Iraq is effectively centralized when it comes to its civil service. The federal government employs 2,060,200 people, not including military personnel.[4] Of these, roughly 40 percent are assigned to service-delivery ministries at the Governorate level and below (including Baghdad). Kurdistan employs an additional 586,502 civilians and *peshmerga* defense forces (see Chapter II). The deconcentrated line agencies are typically headed by a director general or by a director (as in the case of municipalities and public works). The Governors' offices employ about 5,700 civil servants throughout the 15 Governorates. Governorate Councils cannot employ permanent staff, but they do employ some staff on a consultancy basis, in addition to paying sitting fees to council members. In principle, the Governors' offices are the executive branch of the Governorate governments. For the first time this year, they were separated from the MoMPW budget and now appear as independent line agencies (see Chapter III). The budgets for the Governorate Councils are treated similarly, but as a separate line item.

6. **Governorate Councils receive some recurrent funds for sitting fees and technical support, but they do not formally employ staff.** Governors' offices employ civil servants. Until 2006, these were under the MoMPW. In the 2007 budget, for the first time, they were, like the Governorate Councils, non–line ministry line agencies. Recurrent funds are allocated separately to Governorate Councils and Governors' offices. While Governorate Councils are expected to prioritize what have to date been known as the ARPD funds, the Governors' offices are expected to play a significant role in the implementation of these funds.

7. **Fiscal decentralization in Iraq is asymmetric.** The Kurdistan Regional Government operates with significant autonomy whereas central government agencies continue to be prominent in Iraq's fifteen other Governorates. Kurdistan, which encompasses three Governorates in northern Iraq (Dahuk, Erbil, and As Sulaymaniyah), has operated with significant autonomy for more than a decade. In contrast, federal line ministries still play a central role in Iraq's other Governorates. The Governorates themselves are characterized by a significant degree of diversity. Baghdad is a large metropolitan area that sits in the middle of Iraq; as the capital, it has special legal arrangements. Iraq's other Governorates are Al Anbar, Babil, Al Basrah, Diyala, Karbala, Maysan, Al Muthanna, An Najaf, Ninawa (Mosul), Al Qadisiyah, Salah Ad Din, At Ta'mim, Dhiqar and Wasit. The Governorates are characterized by large disparities in resource endowments, notably oil. For example, the southern Governorate of Al Basrah currently accounts for more than fifty percent of estimated oil production.

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[4] Manpower table in 2007 budget law.

**Box I.1 Different Types of Decentralization**

**Decentralization—**the transfer of authority and responsibility for public functions from the central government to subordinate or quasi-independent government organizations or the private sector—covers a broad range of concepts. Each type of decentralization—political, administrative, and fiscal—has different characteristics, policy implications, and conditions for success.

**Political Decentralization** aims to give citizens and their elected representatives more power in public decision making. It is often associated with pluralistic politics and representative government, but it can also support democratization by giving citizens or their representatives more influence in formulating and implementing policies. Advocates of political decentralization assume that decisions made with greater participation will be better informed and more relevant to diverse interests than those made only by national political authorities. The concept implies that selecting representatives from local electoral jurisdictions allows citizens to better know their political representatives, and elected officials to better know the needs and desires of their constituents. Political decentralization often requires Constitutional or statutory reforms, pluralistic political parties, stronger legislatures, new local political units, and effective public interest groups. This form of decentralization is most closely associated with devolution (rather than deconcentration or delegation).

**Administrative Decentralization** redistributes authority, responsibility, and financial resources for providing public services among different levels of government. It is the transfer of responsibility for planning, financing, and managing certain public functions from the central government and its agencies to field units of government agencies; subordinate units or levels of government; semiautonomous public authorities or corporations; or area-wide, regional, or functional authorities. Administrative decentralization has three major forms—deconcentration, delegation, and devolution—each with different characteristics

***Deconcentration*** refers to the redistribution of decision-making authority and financial and management responsibilities among different levels of the central government. Often considered the weakest form of decentralization, it is used most frequently in unitary states. Within this structure, however, policies and opportunities for local input vary: deconcentration can merely shift responsibilities from central government officials in the capital city to those working in regions, Governorates, or districts, or it can create strong field administration or local administrative capacity under the supervision of central government ministries.

***Delegation***. Through delegation, central governments transfer responsibility for decision making and administration of public functions to semiautonomous organizations not wholly controlled by the central government but ultimately accountable to it. Governments delegate responsibilities when they create public enterprises or corporations, housing authorities, transportation authorities, special service districts, semiautonomous school districts, regional development corporations, and special project implementation units. Usually these organizations have a great deal of discretion in decision making.

***Devolution*** is the transfer of authority for decision making, finance, and management to quasi-autonomous units of local government with corporate status. Devolution usually transfers responsibilities for services to local governments that elect their Governors and local councils, raise their own revenues, and have independent authority to make investment decisions. In a devolved system, local governments have clear and legally recognized geographical boundaries over which they exercise authority and within which they perform public functions.

**Fiscal Decentralization** implies the transfer of financial responsibility and resources as a core component of decentralization. If local governments and private organizations are to carry out decentralized functions effectively, they must have adequate revenues—raised locally or transferred from the central government—as well as the authority to make expenditure decisions. This can take many forms, including: (a) self-financing or cost recovery through user charges; (b) cofinancing or coproduction, in which users participate in providing services and infrastructure through monetary or labor contributions; (c) expansion of local revenues through property or sales taxes or indirect charges; (d) intergovernmental transfers of general revenues from taxes collected by the central government to local governments for general or specific uses; and (e) authorization of municipal borrowing and mobilization of national or local government resources through loan guarantees.

**Figure I.1 Iraq's Governorates/Regions**

## B. Decentralized Public Financial Management in Iraq

8. **Decentralized public financial management (PFM) systems are necessary to support the ultimate objective of effective delivery of services at the local level.** Some measures to decentralize PFM have been taken in Iraq in recent years while others are still being debated in parliament. Two major ongoing debates[5] concern legislation to determine how hydrocarbon

[5] A Constitutional Review commission is also examining the need for any potential amendments to the 2005 Constitution.

revenues are to be shared and what powers are to be enjoyed by different levels of government. The preparation of a hydrocarbons law has proven especially delicate because of doubts about the potential role of regions (notably Kurdistan) in regulating new fields. In concert, a new law of revenue sharing is also being tabled to allow for revenue sharing across provinces and regions consistent with the principles set out in the 2005 Constitution. Further draft laws on Local Governance also promise to be passed in the new future. What remains unclear as this process evolves is to what extent this many pronged dialogue on decentralization involves all key stakeholders. Nor is it clear as this juncture whether such a process of broad national dialogue is feasible. Pending the regulations regarding rules based transfers, as part of the revenue sharing law, till date, transfers to Kurdistan and investment allocations to the Governorate Councils are regulated as part of the annual budget process, and not by fiscal decentralization laws. Thus depending on how these debates play out fiscal decentralization could take any of several directions. One trajectory outside Kurdistan may be a gradual strengthening of the Governorate Councils. This strengthening could differ by region and sector. Another trajectory could give Governorates and regions more pronounced control over fiscal resources. A better understanding by both Iraqi policy makers and international development partners of how the system actually functions would help inform debates over these reform options.

9. **The regulatory and institutional arrangements surrounding PFM currently straddle both long-established (legacy) practices and the reforms initiated during the CPA period**. Current practices are shaped by long-standing regulations, with an overlay of new laws introduced under the CPA. Many recent changes involved importing structures from elsewhere without ensuring there was much coherence and coordination with the existing system. The recent reforms did not attempt to strengthen perceived gaps and modernize the system by building on the existing structure. A case in point would be the function of the inspector generals. While designed to fill a gap in that the previous system did not have a robust internal audit function, as is the case in most of the MENA region, the role of the IGs and the BSA are insufficiently delineated and significantly overlap with the newly instituted Commission on Public Integrity in its attempt to reduce corruption.

10. **Current PFM practice at the subnational level reflects much confusion about what the appropriate laws and regulations are**. A considerable portion of the approved capital budget for 2006 was not spent, in part because of this confusion. Thus budget execution guidelines are subject to the Financial Management Law and Public Debt Law (FML) [6] as well as the detailed guidelines provided by the MOF after the budget is passed. MOPDC too has regulations regarding the capital budget that need to be fulfilled. Budget execution instructions issued by MoF lacks clarity and is not comprehensive. A case in point is procurement which is subject to both the existing regulations, the FML as well as regulations issued by the MOF as part of the budget execution rules leading to overlaps.

11. **Many subnational governments face a severe capacity problem. This affects the pace and quality of decentralization**. Until significant capacity enhancement takes place at all levels of government, the recent changes are likely to slow the system down, since there remains a mismatch between the capacity to implement the budget as inherited from the previous system and the new roles and responsibilities provided to different actors in the system. This is true not only at the central level as discussed above but also at the subnational level. Thus, while

[6] Financial Management Law and Public Debt Law – passed by the CPA in 2004 also classified as "CPA/ORD/ 2 June 2004/95" includes the Financial Management Law as Annex A and the Public Debt Law as Annex B - attached to Order 95.

regulations have been changed, at the level of the Governorate and regional treasuries, the accounting and financial staff has not been provided training regarding the new instructions and regulations. As a result, treasury auditors find it difficult to discuss all related matters with the employees when spending is in process.

12. In Kurdistan, this picture is made more complex by the existence of two separate administrations. While Kurdistan has made significant progress in harmonizing these laws, some questions remain as to the extent to which federal or regional laws will prevail in areas including external audit, civil service management, and accounting and reporting. Practices in Kurdistan broadly follow national arrangements and guidelines, but with a series of important modifications and amendments. For example, Kurdistan is not subject to external audit from the federal Board of Supreme Audit; instead, it has its own structure, as discussed in detail in Chapter III.

13. **Capacity to implement the recent PFM reforms needs to be enhanced at all levels of government.** While many of the recent legal changes have indeed had the effect of bringing Iraq closer to recent advances in public financial arrangements across the world, capacity has been a problem in implementing the new arrangements. Thus while the new Financial Management Law and Public Debt Law instituted by the CPA assigns a leading role to the Ministry of Finance for the budget preparation process (macro-economic projections, budget guidelines, negotiations with the line ministries, scheduling, coordination between recurrent and capital expenditures), as required in any modern system, the capacity of the Ministry of Finance to fulfill this role needs to be enhanced for these reforms to bear fruit. In addition the FML has also sought to integrate the capital and current budget thus adding to the responsibilities of the ministry of finance while changing the role of MOPDC. These significant changes to the role and the responsibilities of the Ministry of Finance have not been matched by measures to increase the capacity of the ministry to fulfill this mandate. Moreover, capacity problems at the subnational level are especially acute since the process is new. Thus budget formulation is especially weak since the Governorate Councils have only just been introduced to the process. In addition, the reforms to the classification system and chart of accounts need to be understood and implemented at the subnational levels by officials who have yet to be trained to use the new process.

14. **The role that subnational governments have played in executing budgets has varied between Kurdistan and the other Governorates**. The execution of investment budgets, in particular, remains a very significant concern for both devolved and deconcentrated entities. The partial execution of ARDP funds in 2006 raised questions about the sources of the major execution bottlenecks. Several initiatives in public financial management were undertaken as part of the 2007 budget preparations. But these measures will have to be linked to a series of medium-term efforts to strengthen PFM capacity and accountability at the subnational level to bear fruit. Kurdistan's allocations however, were fully disbursed. While the allocations for the Governorates were released in 2006 (the actual releases came fairly late in the budget year), actual execution was significantly lower. Through the middle of December, only about 40 percent of budgeted funds had been disbursed. The remainder was transferred to the Governorates in late December, with the provision that it could be spent in 2007. This means that Governorate structures are expected to spend four times as much in 2007 as in 2006, namely ID 3 billion for 2007, plus ID 1.8 billion carried over from 2006, compared with ID 1.2 billion in actual spending in 2006.) Although they only succeeded in spending 40 percent of what they received last year.

15. **The key challenge faced by the Governorates in financing and providing services is related to the process by which expenditures are being devolved**. While the central government has increased the resources it makes available to the Governorates, budget execution has suffered for several reasons, particularly the ad hoc delegation of expenditures, lack of clarity

in authority, and varying degrees of capacity across the levels of government. What is critical under the circumstances is the proper sequencing of the decentralization process to reduce the risks and the costs of the transition. The starting point would be to clearly assign spending powers and responsibilities to the appropriate level of government. But the process of decentralization has been conducted rapidly (Annex III), with little consideration for institutional arrangements or capacity at the subnational levels. The lack of detail and sometimes unclear provisions in the body of laws relating to decentralization has provided little guidance on roles and responsibilities at the different levels of government.

## C. Subnational Expenditure Assignments in Iraq

16. **Broadly, the question is whether all regions are able to finance some basic level of assigned expenditure responsibilities given comparable own revenue efforts.** As the next section highlights, given Iraq's dependence on oil, special attention will have to be paid to designing intergovernmental revenue assignments in an appropriate manner. These could be decided on a per capita basis using population or could be further refined to address expenditure needs. Expenditure needs can be based on different indictors such as population, poverty rate, land area. For example, the Center of Statistics and Information Technology of Iraq, housed in the Minister of Planning, is putting in place statistics that could feed into the creation of such a set of indicators.[7] In a number of countries[8] similar indicators are used in rules-based equalization formulas. Another example in a nondecentralized context is the Islamic Republic of Iran, where such indicators are used to prioritize discretionary allocations to Governorates.

17. **Agreement on the appropriate "vertical share" of subnational governments would help clarify other questions of subnational financing.** Before turning to horizontal allocations across Governorates and regions in Iraq, it may be useful to ask what the vertical share of subnational governments might be, given Iraq's prevailing expenditure priorities. Such an analysis would be helpful from a normative perspective, while also providing some indication of the types of subnational PFM and sectoral capacities that will be necessary to adequately manage large transfers of resources.

18. **The 2005 Constitution provides some guidance concerning expenditure assignments, and, consequently, revenue assignments** (see Annex IV for Constitutional Articles Related to Intergovernmental Finance). The Constitution defines exclusive federal roles (Article 110) and shared roles (Article 114), leaving all other roles to subnational governments (Article 115). When discussing these roles it is convenient to distinguish between policy making, financing, and provision (see Table I.1). On the question of financing and provision, the current Constitution leaves some room for interpretation. By contrast, Article 110 assigns clear rights over the armed forces to the federal government. Thus while a region may maintain its own security, the costs are a federal responsibility. The present criteria for allocating revenues to Kurdistan identify purely national expenditures as sovereign expenditures, which are deducted before granting Kurdistan a population-based share of the divisible pool (Article 17 of the 2007 budget). An obvious national expenditure, foreign affairs, is included in this category.[9] Electricity is defined as a shared authority (see Article 114 of the Constitution). Education policy, too, is shared with the center,

[7] Communications with Ministry of Planning, March 2007.
[8] Examples of countries using rules based formulas include Indonesia and Pakistan.
[9] In the case of Kurdistan's revenue allocation, however, defense is excluded from these sovereign expenditures, as it is left to special arrangements between the central and regional leadership (see Article 17[5]).

although the sharing may not extend far beyond policy issues. Clearly a major question for future arrangements will be whether such financing requirements as teachers' salaries will be part of the central or subnational budget. Article 115 of the Constitution is quite extensive in granting subnational agencies all residual power.

19. **In 2007, subnational governments were responsible for just under 18 percent of government expenditures.** Table I.1 summarizes fiscal flows to Kurdistan and the Governorate Councils during the past few years. Kurdistan's government accounts for the largest share of subnational expenditures (11.6 percent of total), with revenues autonomously split between capital and recurrent expenditures. Most funds allocated to the Governorate Councils (5.2 percent of subnational expenditures, or ID 3 billion in 2006 and 2007) are for investment purposes. These funds are allocated across Governorates, based on population.

**Figure I.2 Sub-national Expenditure Shares (2007 Budget)**

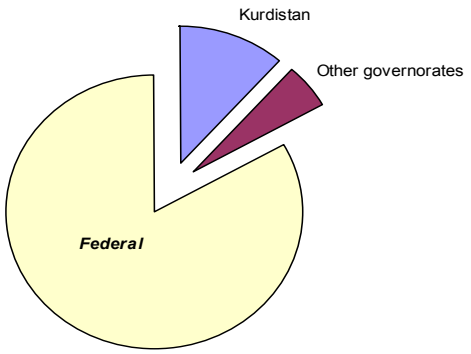
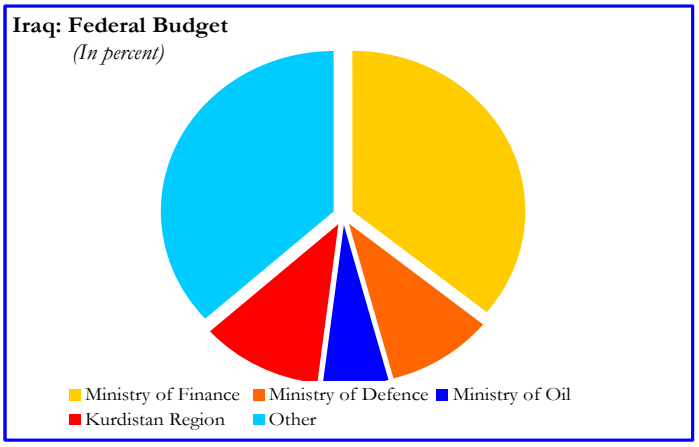



**Figure I.3 Major Spending Items in the Federal Budget (2007)**




20. To illustrate prospective subnational expenditure shares, we examined the 2007 budget in light of its administrative classifications. We considered whether each item in the budget might be (i) exclusively federal, (ii) equally shared (50–50 percent of financing), (iii) shared but primarily subnational (80 percent), or (iv) exclusively subnational. Prevailing spending patterns have the Ministry of Finance (MoF) accounting for just under 36 percent of total expenditures. These expenditures include significant transfer programs (for food and fuel subsidies, for example) as well as servicing of debt, which are considered federal. For each of the expenditure items in the 2007 budget, we prorated prospective expenditures to the national and subnational levels. While this method is obviously crude, given the lack of clarity in roles and responsibilities it makes an important point. It suggests that additional transfers of resources to subnational levels should reflect the purpose for which the transfer is being made. For example, if central line agencies are currently being assigned resources to carry out particular functions, these revenue assignments should not be duplicated at the subnational level and vice versa.

21. **The share of subnational expenditures may grow over time if the proposed assignment of expenditures in the Constitution were to be followed.** Using the shares of expenditures under the current budget and assigning them using the above prospective expenditure assignment, subnational expenditures may already be 10 percent higher, at 27.1, than they were in 2006—the increase being driven by developments in Iraq's Governorates outside Kurdistan. The indicative calculations suggest that the share of subnational expenditures (the "vertical share" of revenues commanded by subnational governments) could increase to just over 27 percent based on current expenditure patterns.

22. **The proposed assignment of expenditures broadly suggested by Articles 110, 114, and 115 indicates that Iraq's expenditure assignment is in keeping with worldwide practice** (see Table I.1). If expenditure responsibilities are divided between a macro/policy oversight function and financing and provision of social, transportation, utility and other services commonly provided by governments, Iraq's suggested expenditure assignment is in keeping with worldwide indicators for most of these services.

**Table I.1 Representative Assignment of Expenditure Responsibilities**

| | Macro Policy/Oversight | | Financing | | Provision | |
|---|---|---|---|---|---|---|
| **Function** | Worldwide | Iraq | Worldwide | Iraq | Worldwide | Iraq |
| **Social services** [a.] | | | | | | |
| Social welfare | C | C, R/G | C | C | C,G,M | C |
| Hospitals | C | C, R/G | C,G,M | C | C,G,M | C |
| Public health | C,G | C, R/G | C,G,M | C | C,G,M | C |
| Universities | C,G | C, R/G | C,G,M | C | C,G,M | C |
| Secondary education | C,G | C, R/G | C,G,M | C | C,G,M | C |
| Primary education | C,G | C, R/G | C,G,M | C | C,G,M | C |
| Housing | C,G | C, R/G | C,G,M | C | C,G,M | C |
| **Transportation** [b] | | | | | | |
| Urban transportation | C,G,M | C, R/G | C,G,M | C,G,M | C,G,M | C,G,M |
| Railroads | C,G | C, R/G | C,G | C | C,G | C |
| Airports | C,G | C, R/G | C,G | C | C,G | C |
| Ports and navigable waterways | C | C, R/G | C | C | C | C |
| Urban highways | C,G,M | C,G,M | C,G,M | C,G,M | C,G,M | C,G,M |
| Interurban Highways | C,G | C | C,G | C | C,G | C |
| **Utility services**[c] | | | | | | |
| Electricity | C,G,M | C | C,G,M | C | C,G,M | C |
| Waste collection | M | M | M | M | M | M |
| Water and sewerage | M | G,M | M | G,M | M | G,M |
| **Other services**[d] | | | | | | |
| Fire protection | M | C | M | C | M | C |
| Heating | M | C | M | C | M | C |
| Irrigation | M | C | M | C | M | C |
| Police | C,G,M | C | C,G,M | C | C,G,M | C |

C = central government; R= Region (Kurdistan), G = Governorate deconcentrated, Governorate Councils; M = municipal government.

a. These services are national in scope. The central government has a role in correcting fiscal inefficiencies and regional inequalities. It should also provide some financing to cover spillovers.
b. The overriding concern is the efficient provision of services. If the benefits of services accrue to local jurisdictions they should be financed by local residents. If the benefits spill over to other jurisdictions, the service is national, and the cost of service should be borne by nonresidents as well as residents.
c. These services are local in scope. If the services are financed by national revenues, nonresidents bear the cost of services. In that case, inefficient allocation of resources is a major concern. However, preservation of the internal common market might also be a concern. The central government may have a regulatory role in ensuring efficiency and equitable provision of some of these services.
d. The primary beneficiaries of these services are local residents; they are most efficiently provided by local governments.

**Table I.2 Current and Prospective Subnational Expenditure Shares (percent, based on 2007 budget)**

| Expenditure assignment by major sector | Current expenditure assignments | Potential expenditure assignments | Federal | Subnational |
|---|---|---|---|---|
| Federal, e.g., foreign affairs | **82.4** | **68.3** | 68.3 | |
| Shared, but with significant federal role (50 percent), e.g., water | | **3.0** | 1.5 | 0.7 |
| Shared, but primarily subnational, e.g., education (80 percent) | | **11.9** | 2.4 | 9.5 |
| Fully subnational | **16.9** | **16.9** | | 16.9 |
| | **99.3** | **100.1** | **72.2** | **27.1** |

## D. Subnational Revenue Assignments in Iraq

23. **The pattern of future fiscal decentralization will be transfer- dependent because of the predominance of oil-based revenues in Iraq**. While Iraq has one of the largest reserves of oil in the world it is predominantly dependent on just the one revenue stream (see Annex I.6). As the recently drafted policy note on fiscal sustainability makes clear, Iraq's fiscal outlook is highly dependent on oil revenues with 95 percent of revenues coming from oil. In the foreseeable future both the national and sub-national governments in Iraq will be directly or indirectly dependent only oil revenues. At present Iraq does not share oil-based revenues on a derivation basis. Considerations of politics and equity mitigate assigning revenues from natural resources to subnational entities, owing both to the volatility and the concentration of those resources. But a number of countries, among them Malaysia, Nigeria, and Indonesia, have systems of subnational sharing. In turn, some form of equalizing transfers may be necessary to address pressures to further devolve revenues. While less significant, other sources of revenues (e.g., customs, sales taxes, and corporate taxation) have the potential of driving both revenue diversification and growth. Effective mobilization of these revenues however depends on clear intergovernmental assignments. However, even if these arrangements are clarified the share of own-source revenues is unlikely to increase significantly in the near term for subnational governments, until economic activity picks up since most possible sources of such revenues are highly dependent on economic activity.

24. **Several countries dependent on hydrocarbon revenues have smoothed the revenue streams that finance public expenditures by establishing oil stabilization funds.** Discussions about creating such a fund are underway in Iraq but are tied to the larger discussion of how revenues will be shared, as well as the not-unrelated topic of sharing authority over petroleum development among different levels of government. At this juncture the Development Fund for Iraq (DFI) plays the role of an oil fund (Box I.2). Oil revenues above the estimated price set in the budget accrue to the DFI. Iraq has applied a simple fiscal rule in preparing its budgets for 2004–07, using very conservative export price forecasts.[10]

[10] For example, while planning its 2007 budget the government twice scaled back its price forecast, reflecting the weakening of the oil markets in the second half of 2006. See draft note on fiscal sustainability.

**Box I.2 The Development Fund for Iraq**

The Development Fund for Iraq (DFI), established under United Nations Security Council Resolution 1483 and housed within the Central Bank of Iraq, holds the proceeds of Iraq's petroleum and natural gas export sales, as well as assets and funds of the former Iraqi Government. Its accounting records are maintained by the Central Bank of Iraq on behalf of the Iraqi Ministry of Finance. Funds are held in the U.S. Federal Reserve Bank in New York (FRBNY).

From 2003 to end-June 2006 the DFI received US$68.8 billion from the proceeds of Iraqi oil export sales and balances from the UN oil-for-food program and frozen Iraqi funds. Of this, US$59.6 billion was disbursed to the Ministry of Finance or used for letters of credit for Iraqi ministries and contracts administered by U.S. agencies.

Until the end of 2007, the International Advisory and Monitoring Board (IAMB) serves as the audit oversight body for the DFI. Thereafter the Government of Iraq's Committee of Financial Experts (COFE) will act as the audit oversight body for the DFI. Established in 2003 under Resolution 1483, the mandate of the IAMB was to ensure that the DFI was used in a transparent manner for the benefit of the people of Iraq and that export sales of petroleum, petroleum products, and natural gas were consistent with prevailing international market practices. The IAMB's first summary report in December 2004 covered operations from May 2003 until the dissolution of the Coalition Provisional Authority (CPA) in June 2004. The second interim report with the IAMB's comments and conclusions was released in December 2006. The IAMB was succeeded by an Iraqi Oversight Board composed of financial experts and chaired by the president of the Board of Supreme Audit. The decision to replace the IAMB with the new body (Committee of Financial Experts) was made by the Council of Ministers in October 2006.

DFI's accounts are audited by an independent international audit firm every six months. The auditor's task is to audit the financial statement, transfers from U.S. agencies to the Government of Iraq, and funds disbursed by all spending ministries. Until its dissolution, the IAMB monitors the reports produced by the contract auditors and determines whether the audits were conducted in a comprehensive and satisfactory manner. Iraq's Board of Supreme Audit follows up on the recommendations of the audit reports, and reports to the IAMB on the steps taken. External audits have revealed unreconciled differences between the DFI's asset balances and related liability balances in the records of the Central Bank of Iraq.

25. **Lack of agreement regarding the desirability of oil stabilization arrangements and fiscal rules between the central authorities and the KRG will make macro management more difficult at the national level and development spending more volatile at the subnational level**. Dependence on a volatile revenue stream requires that stabilization instruments be allowed to run their course. Thus an agreement that makes Kurdistan dependent on actual revenues rather than estimated revenues means that they will need to regulate their expenditures using only their own share of the total revenues and plan their spending keeping this in mind. The disadvantage of such an arrangement is that unless Kurdistan decides to create its own oil stabilization fund, it could be deprived of the benefit of the revenue smoothing function that the DFI now performs; with drastic consequences should prices fall. Moreover, designing the detailed arrangements for the sharing of actual revenues too will present difficulties.

26. **Good practice in intergovernmental finance suggests that finance should follow function.** To ensure that all Iraqis are able to benefit from some basic level of public service delivery, international good practice suggests that functional assignments should follow expenditure assignments. Subnational service delivery can be financed from a number of sources: own source revenues, shared revenues, and transfers. A variety of transfers could encompass block grants or special purpose/conditional grants. A central concern in the design of these transfers would be whether vertical and horizontal imbalances are adequately addressed given variations in the own-source revenues of various subnational entities. Vertical shares broadly refer to total revenues from a variety of sources provided to subnationals overall, whereas horizontal allocations refer to those across subnationals. However, much of the public debate over fiscal decentralization has focused on the potential allocation of oil revenues (either on a

derivation or formula basis), and the creation and powers of new regions. Discussions of Kurdistan's share have occurred in the context of the annual budget negotiations (see Chapter II).

27. **Non-oil revenue collection is currently limited.** Non-oil revenues amounted to 7.2 percent in the 2006 budget. The budget approved for 2007 lowered this to 5.1 percent. Changes between 2006 and 2007 underscore the high degree of uncertainty associated with individual revenue bases. For example, while corporate income taxes were slated to account for almost half of non-oil revenues in the 2006 budget, projected levels for 2007 have been reduced by 90 percent. Similar reductions have been made for the reconstruction levy, which in effect represents a 5 percent customs charge, outside of a broader list of goods with exceptions (such as food, under CPA Order 70, as amended).[11] Moreover, the figures in the federal budget for 2007 do not seem to include all customs revenues collected. The customs revenues collected by Kurdistan at the Turkish border enter Kurdistan's budget, not the federal budget.[12] The limited non-oil revenue collection in the current budget reflects the security situation in many parts of the country and the damping effects of that situation on economic activity.

**Table I.3 Federal Revenue Mobilization in Iraq**

| Revenues | Revised 2006 | Budget 2007 | Percentage Variance between 2007 and 2006 (revised) |
|---|---|---|---|
| **Oil** | **42,106,300** | **39,091,500** | **(7)** |
| **Non-Oil** | **3,286,000** | **2,083,000** | **(37)** |
| Reconstruction Levy | 600,000 | 369,000 | (39) |
| Personal Income Tax | 90,000 | 169,000 | 88 |
| Corporate Income Tax | 1,422,000 | 150,000 | (89) |
| Employee Income Tax | 85,000 | 170,000 | 100 |
| Interest Earned | 73,000 | 273,000 | 274 |
| SOEs | 181,600 | 406,000 | 124 |
| Services | 30,900 | 35,000 | 13 |
| Taxes & Other fees | 491,500 | 311,000 | (37) |
| Pensions Contributions | 144,000 | - | (100) |
| Maks Tax (on Islamic Traders) | 168,000 | 200,000 | 19 |
| | | | |
| **Total Revenues** | **45,392,300** | **41,174,500** | |
| Non oil revenues as percentage of total | 7.2 | 5.1 | |

Numbers in parenthesis have a negative sign i.e. the amount was reduced in the 2007 budget.
*Source:* Ministry of Finance, 2007 Federal Budget

[11] The 2006 federal budget envisioned raising the reconstruction levy to 10 percent, but this measure was never completed.

[12] Article 17(4) of the 2007 budget calls for Kurdistan to submit estimates of its expected revenues for 2007 and statements of revenues realized from all sources for the years 2004–06. All these revenues are to be registered in the accounts of the federal budget. Most of the imports into Iraq through Kurdistan come from Turkey. While data from The Direction of Trade Statistics Yearbook indicates that imports from Turkey to Iraq have increased from 912 USD million in 2003 to 3023 UD million in 2005, it is difficult to estimate how much of this came in through Kurdistan and therefore the amount of customs that are being collected.

28. **A number of laws and regulations provide the legal basis for customs, income, and property taxes (see Annex V)**. Notable amendments/revisions to Iraq's taxation policies were made as part of the CPA's annual tax strategies for 2003 and 2005 respectively (Orders 37 and 70). These involved a number of exemptions and new rate brackets for income taxation. Several ministries collect user fees, which appear to enter the treasury as "self-funding entities." Notable examples include electricity, water, and sewage (in the form of semi-independent commissions under the MoMPW), health-care fees, and school fees.

29. **Most non-oil revenue in Iraq is administered by the Commission for Taxes, a unit of the MoF.** The commission administers the income tax, various property-related taxes (real estate rental tax, vacant land tax, and real estate transfer tax), and sales taxes.[13] Under the income tax law and CPA amendments, salaries, wages, and fringe benefits are subject to withholding. Employers must remit the estimated taxes withheld from salaries and wages to the General Commission for Taxes. A federal tax directorate sits in each Governorate. The commission also appears to assist in the collection of certain taxes flowing to the municipal administrations.

30. **Self-funding municipal taxes currently fall under the purview of the MoMPW.** Under the municipal law of 1963, municipal governments receive building duties (nominal and computed on the basis of building size), slaughterhouse duties (on particular types of livestock), advertisement duties, excise duties on tobacco products (collected by the federal government and shared equally with municipal governments), professional duties (based on the rental values of workplaces), and some producer duties (based on 5 percent rent of factor). Municipal governments also own local assets and properties, which may generate usage or rental fees. By contrast, Governors' offices and Governorate Councils do not hold local assets. Article 16 of the 2007 budget law notes that "the Minister of Municipalities and Public Works is authorized to reallocate the budgeted funds of a self-funding municipality to execute needed services." As noted in Chapter IV, the ministry can supplement the budgets of staff and activities in the self-funding municipalities, but this is exceptional.

31. **Some Governorate Councils appear to be collecting revenues under authority that is disputed by the MoF.** Six Governorates have enacted their own tax laws and administrations. Babil, Al Basrah, Karbala, Maysan, and Wasit are collecting and retaining revenues for use by their Governorate Councils. The councils cite CPA Order 71 (enacting powers for the Governorate administration) to establish the legality of de facto reconstruction levies.[14] These are raised through a 5 percent tax on various activities (including wages, tourist fees, imports, and exports). The collection of such fees is disputed by the MoF. Information is scarce on the types and volumes of the Governorate collections. It seems clear, however, that although the amounts may be significant for individual Governorates, they are not large compared with the federal

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[13] Relevant legislation includes income tax law 113 of 1982 as amended; real estate rental tax law 162 of 1952 as amended; vacant land tax law 26 of 1962 as amended; sales tax law 36 of 1997 (for hotels and restaurants); and the real estate transfer tax (CPA Resolution 120 of 2002). See the website of the General Commission for Taxes at www.iraqtax.org. Foreign companies registered in Iraq or having a permanent establishment in Iraq are subject to corporate income tax at a flat rate of 15 percent on their income earned in Iraq. Income earned from contracts, as defined in CPA Order 17 as amended, and income earned in the connection with work performed under special agreements, such as the Agreement for Economical and Technical Cooperation between the USA and Iraq, are exempt from tax. Since foreign companies cannot own real estate in Iraq, only income tax laws pertain to them.

[14] A key difference in CPA Order 71 was in allowing Governorates to both set and retain certain revenues. The right to retain revenues was originally set out in the law of 1963 but was significantly scaled back in the Law of Governorates of 1969.

budget. In this sense, they could be understood as nuisance taxes. Governors' offices do not collect any notable taxes, save for limited fees for office services.

32. **Kurdistan currently collects some non-oil revenues that are not included in the federal budget.** Available estimates suggest that Kurdistan's own non-oil revenues are no more than 2 percent of the region's total revenues in 2006 (see Chapter II), after transfers from the federal government (financed largely by oil revenues). The 2007 budget law again underscores the need to book those revenues as part of the federal budget.[15]

33. **Our brief review of non-oil taxation suggests that these revenues are likely to remain limited in the short to medium term.** From a subnational perspective, however, they may be important, especially if linked more directly to local accountability for service delivery. In Kurdistan, non-oil revenue mobilization has been used to increase the regional government's fiscal space and to reduce its dependence on central transfers. Further clarification of its revenue assignments will be needed, however, especially with respect to such typically national assignments as customs. Outside Kurdistan, the self-funding municipalities have perhaps the most diverse local revenue base. But Governorate reports suggest that revenue yields are variable and low, suggesting the need to strengthen arrangements in this regard. The primary level of devolved government at present has no official revenue base. This may in part reflect the trend of some Governorates to impose their own taxes, which may not be the most efficient or economically sound way to raise revenue. Consequently, further work will be needed to explore promising ways of allowing the Governorates (and eventually regions) to raise their own revenues.

[15] Article 17 (2): "Kurdistan Region shall have to submit the estimates for their expected revenues during 2007 and statements for the realized revenues during the years (2004–2006) generated from all sources. All these revenues shall be registered in the accounts of the Federal Budget."

# II. STRUCTURE OF PUBLIC FINANCE AND ADMINISTRATION IN KURDISTAN

## A. Introduction

34. **The Kurdistan Regional Government (KRG) operates as a regional government within Iraq.** It encompasses the Dahuk, Erbil, and As Sulaymaniyah Governorates (out of Iraq's 18 Governorates).[16] A unification agreement between the two factions in Kurdistan was announced in Erbil on May 7, 2006, to merge two separate Kurdish administrations. Prior to the agreement, Erbil and Dahuk had been governed by the Kurdish Democratic Party (KDP), while As Sulaymaniyah was administered by the Patriotic Union of Kurdistan (PUK). There are currently 30 ministries in Kurdistan. Four key ministries are in the process of merging with the unified Kurdish administration—the ministries of finance, *peshmerga*, justice, and the interior. The new government is based in Erbil, the Kurdish capital.[17]

35. This chapter documents available knowledge concerning Kurdistan's public finances and civil service management. It details the content, process, and basis for fiscal transfers from the center to Kurdistan. Chapter III provides a more detailed assessment of the quality of prevailing PFM practices. The observations concerning PFM are structured along the lines of the 28 public expenditure and financial accountability (PEFA) performance indicators set.[18]

## B. Fiscal Transfers to Kurdistan's Government

### *Allocation for National/Sovereign Functions*

36. National functions are performed by the central government to represent sovereign Iraq, and are detailed in Table II.1. The 2007 budget also includes 19 national functions and oversight activities, and makes special provisions for defense.[19]

### *National In-Kind Programs*

37. **In-kind expenditure programs include food rations, fuel subsidies, and medical drugs.** These programs, including those in Kurdistan, are deducted from the revenue pool. The in-kind expenditure/programs are itemized in Table II.2. Within each in-kind program, Kurdistan is expected to receive a share (presumably 17 percent). At present, in-kind allocations are a matter of dispute between Kurdistan and the central government, with the former complaining about the lack of transparency in the calculation of values of such allocations.

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[16] Kurdistan also appears to administer a number of localities beyond these boundaries.

[17] Consequently its intergovernmental relations echo may of the issues found in other federal contexts such as Brazil, India, Mexico, Nigeria, Pakistan, and Russia, as well as Australia, Canada, Germany, and the United States.

[18] These capacity-building reforms are to be in a manner that: encourages country ownership; reduces the transaction costs to countries; enhances donor harmonization; allows monitoring of country PFM performance over time; better addresses developmental and fiduciary concerns; and leads to improved impact of reforms.

[19] Article 17 (5) of Budget Law states: "A deal shall be made between the Prime Minister of Iraq and the President of the Region on expenditures of arming and equipping the regions' guards as part of the national defense system."

**Table II.1 In-Kind Expenditures**

| *Budgeted/estimate figures* | 2006 Federal Budget Allocation ID (million) | 2006 KRG ID (million) | 2007 Federal Budget Allocation ID (million) | 2007 KRG ID (million) |
|---|---|---|---|---|
| Public Distribution System (Ration Card) | 4,500,000 | 765,000 | 3,928,000 | 667,760 |
| Farmers' Subsidies | 300,000 | 51,000 | (-) | (-) |
| Pilgrimage Expenditures | 45,000 | 7,650 | 59,400 | 10,098 |
| Electricity Import Expenditures | 450,000 | 76,500 | 378,450 | 64,337 |
| Iraqi Property Claims Commission (excluding Admin) | 300,000 | 51,000 | 300,000 | 51,000 |
| Fuel Imports for Power Plants | 245,000 | 41,650 | 207,000 | 35,190 |
| Fuel Import Expenditures | 3,845,000 | 653,650 | (-) | (-) |
| Medications | 867,000 | 147,390 | 728,280 | 123,808 |
| Election Expenditures | 280,000 | 47,600 | | 0 |
| Census | 47,697 | 8,108 | 130,000 | 22,100 |
| **TOTAL** | **10,879,697** | **1,849,548** | **5,731,130** | **974,292** |

*Source*: Ministry of Finance
*Note*: (-) = Not available

## *Governorate Development Program*

38. **Under the Governorate development program (also known as the Regional Development Fund) Kurdistan's three Governorates receive US$133 million.**[20] Kurdistan's share of this program is 13.1 percent, an amount also based on population shares. This is different, however, from the 17 percent used to determine allocation of cash transfers and in-kind programs and is also calculated on the basis of population share relative to the rest of Iraq. The use of differing population figures is illustrative of the continue divergence in views between the central and Kurdish authorities on basic data issues. Debates over the region's share of Iraq's total population are important to discussions about fiscal transfers. In 2006, Kurdistan received no reconstruction funds whereas all the other Governorates received such funds.

[20] The Regional Development Allocations provided to all Governorates in Iraq. Kurdistan's share of the Regional Development Funds (E') is 13.1 rather than 17 percent—as 13.1 is the percentage that the Ministry of Finance assumes for the three Governorates under KRG's administration, which is lower than 17 percent. The allocations are essentially provided as cash, although it is unclear how this program is ultimately maintained. Kurdistan does not receive a share of the Rapid Reconstruction line item, ID 1.5 trillion, which has been allocated to the other 15 Governorates.

**Table II.2 Regional Development/Reconstruction**

| Regions | Population sum total | Amount allocated for development of territories (Dinar, Billions) | Amounts allocated for speeding up construction of Provinces (Dinar, Billions) | Total 2006 PC Allocation (Dinar, Billions) | Population Estimated 2007 Population | Total 2007 Projected (Dinar, Billions) |
|---|---|---|---|---|---|---|
| Provinces not Incorporated as Regions | 25,238,430 | 1,322 | 1,500 | 2,822 | 26,014,571 | 2,604 |
| Regions/Kurdistan | 3,803,323 | 196 | 0 | 196 | 3,951,809 | 396 |
| **Grand Total** | 29,041,753 | 1,500 | 1,500 | 3,000 | 29,966,380 | 3,000 |
| *Share Kurdistan* | *13.1%* | *13.1%* | *0.0%* | *6.5%* | *13.2%* | *13.2%* |

*Source*: MOF

## *Regional Development Banking Program*

39. Under the regional banking development program, Kurdistan is allocated US$44 million (amounting to 22 percent of total allocations for this development program).[21]

## *Calculation of Kurdistan's Allocations*

40. The exact calculation used for Kurdistan's various allocations in 2006 is shown in Table II.4. Starting with an estimation of total revenues in the federal budget (A, see Table II.4), the basic block grant cash allocations are determined by subtracting a number of purely central expenditures (B, see Table II.4) as well as other in-kind expenditures (see Table II.2) from the divisible pool that is partially set aside for Kurdistan (Table II.4 items C and D). Also deducted from this pool are allocations for regional banking sector development outside of Kurdistan (D). Kurdistan then is allocated 17 percent of this divisible pool (F), or the amount based on its notional population share. In addition, Kurdistan is given its own allocation from the regional banking sector development (H) from the overall divisible pool (compared to the allocation D that the other localities receive).

[21] The Regional Development Bank allocations (H) appear to be determined for strengthening financial sector development, which was a priority of the previous finance minister. The 2006 budget suggests that these funds are being used by the Ministry of Finance to help restructure three regional development banks, to be established in Al Basrah, Mosul, and Kurdistan. The overall capital for the regional development banks is ($500 million), and will be covered in three years beginning in 2006. In the 2006 federal budget, $180 million will be allocated. The amount for Kurdistan was specially allocated and represents 22 rather than 17 percent of the total size of this program.

**Table II.3 Kurdistan's Allocations from Federal Budgets, 2006–07**

| | | 2006 | | | | 2007 | | | |
|---|---|---|---|---|---|---|---|---|---|
| | **Summary Allocation** | Dinars Millions | USD Millions | Kurdistan Allocation | % Total Revenues | Dinars Millions | USD Millions | Kurdistan Allocation | % Total Expenditures |
| | Total Estimated Revenues (2006) | **46,689,298** | 31,654 | | | 42,064,530 | 33,385 | | |
| **A** | *Total Estimated Expenditures (2007)* | | | | 100.0% | **51,727,468** | 41,054 | | 100.0% |
| B | *minus national expenditures (see Table 2)* | -9,312,174 | -6,313 | | 19.9% | *10,135,420* | 8,044 | | |
| C | *minus national "in-kind" programs ( → where 17% earmarked for Kurdistan, see Table III)* | -10,879,697 | -7,376 | X (17%) | 23.3% | 5,731,130 | 4,549 | X (17%) | 11.1% |
| D | *minus Strengthening Regional Development Banks Program (non-Kurdistan allocations)* | -210,000 | -142 | | 0.4% | (-) | | | |
| E | *minus Regional Development Funds ( → where 13.1 percent shared with Kurdistan)* | -1,500,000 | -1,017 | X (13.1%) | 3.2% | -3,000,000 | -2,381 | X (13.1%) | -5.8% |
| **F** | *National Divisible pool for Share Base* | 24,787,427 | 16,805 | X (17%) | 53.1% | | | X (17%) | |
| G | *a Kurdistan Allocation (17% of F)* | 4,213,863 | 2,857 | X | 9.0% | 5,586,356 | 4,434 | X | 10.8% |
| H | *→ Plus Kurdistan Regional Banks Development Allocation* | 60,000 | 41 | X | 0.1% | (-) | | X | |
| **I** | **→ Sub-Total Total Kurdistan (G+H)** | **4,273,863** | **2,898** | | **9.2%** | **5,982,356** | 4,748 | | 11.6% |
| E' | *Plus Development Funds* | 196,000 | 133 | | 0.4% | 396,000 | 314 | | 0.8% |
| | **→ Total Kurdistan Cash Allocations** | 4,469,863 | 3,031 | X | 9.6% | **6,378,356** | 5,062 | X | 12.3% |

*Source*: KRG

*Note*: Some data for 2007 are not yet unavailable.

41. **The total revenue figures used to determine Kurdistan's divisible pool differed slightly from the final revenue estimates used in the federal budget for 2006.** Since Kurdistan's allocation was determined before the completion of the final central budget (dated December 4, 2005), a number of figures used in Table II.4 differ from those in the budget. For example: (i) the total revenue estimate of ID 46.7 trillion is somewhat higher than the ID 45.3 trillion in the final budget; and (ii) some of the estimates for central expenditures, as set out in Table II.1 are higher than in the final budget. The use of these preliminary figures proved slightly more favorable to Kurdistan in the allocated cash transfers in 2006.[22]

### *Kurdistan's Share of the Divisible Pool—Process for Transfer of the Cash Allocation*

42. **Cash allocations are transferred directly to the Kurdistan Central Bank in Erbil.** The bank in Erbil typically receives transfers two to three times per month. While it is still part of the Central Bank of Iraq, its staff is paid by Kurdistan.[23] Prior to the unification of Kurdistan's two administrations, allocations were split 56 percent for Erbil/Dahuk (the former Kurdish Democratic Party–led administration) and 44 percent for As Sulaymaniyah (the former Patriotic Union of Kurdistan administration). This split system was used in 2006 because the unification process was still underway, but was scheduled to change in 2007. Transfers are typically made on a biweekly basis. Although there are complaints of delays, current realizations of these transfers appear to be above 95 percent.

[22] All else constant, this implies a boon of US$149 million for Kurdistan. The differences in the in-kind expenditures would have meant that Kurdistan would have received US$ 8 million more.

[23] Transfers to the Mosul Governorate also seem to be routed via Erbil.

## C. Issues in Kurdistan's Intergovernmental Fiscal Relations

43. A number of issues affect the current determination of fiscal transfers from Baghdad to Kurdistan. These include: (i) how to make fiscal transfers more predictable; (ii) appropriate deductions for national programs; (iii) possible reforms of national in-kind intergovernmental fiscal relations; and (iv) transparency and intergovernmental equalization.

### *Determining the Divisible Pool in an Oil-Dependent Economy*

44. **Kurdistan argues that federal revenue estimations, notably for oil, are too conservative, which in turn affects their transfer entitlements.** Kurdistan believes that the federal government estimates of the overall "divisible pool" on excessively conservative oil price assumptions and consistently underestimates the overall amount of federal revenues owed to Kurdistan.[24] More than 95 percent of Iraq's revenue base depends on the realized output and price of oil and gas production. Because there is no mechanism to redistribute the difference between the estimated and realized amounts, Kurdistan does not benefit if the realized revenue is higher than the estimated revenue. But the effect of lower realized federal revenues is not clear. Preliminary projections for 2006 have realizations for federal oil revenues through the end of October at US$25.3 billion—this projects to US$30.36 billion through the end of the year.[25]

45. **Overall oil revenues accrue to the Development Fund for Iraq (DFI) prior to being partially used to meet the Iraqi budget.** Inflows to the DFI[26] have exceeded commitments in 2005 and 2006 (Ernst & Young 2006).[27] In the first half of 2006, payments into the fund amounted to US$12.573 billion, exceeding outflows to the Central Bank of Iraq/MoF by US$0.952 billion. Outflows have included transfers to the MoF (US$7.75 billion in the first half of 2006, as well as US$4.435 billion in letters for credit for Iraqi ministries, plus some payments for Iraq debt and contracts by administered by U.S. agencies). Consequently, in 2006, Kurdistan would have argued that its transfers should have been based on total oil realizations to the DFI (and whatever other flows it considered to be incomplete). The 2007 shift to an expenditure basis for transfers changes this, although it raises another question: what is an appropriate rules-based allocation that would be consistent with petroleum revenue management?

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[24] The 2006 federal budget oil revenues were based on assumptions of exports of 1.65 million barrels per day at US$46.61 per barrel.

[25] See Bureau of Near Eastern Affairs, U.S. Department of State, Iraqi Weekly Status Report, October 11, 2006, p. 23. Compared to outcomes, Kurdistan's 2006 transfers were slightly more favorable to the region because a more optimistic preliminary revenue projection was used for the budget (although these may in turn have differed from DFI realizations). But the central agency deduction was overstated when compared with the final budget (see Table II.1). The current projections for revised revenues in 2006 suggest that total revenues will be slightly lower, which in turn would reduce Kurdistan's transfer entitlements if they were based on actual revenue. At the same time, deductions for realizations could come in lower owing to lack of disbursement. At least for 2006, however, these figures do not suggest that Kurdistan has been short-changed on transfers in a significant way based on the current allocation rules. In future, it will be important to agree on appropriate rules beforehand.

[26] The DFI was sanctioned under United Nations Security Council Resolution 1483, dated May 21, 2003. The International Advisory and Monitoring Board (IAMB) is an audit oversight body for the Development Fund for Iraq (DFI) (see www.iamb.info).

[27] Ernst & Young. 2006. "Development Fund for Iraq: Interim Results (January 1, 2006–June 30, 2006)." Presentation to IAMB Meeting, October 30.

46. **As with all natural resource revenues, budget assumptions are just that, assumptions.** International experience suggests that revenue volatility can hamper expenditure management, growth, and service delivery. During windfalls, petro states often increase expenditures and even accumulate debt, and do so in an unsustainable manner. During periods of lower or falling oil revenues, painful and disruptive expenditure adjustments are then required (such as for discontinuing capital projects in midstream, deferring operational expenditures, or even laying off staff).

47. **Direct dependence on a volatile revenue source such as oil can worsen revenue predictability.** For this reason, as well as for reasons of interregional equity, the international literature is highly skeptical of concentrating oil revenues in a single producing region either through sharing or direct revenue assignment arrangements.[28] In this context, national governments have an important role to play in managing overall fluctuations in oil revenues, especially when subnational regions may have lower capacity and poorer access to the fiscal and monetary instruments to do so. There are many different institutional arrangements for oil revenue management that involve a variety of roles and responsibilities for subnational governments.[29] For these types of arrangements to work in a federal setting, however, all partners must feel confident that there is revenue transparency particularly on how savings and drawdowns from an oil revenue management account are accessed. A full discussion of these issues is beyond the scope of this note, but each is critical for budget credibility and sustainability in Kurdistan.

48. Kurdistan might wish to negotiate a mechanism for sharing the difference between the realized and estimated oil revenues with the central government**.** If projected oil revenues in the federal budget are too conservative, Kurdistan will contend that it is owed additional transfers at the end of the year. Such an arrangement will also generate a floor for revenues. But the promise of an oil windfall at the end of the year may also undermine budget credibility because policy makers would expect additional revenues not assigned for saving. At the same time, Kurdistan may have to accept that it will ultimately receive less if prices or quantities of production at the central level fall significantly short.

49. **Revenue management for the medium and long term is a central challenge for oil-dependent state such as Iraq.** Given that Iraq is one of the most oil-dependent countries in the world, revenue management is especially critical for the central and subnational governments. Good public financial management practices suggest that expenditure levels in a petro state such as Iraq should be delinked from short-term (that is, annual) oil revenue estimates. For Kurdistan, the appropriate levels of expenditure would ideally be determined in the context of a medium-term expenditure framework. For example, the framework would note the quality and sustainability of expenditure levels by ensuring that capital projects are completed as planned and budgeted, rather than their completion being contingent on the volatility of oil revenues.

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[28] See for example J. M. Davis et al., *Fiscal Policy Formulation and Implementation in Oil-Producing Countries,* Washington, DC: IMF, 2003

[29] For example, because of recent reforms in Nigeria, its states deposit oil windfalls (which they are entitled to under intergovernmental fiscal arrangements) into their own accounts at the central bank, thereby contributing to better macroeconomic management. Alternative revenue management arrangements can also be envisioned, with various degrees of roles and responsibilities designated to KRG and the central government.

### *Issues Relating to the Deduction of Central Expenditures*

50. **Kurdistan maintains that a number of central expenditures should not be deducted from its divisible pool.** Notably, federal investment expenditures provided for the oil sector remain well below estimates in 2006 and are not benefiting Kurdistan. Kurdistan argues that none of the central government's investments in the oil sector were invested in Kurdistan. But it can be argued that federal investments in oil will ultimately benefit Kurdistan through increased federal oil revenues; if current sharing arrangements are maintained, expenditures would indirectly benefit the region through increased national oil production.[30] More generally, Kurdistan argues it should not be penalized for low national execution rates for sovereign items (Table II.1) deducted from its divisible pool, which reduce its fiscal transfers. But linking Kurdistan's transfers to execution rates for national programs could make the process of determining Kurdistan's ultimate fiscal transfers more complex and uncertain. This would entail that Kurdistan's ultimate transfer entitlements depend on a host of factors, including oil revenue and central government expenditure realizations. Each of these could work in favor of, or against, Kurdistan's transfer amount. Second, some would argue that because the current political situation in Iraq could provide perverse incentives for the central government to artificially inflate execution rates, these resources would otherwise accrue to Kurdistan, regardless of the quality of these programs.

### *Reexamination of In-Kind Allocations*

51. **Kurdistan contends that a number of in-kind/earmarked programs should be provided to them in cash.** Provision in cash would allow Kurdistan to purchase goods (such as medical drugs) according to their needs, and enable the region to better monitor the implementation of the full monetary value of these expenditures. Possible arguments to continue earmarked programs in an intergovernmental context would be that they exploit some economies of scale (for example, in procurement), avert negative externalities (such as further distorting markets if fuel subsidy levels are regionally determined), or address national responsibilities and priorities. While beyond the scope of this study, it should be a priority to review these programs against the criteria noted above and strengthen their transparency and the evaluation of their performance.

### *Budget Comprehensiveness and Own-Revenue Collections in Kurdistan*

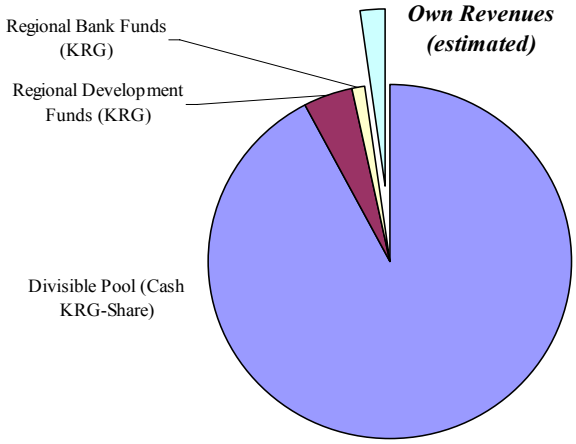
52. **Budget comprehensiveness is considered an important aspect of good public financial management, and includes accurate reporting of all revenues.** At present, the central government contends that Kurdistan does not report revenues collected in its territory. The center argues that this fiscal capacity should be deducted from transfers to Kurdistan, although, to date, this has not been the case. The main source of Kurdistan's income is the customs revenue collected at the borders of Turkey and Iran. This customs revenue amounts to 5 percent of the value on all nonhumanitarian goods.[31] Kurdish authorities estimate this was only US$60–70 million in 2006 (about 2.3 percent of transfer levels). Figure II.1 suggests that reported own-source revenues remain small relative to transfers.[32] Authorities in Baghdad argue, however, that a significant part of customs revenues are off-budget and, moreover, that Kurdistan's border posts charge different rates on imports, thereby

[30] The region argues that oil investments have historically discriminated against Kurdistan; hence, the region is pursuing a number of direct production sharing contacts with international operators.
[31] The 2006 budget assumptions suggest that this rate be raised to 10 percent, but the mission's understanding is that it remains at 5 percent.
[32] The team did not have the opportunity to confirm the validity of these figures.

undermining uniform customs collections in Iraq. International good practice suggests that customs are typically best assigned as a national revenue source. Both parties will need to find an appropriate method for the management of customs revenues as part of broader discussions on revenue assignments and transfer design.

**Figure II.1 Revenue Estimates and Total Cash Transfers, Kurdistan**

***KRG's Own Source Revenues are Limited Compared to its Reliance of Transfers***




*Source*: KRG Ministry of Finance

53. **International best practice suggests that intergovernmental equalization transfers should be based on spending needs and assignments.** Kurdistan should have sufficient resources to meet its Constitutional responsibilities. This implies the need for some agreed-upon standard to budget for expenditures based on need (for example, using proxies such as Kurdistan's population share—a method now in use) and potential fiscal capacity. Other such measures include the cost of providing services and the level of underdevelopment (owing to a range of historical factors). The danger with this type of transfer system is that it could provide a disincentive for Kurdistan to mobilize its own revenues. Hence, it is not advisable to use own-source revenue realization figures to directly offset transfers. Whether Kurdistan's fiscal transfers from Baghdad should be linked to its own fiscal capacity is an open question. Given the relatively small size of current own-source revenues, the absence of good proxies for fiscal capacity in Kurdistan, and low PFM capacity, it is probably more important to focus on a simple and transparent intergovernmental fiscal design in the short to medium term. But if Kurdistan were able to draw on significant flows of direct oil revenues in the future, this issue should be revisited.

54. **Fundamentally, the Baghdad authorities contend that Kurdistan accounts for only 13 percent of the population, not the 17 percent Kurdistan claims.** Baghdad currently uses the latter share as the proxy for expenditure needs, determining fiscal transfers for Kurdistan from the divisible pool. But in the case of the regional development funds for Kurdistan, Baghdad uses only 13.1 percent based on Governorate population figures used by the MoF. Future work will need to focus on the validity of this figure, as well as other potential proxies for regional expenditure needs. However, this is unlikely to be resolved until a national census can be held.

## D. Fiscal Space Considerations

55. **Kurdistan will need to manage its fiscal position in terms of both revenues and expenditures.** Table II.4 illustrates the various options open to Kurdistan in managing its fiscal position in terms of revenues (from transfers, own-source revenues, or borrowings) and expenditures over the short and medium term (IMF/World Bank 2006). The table is not meant to assign potential magnitudes (in nominal terms or as a share of regional GDP).[33] Each of these four areas is that a government, be it national or subnational, can take to enhance its fiscal space to achieve outcomes across sectors (Table II.5).

**Table II.4 Comments on Elements of Kurdistan's Fiscal Space**

| Element | Comments |
|---|---|
| **Increased grants/transfers** | • The analysis assumes that given Kurdistan's dependence on transfers from Baghdad, Kurdish policy makers will negotiate with the central government on the level and design of intergovernmental transfers in an effort to ensure that the revenue stream is not reduced. |
| **Improved revenue effort** | • Kurdistan is also considering other strategies to diversify its revenue base. The regional government anticipates future direct revenue flows from new oil production within Kurdistan's boundaries, but the timing and magnitude of these revenue sources remains uncertain. Increased own-revenue fiscal capacity on the part of Kurdistan may result in an offset of central transfers. |
| **Net borrowing** | • In the short to medium term, it appears unlikely and perhaps even inadvisable that Kurdistan rely on borrowing to address its fiscal space. Good PFM practices are a precondition for credit worthiness, as well as first achieving gains on the other dimensions of the triangle. In the short term, Kurdistan will need to enhance its own capacity for making fiscal projections and managing revenue. Debt agreements are in the exclusive domain of the federal government (Article 110 of the Iraqi Constitution). |
| **Expenditure efficiency** This in Kurdistan's own hands | • Broadly speaking, fiscal expenditures can be categorized as wages, recurrent nonwages, and capital. Kurdistan must both effectively prioritize across sectors, as well as ensure that allocations within sectors are effective. Finally, it must ensure that spending is efficient and reaches front-line service delivery units such as schools and clinics. Effective expenditure management is the greatest challenge for Kurdistan, notably as it translates into tangible public services and investment for the region's citizens. The first step to achieving expenditure efficiency can lie in improving key areas of public financial management (PFM). Most potential: Kurdistan itself can aim to do more with its existing expenditure levels. This will depend both on how it manages its wage bill in combination with non-wage recurrent and capital expenditures. |

### *Modernizing Kurdistan's PFM Arrangements*

56. Following a difficult history marred by persecution and conflict, the region is now poised to improve basic services (such as education, health, and administration) and investments in infrastructure (such as electricity, roads). Public expectations are high and the key challenge will be to translate expenditures into tangible results across both rural and urban areas.

### *Public Sector Wage Bill and Fiscal Sustainability*

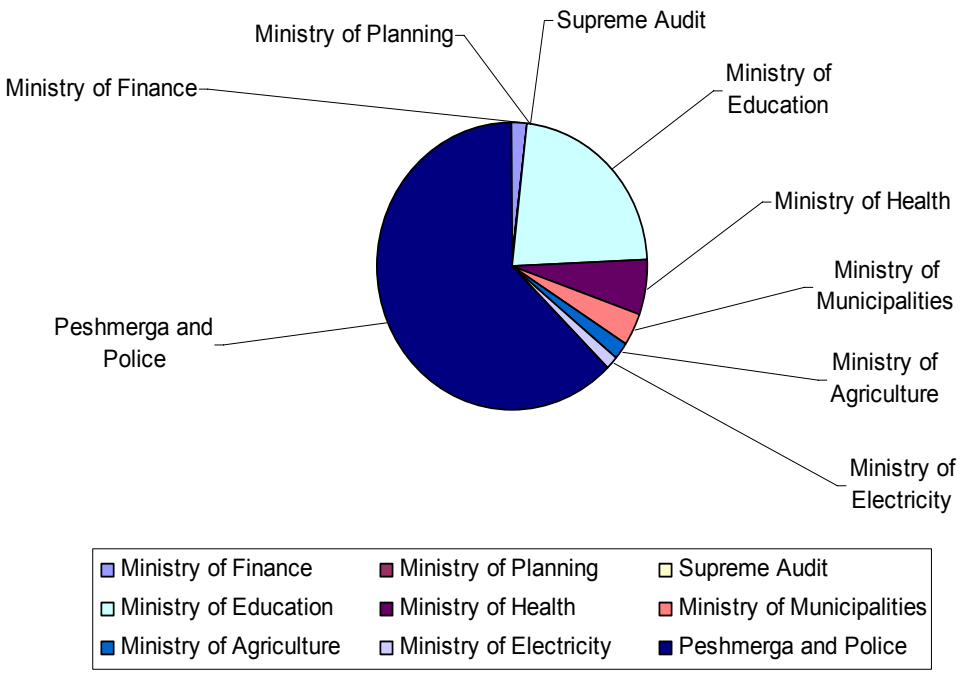
57. **Wage bill pressures in Kurdistan are putting significant pressures on fiscal sustainability.** Continued growth in the wage bill has meant that investment expenditures have in effect had to be rationed, undermining annual budget credibility. These wage pressures are driven by both the number of civil servants and their remuneration levels (which in part are aligned with

[33] The basic data for such an exercise (including Kurdistan's GDP) are unavailable.

national scales). At present, Kurdistan's civil service wage bill is serving largely as a social safety net, rather than financing a capable and modern civil service. To enhance expenditure efficiency, Kurdistan will need to explore other ways of providing social transfers.

58. A further important challenge is to improve the professionalization of the KRG civil service and to ensure that priority areas are properly staffed and paid (see Figure II.2 for staffing pattern in Erbil/Dahuk).

**Figure II.2 Estimated Public Sector Staffing Levels in Kurdistan, 2006 (Erbil/Dahuk)**




59. Recently Kurdistan decided to provide teachers (estimated at 70,000) a monthly supplement of US$ 90 (at an estimated cost of US$ 76 million, or 2.7 percent of transfers). The increase was also deemed necessary to maintain competitiveness and attracting new teachers to the workforce. The police forces are also hoping for an increase. A recent decision by Baghdad to merge and increase pay levels in the lowest grades, if extended to Kurdistan, is likely to have important implications for Kurdistan's salary expenditures.[34]

60. Public sector pay is based on the 13-grade scale (high-class A/B and levels first through eleventh) maintained at the national level. The wage bill is comprised of base wage rates (with some flexibility for raises), supplements, and the overall number of staff (including transition to pensioners). More detailed analysis of filled posts in As Sulaymaniyah suggests that while staffing at the lowest grades tends to meet or exceed targets, the region has problems attracting skilled personnel in the middle tiers (such as teachers).

[34] The Coalition Provisional Authority (CPA) decision to increase the salaries of public servants nationwide in 2003 also had a direct impact on KRG's budget.

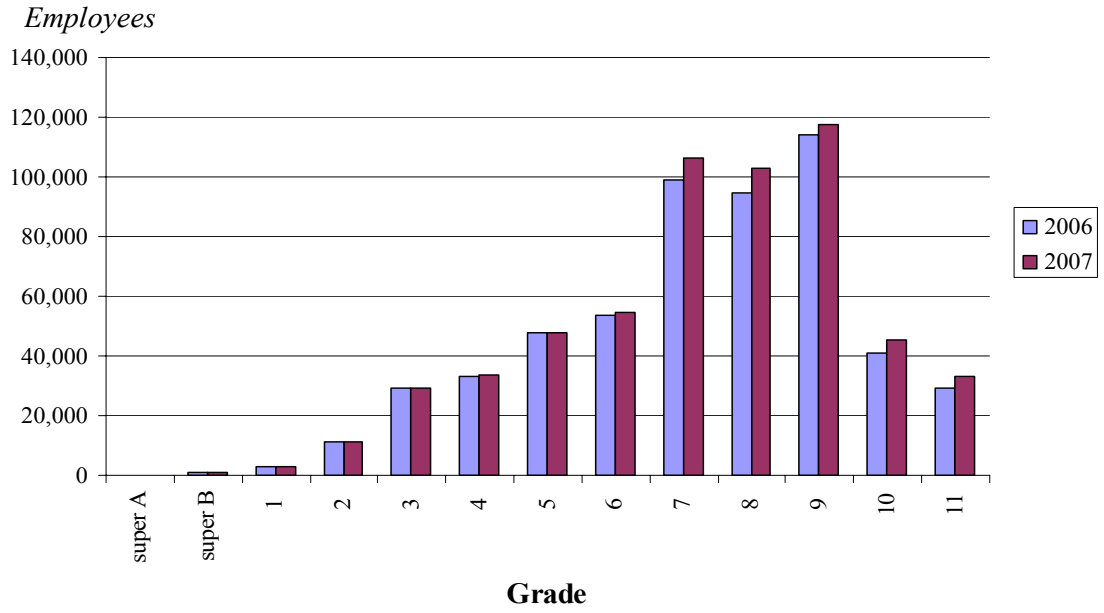
61. **Strengthened human resource management will be critical to effective public service**. Measures to strengthen human resource management could include: clarifying roles, responsibilities, and accountabilities of functional departments; grouping similar activities while avoiding ambiguity, duplication, and overlap across different levels of government within Kurdistan (that is, Erbil, the Governorates, and mayoralties/communities); creating better information systems (such as a unified civil service database); ensuring effective human resource management and meritocracy, in particular among key management staff and front-line service delivery personnel. Further and more detailed analysis is required on the appropriate pay grades, structures, and benefits of maintaining national standards. The modernization objectives of Kurdistan, however, should strive to avoid the proliferation of ad hoc supplementary payments that are poorly linked to effective human resource management.

62. **Better cost-recovery measures could help finance additional services for the poor.** Services such as health care are free for all residents of Kurdistan. In order to fill the deficiencies of in-kind transfers from Baghdad, a significant amount of Kurdistan's budget is spent on these services. Income-based cost recovery along a sliding scale against family income, particular among those able to pay, could free up recurrent expenditures to finance additional drug needs and ensure a pro-poor health-care policy.

63. **Wage bill control in Kurdistan has two aspects: (i) control over the number of approved posts, and (ii) compensation policy**. Total public sector employment in Kurdistan accounts for about 14.3 percent of the population, a high percentage by international standards. Each ministry, department, and agency is assigned a number of approved posts, by grade. Increases (or reductions) to this cap can take place only during the annual budget process. Compliance with the cap can be enforced in two ways. First, all new appointments must be signed by Kurdistan's prime minister. If a department has filled all its posts, the prime minister can refuse to sign an appointment letter. Second, if a ministry, department, or agency submits a monthly payroll request to its respective treasury office with an unexpected increase in the wage bill, the pertinent treasury official—we were informed—is likely to request an explanation, and in the case of additional employment, to ask for proof of budget authorization before sanctioning the treasury release.

64. Total monetary compensation for public employees includes base pay, allowances, and a pension entitlement. The base wage scale (as of February 2007) for all public employees in Iraq was established by CPA Order 30 (September 8, 2003). The order stipulated that the wage scale would remain effective until September 30, 2004, but it has remained valid until the present day. The 2007 budget includes a revised base pay scale, with pay increases for grades five and below. The new scale also eliminates grade 11, merging these employees in grade 10. (Prior to CPA Order 30, Iraq had an eight-grade scale, without horizontal steps).

**Figure II.3 Government Employment by Grade, KRG**




65. It is not uncommon for the distribution of public employees to be skewed toward the lower end. But a well-structured civil service will generally have a bell-shaped profile because most service delivery roles require some specific skills. A civil service highly skewed to the low end often indicates patronage employment. While the post-distribution profile in Kurdistan is not obviously improper, it is a cause for concern that the 2007 allocation displays an evident shift toward the lower grades.

66. **Kurdistan is considering some measures to reduce the civil service.** It has put forward a plan whereby, on a voluntary basis, government employees would receive half pay for two years, and leave their government job, thereby encouraging them to find employment in the private sector. There are two concerns with this proposal: (a) Will spaces vacated under this plan be filled by newly hired patronage employees? and (b) Will the released employees return to the government after two years, as they are entitled, thereby bloating the roster once again?

67. **The Iraqi Constitution appears to empower Kurdistan to establish a separate base pay scale for its employees.**[35] Kurdistan has adhered to the national pay-setting scheme, however, and does not appear to have seriously considered striking out on its own in this area. This is in contrast to allowances, where Kurdistan has established several of its own.

68. **The CPA order eliminated all previous monetary allowances, permitting only risk and geographic allowances.**[36] Police officers and drivers in Kurdistan (as well as the rest of Iraq) are entitled to a risk allowance of ID 50,000 per month. There are no geographic allowances established

[35] Article 121 states: "The regional powers shall have the right to exercise executive, legislative, and judicial powers in accordance with this Constitution, except for those authorities stipulated in the exclusive authorities of the federal government. The regional government shall be responsible for all the administrative requirements of the region."

[36] These allowances include family allowances, qualification allowances, position allowances, vocational allowances, and so on.

in Kurdistan (or any Governorate in Iraq). But Kurdistan has established several allowances in the education sector. Allowances are authorized by the prime minister, following input from the MoF. A professional allowance of ID 125,000 was established for all teachers in September 2006. Between 2005 and 2006, a series of additional allowances were established.[37]

69. **In most areas of human resource management there is substantial room for improvement.** Indications are that there are no approved organizational structures below the highest levels of each ministry, department, and agency. In the absence of an approved organizational structure, it is not surprising that there are no approved staffing lists for each ministry, department, and agency in Kurdistan (for example, number of drivers, clerks, accountants, assistant managers, senior managers, and so on). Rather, there are only establishment lists with the overall posts by grade.[38] Detailed staffing lists—and a census of existing staff positions—are likely to reveal the significant problem of hiring too many employees. (There are many anecdotes of ministries, departments, and agencies where less than half the staff performs meaningful work.) Few job descriptions specify the tasks to be performed by the jobholder, or identify experience and abilities that a prospective hire for that post must possess. Without job descriptions it is impossible to select employees by merit.

70. **A critical first step is to modernize the Kurdish civil service.** Kurdistan should consider creating an independent civil service commission to ensure merit in personnel selection. Commissions can perform an oversight role to ensure that merit-based criteria, rather than patronage or personal favoritism, determine hiring decisions for the civil service. They can serve as an appeals body when there is an allegation of an improper selection, promotion, or disciplinary decision. In some countries, the civil service commission itself carries out the selection process for new hires.

71. As the economy of Kurdistan grows more robust and private sector employment expands, Kurdistan will want to compare relevant labor market data on private sector jobs in the region and similar public sector posts. Comparisons of this kind will be possible only after detailed job descriptions have been crafted**.**

72. Kurdistan's civil service could also be modernized with the establishment of a central office of public administration or office of personnel management. The name does not particularly matter. What does matter is that the agency maintain a database on public posts and employees, prepare (or approve) job descriptions, and review compensation levels. Like the civil service commissions, these are not ad hoc committees but rather permanent institutions of government—in many countries, linked to the executive or prime minister's office, or to the ministries of finance or planning. Regardless, it is always important that the MoF has a formal role in sanctioning any personnel or pay increases that have a fiscal impact on the budget.

73. **International experience suggests various governance arrangements for the civil service.** In some countries, the civil service commission or office of personnel management is a single organization with a judicial body and a sizable secretariat. If the government wishes to make palpable improvements in human resources management—which should be a top priority—it should

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[37] In addition to monetary compensation, it is generally understood that public employees across Iraq are entitled, at some point, to receive a plot of land from the government. This promise is not always kept, and those who are first hired are not necessarily the first to receive a plot of land. It is impossible, therefore, to quantify the value of this benefit.

[38] For instance, the Ministry of Health will know the total number of doctors and nurses it employs, but not the overall staffing mix.

establish at least one institution (and perhaps two) to guide and oversee the modernization of the civil service.

74. **The merging of Kurdistan's two administrations provides a unique opportunity for reforming the PFM system.** Care must be taken, however, to ensure that bottlenecks in implementation and absorptive capacity do not derail this process. In both the areas of (i) modernizing PFM and (ii) building a capable effective civil service the Kurdish authorities will need to sequence a program of reform building on local ownership.

# III. QUALITY OF PUBLIC FINANCIAL MANAGEMENT IN KURDISTAN

75. The previous chapter outlined several major challenges facing the Kurdistan Regional Government (KRG) in the areas of fiscal management and public administration. This chapter examines Kurdistan's PFM system in detail using a standard set of 28 public expenditure and financial accountability (PEFA) indicators (see Table III.1) that cover (i) budget credibility, comprehensiveness, and transparency (PI 1–10); (ii) policy-based budgeting (PI 11–12); (iii) predictability and control in the budget (PI 13–21); and (iv) accounting, reporting, and external scrutiny and audit (PI 22–28). Individual indicators may have up to four sub-indicators. Ratings are on an *A* (best) to *D* (weakest) scale.

76. Two findings are clear from the assessment. First, most indicators are rated D. Second, there are many indicators, or sub-indicators, for which not enough information is available to arrive at a suitable rating. This in itself provides a clue about the state of PFM in Kurdistan. However, some caveats are also necessary. The weaknesses of Kurdistan's PFM system may be due to difficulties encountered in the unification of the two prior administrations, or to administrative confusion sown by changes to the legal framework by the Coalition Provisional Authority (CPA). If so, one may expect improvement as these difficulties and confusions decline over time. Also, in the absence of supporting documentation about current practices, conservative rather than liberal ratings have been assigned. Indicators with multiple subcomponents are scored on a "weakest-link" basis, meaning the weakest score largely drives the overall rating (World Bank 2005b). At this stage, the exercise should be construed largely as an effort to assist Kurdistan's policy makers in understanding PEFA indicators, learning how to apply them in future budgets, and identifying key areas of reform.

77. The next few sections discuss the PEFA indicators for KRG in terms of the three broad categories noted above. An indicator by indicator review is provided in Annex I.

## A. Budget Credibility, Comprehensiveness, and Transparency (PI 1–10)

78. **Data for 2005 and 2006 suggest low budget credibility.**[39] This is reflected in the following findings based on Table III.2 which provides expenditure data for the two sub-administrations, Erbil/Dahuk and As Sulaymaniyah: (a) Aggregate realized expenditures in As Sulaymaniyah were substantially below budgeted spending in both 2005 and 2006 though they were on target in Erbil/Dahuk in 2005; (b) The composition of actual spending deviated substantially (by more than 25 percent) from the budget for both sub-administrations in both years; and (c) Actual revenues received were substantially below those budgeted in As Sulaymaniyah (similar data were not available for Erbil/Dahuk.) Furthermore, while KRG officials indicated that arrears in payments (to contractors, vendors, staff etc.) were not a major issue, the lack of timely budget and realization data casts doubt on the ability of the authorities to accurately track arrears.

[39] These data were not readily available and different versions were not always consistent with each other. Moreover, the mission was not able to compile this information according to administrative and functional classifications. The data presented here are based on the economic (known as 'chapters') classifications traditionally used in the Iraqi central budget. The limited availability of consistent budget information itself undermines budget credibility and makes it difficult to manage the budget.

**Table III.1 Summary Budgets in Kurdistan, 2005–06**

| | Erbil/Dahuk (millions Dinars) | | | | As Sulaymaniyah (millions Dinars) | | | |
|---|---|---|---|---|---|---|---|---|
| | 2005 Budget | 2005 Realized | 2006 Budget | 2006 Realized* | 2005 Budget | 2005 Realized | 2006 Budget | 2006 Realized* |
| | *(i)* | *(ii)* | *(iii)* | *(iv)* | *(v)* | *(vi)* | *(vii)* | *(viii)* |
| Transfers/Baghdad (Cash) | | | *2,307,960* | *1,740,152* | 2,646,037 | 1,772,614 | *1,966,040* | 1,142,694 |
| Own Revenues | | 15,290 | *48,122* | | 3,080 | 24,911 | 5,175 | 21,226 |
| **Total Revenues** | | | **2,356,082** | | **2,649,117** | **1,797,525** | **1,971,215** | **1,163,920** |
| | | | | | | | | |
| **Expenditures** | **2,036,767** | **2,035,766** | **2,322,886** | | **2,646,037** | **1,889,637** | **2,801,769** | **1,281,862** |
| Salaries | 580,517 | *839,035* | 762,639 | | 456,146 | 668,387 | 746,713 | 555,363 |
| Service Requirements | 72,500 | *98,398* | 75,000 | | 57,000 | 56,516 | 50,000 | 17,112 |
| Goods Requirements | 66,000 | *96,884* | 66,000 | | 63,940 | 52,277 | 60,000 | 16,532 |
| Asset Maintenance | 82,000 | *64,925* | 354,247 | | 91,525 | 104,659 | 109,529 | 55,860 |
| Capital Expenditure | 73,000 | *112,632* | 75,000 | | 72,000 | 60,136 | 110,000 | 28,020 |
| Transfer Costs | 571,150 | *202,296* | 370,000 | | 482,397 | 337,925 | 394,735 | 283,849 |
| Investment Projects | 420,000 | *420,000* | 420,000 | | 330,000 | 353,652 | 330,000 | 255,000 |
| Pensioners' Salaries | 171,600 | *201,597* | 200,000 | | 159,400 | 209,210 | 150,000 | 70,127 |
| Governing Expenses | | | | | 933,629 | 46,876 | 850,792,080 | 39,100,000 |
| ex-Kurdistan regions (e.g., Kirkuk) | | | | | | | | |
| | | | | | | | | |
| Dinar/USD | 1,474.0 | 1,474.0 | 1,475.0 | | 1,474.0 | 1,474.0 | 1,475.0 | 1,475.0 |
| Transfers/Baghdad (USD Millions) | | | | | 1,795.1 | 1,202.6 | 1,332.9 | 774.7 |
| Own Revenues (USD Millions) | | 10.4 | 32.6 | | 2.1 | 16.9 | 3.5 | 14.4 |
| * Through 31 July 2006 | | | | *1,461,558* | | | | |
| Budgets are after transfer amount has been confirmed by Baghdad | | | | | | | | |
| * Does not include amounts for Regional Development Projects allocation | | | | | | | | |

*Source:* KRG

79. **Documentation of KRG's budget is either unavailable or difficult to interpret.** Without adequate budget documentation, it difficult to assess what is or is not in the budget, a feature that hampers assessments of budget performance. The current classification system is too aggregated to allow meaningful decisions about spending, and does not facilitate control and tracking of individual spending items.[40] The classification of the budget is still based on the old Iraqi chart of accounts. Administrative and economic (also known as 'chapters') classifications are not used. Moving to the proposed new system being adopted by Baghdad—a system that is based on IMF GFS 2001 — will lead to improvements. Problems with basic reporting also mean that the extent of government operations currently being covered (including state-owned enterprises) is not clear. At this point, it is not clear what the size of the state-owned sector is in Kurdistan and what sort of fiscal risk is posed by it. Finally, at this stage, the federal MoF does not appear to be systematically tracking donor-funded projects in Kurdistan.

80. **There do not yet appear to be clear, rule-based allocations to lower levels of government.** Transfers to local governments are currently managed by the Ministry of Municipalities and Public Works (MoMPW). These transfers are not based on clear rule-based allocations (such as block grants) nor are the roles and responsibilities of different levels of local government adequately defined and demarcated. The passage of Kurdistan's Constitution should address some of these issues. The ministries of finance, planning, and municipalities should clarify how allocations to subregional Kurdish entities (including councils) are to proceed, and should improve their monitoring, including any autonomous revenues that might be collected by these levels.

## B. Policy-Based Budgeting (PI 11–12)

81. **Sector budget allocations are project rather than policy based as is true of the national budget and the Governorate budget.** This situation is compounded by the central government's inability to provide in-kind allocations in a timely fashion, which in certain instances forces Kurdistan

[40] The mission did not receive disaggregated budgets and expenditure realization by functional and economic /administrative classification and, as previously noted, was not able to ascertain budget predictability at that level.

to make emergency purchases in such areas as medical drugs.[41] Within these constraints, however, Kurdistan has a significant agenda in moving to policy-based budgeting, from what in many areas current appears a rather ad hoc planning and budgeting process. Line agency participation in the budget process has been weak and perspectives have not been multiyear.

82. **Currently, the budget in Kurdistan mirrors the federal budget process as set out in financial management law and public debt law, CPA Order 95.** But the draft Constitution of Kurdistan anticipates its own budget law and budget process. Budget proposals from the Governorates are collected by the directorate of finance in each Governorate. This includes priorities identified by all the directorates in the region. The directorate of finance in each Governorate negotiates priorities and budget allocations with the Governor and his or her executive council. In addition, the various Kurdistan ministries submit budget proposals to the minister of finance, who may negotiate budget figures. Kurdistan uses the same forms as Baghdad in preparing its budgets. The council of ministers deliberates over these proposals and identifies priorities based on allocations received from Baghdad in the previous year.

83. **Kurdistan generally needs to be more realistic about revenue transfers from Baghdad earlier in its budget cycle.** The late announcements of transfer levels from the center pose a number of budget challenges for regional ministries. Kurdistan may wish to budget and plan as early as possible based on realistic transfer projections. To date, the process appears to begin with a rather unrealistic view of what transfers may materialize from the center (for example, lists of capital projects totaling more than two to three times what is ultimately approved.

84. **Sector expenditures are not fully aligned with strategic priorities.** At present, budget requests do not reflect strategic priorities within sectors, or more broadly across the sectors. This may be due to weaknesses in the budget process as well as low capacity (in terms of data systems and human resources). The lack of budget predictability makes it difficult for ministries to effectively plan and implement programs. These programs are project based rather than policy based. The Council of Ministers/MoF rations the capital budget. Kurdistan's ministries are, as a rule, poorly informed about ex ante budget ceilings. While the recent establishment of a Ministry of Planning can contribute to improvements in planning and prioritization, care must be taken not to artificially segment capital and recurrent budgeting.[42] International experience suggests that placing these two functions into different ministries adds to the costs and difficulties of harmonizing large capital projects and their recurrent costs.

85. **A multiyear perspective is not effectively followed in fiscal planning and spending.** International experience suggests that special care needs to be taken to ensure that capital and recurrent budgets are not artificially segmented as part of this process. For example, capital projects (such as the construction of a school) need to be clearly associated with future costs in wages, maintenance, and resourcing on the recurrent side. The recent introduction of the Ministry of Planning could become a means to improve the quality of capital investment planning and prioritization. However, if implemented poorly this could lead to fragmentation of the budget process. Coordination between the ministries of planning and finance will therefore need to be assured.

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[41] In-kind allocations are defined here as Iraqi public expenditures that are intended to benefit residents of Kurdistan, but are executed through the national budget rather than the region's budgets. Examples include food rations, fuel subsidies, and drugs.

[42] PEFA, Integrating Recurrent and Capital Budgets, July 2005.

## C. Predictability and Control in Budget Execution (PI 13–19)

86. **Limited information is available about the collection of own revenues.** [43] While it is known that the bulk of revenues come as transfers from the center and the own revenue base is presently small, little information is available about the manner in which own revenue is collected. Customs, rent incomes, and other fees are the main sources of own-revenue and are managed under a directorate general in the Kurdish Ministry of Finance. Anecdotal evidence suggests that taxpayer registration is quite limited in Kurdistan, as are collections. At present, Kurdistan does not yet appear to be collecting tax revenues from production-sharing agreements in the oil sector.

87. **Budget predictability and monitoring appear weak.** Kurdistan's MoF does not appear to regularly share data with the spending ministries, which have no reliable information on the availability of funds, and therefore cannot commit expenditures. This appears to be especially acute for nonwage recurrent and capital budgets. The MoF appears to maintain centralized control over the initial addition of civil servants to the wage bill, as well as the payments of pensions. Respondents noted, however, that this system was cumbersome because of the many employment seekers directly approaching the ministry. Cash for commitments, especially for capital projects, appears to be rationed throughout the year. Ministries requiring access funds often have direct recourse to the respective minister or Council of Ministers.

88. **Although staffing decisions are overseen centrally by the MoF, the management of wage bills and staffing appears to occur at the level of the regional ministries**. The current information system does not appear to have a central civil servant database or payroll. Staff members have identification numbers at the agency level, while internal controls depend on individual ministries.

89. **Procurement is managed at the agency level, roughly following Iraq's national standards.** Procurement is managed by individual ministries, and boards are organized within these agencies. Standards appear to roughly follow guidelines prevailing in the rest of Iraq. It should be noted that new procurement guidelines are being developed at the national level. As Kurdistan works on strengthening different areas in PFM, it should consider whether to modernize procurement practices in the near term and whether to implement national standards. The assessment suggests that improving procurement might produce considerable savings in the public budget. Generally, respondents noted problems associated with ensuring value for money in procurement. On the one hand, projects were often delayed by unavailable resources. The absence of letters of credit and the weak financial system also made it very difficult to open competition to international providers. The Ministry of Health was concerned about its ability to assess the quality of drugs being offered by listed providers operating in the region.

90. **Internal controls are largely maintained at the agency level based on cash rationing.** There exists no system of identifying, capturing, and recording commitments. Kurdistan essentially maintains a cash-based system of accounting. Its Board of Supreme Audit (BSA-Kurdistan) does provide overall guidance for maintaining a system of internal controls. But the depth and coverage of internal controls varies from one ministry to another.

91. Internal audit is discussed in Chapter V in detail. In Kurdistan, the internal audit units in a directorate have no formal work plan for the audits they conduct, but they audit all programs of the directorate. All completed documentation following an audit of a program is sent to the Directorate of Finance and Economy to be checked. If a problem is identified by that directorate, the file is sent back

[43] This is not to say that KRG does not provide the relevant information but that it was not easy to obtain.

to the internal audit unit, and the personnel from both directorates investigate the problem and discuss next steps. Reports of the internal audit units are taken into consideration when the Directorate of Education is putting together its expenditure allocations for the budget for the next fiscal year. The internal unit reports are not public. Reports of the internal units are also scrutinized by the Council of Ministers' own finance and audit unit, which has the authority to check on accounts of all ministries.

## D. Accounting, Reporting, and Controls (PI 20–25)

92. **Accounting, recording, and reporting appear weak overall.** The reconciliation and consolidation of accounts appears quite rudimentary. Reporting is limited to preparation of trial balance which is essentially a book balancing tool and provides no budget management information. It is mainly manual and largely depends on the individual agencies and their relationships with central ministries (see PI 22). This weak capacity is further compounded by the fact that a large number of spending units are on a decentralized system of financial management. Under this arrangement, cash transfers are made by MoF or Governorate treasuries to respective bank accounts of spending units with minimal controls over appropriations. At the treasuries, such transfers are booked as expenses as and when they are made, even though funds may still be present in bank accounts of spending units. Detailed implementation reports (PI 24) or financial statements (PI 25) are not available upon request suggesting that these are not available under current processes. The limited evidence from school and clinic visits suggests that service delivery units suffer the same lack of transparency and predictability concerning intended allocations (PI 23). A number of initiatives however, are promising, such as the Ministry of Education's efforts to build an education monitoring information system (EMIS). Here, some international assistance already appears to have been instrumental.

93. **Databases and information systems are generally weak.** A unified database of civil servants does not exist. A terminal for the financial management information system (FMIS) was under implementation under USAID's Bearing Point FMIS Project with limited functionality and usage[44]. Each month, copies of trial balances are received from regional treasuries at the terminal site. Data are entered into the system and then uploaded to the main server maintained in the MoF in Baghdad. Training on data entry was provided to MoF staff. To what extent the existing FMIS meets the requirements of Kurdistan is unclear. However, implementation of a customized FMIS could provide an important reform opportunity. Kurdish authorities should carefully plan FMIS implementation. It would be a normal practice to have an information technology strategy in place that also encompasses financial management. Capacity building must be prioritized and sequenced to ensure that Kurdistan's public administration achieves good international practices in the short to medium term.

## E. External Scrutiny and Audit Process (PI 26–28)

94. **External audit in Kurdistan suffers from complicated institutional arrangements.** The Board of Supreme Audit (BSA) was established in 1997 in Erbil/Dahuk and in 1994 in As Sulaymaniyah. Thus Kurdistan has two chapters of the BSA. The BSA is an independent body but is linked administratively to the Council of Ministers, although the council is subject to financial supervision by the BSA. The legal framework of the BSA is based on the 1990 Iraqi law, which has been modified over the years by the two Kurdish administrations. But a new Kurdistan-specific BSA law is being drafted to take into account Kurdistan-specific issues such as those resulting from unification. Points of contention between the two BSAs were expected to be resolved by the end of December 2006, but at the time of writing, the unification of the two BSAs had not been completed.

[44] The FMIS project has currently been suspended. However, discussions about its continuance are underway.

The delay in unification of the BSAs is tied to the delay in unification of the two finance ministries of the previous administrations. This delay reportedly stems from the vast number of capital projects under each MoF, and from concerns about the impact of unification on financing arrangements for these projects.

95. The BSAs get their budget allocation directly from Kurdistan but coordinate with the ministries of finance in Erbil and As Sulaymaniyah. Whilst the BSA (S) reports to the Council of Ministers, the BSA (E) reports to the President of the KRG. A BSA task force has representatives from both BSAs, and it presents audit reports to the Kurdistan parliament, signed off by the two BSA heads. Despite unification, reports are filed to the heads of the two administrations. A proposed law before Kurdish parliament sets out the institutional arrangements of the unified BSA. The team was unable to obtain the text of the draft law.

96. The unification of the two BSAs will result in one BSA in Kurdistan, with offices in each Governorate. It will report to the Kurdish parliament. Both BSAs have four directors general charged with auditing different ministries. Auditors have to be licensed by the professional body of accountants and each team includes a lawyer. Other specialists such as engineers and finance are often attached to teams depending on the auditing task at hand. The engineers at the BSA are under a great deal of pressure owing to the current boom in construction. Priority is given to auditing agency finances rather than measuring performance. The BSAs do not use outside experts. The team size depends on the ministry's scope of work. BSA/As Sulaymaniyah has 230 staff members, with as many as 100 auditors. For example, the BSA/As Sulaymaniyah stated that the largest teams were for the ministries of finance, municipalities and public works, roads, and reconstruction. The BSA/As Sulaymaniyah has permanent teams in these ministries. BSA/Erbil has 32 auditors and 60 administrative staff. The decision about hiring staff is approved upon request by the Kurdish Council of Ministers, and both BSAs reported that they currently do not have adequate staff.

97. The BSAs plan audits in conjunction with the MoF/Kurdistan. Guidelines and bylaws for audits are also coordinated with the MoF/Kurdistan. The internal audit units within each ministry prepare their statement of accounts in preparation for BSA audits. Currently, internal audit units coordinate audits with the respective ministries of finance rather than directly with the BSA. With unification, coordination issues will be raised to Kurdistan level.

98. The roles of the two BSAs are the same: to control and audit accounts of the bodies receiving public funds from the two administrations in Erbil and As Sulaymaniyah and to ensure that laws, regulations, and financial instruction are properly applied. The BSAs are tasked with ensuring that public expenditure transactions are appropriate and do not exceed the amount stipulated for them in the budget. In addition, the BSA audits are to ensure that there is no waste, extravagance, or malpractice. The BSAs also examine transaction cycles of budget estimation, appropriation, receipt, and management to ensure that the proper procedures have been applied. The BSA expresses opinion on financial statements and reports of publicly funded entities, and ensures that they have been prepared according to legal requirements. The BSAs are also required to conduct performance evaluations, but it is unclear to what extent they do so, or what methodologies they use.

99. The MoF/Kurdistan, in coordination with the BSA, issues orders to ministries and other government agencies on the deadline for closing accounts. At present, the deadline is usually the end of May. The MoF can extend the deadline. The auditing process is ongoing—occurring both before and after the closing of accounts. If ministries have not closed their books prior to the cutoff date, it is noted in the BSA report. The BSAs review audits completed by the internal audit units using a risk-based methodology and verifying that the funds are being spent in accordance with guidelines and

that agencies have not surpassed allocations. The BSA audits all publicly financed government bodies.

100. The internal audit units provide the BSA with a detailed report on the contracts awarded. When investment funds are audited, the BSA ensures that funds are being properly spent on projects and milestones are met. A public declaration of tenders is required under the law, and bids have to be received in a sealed envelope. There are two committees for each project —a supervision committee and a project completion committee. The contract awardee has to put up 5 percent of the estimated project value as a bond, which is returned after a year to ensure that the projects have been properly completed. At the completion of a contract, the awardee signs a declaration of completion.

101. Audits are not computerized. Findings of poor performance, corruption, or waste are recorded in the BSA report. The report is discussed with the head of each ministry. The ministers, together with the responsible directorate, are given an opportunity to clarify matters. In very serious cases of corruption, the matter is taken directly to the Council of Ministers. These reports are confidential. A panel within the council analyzes the findings of the BSA and makes recommendations. Both BSAs stated that cases had been referred to the courts for both civil and criminal proceedings. The matters are sent to the courts by the relevant ministry. BSA/Erbil stated that five to six cases had been referred to the courts in 2005. There are currently no procedures governing follow-up for inaction on BSA audit recommendations.

102. **The BSAs in Kurdistan work independently of the BSA in Baghdad.** The only link mentioned was a joint workshop with the Baghdad BSA in July 2005 The central BSA has not been allowed to operate in the Kurdish area. The president of BSA/Baghdad has proposed to the national Council of Ministers that either the BSAs in Kurdistan become branches of the national BSA or the BSA establish its own regional office in Kurdistan to audit federal funds. Both these options appear unlikely to attract the support of the KRG. The BSAs have had few links with either the International Organization of Supreme Audit Institutions or ARABOSAI**,** and asked the World Bank to facilitate such links. The heads of both BSAs stated that they are aware that the audit laws and procedures do not meet international standards. They try to monitor developments via ad hoc research on the Internet.

## F. Access to Information

103. **Public access to information and government accountability are still new concepts**. For example, the BSA annual report is not public, perhaps due to fear of political repercussions. On the other hand, the draft Kurdistan Region Petroleum Act contains robust public information provisions that may indicate a shift in the attitude towards transparency.

104. **The recent unification of the Erbil-Dahuk and As Sulaymaniyah administrations provides an opportunity to strengthen internal and external audit bodies and the system of controls**. Final negotiations for the merger of the BSAs in Erbil and As Sulaymaniyah are being conducted. Discussions with the BSAs indicate ongoing efforts to review and strengthen their laws. They seem to be isolated, however, from regional and international audit bodies and recognize the need to build capacity in modern audit issues, techniques, and best practices. As in other countries, this would include making the findings of the BSA public in addition to the current practice of reporting only to the cabinet.

105. **Legislative scrutiny of the budget law is limited.** Underlying this fact is the poor quality of overall budget documentation. This oversight function appears to be concentrated in the Council of Ministers. Legislative capacity (for example, in the financial commissions) is itself weak.

## G. Opportunity for Reform

106. **With the 2007 budget unification, Kurdistan has the opportunity to make significant progress on its PFM practices.** This preliminary review suggests that Kurdistan needs to take a series of actions both to improve the management of its fiscal space and its PFM practices including budgetary reforms, accounting reforms, treasury reforms and public sector auditing reforms. The PEFA indicators provide a useful framework to help Kurdish policy makers prioritize and sequence potential capacity-building measures. The findings set out in this note should be considered highly preliminary and are meant only as a basis of discuss and validation with Kurdistan counterparts. Nevertheless, the preliminary scores highlight that Kurdistan will need to engage in a concerted process of capacity building to strengthen its PFM outcomes across the full range of the budget planning, allocation, execution, reporting, and assessment process.

107. Key priorities for the 2007 budget year include publishing a comprehensive budget, identifying expenditures by economic, functional type and administrative agency—expenditures that comply with IMF GFS reporting standards. Realizing budget predictability will require a good estimate of anticipated wage liabilities for 2007, including how anticipated changes in pay and grading structures will affect expenditures given existing staffing levels. In a number of areas, such as procurement, it will be important to clarify the standards and guidelines being used by Kurdistan. The anticipated passage of Kurdistan's Constitution will also likely take an important role in clarifying some of the issues identified in this document.

# IV. STRUCTURE OF PUBLIC FINANCE IN IRAQ'S GOVERNORATES

## A. Introduction

108. The previous two chapters describe public financial management structures and issues relating to the three Governorates that fall in Kurdistan. The next two chapters provide a similar discussion for the remaining fifteen Governorates in Iraq. In the process, attention is drawn not only to formal differences in legal provisions but also to *de facto* differences in practices across the fifteen Governorates.[45] The basic legislative underpinnings of the subnational system are provided by the Coalition Provisional Authority (CPA) Order 71/2004, which came into effect on April 6, 2004.

## B. The Status of Decentralization in the Governorates

109. Governorate Councils were first elected in January 2005. They select the Governor and deputy Governor and prioritize the allocations they receive from the central government under the Accelerated Reconstruction and Development Program (ARDP). They can also alter central line agency projects with a two-thirds supermajority. Representative structures are also replicated at the sub Governorate level (see Figure IV.1 and Annex VII). These are intended to channel local requests from the bottom up, and to hold executive structures to account at lower tiers.

110. The 2005 Constitution sets out a vision of more decentralized regional and Governorate structures, characterized by a significant degree of autonomy. But it leaves the details of financial and administrative arrangements to the legal system. Given the quick succession of political transitions since 2003, Iraqi systems and institutions are still in a state of flux. The functioning of the current decentralized structures is best understood in relation to the legacy of a centralized state; recent CPA reforms; and a general trend toward greater subnational autonomy.

## C. Government Structures in the Governorates

111. The key subnational government entities are: (i) Governors' offices; (ii) Governorate Councils; (iii) municipal offices, and (iv) Municipal Councils. Representative offices of the central ministries include: (i) Governorate treasury offices and (ii) offices of the line agencies (line agency directorates, including directorates general of education, health, and municipalities and public works; see Box IV.1).

[45] This chapter benefited from direct inputs by Governorate representatives, typically from Governorate treasury offices, provided during workshops in Erbil (February 2007) and Beirut (April 2007). Governorates participating in this exercise included Diwaniya, Karbala, Kirkuk, Maysan, An Najaf, Salah Ad Din, Dhi Qar, Wasit, and Al Basrah. Typically these were filled out by the director of the Governorate treasury.

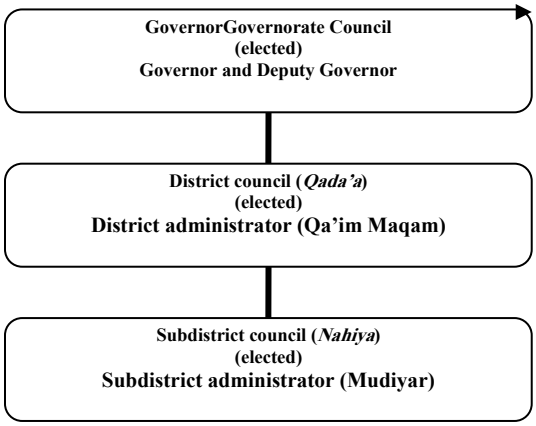
**Box IV.1 Government Agencies across Levels of Government**

| | Ministry of Finance | Ministry of Education and all other line agencies | MoMPW | Governorate Councils and Governors' offices |
|---|---|---|---|---|
| **Central level** | – | – | – | – |
| **Governorate level** | Director of accounts in each Governorate; about 1,000 staff. Reports to MoF<br><br>Treasury Office | Directorate general in each Governorate heads the office. Reports to MoE or respective line agency | Through 2006, directors reported to both the ministry's director general and the Governor | Governors' offices including those in Baghdad; Governorate Councils (in many Governorates, the Governor has been selected by the Governorate Council) |
| **District** | Suboffices in some report directly to director | Some line agencies have suboffices reporting to the DG | No offices at district level but corresponding offices at municipal level | Mayoral councils receive investment funds through municipalities and report to MoMPW.<br><br>Municipal Offices are accountable to Municipal Councils and report to MoMPW. |
| **Subdistrict** | Suboffices in some report directly to director | Some line agencies have suboffices reporting to the DG | | |

*Source*: MOF, Governorate Offices
*Note*: MoMPW = Ministry of Municipalities and Public Works.

112. Governorates are further subdivided into districts and subdistricts. The MoF, line agencies, and Governors' offices in turn may have representatives at these levels. Organizational structures and processes are set out by a variety of laws, CPA orders, and other instruments (see Annex V). *It should be noted that line agencies tend to follow respective ministerial orders rather than general regulations and laws or, notably, CPA orders.* Figure IV.1 depicts the three subnational tiers of government as established by CPA Order 71/2004. Prior to 2007, Governors' offices were formally associated with the Ministry of Municipalities and Public Works (MoMPW), but are now considered independent agencies.

**Figure IV.1 The Three Subnational Tiers of Government**



113. The status of subnational governance, as envisaged in CPA Order 71/2004 on local governmental powers, was confirmed in Iraqi Constitution of 2005[46]. Under the federal Constitution, the system consists of the federal capital (Baghdad); regions; and Governorates composed of a number of districts, subdistricts, and villages (Article 122, first item). Under the Constitution, the Governorates are granted broad administrative and financial authority to manage their affairs based on the principles of decentralized administration (Article 122). The mechanisms of intergovernmental relationships between the regional governments and their component Governorates are to be determined by law. Until this law comes into force, CPA Order 71/2004 is technically still in operation.

114. **Status of foundational laws and regulations.** Various laws and regulations defining intergovernmental arrangements are in the final stages of drafting**.** The basic law stipulated in the Constitution[47] has been drafted but has not yet been tabled in parliament as it is still undergoing discussions and revisions. In September 2006, the law to form regions was passed, essentially delaying the formation of new regions for a period of 18 months from that date. In addition, the draft financial resources law outlining the basis for sharing revenues, as well as the arrangements for collecting and transferring the revenues together with reporting arrangements, was tabled in late June 2007. The law outlines population as the basis for determining the share of Governorates (Article 4) and outlines arrangements for ensuring that the cash needs of the Governorates are met by the MoF. However, this too has yet to be passed and discussions are still ongoing.

***Governors' Offices***

115. The Governor is selected by the Governorate Councils, although this is not yet the case for all Governorates. Governor's office staff are subject to central civil service rules and grades, and range from about 225 employees (An Najaf) to over 600 (Baghdad). Through the 2006 budget year, the operating budget of the Governorates was under the MoMPW. Starting with the 2007 budget year, the budget allocations for the Governor's office are now directly negotiated with the MoF in Baghdad. This move is partly in response to complaints by many Governors of being starved of funds by the MoMPW. At present, the Governors' offices do not collect own-source revenues (save for a limited number of administrative fees), which revert to the central treasury. The latest available draft Governorate law envisions that Governorates are assigned revenues through additional laws. Whereas Governors' offices perform a largely coordinating role of territorial administration, additional functions may be assigned in future.

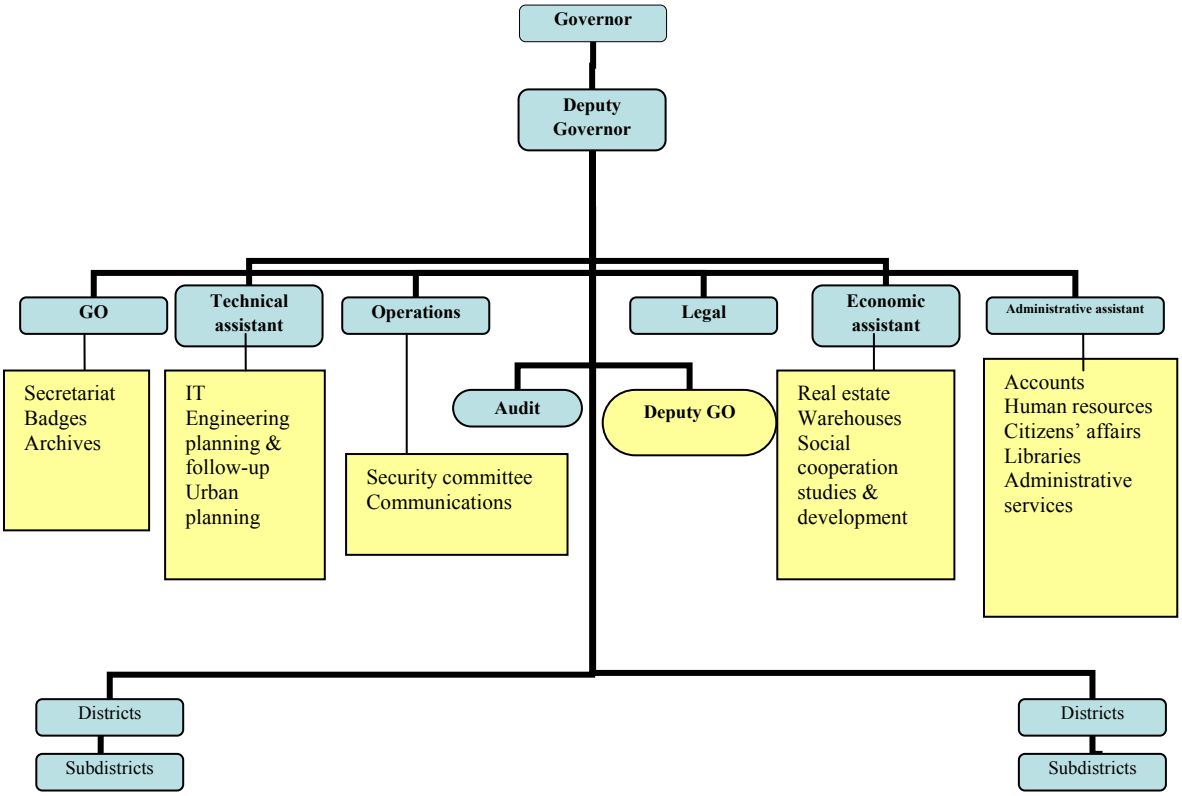
116. The organizational structure of the Governorate Council in Baghdad is somewhat different from that in other Governorates**.** Baghdad's municipal borders are the capital of the Republic of Iraq, and its administrative borders constitute the Governorate of Baghdad (as per Article 142 of the Constitution). The Constitution stipulates that the capital may not merge with a region. The Baghdad Governorate has about 17 sections and subsections (see Figure IV.2). The total number of employees is about 600–650. Baghdad has 10 districts and 22 subdistricts. The municipalities of the districts Rasafa, Karakh, Adhmiyah, Kadhemiyah, First Sadr City, and Second Sadr City (called "Baghdad center") belong to Baghdad Amanat. The municipalities of the districts Abu Ghraib,

[46] See section 5, Chapter II of the Constitution of Iraq.

[47] Article 122, second item: Governorates that are not incorporated in a region shall be granted broad administrative and financial authorities to enable them to manage their affairs in accordance with the principle of decentralized administration, and this shall be regulated by law.

Mahummedhiyah, Tarmiyah, and Mada'an (called the "Baghdad outskirts") belong to the municipalities' directorate of Baghdad.

**Figure IV.2 Organizational Chart of the Baghdad Governorate**




*GO refers to Governors Office*

### *Governorate Councils*

117. Governorate Councils have been elected and established in all Governorates**.** Each province has a 41-member council, except for Baghdad, whose council has 51 members. Governorate Councils cannot hire their own permanent staff, and are expected to rely on the executive structures of the Governors' offices. But they have committees, including for finance and monitoring. The Governor is appointed by the Governorate Council. In fiscal year 2006, the Governors worked with the Governorate Council in the budget-preparation process. But the operating budget request by Governors' offices for 2006 was put forward for consideration by the MoMPW. The draft law confirms that the Governor is to be elected by the GC as are his deputies (see Box IV.4). It provides broad fiscal powers to Governorates but does authorize borrowing. It calls for transparency regarding decisions made and provides approval power over the changes enacted by the lower level. It does not clarify the dispute resolution mechanism if the regulations, decisions enacted by the GC contradict federal laws.

118. **Relations between the Governor and the Governorate Councils and directorates general are statutory and in accordance with CPA Order 71/2004.** Thus the chair of the Governorate Council has the oversight of the Governor and the Governorate Council exercises direct oversight over the directorates general. The Governorate Council can remove the Governor with the approval of

a two-thirds majority of council members. The Governorate Council suggests the names of new directors general when there is a vacancy. The Governorate Council can ask for these directors to be removed if they do not cooperate with the Governorate Council. There were two removals during the last government and one during the current one.

119. **In practice, horizontal relations between the Governor and the directorates general do not always conform to the new laws.** The horizontal relations between the Governor and the directorates general are also statutory and are based on the old Governorates law of 1969 and law on revolutionary councils of 1995. CPA Order 71 split the horizontal relations between the directorates general and the Governorate Councils, and these bodies are still adjusting to changes in the institutional and reporting structure. The degree of adjustment seems to depend on how strong the Governor and the Governorate Councils are in each Governorate. Despite the fact that Order 71 supersedes both the Governorates law and the revolutionary council's law, local authorities refer to these laws in case of gaps. It is reported that in some Governorates, such as Anbar and Salah Ad Din, Order 71 is generally ignored.

120. **Governorate Councils have been authorized by the MoF to appoint staff to implement the duties of oversight and control on investment projects funded via the ARDP.** In response to this some Governorate Councils have set up accounting offices while others (such as Babil, Karbala, An Najaf, and Baghdad) have more complex administrative arrangements as described in the report on management of ARDP funds (USAID/RTI LGP2 2006). In addition, some Governorate Councils have appointed tax collectors (see USAID RGP2). While Governorate Council revenue-raising powers are unclear, some exercise these powers. Many Governorate Councils in the south collect some fees and customs surcharges. The basic taxation powers are also in CPA Order 95, the financial management law and public debt law. The MoF's responsibilities are also explained in that document.

121. **The Governorate Council has the authority to dissolve the district and subdistrict councils and some have already exercised this power.** Relations between the Governorate Council and the district and subdistrict councils are statutory. The Governorate Council can dissolve the district and subdistrict councils, but it cannot reappoint them or call for new elections. Elections are in the ambit of the independent elections commission. While they do coordinate, the Governorate Councils have the power of enforcement under certain conditions and can dissolve these lower-level Councils. Thus far, there have been two dissolutions reported: the Baghdad Governorate Council dissolved the Baghdad city council and, in Dhi Qar, one District Council was dissolved by the Governorate Council. The powers and competencies of the Subdistrict Council are clearly stated under the draft law including which level will prevail in the case of a dispute.

### *Municipal Councils*

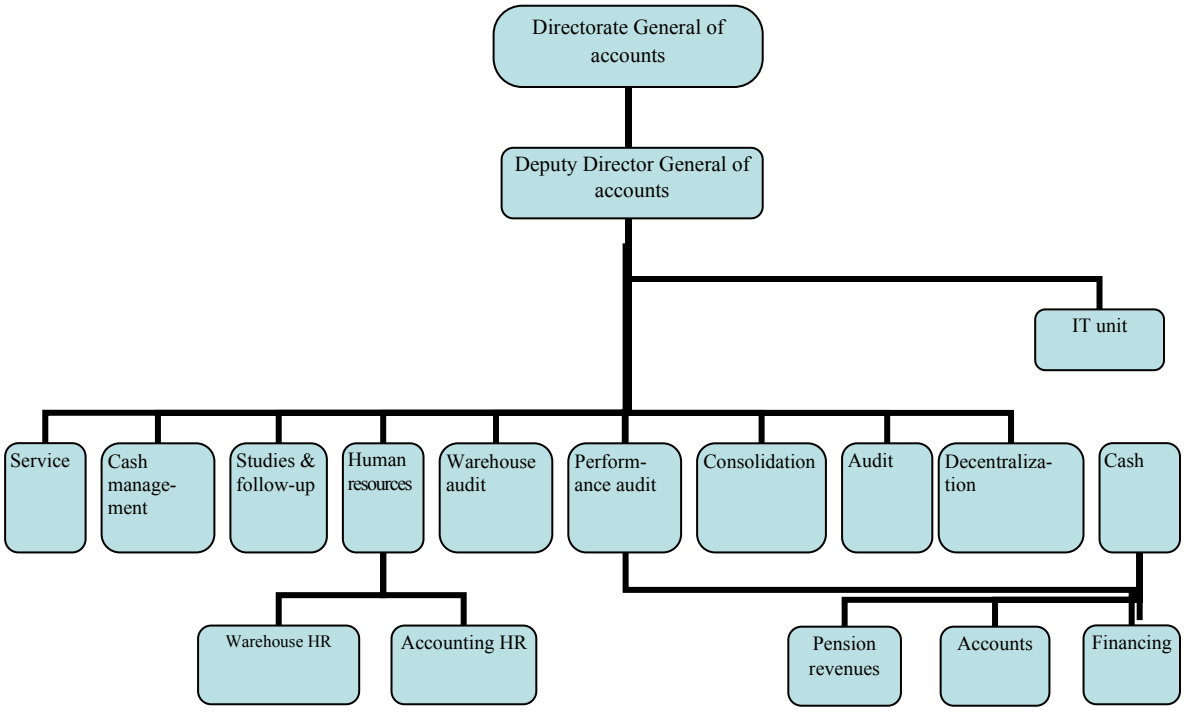
122. **While Governorates in Iraq are subdivided into districts and subdistricts, there are also municipal executive structures *(Amanat)* that carry out executive functions.** Functions include cleaning parks, garbage collection, basic elementary municipal infrastructure, municipal property management, and urban development (permits and so forth). Some ministries, such as the MoF, maintain offices at the district and subdistrict levels. Central funds for the municipalities, or *beladats,* are provided through the MoMPW. The A*manats* also collect direct revenue based on the law of 1963 including fees for licenses and some cadastral assessments. The *beladats* are in effect supervised by the office of the MoMPW in the districts and subdistricts. The employees of the *Amanats* are civil servants. The A*manats* are directed by the mayor, who is accountable to the district councils. The district council has the power to appoint and remove the mayor (based on CPA 71). The Governorate Councils, in turn, have the power to dissolve district councils. On balance, the day-to-day work of the A*manats* seems to be primarily focused on the MoMPW rather than the Governorate Councils.

123. **Governorate Councils have the authority to dissolve the Municipal Councils.** This has been the case in Baghdad and in other Governorates. There was some initial confusion surrounding the relationship between Governorate Councils and Municipal Councils. The former saw Municipal Councils as their executing mechanisms, since one function of the Municipal Councils is to collect bottom-up development planning priorities. While there was some relationship between the Governors' offices and the A*manats*, this was severed in 2007.

***The Ministry of Finance and Governorate Treasury Offices***

124. **The funds for both the devolved and decentralized structures in the Governorates are routed through the Governorate treasuries.** These are overseen by a director reporting to the MoF who acts as Governorate treasurer. The Governorate treasurer reports to the Accounts Directorate in the MoF in Baghdad (Figure IV.3), which employs an estimated 300–350 staff. Funds for Governorate line agency directorates and block grants for Governorate Councils/Governorates are mostly routed via the Central Bank in Baghdad to Governorate treasuries. The MoF employs about 1,000 staff throughout the Governorate. Treasuries are also present at the district and subdistrict levels, with both reporting directly to the director of the Governorate treasury.

**Figure IV.3 Ministry of Finance Accounts, Directorate Organizational Chart**




*Source*: MOF

125. **Each Governorate has a treasury office (GTO) headed by a treasury director who reports directly to the Accounts Directorate in the MoF.** The number of people employed varies from around 70 to 90 and includes accountants; auditors; and IT, administration, archives, cash, supervision, warehouse, receipts, and expenditure staff. There are 18 treasury offices across Iraq. A typical treasury office is organized into the following sections. The director of the treasury usually heads the administration, with the audit director heading the audit department

126. In the next tier after the GTO are the district treasury offices (DTOs) or *Qazaya* treasury offices. These are headed by a director of finance who reports directly to the director of treasury at the GTO. The number of DTOs in each Governorate depends upon the size and volume of transactions in each Governorate. There may be one DTO serving each district. The exact number of DTOs is unknown. Each DTO is organized into cash (safe deposits) and collections (tax).

127. The tier after the DTO consists of the subdistrict treasury offices (SDTOs) or *Nahiya* treasury offices. These mirror the DTOs and are headed by a finance officer who reports directly to the director at the GTO. The number of SDTOs in each Governorate depends upon the size and volume of transactions in each subdistrict. In most cases there are a few SDTOs in any given district. The exact number of SDTOs is unknown. Each SDTO is organized into cash and collections sections.

128. **There is no direct reporting relationship between DTOs, SDTOs, and the MoF.** All staff working in the GTOs, DTOs, and SDTOs are employees of the MoF. They receive salaries from the GTOs in the form of cash/bearer checks. The treasury director in each DTO reports directly to the Accounts Directorate in the MoF. Directors of finance in the DTOs and finance officers in the SDTOs report directly to their respective Governorate treasury director.

129. **All GTO offices are required to provide account details for the preceding month.** These include trial balance, statement of receipt, and expenditure for consolidation into monthly fiscal accounts by the 15th of each month. There appears to be no formal system of preparing or submitting annual reports and accounts at the level of the GTO, DTO, and SDTO to the MoF.

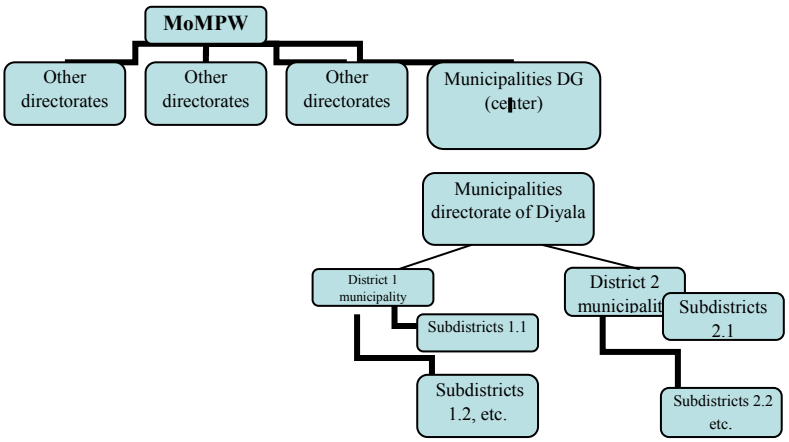
***Line Agencies***

130. **Line agencies tend to be guided by ministerial orders rather than general laws.** Sectoral line agencies typically have a directorate general in each Governorate, with organizational structures and processes set out by a variety of laws and CPA orders. While, in principle, their operation is subject to the provisions on local governmental power under CPA Order 71/2004, line agencies tend to follow ministerial orders relevant to their agencies. Staff of these sectoral line agencies is subject to civil service rules and grades. According to the CPA Order 71, staff appointment and removal can be approved or vetoed by the Governorate Councils. Ministries such as education and health are represented by a director general at the Governorate level, with reporting lines directly to the minister in Baghdad. This may be because of their relatively larger portfolio.

131. **The MoMPW retains special roles in overseeing municipal offices at the district level.** Municipal office (*beladat*) structures at the district and subdistrict office level (Figure IV.4) are responsible for delivering basic urban services. Municipal Councils appear to have some oversight/consultative role in the operation of the MoMPW municipal offices. To date, the MoMPW is represented by a director in the Governorate, with reporting lines to a directorate general in Baghdad. Figure IV.4 sets out the organizational structure of the MOMPW together with an example of how municipalities and municipal districts under them are structured using the example of Diyala. MoMPW Governorate directors also have reporting lines to the Governor. Directorates are centrally financed. Under this arrangement, the Governor is the senior executive chief (direct chief) of municipalities within his or her Governorate. The director of municipalities is the senior financial officer (higher chief) of municipalities within the Governorate and is below the Governor. After 2006, the relationships between the MoMPW and the Governors' offices were reorganized, and appear to have been delinked (in line with the more general delinking of the Governor's office operating budget from the MoMPW). Municipal offices at the districts and subdistrict levels are "self-financed." While municipal offices collect a specified set of revenues, these are apparently collected at the national

treasury. Because they lack sufficient operational and capital funds, they can receive grants for the financing gap from the MoMPW.

**Figure IV.4 Organization of the Ministry of Municipalities and Public Works**




## D. Subnational Financing

132. **The diversity of subnational structures in Iraq's Governorates is accompanied by different patterns of financing.** The primary fiscal flows to Iraq's "devolved" structures in the Governorate are the ARDP funds allocated in 2006. The funds are earmarked for investment purposes (including some residual amounts specified in the regulations for project management). This means that Governorate Councils/Governorates were allocated about IQD 4.5 trillion in ARDP funds for implementation in 2007 (see Annex VI for ARDP Funds allocated by Governorates). In addition, the central budgets have allocated operating expenditures to the Governorate Councils and Governors' offices (that is, the legislative and executive branches).[48] These flows are far smaller than the ARDP allocations in volume (less than 5 percent on an annual basis), but play a vital part in the operations of these institutions. In 2006, total operating expenditures allocated to Governors' offices totaled about US$ 32.1 million. The Governorate Councils were allocated US$ 75.3 million. In contrast ARDP allocations for 2006 amounted to US$ 1.77 billion for Governorates. But 60 percent of these allocations remained unspent and have now been carried over to 2007. In addition, line agencies in the Governorates (for education, health, and so on) also receive operating and investment allocations through their respective ministries.

133. **The method of allocating funds for Governorates changed significantly in 2007 when compared to 2006.** In 2006, funds appeared under transfers in the MoF budget, whereas in 2007 they are shown as a separate administrative line item like that of any other line ministry. Table IV.2 summarizes the main arrangements and flow of funds to the main entities at the subnational level. Since 2005, Governorate Councils have received some operating expenditures (following their 2005 election). ARDP funds were first allocated to them in 2006, although the implementation processes changed in 2006 and 2007.[49] While the Ministry of Planning still plays an important role in the implementation of these funds in that all ARDP allocations are submitted to MOPDC, the Governors'

[48] Whether or not these allocations also include the funds for the Municipal Councils is yet to be confirmed.

[49] As noted in Chapter II, in 2006, the Governorates in Kurdistan received only development funds. In 2007, Kurdistan Governorates are projected to receive a share of the overall pool, that is, development and reconstruction funds. In Kurdistan, however, these funds are channeled via regional government structures.

offices now play a larger role (with the Governorate Councils setting priorities and monitoring). The MoMPW, meanwhile, retains an oversight role in municipal offices. Line agencies are, in turn, differentiated by those that operate through the provincial treasuries versus those that operate through their own national structures in terms of implementing the flow of funds (such as for agriculture).

**Box IV.2 Decentralized Operation and Development Allocations**

| | Governorate Councils | Governors' offices/municipal offices | Ministry of Municipalities and Public Works (MoMPW) | Line agencies |
|---|---|---|---|---|
| 2005 | Receive limited operational money through MoMPW | Operational through MoMPW | Self-funding ministry through municipal/Governor's office revenue collection, plus transfers through MoF Governorate treasuries | Central/decentralized/state-owned enterprises<br><br>Some, such as agriculture, do not interact with MoF Governorate treasury<br><br>Education and health are decentralized and have own revenues |
| 2006 | MoF allocation for operations through MoF plus ARDP funds for development and reconstruction, with latter classified as transfers | Operational through MoMPW | | Governorate Councils can change line agency investment plans (within set budget limits), with 2/3 supermajority. Not clear to what extent this has occurred in practice |
| 2007 | For operations, MoF allocation of ARDP funds, classified as investment budgets for non–line agency entities | Operational through MoF;<br>Governor's office potential has greater execution autonomy over ARDP funds | MoMPW no longer directly responsible for Governors' offices, but still appears to incorporate/fund municipal offices | |
| 2008 | Governorate development strategies should integrate GC and line agency capital budgets in annual federal budgets | | | |

### *Governorate Councils*

134. **As of 2006, ARDP funds flowed to bank accounts in the name of the Governorate Councils (opened by the Governorate treasurer).** As of September 2006, 40 percent was disbursed and distributed. The remaining balance was transferred to Governorate treasuries, and in some cases, to Governorate Councils and Governorates in the middle of December 2006. MoF's 2006 instructions also allow for the allocation of some ARDP funds for recurrent use (about 2 percent). While this

contravenes the financial management law (FML), the carry-forward was approved in the annual budget law (2007).[50]

135. **Governors' offices collect own-revenues from stamp and rental fees.** It is estimated that these revenues meet less than 5 percent of their annual operating budget. These revenues are deposited in the same accounts used for treasury financing. Governors' offices report their self-revenues and cash balances to the MoF Accounts Directorate on a monthly basis.

### *Mayoral Councils and Municipal Offices*

136. **The Municipal offices are funded through the MoMPW.** They also collect self-revenues from a number of resources, notably real estate. Article 19 of the 2007 budget provides for the ability of the MoMPW to "to reallocate budgetary funds of a self-funding municipality to execute needed services." In effect, the MoMPW appears to provide bottom-up funding to municipal offices where funds are insufficient, but can also control these.

### *Financing of Line Agencies*

137. **Governorate level offices of the central line agencies (for education, health, and water and sanitation, and so on) are financed directly from their central ministries.** This breakdown is not provided in the overall budget. This amount varies across governorates. Reports suggest that Governorate Councils in some Governorates may have significant sway in terms of how these resources are spent.[51]

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[50] Budget Law 2007, Article 13. The MoF may transfer unspent funds of 2006 federal budget appropriations allocated for the regional and provisional reconstruction and development and rehabilitation marshes to the recipient solely to spend them during 2007 to complete their projects in exception of the provisions of section four (paragraph one) of the financial management law (i.e. Annex A of CPA/ORD/ 2 June 2004/95).

[51] Human resource/hiring decisions are effectively made at the provincial level, but are financed by central transfers. This raises the question of how, if at all, hard-budget constraints are being set for payroll expenditures at the subnational level. Alternatively, the payroll envelopes for individual Governorate Governorates /agencies may also be part of a process of discretionary bargaining between the center and subnational officials/politicians.

# V. PUBLIC FINANCIAL MANAGEMENT IN IRAQ'S GOVERNORATES

138. The previous chapter described the structures and main financing sources of Governors' offices, Governorate Councils, line agency directorates, Municipal Councils, and Municipal offices. This chapter focuses on the quality of PFM processes related to (i) allocations under the Accelerated Reconstruction and Development Program (ARDP), (ii) investment expenditures by line agencies, and (iii) operating expenditures by both line agencies and Governors' offices. In this context, line agencies also differ as to whether they operate through the Governorate Treasury Office (GTO) of the Ministry of Finance (MoF) (e.g., education, health) or not (e.g., agriculture). Unlike in Kurdistan, where the region does produce a single annual budget and is endeavoring to consolidate PFM processes into an integrated regional structure, a number of parallel (if linked) processes occur in the other Governorates. Therefore, we do not attempt to rate performance using the individual high-level indicators of the public expenditure and financial accountability (PEFA) framework. Rather, the PEFA framework is used to structure a *qualitative* discussion of the various subnational PFM processes, including their observed variations across Governorates. Annex II lists all the indicators with observations about the key dimensions of the indicators.

## A. Credibility of Subnational Budgets

139. **Overall budget credibility in 2005/06, especially for investment expenditures, has been weak.** Only 40 percent of ARDP funds were implemented by the Governorates in 2006, before being carried over to the 2007 budget year. In part, this may have been due to the prevailing security situation. More generally, however, unfamiliarity with new procedures and unclear roles and responsibilities (e.g., within the ministries of finance and planning, and between line agencies) must be addressed to improve performance in this area. Detailed information on sectoral composition of budgets was not available. Overall Iraq remains highly dependent on oil for revenues, a fact mirrored by the dependence of all provincial entities on central government transfers. "Self-funding" municipal offices/councils receive earmarked funds from real estate taxes. But data on outturns of these subnational revenues were not available. Significant payment arrears were reported.

## B. Comprehensiveness and Transparency

140. **The PFM process is deficient in several areas related to comprehensiveness and transparency.** A new chart of accounts, based on the GFS template, was introduced in 2007 because the existing one was not adequate in its coverage. The new chart is applicable to line agency directorates, Governors' offices, and Governorate Councils. Intergovernmental relations within governorates (relations between Municipal Councils and Municipal offices, for example) remain subject to clarification. In the Municipal offices, Iraq has a tradition of "self-financing" entities at the local level. These still appear to be subject to the Ministry of Municipalities and Public Works and Governors' offices, however, so the precise degree of autonomy, predictability, and transparency of transfers to this third tier is not clear. The federal budget does itemize detailed ARDP allocations to subgovernorate levels.

## C. The Budget Cycle at the Decentralized Level

### *Budgeting and Planning Processes at the Governorate Level*

141. **The Governorate budget process is part of the federal budget process.** Budget allocations for Governors' offices, Governorate Councils, and the line agency directorates are supposed to be prepared simultaneously, under instructions issued by the MoF and the budget request sent to the

ministry (Table V.2). Budget preparation is guided by the Financial Management Law (articles 1 and 2, section 6), which sets out the overall framework for budget preparation (see Annex VIII for relevant sections of the FML as they apply to subnational governments). Instructions for budget preparation include items that fit the general framework and specify how each line ministry should provide a request. Details about the budget calendar are also provided.

**Box V.1 Understanding the Ministry of Finance's Budget Circular**

The MoF's annual budget circular is sent to centrally financed agencies and ministries and to self-financed agencies that have insufficient funds, including SOEs, municipalities, some hospitals, and the agricultural directorate. The instructions specify that the proposed budget of the agency should take into account unexpected circumstances that will affect the budget of the year in question, reflecting the priorities that have been determined for the year. For 2007 these priorities included security; building minimum capacity; and developing plans to conduct economic activities to raise revenues, reduce employment, and improve the environment.

The circular outlines the steps to take to reach reasonable estimations (for ministries and independent agencies). Specified steps include (i) transparency; (ii) adding new projects only when necessary; (iii) concentrating on completing current projects; (iv) stressing execution of projects by local contractors and involving foreign contractors only if necessary; (v) ensuring that new projects comply with economic assessments as laid out in Order 1 for 1984, taking into consideration environmental effects; (vi) reducing hiring of government staff; (vii) curbing extra budgetary bonuses; (viii) ensuring that investment plans comply with the regulations issued by the MoF and sending these plans directly to MoPDC, (ix) avoiding mixing up current and investment; (x) encouraging private sector participation; (xi) listing all executed projects whether centrally financed or self-financed or from donors; and (xii) ensuring that the ministry's request includes the needs of all directorates, the amounts of the contracts and commitments they will enter into. Independent estimates for each section and subsections must be provided, with enough justification to facilitate reaching reasonable estimates.

The circular sets forth the following procedure. It requires that each ministry (or directorate or agency not affiliated with a ministry) form a high committee headed by a deputy, minister, or director to discuss the budget estimates proposed by the units under its purview. It also specifies that a committee on the level of each directorate in each ministry (or independent agencies headed by a director) be established including the director of finance, accounting, internal audit, and human resources, as well as the director of each section responsible for preparing a budget. Moreover the internal audit section should thereafter check the budget that is prepared to check its accuracy.

142. **The federal budget preparation process however is in transition.** The budget circular (see Box V.1) for 2007 had to be revised due to the changes to the classification system. The budget was approved after the start of the fiscal year. At this current juncture, the budget lacks a multiyear perspective in that no forward estimates of fiscal aggregates are prepared by the MoF. Moreover, the sectors do not have costed sectors strategies. The linkages between Governorate budgets and the sectors are weak. Operating and investment budgets are planned separately.

143. **The Financial Management and Public Debt Law (CPA 95) unified the operational and capital budgets.** Authority for executing the federal budget lies with the Minister of Finance, who may consult with the Ministry of Planning and Development Cooperation (MoPDC) about the capital budget. But under the law the MoF has been made responsible for preparing the capital budget and distributing allocations on the listed projects, while approving changes to the projects within the year. The law does not mention the powers or responsibilities of the Ministry of Planning and Development Cooperation regarding the preparation of the capital budget.

144. **Budget preparation is divided into separate processes for the operating and capital budgets.** Notwithstanding the specificities of the FML, institutionally, the MoF prepares the operating budget. MoPDC (along with line ministries) undertakes the responsibility for preparing the capital budget which is then proposed to MoF for approval. In 2007 ARDP allocations at the Governorate level were made on the basis of a simple population formula. However, ARDP-funded projects in the Governorates must be described in a list to the MoF and the MoPDC. Nevertheless the

allocations were not linked to the list but rather determined on the basis of population and on the size of the allocation made in the previous budget as would be in a system based on fiscal transfers (unlike the process followed in the sector ministries).

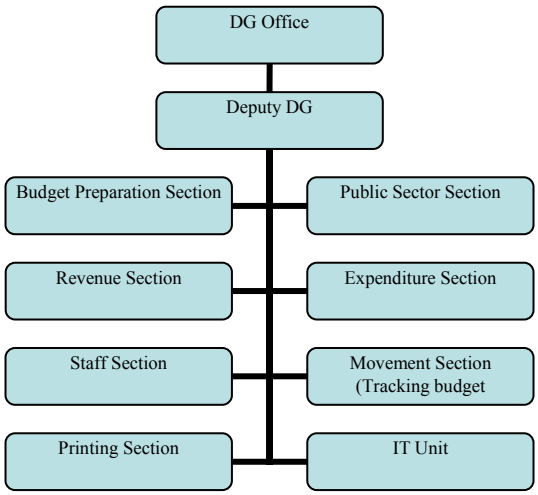
145. **The process for preparing Governorate budgets differed in 2007 from the previous year.** The Governors and directorates general of line ministries prepared the budget request, and, in most Governorates, the Governorate Council approved these budget requests between May and September 2006. The Council of Representatives approved the budget, and the MoF made allocations to Governorates and central administrations. Thus the projects that reach directorates general have already been allocated in the budget and approved by the line ministry (See Annex IX for the budget timeline).

***Operating Budget***

146. **The budget preparation exercise begins with the issuance of the budget call circular (BCC).** The MoF issues the BCC to line ministries (and other departments under them), as well as to the Governors' offices. Since the Governorate Councils do not employ their own staff, they are not involved in requests for the operating budgets. The BCC contains instructions and forms to be used in preparing and submitting budget requests. The finance department in line ministries receives the BCC and sends it to all spending units that fall under that ministry (e.g., the directorate general of education in a given province). The MoF issues BCCs to all ministries and agencies, and subnational governments that are centrally financed—that is, Governors' offices (as of 2007), Governorate Councils, and the Kurdistan Regional Government (KRG). More details on the BCC are provided inbox V.1.

147. **Budgeting is largely incremental.** The finance and account departments in each spending unit are responsible for developing budget estimates. To arrive at estimates of next year's budget several principles are used. One is to compute the actual expenditure for the first six months, which is then added to actual expenses for the last six months of the previous year. Another formula is to compute actual expenditure for the first six months and then project the same for the next six months. In either case, the estimation process remains incremental.

**Figure V.1 Organization of the Budget Directorate, Ministry of Finance**



148. Once the spending unit has prepared its budget, it forwards it to the line ministry, which in turn compiles the budgets and sends them to the Budget Directorate in the MoF for discussion and approval (see Figure V.1 for the organization of the budget directorate itself). But certain spending units send their budgets straight to the MoF Budget Directorate, rather than to their respective line ministries. On receiving the budget requests, the MoF Budget Directorate checks them for discrepancies. The Budget Directorate has employees designated for each ministry, who provide a report to each ministry's budget directorate. (The MoF Budget Directorate employs 70 to 80 people, with each section having an average of 8 to 9 employees.) This report is then used during negotiations with line ministries. The MoF Budget Directorate asks detailed questions about the previous year's spending—including the rate of spending through the year, especially if it is unusual (if, for example, the total budget is spent in the first five months of the year or if none is spent in the first three months). Each agency's achievement percentage is carefully scrutinized. The MoF Budget Directorate provides agencies such as the Governors' offices with a budget notification sometime in late summer prior to the budget year.

149. In the 2007 budget process, the operating budgets of Governors' offices were subject to the same process used for other spending agencies although this had not been the case before. In August 2006, however, the Governors' offices received a form requesting them to provide estimated realizations for 2005, as well as the budget for 2006 and mid-year realizations through June 30. The Governors' offices were then asked to enter an estimated amount of need for the following year. These appear to have been completed largely on an incremental basis. The Governors' offices subsequently discussed these estimates with the budget committees in Baghdad. About November 2006, they were informed of their notional annual budgets by chapters. Collections of self-generated revenue are part of this budget and are considered as part of the cash released to the Governors' offices in the course of the year.

150. **Budget ceilings are not included in the BCC, but most agencies are given an approximate budget estimate during negotiations.** Salaries and wages are separated in the budget forms. The staff section examines salaries and wages to see what posts have been added or removed, how many staff members were promoted, how many quit the service, and how many retired. A report is prepared on proposed changes in staff numbers. Final decisions regarding increases (or reductions) are left to the MoF. The MoF Budget Directorate examines the rest of the recurrent budget. Its staff prepares notes on the issues it intends to discuss with spending units in the ministries and agencies.

***Capital Budget***

151. **In practice, MoPDC has principal authority over the capital budget, although with an important role for the MoF.** A separate Budget Call Circular for the capital budget is sent in July to all line ministries, departments, Governorate Councils, and agencies at all level. It includes forms and instructions to be followed in preparing budget estimates. Line ministries develop their estimate using the BCC and send them to the MoPDC for approvals. In the past, requests from the Governorates would be consolidated into the line ministry budget before being sent to MoPDC. This process is undergoing changes. See Annex X for a detailed summary of the capital budget process.

152. **The capital budget is divided into six sectors:** (1) agriculture; (2) construction, housing, and services; (3) economic planning; (4) industrial planning; (5) communication; and (6) transport. Once the capital budget proposals are received from ministries and all agencies they are sent to the respective directorates in the MoPDC for analysis and discussion. Ministries that provide services such as health and education interact mostly with the directorate for construction, housing and services, since their capital budget requests deal largely with building schools, health centers, and hospitals. Ministries such as agriculture and water resources, by contrast, interact with the agricultural

directorate. Projects that include more than one component, such as building a dam, interact with both the industrial directorate and the agricultural directorate, thus allowing supervision of the project by technical experts who can assess the separate components according to their expertise.

153. Ministries submit their project proposals, together with cost and feasibility studies, by September. The budget preparation is overseen by the planning directorate in each ministry. Technical and financial experts in each directorate analyze the proposals and discuss them with the concerned line ministry over the next three months. The total budget for each ministry, including ongoing and proposed projects, is finalized between the two ministers. The capital budget is sent to the cabinet for approval at the same time as the operational budget, but the two are discussed separately. Not all projects are approved—those deemed to be of lower priority are postponed.

154. When preparing their 2007 budget, all spending units including those at the Governorate level were required to provide the following information on compact disc.

- 2005 actuals as signed by the Board of Supreme Audit (BSA).
- The approved and revised budget for 2006 (to be checked by the section of the Budget Directorate that tracks changes)
- Actual expenditures through June 2006 (this is not checked—just accepted).
- Proposed spending.
- Staffing numbers.

**Box V.2 Challenges in Executing the Capital Budget**

In the past three years only a small share of the capital budget has been spent. The shortfall can be traced to several causes:

*Project preparation and administration*

• Some ministries include projects in their capital budget without preparing appropriate sites (land) in advance. This results in delays in turning the projects over to contractors for execution. On occasion sites designated for projects are occupied and must be vacated, which can take time. Conflicts over the ownership of lands and buildings may arise between ministries and government departments.

• Project managers have limited authority. Implementation is often slowed by delays in decision making in the line ministry. Further delays arise because of differences between the contractor and owner. Sometimes, this is because contracts are insufficiently detailed and specific.

• Some executive departments are not committed to the regulations. Others have very low capacity for execution. Some ministries fail to follow project timetables. No procedure exists for resolving such delays.

• There are no precise estimates of the total annual allocations for some departments, which leads to many amendments in the course of project implementation. Once begun, projects may not be adequately funded in future years, thus delaying execution.

*Technical matters*

• Qualified engineers are in short supply. Few specialized companies have the technical expertise and experience to execute projects. Even fewer are sufficiently committed to quality control and high technical standards.

• Guidelines for preparing project plans and descriptions are lacking, giving rise to ad hoc amendments and modifications—which tend to raise project costs.

• Background studies and designs are poorly prepared, leading to delays while design mistakes are corrected. Designs are often changed as work orders are modified.

• Machinery and equipment are scarce. The concentration of tenders within a very short period leads to competition for existing equipment thus raises rental prices.

*Financial matters*

• Prices of materials tend to rise in the course of the project, which often affects the ability of the contractor to continue work on the project. Labor costs continue to rise.

• Contractors are inefficient.

• Payments to contractors are often delayed.

*Security*

• The volatile security situation slows project implementation. Projects often are brought to a halt by threats to employees, kidnapping, or sabotage.

• Outsiders intervene in project related matters slowing down the work and therefore delaying project implementation.

*Source:* Ministry of Planning and Development Cooperation.

155. Spending units have a week to prepare their submission following the distribution of forms. Although this is not specified in the budget circular, submissions may be 10 percent higher than in the forecasted budget.

**Box V.3 Budget Execution and Conflicts among Levels of Government**

*Conflicts between ministries and Governorates*
With decentralization, some responsibility for preparing and executing development programs has been transferred from national ministries to the Governorates, thus requiring the Governorates to participate in identifying priorities, planning projects, and administering resources (whether from the budget, grants, or loans). To implement projects, ministries have established regional development programs, which have caused conflicts among central ministries, Governorates, and provincial councils. As a result, projects have been selected without consultation with the line ministries. As a result Governorate Councils have selected projects of national scope in sectors such as oil, electricity, industry, and highways. Such projects should fall within the purview of the national government and line ministries.

*Between Governorates and Governorate Councils*
In execution of the regional development program for 2006, the Ministry of Finance issued various instructions and special authorizations. Spending authority was given to the head of the Governorate Council and the Governor. The ministry later issued other instructions conferring authority on the Governor, thus creating confusion and conflict between the Governors and heads of Governorate Councils. The conflicts delayed project launches, with the result that most budgeted funds remained unspent by the Governorate Councils. Differences persist over the locus of authority in many matters, even though the Government's General Law of the Budget for 2007 defined the tasks and authorities of each party (Chapter III, Article 3). Under that law, the Governor has the authority to execute the construction plan, while the Governorate Council is responsible for monitoring project execution.

### *Predictability and Control in Budget Execution*

156. **The Annual Budget Law passed by the Council of Representatives empowers the MoF to issue budget execution guidelines and instructions to all spending units, including the Governorates.** The budget cannot be implemented until the MoF issues these instructions. The instructions are fairly detailed, covering (i) treatment of income and expenditure; (ii) procurement authority (contracting limits) (iii) contract awards; (iv) cancellation of debts; (v) transfers; (vi) financial violations; (vii) capital expenditures; (viii) maintenance of inventories; and (ix) the scope of authority of ministers and heads of independent agencies. However, these instructions do not provide guidance to budget and accounting officers about who has authority or jurisdiction in executing these instructions and at which point in the execution process these regulations should be followed. A large part of the prescribed instructions describes general assignments of financial powers and limits, procurement and staffing procedures. Moreover, it is unclear to what extent these rules are observed. In any event, there are other, competing regulations and laws. For example, in 2007, rules dating from 1973 on decentralization of financial management functions were applied in procurement matters.

157. **At the Governorate level, the primary responsibility for budget execution rests with the GTOs.** The overall treasury function, however, is performed and managed by the Accounts Directorate in the MoF in Baghdad. Treasuries managed by the Accounts Directorate represent the MoF at the subnational level while also serving the Governorates and other spending units that fall under their jurisdiction. The structure of the Governorate, district, and subdistrict treasury offices is described below. The following paragraphs outline the cash-flow process of both the centralized and decentralized spending units. Spending units at the subnational level can be divided into two broad categories, (i) those that are funded directly from Baghdad (such as agriculture and the universities), and (ii) those that function through GTOs.

**Box V.4 Dhi Qar's Experience with the Investment Budget in 2006**

In 2006, the Dhi Qar Governorate received ID 248 billion in investment funds. Of the total, ID 96 billion was intended for building and construction, ID 83 billion for other regional development, and ID 69 to revive and protect marshlands.

The Governorate formed a task force, headed by the Governor, to manage construction. Other members were the technical assistant, director of planning, director of follow up, director of accounts, director of legal affairs, and directors from various sectors and ministries. The task force met regularly to discuss achievements, obstacles, challenges, and solutions. It forward despite delays in the allocation of funds and in the issuance of regulations, and problems deriving from overlap in the authority of the Governorate Council and the Governor. Delays consumed the first five months of the year, as issues were resolved by the Council of Ministers.

By the end of 2006, Dhi Qar had spent only ID 96 billion, just 38 percent of its investment budget.

The main problems were as follows: in Dhi Qar, as elsewhere, the local government could not commit itself financially to projects with a time ceiling of more than one budget year. Under a resolution of the Council of Ministers, funds not spent by the end of the budget year could not be carried forward. Allocations therefore were concentrated on those projects that could be most quickly achieved rather than those of highest priority. Outcomes were not immediate, and the citizens of the Governorate did not feel their impact immediately and clearly.

As an extraordinary measure, unspent funds from 2006 were transferred to the Governorates in 2007 to help them finish their projects, but issues of capacity remain. For example, because of the Governorate's lack of experience with planning and executing investment budgets, project planning often did not take operating expenses into account. Consequently, new schools and clinics were left without furniture or personnel. Furthermore, few companies were qualified, financially and technically, to bid on the projects advertised. The shortage of qualified firms remains a basic obstacle in the current year (2007).

There was incompatibility between the authorities given to the Governorates and the volume of work and the level of allocated funds for regional development.

No serious effort was made to improve the capacities of engineering and accounting staff to achieve the tasks assigned to them. As a result, although the Ministry of Finance allocated investment funds to the Governorate, the Governorate lacked the capacity to perform the full range of tasks covered by the allocation.

*Source:* Presentation of Jabbar Hussein Ali, Senior Director of the Department of Accounts and Budget, Governorate of Dhi Qar at World Bank Workshop on Subnational Budgeting in Iraq, Beirut, April 2007.

### *Directly Funded Spending Units*

158. **The first category of spending units receives bank transfers directly from the MoF Accounts Directorate in Baghdad.** There are approximately 400 such units spread across Iraq in various sectors—among which are agriculture, the universities, electricity, the environment, and trade. All such units maintain a bank account at the Rashid / Rafidain Bank that can be accessed only after the prior approval of the Accounts Directorate.

159. At the outset of each fiscal year the spending units send a memo requesting a funds release to the Accounts Directorate, along with standard documentation that includes a trial balance, a statement of receipts, a statement of expenditures, and a certified bank statement. A standard form is used by spending units when submitting such requests. The Accounts Directorate sends the request to the Cash Section, where it is broken down into three parts, the first of which is completed by the Cash Section. The Cash Section records allocations (broken down into salary, nonsalary, and capital), previous funds drawn, and remaining balance (presumably the budget balance). The request form then moves to the Decentralized Section, which records the latest trial balance and other details. Thereafter

the request is sent to the Audit Section, which performs checks and procedures and vets the work of the previous two sections. Once the request has passed through this process, the Accounts Directorate issues instructions to the Central Bank of Iraq (CBI) to transfer the funds to the bank account of the spending unit. The Accounts Directorate also sends a copy of the spending unit's original funding request to the line ministry.

160. There appears to be no formal monthly reconciliation process between these centralized spending units and the Accounts Directorate. Among the records, however, an appropriation card is maintained. That card records budgeted and actual figures.

***Funds through GTOs***

161. **Some decentralized spending units draw their funds from the GTOs through bank transfers**. All spending units relating to the Ministry of Health, Ministry of Education, Ministry of Water Resources, and Governors' offices receive some funds through the GTO. They maintain a bank account (or, in certain cases, separate accounts for the operating and investment budgets) for the purpose of receiving transfers. These entities can draw only certain types of budgeted funds from the GTOs (Table V.3). The ARDP program is also channeled through the GTOs.

**Table V.1 Spending through Governorate Treasury Offices**

| Sector | Salary | Nonsalary | Investment | ARDP |
|---|---|---|---|---|
| Health | Yes | Yes | Yes | Through line ministry / MoF |
| Education | Yes | Yes | Directly from Baghdad | Through line ministry / MoF |
| Water Resources | Yes | Yes | Directly from Baghdad | Through line ministry / MoF |
| Governorates | Yes | Yes | Yes | Yes |

At the start of each year, the GTOs receive copies of the budgets of entities under their jurisdiction. The spending units draw from the GTO as follows. The head of the department writes a memo (on an official form) requesting a draw against the budget. The details of the request are broken down by salary, nonsalary (by economic classification/ chapters), and investment category (as the case may be). The request also includes a statement of receipts, statement of expenditures, and a certified bank statement, among other details.

- Once the request is received it is checked against the budget and against the unit's bank statements.
- If the documents are in order, the GTO's director signs a fund transfer letter requesting the Rashid / Rafidain Bank to transfer funds to the entity's account.

162. These spending units are not subjected to an extensive internal check and review, as are those that receive their transfers directly from the MoF in Baghdad. At the end of each month they are required to provide a trial balance, statement of receipts, expenditures, security deposits, and loans. They do an overall appropriation check between salaries and nonsalaries and then consolidate them into overall accounts. The GTO does not exercise control over reappropriations between salary and nonsalary expenditures or reappropriations within nonsalary expenditures.

163. Public services, such as hospitals, health centers, and schools, draw their funds through the accounts offices of the Health Directorate. In some instances they also maintain independent bank accounts. The details of financial management at schools, hospitals, and health centers remain unclear. In certain cases they maintain their own set of books and accounts; in other cases the books are maintained by centralized directorates of the MoF.

164. **Other spending units receive funds from the GTOs in the form of checks.** All entities other than those falling under the Ministry of Health, Ministry of Education, Ministry of Water Resources, and Governors' offices receive funds from the GTO in the form of checks (like standard treasury operations) In most cases these spending units also maintain bank accounts for making budgetary expenditures. These spending units are allowed to draw both salary, nonsalary, and investment funds against budget allocation.

165. At the start of each year GTOs receive copies of the budgets of entities that use this regime of payments. To make a draw against its budget, the head of the spending unit writes a memo (on an official form) to the GTO director. The request must be broken down by salary, nonsalary (by economic classification), and investment category (if applicable). The GTO director then issues instructions for a comprehensive review by the GTO's accounts and audit sections. A check is then prepared and signed by three people in the GTO, including the director.

166. The GTOs perform a comprehensive check against all requests received, which includes monitoring reappropriations. It is still unclear how authorizations for reappropriations are managed.

167. **All GTOs are funded by the MoF Accounts Directorate through the CBI.** The CBI maintains an account for each GTO. Each GTO, in turn, maintains a single bank account at the Rashid / Raffidain Bank (acting on behalf of the CBI). The funds in this bank account are transferred from the Accounts Directorate and used to fund spending units in the Governorates. GTOs' bank accounts are used only to make payments, whereas those of the district treasury offices (DTOs) and subdistrict treasury offices (SDTOs) are maintained for receiving payments. The bank accounts maintained at DTOs and in certain cases SDTOs are in the name of the GTOs. Cash can be deposited but not withdrawn.

168. Whenever, funds are required (typically at the end of the month) the GTO director submits a trial balance, statement of revenues, statement of security deposits and trust funds, statement of expenses, and a certified bank statement to the Accounts Directorate in the MoF. The submitted documents are sent to the Treasury Audit Section of the Accounts Directorate for examination, after which payment is made by bank transfer through the CBI. Once the process is complete, the documents are sent to the Consolidation Section of the Accounts Directorate for integration into fiscal accounts.

169. Payment authorizations up to ID 500 million are signed by the assistant director of the Accounts Directorate. Payments in excess of ID 500 million are signed by the director general. Payments are made by the 15th of each month.

170. **The role of the DTO is limited to collection of receipts—for example, real estate taxes, court fees, rent on public property, fines, and stamp fees.** Most DTOs maintain a bank account in the GTO's name. In most cases, citizens deposit money into the bank account, which issues three receipt copies. The first copy is retained by the person depositing the money; the two other copies are submitted to the authorities responsible for collecting money. One receipt finds its way to the DTO. In very limited cases the DTOs collect cash, which is kept in safe deposit boxes. At the end of each month, DTOs prepare a statement of expenditures attach copies of receipts, and send the statement to the GTO. The GoI requires that all security deposits and trust funds that go unclaimed after five years to be treated as government revenue. The revenue collection functions of the SDTOs resemble those of the DTOs but are lower in volume.

171. Municipalities are self-financing spending units that generate funds to meet their spending needs. In the past they obtained funds through checks issued by the national treasury. They now

appear to be more autonomous. Municipalities rely on Baghdad to make up their deficits, after review and approval by the Ministry of Municipalities and Public Works. District municipal offices and subdistrict offices obtain funds directly from the Municipality Directorates in the Ministry of Municipalities and Public Works (MoMPW), under whose jurisdiction they have been since 2006.

172. **Predictability and availability of funds at the subnational level are hampered by budgets not being released on time from the Ministry of Finance and thereafter the treasuries.** Information on the availability of funds is not available to subnational units or agencies. The budget is generally not released on time. In December 2006 allocations were provided in contravention of the FML law. However, this is partly due to the cash-flow forecasts not being prepared by the treasury partially due to lack of forecasts of cash inflows and outflows. (See Annex II PI-16 and 17) Individual spending units at the subnational level as with all other levels do not out together commitment plans in part due to problems with procurement rules and regulations (see following paragraphs). Annex XI shows the financial flows of entities funded through the GTOs and those funded directly through the MOF.

***Procurement***

173. **The major issue facing public procurement is the current uncertainty of public procurement laws and regulations.** Procurement procedures have a number of features that are not in line with generally accepted standards of sound practice. These range from inadequate requirements for registration of suppliers and contractors and absence of adequate national bidding documents to insufficiently transparent bid submission, opening and evaluation procedures, and contract award procedures as well as lack of effective bid protest mechanisms and publicity on contract awards (See Annex II PI-19 for a more comprehensive list). While new regulations are being issued – they still have major shortcomings. All of the above effect quality and transparency of the procurement regulatory framework in terms of establishing the use of open and fair competition and value for money.

174. Procurement is managed by the Governor's office through a committee that includes representatives of both the Governorate Council and the Governor's office**.** Current procurement procedures follow the law of 1973, the terms of which are very general. The MoPDC issues regulations interpreting the law. The first set of regulations, which dates from 1973, was updated and expanded in 1995 and in 2005. The Coalition Provisional Authority (CPA) issued replacement regulations (CPA Order 87), but the Iraqi authorities have shown no signs of intending to implement it. One sticking point is the independent organism for handling tenders and contracts called for in the CPA rules. Another is the requirement that companies must be registered in a particular way, which some believe restricts competition to incumbent contractors. The MoF and MoPDC issued a new set of so-called "unified instructions" last December. The project is being implemented by an accountant from the Governor's offices.[52]

175. Once contracts for projects are signed, the agency asks the MoPDC to send the request to the MoF for release of funds. The High Tender Committee then must ratify the contract. According to guidelines for contract performance signed by the Secretariat for Economic Affairs, the committee is respond to ministerial requests for payment within three weeks. If a response is not forthcoming

[52] The World Bank has been working with the Iraqi authorities to update the procurement law (World Bank OPR 2006).

within that period, the request is automatically approved and sent to MoPDC for vetting.[53] The request is then handed over to the MoF, whereupon a line of credit is opened in the amount requested. Problems have been reported in the issuance of letters of credit and in the use of Iraq Trade Bank for international transactions.

***Internal Control***

176. **In order for an internal control system to be effective, procedures should be clear, predictable, and standardized—which is not the case in Iraq.** As the previous sections illustrate, the guidelines and instructions provided to officials are not clear, roles and responsibilities overlap, and there is no clear separation of duties in handling expenditures and managing resources.

177. **The overall control environment at all levels of government in Iraq is weak.** The lack of accountability and weak control systems are due to a combination of factors relating to (i) the existing political realities on the ground (political capture and the lack of security and adequate reporting); (ii) unclear or poor systems; (iii) the absence of systemized transaction recording procedures and a lack of capacity; and (iv) a confusing array of new and old laws, systems, and procedures. For example, the lack of a budget classification system in the past made it difficult if not impossible to track expenditure within such poorly defined fields. This is being addressed by the new system being used for the 2007–08 budget. Similarly, uncertainty about the procurement law and regulations, the criminal law's revolutionary command provisions on corruption, and the obligation of the Commission on Public Integrity (CPI) to investigate alleged abuses to determine whether the alleged act of misconduct did or did not occur, has meant that decision makers are faced with a variety of actors with overlapping jurisdictions regarding control of corruption. This has led to overall reluctance to sign off on transactions and to disburse funds in fear of allegations of misconduct.

178. The Financial Management Law CPA Order 95/2004 does not precisely describe the new system of internal control and audit, but refers to further regulations for guidance**.** The FML sets the guidelines for internal controls at all levels both the federal and subnational. It gives to the MoF a central regulatory role in defining these new rules, which the MoF fulfills by issuing regulations and guidelines to spending units at all levels. For example, the regulations for executing the federal budget of 2007 set out reporting requirements that include a monthly trial balance to be submitted to the MoF, Department of Accounting; a monthly cash balance for actual expenditures and revenues including loans and deposits; specifications for recording, reporting, and use of revenues from donations, aid, grants, and loans; and a consolidated monthly report. There are also detailed requirements for managing expenditures, including recurrent and capital expenditures, procurement, contract compliance, spending of rewards/bonuses, canceling debts and assets, transfers, management of nonfinancial assets and services, personnel, and steps that need to be taken in the event of financial violations. The law sets out the role and responsibility of the MoPDC in relation to the capital budget and details the authority of the concerned head of a ministry or independent agency.

179. Specific executive instructions for both regional projects and instructions for expediting reconstruction in the Governorates were issued alongside the Federal Budget Law of 2006. These instructions set out in some detail the roles, authorities, and responsibilities of the Governors' offices and Governorate Councils, as well as the role of the GTO. The authority of the MoF in relation to these funds is also listed.

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[53] Guidelines to this effect were promulgated by the Deputy Prime Minister's office in August 2006. These regulations were circulated to all ministries and centrally financed agencies in September 2006.

180. **The Constitutional Review Committee is drafting umbrella intergovernmental and fiscal laws**. This is to give effect to the Constitution and reflect the distribution of exclusive, shared, and residual powers among the central, regional, and subnational tiers of government. The Governorate law draft is also being considered by the Council of Representatives (CoR), with implications for the current framework of internal controls.

181. **The *ex ante* control (or predisbursement audit) process at the subnational level is performed by the Commission of Auditing located in the Governorate treasury**. They are in charge of clearing the existence of a budget allocation and of each step of the expenditure cycle (commitment and payment order) to ensure regularity and legality according to prescribed criteria (such as correct documentation, proper application of procurement rules or wages rules, correct application of budget classification). This should not be confused with internal audit as it is usually understood. Internal audit refers to the assessment of the effectiveness and efficiency of the procedures of internal controls (in particular the predisbursement audit performed by the Commission of Auditing) in place within the agency in order to ensure that the agency is financially accountable. Internal audits as defined above are not performed either at the national or subnational level in Iraq (see section on internal audit below).[54]

182. **However, internal controls are generally ineffective for a variety of reasons**. For example, there is no clear and common understanding of the existing procurement and contract law. It is reported that ministries issue their own guidelines for implementing the relevant laws and regulations. As a result, rules and procedures vary among ministries and sometimes within central and subnational spending units within ministries. Furthermore, the extent to which these rules are checked is uncertain, but probably varies depending on the ministry, the sector, and the level of control (central or deconcentrated).

183. Verification of accounts at the subnational level which is akin to ex post control of the accounts is undertaken by Commission of accounts which responsible for monitoring and recording the records of the accounts (running checks for violations), and preparing the accounts and sending them to the MoF. The commission is divided into two sections: (a) Accounts of the center: responsible for all accounting processes related to the center (b) Accounts of districts and subdistricts: responsible for sending all trail balance accounts and charts of analysis to the department of auditing treasury accounts in the ministry of finance.

184. All spending units, including those at the subnational level, are required to report on realized receipts and executed payment to the MoF within 30 days following the end of each month. In accordance with Financial Management Law 95/2004, by the 15th of the subsequent month, the MoF is to compile a consolidated report on realized receipts and executed payments on the basis of the reports submitted. This information is meant to be made publicly available in the official gazette and other media as appropriate. But because of powerful sectarian interests, a lack of systems and procedures, and the security situation, this deadline is not met on a regular basis. The reports are also not made public for the same reasons.

***Internal Audit***

185. **In Iraq, some tasks related to the internal audit function are deemed to be performed by the inspectors general established by CPA Order 57/2004 in each ministry.** The system is modeled along that of the U.S. Currently; there are 31 inspectors general in 31 ministries of the

[54] In this Iraq is not unlike other countries in the region.

government. Many are drawn from what was previously called the "internal audit" unit—the internal ex ante control unit discussed above. Most of the current inspectors general are accountants and lawyers, with other professional backgrounds also represented. There are currently 2,500 employees in the entire inspector-general system. The inspectors general are appointed by the president for a five-year term following confirmation by a majority vote of the CoR. The five-year term can be renewed at the discretion of the president, subject to confirmation by a majority of the CoR. Before 2004, there was no system of internal audit as such in Iraq. However, this is related to spending by the ministries alone.

186. The issue of where to locate inspectors general at the Governorate level is an important one. Some of the models being discussed include:

- Deconcentrated inspector general's offices in the line ministries in the Governorates. But there is resistance to this model as Iraq moves toward fiscal decentralization.
- An inspector general attached to the Governor's office, together with an investigative judge. These inspectors general could then coordinate with the Governorate-level offices of the BSA and the CPI.

187. Order 55 covers the Baghdad Governorate, the CBI, and Government Religious Affairs, as the government owns religious sites throughout Iraq. There are now three inspectors general for religious affairs—one each for Shiites and Sunnis, and one for non-Arab sites. The Baghdad Governorate inspector general monitors service delivery issues across the Governorate, and reports to the mayor. The CBI has regional outreach to banking institutions in the provinces; however, the inspector-general system is not very strong. Similarly, the religious affairs inspectors general have regional outreach, but they are not very effective.

188. Inspectors general have been given full access while taking authorized actions necessary to "initiate, carry out, or complete any audit, investigation or review from obtaining documents relevant to any pending audit or investigation." No organization or individual is to prevent this access. Attempts to violate this provision are themselves to be subject to investigation and prosecution by the CPI, in accordance with the law.[55] In addition, inspectors general are charged with:

- Auditing all records of the ministry for the purposes of ensuring the integrity, transparency, and efficiency of ministry operations; reviewing ministry systems to measure performance; and making recommendations and providing information to improve ministry programs for investigation, policies, and procedures.
- Receiving and investigating complaints of fraud, waste, abuse of authority, and mismanagement affecting ministry interests from any source or upon its initiative; and providing quality control to ensure the timeliness, independence, and thoroughness of responses.
- Referring investigations to the relevant investigative authority and providing information and evidence regarding potentially criminal acts to appropriate law enforcement officials; and referring matters for further civil, criminal, and administrative action to the appropriate administrative and prosecutorial agencies and cooperating fully with investigators, the judiciary, and the CPI.

[55] At a World Bank–organized workshop on anticorruption in Iraq—which included the participation of the BSA, CPI , the inspectors general, and the courts—the inspectors general called for full independence so that they are empowered to carry out quarterly reviews of their agencies.

- Formulating policy to prevent fraud, waste, abuse, and inefficiencies; this includes review of legislation, rules, regulations, policies, procedures, and transactions, including of the inspector general's office.
- Monitoring corrective action in response to the findings and recommendations of inspectors general.
- Training ministry staff and coordinating public awareness programs.

189. **The internal auditing system in Iraq requires strengthening.** Many related issues have been identified in Chapter III. Internal auditing is particularly challenging at the subnational level, yet it is a critical aspect of Iraq's advancing decentralization agenda, as envisioned in the Constitution. Like many institutions in Iraq, there is no systematic internal auditing system process at the central level, let alone at the subnational level for a variety of reasons some of which have been identified above. An additional problem is that there is no capacity to fulfill all of the obligations of the office at either the central level or the subnational level. A critical factor in this is the security situation, which makes it extremely risky and difficult to conduct field work. There are currently 120 inspectors general, and, to date, 14 have been killed.

190. **Independence and objective assurance are not ensured.** Internal auditing should provide an effective tool for both management and government to gauge the extent to which the auditee has delivered on-budget and effective services. Ideally, internal auditors should not be involved in day-to-day management activities. But, in some instances, the inspectors general are themselves involved in establishing internal control and procedures. While ongoing communication with the head of the institution is required, internal auditors should not be under the control of the related head of the institution—as is the case in Iraq.

191. **Lack of independence, is a critical issue in Iraq.** Inspectors general in Iraq are placed within the ministries themselves, and have to work with the ministry officials whose work they audit. This makes it difficult to carry out effective investigations.

192. Measures have been taken to address some of the issues raised above. The budget of the inspectors general has been increased so that their office is able to hire an extra 1,000 staff.[56] The MoF also approved a hazard pay of 70 percent of base pay, which brings the wages for the inspectors-general office in line with those of the BSA and CPI.

***Accounting, Recording, and Reporting***

193. **The GoI primarily uses cash-based accounting, with transactions and events recognized when cash is paid or received.** But certain accounting elements are treated as under an accrual basis of accounting on a selective basis. This is seen by the government as a step toward an accrual basis of accounting and the introduction of a computerized general government accounting and reporting system.[57] (See Annex II PI22-25).

194. All spending units are required to report on a monthly basis to the MoF's Accounts Directorate or to the GTO. The financial reports are typically limited to a trial balance (the most common type of financial report), statement of expenditure, statement of receipts, bank statement, and so on. The trial balance contains details of account balances on a given date. Books in the GoI are

[56] Does not include inspectors general for the Ministry of Interior, who mainly police human rights complaints, and whose numbers have increased significantly.
[57] USAID, Implementation of Financial Management Information System.

being maintained on a double-entry system of bookkeeping. This is evident since the trial balance is being balanced on a regular basis.

195. **The overall financial reporting framework seems rudimentary.** There are no standard reports for budget variance, cash flows, bank reconciliation, fixed assets, and so on. The Governors' offices report on a monthly basis to the MoF's director of accounts. The reports need to be submitted within ten days of the end of the month, and are submitted in hard copy. Reporting includes expenditures, inflows (including self-revenues), and bank account statements. The Governorate Council reports to GTOs. By the seventh of each month, all spending entities under the GTO are required to provide a statement of receipt (including security deposits), statement of expenditure, trial balance, and certified bank statement.

***External Scrutiny and Audit***

196. Outside Kurdistan, external audit is the responsibility of the national Board of Supreme Audit (BSA) which has its headquarters in Baghdad. The BSA has a long history, having been established by law in 1927. Over the years, its powers have been modified by legislation, most recently by CPA Order 77/2004.[58] The main tasks of the BSA are set out in the BSA Law No. 6 of 1990 which were amended in 2004. Article 2 sets forth the Board's eight tasks: (i) auditing all governmental units for financial compliance; (ii) carrying out performance auditing mandates; (iii) supplying technical assistance in recordkeeping to accounting entities; (iv) modernizing systems in accordance with international standards; (v) helping to detect and expose cases of corruption, fraud mismanagement, and malfeasance through financial and performance audits; (vi) investigating specific disbursement issues as requested by the CoR; (vii) reverting all corruption and corruption-related issues to the ministerial inspector general's office; and (viii) preparing and presenting procedures and enactments to the CoR for the BSA's improvement and increased effectiveness.

197. **The BSA is generally regarded as a relatively credible and well-established organization**.[59] It is the oldest of the three bodies or "pillars" charged with addressing corruption, which include the CPI, the office of the inspector general, and the BSA. While BSA auditors are generally considered professional, they have only recently been introduced to modern auditing techniques. Given that internal controls and the internal audit system are weak, the Board is unable to depend on inspector-general reports for their audits. The BSA often has to work with the inspectors general to implement systems for managing public funds and achieving agreed-upon objectives.

198. **The scope of the BSA is wide and encompasses private companies and nongovernmental sectors, as well as the local and national government.** The board's audit powers are *ex post* (Article 9), whereas in the 1990 law, the board had the right to conduct a pre-contracting audit if deemed necessary for public interest. The draft law that is to be considered by legislature attempts to reclaim some of the BSA's previous investigative powers.

199. **A draft law was submitted to the CoR for reading and adoption in May 2007 in accordance with the Constitution of 2005.** The draft law states the BSA's duties more concisely, and the language used is better aligned to public financial management terminology. For example, the draft law states its duties as testing and verifying public expenditure transactions and ensuring their

[58] CPA Order 77 passed on April 2004 confirms the status of the BSA as an independent public institution with juridical personality that exists to: "enhance the economy, efficiency, effectiveness and credibility of the Iraqi government."
[59] Office of Inspector General and Broadcasting Board of Governors, 2006.

correctness within approved appropriations in the budget. Other duties are added to the CPA order, including evaluating the performance of the auditees and offering technical assistance in auditing and accounting in relation to institutional systems and procedures.

200. One of the competencies that the draft BSA law attempts to reclaim for the Board is its former investigative powers, which were removed with the establishment of the CPI and the inspector general's office**.** It also attempts to bring back the power of the BSA to conduct precontract audits if deemed necessary for public interest. The draft law has been considered by the CoR, and the Board is currently working on addressing some of the Council's recommendations. These include addressing some provisions within the draft on investigative powers of the BSA, objections to CPI findings and the relationship between the BSA and the CPI. The draft law states the objectives and duties of the Board much more explicitly, including: (i) safekeeping and protecting public funds from waste, loss, or misusage; (ii) ensuring efficiency of use; and (iii) expanding the accounting and auditing standards based on local and international standards. There are currently 14 accounting standards for items such as cash flow, currency and price fluctuations, tax incomes, and investments.

201. Most ministries have BSA offices in Baghdad. There are currently six regional offices to serve the 15 regions of Iraq.[60] The Board has recently made attempts to establish links with the two boards in Kurdistan, which operate independently of the board at the center. The draft law also proposes a seventh region, to include Kurdistan. All new Board recruits have a degree in accounting, law, or economics. While the Board has a long tradition of providing on-the-job training, there is a need to modernize training materials and methodologies.

202. **Though the BSA has regional offices, the central BSA sets out the strategic directions for the year, and the regional offices present their plans accordingly.** The President of the central BSA has also initiated a computerization program across all offices to coordinate data collection and interconnectivity. This is an important step toward better information management. There are growing concerns about the decentralization process currently underway in Iraq, and the existing mechanisms of controls, audit, and enforcement. It is reported that sub-national government agencies are reluctant to accept and act upon audit findings.

203. **While the Constitution and the law gives the BSA *de jure* independence, the BSA does not have complete independence from the government, and this affects its ability to provide independent audit conclusions and recommendations.** Independence of the external audit process is usually achieved by setting the auditing entity organization apart from the government, with its mandate and scope of work laid down in the Constitution and/or in law. The Constitution lays out in Article 103 that the BSA is accountable to the legislature. The Constitution sets out that the BSA is financially and administratively independent, is to be regulated by law (Article 103), and is attached to the CoR, Iraq's legislature, and as such reports to it. The budget for the Board comes through the legislature, which is a necessary first step towards ensuring its independence. However, the independence of individual auditors with respect to the audits they are working on is key to the functioning of the system. While conflict-of-interest provisions are set out in BSA regulations, individual independence is hampered in other ways. The personal risk involved for audit teams because of the conflicting interests of different ministries is the most critical factor in this regard. In addition, the establishment of the inspector general's office and the CPI has created some legal and procedural confusion as well as institutional tensions. The officials of the new institutions generally

[60] The six regional offices are located in Mosul (covering Mosul); Al Basrah (covering Al Basrah, Dhi Qar, Maysan); Babil (covering Babil, Karbala, An Najaf); Kirkuk (covering Kirkuk, Salah Ad Din); Diyala (covering Diyala, Wasit, Al Anbar), Ad Diwaniyah (covering Ad Diwaniyah and As Samawah).

have lower capacity than the BSA, which has a fairly robust training program for new entrants. There is an urgent need to review the laws and regulations governing the "three pillars" of anticorruption, and ensure that roles and responsibilities are clear.

204. **Laws and regulations should also be updated to reflect the decentralization process envisioned in the Constitution.** The BSA and the CPI have branch offices, with the BSA, as mentioned before, having six of the more active regional offices. With the new decentralized public financial management system coming into play, the role and function of the "three pillars" across Governorates should be clearly defined by law. The two BSAs in Kurdistan operate independently of the BSA at the center. They still follow the 1990 law, with amendments passed by the regional government. The audit reports of the regional government are considered by Kurdistan, and are not considered by the CoR at the center, though 17 percent of regional funds are derived from federal sources. Kurdistan also has a different internal audit system.

**While the BSA is considered the one institution among the three pillars with the greatest capacity, there is a need to provide training on modern auditing standards and techniques.** The president of the BSA has already embarked on an initiative to increase the capacity of auditors through a mentoring arrangement with the U.K. National Audit Office. The president has identified the need for training in areas such as risk-based auditing and social accountability and has initiated the process of acquiring this training for the members of the BSA.

205. **Governorate Councils are composed of elected representatives from districts and subdistricts responsible for legislative oversight and monitoring of development work.** The GTOs also serve the Governorate Councils like any other spending entities that draw funds using bank transfers. Governorate Councils are newly established entities with limited capacity to manage finances. Each Governorate Council has a finance committee who coordinates directly with the GTO in all financial management functions.

206. **Unlike the monthly reports to the GTO, Governors' offices do not report to Governorate Councils on a regular basis.** But Governorate Councils can request information. These links are likely to be stronger in Governors' offices, where the Governor has been selected by the GO. Governors' offices can also request information from the Governorate line agencies (that is, the respective Governorate Councils or directorates). Under CPA 71 he Governorate Councils have the power to remove the Governorate heads of line agencies, although this needs to be approved by the MoF.

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# ANNEXES

**Annex I. Annotated and Scored PEFA Indicators for Kurdistan[61]**

| Indicator | Score | Brief Explanation |
|---|---|---|
| **A. Budget Credibility** | | |
| **PI 1. Aggregate expenditure outturn compared to original approved budget** | D | Kurdistan's aggregate revenue outturns depend largely on the realization of transfers. Unlike the rest of Iraq, the region does not appear to have had significant trouble executing expenditures, which in turn are dominated by wages. Final approved budget estimates are not clear. Initial estimates for capital projects associated with fiscal transfer requests submitted to the Ministry of Finance have been well above realistic amounts, given the current method of allocation transfers. Fiscal transfer projections are well above final amounts approved by the central government. But final amounts were only clarified close to the budget year 2006. Actual realizations on central transfers in 2005 and 2006 appear to have been above 95 percent. Kurdish revenues as reported account for less than 3 percent of overall revenues (see PI 3). Consequently transfers rather than domestic revenues represent the main drivers of budget predictability on the revenue side in Kurdistan. |
| **PI 2. Composition of expenditure outturn compared to original approved budget** | D | Detailed data for functional/administrative units was not available. But figures provided for A Sulaymaniyah suggest that outturns across economic classifications were skewed (e.g., overspending on wages and associated rationing of capital expenditures). Salary expenditures have tended to exceed original projections more significantly (by almost 50 percent in As Sulaymaniyah in 2005). As a result, capital expenditures have tended to be rationed within the revenue envelope dominated by central government transfers (see PI 8). Budget allocations and realizations by administrative units (that is, Kurdish ministries) were unclear; data was not available at this level. |
| **PI 3. Aggregate revenue outturn compared to original approved budget** | D | The predictability of other revenues raised by Kurdistan, including customs, appears very weak (e.g., As Sulaymaniyah's estimates for customs and other revenues were under predicted by six to eight times). |
| **PI 4. Stock and monitoring of expenditure payment arrears** | D | Kurdistan officials suggested that there were no longer existing arrears concerning wages, and that wages were typically paid within days of when they were due. Exceptions included when fiscal transfer allocations to the Kurdish central bank were delayed, which typically occurred two to three times per month. Officials also suggested that there were no major arrears in terms of recurrent or capital expenditures. Capital projects were often significantly delayed, however, or spread out across fiscal years for cash management purposes. [62] |
| (i) Stock of expenditure payment arrears (as a percentage of actual total expenditure for the corresponding fiscal year) and a recent change in the stock | *NA* | NA |
| (ii) Availability of data for monitoring the stock of expenditure payment arrears | *D* | The monitoring of arrears does not appear to be consolidated in a timely fashion at the level of the Ministry of Finance, but appears to reside at the level of individual line agencies. |

[61] This assessment is based on two missions undertaken to Kurdistan by the team from September 13th to 21st, 2006 and January 28th to February 1st, 2007.

[62] No verification of the existence of arrears was undertaken by conducting direct interviews with government suppliers or contractors.

| Indicator | Score | Brief Explanation |
|---|---|---|
| **B. Comprehensiveness and Transparency** | | |
| **PI 5. Budget classification** | D | Kurdistan uses the national budget classifications for seven chapters at the national level, and adopts its own administrative headings given its subnational government structures. Like the rest of Iraq, Kurdistan has just committed to adopting a new chart of accounts compliant with the new International Monetary Fund government finance statistics standards. However, the actual roll out of this change is very slow. Actual reporting, even along existing chart of account lines for budgets and realizations, appears quite limited (see PI 6). |
| **PI 6. Comprehensiveness of information included in budget documentation** | D | Final budgets and realizations are only prepared in a very partial manner, and do not appear to be widely disseminated or documented. |
| **PI 7. Extent of unreported government operations** | na | Given the current lack of budget documentation, what is reported as part of government operations cannot be determined. |
| (i) Level of unreported extrabudgetary expenditure | *NA* | • NA |
| (ii) Income/expenditure information on donor-funded projects | *NA* | NA |
| **PI 8. Transparency of Intergovernmental Fiscal Relations** | D | |
| (i) Transparency and objectivity in the horizontal allocation among subnational governments | *D* | There appear to be no rule-based transfers to Governorate or local levels. Moreover, there still appears to be some lack of clarity about the role of Governorate Councils relative to Kurdistan's National Assembly and mayoral assemblies. The relationship between devolved levels of government (such as Governorate Councils) and deconcentrated agencies (Governorate and district line agencies, Governors' offices) could be clarified. |
| (ii) Timeliness and reliable information to SN governments on their allocations | *D* | Governorates and line agencies have no clear indication of their annual allocations. |
| (iii) Extent of consolidation of fiscal data for general government | *D* | As with general budget information, no consolidated information concerning subnational governments seemed to be available. |
| **PI 9. Oversight of aggregate fiscal risk from other public sector entities.** | NA | The information about whether Kurdistan adequately assessed risks from public sector entities, given lack of even basic budgetary documentation is unavailable. |
| (i) Extent of central government monitoring of AGAs/PEs | *D* | Basic budgetary/consolidated fiscal information not yet available. |
| (ii) Extent of central government monitoring of SN governments' fiscal position | *NA* | See also indicator PI 8. |
| **PI 10. Public access to key fiscal information** | D | Public access to key fiscal information remains very limited in Kurdistan. |
| ***C(i) Policy-Based Budgeting*** | | |
| **PI 11. Timely and organized participation in the annual budget process** | D+ | As a subnational region dependent on fiscal transfers from the center, its budget calendar is heavily driven by confirmation of transfer ceilings from the central government. |
| (i) Existence of, and adherence to, a fixed budget calendar | *C* | A budget calendar exists and appears to be based on the national cycle, but this does not appear to be strictly complied with. |

| Indicator | Score | Brief Explanation |
|---|---|---|
| (ii) Guidance on the preparation of budget submissions | *D* | Ministries appear to be poorly informed if not at all aware about the budget process. |
| (iii) Timely budget approval by the legislature | *NA* | Not clear if only the legislature approved, or just the council of ministries. |
| **PI 12. Multiyear perspective in fiscal planning, expenditure policy, and budgeting** | **D** | Annual budgeting remains weak. Capital projects do not appear to be implemented in a multiyear perspective, but are spread across years largely owing to cash management reasons. KRG claims not to have significant debt liabilities, so no debt sustainability analysis has been undertaken. |
| (i) Multiyear fiscal forecasts and functional allocations | *D* | NA |
| (ii) Scope and frequency of debt sustainability analysis | *NA* | Kurdistan does not appear to be contracting debt at this moment. |
| (iii) Existence of costed sector strategies | *D* | Sector strategies for key ministries are rudimentary if at all existent and typically not budgeted. The links between capital projects and forward estimates of recurrent costs are weak. |
| (iv) Links between investment budgets and forward expenditure estimates | *D* | In some sectors, such as school construction, some account is taken of forward teacher costs in new schools, although this does not appear to be done in the context of multiyear sectoral perspectives. |
| **PI 13. Transparency of taxpayer obligations and liabilities** | **D** | |
| (i) Clarity and comprehensiveness of tax liabilities | *D* | Direct taxation, other than customs revenues, appears to be very limited. Taxes are charged on rental incomes, but overall the base appears to be limited. |
| (ii) Taxpayer access to information on tax liabilities and administrative procedures | *D* | While the Constitution implicitly assigns tax policy to the regions, taxpayers and investors/corporations (foreign and domestic) require more and clearer guidance. Investor uncertainty about national versus Kurdistan-level corporate tax liabilities needs to be addressed. |
| (iii) Existence and functioning of a tax appeals mechanism | *NA* | The existence of a functioning tax appeals mechanism in key areas of taxation could not be confirmed. |
| **PI 14. Effectiveness of measures for taxpayer registration and tax assessment** | **NA** | |
| (i) Controls in taxpayer registration system | *Na* | |
| (ii) Effectiveness of penalties for noncompliance with registration and declaration obligations | *Na* | |
| (iii) Planning and monitoring of tax audit and fraud investigation programs | *Na* | |
| **PI 15. Effectiveness in collection of tax payments** | **NA** | *While KRG,* stressed the transparency and effectiveness of its customs revenue collection points along the Kurdish border, the data Is not reported to GOI. |
| (i) Collection ratio for gross tax arrears, being percentage of tax arrears at the beginning of a fiscal year, which was collected during that fiscal year | *Na* | |
| (ii) Effectiveness of transfer of tax collections to the treasury by the revenue administration | *D* | There are questions about whether customs should be remitted to the national treasury or Kurdistan. |

| Indicator | Score | Brief Explanation |
|---|---|---|
| (iii) Frequency of complete accounts reconciliation between tax assessments, collections, arrears records and receipts by the treasury | *Na* | |
| **PI 16. Predictability in the availability of funds for commitment of expenditures** | **D** | Priority is given to salary payments. Predictability of nonwage expenditures is especially limited, with ministries apparently having to make same-year requests to the Ministry of Finance and council of ministries. |
| (i) Extent to which cash flows are forecast and monitored | *D* | |
| (ii) Reliability and horizon of periodic same-year information to spending agencies on ceilings for expenditure | *D* | |
| (iii) Frequency and transparency of adjustments to budget allocations which are decided above the level of management of spending agencies | *D* | |
| **PI 17 Recording and management of cash balances, debt, and guarantees** | **D** | |
| (i) Quality of debt data recording and reporting | *NA* | |
| (ii) Extent of consolidation of the government's cash balances | *D* | Once projects are initiated, cash balances are transferred to individual ministries that open approved sub accounts. But no regular consolidation of these accounts appears to take place. |
| (iii) Systems for contracting loans and issuance of guarantees | *NA* | |
| **PI 18. Effectiveness of payroll controls** | **D** | Payrolls are managed at the level of individual ministries, although a department in the Ministry of Finance has oversight over the approval of new positions. |
| (i) Degree of integration and reconciliation between personnel records and payroll data | *D* | Updated only at the level of individual agency. |
| (ii) Timely changes to personnel records and the payroll | *D* | Updated at the only level of individual agency. |
| (iii) Internal controls of changes to personnel records and the payroll | *NA* | |
| (iv) Existence of payroll audits to identify control weaknesses and/or ghost workers | *NA* | |
| **PI 19. Competition, value for money, and controls in procurement** | **Not scored** | Procurement committees are established at the level of individual agencies. Guidelines are roughly adopted from national guidelines. The threshold and its coverage for open market procurement could not be determined. Regulatory requirements do not appear to be clear. There was no evidence of a clear mechanism of procurement complaints. A new procurement law for all of Iraq is currently being deliberated. It will need to be clarified to what extent Kurdistan sees its own capacity building in this area being aligned to the upcoming law. |
| (i) Use of open competition for | *Not* | |

| Indicator | Score | Brief Explanation |
|---|---|---|
| award of contracts that exceed the nationally established monetary threshold for small purchases | *scored* | |
| (ii) Justification for use of less competitive procurement methods | *Not scored* | |
| (iii) Existence and operation of a procurement complaints mechanism | *Not scored* | |
| **PI 20. Effectiveness of internal controls for nonsalary expenditure** | **NA** | Nonsalary expenditures are managed at the level of individual line agencies. |
| (i) Effectiveness of expenditure commitment controls | *NA* | |
| (ii) Comprehensiveness, relevance and understanding of other internal control rules/ procedures | *NA* | |
| (iii) Degree of compliance with rules for processing and recording transactions | *NA* | |
| **PI 21. Effectiveness of internal audit** | **NA** | Internal audit arrangements are managed largely at the level of individual agencies, although significant variations in capacity appear to be evident across agencies visited. |
| (i) Coverage and quality of the internal audit function | *NA* | |
| (ii) Frequency and distribution of reports | *NA* | |
| (iii) Extent of management response to internal audit findings | *NA* | |
| ***(iii) Accounting, Recording, and Reporting [["(iii)"? correct number here?]]*** | | |
| **PI 22. Timeliness and regularity of accounts reconciliation** | **D** | Accounts are managed at the level of individual agencies, and no systematic, timely reconciliation appears to take place. |
| (i) Regularity of bank reconciliations | *D* | |
| (ii) Regularity of reconciliation and clearance of suspense accounts and advances | *D* | |
| **PI 23. Availability of information on resources received by service delivery units** | **D** | Information systems concerning such service delivery networks as schools are still being established. For the health sectors, expenditures cascade down the health system, with higher-level nodes having financial accounts, and lower-level establishments (such as basic clinics) receiving cash transfers. |
| **PI 24. Quality and timeliness of same-year budget reports** | **D** | Lack of clarity concerning budget allocations by administrative heads is compounded by the fact that little reconciliation is done by individual agencies. |
| (i) Scope of reports in terms of | *D* | |

| Indicator | Score | Brief Explanation |
|---|---|---|
| coverage and compatibility with budget estimates | | |
| (ii) Timeliness of the issue of reports | *D* | |
| (iii) Quality of information | *D* | |
| **PI 25. Quality and timeliness of annual financial statements** | **D** | No consolidated government statement appears to be prepared to date for the two administrations, and it is not clear whether capacity building is planned to allow this as part of the newly unified 2007 budget year. |
| (i) Completeness of financial statements | *D* | |
| (ii) Timeliness of submission of financial statements | *D* | |
| (iii) Accounting standards used | *D* | |
| **PI 26 Scope, nature, and follow-up of external audit** | **D** | Audit is conducted by Kurdistan's external audit institutions. Audit institutions underscored their limited knowledge of prevailing international standards. The audit boards interviewed in Suleimaniah and Erbil stated that their biggest clients were the Ministry of Finance and the Ministry of Municipalities and Public Works, where they have permanent teams. |
| • (i) Scope/nature of audit performed | *C* | All administrative units appear to be subject to some annual external audit. |
| (ii) Timeliness of submission of audit reports to legislature | *D* | Delays appear to exceed 12 months. |
| (iii) Evidence of follow-up on audit recommendations | *D* | The legislature appears to have very limited roles or awareness of the details of budget implementation, as this role is largely undertaken by the Council of Ministers. Ministers seemed to regularly make ad hoc appeals for any programmatic shortfalls to the Minister of Finance or the Council of Ministers. |

| Indicator | Score | Brief Explanation |
|---|---|---|
| **PI 27 Legislative scrutiny of the annual budget law** | D | The legislature appears to have very limited roles in or awareness of the details of budget implementation, largely undertaken by the Council of Ministers. |
| (i) Scope of the legislature's scrutiny | *D* | The financial committee of the legislature did not appear to have a proactive role or high capacity for scrutiny of the budget. |
| (ii) Extent to which the legislature's procedures are well-established and respected | *D* | There is an overall lack of clarity concerning the legislative role, although this may be clarified under the draft Kurdistan Constitution currently being deliberated. |
| (iii) Adequacy of time for the legislature to provide a response to budget proposals both the detailed estimates and, where applicable, for proposals on macro fiscal aggregates earlier in the budget preparation cycle (time allowed in practice for all stages combined) | *NA* | |
| (iv) Rules for same-year amendments to the budget without ex ante approval by the legislature | *D* | The Council of Ministers appears to control all changes to the same-year budget, with a marginal role for the legislature. |

| Indicator | Score | Brief Explanation |
|---|---|---|
| **PI 28 Legislative scrutiny of external audit reports** | D | Audit reports do not appear to be made public, but are only referred to the Council of Ministers. But both audit boards stated that there had been civil and criminal action taken against wrongdoers in the past year. |
| (i) Timeliness of examination of audit reports by the legislature (for reports received within the last three years) | *D* | Audits not subject to legislative scrutiny. |
| (ii) Extent of hearings on key findings undertaken by the legislature | *D* | No evidence of hearings. |
| (iii) Issuance of recommended actions by the legislature and implementation by the executive | *D* | No evidence of instructions by legislature. |

| Indicator | Score | Brief Explanation |
|---|---|---|
| **D. Donor Practices** | | |
| **D 1 Predictability of Direct Budget Support** | NA | Donors do not appear to be providing direct budget support from donors currently does not appear to be the case. |
| (i) Annual deviation of actual budget support from the forecast provided by the donor agencies at least six weeks prior to the government submitting its budget proposals to the legislature | | |
| (ii) Same-year timeliness of donor disbursements | | |
| **D 2 Financial information provided by donors for budgeting and reporting** | **NA** | |
| (i) Completeness and timeliness of budget estimates by donors for project support | *NA* | |
| • (ii) Frequency and coverage of reporting by donors on actual donor flows for project support | *NA* | |
| **D 3 Proportion of aid that is managed by use of national procedures** | **NA** | |

**Annex II. Annotated Overview of PFM Issues in the Governorates using PEFA Indicators**

| | Governorate Council (GC) and Governor's office (GO) "devolved" expenditures | Line agency (LA) "deconcentrated" expenditures |
|---|---|---|
| **A. PFM OUTTURNS: Credibility of the budget (PI 1–4)** | Budgets using funds from Accelerated Reconstruction and Development Program (ARDP) subject to significant underrealization in 2006. | National execution rates for investments well below target; limited quantitative evidence on execution by province/sector. |
| **B. KEY CROSS-CUTTING ISSUES: Comprehensiveness and transparency (PI 5–10)** | To date, no single subnational budget. But the Government of Iraq introduced a new, GFS-compatible chart of accounts in 2007 applicable to all spending units (see PI 5). While this is an improvement, reports on provincial finances across various entities remain fragmented. | |
| **C. BUDGET CYCLE** | | |
| *C(i) Policy-based budgeting (PI 11–12)* | GC budget projects within population-based ARDP allocations, as well centrally determined envelopes for operating expenditures. GOs budget operating expenditures largely on year-on-year incremental basis. | LA appear to budget operating expenditures largely on recurrent basis. |
| *C(ii) Predictability and control in budget execution (PI 13–21)* | No well-defined system of local own source taxation (PI 13–15); GCs/GOs depend on disbursements though MoF GTOs; no formal system of subnational borrowing to date (PI 17). | "Self-financing" municipal offices at district level are earmarked real estate taxes, but with role of National Taxation Authority (PI 13–15). |
| | New inspector general structures are intended to strengthen internal audit. | |
| *C(iii) Accounting, recording, and reporting (PI 22–25)* | Ongoing efforts to implement an FMIS are only based on partial specifications; summary reporting is done to GTOs. | |
| *C(iv) External scrutiny and audit* | External audit conducted by the Board of Supreme Audit. | |

| C(i) Policy-based budgeting | | |
|---|---|---|
| PI 11 | Orderliness and participation in the annual budget process | The process is clearly in flux. The budget circular for 2007 had to be revised due to revision of the classification system. The budget was approved after the start of the fiscal year. |
| PI 12 | Multiyear perspective in fiscal planning, expenditure policy, and budgeting | No forward estimates of fiscal aggregates are prepared by the MoF. The sectors do not have costed sectors strategies. Poor linkages between Governorate budgets and the sectors. Operating and investment budgets are planned separately. |
| C(ii) Predictability and Control in Budget Execution | | |
| PI 13 | Transparency of taxpayer obligations and liabilities | Few taxes are collected directly by subnationals. These vary from Governorate to Governorate. |
| PI 14 | Effectiveness of measures for taxpayer registration and tax assessment | Information not available |
| PI 15 | Effectiveness in collection of tax payments | Information not available |
| PI 16 | Predictability in the availability of funds for commitment of expenditures | At the subnational level cash-flow forecasts are not prepared. Information is not available to subnational units or agencies. The budget is generally not released on time. In December 2006 allocations were provided in contravention of the FML law. |
| PI 17 | Recording and | Calculation of balance takes place irregularly, and the system does not yet |

| | | |
|---|---|---|
| | management of cash balances, debt, and guarantees | allow for consolidation of bank balances. |
| PI 19 | Competition, value for money, and controls in procurement | The major issue facing public procurement is the current uncertainty of public procurement laws and regulations.<br>Procurement procedures and practices, have a number of features that are not in line with generally accepted sound public procurement practice. These features include:<br>inadequate requirements for registration of suppliers and contractors<br>insufficiently transparent and fair debarment procedures<br>continued use of obsolete methods and procedures for procurement of goods and works and selection of consultants undue restrictions on access to bidding documents<br>Absence of adequate National Bidding Documents<br>insufficiently transparent bid submission, opening and evaluation procedures, and contract award procedures<br>Lack of effective bid protest mechanisms and publicity on contract awards.<br>While new regulations are being issued – they still have major shortcomings.<br>All of the above effect quality and transparency of the procurement regulatory framework in terms of establishing the use of open and fair competition and value for money. |
| PI 18 | Effectiveness of payroll controls | The payroll is not subject to the control of subnational units or Governorate departments. But payroll is poorly managed. |
| PI 20 | Effectiveness of internal controls for nonsalary expenditure | Commitment control systems are generally lacking.<br>Clear, comprehensive control rules and procedures are lacking in other important areas. No information on degree of compliance. |
| PI 21 | Effectiveness of internal audit | Weak internal audit, though the creation of inspectors general and relevant agents in all ministries was intended to strengthen this capacity. |
| C(iii) Accounting, Recording, and Reporting | | |
| PI 22 | Timeliness and regularity of accounts reconciliation | With USAID/Bearing Point support, the government has sought to roll out an FMIS system. In terms of subnational coverage, however, the functionality of the system is currently focused on reporting trial balances from respective spending units. These appear to include the Governorate treasury offices (GTOs). |
| PI 23 | Availability of information on resources received by service delivery units | Limited systematic information appears to be available beyond disbursements made from GTOs. |
| PI 24 | Quality and timeliness of same-year budget reports | Reporting to GTOs is mandated on a periodic basic. But upward consolidation is subject to significant lags. |
| PI 25 | Quality and timeliness of annual financial statements | |
| PI 26 | Scope, nature, and follow-up of external audit | The BSA is responsible for supreme audit. But the roles and responsibilities of the "three pillars" of anticorruption—the BSA, inspectors general, and the CPI—overlap. In addition, *de jure* and *de facto* impact of decentralization on BSA operations have yet to be determined. |
| PI 27 | Legislative scrutiny of the annual budget law | Governorate Councils (GCs), in principle, monitor all regional budget plans, not just the ARDP, but also Governors' offices and line agency directorates. To date, no such integrated plan/document exists at the Governorate level, although there are plans for 2008 to prepare integrated |

| | | |
|---|---|---|
| | | plans. The quality of legislative scrutiny by GCs appears to vary significantly across Governorates. |
| PI 28 | Legislative scrutiny of external audit reports | BSA reports do not appear to be made public, so legislative scrutiny by GCs is not likely to occur. |

## Annex III. Timeline of Political Transitions in Iraq since 2003

| Timeline | Event | Comments |
|---|---|---|
| 2003 | | |
| Jun 23 | Coalition Provisional Authority (CPA) established | The CPA was led by Ambassador Paul Bremer. The CPA replaced the Office of Humanitarian Affairs (ORHA) headed by Lt. Gen. Jay Garner. |
| Jul 13 | Interim Governing Council (IGC) | Appointed by the CPA |
| 2004 | | |
| March 8 | Transitional Administration Law (TAL) or the interim Constitution approved by the IGC | The TAL sets out a six-and-a-half month Constitutional process. The TAL also provides a six-month extension in Article 61(F).<br>Chapter VIII of the TAL sets out the powers and responsibilities of the regions, Governorates, and municipalities. |
| April 6 | CPA Order 71/2004 on local governmental powers comes into effect | Details the powers and responsibilities of subnational governments as set out in the TAL. |
| May 31 | Independent Electoral Commission of Iraq (IECI) established | CPA Order 92 |
| June 28 | Handover of sovereignty to the IGC | Sovereignty is transferred from the U.S.-led coalition to the IGC. |
| 2005 | | |
| Jan 30 | Elections for the:<br>• Transitional National Assembly (TNA)<br>• Governorate Councils (GCs)<br>• Kurdistan Regional Government (KRG) | 58 percent of eligible Iraqis voted; 31 percent women made up the TNA in the national elections.<br>Kurdish Coalition won 75 seats<br>United Iraqi Alliance won 140<br>Sunni Arabs lost 17 seats |
| October 15 | Referendum on Constitution | PASSED |
| Dec 15 | Elections for permanent National Assembly | 275 seats in the Council of Representatives.<br>More than 120 parties authorized to field candidates for the assembly. Each presented a list of at least 12 candidates. Every third name had to be a woman's to ensure that at least 25 percent of the seats in the assembly went to women. |
| Dec 31 | Council of Representatives: new term | Iraq's new Council of Representatives begins a four-year term. |
| 2006 | | |
| Feb 7 | Presidency council sworn in | |
| Mar 16 | Iraqi Parliament sworn in | |
| May 20 | Prime Minister Nouri al-Maliki assumes office | |

**Annex IV. Key 2005 Constitutional Articles Related to Intergovernmental Finance**

| Constitution | Type | Asymmetric arrangements | Expenditure/Role assignments | Own tax assignments | Intergovernmental revenue assignments (shared/transfer) | Borrowing | Other special intergovernmental arrangements |
|---|---|---|---|---|---|---|---|
| (i) | (ii) | (iii) | (iv) | (v) | (vi) | (vii) | (viii) |
| Constitution of the Republic of Iraq approved by referendum on October 15, 2005<br><br>Encompasses 144 articles | Federal (Art. 1). Governorates are made up of districts, subdistricts, and villages (Art. 116). | Sets out special region of Kurdistan (Art. 117, see also Art. 141 grandfathering previous agreements by Kurdistan). Art. 143 protects Art 53(A) of the transitional authorities' law concerning status of Kurdistan (and Art. 58 on Kirkuk).<br><br>Calls for law to be issued within six months (Art. 118) to regulate, with some further clarification in Articles 120–121 the creation of other regions. (A law as passed in Oct. 2006 deferring creation of new regions for 18 months, that is, through April 2008).<br><br>Baghdad may not become part of a region (Art. 124). | Art. 110 sets out exclusive federal authorities. Art. 114 sets out shared competencies. All residual powers are assigned to the regions and Governorates (Art. 115).<br><br>Art. 123 allows for both an upward and downward delegation of powers.<br><br>Role of local governments, notably for protection of minorities, to be set out by law (Art. 125). | Art. 111 assigns oil and gas to be owned by people in all Governorates and regions.<br><br>Taxes/fines must be regulated by law (Art. 28).<br><br>Art. 110 (iii) notes that federal government has exclusive authority to formulate "fiscal and customs policy." Article 114 (i) notes coordination in administration of customs with regions/Governorates as shared power. | Art. 112 states comanagement of hydrocarbon exploitation in endowed regions/Governorates, but calls for fair distribution based on population and historical damages.<br><br>Art. 106 gives public commission, to be regulated by law, authority over all federal revenues. | (International) debt responsibility of federal government (Art. 110) No specific mention of borrowing, unless considered part of Art. 110 concerning federal government's exclusive authority in formulating "fiscal and customs policy." | Federation Council to be established through follow-up legislation through two-thirds majority of Council of Representatives (Art. 65), which will also specify its "specializations and all that is connected to it." Art.137 further delays this to the second electoral term after the Constitution is enacted.<br><br>Federal Supreme Court to address intergovernmental disputes (Art. 93)/<br><br>Public Commissions for Revenue Management (Art. 106), including audit functions, to be regulated by law (pending 2/2007).<br><br>Public commission for "interest of regions" (Art. 105) (pending 2/2007). |

**Annex V. Selected Laws and Regulations**

| Iraqi laws | Subject of law | Name of law (Arabic) | Notable issues |
|---|---|---|---|
| Law 1945 | Accounting | قانون المحاسبات | |
| Law 1952/162 | Real estate | العقارات قانون | Regulates property of municipalities and fees, see also Law 1963/130 on municipalities |
| Law 1962/26 | Vacant land tax | ضريبة العقارات الغير مشغولة | Revenue tax for municipalities |
| Law 1963/130 | Municipalities | قانون البلديات | |
| Law 1969/ | Governorates | قانون المحافظات | |
| Law 1973/ | Procurement and purchases | قانون المشتريات | Large Array of Instruction 1973, 1995, 2005 |
| Law 1982/113 (Amended 2003) | Income tax | قانون ضريبة الدخل | Does not include SOEs. Covers general federal government revenues. |
| Law 1995/25 | Revolutionary councils | قانون مجالس الثورة | |
| Law 1997/36 | Sales tax | | For hotels and restaurants |
| Law 19xx/ | Chambers of commerce | قانون غرف التجارة | Regulates contractors, in particular who can bid on public contracts |
| Resolution 1220/2002 | Real estate transfer tax | | |
| Law 2005 | Annual budget | قانون الموازنة | |
| Law 2006 | Annual budget | قانون الموازنة السنوية | |
| Law 2007 | Annual budget [draft] | مشروع الموازنة السنوية | |
| Draft Law on Governorates | | مشروع قانون المحافظات | First draft by GC, then redrafted by council |
| New procurement law | | قانون مشتريات جديد | |

**Annex V. (cont.)**

| Law | Subject | Date | Arabic name | Comments |
|---|---|---|---|---|
| CPA Orders | | | اوامر سلطة الائتلاف | |
| CPA Order 1 | De-Baathification of Iraqi society | May 26, 2003 | | |
| CPA Order 30 | Reform of salaries and employment | Sept. 8, 2003 | امر تعديل سلم الرواتب | |
| | Transitional administration law | March 8, 2004 | قانون الادارة الانتقالية | Precursor to Constitution, superseded save for Kirkuk referendum |
| CPA Order 38 | Reconstruction levy | Apr. 4, 2004 | ضريبة الاعمار | Regulates 5 percent customs levy surcharge; important revenue source for GCs |
| CPA Order 71 | Local governmental powers | Apr. 6, 2004 | قانون صلاحيات المحافظات | |
| CPA Order 87 | Public contracts | May 16, 2004 | امر سلطة الائتلاف حول المشتريات | Incomplete implementation, still prefer law of 1973 |
| CPA Order 95 | Financial management and public debt | June 4, 2004 | المالية قانون الادارة والدين العام | |
| CPA order on changing planning 45 | | | امر سلطة الائتلاف عن وزارة التخطيط | |
| Constitution of the Republic of Iraq/2005 | | Oct. 15, 2005 | دستور عام2005 | |

**Annex V. (cont.)**

| Ministerial Instructions | Subject | | Comments |
|---|---|---|---|
| Resolution 2002/120 | real estate transfer tax | قانون ضريبة نقل العقار رقم 120لسنة 2002 | Tax on transfer of land |
| | instruction for implementing projects, Ministry of Planning 1973, 1995, 2005 | تعليمات تنفيذ المشاريع صادرة من وزارة المالية | http://www.iraqbuildingcodes.org |
| April 2006 | Annual Budget Law 2006, executing instructions for regional projects and expediting reconstruction in Governorates | قانون الموازنة السنوية لعام2006 | |
| September 2006 | amendment to executing instructions | تعديلات على تعليمات صرف نفقات تنمية الاقاليم | States that only Governor can sign checks |
| September 2006 | Ministry of Municipalities and Public Works instructions for transition of ARDP projects 2006–7 | وزارة البلديات والاشغال العامة: تعليمات انتقالية 2006–7 | Establishes rules for making projects; multiyear budget |
| Ministry of Finance Regulation 2007 [undated] | new draft instructions for 2007 | مسودة تعليمات تنقيذ موازنة2007 | |
| Resolution 2002/120 | real estate transfer tax | قانون ضريبة نقل العقار رقم 120لسنة 2002 | Tax on transfer of lands |
| Economic Affairs Committee, Aug. 2006 | contract execution regulations | قانون تنفيذ العقود | Signed by Barham Salih, deputy prime minister |
| Sep. 6, 2006 | 2007 budget circular | تعليمات اعداد الموازنة | Five pages, including forms for budget preparation |
| Ministry of Finance, Feb. 20, 2006 | 2006 budget execution regulations | تعليمات اعداد الموازنة لسنة2006 | |
| Dec. 12, 2006 | spending authorities | صلاحيات الصرف | Section Article 4, Section 7 of FML Law Authorized to Spend Dec, authorization, |

**Annex VI. Regional Development/Reconstruction Funds (ARDP Funds)**

| No. | Province | Population sum total | Amount allocated for development of territories (Dinar, Billions) | Amounts allocated for speeding up construction of Provinces (Dinar, Billions) | Total 2006 PC Allocation (Dinar, Billions) | Population Estimated 2007 Population | Total 2007 Projected (Dinar, Billions) |
|---|---|---|---|---|---|---|---|
| *Provinces not Incorporated as Regions* | | *25,238,430* | *1,322* | *1,500* | *2,822* | *26,014,571* | *2,604* |
| 1 | Ninawa | 2,722,931 | 141 | 162 | 303 | 2,848,437 | 285 |
| 2 | Kirkuk | 1,097,961 | 57 | 65 | 122 | 1,150,404 | 114 |
| 3 | Diyala | 1,344,900 | 69 | 80 | 149 | 1,364,429 | 138 |
| 4 | Al Anbar | 1,309,145 | 68 | 78 | 146 | 1,348,956 | 135 |
| 5 | Baghdad | 6,786,207 | 350 | 404 | 754 | 7,022,655 | 705 |
| 6 | Babil | 1,504,084 | 78 | 89 | 167 | 1,413,375 | 141 |
| 7 | Karbala | 837,182 | 43 | 50 | 93 | 903,692 | 90 |
| 8 | Wasit | 997,830 | 52 | 59 | 111 | 1,057,158 | 105 |
| 9 | Salah ad Din | 1,119,891 | 58 | 67 | 125 | 1,159,759 | 117 |
| 10 | An Najaf | 1,064,680 | 55 | 63 | 118 | 1,113,147 | 111 |
| 11 | Al Qadisiyah | 998,550 | 52 | 59 | 111 | 820,948 | 81 |
| 12 | Al Muthanna | 622,351 | 32 | 37 | 69 | 651,976 | 66 |
| 13 | Dhiqar | 1,611,152 | 83 | 96 | 179 | 1,744,517 | 174 |
| 14 | Maysan | 899,412 | 64 | 53 | 117 | 961,362 | 96 |
| 15 | Al Basrah | 2,322,154 | 120 | 138 | 258 | 2,453,756 | 246 |
| *Regions/KRG* | | *3,803,323* | *196* | *0* | *196* | *3,951,809* | *396* |
| 16 | Dahuk | 879,694 | 45 | 0 | 45 | 916,174 | 144 |
| 17 | Erbil | 1,385,227 | 72 | 0 | 72 | 1,438,240 | 159 |
| 18 | As Sulaymaniyah | 1,538,402 | 79 | 0 | 79 | 1,597,395 | 93 |
| **Total** | | **29,041,753** | **1,500** | **1,500** | **3,000** | **29,966,380** | **3,000** |
| *Total (est. USD millions)* | | | *1,017* | *1,017* | *2,034* | | *2,362* |
| *Share KRG* | | *13.1%* | *13.1%* | *0.0%* | *6.5%* | *13.2%* | *13.2%* |

*Source*: MOF

**Annex VII. Summary Powers at the Subnational Levels of Government**

| Legislative | Executive | Executive agencies |
|---|---|---|
| **Governorate Council (GC)**<br>• Funded by direct block grants from the center.<br>• Sets priorities for Governorates.<br>• With two-thirds vote, can amend local projects in annual ministry budget plan if no interference with national objectives.<br>• Monitor and recommend improvements to the delivery of public services.<br>• Collect revenues by imposing taxes and fees.<br>• Organize operations of Governorate administration.<br>• Performs functions independent of the control or supervision of any ministry.<br>• Has approval/veto powers over the appointment of directorates general and other local ministerial (senior) officials.<br>• Appoints Governors and deputy Governors.<br>• Each Governorate may, by majority, vote for other administrative units with the Governorate to achieve greater economies of scale. | **Governor and Governor's office (GO)**<br>• Funded by direct block grants from the center.<br>• The head civil official of a Governorate.<br>• Accountable to the GC.<br>• Responsibility is to direct, coordinate, and oversee actions in implementation of the GC's decisions.<br>• Deputy Governors report to the Governor.<br>• Governor and deputy Governors can attend regular GC meetings as nonvoting members.<br>• Appoint Governorate officials, provided that appointments of directorates general serving directly on the staff of GOs is approved by the majority of GCs.<br>• Governors have final authority to remove those officials who they are authorized to appoint (with majority vote of the GC). | **Ministry of Finance (MoF), Accounts Directorate/treasury offices**<br>• Coordinate funding needs with the GO.<br><br>**Ministry of Interior**<br>• Within each Governorate, there is a chief of police responsible for overseeing all civil law enforcement activities within the Governorate.<br>• Positions are advertised nationally, and the GC is notified of vacancies. The GC selects from short-listed candidates provided by the Ministry of the Interior.<br>• The chief of police is to work with the Governorate and Governor to coordinate local security plans.<br><br>**Offices of other line agencies**<br>• Usually headed by a director general.<br>• Works together with the GC to ensure local needs are being addressed. |
| **Local councils**<br>Can be organized in the following manner:<br>• District council, *Qada'a*<br>• Subdistrict council, *Nahiya*<br>• Councils, *Beladiya*<br>• Neighborhood councils, *Hayy*<br><br>• Responsible for organizing and representing their constituents.<br>• Ensure public services respond to local need.<br>• Organize the operations of local administration.<br>• Review local ministry plans.<br>• Collect and retain local revenues, taxes, and fees.<br>• Identify local budgetary requirements through the national budgeting process.<br>• Assist in initiating and implementing local projects together with international and nongovernmental organizations.<br>• Conduct other activities granted by GCs, consistent with the applicable law. | **Mayors**<br>• Senior administrators of local councils and are accountable to the local council.<br>• Mayors direct, coordinate, and oversee actions in implementation of the decision of the local councils, and serve as the primary liaison between the local councils and the Governors.<br>• Elected by the district council.<br>• Mayors appoint local government officials, provided that their appointments serving directly on the local government staff and other senior positions within the administrative unit are approved by majority vote.<br>• Can remove officials supported by majority vote of the local council.<br>• Mayors meet regularly with directors within their geographic areas of responsibility, and, where authorized, direct delivery of public services.<br>• Mayors meet with other mayors to ensure that services are being provided equitably and efficiently. | MoF, line agencies, and GO may have representatives at these levels.<br><br>**Ministry of Municipalities and Public Works** coordinates with Municipal Councils to collect municipal taxes |

*Source:* CPA regulations, others

## Annex VIII. Financial Management Law and its application to subnational Governments

**COMPETENCE IN DRAWING UP THE FEDERAL BUDGET OF IRAQ**

**Section 4: general provisions, para 3**.
Pursuant to Article 25 of the Transitional Administrative Law: federal government has exclusive competence in drawing up the federal budget of Iraq.
Pursuant to Article 25, Section 2, of the Local Government Powers Law, GC has limited authority to amend the budget plan of a ministry with regard to a specific project.

- Individual Governorates' budgets for the fiscal year shall be passed by the GCs.

Individual regions' budgets for the fiscal year shall be passed by the regional governments.

Application under the Iraqi Constitution, 2005
Article 143: the Transitional Administrative Law and its Annex shall be annulled on the seating of the new government, except for the stipulations of Article 53(A) and Article 58 of the Transitional Administrative Law.
Article 110 (3): formulating fiscal and customs policy; issuing currency; regulating commercial policy across regional and Governorate boundaries in Iraq; drawing up the national budget of the state; formulating monetary policy; and establishing and administering a central bank.
Article 110 (7): drawing up the general and investment budget bill.

**COMPONENTS OF THE ANNUAL BUDGET**

**Section 4: general provisions, para 4.**
Transfers, including to regional governments, Governorates, and municipal and local governments, including special budgetary funds.

**RECEIPTS TO INCLUDE**

**Section 4: general provisions, para 7.**
Transfers from regional governments, Governorates, and municipal and local governments, including special budgetary funds.

**PAYMENTS INCLUDE**

**Section 4: general provisions, para 8.**
Transfers to regional governments, Governorates, and municipal and local governments, including special budgetary funds.

Application under the Iraqi Constitution, 2005
121 (3) on revenue allocation to regions: regions and Governorates shall be allocated an equitable share of the national revenues sufficient to discharge their responsibilities and duties, but having regard to their resources, needs, and the percentage of their population.
122 (2) on powers of Governorates: Governorates that are not incorporated in a region shall be granted broad administrative and financial authorities to enable them to manage their affairs in accordance with the principle of decentralized administration, and this shall be regulated by law.

**BUDGET PROPOSAL**

**Section 6: para 2.**
Every May, MoF shall issue a report on fiscal policy for the next fiscal year, including total spending limits to be approved by the Council of Ministers.

Application under the Iraqi Constitution, 2005: Article 114 (4)
To formulate development and general planning policies.

**BUDGET CIRCULAR**

**Section 6: para 3.**
Every June, MoF in consultation with MoPDC will issue a circular setting guidelines and objectives of fiscal policy for spending units including the Governorates. Will include key economic parameters, procedures, and timetable for budget preparation, as well as total levels of expenditure for each spending unit.

**BUDGET REQUESTS**

**Section 6: Para 4.**
Spending Units will submit requests, including the information prescribed to the MoF for allocation of funds. Copies also to MoPDC. Information to be included: expenditure estimates for the budget year in the functional classification systems

- Value of outstanding commitments for the current or prior year
- Expenditure estimates for the year following the budget year
- Estimates of funds required for personnel
- Estimates of requirements for other operating costs
- Multi-year commitments, along with separate capital expenditures
- Estimates of receipts from the core activities of spending units.
- Estimates of expenditures due in foreign currency.

**BUDGET ALLOCATION**

**Section 6: para 5.**

- MoF and MoPDC, on the basis of estimates of revenue and submitted budget proposals for the allocation of budget funds, and in light of discussions with proposing heads of spending units, determine estimated payments for spending units.

**Application under the Iraqi Constitution, 2005**

- A public commission shall be established by law to audit and appropriate federal revenues. The commission shall be comprised of experts from the federal government, the regions, the Governorates, and its representatives, and shall assume the following responsibilities:
- First: To verify the fair distribution of grants, aid, and international loans pursuant to the entitlement of the regions and Governorates that are not organized in a region.
- Second: To verify the ideal use and division of the federal financial resources.
- Third: To guarantee transparency and justice in appropriating funds to the governments of the regions and Governorates that are not organized in a region in accordance with the established percentages.

**Section 6: para 5.**
Every September, MoF will prepared the annual federal budget and submit it by October 10 to the CoR for approval.

**BUDGET REALLOCATION**

**Section 7: para 3.**
The CoR has the right to reallocate proposed spending and reduce total amounts in the federal budget.

**NONAPPROVAL OF BUDGET BY COM**

**Section 7: para 4.**
If the federal budget is not approved by the CoR by December 31, the MoF will approve funds on a monthly basis for spending units up to 1/12 of appropriations of the previous fiscal year until a budget is approved.

**AMENDMENT OF THE FEDERAL BUDGET**

**Section 7: para 5.**
The annual federal budget may be amended through a supplementary budget only on the basis of a significant and unexpected change in economic circumstances or national priorities. The supplementary budget must be determined by the Council of Ministers on recommendation of the MoF and approved by the CoR.

## Annex IX. Budget Timeline

| Dates | Activity |
|---|---|
| January–April 30 | Spending units consult with the ministry of planning and development cooperation on priorities, estimates of total funding, procedures for preparing capital spending plan, and implications of capital expenditures, including those to be financed from external sources. |
| May | The ministry of finance issues a report with fiscal priorities for the next fiscal year, including the overall limit and limit for each spending unit (line ministry).<br>This report is submitted to Council of Ministers for approval, together with final accounts of the federal budget as submitted to the Board of Supreme Audit (BSA). |
| May 31 | The minister of finance reports first quarter spending to the Council of Representatives. Details to be included in quarterly and mid-year reports include budget revenue, expenditures and financing. |
| June | The minister of finance consults with the minister of planning and development cooperation, and, based on the priorities for fiscal policy established by the Council of Ministers, issues a circular containing guidelines and objectives of the fiscal policy. The circular is sent to spending units to help them prepare their budgets. It should include key economic parameters, procedures, and a timetable for budget preparation, as well as total levels of expenditure for each spending unit. |
| July | Spending unit submit their requests to the minister of finance. Copies of the capital portion of the budget are submitted to the minister of planning and development cooperation. Each request includes:<br>• Expenditure estimates as set out in the classifications set by the Ministry of Finance (MoF), including the value of outstanding commitments from the previous year.<br>• Estimates for the next three fiscal years, if possible.<br>• Estimates of personnel.<br>• Estimates of operating costs.<br>• Multiyear commitments and separately prepared capital expenditures.<br>• Estimates of receipts from core activities of spending units.<br>• Estimates of the proportion of expenditures due in foreign currency.<br>The minister of finance may determine more specific requirements for the content and format of the request. |
| July–September | The minister of finance, in consultation with the minister of planning and development cooperation, and on the basis of estimates of revenues and submitted budget proposals, determines estimated payments, as well as the amount of the contingency reserve.<br>In the event of irreconcilable disagreement during discussions between the minister of finance and the ministers responsible for the spending units, the minister of finance will note the disagreement and propose a solution.<br>The Council of Ministers, within the agreed aggregate limit, adjusts appropriations in accordance with their collective priorities. |
| August 31 | The minister of finance reports to the Council of Representatives on mid-year spending under the budget approved for the current fiscal year. |
| September | The minister of finance prepares the draft annual budget and submits it to the Council of Ministers for approval by October 10 |
| October 10–<br>December 31 | The Council of Representatives can reallocate proposed spending and increase expenditures. If approved by the Council of Representatives, budget details are published in the *Official Gazette.* If not approved by January 1, the MoF will allow spending units to spend 1/12 of their appropriations for the previous fiscal year until the budget is passed. |
| November 30 | The minister of finance reports to the Council of Representatives on third-quarter spending under the budget approved for the current fiscal year. |
| Next fiscal year | |
| April 15 | The MoF prepares annual final accounts of the federal budget, including special budgetary funds, and submits these to the BSA. |
| June 15 | The BSA provides the Council of Ministers with the audit report on final accounts. |
| June 30 | The Council of Ministers submits final accounts and related audit report to the Council of Representatives. |
| | When the Council of Representatives approves the audit report, it is published in the *Official Gazette* and made publicly available. |

**Annex X. The Capital Budget Process at the National Level**

**STEP 1.** Preparing the capital budget is one of the most important steps in the process of preparing the annual federal budget. It proceeds through the same chronological stages as the rest of the budget. The process begins with the formation of a special committee to establish the basis and general principles of the federal budget and to identify the general financial frame of the budget. The committee is formed by representatives from the Ministry of Finance, Ministry of Planning and Development Cooperation (MoPDC), Ministry of Oil, Ministry of Trade, and the Central Bank of Iraq.

The committee begins to meet in June of each year. It undertakes the following tasks.

a) Estimating the volume of financial revenues expected for the next year.
b) Estimating the volume of spending in accordance with the chapters and contents of expected spending.
c) Identifying the gap between revenues and spending, and how to bridge that gap.
d) Explaining the basis and general principles followed in preparing the envelopes within which the ministries and other departments must work. The most important of these general principles are:
    1) To emphasize the economic feasibility of projects in any discussion of their execution.
    2) To propose only the best projects so as to ensure the most efficient possible use of the investment.
    3) To exclude operational spending from the capital budget.
    4) To specify the need for hard (foreign) currency so as to be able to choose the projects that require the lowest amount of foreign currency as a share of expected revenues.
    5) To estimate the time required for implementation of each project.
    6) To ensure that the private sector has an equal opportunity to participate in projects.
    7)

**STEP 2.** After the financial framework is approved by the committee, it is sent to the Council of Ministers for discussion and approval.

**STEP 3.** Once the Council of Ministries approves the financial framework, the MoF and MoPDC distribute the annual allocations to the ministries and independent agencies. The following standards are observed in the distribution process:

- The executive capability and spending efficiency of each spending unit as revealed in data covering the most recent six months of the current budget year and the prior year.
- Investment priorities as detailed in the GoI's strategy for financial, economic, political, and national development.

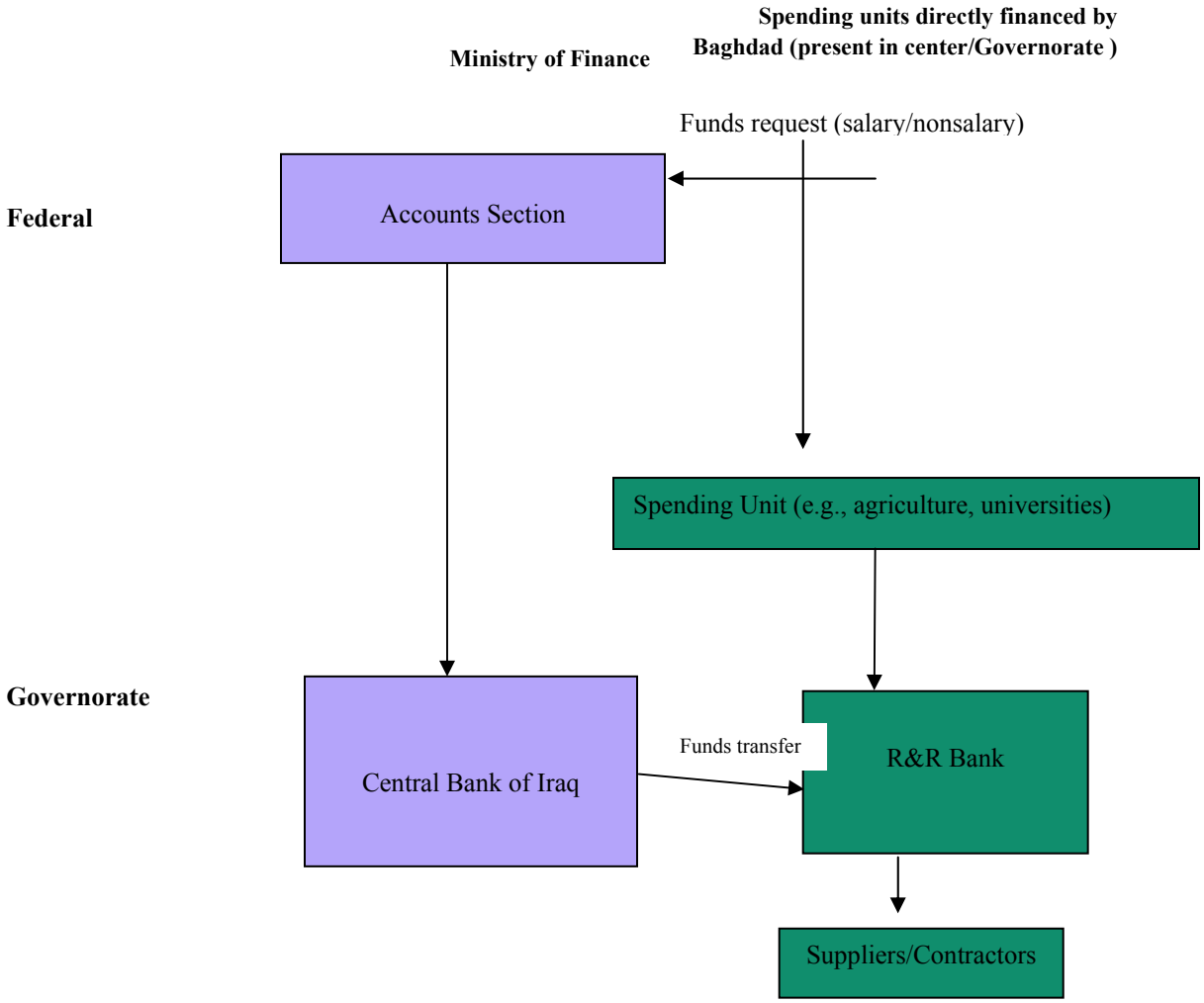
**STEP 4**. After identifying the initial financial ceilings, the MoF circulates it to all ministries and independent agencies to guide them in preparing their capital budget requests for next year. These requests should itemize all proposed projects, providing detailed and comprehensive information about each.

**STEP 5**. After receiving the suggestions referred to in the previous step, the technical departments review and verify all data. These budget request forms form the basis of discussions between the executive agencies and the MoF Budget Directorate. The discussions are conducted in August of each year. The participants in these discussions are the directors of departments of planning and execution, as well as staff responsible for project execution. Together they determine the annual allocations for each project listed in the capital budget proposal. They also determine the final financial ceiling of all ministries.

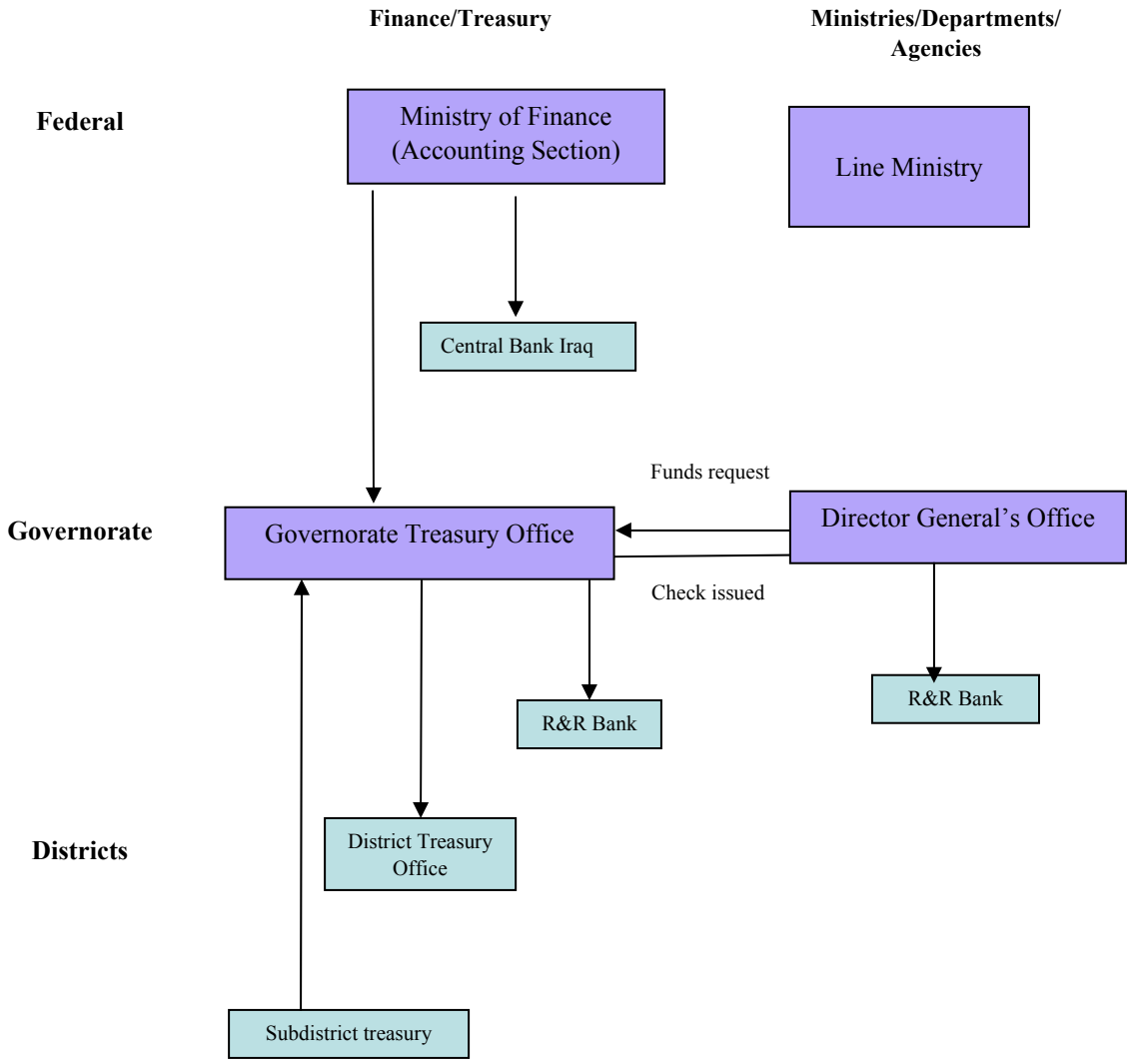
**STEP 6.** After determining the annual allocations and distributing them to the departments responsible for carrying out capital projects, the Department of Government Investment at the MoPDC integrates the data and prepares the capital plan in its final form. It is then sent to the MoF to be consolidated with operational budgets. The consolidated budget is forwarded to the Council of Ministers in September.

Source: Presentation of Mr. Qassim Enaya Frez, director general, Government Investment Planning, MoPDC, to World Bank Subnational PFM Workshop, Beirut, April 2007.

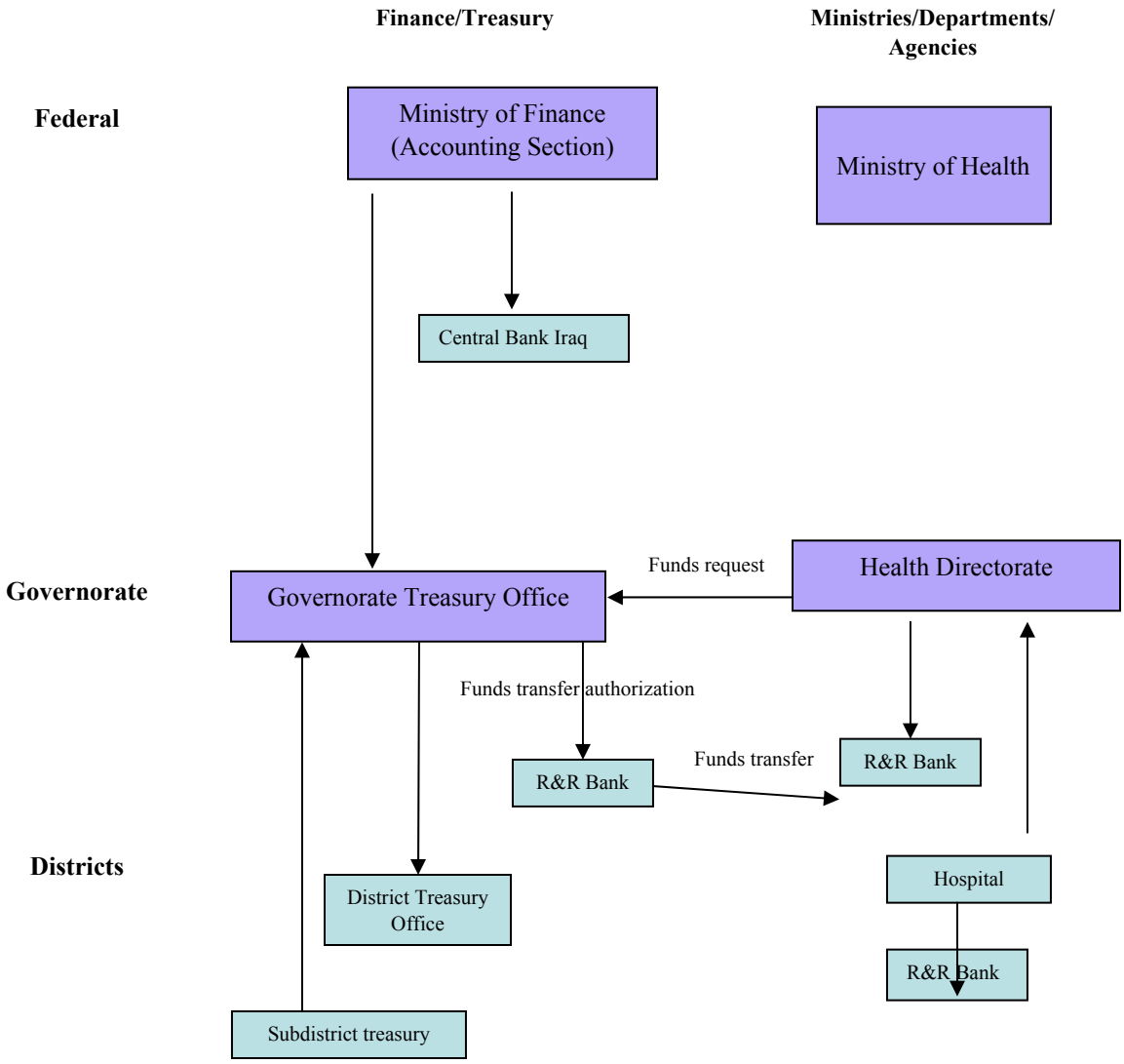
**Annex XI. Financing Flows for agencies funded by GTOs and MOF**



**Funding Flows for Entities Drawing on Governorate Treasury Offices (Variant 1)**



**Funding Flows for Entities Drawing on Governorate Treasury Offices (Variant 2)**



Discussion Paper Number 8 (December 2007)

# REVENUE ASSIGNMENT AND FISCAL INTERGOVERNMENTAL ISSUES IN THE NEW CONSTITUTION INTERIM PERIOD IN IRAQ

**Esam Younis, Najed Hamody, Halwan Siwaily and Ricardo Silva-Morales**

**Fiscal Policy Area LGP2**

**Edited by Nigel Atkin**

**The views and concepts expressed in this paper are those of the authors and do not represent those of the USAID or the US Government**

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## Abbreviations

| | |
|---|---|
| **DG** | **General Directorate** |
| **LGP2** | **Local Government Strengthening Project 2** |
| **MMPW** | **Ministry of Municipalities and Public Works** |
| **MPCD** | **Ministry of Planning and Cooperative Development** |
| **MOF** | **Ministry of Finance** |
| **GOI** | **Government of Iraq** |
| **USAID** | **US Government Agency for International Development** |
| **ECON II** | **Economic Governance Project II** |
| **SOEs** | **State Owned Enterprises** |
| **USA** | **United States of America** |
| **CPA** | **Coalition Provisional Authority** |
| **Beladiya** | **Office of the Ministry of Municipalities and Public works in the District. The Beladiya is usually named as the municipality office.** |
| **Qada'a** | **District—corresponds in generic terms to what is understood in the west as a municipality** |
| **KRG** | **Kurdistan Regional Government** |

## INTRODUCTION

The new Constitution of 2005 confirmed Iraq as a Federal State. As a consequence of this shift from unitary to federal several aspects to further the reformed Iraqi State got subjected to future legislation. In the interim period between the adoption of the Constitution and the enactment of subsequent legislation, there is a subjacent reality that both politicians and bureaucracy are struggling to escape from. This reality is the current international practice demonstrates States—both unitary as well as federal—need to work within a decentralized fiscal arrangement to properly respond to their citizens needs[1].

The current development of the State as a political entity has successfully come to terms with the reality that the main purposes of the organization is not to arbitrarily impose government on the inhabitants, but to serve them and above all facilitate security and the continuous improvement of living standards[2]. Failure of the State nowadays is sensibly observed when both political groups and the administration fail to accomplish the State's main purposes. In this context of facilitating adequate living standards to the inhabitants, the role of the communities in identifying needs and priorities is essential to ensure proper levels of satisfaction by the recipients of any State-provided services[3]. This document sustains that the best way to gain sense of what a respective community's will is, the natural positioning of elected local authorities is hard to surpass. Therefore, enhancing the role of elected local authorities is one of the key elements of a State's success.

This document is a follow up to prior analysis on fiscal devolution in Iraq by LGP2. To implement this document's viewpoints in Iraq it is required to understand what fiscal federalism is and how it could be applied to the Iraqi case, given the extreme fiscal centralization model that the new Iraqi State inherited. This time in this document it shall be paid more attention to the possibilities for enhancing fiscal devolution within the current legal framework and practices by following the principles of fiscal federalism.

Despite fiscal federalism has mostly been associated with the Public Choice approach to economics, in this paper the analytical approach would be closer to the ideas proposed by the New Institutional Economics School of thought. Under the frame proposed by the New Institutional Economics School of though institutions and organizations are the main focus of analysis. In any case, some element of Public Choice shall be considered when required.

The main purpose of this document is to provide Provincial and District Authorities in Iraq with policy elements so they can fully understand the implications of decisions in the area of revenue assignment. Hence the paper would most of the time will follow a didactic format.

Accordingly, the first part of the document will explain what Revenue Assignment is and its overall role in fiscal intergovernmental relations. To this purpose it will look at the way the fiscal arrangement for decentralization operates as a standard of international practice. This will be done by looking at cases of more economically developed States embracing sound international practices and drawing some ideas from these experiences. It is not strange the research finds there is large room for improvements in this area in Iraq.

The second part of the document shall focus on revenue assignment as such and on how this would apply to Iraq. The document looks at correspondences between fiscal federalism principles and sound international practices in revenue assignment, contrasting them with the

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[1] The issue is first identified by Ronald Duncan and Christine Fletcher in the article "The Economic and Political Challenge of Equity" inserted in the book "Equity & Development across Nations-Political and Fiscal Realities. The Australian National University. Canberra 1996.

[2] In this regards see the overview "Understanding Economic Change" by Douglas C. North in the book Transforming Post-Communist Political Economies. National Academy Press. Washington DC, 1997.

[3] Sic. The authors suggest "what concerns people most is not absolute levels of income but changes in relative income"

rules contained in the Iraqi Constitution. In this section short term and medium term proposals are presented. For the medium term proposal LGP benefited from the exchange of concepts and viewpoints with experts of Econ II project by USAID. During 2006 Econ II experts provided assistance to the Tax Policy Unit of the Ministry of Finance in Iraq for the preparation and issuance of a document namely: "A Plan for the Overhaul of the Iraqi Tax System"[4]. The document was presented to and discussed with other areas of the Ministry of Finance, and other Federal offices. In that document for the overhaul of the tax system in Iraq, a proposal for intergovernmental tax sharing structure was suggested after discussions and advice from LGP.

The third part of this paper is dedicated to the analysis of roles and responsibilities within the current framework for intergovernmental relations in Iraq. Though this framework is not entirely new, it has evolved recently in diverse ways and it is important to observe in a comprehensive fashion. For the content of this third part LGP has undertaken considerable research. This third section also analyzes the mechanisms for implementation of federal revenue distribution as proposed in the Constitution. Emphasis is placed in the representation of the governorate authorities in the public body for monitoring—audit and appropriation--of federal revenues as described in article 106 of the new Constitution.

In the Appendix some examples of fiscal arrangements in other countries is presented. Also in the Appendix there is a description of the methodology followed to establish the level of fiscal participation of sub-central governments in the overall public expenditures of Iraq. This exercise follows standard OECD methodology. In addition, a table-matrix with suggested distribution of roles and responsibilities proposed by LGP1 is inserted as reference on potential changes in this area.

To facilitate reliable reference sources for readers the document primarily but not exclusively uses examples from OECD countries. This is because they are current and well documented, which allows for more systematic observations. However sometimes non OECD states are also mentioned.

[4] Michael Dunn, Tax Policy and Macro Fiscal Analyst, Bearing Point, December 7, 2006.

## CONCLUSIONS

1- Iraq is in an interim period following the declaration of the federal state by the new Constitution. Several key legislative pieces require to be issued in a harmonic and integral manner, including those related to intergovernmental fiscal matters.

2- The country remains strongly centralized and initiatives to foster fiscal decentralization though important, still fall short compared to what the Constitution asks and the sub-central authorities and general public seem to expect. Fiscal centralization continues being an obstacle for improving living standards and basic service delivery across Iraq. Adopting international practices can help Iraqi authorities find options to reach a fiscal intergovernmental arrangement that simultaneously complies with the Constitution and properly addresses sub-central authorities and general public expectations.

3- Fiscal federalism principles can help to enhance fiscal devolution in an orderly fashion. Orderly devolution facilitates obtaining the benefits expected of a properly implemented decentralization process. International practice demonstrates fiscal federalism applies to the federal state and to the unitary state alike. Fiscal federalism practices imply effective devolution of fiscal powers to the sub-central authorities.

4- Revenue assignment is only one element of the overall intergovernmental fiscal arrangement. In research literature revenue assignment refers to the empowerment of each tier of government to raise revenue. Revenue raising powers need to be accompanied by clarification of roles and responsibilities to have impact on the overall delivery of services by the State. These powers can be absolute on certain sources or can be part of a tax sharing arrangement. Research literature also recognizes that a stable and well directed policy of intergovernmental transfers can produce similar effects as experienced in a proper arrangement for revenue assignment. Intergovernmental transfers in Iraq and other countries are relevant to enhance territorial fiscal equalization mandates. Sound international practices show there are always some revenue raising powers at the sub-central tiers of government to ensure relevant levels of fiscal autonomy. Relevant levels of sub-central fiscal autonomy are usually needed to facilitate reaping the many benefits of any decentralization process.

5- Revenue assignment in Iraq seems substandard when compared to a sample of OECD countries. By analyzing the share of sub-central authorities in total budget revenues in Iraq it is evidenced their participation is extremely low—0.07% while other countries in the sample show participation above 11%. Because a policy of transfers can supply for a proper revenue assignment based on tax authorities or tax sharing mechanisms the best indicator for fiscal decentralization is the share of sub-central authorities in total expenditures. In Iraq by using the federal budget as reference the share of sub-central authorities in state expenditures surrounds 16% while in the other countries it is above 28%. An additional indicator of positive fiscal decentralization refers to the empowerment of sub-central authorities to set tax base and tax rates, there is less agreement on the usefulness of this indicator because it is rather difficult to elaborate, however it could be acceptable to use it as a measure as Iraq sub-central share in setting tax basis and tax rates approximates 0.8% and in the other countries in the sample is above 9%.

6- International practice supports basic revenue assignment principles. Practical application of these principles for Iraq is proposed in the Table 3- An idea on assignment of non-oil revenues. The proposal for Iraq is based on a tax sharing arrangement.

7- Because the revenue assignment is only one element of the overall intergovernmental fiscal arrangement it can not be observed in isolation of the other elements. The fiscal arrangement usually comes from constitutional mandates or legal traditions. In Iraq the main elements of the fiscal arrangement are in the Constitution and refer to territorial fiscal equalization and sharing of: (a) revenues and (b) roles and responsibilities, among tiers of government. Because In Iraq an average of 93% of all State fiscal resources come from the sales of oil there is need to include the sharing of oil revenues in any intergovernmental fiscal arrangement. The Constitution has specific rules for this process in article 112. In addition, turning the non oil revenues into a relevant revenue source calls for a large tax overhaul of the tax system that can take years.

8- To address the problem of intergovernmental fiscal relations research literature identifies several useful approaches. In all approaches the main element is the need for fiscal rules. Fiscal rules are usually elements of an overall fiscal framework. In article 106 the Iraqi Constitution orders a cooperative and participatory approach between Federal & sub-central levels of government in the definition of intergovernmental fiscal relations. This is done via the creation of a public commission to monitor—audit and appropriate in some translations—federal revenues according to formula and with the participation of federal, governorates and regions experts and representatives of the governorates and the regions. The same article 106 established the principle of territorial fiscal equalization. Furthermore in article 112 the Iraqi Constitution emphasizes the principle of fiscal equalization with oil revenues should be per capita based and should cover the whole country. The article 112 emphasizes the distribution of oil revenues must give special consideration to provinces that suffered deprivation and destruction and must also pursue balanced development of all areas in the country. This in gross terms is the fiscal arrangement proposed by the new Constitution in Iraq.

9- Fiscal intergovernmental arrangements need to be expressed in the fiscal framework. The fiscal framework contains the fiscal rules for the implementation of the arrangement. These fiscal rules are aimed to guarantee the sustainability of the overall fiscal balance and hence moderate the fiscal powers of sub-central levels of government without totally eliminating them. A tax sharing framework is advisable for Iraq in the medium term. This is because the current tax system needs a full overhaul before it can become a relevant source of revenues.

10- Because both articles—106 and 112--of the Iraqi Constitution require to be further developed by law this paper suggests the same public commission that should ensure fair distribution of all federal revenues must also be in charge of monitoring the distribution of oil revenues. For that purpose a sub committee inside the public commission can be arranged. The suggestion comes out of the positive lessons from international practices regarding the use of this type of public bodies to address intergovernmental fiscal issues. Comparable commissions include the Commonwealth Grants Commission in Australia, Financial and Fiscal Commission in South Africa, Council for Fiscal and Financial Policy in Spain, and Join Commission in Poland.

11- To grantee proper representation of the governorates in the public commission of article 106 of the Constitution, the current Governorates Coordinating Committee could be given that role in the same law that creates the public commission. International practice in Poland and Spain demonstrates the participation of the sub-central authorities in these bodies for policy dialogue is beneficial. The case of Poland specially demonstrates the benefits in using Local Government Association type bodies to address the participation of the sub-central authorities in a permanent policy dialogue body, for instance the Join Commission in Poland.

12- In the short term fiscal intergovernmental relations in Iraq will continue more focused on the redistribution of fiscal wealth by the Federal Government via transfers. In the medium term once the overhaul of the tax system takes place it is foreseeable to go into a mixed mechanism of transfers and tax sharing to supply the country with a proper and sound fiscal decentralization framework.

13- In the short term is important to start moving form the current total centralization of revenues to a framework that allows more possibilities for the governorates to exercise their revenue raising powers. It is better to set up sound fiscal rules regarding tax rates and tax basis than continuing with the current total prohibition. Transfers also need to be more flexible to allow governorates and Districts to undertake maintenance and operational expenses so that they can develop their own cadre and administrative capacities to improve the delivery of services.

14- In the short term it is important to modify the current intervention by the federal authorities on all aspects of fiscal life in the Districts. Qada'a Councils need to be allowed major involvement in district's fiscal issues and in the delivery of basic services. It is also important to modify the current funding arrangement—matching grant from the federal government to the municipalities—Beladiyas—transferring the control on these funds to the Qada'a councils and changing the criteria to determine the size of the transfer. Currently the transfers to the Qada'as are determined on basis of historic fiscal capacity and operational cost, this needs to be shifted into a needs assessment based determination. Also Qada authorities need to be allowed to participate in the offices and boards of the SOEs in charge of water, sewage and electricity.

## I. REVENUE ASSIGNMENT PRINCIPLES AND APPLICABILITY TO THE EMERGING IRAQI STATE

Revenue assignment is only one factor in the equation of intergovernmental fiscal relations. Intergovernmental fiscal relations are sometimes referred as to the glue that keeps together the contemporary State[5]. While this unifying effect is easier to observe as a day to day happening in states such as Germany, Switzerland, Canada or Australia, it is less evident in others such as the United States of America. The utilization of tax sharing structures between the central and sub central governments is well extended however it is not the only way to address revenue assignment. Current research in fiscal intergovernmental relations recognizes a sizable and stable grants transfers' structure—found in both the USA and Australia--can produce similar results as a tax sharing structure, for revenue assignment purposes[6]. In the case of the USA the states and in Canada the provinces enjoy large tax autonomy while in Germany and Australia this is more limited, however in all four countries their sub-central territorial governments have a base of own revenues that ensures levels of fiscal autonomy.

**Box 1**
**National unity and the promotion of national objectives does not in it self require strong centralization of revenue collection**

*Walsh Cliff. Intergovernmental fiscal relations in unitary systems and federations. Australia as a model. Article in the book Equity and Development-Political and Fiscal Realities. The Australian University. Canberra. 1996*

Despite the issue of revenue assignment could be though of as an institution of the federal state, it is not. In fact unitary states have forever had this type of arrangements too but in an effort to impose the power of the central authorities they tended to make them unapparent or unimportant. In most cases the intergovernmental fiscal arrangements in the federal state were more transparent. Transparency facilitated the study of revenue sharing structures in the federal state despite the fact they are common to all types of states. Hence, it is not estrange the studies available on the subject are framed under what is being called "Fiscal Federalism" or simply fiscal decentralization.

Fiscal Federalism is a set of principles that ensure decentralization and devolution occurs in our contemporary State in an organized and beneficial manner. It is supported intellectually and academically and is universally accepted as a unifying model beneficial to both the Unitary and Federal State. This is important as orderly devolution of powers usually enhances living standards and content of the inhabitants[7]. To a large extend in a decentralized environment the tier of government provider of the most authority and services is the one closer to the recipient—communities and citizens. Fiscal Federalism is not the only way of addressing fiscal devolution but it is a congruent set of rules that allow addressing the process of fiscal devolution in an orderly manner. Fiscal Federalism principles are illustrated in appendix A of this paper.

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[5] The Economic and Political Challenge of Equity by Ronald Duncan and Christine Fletcher. Article inserted in Equity & Development across nations-Political and fiscal realities. The Australian National University. Caberra. 1996

[6] Tomas Lubach—Fiscal Relations across levels of Government in the United States—quoting work by Knight , 2002 and Gordon, 2004, while analyzing federal highways funding and Title 1 education spending. OECD Economic Department working papers, Nov 2005.

[7] Cliff Walsh. Intergovernmental fiscal relations in unitary systems and federations-Australia as a model. Article in Equity & Development across nations-Political and fiscal realities. The Australian National University. Camberra. 1996.

**Revenue assignment and its principles**

The legal arrangement that defines what the revenue raising powers of each tier of government are in a given State is the revenue assignment[8]. A revenue source may be either assigned on exclusive basis to a specific tier of government or can be shared by several tiers. Overall the principles to properly define the right distribution of revenue raising powers among tiers of government help to guide any decision in this regards. The most commonly accepted principles to follow for a sound revenue assignment are[9]:

Efficiency of the internal market Often quoted as the one principle to be complied with when designing a revenue assignment structure. To ensure efficiency of the internal market the revenue raising legislation must prevent uncoordinated setting of taxes. When each territorial entity is allowed to freely set any type of taxes each tax structure may end up differing in its rates and its basis. This promotes fiscal competition where the territorial jurisdiction with the lower tax would be chosen by taxpayers to perform transactions on capital and tradable goods based only on tax advantages and not in marked objective elements of efficiency. Also this situation may increase administrative and compliance cost to entrepreneurs willing to work in more than one territorial jurisdiction. In addition the need to compete by lowering tax burdens would lead to taxes that would generate revenues well below both their potential and the needs and expectations of the governmental tier hoping to fund its operation from these revenue sources.

National Equity or equalization It is a principle to consider when defining revenue rising powers by the diverse tiers of government. The best way to achieve some level of equalization nationwide is by leaving the main redistributive role in hands of the Federal Government. This does not preclude the role of the sub-central governments that may want to improve internally whatever national equalizing policy in place. To the purpose of facilitating the Federal Government role in fostering equalization it is customary to allow access to the Federal Government to taxes that are redistributive in nature—income and wealth taxes. This does not need to happen on exclusive basis. A tax redistributive in nature can be shared by all tiers of government however there is need to ensure the share of the Federal Government is adequate to provide it with enough resources to make the national redistribution meaningful.

Minimization of administrative and compliance cost Another principle to follow when establishing intergovernmental revenue assignment schemes. Both the administrative and compliance cost affect the public sector and the taxpayers. One way to keep the cost in check on both sides is by resorting to joint collection administrative mechanisms. Another feature desirable to keep the cost in check is to resort to broad base taxes and having tax rates as low as possible.

Fiscal Accountability Also recognized as a principle to observe when defining intergovernmental revenue raising schemes. This can be better granted if the corresponding level of government is provided with authority on taxes it actually can handle. Access to revenue sources must be matched as closely as possible to revenue needs.[10]

Harmonization Despite of harmonization being handled in the research literature as a feature of tax decentralization it is in fact a principle of revenue assignment. Tax harmonization or tax cooperation looks after preserving the advantages of autonomous decision making by the sub-central tiers of government on some predictable amount of fiscal resources. This is achievable without jeopardizing overall economic efficiency in the market created by the

[8] Fiscal Federalism: Principles and Practices. Ch.5 by Robin Boadway and Anwar Shas. World Bank—Working Paper. 2006
[9] Ibiden 6
[10] Ibiden 6

territories composing the State. Under this principle, solutions such as: (a) revenue sharing, (b) state surtax or Tax on base systems, are contemplated.

All these principles apply to a potential revenue assignment scheme for the Iraqi State emerging from the new Constitution of 2005. The legislation in place allocates some revenues to the districts; and although nominally still belonging to the districts[11] these revenues have ended up under control of the Federal Government. As well these revenues to the districts are depending on national legislation for definition of rates, tax basis and in the administration and disposition of the amounts collected. With the fall of the dictatorship in 2003 the governorate administrations have been given wide tax powers that required implementing legislation that was not subsequently enacted. The only revenue the Governorate authorities find indisputable is the 5% surcharge—althma'am—granted to them in number 1) of Section 8 of Law 71 of 2005—CPA order 71 of 2004[12]. The Federal Government that is entitled to collect broad base taxes on income and consumption anyhow has evolved slowly in the overhaul of these taxes to turn them into more relevant revenue sources. This slow phase in the overhaul of taxes follows a path of less resistance and relevance of controlling the largest source of all governmental revenues in the country-that of oil receipts.

With the adoption of the new Constitution the governorates were reaffirmed in their right to autonomous finances however there remained some doubts as to their legislative powers. The existence of constitutionally endorsed legislative powers for the governorate representative bodies recently received judicial support. This judicial support came in the form of an opinion by the Supreme Court in answer to clarifications requested by the Council of Representatives on this and other issues[13].

In Iraq there is no other source of revenue that can provide as much inflows to the Treasury as those coming from oil. Informed by this situation the new Constitution sets up a special mechanism to handle the intergovernmental distribution of oil based fiscal wealth. In addition, the new Constitution ordered a more general process to define the intergovernmental distribution of all fiscal resources concentrated at the Federal Government level. All this indicates the revenue equalization in Iraq needs to have a vertical emphasis. The concentration of fiscal wealth in the federal level means the Federal Government would need to act as the re-distributor, at least at the beginning. To ensure this top-bottom approach does not hamper horizontal equalization efforts the Constitution contains a mechanism to make the distribution of federal fiscal wealth a participatory process where the obvious distributor—Central Government--can not impose unilateral terms to the other levels of government. Concrete suggestions to the implementation of this process will be presented further below in part III of this document.

### Respect for Sub-central Fiscal Autonomy. What are the boundaries?

Fiscal autonomy refers to the faculty of a given tier of sub-central government to assemble its budget. This means control over revenue sources and authority in expending these moneys according to needs identified by their jurisdiction. An institutional process—meaning legal and administrative procedures and entities--for budgeting in the sub-national tier of government it is required. In all cases the autonomy of each tier of government is assessed by the legal capacity to: (a) enact taxes (b) control the tax base and the tax rates and (c) to resort to

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[11] Baghdad city has been an exception to this. The Amanat of Baghdad—Office of the Amin or Mayor—has wide technical capacity and controls most of the taxes of the city and successfully coordinates budget implementation with the central ministries

[12] Despite legal the collection of the surcharge by the governorates has faced stiff resistance from the Ministry of Finance

[13] Iraq's Supreme Court. Advisory Opinion of July 31st 2007 on 4 constitutional issues. Widely commented in detail in the legal policy paper number 14 of October 26, 2007 by Dr. Vijaya Samaraweera, Team Leader of the National Policy Team of LGP/USAID-Baghdad

other sources of revenues. Similarly the power to decide on expenditures to take place inside their territorial jurisdiction is part of the fiscal autonomy.

**Box 2**

**In most OECD countries central governments impose limits on tax rates and tax relief that can be set by sub-central governments, but most posses some tax autonomy.**

**Granting sub-central governments some autonomy over (mobile) tax bases can introduce conditions conductive to tax competition, which can serve to restrain the growth on the aggregate tax burden and as such the overall public sector.**

*Douglas Sutherland, Robert Price and Isabelle Joumard. Fiscal rules for sub-central governments: Design and impact. OECD. Economics Department. Working paper 456. 2005.*

Sub-central levels of government need to have some level of revenue raising powers to preserve and reinforce fiscal autonomy. How much is the right share of power in this area is the subject of most discussions world wide. As in all true democracy no power is absolute so the fiscal powers of the sub-central governments in this aspect can't be absolute either. In fact the existence of any State is based on the capacity to negotiate and resolve do day to day concessions to remain unified despite ethnicity, beliefs or any other difference of choice[14]. This is so regardless of the character of unitary or federal a country as such may have adopted.

## International Experiences and Practices

**Box 3**
**There is relatively little dispute about the merits of decentralizing expenditures responsibilities.**

*Robin Boadway and Anwar Shah in Chapter 5, Fiscal Federalism, of the Paper Revenue Assignment. World Bank, working paper*

To better understand how the intergovernmental fiscal arrangement works we seek comparisons from similar international experiences and practices.

Revenue assignment is just one factor in the intergovernmental fiscal arrangement. The intergovernmental fiscal arrangement sets up the overall framework for fiscal decentralization and as such contains the fiscal rules and enforcement mechanism to make it workable. To illustrate this topic we will resort now to examples of fiscal arrangements and resulting fiscal frameworks in OECD countries.

Recent studies by OECD[15] on the subject of revenue assignment illustrate how in developed countries with federal state structure it is easier to devolve service delivery responsibilities than to agree on devolution of revenue raising powers. A similar conclusion can be extracted from recent experiences of States that have undergone large reforms due to fundamental regimen changes—e. g. South Africa--, or needed to stabilize the situation in disgruntled separatist regions. Worth mentioning as well the devolution of revenue raising abilities is a lot more difficult process in unitary states. Table 1 illustrates the case of how much the revenue raising powers by sub-central levels of government is a feature of more developed states.

[14] In this regard Cliff Walsh sustains: "Decentralization, in principle, allows for greater self-expression". Intergovernmental Fiscal Relations in Unitary systems and Federations. Article in Equity & Development across nations-Political and fiscal realities. The Australia University, Canberra, 1996.
[15] Fiscal Rules for Sub-Central Governments: Design and Impact. OECD, Economics Department, 2005

**Table 1. Sub-national Revenue rising powers vis-à-vis**

**Participation in total Revenues and Expenditures**

| Federal Countries | % of Sub-national spending in the total Public Sector (2001) | % of Sub-national revenue in the total Public Sector (2001) | Sub-national discretion to set tax rates and/or tax bases (as % of tax basket) |
|---|---|---|---|
| Austria | 28.5 | 21.4 | 9.5 |
| Belgium | 34.0 | 11.3 | 57.9 |
| Canada | 56.5 | 49.9 | 100 |
| Germany | 36.1 | 32.4 | 12.8 |
| United States | 40.0 | 40.4 | -- |
| Iraq (*) | 16.0 | 0.07 | 0.8 |

- Source for OCDE countries: OCDE, Economic Outlook 74. 2003—V. Fiscal relations across levels of government. Table extracted by the author.
- (*): Includes 17% share in the divisible pool planned as transfers to the KRG. Total shares calculated on a three years projection following OECD methodology
- For details on the calculations for Iraq please see Table C in the Annex

OECD studies show there is not a direct relation among: (a) the level of revenues, (b) the share on expenditures and (c) the share in revenue raising powers that a tier of a sub national government has. This also demonstrates that the fiscal importance of the sub-central governments is not tied to the character of federal or central state a society has adopted; table 1 above illustrates these aspects. Research indicates how tax harmonization and cooperation is paramount to a sound fiscal arrangement.

**Box 4**
**There are significant differences across countries in the sub national share of government spending and revenues-The most conventional yardstick for measuring fiscal decentralization. Moreover, the importance of sub-national governments is not linked to whether a country has a unitary or a federal government. Sub-national governments already account for higher share of general government expenditures in some unitary countries, particular the Nordic and continental European countries, than in constitutionally-defined federations, such as the United States and Germany.**

*OECD. Economic Outlook 74. Chapter V. Fiscal Relations Across Levels of Government. 2003*

The obvious conclusion to any application of fiscal federalism principles is the development of mechanisms to redistribute fiscal wealth in ways all the participants find is fair. Fairness on one hand implies that the mechanism adopted counts with the active participation of sub-central governments so they find it transparent. Transparent means that all participants believe the intergovernmental equalizing deal is fair, administered fairly and is enforceable. Enforceability means not only that the Central Government is liable for not complying with its share it also means that there must be reasonable measures to enforce compliance of sub-central governments. All the elements needed to implement this are usually contained in the intergovernmental fiscal arrangement.

**Box 5.**
**Fiscal equalization is a transfer of resources across jurisdictions to offset disparities in revenue raising capacity or public service cost.**

*From: Fiscal Equalization in OECD countries, OECD Economics and Governance Departments. Paper 4, 2007*

## How do fiscal intergovernmental arrangements work?

Fiscal science has not arrived on a universal model of dealing with the intergovernmental fiscal arrangement but there is concurrence on the principle that intergovernmental fiscal arrangement needs to respect the overall fiscal balance[16]. Within the intergovernmental fiscal arrangement there is a set of foundational rules that guide the process of political and technical distribution of fiscal resources of a country. This process usually follows very general rules dictated in the constitution, legal dispositions or traditions of a specific country. When the intergovernmental fiscal arrangement includes rules for a negotiation process this negotiation takes place between the central government and the sub-central tiers of government. The negotiation process of the distribution of fiscal resources is a distinctive feature in many democratic countries. Countries with non participatory fiscal arrangement usually fall into the mistake of ignoring regional and provincial aims, which is a factor among the ones that promote independent or separatist aimed movements[17].

Intergovernmental distribution of fiscal wealth is frequently tied to the fiscal equalization goals. Fiscal equalization—the equalizing deal--is an important element that can be addressed via distributing revenue raising capacities or via covering differences in cost for delivering public services—also called public service cost equalization method[18]. In this section we have focused mainly in distribution of revenue raising capacity as public service cost equalization requires levels of elaboration that Iraq nowadays may not be able to undertake. In addition, international practice shows that revenue equalization leads to less often adjustments—every five years average—facilitating more stability while public service cost equalization usually demands adjustments almost every other year[19].

Satisfactory fiscal capacity equalization is an effective way to demonstrate the equal consideration a State gives to its citizens regardless of the many differences they may like to pledge as existing among them selves. This could easily be identified as the way federal states overcome differences. This way to generally overcome differences has been accepted by most all current states around the world, regardless of their federal or unitary structure.

International experience demonstrates that an intergovernmental fiscal arrangement must respect the overall fiscal balance to be successful[20]. If the aims of sub-central governments constantly push the overall size of expenses in the public sector to levels that private sector

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[16] In a simplistic way the overall fiscal balance can be defined as the level of resources the government can appropriate in the economy without creating generalized economic imbalances. Is simply measured as the level of deficit or surplus the consolidated public sector can afford without discouraging private activity. E.G.: Recently one of most problematic aspects in the European Union has been the target for fiscal deficit the member states should meet.

[17] Of course this is not the only factor for separatist attitudes, but when fiscal punishment or even the perception of unfair fiscal consideration is added to ethnicity or religious differences the cocktail is more explosive. Recent examples are Scotland in the United Kingdom and Some Regions in France, but also Darfur in Sudan.

[18] Hansjorg Blochinger, Olaf Merk, Claire Charbit, Lee Mizell. Fiscal Equalization in OECD. Economics Department and Governance Department. OECD, 2007.

[19] Cost equalization calls for more politicized activity in the definition of intergovernmental fiscal relations enhancing instability. Revenue sharing on the other hand allows for more time to until its effects set in. For further elaboration see Robin Boadway and Anwar Shah in “Fiscal Federalism: Principles and Practices. World Bank Working paper, 2007.

[20] Germnay, Spain, Italy and Austria are examples of this.

finds unacceptable the overall fiscal balance is disrupted, financial resources get misallocated depriving private sector from accessing them on a competitive basis and the necessary trust to ensure private entrepreneurial participation in the economy decays. Many countries have found ways to accommodate the fiscal aims of their communities in the territorial entities without disrupting the overall fiscal balance. This is done by using the intergovernmental fiscal arrangement to adopt a workable intergovernmental fiscal framework. An intergovernmental fiscal framework contains the fiscal rules and the enforcement mechanisms to handle the complexities intergovernmental fiscal relations demand. The Fiscal framework is the conclusion of the negotiations under the fiscal arrangement.

Intergovernmental fiscal framework can be shaped in diverse ways. Lately it has been common to adopt a stabilization pact between the central government and the sub-central governments as part of the general intergovernmental fiscal negotiation[21]. Formality and the ways compliance with the intergovernmental fiscal framework is handled often differ among countries. One way to address compliance with the intergovernmental fiscal framework is the cooperative approach. In the cooperative approach all levels of government work with agreed upon targets on fiscal balance and how to share any surpluses. There are temporary measures that can be taken if one participant does not follow or meet targets and there are escape clauses available in cases of exceptional circumstances.

Another way to handle the compliance with the intergovernmental fiscal framework is by adopting a fully fiscal rules based approach. Under the fully fiscal rules based approach all levels of government have to comply with the stabilization of their own finances—no deficits are allowed[22], however escape clauses remain for exceptional cases.

A further way to handle the intergovernmental fiscal framework is not to have any formal coordination among tiers of government. Basically every participant follows its needs and manages its fiscal resources at will allowing financial market forces to regulate how far they can go. For this approach an advanced open market economy and non state banking sector is needed and a very satisfactory distribution of revenue raising authorities among tiers of government must exist. This financial marked forces control approach to compliance with the intergovernmental fiscal framework does not apply to any transition economy and even less to Iraq. Table No.2 below summarizes the main elements of the intergovernmental fiscal framework in diverse countries.

**Box 6.**
**Poland's mid-level decentralization reform in 1999 was an immense undertaking that included administrative, political, and fiscal decentralization, as well as territorial re-division of the state. The goals of the reform were to bring government closer to the people, improve public services, and further "de-communize" the public bureaucracy. However, a closer look at the level of social services provision reveals many unfulfilled promises and unintended consequences of decentralization.**

*Janelle Kerling. Poor Decentralization Policy Burdens Poland's Social Services. Beyond Transition News Letter, May-June 2002. World Bank, Washington D.C.*

It is important to remark that without consensus between the sub-central governments and central government any fiscal framework will fail. Most recent examples from Poland and Spain demonstrate how important the fiscal part of any initiative for decentralization tied to a commonly agreed upon fiscal framework.[23]

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[21] Ibiden 17.

[22] This approach is criticized because it does not allow taking advantage of short term opportunities and is too much pro cyclical, exceptional circumstances are always part of the deal.

[23] According to recent World Bank studies lack of consensus in the fiscal design of the decentralization reforms in Poland created the current situation of services disarray and scattered unfunded mandates in social services to the local authorities. This situation is removing many potential gains to be made out of any decentralization process due to lack of proper resources to match the devolved and delegated

## Table 2- Intergovernmental Fiscal Arrangement in Selected OECD Countries

| Country | Intergovernmental Fiscal Framework | Enforcement Mechanisms |
|---|---|---|
| **Austria** | **Cooperative Approach** ***A domestic stability pact*** requires the municipalities to balance their budgets and set a surplus target for the Lander (Region)<br>**Borrowing** No restrictions on borrowing by the Lander. Municipal borrowing is regulated by the Lander | **Peer Pressure and financial sanctions** No compliance fines are reimbursed if compliance is restored within one year or allocated across the complying jurisdictions, otherwise<br>**Escape clause** in case of serious economic slowdown |
| **Spain** | **Fiscal Rule** All levels of government face a ***balanced budget constraint.*** Tax powers by the autonomies is centrally controlled<br>**Borrowing** Subjected to Golden Rule and ministerial approval depending on the debt service burden | **Administrative sanctions** A fiscal consolidation plan is required for non complying jurisdictions<br>**Financial sanctions** European sanctions are shared with non complying jurisdictions |
| **Germany** | **Cooperative Approach** ***A domestic stability pact is in place.***<br>**Borrowing** Most of the Landers face a golden rule. Municipal borrowing (subject to golden rule) requires Lander approval | **Peer pressure** The Financial Planning Council monitors fiscal developments at all levels of government and makes recommendations for restoring fiscal discipline in event of non-compliance |
| **United States** | **No Formal co-ordination** Most states have ***balanced-budget constraints in state constitutions***<br>**Borrowing** No restrictions | **Market Discipline** The federal government does not grantee sub-national loans |

- Source: OCDE, Economic Outlook 74. 2003—V. Fiscal Relations Across Levels of Government. Table extracted by the author.
- Golden rule: Borrowing is only allowed for capital investment projects and the tier of government that borrows should be able to pay back with its own resources.

Another important aspect to consider when analyzing the fiscal framework for decentralization is the frequent change of aims by communities in the sub-central tiers of government. Intergovernmental relations are a living process and the institutions organized to deal with this process need to have permanence to be able to reflect the constant changes created by the evolving intentions of different communities.

Even when compliance with an intergovernmental fiscal framework is based on a cooperative approach many fiscal rules apply. When developing a fiscal framework minimal rules must apply. They must also apply on the supporting institutions.

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tasks. "Poor Decentralization Policy Burdens Poland's Social Services." Article in: Beyond Transition News Letter by Janelle Kerlin—Urban Institute Visiting Dissertation Fellow. World Bank, Washington, May-June 2002.

## What are the fiscal rules?

Today the most common fiscal rules in OECD countries include[24]:

- Budget Balance Requirement
- Tax and expenditure limits
- Borrowing constraints
- Process rules and rules implementation

**Box 6**
**Fiscal rules are a set of institutional constraints on policymakers' decision-making discretion. Such rules may be imposed on sub central governments by a higher level of government, or sub-central governments may adopt them themselves where constitutional arrangements grant them autonomy to do so.**

*Douglas Southerland, Robert Price and Isabelle Joumarr. OECD Economics Department. Working paper 465, 2005*

International practice indicates that there are not ideal sets of fiscal rules. In OECD countries fiscal rules differ as countries differ on Constitutional mandates and welfare functions[25]. This means each country needs to find its own set of fiscal rules according to its priorities and make sure there are mechanisms that can adjust the rules in a consultative manner when priorities change. International practices can be useful reference for finding the right rules and consultation mechanisms to reflect changes.

Fiscal rules must be simple, clear and targeted to the priorities of the specific country. Overall fiscal balance is the only universal paradigm in fiscal rules, however there are cases where it can be also discussed[26].

When the priority is fiscal equalization, as is the case of Iraq, it is important to understand that the redistribution refers only to fiscal wealth. A wealthy territory can not be forced to share its own total economic wealth. However the fiscal wealth is an aspect that is commonly accepted must be shared within clear rules and limits. Different thing is that a source of wealth located in a territory is deemed Federal property or common wealth to all inhabitants in the country. In that case the source of wealth needs to be part of the national fiscal resources as the national authority is the only one with that kind of comprehensive representation.

As mentioned above the intergovernmental fiscal arrangement translates into an intergovernmental fiscal framework. The intergovernmental fiscal framework is the set of rules under which all participants agree to live in. Fiscal rules for intergovernmental fiscal relations are hence a very important aspect of the intergovernmental fiscal legislation.

The most common fiscal rule is the budget balance requirement. As illustrated in Table 2 above, either by their initiative or as consequence of the fiscal stabilization pact[27] the sub-central governments look after fiscal balances and only set forth surplus targets when this is part of the overall redistributive scheme--E.G. Municipalities in Austria. It is important to define who is to retain this redistributive role as the access to significant revenues must be allocated to that specific level of government. We have explained above the redistribution role works better when in hands of the Central or Federal Government, but no unilateral impositions from this level of government can be acceptable if this is going to work for all participants.

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[24] Douglas Sutherland, Robert Price and Isabelle Joumard. Fiscal Rules for Sub-Central Governments: Design and Impact. Working Paper No. 465, conclusions. Economics Department, OECD. 2005
[25] Ibiden 18
[26] Ibiden 17
[27] Nowadays Germany, Italy, Spain and Austria are examples of this type of pacts

**Box 7.**
**Governments have often adopted or strengthened fiscal rules at the sub-central level to correct or pre-empt unsustainable increases in debt or public spending.**

*Douglas Southerland , Robert Price and Isabelle Joumard. Fiscal Rules for Sub-Central Governments: Design and Impact. OECD's Economics Department, 2005*

Limiting revenue raising faculties is never done at the expense of suppressing fiscal autonomy. Common mechanisms to control revenue raising faculties imply control on tax basis and on tax rates by the central government. In Iraq the revenue rising faculties provided to the local tier of government presents a very inflexible and out dated design. Most rates are specific—a fixed amount of money—without any adjustment for inflation or currency depreciation, etc. In addition the local authorities have no entitlement to adjust rates. Despite there is faculty to properly adjust the tax base of some taxes—especially property taxes—the technical resources available reduces the potential collection to medium and large urban centers with technical capacity. In addition since 2007 the overall design for funding of local entities presents disincentives to enhancements of local fiscal effort.

Regarding the governorates, the flexibility and relative autonomy for this tier of government to start collecting their own revenues have been hindered by the lack of clear legislative powers. In a recent opinion by the High Court of Justice these legislative powers were judged to exist and it is now a matter of when these powers would be fully exercised rather than how they would be exercised. In any case opposition by the federal authorities to the exercise of the revenue raising powers by the governorates has been expressed via a cabinet letter and verbal statements indicating that any revenue collected by the provinces would be faced with a corresponding reduction in federal transfers. Many governorates hesitate in undertaking their legitimate right, not wanting to upset the Federal Government. All governorates have delayed the adoption of comprehensive tax frameworks that can also benefit the Districts and sub-districts, again often due to federal authorities' opposition.

In section II below this document elaborates on the potential improvement to provincial and local revenue raising powers in Iraq.

**Box 8.**
**Sub-central governments in most the OECD countries possess some tax autonomy. Central Governments usually impose limits on tax rates and relief that can be set by sub-central Governments.**

*Douglas Southerland , Robert Price and Isabelle Joumard. Fiscal Rules for Sub-Central Governments: Design and Impact. OECD's Economics Department, 2005*

Fiscal rules rarely refer to sub-central spending and rather focus on limiting access to credit and revenue raising faculties. This is because sub-central spending is more politically-sensitive. And, for properly control it would require a lot of rules. Enforcing many fiscal rules would involve large central level government micromanagement which is expensive, demanding, often resented as intrusive and hence ineffective. In Iraq sub-central expending and revenue raising faculties are tightly controlled by the central government. Even the current system of transfers to the governorates, which is the most flexible feature of the current intergovernmental arrangement, has strong centralizing controls and legal limitations. At district level the control on expenditures is even greater as no expenditures decision can be made by the district authorities without the consent of the representatives of the Ministry of Municipalities and Public Works—MMPW--in the governorate. In fact, the control of all public finances in the districts is in hands of the offices of the MMPW in the district—beladiyas—and not in the ones of the representative body—Qada'a councils.

**Box 9.**
**In Iraq there are not budgets as such being prepared by sub-central administrations. At the Governorate level the authorities prepare a list of projects to justify the application of funds transferred for public capital investment. Giving some level of autonomy for the provinces to decide on this portion of the capital investment budget is a step in the right direction. Governorates are evolving fast and assuming larger functions thanks to this process of transfers. Governorates also prepare a budget request for operational and maintenance expenses of the councils and governors' offices. Provincial Councils and governors participate in a consultative manner in the preparation of the budget request by the federal ministries offices in the province but this intervention is mere protocol as their approval to these budget requests is not respected by the central offices of the ministries.**

**Box 10.**
**Local authorities in Iraq are not preparing the public budget of their territorial units. The MMPW is in charge of controlling the financial management of these administrations and rarely consults with the representative bodies. Basic services delivery is arranged through the Beladiya, the offices and SOEs in charge of water and sewage, and SOEs of the ministry of electricity in the area. All these offices follow federal ministry instructions distancing them selves from community pledges and requests. Representative bodies in the districts have the ability to coordinate services delivery in their territorial jurisdictions but the exercise of these powers is uneven and random.**

Enforcement mechanisms are necessary to ensure objective-setting budget rules are implemented. Experience shows there is no purpose in developing complex compliance indicators. International practice shows that it is more effective to foster transparency in budgetary policy by sub-central governments. Transparency and citizens' participation are closely linked, thus channels for citizens to obtain timely information on related budget decisions are key to achieve effective enforcement mechanisms. Sanctions for deviations are needed as shown in Table. 2 above, however the effectiveness and credibility of these sanctions are not fully clear.

Limitations to credit utilization usually come after the banking sector demonstrates excessive leniency with sub-central authorities. This often occurs due to a perception the central government would bailout the sub-central authorities from any potential default. Importantly increases in debt in Mexico and Japan have demonstrated the importance of having fiscal rules to foster sustainable fiscal policies by the sub-national authorities. The cases of Australia and Canada in the 90s show how the sub-national authorities opted for restrained their own policy makers from credit taking. These restrictions ensued after experiencing important downgrades in lenders international ratings. Of course this example is one where financial market oversight impacts on the choice of rules and by all means this is a feature for advanced open market economies. In Iraq with a banking system largely State owned and given the aim of resurrecting regional credit institutions any unpaid debt by the sub-central administrations would sooner or later be assimilated by the central government turning these lending operations into just another type of budget transfer. This is especially true in view of the lack of own revenue sources at the sub-central levels of government. Therefore rules for limiting credit in Iraq require different approaches as there is no market oversight and no repayment capacity by the sub-central authorities as recipients of credit.

**Box 11.**
**Golden Rule: Borrowing by any level of government, if allowed, can be only used for funding capital investment projects. Payment must also to be done with fiscal resources of the tier of government that borrowed the money.**

## II. HOW THE PRINCIPLES AND RULES ON REVENUE ASSIGNMENT COULD BE APPLYED TO THE IRAQI STATE

The new Iraqi Constitution has several elements for the intergovernmental fiscal arrangement. All of them aim to achieve levels of fiscal equalization and some principle of distribution of roles and responsibilities. A major benefit of the Constitution is that most everything can be negotiated between the diverse levels of government. This is facilitated by allowing **delegation** in each case to any power is attributed to any specific government tier.

Since 2006 the federal authorities have been trying to move towards the mandated participation of the provinces and the region in the revenues currently the sole dominion of the Federal Government. This has been done by transferring a share of the total capital investment and reconstruction funds to the governorates on a per capita basis, for their semi-autonomous disposition. It is important to note this is the first time this responsibility has been given to the sub-central authorities since the independence of the country. Although the transfers to the governorates are a very important step in the right direction it is far from satisfying the principles outlined in this document and adhering to the orders of the new Constitution.

Table 1 above illustrates the differences Iraq intergovernmental fiscal relations present compared to more economically developed countries. Giving the specifics of Iraq it is fair to say the country has a long way to catch up to a sound fiscal framework for fiscal decentralization. There are many virtues of fiscal decentralization and some have been evidenced in Iraq since 2006 with the transfer of capital investment and reconstructions funds to the Governorates. At this point in Iraq, the transfers to the governorates have provided the public sector with the very much needed effectiveness that the central ministries have not been able to provide[28].

The article 106 of the new Constitution calls for a "Public Commission" to monitor—audit and appropriate in some translations—the distribution of federal revenues. A law that would define this commission should reunite the basic fiscal principles expressed in the Constitution such as:

Participation The Commission can not be exclusive. It has to be inclusive of at least: (a) Experts from the Federal Government, the Governorates and the Regions, and (b) Representatives of the Governorates and the Regions. This means it is not only a technical public commission is also a political public commission.

Fiscal Equalization The resulting distribution of federal revenues needs to be fair meaning for that it: (a) has to pursue the entitlements of the Governorates and the Regions, (b) has to guarantee transparency and justice, and (c) has to be in accordance with established and agreed upon percentages.

**Box 12.**
**Iraqi Constitution**
**Article 106:**
**A public commission shall be established by a law to monitor--audit and appropriate in other translations--federal revenues. The commission shall be comprised of experts from the federal government, the regions, the governorates, and its representatives, and shall assume the following responsibilities:**

**First: To verify the fair distribution of grants, aid, and international loans pursuant to the entitlement of the regions and governorates that are not organized in a region.**

**Second: To verify the ideal use and division of the federal financial resources.**

**Third: To guarantee transparency and justice in appropriating funds to the governments of the regions and governorates not organized in a region in accordance with the established percentages.**

*2005 Iraqi Constitution*

Furthermore, Article 112 of the Iraqi Constitution emphasizes fiscal equalization by stating the join management of the present oil fields by the Federal Government and the producing regions and provinces is conditional on the distribution of that revenue in a fair manner in all parts of the country following certain rules: (a) it must be done accordingly to population distribution, and (b) it must provide a balanced development in different areas of the country

[28] To further illustration on this point see: Report on ARDP Funds utilization By PCs (The Sector Distribution). Discussion paper by LGPII National Policy Team, Baghdad, February 2007.

and to that purpose an allotment must be specified for a certain period of time for damaged regions that were deprived by the former regime in unjustified manner and for the regions damaged subsequently.

Arguably, the same Public Commission that must take care of Federal Revenue distribution according to article 106 can be instrumental in the implementation of the rules described in article 112, as that article does not designate any specific body to take care of it and the mission of the Public commission of article 106 fits the task described in 112.

Besides these rules set forth in the Constitution, it is important to take into consideration the ones mentioned in this paper. By following sound[29] international practices there are more chances the country would find its own accommodation of factors inside a real fiscal decentralization framework. The accommodation process requires an open exchange between the sub-central representative authorities and the Federal ones.

**Box 13.**

**Iraqi Constitution**

**Article 112:**
**First: The federal government, with the producing governorates and regional governments, shall undertake the management of oil and gas extracted from present fields, provided that it distributes its revenues in a fair manner in proportion to the population distribution in all parts of the country, specifying an allotment for a specified period for the damaged regions which were unjustly deprived of them by the former regime, and the regions that were damaged afterwards in a way that ensures balanced development in different areas of the country, and this shall be regulated by a law.**

**Second: The federal government, with the producing regional and governorate governments, shall together formulate the necessary strategic policies to develop the oil and gas wealth in a way that achieves the highest benefit to the Iraqi people using the most advanced techniques of the market principles and encouraging investment.**

*2005 Iraqi Constitution*

### What could then be the mechanism in Iraq?

The public commission to monitor—audit and appropriate in some translations[30]—the distribution of federal revenues must be a participatory body. It has to include experts from the Federal Government, the Regions and the Provinces and its representatives. Both requirements imply the commission must be a permanent body as these functions can not be accomplished in ad hoc fashion or via occasional gatherings. The commission must have permanent technical staff and must possess powers to access and follow up information on public finances relevant to the fiscal rules.

The best examples of public bodies similar to what the article 106 calls for can be found in Australia—Commonwealth Grants Commission—South Africa—Financial and Fiscal Commission, and in Spain—Council for Fiscal and Financial Policy. In the research literature the grants commissions have been recently accused of making their task more complex than needed looking increasing costs and bureaucratic importance. However systems based on ad hoc bodies gathered occasionally to revise the intergovernmental arrangement have shown to real problems arriving at consensus as the issue gets more politicized than is needed or advisable. Some experts argue the reason for the exacerbated politics in the definition of distribution of the common fiscal wealth comes out of the example that distributive schemes

[29] The qualification of sound is relatively objective if one observes the results of the fiscal arrangement for the given countries isolated from idiosyncratic factors.
[30] Given the political and technical aspect of this commission is very difficult to expect that by monitoring is not going to end up actually influencing the distribution and appropriation of federal revenues. At this point focusing on the right translation of the Constitutional text would have little effect on the reality this commission is called to create.

are based on services cost equalization[31]. However countries with fiscal arrangement based on distribution of revenue raising faculties also face the same situation. A permanent body facilitates revisions to the fiscal arrangement inside a sound technical framework within a more moderated influence of politics. When the commission gathers occasionally—e.g. once a year—the controversy and the consistency with stated goals is heavy and usually unsatisfactory. Also the reliance on a Federal Ministry for technical support reduces process objectivity[32].

The fiscal decentralization process in Iraq is asymmetric. A province possesses different revenue raising faculties than a region. This is not uncommon in the world, but helps to support the proposal for a permanent commission for federal revenue distribution. A permanent Public Commission for monitoring and appropriation of federal revenues would better serve as the versatile institution. It could assess options to enhance the revenue raising faculties of the provinces and the regions in a phased fashion based on transparent, harmonic and cooperative arrangements.

Another argument for the permanent character of the public commission is the need to maintain surveys and consolidate fiscal information affecting the levels of transfers. An example is the current fiscal arrangement for transfers to the provinces. It has been a common complaint that the census used to define the per capita distribution of transfers for capital investment is not realistic. That argument can always be used as population mobility is a reality. International practice shows all levels of Government either agree on using the estimates of the census bureau or accept alternative means to determine the realities of a mobile population in a given territory, especially when this affects their share of transfer payments.

The fiscal arrangement in article 106 of the Constitution implies regional and governorate representational participation in the public commission. In Iraq so far there is only one Region so the representation can be direct at this point, but the provinces not constituted into a region are many and the only body representing their interest is so far the Governorates Councils Coordinating Committee--GCCC.

An argument can be made that the GCCC must be the representative of the provinces in the Public Commission because other formulas can reduce the representation of the provinces as such into groups of governorates at any given time. Fractionated representation can seriously hinder the equalization principle embedded in the Constitution as groups of governorates would obviously favor the governorates they represent and not all of the governorates. This is the case if COR members are decided to be appointed as representatives of the Governorates in the Public Commission. On one hand unless the whole COR is appointed the representation would be incomplete and possibly biased, on the other hand appointing the whole COR with above 300 members hardly can be a commission. Governors are not natural representatives of the governorates as they are not elected by the population. In contrast the GCCC is a body integrated by members of the representative body of each governorate and elected by them in grounds of equality.

Because oil policy is a different matter according to number 2) of article 112 of the Constitution, the Public Commission for distribution of federal revenue does not need to be involved in that. The public commission for federal revenue distribution however can address the sharing of oil fiscal resources according to the rules proposed in number 1) of article 112. This is the case even if a law on oil is passed. The only draft currently in the parliament regarding distribution of oil wealth states the distribution of this wealth by the Federal Government would be done on a per capita basis. However this is again too general.

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[31] Robin Boadway and Anwar Shah. Revenue Assignment. Chapter V. Fiscal Federalism: Principles and Practices. Working Paper-World Bank, Wash DC 2007.

[32] These conclusions belong to the author. For detailed discussion see “Fiscal Equalization in OECD Countries” join paper number 4 by the Economics and Governance Departments of the OECD. 2007.

**Box 14.**
**The current arrangement with the KRG serves as example of the consequences of not having the institutional ensemble to conduct a harmonious and cooperative approach when defining the fiscal arrangement Central-sub central levels of government.**

**While the KRG is entitled to co-manage Customs revenues there has not been any development to make transparent the way it should account for this revenue. On the other hand the Federal Authorities apply an equally non transparent mechanism to assess and deduct these revenues held by the KRG from the stream of federal transfers. One way is deducting the balance in the authorized bank accounts from any cash transfers. Another way has been non fulfilling transfers in kind. At the same time the KRG seems to hide some share of the collection to prevent the full impact of these deductions. Transparency implies the fiscal arrangement should be fixed totally in cash terms and the mutual duties such as reporting and computation of the credit must be clear for all the participants. More importantly, the arrangement must also cover other related fiscal events such as the share of KRG in foreign debt repayments and rights for the KRG to receive increased transfers when additional budgets occur.**

**Another aspect is the level of transfers needs to be based on a per capita basis and the Federal authorities always argue KRG represents only 13% of Iraq's population and not 17%.**

**With the precedent of the way relations with the KRG are being handled any new region can actually grossly affect the overall fiscal balance of the country. This kind of arrangement needs to be negotiated, studied and implemented in clear steps. Similarly, changes to these arrangements and to the arrangements with the governorates not constituted into a region require thoughtful analysis before unleashing the political processes. Only a stable, independent and participatory consultative body can respond to these needs properly.**

In a simplistic scenario 95% to 97% of the total federal revenues come from oil sales. Going into a full per capita distribution per province would mean even the central level ministries need to allocate their budget expenditures on a per capita basis and not necessarily on a service needs basis. This of course can happen only by accepting that the expenditures by the central ministries can be recognized as distribution of the oil wealth, which is not a clear cut statement. Again the instances for negotiation here need to be participatory and cooperative and the only legal route is the establishment of a Public Commission called for in article 106.

Another advantage of the Public Commission for Federal Revenue Distribution relates to the transparency of the fiscal equalization process mandated by the Constitution. With the maturity of the governorate administrations their self awareness has grown and the logical consequences a politically stronger governorate would start haunting for additional federal funds as current transfers have proven to be not enough for the large and growing needs each governorate identifies. Granting a minimal level of fiscal equalization in a transparent fashion is required. All additional funding channeled on behalf of any province for special reasons should guarantee not reducing the share for fiscal equalization. In addition there is no reason for not showing any additional allocated funding in a transparent manner, to ensure everybody is aware of these developments. Overall transparency in the federal revenues distribution system would make it is less liable for abuse by politically stronger provinces or by Federal Authorities.

### In Iraq there is room for improving the current federal revenue distribution arrangement without affecting the overall fiscal balance

Table 1 above illustrates how Iraq, compared to another countries with similar legal mandates for fiscal intergovernmental equalization, still has large margin for improving the three basic element used to assess the level fiscal decentralization.

It is feasible in the short term to increase the direct participation of the provinces not constituted into region in the total expenditures of the public sector on stable basis. Doubling the current share of the provinces—excluding the 17% on the divisible pool for the regional government—would take the stable share of the provinces not constituted into a region from a current 6.2% to 12%. Overall this would increase the total stable share of sub-central

governments in the overall public expenditures from 16.3% to 22% which is still well below that of Austria—the lowest in the sample of table 1 above.

In the medium term the revenue raising powers of the provincial administrations need to be recognized. Despite CPA order 71 of 2004 provides faculties for the governorate councils to rise and retain revenues, taxes and fees the Ministry of Finance has opposed the full application of that attribution. The Constitutional and other legal bases of the opposition by the Ministry of Finance again have never been clearly explained. Recent opinion by the Supreme Court reiterates the legislative powers of the governorates inside their territorial jurisdictions and that undoubtedly includes the exercise of their tax powers as granted in the CPA order 71. In this regards the new Constitution also guarantees the right to autonomous finances to the governorates.

From the technical view point going into an intergovernmental tax sharing arrangement in the medium term to foster the decentralization process is not a conceptual problem. As a potential example of the way the revenue sharing arrangement could look in the medium term, table 3 below transcribes the proposal for the overhaul of the tax system in Iraq[33]. The real obstacle to implement any tax sharing arrangement is the readiness of the governorate administrations to handle the administration of any given tax structure. For this purpose the international practice shows the federal tax administration can be in charge of the unified collection. It is then matter of systematically distributing the inflows according to the pre arranged shares per type of tax.

By providing the sub-central administrations with own revenue sources the exercise of their fiscal autonomy is granted. In the current budget transfers' mechanism, despite of being a great step in the right direction, the full exercise of financial autonomy by the governorates is not feasible. In the federal transfers framework the governorates have to follow all federal regulations in the handling of money which is proper, but in addition, this favors imposition of restrictions to governorate decisions on what and how to apply these moneys according to the agenda of the central authorities. This removes the good properties of the current transfer mechanism. As well, the transfers refer only to public capital investment activities depriving the provinces of essential inflows of money for urgent maintenance and other operational expenses.

Under the Public Commission concept governorate autonomy would be preserved as long as their participation ends up reflected in the final decisions by the commission. This provincial participation needs to be democratic and adhering to the only limiting features, being these the preservation of the overall fiscal balance and the minimal fiscal equalization principle.

[33] Michael Dunn and Fiscal Policy Unit of the Ministry of Finance of Iraq. A proposal for the Overhaul of the Iraqi tax System. USAID-Ministry of Finance of Iraq, December 2006.

## Table 3- One idea on assignment of non oil revenues (*)

| GENERAL PRINCIPLES OF REVENUE ASSIGNMENT | | | | |
|---|---|---|---|---|
| Key:<br>C: Central government<br>R: Region<br>G: Governorate<br>L: Local or municipal government<br>A: Administrative body | Tax Assignment Options<br>Assignment of Responsibility for: | | | |
| Tax | Base | Rate | Revenue | Administration |
| 1. Personal income tax | C, (R) | C, (R), (G*), (L*) | C, (R), (G*), (L*) | C, (R) , (G*), (L*) |
| 2. Corporate income tax | C | C, (R*), (G*) | C, (R), (G*) | C, (R), (G*) |
| 3. VAT | C | C, (R*), (G*) | C, (R*), (G*) | C, (R*), (G*) |
| 4. Consumer sales tax or consumption-based excise or luxury goods or services tax | C, R, G, (L) | C, R, G, (L) | C, R, G, (L) | C, R, G, (L) |
| 5. Production-based excise tax | C, (R) | C, (R) | C, (R) | C, (R) |
| 6. Customs duties and border taxes | C | C, (R*) | C, (R*) | C, (R*) |
| 7. Natural resource taxes | C, (R, G) | C, (R, G*) | C, R, G* | C, (R) |
| 8. Environmental and pollution taxes | C, (R) | C, (R), (G*), (L*) | C, (R), (G*), (L*) | C, (R) , (G*), (L*) |
| 9. Social security and general payroll taxes | C, (R) | C, (R), (G*) | C, (R), (G*) | C, (R) , (G*) |
| 10. Property taxes<br>- On businesses<br>- On residences | <br>C, R, G<br>C, R, G, (L) | <br>(R), G, L<br>(R), G, L | <br>(R), G, L<br>G, L | <br>(R), G, L<br>G, L |
| 11. Local, governorate and regional fees, levies and charges for infrastructure and services | (C), (R), G, L | (C), (R), G, L | (R), G, L, A | (R), G, L, A |
| 12. Cost-based services and user fees | C, R, G, L | C, R, G, L | C, R, G, L, A | C, R, G, L, A |
| Notes: (1) An asterisk indicates that a regional, governorate or local tax rate that would be a fixed percentage of the central tax collections or the central base. (2) A bracket represents a weaker recommendation. | | | | |

(*) Proposal by Michael Dunn, Tax Expert at the Economic Governance Project, BearingPoint/USAID

"Drafting a Plan for the Overhaul of the Iraqi Tax System in the Medium Term." Baghdad, Sept/06

An important aspect to consider any way is that an overhaul of the tax system is required to transform these taxes into meaningful revenue sources. The poor revenue rising potential of the current tax structure would hinder any interest to rely on it as an independent source of revenues. It is worth mentioning that the perception of usefulness of sub-central taxation in Iraq was lost during the times of prior oil wind falls during the 50s and 70s when federal resources coped with most every need. It often seems easier to request money from the centre than asking community neighbors to pay taxes. However by 2006 Iraq's GDP shows oil accounts for around 59% of the total, also private consumption surrounded 42.8% of total consumption in the economy. Both figures serve as indicators there is margin to improve revenues from non-oil sources. Non-oil revenue sources in the federal budget for 2006 surrounded merely 6.8% of total State revenues.

It is difficult to turn the current non oil taxation system into a meaningful revenue raising source for either the central of the sub-central levels of government in the short term in Iraq. To balance this weakness of the fiscal framework, until the overhaul of the tax system takes place there is need to introduce more flexible rules in the type of grants provided to the governorates from the federal budget. It seems also timely to grant some higher level of

fiscal autonomy to the districts either by providing them with untied grants, or by reinstating fiscal authority of their representative bodies—Qada councils. To do this in the short term would create a perceptible improvement in State provided services.

## III. REVENUE ASSIGNMENT AND THE DISTRIBUTION OF ROLES AND RESPONSIBILITIES

It is widely accepted practice for any revenue assignment model to follow a determined distribution of roles and responsibilities. This is usually the product of the evolution of intergovernmental relations where sub-central governments have either: (a) retained, (b) requested, or (c) agreed to assume the control of certain activities related to service delivery. The distribution of roles and responsibilities regarding service delivery is not necessarily a total transfer of all aspects of the delivery of the service, it is more common to share diverse activities related to the delivery of a specific service among various tiers of government.

Delivery of a specific government service implies several functions negotiated as capacity is determined, service delivery negotiated, and respective roles and responsibilities of each specific tier of government are defined. Functions that customarily recognized include[34]:

- Policy design
- Regulation
- Financing
- Organization/Administration
- Production/Administration

The Iraq Constitution is fairly clear on what government provided services are to be shared with the sub-national governments. These services are:

(a) Customs
(b) Electricity
(c) Environment protection
(d) Planning and development
(e) Health care
(f) Education
(g) Consular activities
(h) Follow up on cultural, social and local development

In most cases the shared function relates either to policy design or to regulation of the service delivery. Only in a few cases does the sharing of functions relate to Administration (organization and production).

The Iraq Constitution establishes that anything can be delegated, and is clear that the revenue assignment must relate to the funding of two aspects: (a) activities that are clearly stated should be shared among tiers of Government, and (b) activities that could be delegated.

Iraq's post constitutional[35] interim period shows an evolving multi-faceted accommodation to roles and responsibilities. For instance, the Federal Government is sharing a fraction of revenue with regions, in a specific case the Kurdistan Regional Government, allowing it to participate in policy design, organization and the production of all basic services together with the Federal Ministries up to the level of the share of the region in the total federal budget. An average 10.1% of the total budget resources are allocated in cash to the Region—See annex 3 for calculation. This percentage refers to all government provided services not related to social distribution programs. So we can appreciate the Region shares most all functions with

[34] Jorge Martinez-Vazquez. Conference on decentralization and distribution of roles and responsibilities. World Bank. Katmandu, 1999.
[35] We refer here to the current period between the enactment of the new Constitution and the issuance of the multiple laws ordered on it.

the Federal government up to the level of funding allocated to it. An additional cash transfer to the KRG above the 10.1% mentioned above, corresponds to the transfers for capital investment projects to the governorates inside the KRG. This extra allocation for capital investment is controlled by the governor only in Dahuk and Arbil, while in Suleymanuya the governorate council performs its role. In the KRG, activities above those financed from the shared budget are not planned in a joint fashion between the federal authorities and regional ministries.

In all governorates countrywide, since 2006 the Federal Government provides the governorate authorities with a transfer from the federal budget that must be dedicated to public capital investment only—reconstruction and new development projects. The average share for 2006, 2007 and 2008 is around 5.9% of the total planned expenditures. This is to be divided among 18 provinces--in a per capita basis.

For provinces deemed unfairly deprived by the former regime and those suffering destruction afterwards, the Ministry of Planning developed a deprivation index. The deprivation index adjusts the portion provided for reconstruction to these provinces reducing somehow the amount for reconstruction that would have corresponded to the provinces that did not suffer from deprivation and destruction if the account were to be done on a strict per capital basis. The three provinces associated under the Kurdistan Regional Government don't receive allocation for reconstruction at all. Baghdad Capital enjoys a distinctive status and the Amanat—executive office of the city—coordinates the delivery of services around the urban area with the central offices of the line ministries directly. Despite the specific appropriation for Baghdad Amanat in the Federal Budget, this money can not be qualified as clearly controlled by a sub-central tier of government.

The Region in Iraq participates in all the functions related to the provision of government provided services. Governorates not constituted into a region participate in financing, organization and production but not in the policy design or regulation as consigned in the Constitutional text. In both cases region and provinces funds availability is the main element to determine what activities have Federal involvement and what provincial and regional. Internal rules to control public procurement by each line ministry sometimes operate to differentiate what part of the function is sub-central and what federal. e.g. in education the province can build a school but the materials, furniture and teaching staff is Federal involvement. In health care the governorate can build and refurbish all type of facilities but the procurement of medical equipment is reserved for the Federal authorities. In electricity and drinking water all purchases of new equipment is a Federal responsibility but the governorates can fund some small expansions and equipment, and at times even maintenance expenses of the federal installations.

Contrary to what the Constitution outlines the Central Ministries seem to be promoting a recentralization initiative restraining the provinces from making certain investments. The lack of legal authority to do this has lead to the constant issuance of contradictory and confusing communications often in the form of recommendation letters. In one such letter the provinces are recommended not to invest in Electricity, Industry and Oil. In another they were advised not to channel funds for agriculture. In addition there has been a letter indicating the provinces should not look after projects that would take more than 12 months implementation term. While these examples can be debated for both technical and constitutional soundness, all of these kinds of discussions and debates can be resolved within the cooperative and participatory framework as proposed by article 106 of the new Constitution—the Public Commission.

To properly implement the Constitution two legal bodies need to be coordinated—Provincial Powers Law and the law for federal revenue distribution that contains the Public Commission. As mentioned before, it makes sense the Public Commission for federal revenue distribution is involved in the implementation of the rules for distribution of oil revenues mentioned in number 1) of article 112.

Correspondence between the level of revenues assigned to the provinces and the roles and responsibilities they would end up undertaking is paramount to the success of the decentralized Iraqi State. Precluding the exercise of provincial powers for raising revenues creates all conditions for the occurrence of unfunded mandates. For instance the Constitution orders the State shall maintain public health and provide the means of prevention and treatment by building different types of hospitals and health care institutions—Article 31--; if by any chance it is decided the Federal Government is to do the building and the governorates have to undertake the maintenance of these facilities the corresponding revenues need to be planned and resources allocated.

Equally important is the ability of the governorates to have the full authority to deliver services at the provincial level. For instance the tendency to preclude the participation of the governorates in the procurement of certain goods and services has already been shown to be counterproductive. On one hand assets built or rehabilitated by the provincial governments have not received the adequate support or investment from the Federal Ministries. As a result these assets go unused—E.G. School buildings rehabilitated have not received furniture or teaching material or teaching staff. On the other hand solving the provincial needs implies most of the time lower investment and projects that can be implemented faster. This is the case of electricity where the provinces have been recommended not to invest despite procurement and implementation by the provinces is somehow faster and the potential projects would be easier to implement. It is true in a large scale investment—e.g. a big dam—financial efficiency is ensured. From another perspective, the dam that would solve the problem of lack of electricity nationwide that could take 10 years to start up just the generation phase while diesel generators or the interconnection to international gridlines could solve the provincial scale problem in a lot less time. Efficiency of the investment versus overall economic efficiency measured as a loss of economic activity due to the absence of the service that enables it is to be balanced in the decision making. Other considerations include such things as the public's low appreciation of State effectiveness in the delivery of essential services and having to wait several years to have the service provided in a reliable fashion. These kinds of things are examples of what needs to be balanced before going in the distribution of roles and responsibilities.

Table B in the Appendix shows a proposed distribution of roles and responsibilities that is based on international practices and the benefit area principle. This table was discussed with a wide range of Iraqi authorities at the Governorates level during 2004. Despite being a pre constitution exercise, it does not necessarily oppose the constitutional design and the discussion does represent a good effort to identify how local authorities think about the subject of devolution. Notably the table does not address sharing roles and responsibilities in oil which is an important claim by the KRG. Nor it does address telecommunications which has been a very active sector subjected to claims for devolution in many European and South American countries. The benefit area principle estates service provision activity must be assigned to the level of government that would have the most immediate benefit from it. A specific tier of government must benefit from any given service irrespective of population and as well have the financial resources to undertake the implementation of the services. Another objection might involve the question of economies of scale, especially if services are designed with only one governorate is considered. When the intergovernmental fiscal equalization principle has a role the questions arises as to who should be given the role to lobby for specific common needs and then who should solve the problem. A long term international practice has been the association of the incumbent local governments to supply for specific common needs. In this situation again, a good case can be made for the Public Commission to function as the proper body to balance the social needs with such things as economies of scale, and cost benefit analysis.

Table C in the Appendix illustrates the distribution of roles and responsibilities between tiers of government in the current legislation and practice in Iraq. The caveat to this distribution is that it was not fully applied in the whole country because for many activities the Central Government line ministries needed to agree on the transfer of functions. Evidence shows the

transfer of functions happened unevenly and mostly to the benefit of large urban centers. Also the proposed transfer of functions as designed in that law did not in all cases facilitate a proper or efficient delivery of the services when passed in full to the local authorities. There is not full agreement among legal experts in the country regarding the validity of the legal text—Law 159 of 1969—that supports this distribution. Some legal scholars sustain that most of law 159 was superseded by the Law of Revolutionary Councils enacted by the Baath regime in 1995. In the Law of Revolutionary Councils most functions for Qada'as are focused on providing social services. The situation comes more complex as CPA order 71 actually superseded the law of Revolutionary Councils of 1995 and expressly stated the authority of the law 159 of 1969 remains in place, with the adjustments provided in the mentioned Order.

**What improvements can be made at governorate level in the short term?**

The current legislation makes possible to improve several aspects of the intergovernmental fiscal framework. While the current budget transfer mechanism is a great step in the right direction the governorates can not exercise full financial autonomy. It is evident that to enhance decentralization a more flexible system to transfer funds to governorates is needed. To this end Governorates need authorization to undertake maintenance and operational expenditures and to develop their own administrative cadre. Also the transfer needs to be treated as a grant reducing the interference by central authorities in the steps for its utilization.

Current restrictions to exercise of revenue rising powers by the governorates must be changed for a system of clearly agreed fiscal rules. Under a fiscal rules arrangement the power to set tax basis and tax rates by the governorates could be regulated.

**What improvements can be made at the District level in the short term?**

While current legislation in Iraq allows many partial activities to be covered by the Beladiyas—municipalities offices--and Quada'as—Districts[36], there is no specific distribution of roles to the Nahiya. Evolution of the management of the scarce revenues allocated to the Beladiyas and Qada'as in the legislation has ended up in total control by the Ministry of Municipalities and Public Works—MMPW. The MMPW has developed this control through the Beladiyas which are actually the offices of the MMPW in each Qada'a nationwide. Order 71 authorized the Governorate to participate in each service delivery activity in their territory. The Constitution on the other hand, by ignoring the Qada'as and Nahiyas opened the possibility that each Governorate would be in charge of organizing their internal territorial administration at will however this would need to be clearly stated in a corresponding law implementing article 120. Until this happen the Qada'as remain the local authority and the Qada'a council the legitimate representative body.

Alternatives to provide Qada'as with better standing to serve their neighbors require enhancing funding capacity and recognition of the role that belongs to the Qada'a councils and to the Qa'im-maqams—Qada'a managers. The best and most expeditious way is to modify the rules for the current matching grant arrangement to fund Qada'as. Under the current arrangement the budget request by the Qada'a is controlled by the Ministry of Municipalities and Public works via the beladiya for the following services:

- Surfacing and maintenance of roads
- Building and maintenance of gardens and parks
- Defining the usage of land for commercial and residential purposes, and distribution of land among the citizenry
- Placement of traffic signals as well as cleaning of public places and organization of streets
- Garbage collection and its safe disposal

[36] Laws 130 0f 1963, 159 of 1969 and CPA order 71 of 1994.

- Environmental controls and actions to prevent and clean pollution

The beladiya does not follow a needs assessment model for determining a maintenance and operations budget, let alone priority investments. The beladiya has to follow the instructions for budget preparation provided by the MMPW which for a long time has used incremental base budget factors to control the budget request. Also the historic fiscal capacity of the Qada to pay for the 40% of the resulting budget request is taken into consideration. The grant formula needs modification in the following manner:

- Eliminate the transfer to other Qada'as of potential surplus in own revenue collections any given Qada'a may present. The appropriation of the surplus by the central government is not the right policy even if it looks after redistributing that surplus to fiscally poorer Qada'as. Intergovernmental fiscal equalization using municipal generated revenue is not a sound fiscal policy; it hinders fiscal effort in the tier of government that has the most immediate responsibility before the inhabitants.

- The definition of surplus-Qada'a must be linked to a detailed budget based on needs assessment, both transparent and with input from the public resident in the Qada'a. This is opposite to the incremental base budget request the beladiya currently prepares following the instructions of the MMPW.

- Fiscal effort in the Qada'a must be rewarded by allowing the use of any extra amounts collected in the by the Qada'a authorities

- Use of the resources allocated to the Qada'a must be done under the approval and oversight of the Qada'a council. Qada'a council must be the authority to decide what, how and when the planned resources are applied. In this proposal Beladiyas must supply technical support to the Qada'a authorities in the implementation of these resources.

- Beladiya operational expenses—especially salaries-- must continue in the head of the MMPW.

- Local revenue collection must continue supported by the Ministry of Finance where Qada'a has no capacity to develop tax administration. In any case Qada'a authorities must be allowed to exercise their coordination powers to improve tax collections.

The only way to go back to the healthy needs identification and needs assessment method is allowing the Qada'a authorities to participate in the preparation of the budget request by the beladiya. At the same time the MMPW would not be allowed to reduced or modify this local budget. Qada'a authorities must be instructed on consulting the communities to determine the expenses with the grant transfer. While proper needs assessment skills by Qada'as are perfected, the Federal Government needs to set a grant transfer amount for the respective Qada'as on a per capita basis. This grant transfer must allow the Qada'a authorities to use it for either: Maintenance, Operation or Capital Investment, restricting the amount that can be used for contracting short term personnel to no more than 35% of the total amount of the grant. According to the governorate authorities[37] and to the data of the recent utilization of transfers to the Governorates[38], the amounts dedicated to supply for the requests placed by Qada'as represents around 25% to 30% of the total expenditures contracted by the governorates. Until a more scientific method to establish the right level of the transfer to the Qada'as is developed, it seems reasonable to set the initial grant transfer in an amount equal

[37] Letter to the Prime Minister from representatives of 12 governorates dated October 22nd 2007.
[38] Report on ARDPs Utilization—the sector distribution—LGP2, 2007.

to 30% of the total allocation provided to the governorates for capital investment. The allocation for the Qada'as must be independent and must not affect the allocation to the governorate. Also funding must be based on per capita figures. Baghdad City grant allocation could be balanced with other allocations to the Amanat as this office performs an acceptable budget request work. The rest of Qada'as in Baghdad province—out of the capital boundaries--must be included in the grant transfer with all other Qada'as of the country.

But improving the fiscal situation in the Qada'as does not end with the modification to the grant to the Qada'as. The provision of basic services such as water, sanitation and electricity in the Qada'as are also in hands of offices and SOE of the MMPW operating in diverse areas of the provinces often servicing more than one Qada'a. The major defect of this organization of service delivery is that is not service providing oriented. Direct consequence the patterns and priorities of the SOE hardly would match those of the clients—served population. The key to change this would be including the participation of either members of the representative body of the Qada'a or the Qada'a manager from all districts served by the SOE in the directive board of the enterprise. This democratization of the SOEs management has proven successful in France[39] and other countries. Future measures should include the possibility of privatization preserving the place of the Qada'a authorities in the resulting services providing entity.

[39] Isabelle Joumard and Claude Giorno. Getting the most out of public sector decentralization in Spain. Contains a comment on this specific case in OECD countries. OECD Economics Department, working paper, July 2005.
[39] Ibiden 27

## Appendix

### I. The Principles of Fiscal Federalism

Diversity
Communities must not be forced into uniform fiscal arrangements and priorities for the provision of services.

Area benefit (effectiveness)
Also known as “Equivalence or Match principle” is such that the authority of the area that most directly benefits from the service should be the one in charge of organizing and managing the delivery.

Location neutrality
Any intergovernmental fiscal arrangement should prevent fiscal competition among the territorial entities to gain the favor of investors.

Centralized Economic Stabilization
Taking the aggregate of the country, fiscal balances need to be instruments of macroeconomic policy for the whole union. This can only be achieved if the federal government is in control of these balances—monetary, fiscal and international trade.

Minimal Provision of Essential Services
The national government should through grants and transfers to regions and lower level administrative bodies to ensure that every citizen receives at least a minimum level of essential services such as security, health care, welfare and education.

Equalization of Fiscal Position
The central Government, through its own revenues is in charge of equalizing territorial fiscal imbalances. To that purpose nationwide plans to stimulate territorial fiscal efforts to reduce potential dependency on central government funding needs to be explicit and part of the framework to equalize territorial fiscal wealth.

## II. Two Useful Models to Compare: Poland and Spain[40]

Finding a reference model for decentralization in Iraq is a difficult task. No Arab or middle-east country has a meaningful fiscal decentralization practice that would resemble the demographics, economy and historical developments in Iraq. Iraq is not an Islamic republic, is not a kingdom as Saudi Arabia or a confederation of Principalities as the UAE[41]. Iraq's economy is not as diversified as Egypt's and its potential is larger than Lebanon, or Jordan. Certainly Iraq is looking to turn into a democracy hence can not see the Syria, Libya or Morocco as a model and Iraq is socially and economically more ahead than many Muslim African countries to find out a reference model there. It does make sense to compare Iraq with the former Soviet countries as the rule of the Baath party tried to implementing similar economic and intergovernmental structures. The Baath party openly looked at communist Poland as a source of inspiration and a model in governance. Following the adoption of the new Constitution a growing number of Iraqi authorities have focused on Spain as a model for decentralization in democracy. This inclination towards the Spanish model is due to resemblances in history and diversity in ethnic and cultural compositions and the clear success in economic development.

Poland

The Polish devolution process is one model often looked after in Iraq because the Baath party modeled the Iraqi intergovernmental relations on the former Communist Polish State. By 1989 with the new Polish democratization the old structure of 49 weak and small regional administrative districts—provinces--was maintained. The new legislation stated these districts should be made autonomous however the governor of the districts continued to be appointed by the central government and numerous district powers were removed and given to the central government.

By 1990 2,500 municipalities were empowered through self government and their authorities became elected in a voting mechanism of public balloting. Municipalities were given control of the following basic services:

- Water and sewage
- Solid waste management
- Maintenance, administration and construction of local roads, municipal cemeteries, pre-school and elementary schools
- Administration of social welfare programs for the needy and
- Administration of municipal housing

The municipalities were organized with elected councils that have the powers to select the Mayor. The major was provided with managerial support in the form of a municipality board. The municipalities were granted fiscal powers in the form of granted shared revenues from personal and corporate income tax, real estate tax, vehicles tax, rent from municipal owned properties, and diverse fees. Municipal associations were permitted. Many were actively formed and today there are 130 and one third of all municipalities are members in at least one association.

In the same 1990 reform 268 regions—counties--were formed following closely the design of the Polish state before 1975. The communist reform of 1975 abolished the counties and split the large provinces into 49 regional districts. Counties were attributed functions deemed too large for a municipality to take over—secondary schools, health care, law enforcement, fire

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[40] Description of the Spanish case comes out of direct contact with the system by the author and from the summary in the OECD paper: Taxing Powers of State and Local Government. Tax policy studies No.1. and Isabelle Joumard and Claude Giorno. Getting the most out of public sector decentralization in Spain. OECD Economics Department, working paper, July 2005.

[40] Ibiden 27

[41] Despite the federation arrangement can sound attractive to a new born federal state like Iraq in the case of the UAE this arrangement provides for a very fiscally weak Federation Government that Iraq might not be able to assimilate.

protection, sanitation, veterinary control, and building inspection. The reform preserved 40 special administrations and the national offices continued to operate following their own territorial divisions.

Despite the 1990 reform effort the intergovernmental fiscal arrangement continued to be heavily centralized with local revenues counting for only 17% of the total public sector and the majority source of these local revenues being a share of national taxes. By 1995 the share of local governments in total public sector spending was a mere 19%. Major unfunded mandates started to appear with the transfer of the administration of primary schools to the municipalities carried out in 1996.

Notwithstanding the many obstacles mentioned above, the 1990 cancellation of the central planning model with its central administrative controls in the Polish State leaded to the success of local governments. Once free from the dictates of the central planning bureau and with real democratic elections, local governments undertook direct and indirect control of public investment, growth of small business, and the development of civil society at the local level. Success was achieved by combining development strategies with proper land planning—spatial planning. The efforts were directed to create sustainable employment and investment in a favorable climate. The strategy fought three major poverty factors as identified in Poland at that time—unemployment, poor infrastructure, and shortage in housing[42].

By1999 a complete mid-level focused decentralization reform in the political, fiscal and administrative areas changed the territorial re-division of the State. Regional administrative districts were reduced form 49 to 16 and the 40 special administrations and 268 administrative regions were merged into the new provinces that were recognized as self governing entities where the elected provincial parliament appoints the Marshall—Governor—and the executive bodies of the province under the Marshall. The Prime minister supervises the Provinces through a representative--Voivod. The control on the offices of the national ministries in the regional districts—DGs--was delegated to the province with large resistance from the central ministries as the funding of salaries and other expenses continued on the national budget but out of the line ministries control. Many functions were delegated to the new territorial entities. The provinces undertook the implementation of development policies taking advantage of the success of the municipalities after the disbanding of the central planning bureau. Also the provinces undertook the promotion of education, international cooperation, public private sector partnership, environmental protection and cultural activities. They have so far excelled in coordinating and fostering investment—both public and private—with overall positive results.

Counties were created as an intermediate layer of government between the Regional District and the municipalities in 1999. The multiplicity of new territorial entities—373 counties, including 65 cities with county status--seems to have favored the appearance of unfunded mandates and have created counterproductive situations in the delivery of social services[43]. However these studies where made just after the reform, not giving enough time for the changes to set in. Counties and municipalities have not any authority directly appointed by the central government.

Further reforms in 2002 introduced direct election for municipal mayors and to date there have been positive results including enhanced accountability and improved governmental performance.

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[42] Source: Mirror-UNDP. Case Studies, Decentralized Governance in Poland: The cases of Bilgorag, Ilawa and Tarnowo Podgorne.

[43] Janelle Kerling. Political Means and Social Services Ends of Decentralization in Poland. International Activities Center, The Urban Institute, Washington D.C. 2002.

The elimination of the central planning bureau and its processes undertook in 1993 was followed by the creation of the Joint Committee of State and Local Self-government that is nowadays in place. This Joint Committee is recognized as a fundamental piece for intergovernmental coordination. In the Joint Committee both central government and local governments are represented through members of the diverse associations of local self-governments that have been growing amid the tiers of government have been modified. This Joint Committee serves as forum for dialogue and facilitates the agreement of different issues affecting local self-government so that they are coordinated in line with central government policies. Nowadays it is recognized this committee has been a key player in the current success of the decentralization and democratization of Poland.

To contrast the Polish experience with that of Iraq one notes that the process of transferring full authority on the DGs to the governorate was only partially accomplished—see CPA order 71 of 2004. Governorate authorities may request the removal of heads of DG in the governorate but the central authority has many avenues to ensure that this not to be carried out. In practice the process of accommodation of DGs in the governorate and governorate authorities has occurred with diverse outcomes in each governorate. However, in the most progressive governorates authorities continue struggling to create their own technical offices in view of the difficulties to harmonize central line ministries orders to the DGs with the governorates identified needs. Also in Iraq after the initial rejection of the concept of central planning it has regained terrain lately at the federal government level. However this tendency seems moderated by the proactive attitude of the governorates in preparing their own strategic development plans. An important element to bear in mind is the governorate authorities do consult the communities in the province to identify and assess needs in economic development and services delivery while the DGs and central line ministries don't do so.

Spain

The devolution process in Spain is also referenced quite often in Iraq in terms of asymmetrical decentralization. Asymmetric decentralization occurs when similar tiers of government have different responsibilities and empowerments. This is the case of Iraq where Regions and Governorates are empowered with different responsibilities.

There are three tiers of sub-central government in Spain: a) autonomic governments, b) the provinces and c) the local governments. In the Spanish case National revenue is shared with the regional and local authorities, except in the case of the Pais Vasco and Navarra that collect their own taxes due to historic arrangements made prior to the 1978 Constitution. This is known as the foral or traditional rights system. For all practical purposes autonomies in the foral rights system follow anyway similar fiscal rules as the rest in their relations with the central government.

While 7 provinces decided to join into a single autonomic region—Vasque country--after the 1978 Constitution allowed this process, the remaining 43 provinces have ended their respective formation of 17 autonomous regions each citing common interests. Generally in Spain, intergovernmental fiscal relations with autonomies are ruled by a common system, and sometimes by the foral system, as mentioned above. There are however, special fiscal practices for the Canary Islands and for two autonomous cities located on the coast of North Africa - Ceuta and Melilla.

Until 2001 there were separate autonomic government groups using what is called the "common system". One group of autonomies was bounded by the legislation of 1997-2001 while the other group—Castilla-La Mancha, Extremadura and Andalucia--have a different arrangement. The major difference between the 1997-2001 fiscal rules and the other arrangement was the three late entrants were not allowed to introduce tax credits to the Personal Income Tax. By 2002 it was decided to equalize revenue rights for all autonomies in the common system.

Revenues types for all the common system autonomies include fees for services, loans and the so called ceded taxes:

- wealth tax
- inheritance and gifts taxes
- transfer tax and stamp tax
- duties on gambling
- Tax on certain means of transportation

Another revenue source for these autonomies under the common system is the share of the national personal income tax.

The central government mostly regulates the tax basis and relative flexible rules allow the autonomies to set some of the tax rates.

Each of these regions has the right to receive a block grant equivalent to 15% of the total personal income tax levied in its territory. The share can be diminished if the expenditure to be funded with these moneys is lower than the 15% of collections levels. All the autonomies have the right to retain additional 15% of the personal income tax actually collected in their territory. Autonomies can also introduce tax credits to the personal income tax within certain limits and conditions.

All common system autonomies are entitled to a share of the rest of the State General Tax Revenues but have no power to change the tax base or tax rate. This share is variable, subject to the transfer of new responsibilities involving larger outlays for the province—thus preventing unfunded mandates. Also subject are transfers of new taxes or changes in socioeconomic data that makes advisable either increase of diminish the share[44].

Under the foral system Pais Vasco and Navarra share with the central government most taxes. Pais Vasco has an arrangement namely “concierto economico”—economic agreement--under which it must contribute to the Central government with a “cupo”—quota--to cover part of the cost of the national administration and other expenses the national government makes in its behalf. Similar situation occurs in Navara where the arrangement is called “convenio economico”—economic covenant--and the transfer to the national government is called “aportacion economica”--economic provision. Taxes excluded from the sharing pool with the foral autonomies are:

- Customs duties
- Some excises
- VAT
- Personal Income Tax from non residents

Special cases are constituted by Canary Islands and the autonomous cities of Ceuta and Melilla. The three are entitled to collect and retain a VAT as an own tax. In addition the Canary Islands enjoy special corporate tax regime for investors[45].

Equalization is conducted by the central government through the so called “Fondo de Suficiencia”—sufficiency fund--, where the fiscal surplus of the fiscally wealthy region is gathered. Grants to the deficit regions are granted by the central government via resources in the Fondo de Suficiencia—Sufficiency Fund. To determine whether a region is a surplus or a deficit region a special formula from the law on the financing arrangement of 2002 is applied. In 2003 a fiscal stability law was enacted to maintain fiscal discipline at all levels of government which in turn ensures the overall fiscal balance.

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[44] For detail and formulas see: Isabelle Joumard and Claude Giorno. Getting the most out of public sector decentralization in Spain. OECD Economics Department, working paper, July 2005.
[45] Ibiden 27

Taxing powers by the municipalities are extensive while their responsibilities are relatively low. Just few years a go the municipalities were involved in the provision of some levels of education and health care services and had similar levels of expenditures as other third tier governments in the OECD that have a lot more responsibilities. Spanish Municipal authorities have statutory right to manage revenues with significant autonomy—setting rates within wide ranges provided by national legislation and provision of tax relief. These sources are:

- Real estate
- local business taxes
- Taxes on motor vehicles
- Construction and public works
- Capital gains on land
-

In 2003 there was a major tax reform that introduced significant exemptions to the local business tax on individuals and medium size companies. The reform compensated municipalities with grants and tax sharing arrangements on VAT, PIT and excise taxes.

Table A- Sub-national Share on Total Budget Expenditures Based on OECD Applied Methodology

Recent Budget Figures (Planned)

| | 2006 | | | 2007 | | | 2008 Draft | | |
|---|---|---|---|---|---|---|---|---|---|
| **Concept** | **Amount Million of ID** | **Amount in U$ millions** | **%** | **Amount Million of ID** | **Amount in U$ millions** | **%** | **Amount Million of ID** | **Amount in U$ millions** | **%** |
| Revenues | 46,689,298.00 | 31,654.00 | | 42,064,530.00 | 33,385.00 | | 50,775,000.00 | 42,312.50 | |
| Expenditures | 50,963,161.00 | 34,551.53 | | 51,727,468.00 | 41,054.20 | | 58,110,000.00 | 48,425.00 | |
| deficit/surplus | -4,273,863.00 | -2,897.53 | | -9,662,938.00 | -7,669.20 | | -7,335,000.00 | -6,112.50 | |
| | | | | | | | | | |
| KRG share on expenditures | 4,469,863.00 | 3,030.44 | 8.77 | 5,982,353.00 | 4,747.97 | 11.57 | 5,799,450.00 | 4,832.88 | 9.98 |
| Provinces share on expenditures | 2,949,980.00 | 2,000.00 | 5.79 | 3,000,000.00 | 2,505.51 | 5.80 | 4,000,000.00 | 3,333.33 | 6.88 |
| | | | | | | | | | |
| | | | | | | | | | |
| | | | 14.56 | | | 17.37 | | | 16.86 |
| ID/U$ | 1,474.99 | | | 1,197.60 | | | 1,200.00 | | |
| | | | | | | | | | |
| | | | | | | | | | |
| average for 3 years | | 16.3 | | | | | | | |
| | | | | | | | | | |
| Provinces share | | 6.16 | | | | | | | |
| KRG Share | | 10.11 | | | | | | | |
| total average | | 16.27 | | | | | | | |
| | | | | | | | | | |

Methodology extracted from OCDE, Economic Outlook 74. 2003—Chapter V. Fiscal Relations Across Levels of Government.

Transfers to Baghdad Amanat excluded. Random transfers from Donors and Off Budget funds excluded.

**Table B- Simplified Distribution of Roles and Responsibilities Among Tiers of Government Based on Area Benefit Principle**
**(Proposal for Iraq, LGPI, 2004 discussed with Iraqi officials from diverse tiers of government at Governorate level in diverse governorates)**

| Area of Activity | Federal (Central) | Governorate | Qada'a | Urban Nahiya | Rural Nahiya |
|---|---|---|---|---|---|
| **1. Security**<br>1a. Police<br>1b. Traffic Police<br>1c. FPS | 1. National Policy | 1. Development of security strategy for governorate, involving police, border police and facilities<br>1a. Approval Police Plan | | 1a. Approval of Police Plan for area<br>1b. Approval of Traffic Police plan for area<br>1c. Approval of strategy for deployment of Federal Police Staff | 1a. Approval of Police Plan for area<br>1b. Approval of Traffic Police plan per area<br>1c. Approval of strategy for deployment of Federal Police Staff |
| **2. Municipal Services**<br>2a. Solid Waste<br>2b. Parks and recreation<br>2c. Drainage<br>2d. Street Cleaning | 2. National Policy and standards for provision of services | 2a. Review location of final disposal sites if serving area larger than Qada'a or near environmentally sensitive area | 2a. Final Disposal Site Management | 2a. Collection and recycling<br>2b/c. Development and maintenance<br>2d. Management | 2a. Collection and recycling<br>2b/c. Development and maintenance<br>2d. Management |
| **3. Planning**<br>3a. Strategic Plan<br>3b. Infrastructure Plans<br>3c. Master Plans | 3. Establishes system of planning and frequency of planning<br>3a/b/c May call in on appeal | 3a. Primary responsibility after consultation with Qada'a<br>3b. Prepares structure plan for Governorate<br>3c. Checks Master Plans of Qada'a consistent with Structure Plan | 3a. Input to Governorate strategy based on inputs from Nahiya<br>3c. Prepares master plan and checks detailed land use plans prepared by Nahiya are consistent | 3a. Input to Governorates Strategy, sent to Qada'a<br>3c. Detailed Land Use Plans for urban areas Approves development proposals consistent with Qada'a master plan and Detailed Land Use Plans | 3a. Input to Governorates Strategy, sent to Qada'a<br>3c. Detailed Land Use Plans Approves development proposals consistent with detailed Land Use Plans |
| **4. Education**<br>4a. Kindergarten<br>4b. Primary<br>4c. Secondary<br>4d. Technical schools<br>4e. Teachers training<br>4f. School curriculum | Policy, in particular compulsory education policy and basic educational standards<br>4f. Setting of curriculum and National examination standards for all subjects | 4d. and 4e. Construction and staffing of technical and teacher's training schools | 4c. Secondary school construction and staffing Additional curriculum subjects for secondary schools | 4a. Kindergarten construction and staffing<br>4b. Primary school construction and staffing with additional curriculum subjects for primary schools | 4a. Kindergarten construction and staffing<br>4b. Primary school construction and staffing with additional curriculum subjects for primary schools |

| Area of Activity | Federal (Central) | Governorate | Qada'a | Urban Nahiya | Rural Nahiya |
|---|---|---|---|---|---|
| **5. Health**<br>5a. Primary Health Care<br>5b. Health Education<br>5c. Health Clinics<br>5d. Community Hospitals<br>5e. General Hospitals<br>5f. Specialized hospitals | 5. Policy and minimum service standards initially based on access to medical care and later quality of care available<br>Policy on medicines production, importation, distribution and licensing<br>5e. Construction and staffing and all cost of specialized health centers | 5e. General Hospitals construction operation and maintenance | 5d. Community hospitals construction, operation and maintenance | 5a. Primary health care delivery and education, including health checks on all compulsory schools aged children<br>5c. Health clinics—dispensaries--construction, operation and maintenance | 5a. Primary health care delivery and education, including health checks on all compulsory schools aged children<br>5c. Health clinics—dispensaries--construction, operation and maintenance |
| **6. Drinking Water**<br>6a. Water treatment<br>6b. Main distribution<br>6c. Secondary and tertiary distribution | 6. Policy and Minimum service standards | 6. Strategy for drinking water delivery in Governorate, to meet national guidelines<br>6a/b. Water treatment and mains distribution construction and management where system serves more than one Qada'a | 6a/b. Water treatment and mains distribution construction and management | 6c. Secondary and tertiary water networks which can be supported by the water provision capacity of mains water treatment and distribution systems. Planning in conjunction with Qada'a authorities | 6a. Small scale water treatment plant construction, operation and maintenance where main system not available |
| **7. Roads**<br>7a. local roads<br>7b. Governorate roads<br>7c. National roads | 7. General policy on system of classifying roads between National, Governorate and Local<br>7c. Planning construction and maintenance of National Roads network | 7. General strategy for road construction in Governorate<br>7b. Planning construction and maintenance of Governorate roads | | 7a. Road construction and maintenance within urban area, not part of Governorate or National Road System | 7a. Road construction and maintenance in villages and between villages within Nahiya, not part of Governorate or National Road System |
| **8. Fire Protection** | 8. National Policy and standards | | | 8. Provision of fire stations, their staffing, operations and maintenance | 8. Development o village fire fighting capacity |

| AREA OF ACTIVITY | Federal (Central) | Governorate | Quada'a | Urban Nahiya | Rural Nahiya |
|---|---|---|---|---|---|
| **9. Sewage disposal**<br>9a. Sewage treatment Plant<br>9b. Sewerage network<br>9c. Septic tank Evacuation<br>9d. Sanitation Education | 9. General policy on sanitation, covering standards for construction of basic sanitation systems and effluent discharge into ground water or water courses<br>8d. Preparation of Sanitation Education program and materials | 8a. Approval of Sewage treatment plant location | 8c. Control over location of places for discharge of effluent from septic tanks | 8a/b. Construction, operation and maintenance of sewerage network and treatment plants<br>8d. Implementation of national sanitation education programs<br>8c. Septic tank emptying in areas not covered by main sewerage system | 8c. Septic tank emptying and arrangements for final disposal |
| **10. Environmental Control**<br>10a. Strategy<br>10b. Enforcement | 10. General Policy on environmental standards | 10a. Environmental strategy, including identification of sensitive areas, conservation areas, and areas of special environmental interest | 10b. Enforcement of national standards and including of adequate planning/development safeguards for environmentally sensitive areas | 10b. Ensuring that all development proposed in Nahiya conforms with national standards and observes development restrictions in environmentally sensitive areas | 10b. Ensuring that all development proposed in Nahiya conforms with national standards and observes development restrictions in environmentally sensitive areas |
| **11. Social Protection**<br>11a. Unemployment<br>11b. Widows and Orphans<br>11c. Special Needs Groups | 11. National Policy and Programs to meet needs of special interest groups | 11. Governorate strategy on employment generation and special needs groups | | 11. Planning, operating, maintenance and staffing special needs schools<br>11a/b/c. Delivery of goods hand outs and cash subsidies by delegation according to national programs and funding | 11a/b/c. Delivery of goods hand outs and cash subsidies by delegation according to national programs and funding |

| AREA OF ACTIVITY | Federal (Central) | Governorate | Quada'a | Urban Nahiya | Rural Nahiya |
|---|---|---|---|---|---|
| **12. Housing**<br>12a. Public Housing<br>12b. Land distribution | 12. Policy on housing provision<br><br>Standards and building regulations | 12. Housing development (including land) strategy for Governorate to meet national policy requirements | 12b. Housing land estimates for Quada'a included in Master Plan | 12a. Regularizing titles to land with informal housing that complies with general land uses<br>12b. Creation of services sites for low cost self-build housing | 12a. Regularizing titles to land with informal housing that complies with general land uses<br>12b. Creation of services sites for low cost self-build housing |
| **13. Electricity**<br>13a. Generation<br>13b. Distribution<br>13c. Connections<br>13d. Street lighting | 13. National Power Generation and Distribution Policy Plan. Construction, management and maintenance of the national generation and distribution network | 13. Input to creation of National Power Plan.<br>Interim solutions to shortages of electricity from the national network Governorate wide | 13. Estimated power requirements for Qada'a. Maintenance of interim means provided by the Governorate to solve lack of electricity from the national network | 13d. Street lighting | 13a/b/c. Local generation, distribution and connection in isolated locations<br>13d. Street lighting |
| **14. Culture and Sports**<br>14a. Stadium Construction<br>14b. Sports facilities<br>14c. Theatre construction<br>14e. Cultural Events | 14. General Policy and Standards of provision | 14a/b/c. Regional stadium and sports and cultural facilities construction and operation<br>14d/e. Regional sports and cultural events | 14b/c. Construction, operation and maintenance of local sports facilities and theatres<br>14d/e. Organization of cultural events | | 14b. Construction, operation and maintenance of sport facilities<br>14d. Organization of local sports events |
| **15. Agriculture**<br>15a. Veterinary Services<br>15b. Agricultural laboratories, and research<br>15c. Agricultural supplies Distribution<br>15d. Extension services<br>15e. Land reclamation<br>15f. Agricultural Education | 15. National policy in aid and assistance to sector. Policy on 15a, 15b, 15c, 15f,and monitoring of same | 15. Strategy for sector<br>15b. Agricultural laboratories and meteorology stations placement<br>15e. Storage and monitoring and use of reserves<br>15f. Strategy for reclamation of land | 15a/d. Location of Agricultural support services and extension workers<br>15c. Location of agricultural supplies distribution centers<br>15e. Reclamation projects | | 15a. Veterinary and meteorology stations and services centers construction, management, and maintenance<br>15c. Distribution capacity<br>15e. Reclamation monitoring<br>15f. Agriculture education programs |

| AREA OF ACTIVITY | Federal (central) | Governorate | Quada'a | Urban Nahiya | Rural Nahiya |
|---|---|---|---|---|---|
| **16. Irrigation**<br>16a. Water resources<br>16b. Damns and main water distribution Networks<br>16c. Secondary and Tertiary systems<br>16d. Irrigation sharing systems | 16. National policy on irrigation and water resources | 16b. Major irrigation projects<br>16d. Strategy between Governorates | 16c. Planning and construction of secondary systems<br>16d. Strategy between Qada'as | | 16c. Planning construction and maintenance of irrigation tertiary networks. Cleaning of secondary systems<br>15d. |
| **17. Transportation**<br>17a. Public Transportation<br>17b. Traffic Management<br>17c. Traffic Police | 17. National Policy<br>17a. Rail transportation and air transportation policy, operations and management of facilities and airports<br>17b. Air traffic control<br>17c. Railway police | 17a. Regional public transportation policy and development and management of systems, pricing, etc | | 17a. Local public bus company, licensing of private sector and routing management<br>17b. Local traffic management<br>17c. Traffic police | |

**Table C– Distribution of Roles and Responsibilities according to the law 159 of 1969—Governorates Law**

| (E) Stands for Empowerment: New activity authorized to be undertaken by the sub-central authorities in the new law<br>(T) Stands for transferable: Central authorities may agree to transfer that specific activity to the sub-central authorities | |
|---|---|
| Agriculture, Agro-industry, forestry and Live Stock Breeding | -Reforming and drying up pools and swamps in the lands owned by the State (E)<br>-Establishing Veterinary clinics and sheep washing facilities (E)<br>-Establishing and maintaining Woods and Bushes and improving their trees (E)<br>-Maintenance of the Health and veterinary popular clinics (E)<br>-Establishing, managing and supplying Agricultural Guidance Departments, collecting the agricultural and animal statistics, controlling the agricultural plights, executing the agricultural interdiction, distributing and selling seeds (T)<br>-Establishing, supplying and managing Hospitals and Veterinary Popular Clinics, Centers and Departments for controlling animals and poultry diseases, controlling flaying and testing meats (T)<br>-Establishing and managing museums, exhibitions and libraries related to animal and agricultural sciences (T)<br>-Establishing, supplying and managing local animal's gardens (T)<br>-Establishing, supplying and managing the agricultural rooms, typical and experimental fields and farms, and the agricultural schools (T)<br>-Establishing, supplying and managing Stables for the animals prepared for improving the birth(T)<br>-Establishing, supplying and managing apicultural stations, fish farms and cows breeding shops and pools, selling and marketing them (T)<br>-Establishing, supplying and running Dairy plants, Centers for gathering & cooling dairy and marketing them to the plants (T)<br>-Establishing, supplying and managing interests of Machines and agricultural Machinery, leasing them to the farmers for harvest, threshing , cultivation, cleaning purposes, like irrigating brooks and establishing Cooperative Agricultural Companies participated by the local Administration and taking part in its management (T)<br>-Establishing, supplying and managing Cotton Ginning Plants, Centers of supplying Chemical and Organic Fertilizers and encouraging utilizing and selling them by the farmers (T)<br>-Establishing, managing Mechanical Units to repair Pumps and Agricultural Machinery (T)<br>-Providing cooperation and facilities for the farmers, distributing seeds and good seedlings for agricultural purposes (T)<br>-Forming Agricultural Cooperative Societies, supervising them and offering financial and moral supports to discharge their duties (T)<br>-Giving suggestions about executing the Agricultural Reform Law (T) |
| Industry | Establishing and managing Carpentry and Textile Factories and Printing Houses (E) |
| Culture | -Establishing, supplying and managing public Libraries (E)<br>-Establishing, supplying and managing the media headquarters and offices (T)<br>-Establishing, supplying and managing Museums and the local archeological sites (T)<br>-Establishing, managing a Tourism Board, encouraging increasing the archeological and historical sites, and preparing their means of convenience (T)<br>-Supervision of typing and publishing newspapers, local magazines, books and encouraging the authors and writers (T)<br>-Establishing, managing theaters and artistic groups and organizing the local artistic competitions (T)<br>-License of presenting movies, acting novels and a license of the artistic and acting groups (T) |
| Economic Development | -Opening, establishing and managing exhibitions for the animal wealth, local industries and commercial purposes (E)<br>-Establishing booths and modern markets outside the boundary of the Municipality (E)<br>-License of opening Chambers of Commerce, supervising them, and to decide dissolving them according to the concerned law (T)<br>-Establishing, supplying and managing the economical interests to provide the necessary requirements for the citizens (T)<br>-Establishing, managing the interests of marketing the agricultural yields, local industries and storing them (T)<br>-Developing the local Industries, establishing and managing the shops to sell them (T) |
| Education (elementary, secondary and technical) | -Establishing, and managing Primary schools and kindergartens, Basic Education Centers and eradicating illiteracy (E)<br>-License of opening private primary schools and kindergartens (E)<br>-Performing Nutrition programs for the students of primary schools kindergartens, and provision of clothing (E)<br>-Establishing the buildings of the Intermediate and Secondary Schools, Boarding Departments, Clubs, Halls, Stadiums and Swimming pools (E)<br>-Opening, establishing and managing technical, vocational and craft schools and Institutes (E)<br>-Choosing and appointing the sites of establishing the Primary Schools (E)<br>-Opening, establishing and managing Intermediate and Secondary Schools (T)<br>-Opening, establishing and managing the Boarding Departments and their maintenance (T)<br>-Establishing Residential houses for the teachers except the University Education (T)<br>-License of opening the private Intermediate and Secondary Schools in light of the General Policy of the Education in a way that will cope with the local requirements according to the required conditions and granting support to them (T)<br>-Submitting proposals about establishing Scientific Institutes and Colleges of the Governorate (T)<br>-Using the local language besides the Arabic language in the Primary Education stages at the Administrative Units whose majority are of the residents of non-Arabs (T)<br>-Controlling executing the curriculums required by the Ministry of Education and Teaching, submitting recommendations, application and suggestions problems related to amendments which are required by the local Environment (T)<br>-Determining dates of the school holidays according to the local circumstances, taking into consideration the longitude of the required academic year excluding the dates of the Ministerial |

| | |
|---|---|
| | General Examinations decided by the Ministry of Education and Teaching (T)<br>-Determining the daily study times in a way that do not contradict with the hours required in the academic curriculums prepared by the Ministry of Education and Teaching (T)<br>-Executing Illiteracy eradication policy which is decided by the Government (T)<br>-Choosing the sites of the Boarding Schools within the specialty of each council (T).<br>-Facilitating all what is related with the School Health Care (T) |
| Health Care (primary, secondary and tertiary) | -Establishing the fixed popular Health clinics and ambulance service (E)<br>-Establishing, supplying and managing the Public Hospitals (T)<br>-Establishing, supplying and managing Ophthalmology Hospitals (T)<br>-Establishing, supplying and managing Thoracic and Mental Diseases Hospitals, Viral Hospitals, Pediatrics, Maternity, Motherhood and Childhood (T)<br>-Establishing, supplying and managing School and Training Courses for female-nurses and male-nurses, midwifes female and male medical dressers, Medical Users and circumcisers (T)<br>-Establishing, supplying and managing Medical drugstores attached to the Administrative Units (T)<br>-Forming and managing the Local Medical Committees(T)<br>-License of opening private Hospitals according to the bases placed by the Ministry of Health and determining the wages fulfilled by these Hospitals and to supervise them (T)<br>-License of opening the private medical clinics according to the bases formulated by the Ministry of Health and determining the wages fulfilled by the physicians in these clinics (T)<br>-License of opening Pharmacies according to the bases placed by the Ministry of Health and to supervise them (T)<br>-License of female-nurses and male-nurses, medical female-dressers and male-dressers, midwifes, circumcisers, medical users according to the bases put by the Ministry of Health (T)<br>-Establishing, supplying and managing all popular clinics and external clinics (T)<br>-Establishing, supplying and managing Health Institutions related to schools students according to the bases designed by the Two Ministries of Health and Education and Teaching (T)<br>-Establishing, supplying and managing Preventive Health Units according to the plan formulated by the Ministry of Health (T)<br>-Establishing, supplying and managing the Units of controlling harmful insects (T)<br>-Appointing Hospitals, Popular clinics and Health Institutions (T)<br>-Hospitals, Typical Health Institutions and Hospitals prepared for purposes of Scientific Research and Training are to be excluded from the provisions of the previous items (T) |
| Housing | -Establishing Residential houses for the employees and users of the local Administration (E)<br>-Executing residential projects for the citizens, selling, leasing and selling the residential lots of land to them (T)<br>-Constructing the Governmental Buildings (T)<br>-Maintaining and up keeping the Governmental Buildings (T) |
| Communications | -Opening and establishing sub-roads that connect the district villages (T)<br>-Establishing passage ways, arched bridges and small bridges (E)<br>-Maintenance of the main roads that connect the Governorate Centers by the relevant Administrative Units (T)<br>-Supervision of opening and constructing the main roads, arched bridges and bridges which are out of their powers, and suggesting what is required to them to the competent Ministry (T)<br>-Submitting suggestions to the Ministry of Communication concerning the movement and direction of the trains, establishing stations and improving the services in the railways (T)<br>-Submitting recommendations related to improving the services in the ports and anchorages (T)<br>-Establishing, supplying and managing interests of water transportation of the passengers (T) |
| Irrigation | -Establishing, maintaining dams and controlling floods as decided by the Departments of Irrigation (T)<br>-Opening, purging brooks and agricultural canals whether they were on the account of the local Administration or the beneficiaries or both of them (T)<br>-To suggest establishing dams, opening up brooks and cultivating lands (T) |
| Land Use & Zoning | Establishing modern villages, and entering improvements on the established villages (E) |
| Recreation and Sports Activities | -Establishing, supplying and managing Public facilities of the youth according to the plan of the competent Ministry (E)<br>-Establishing and managing public gardens (E)<br>-Establishing and managing Sport Stadiums, Meeting Halls, Acting Halls, and Public Swimming pools (E)<br>-Establishing popular baths outside the boundary of the Municipality (E) |
| Labor and Social Welfare | -Establishing and managing Nurseries (E)<br>-Submitting cash or moral supports for the handicapped and charity societies (E)<br>-Establishing and managing Charity Institutes (E)<br>-License of the Cooperative Societies according to the Cooperative Societies, to supervise them and dissolving them (T)<br>-Establishing, managing and financing manual rural Industries, and establishing exhibitions and their propaganda (T)<br>-Fixing the payment the relief compensations in case of disasters and general catastrophes, and also settling the payment of the cash and moral various social aids not exceeding Ten Dinars per case (T)<br>-Establishing, managing the Aged houses and workshops for the handicapped (T)<br>-Establishing and running work offices and finding work for the unemployed (T)<br>-Establishing, managing Bureau for inspecting interests, Companies and Private and Official Plants to make sure of executing the labor law in them, and taking procedures stipulated upon in the labor law against the violated under this said law (T)<br>-License of nightclubs and movie houses (T)<br>-Establishing, managing and supplying homeless and criminals houses and schools, kindergartens for the foundlings and those poor people who have lost their mothers and schools for poor orphans (T)<br>-Establishing, managing and supplying bread bakery, various bakeries for baking bread, selling it with low prices (T) |

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| | -Buying cereals, milling them and distributing them on the Administrative Units (T)<br>-License of the private bakeries to bake bread and providing wheat to be distributed on the needy people in low prices, and controlling labor and production at these bakeries (T)<br>-To decide to include the Administrative Units or villages by ration when necessary & particularize the quantity of wheat or flour required monthly & also increase or decrease its specified quantities according to the need (T) |
| Tourism | -Establishing and managing Hotels and Reception Houses (E)<br>-Organizing parties and festivals in the National occasions or for Official purposes (E) |
| Security | -Establishing the buildings of the police Stations (E)<br>-Maintaining the buildings of the Police Stations and Centers (E) |
| Public Assets Management | -Maintaining the buildings, and establishments of the local Administration (E)<br>-Undertaking the management of Real-estates and movable funds of the local Administration (E) |
| Other infrastructure | -Executing the projects and works whose credits are certified in the balance of the economical plan of the local Administration in the Governorate (E)<br>-Establishing, managing and supplying water and electricity projects in the villages in which there are no Municipality (E) |

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**Chapter X**

# Budgeting Under Resource Abundance and Hesitant Steps to Decentralized Investment Planning and Budgeting in Iraq

**Ronald W. Johnson**

**Ricardo Silva-Morales**

## Political and Economic Background

This chapter describes Iraq's overall budgetary decision-making structure and process since the adoption of the 2005 Constitution and focuses on capital investment planning and budgeting. Iraq's budgetary structure and process is influenced by traditions from the previous regime and conflicts that became manifest after the Saddam Hussein regime was overthrown by the U.S. Sectarian tensions since 2003 have intruded into the policy process, including budgetary decision making. Tensions between the desire by many to limit the power and authority of central government and concerns by others that a weak central government could not successfully address internal security conditions also have had an impact. The first part of this chapter focuses on the framework for budgetary decision making. The second part of this chapter focuses on investment planning and budgeting to address severe public service delivery deficits caused by a neglected and crumbling public infrastructure base.

Iraq's 2005 Constitution created a mixed federal/unitary system that gave constitutionally protected authority to regions and governorates (provinces), but ensured central legislative

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authority over important provincial structures and authorities. Central government ministries are responsible for providing basic public services throughout those provinces not organized into a regional government. However, public investment planning within regions and provinces is a decentralized authority. The central government makes modest central budget allocations to regional and provincial authorities for investment projects. The majority of capital investments is contained within central ministry budgets and is implemented by central ministries. Provincial operating budgets for elected provincial councils and governors (selected by councils) are appropriated in the annual central government Budget Law and, like the investment funds, are considered transfers or allocations of the central budget, not intergovernmental grants or revenue sharing.

Investment budgeting takes place in a context of tensions between those that prefer greater decentralization of authority, partly in response to excessive centralization of the previous regime, and those that prefer a more modest decentralization, partly out of fear of a tyranny of the majority and also from a strong tradition of central control that is comforting during periods of conflict. Budgeting, and other public sector decision making, is further complicated by ethnic and religious schisms and by weak central executive authority over functional and operating ministries.

Iraq is a resource-rich country. The politics of relative abundance, more so than the politics of relative scarcity, influence the budget process. Government in Iraq has historically dominated and currently dominates the economy. The government budget is between 55 and 65 percent of gross domestic product, and oil revenues constitute 90 percent or more of public sector revenues. [1] During the previous regime, public sector resources, mainly from oil and, to a lesser degree,

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agriculture, were redistributed to favored regions of the country and were controlled by favored party officials.

Budgeting in Iraq, like other natural resource-rich countries in which the state controls the distribution of wealth from natural resources, focuses more on the allocation of revenues from the exploitation of oil than on expenditure priorities. During 2006 through 2008, the planned budget had little correspondence with the executed budget. Budgeting activities in Iraq have focused more on mobilizing funds (from oil revenues) during the budget year than on developing and executing an expenditure plan.

Taxation, beneficiary charges, and other forms of generating public sector revenue have never played a significant role in budgetary decisions. The price of oil on the world market is the primary determinant of public sector revenue availability. Expenditures are subsequently adjusted to fit the expected revenue. Since the new government was elected after the 2005 Constitution, oil prices have fluctuated wildly, causing the government budget to range from approximately US$30 billion to US$70 billion in the budget years 2006 through 2008, with a planned 2009 revenue budget of approximately US$42.7 billion. The 2009 Budget Law estimated expenditures of US$58.6 billion. The deficit would be covered by reserves created by 2008's extraordinarily high oil prices, causing a carry-over of unspent 2008 funds. The carry-over was caused by mainly slower than planned implementation of capital investment projects from 2006 through 2008. [2]

**Structure and Process**

***Budget Framework and Budget Preparation***

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Budgeting in a multiparty framework is new to Iraq, dating from the development of a parliamentary democracy following the U.S. overthrow of Saddam Hussein's regime in 2003. The budgetary process reflects a constitutional structure created in 2005 and implemented with national elections in 2006, with a modest degree of decentralization of authority and responsibility to subnational units of government. The politics of the budgetary process is shaped by the process of reconciling historical regional conflicts within Iraq, as well as sectarian conflicts awakened by the destruction of the previous authoritarian regime. Continuing security costs have dominated budget allocation among sectors, with about half of the budget going to various security functions.

The budgetary process in Iraq is evolving from a history of centralized regimes that were dominated by executive power emulating soviet-style central planning to a system with a greater degree of separation of powers at the center and modest decentralization of authority to subnational governments. Under the most recent regime prior to its overthrow by the U.S. in 2003, centralization had reached an extreme with a formal structure favoring executive power and no delegation of authority to regions or provinces. In addition, the President wielded both formal and informal control over all societal resources through his leadership of a single party—the Ba'athist Party. Leadership succession in the Ba'athist Pary was often marked by coups and violent overthrow.

The Constitution grants specific authority to the national government, including the authority to exploit the oil resources, to control water sources that originate outside the borders—mainly the Tigris and Euphrates Rivers—and to formulate foreign and national security policies. Other authorities are shared between national government and regional or provincial-level government,

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including regulating electrical energy, environmental policies, development planning, public health and education policy, and internal water resources. All other powers "not stipulated in the exclusive powers of the federal government belong to the authorities of the regions and governorates that are not organized in a region" (Article 115 of the Constitution). [3] There are considerable differences between the powers reserved to a region and to provinces. The Constitution permits provinces to form regional governments, with the Kurdistan Regional Government (KRG) having been recognized simultaneously with the adoption of the Constitution. Regions may write their own constitutions, as long as they do not contradict any part of the national Constitution. A regional government enjoys considerable autonomy over governmental structure and authority within the region, as well as public finance.

Provinces, on the other hand, yield to considerable central legislative authority over the provincial-level exercise of constitutional powers. Detailed specifications of the structure of provincial government, revenue authority, and other functions are subject to national legislation. Article 122 of the Constitution stipulates that "A law shall regulate the election of the Governorate Council, the governor, and their powers." Article 123 of the Constitution states that "Powers exercised by the federal government can be delegated to the governorates or vice versa, with the consent of both governments, and this shall be regulated by law."

The draft general budget and the development plan for the state is the responsibility of the Council of Ministers under the direction of the Prime Minister (Article 80 of the Constitution). Iraq's first elected government under the 2005 Constitution was initially characterized by a weak and complex coalition of political parties. Ministry leadership posts were negotiated with key parties and factions in the coalition. Hence, the Council of Ministers included numerous

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ministers more loyal to their party or faction than to the government. The provincial elections of 2009 resulted in a somewhat surprising show of strength for the Prime Minister's party at the provincial level, potentially strengthening his hand for later national elections and with the Council of Ministers. However, as is typical of parliamentary systems, some ministers have greater control over ministry budgets than the Prime Minister, given the necessity of negotiating a coalition in order to form a government. [4]

The draft General Budget is to be submitted to the elected Council of Representatives (COR) prior to the next budget year (January 1 through December 31). Typically the draft general budget and the Budget Law are not completed before the beginning of the budget year, and ministries spend in accord with a continuing resolution. Once the COR passes the Budget Law, the Presidency Council has the authority to review and comment and, on occasion, recommend changes in the legislation. Once negotiations between the Presidency Council and the COR are complete, or the COR overrides the Presidency Council with a 60 percent majority, the annual General Federal Budget Law is decreed. The decree is followed by implementation instructions from the Ministry of Finance (MOF).

Budget authorizations are limited to the budget year, and do not carry over to the following year, although exceptions can be granted. [5]

**Table 1** illustrates the budgeted amounts for the main budget categories for 2006 through 2009.

[insert Table 1 here]

The figures for 2006 through 2009 make clear the effects of the 2008 oil price spike. A supplemental appropriation—a 40 percent addition to the original 2008 budget—was approved

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in mid-2008, bringing the original US$50 billion budget to just over US$72 billion for the year. Subsequent oil price drops brought the anticipated revenue for 2009 back down to 2007 levels.

**Table 1** also illustrates the budget split between capital or investment budget and current operating budget—typically 24 to 29 percent of the total budget has been appropriated for capital investment projects since 2006. Of the total investment budget, 30 to just more than 50 percent has been allocated to investment or capital projects/acquisitions under the authority of the provincial or regional governments. The 2009 budget law passed in March 2009 reflected the drop in oil prices below US$50 per barrel. The biggest loser in the budget cuts for 2009 was the category of allocations to provincial and regional governments, and capital investments in general. Budgeted investment as a percent of total budget was down in 2009 to 22 percent, but provincial and regional government absorbed most of the cuts with their share of the investment budget falling below 20 percent.

***Budget Implementation***

**Table 1** illustrates budget appropriations. Implementation of budget appropriations has consistently lagged since the first budget after the 2005 Constitution. Central ministries, and to a somewhat lesser degree provinces, have consistently been unable to implement the full budget. Between 2006 and 2008, only 65 to 75 percent of the budget actually was expended during the budget year. [6] A U.S. General Accounting Office (GAO) analysis notes that the Iraqi government spent 80 percent of the current operating budget but only 25 percent of the funds allocated to capital investments.

**Table 2** displays the MOF's official record of budgeted versus actual expenditures, in broad terms.

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[insert Table 2 here]

According to the MOF's figures, between 67 and 69 percent of the 2006 through 2008 budgets were executed, on a cash basis, during the budget year (by the end of December 31). Just over 30 percent of the budgeted funds were not expensed in those budget years. **Table 2** also illustrates the differences between operating and investment budget execution. For example, in 2008, 80 percent of the operating budget was executed in the budget year, but only 40 percent of the investment budget.

Of the investment budget, the performance of the KRG and the 15 provinces in capital investment execution was better than the performance of central ministries, as will be discussed more fully in the next section on development planning and budgeting.

There are practical and technical explanations for the large discrepancies between budgeted and expended amounts. High levels of violence from mid-2006 to early 2008 contributed to a much slower execution of construction projects. Additionally, skilled personnel in key ministry positions were lost early in 2003–2004 to the de-Ba'athification process and migration outside Iraq by many technical professionals in government employ. Further, there are significant differences in accounting for expended funds. As the GAO noted in an analysis of data weaknesses in assessing Iraq budget performance, the government of Iraq operates on a cash basis. [7] Funds are considered expenditures only after receipts are presented and funds are paid out. Based on these accounting methods, capital investment expenditures lag considerably behind current operating expenses and substantially behind expenditures for government employee salaries.

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Overall, budget implementation in Iraq reflects the budgetary politics of relative resource abundance. Budgeting is about anticipating revenues from oil, and expenditure plans generally are not up to revenue levels. In the future, starting with 2009, it would not be surprising to see actual expenditures come much closer to the budget figures in years in which oil prices are lower on the world market. That would be consistent with budgeting in other resource-wealthy countries.

**Capital Investment Planning and Budgeting**

The legacy of the Iran-Iraq war, Iraq's invasion of Kuwait and the subsequent first Gulf War, a decade of international sanctions following that war, and mismanagement of the country's public resources was a crumbling infrastructure base. Both the U.S. reconstruction program and the Government of Iraq's budget process have struggled to remedy this situation. [8]

Budget reform to address the public infrastructure deficit since 2003 has had both political and technical dimensions. The political dimension has been the attempt to balance the tensions between control of investment budget decisions by the central government and by regions and provinces. Technical budget reform, both during the U.S. Coalition Provisional Authority administration of Iraq and since the adoption of the 2005 Constitution, has focused on improving the capital investment planning and budgeting process more so than current operations budgeting. Donor participation in budget reform has focused on the development planning process and, through the International Compact with Iraq in 2006, attempts to assist Iraq in developing a Medium-Term Expenditure Framework (MTEF) approach. The following sections analyze the development planning framework and process, and capital investment budgeting and execution.

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***Multiyear Development Planning: Central versus Local***

Capital investment planning in Iraq is a subset of the larger national development planning process. Public administration in the modern era (since the 1950s) reflects a tradition of multiyear national development planning dominated by the central planning agency—today the Ministry of Planning and Development Cooperation (MOPDC). Historically, central planning in Iraq was influenced by assistance to the Ba'ath Party government from the Socialist Republic of Poland. This model of central planning corresponded closely to the Soviet Union's approach to managing public finances. In the former Soviet central planning approach, the central planning committee—Gosplan—controlled decisions on all available resources including public funds, particularly capital investment funds. Emulating the Soviet style, Iraq's MOF was more an implementation agent for central planning and the responsible party, along with the Central Bank for the treasury function of controlling financial flows. Multiyear (five-year) development plans under the Ministry of Planning's control encompassed both the allocation of national economic resources to the public sector and the allocation of the investment portion of the budget among public sector functions. With as much as 80 percent of the economy in the public sector, the control of the development planning process was the top political prize.

Since 2003, Iraq's centralized national planning model has been challenged on several fronts. The first serious challenge to central government control of development planning was the U.S. reconstruction program. The sheer size of the U.S. reconstruction program was, in 2003–2004, the dominant source of "public sector" investment capital. This US$17 billion reconstruction program [9], whatever its successes and failures in effectively rebuilding the infrastructure base, introduced a planning and decision-making process largely outside the influence of Iraqi

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authority, even after the end of the formal occupation. Throughout the interim and transitional Iraqi governments (mid-2004 through 2005) and the first years of the constitutional government (2006–2007), external donor funding, mainly from the U.S., created a donor-driven capital investment budget decision-making process parallel to that of the Government of Iraq. Donor-funded investment choices were based largely on donor perceptions of investment needs and not integrated with the government's investment decision-making processes. In 2003–2004, virtually the only investment spending was the externally funded reconstruction program. In 2005–2006, externally funded investment spending in total was still a major proportion of total investment spending. This donor-driven process weakened the function of central planning, although initially it did not contribute to the development of an alternative. However, as the Government of Iraq's own allocation to capital investment starting in 2006 grew from approximately US$2.5 billion to approximately US$8.5 billion in 2008 (investment *expenditures* as shown in **Table 2** above), the quantitative impact of external investment funding on Iraq's own investment planning and budgeting waned.

The second challenge to the historical dominance of central planning in Iraq was the shift in U.S. strategy for building the capacity of Iraqi institutions. An initial U.S. focus on central government strengthening shifted to an equal or greater focus on strengthening the role and capacity of provincial and regional governments, in order to reinforce the modest decentralization features in the Iraqi Constitution (Article 112). The U.S. introduction of Provincial Reconstruction Teams (PRTs) in late 2005–2006 focused much of the U.S. development effort on strengthening provincial and regional government. The PRTs promoted a more decentralized decision-making process that emphasized, at least somewhat, provincial

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priorities in capital investments. Further, the overall international donor community's engagement with Iraq, formalized initially in the International Compact with Iraq in 2006, represented a key role for subnational government in development planning and budgeting. The Compact emphasized devolution in the planning process, noting that Iraq was undergoing a "major transition from a highly centralised model of managing the economy to one based on devolution." Further, the Compact expressed the Government of Iraq's pledge that the "transition to regional, governorate and area-based development is a central theme in Iraq's National Development Strategy and will be supported in the Compact implementation. Transition should be a gradual process, given the high degree of centralization in the Iraqi economy at present, legislative and regulatory gaps and low and variable planning and execution capacities at both national and sub-national levels." [10]

The international donor focus exemplified in the International Compact with Iraq also stressed Iraq's adoption of the MTEF approach as the vehicle for integrating macroeconomic forecasts and policies with investment planning and budgeting. The MTEF approach seeks to integrate multiyear development planning, macroeconomic forecasting—especially public sector revenue forecasts—and multiyear capital or investment budgeting. [11] The donor community sees the MTEF as a particularly important tool for Iraq because of the dominance of oil in the country's economy and the public sector budget, and the volatility of oil prices. The MTEF's objective in Iraq is to develop a rational public sector investment planning and budgeting process that can operate within a safe margin of oil price fluctuations, while planning for an effective use of surpluses that arise from unanticipated price increases. For Iraq, the complications have been largely on the side of integrating development planning; translating development planning into

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specific, multiyear capital budgets; and implementing budgeted capital projects. At least in Iraq, the MTEF approach has tended to strengthen the hand of the MOPDC.

The third challenge to a completely centralized investment planning process is Iraq's own national legislation that further specifies the powers and authority of provincial-level governments, the *Law of Governorates Not Incorporated into a Region.* [12]. Article 7, paragraph 4, specifies that the governorate (provincial) council shall: "Outline, in the development of the plans for the governorate, the general policies in coordination with the competent ministries." In conjunction with the general provisions of the Constitution that assign all powers not specifically designated as central government or shared with central government to regions and provinces and the National Development Strategy, this paragraph generally is interpreted to give subnational government the authority to prepare multiyear development plans that either contain or implicitly lead to multiyear investment plans.

***Developments in the Practice of Provincial Development Planning***

Within the context of the formal policies and the mainly external circumstances that have led away from total central control over development planning to a shared responsibility with regional and provincial government, the 18 provinces began a process in 2007 of preparing a *provincial development strategy* (PDS) as a local initiative. No formal instructions or guidelines from MOPDC preceded this bottom-up process of provincial development planning. [13] External donor assistance (U.S. Agency for International Development [USAID]) provided logistics and financial support, technical support for facilitating the process in each province, and various other external resources, including the technical and logistic capabilities of PRTs.

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Each province created a PDS planning or coordinating committee, usually at the invitation of the governor or the provincial council. In some provinces, the PDS chairperson and other key leadership positions were filled by elected provincial officials; in other provinces, provincial government supported and participated in the process, but business, professional, and traditional leaders (tribal and religious) and other private citizens provided the primary leadership. Workshops facilitated by private Iraqi citizens trained in participatory planning processes established committees to carry out functional tasks, reviewed and discussed committee reports, formulated broad statements of economic and social vision, and ultimately developed, to varying degrees of specificity, a statement of longer-term strategy. Longer term meant different things in different provinces. Basrah Province, for example, prepared a two-year strategy, whereas Babil, Baghdad, and other provinces prepared four- to five-year strategies.

The general form for each PDS was similar across the provinces. An assessment phase of the planning process identified key economic, social, and public services weaknesses. Some assessments were impressionistic views resulting from open public meetings. Other provincial assessments were more quantitative, relying on data from various central government ministries on service delivery, economic base (mainly state-owned enterprises), and social issues, such as numbers of displaced persons. The assessment phase was followed by general discussions in the PDS committees, including several large, open public forums to in some provinces to identify the highest priority issues. Anbar Province's PDS committee was composed of approximately 100 individuals from provincial-, district-, and subdistrict-level government; some traditional leaders; and leaders of private business (transportation and construction/engineering). This committee met mostly outside the province because of the high intensity conflict occurring at that time.

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Kirkuk Province's PDS committee involved hundreds of citizens through numerous public meetings.

From the priority setting process, a broad statement of ambition or vision was developed in most of the provinces. Some provinces started with a broad vision statement prior to assessing conditions in the province. Several provinces had extensive involvement from central ministries responsible for service provision at the provincial and cross-provincial levels, while others had limited input and coordination with central ministries. Baghdad Province, for example, had representatives from more than 30 central ministries in almost every general session and many of the working group sessions. Muthanna Province had little involvement from central ministry personnel in the province, likely because it is remote from Baghdad and central ministry management and central ministry leaders issued no instructions or guidelines for province-based personnel to participate in the PDS process.

The culmination of the PDS process was the formal delivery of bound copies of their PDS by each of the provinces in an official ceremony in May 2008, presided over by the Prime Minister and the Minister of Planning and Development Cooperation. All 18 provinces participated in the ceremony, and the central government leadership committed to incorporating the basic provincial strategies in the overall national development strategy in ensuing years. To observers, MOPDC was caught somewhat by surprise that the process would have produced strategies that represented a fairly broad swath of Iraqi society in every single province. [14] One of the subsequent responses was for the MOPDC to increase its staff in the provinces, creating offices to coordinate provincial planning among the ministries. This action was interpreted by some as an attempt by the MOPDC to regain the initiative from the bottom-up provincial process. [15]

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***Linking PDS to Investment Planning***

The importance of the decentralized PDS process for capital investment planning and budgeting is the extent to which strategies lead to investment priorities that, in turn, result in the development of detailed investment plans and budgets. In that respect, the variation across Iraq's provinces was pronounced. The Baghdad PDS, for example, contains approximately 50 pages of text describing conditions in the province and laying out a broad strategic vision. This is followed by 70 pages that briefly list several hundred capital investment projects organized by sector, problems addressed, parties responsible (a specified central ministry budget or planned by the Province to be funded through the MOF investment budget allocations to Baghdad Province), implementation schedule between 2008 and 2012, and estimated costs by year. [16] Other provinces include no specifically identified capital projects at all, deferring the process to the subsequent preparation of a provincial development plan; and still other provinces' PDS contain only those projects the province anticipated funding in the year the strategy was prepared, from funds allocated by the MOF.

With the provincial elections of January 2009 and the subsequent formation of new provincial governments, experience has not been sufficient to predict whether the PDS process will continue with periodic review and revision of basic strategies and with the development of more thorough multi-year capital investment plans and budgets. Some provinces used the process to generate broad population support to address provincial priorities (Kirkuk, for example). Other provinces used the PDS process to generate comprehensive economic development programs. For example, from the PDS process and other activities by the governor and provincial council, Najaf launched a major program of capital investment financed by revenues produced by

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religious pilgrimages to holy sites in Najaf and nearby provinces. The PDSs of the three provinces of the KRG had their strategies subsumed by and into the more comprehensive regional economic development strategy.

***Iraq's Performance in Capital Budgeting and Budget Execution***

Although some PDSs contain capital investment projects that are planned to be executed over several years (five years in Baghdad's PDS) and include capital projects to be implemented by central ministries and by provincial authority, capital budgeting and implementation has not had a stellar track record since 2006. **Table 2** above shows that since the formation of the constitutional government in 2006, in no year did capital budget execution reach 50 percent of budgeted funds, whereas operating expenditures each year have reached between 70 and 80 percent of budgeted funds.

Provincial-level capital budget execution, however, has been more successful, in two respects—in the proportion of budgeted funds actually being implemented and in the project selection process. **Table 3** differentiates capital budget execution by central government ministries versus provincial capital budget execution.

[insert Table 3 here]

During the three years between 2006 and 2008, the central ministry capital budget execution ranged from as high as 46 percent to as low as 23 percent. By contrast, provincial capital budget implemented (expensed) as a percent of the budgeted total was 57 and 60 percent in 2007 and 2008, respectively. The provincial capital budget expensed was low in 2006—31 percent—because the capital allocation to provinces was made four months into the budget year, and this was the first time the provincial-level governments had the authority to make capital budget

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decisions and implement capital projects. It is also noteworthy that the central ministry performance, as low as it is, is still somewhat exaggerated. In 2007 and 2008, letters of credit issued in advance of expenditures were counted as executed budget for the central government. This deviates from the otherwise cash or expense accounting basis for budget execution. The letter of credit mechanism enables ministries to purchase equipment from abroad or to enter into other contracts. However, a letter of credit does not represent an actual transaction; only when a vendor is paid on the letter of credit has an expenditure taken place. For example, during 2007, of around US$8 billion in letters of credit requested by central ministries, only 50 percent actually turned into expenditures. The average processing time was 10 months. [17] If calculations had been made only on a cash basis, central ministry execution would have been less than reported in **Table 3**.

There are three related explanations for the difference in performance between central ministries and the provinces. First, the letter of credit process, as noted in the previous paragraph, delays capital budget execution because central ministry projects involve more imported capital goods. Capital goods imports, in turn, depend upon issuance of letters of credit. Hence, the slow process of obtaining letters of credit delays imports, and in turn delays capital project execution. Second, central ministry projects generally are larger and more technically complex than the capital projects implemented by provincial governments and require more time to implement. Third, provincial governments have more political stake in demonstrating public service improvements. The implementing authorities are the elected provincial councils and the governors and their execution of the budget is likely to influence voter behavior. The January 2009 provincial elections seem to support this assertion. About 80 percent of the provincial

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council members elected were first-time council members, reflecting general public dissatisfaction with the pace of improvement in basic conditions in Iraq. [18] On the other hand, central ministry budget execution is much less visible to voters, and the incentives to perform are more related to bureaucratic incentives. It is important to note that a substantial proportion of the low level of capital budget implementation is concentrated in only a few ministries, mainly the oil ministry. Nonetheless, the decentralized portion of the capital budget has been characterized by better performance than the central ministry portion.

A second aspect of provincial performance in capital budget planning and execution has been in project selection. Under the centralized planning model and a regime that was not subjected to any form of accountability to the public, central ministries made decisions without any means of public input. In the three years that provincial authorities have had capital funds at their discretion (2006–2008), they have been subject to election and, by virtue of the local nature of projects budgeted and executed, their performance has been more visible. It may even be the case that provincial officials elected in 2006 suffered in the 2009 elections for the overall weak performance of central and provincial government in revitalizing Iraq's public infrastructure base.

To the provinces' credit, there are partial data that indicate attempts on the part of provincial officials to fund investments that conform to the population's expectations. **Table 4** illustrates preliminary data for 2006 investment project implementation by 10 provincial governments. [19]

[insert table 4 here]

The table shows the U.S. dollar amount and percentage of project value implemented in those 10 provinces by sector. Priority areas were the improvement of water, health care, and

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municipalities' services. Municipalities' services include solid waste collection and disposal, street maintenance, street lighting, drainage, and similar basic municipal functions. A second cluster is also apparent—education and sewage. Almost 94 percent of the investments were concentrated in the eight sectors that have consistently been shown to be the highest priority in various public opinion polls. [20]

Since 2007, as described in the discussion of the PDS process, provincial capital investment planning has been increasingly characterized by participatory processes that involve district- and subdistrict-levels of government, as well as citizens, opinion leaders, and, in some provinces, hundreds of individuals. Generally, at a minimum, the selection of capital improvements sectors in which to invest at the provincial level has a basis in public opinion and in participatory processes.

There has been push back from those that continue to favor a more centralized state, including the central planning ministry. Since 2008, the MOPDC has been successful in inserting a chapter in the annual budget describing the approved projects by name, which makes inflexible the reorganization of capital investment initiatives during the year. This list includes both projects identified by the provinces and projects planned by central ministries. While there is no evidence from 2008 that MOPDC used this device to reorder provincial priorities, this reassertion of the prerogatives of the central planning ministry reflects the ongoing tensions between decentralization and recentralization of power and authority.

**Conclusions**

Iraq's budgetary framework, and the experience to date from three years of a new constitutional government, reflects a departure from a highly centralized tradition. The extent to which regional

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and provincial governments will play a major role in public sector budgeting remains unclear because there are forces in favor of centralized authority as well as decentralized authority. Evidence on budget execution tends to support the proposition that regional and provincial governments are performing better than central ministries in addressing Iraq's serious infrastructure deficits that are the legacy of decades of war, neglect, and misuse of public funds. 2009 provincial elections also showed some support for the proposition that voters paid attention to performance, which may strengthen the position of regional and provincial government in delivering basic public services. However, future national elections, and the continuing tension between proponents of strong central authority who believe it is necessary to address on-going security issues and proponents of decentralized authority, are likely to mean a budgetary process in flux for some years to come.

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**Endnotes**

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[8] Special Inspector General for Iraq Reconstruction (2009). *Hard Lessons Learned: The Iraq Reconstruction Experience.* Washington, D.C.: U.S. Government Printing Office.

[9] Special Inspector General for Iraq Reconstruction (2009). *Hard Lessons Learned.* Washington, D.C.: U.S. Government Printing Office.

[10] *International Compact with Iraq*. http://www.iraqcompact.org/ici_document/INTERNATIONAL_COMPACT_WITH_IRAQ_FINAL__English_final_2_.pdf (accessed April 15, 2009), pp. 31–32.

[11] A list of documents with country case studies, descriptive material, and critical commentary on the practicality of implementing MTEF is available at: http://web.worldbank.org/WBSITE/EXTERNAL/TOPICS/EXTPUBLICSECTORANDGOVERNANCE/EXTPUBLICFINANCE/0,,contentMDK:20235448~pagePK:148956~piPK:216618~theSitePK:1339564,00.html (accessed May 1, 2009).

[12] RTI (2008). *Law of Governorates Not Incorporated into a Region: An Annotated Text*. Washington D.C., and RTP, N.C.: USAID and RTI. http://www.lgp-iraq.org/publications/index.cfm?fuseaction=throwpub&ID=274. All references to the text of the Law and interpretations of its meaning refer to this document.

[13] RTI (2007). *Writing the Future: Provincial Development Strategies in Iraq, Volume I.* Washington, D.C., and RTP, N.C.: USAID and RTI. http://www.lgp-iraq.org/publications/index.cfm?fuseaction=throwpub&ID=187. Discussion of the PDS process is based on this document and the authors' participation in phases of the process.

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[14] Authors' observations of the formal presentation ceremony and comments made by the Minister and other ministry staff at the workshops to discuss next steps, held on the same day as the formal presentation.

[15] Authors' interviews with the coordinator who was appointed by the Minister of Planning during the workshop.

[16] *Baghdad Provincial Development Strategy*. Unofficial English translation, available at: http://www.lgp-iraq.org/publications/index.cfm?fuseaction=throwpub&ID=130.

[17] MOF figures, 2008.

[18] Figures are unofficial counts by RTI staff implementing the USAID-funded Local Governance Program. Opinion expressed is solely that of the authors.

[19] Caution is necessary in interpreting Table 4 because the records only cover 10 of the 18 provinces and are, in some cases, incomplete in the 10 provinces. The results reported in the table should be considered indicative rather than definitive.

[20] Various polls conducted for and reported by ABC/BBC news services, usually at least four times a year since 2005, are readily available, for example: *Iraq and Afghanistan Polls: "Where Things Stand*" (http://abcnews.go.com/PollingUnit/story?id=6627152&page=1)

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Tables

**Table 1*: Total Government of Iraq Budget, 2006–2009 (in millions of U.S. dollars)**

| | 2006 | 2007 | 2008 Initial | 2008 Supplemental | 2008 Total | 2009 |
|---|---|---|---|---|---|---|
| **Total Government Budget** | **33,975** | **41,118** | **49,885** | **22,352** | **72,237** | **58,615** |
| Current (Operating) Expenditures | 25,794 | 31,055 | 36,826 | 14,298 | 51,124 | 45,888 |
| Investment (Capital) Expenditures | 8,181 | 10,063 | 13,059 | 8,054 | 21,113 | 12,727 |
| Central Government Only Investment | 5,681 | 6,432 | 7,511 | 3,771 | 11,282 | 10,293 |
| Allocation to KRG for Investment | 500 | 1,560 | 2,528 | 1,173 | 3,701 | 292 |
| Allocation to Provinces for Investment | 2,000 | 2,071 | 3,333 | 3,110 | 6,443 | 2,142 |
| Total Subnational Allocations for Investment | 2,500 | 3,631 | 5,861 | 4,283 | 10,144 | 2,434 |
| | | | | | | |
| **Percent of Expenditures and Investments** | | | | | | |
| Current Expenditures as Percent of Total Budget | 76% | 76% | 74% | 64% | 71% | 78% |
| Budgeted Investment as Percent of Total Budget | 24% | 24% | 26% | 36% | 29% | 22% |
| Central Investment Only Investment as Percent of Total Budget | 17% | 16% | 15% | 17% | 16% | 18% |
| Regional (KRG) + Provinces Investment as Percent of Total Budget | 7% | 9% | 12% | 19% | 14% | 4% |
| KRG Investment as Percent of Total Budget** | 1% | 4% | 5% | 5% | 5% | 0% |
| Provinces Investment as Percent of Total Budget | 6% | 5% | 7% | 14% | 9% | 4% |
| Regional (KRG) + Provinces Investment as Percent of Investment Expenditures | 31% | 36% | 45% | 53% | 48% | 19% |

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Source: Official MOF figures for 2006 through 2008. For 2009, figures were from *Government of Iraq: The Federal Budget Law of 2009* (U.S. Embassy translation).

* Small discrepancies among Tables 1, 2, and 3 are caused by different treatments of nonfinancial assets and how allocation to the KRG is treated by the MOF in different MOF source documents.

** After the 2007 Budget, allocations to KRG, specifically from the Accelerated Reconstruction and Development Program, were no longer fully distinguished from other allocations to KRG.

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**Table 2: Budgeted versus Executed Expenditures, 2006–2008***

| | Budgeted (in millions of U.S. dollars) | | | Executed (in millions of U.S. dollars) | | |
|---|---|---|---|---|---|---|
| | Total Operating Budget | Projects and Reconstruction Budget | Total Budget | Total Operating Expenditure | Total Projects and Reconstruction Expenditures | Total Expenditure through December 31 Budget Year |
| 2006 | 25,794 | 8,181 | 33,975 | 20,298 | 2,491 | 22,789 |
| 2007 | 31,055 | 10,063 | 41,118 | 21,977 | 4,623 | 26,600 |
| 2008* | 51,124 | 21,113 | 72,237 | 41,032 | 8,471 | 49,503 |

Source for all figures: MOF annual reports, updated as of April 2009.

*Notes:
2008 expenditures are provisional, and include the supplemental budget for that year.
All expenditure figures are cash based as of the end of budget year (December 31).
Authors reclassified budgeted central allocations to KRG and provinces as capital; MOF includes operational expenditures as transfers
Budget amounts are only those appropriated in that year and exclude carry over from previous year's unspent funds.

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**Table 3: Budgeted versus Actual Capital Projects for Central and Provincial Government (in millions of U.S. dollars)***

| | Central Ministries Budgeted Funds | Central Ministries Expended Funds | KRG and Provinces Budgeted Funds | KRG and Provinces Expended Funds | Total Budgeted Funds | Total Expended Funds |
|---|---|---|---|---|---|---|
| 2006 | 3,681 | 1,704 | 2,500 | 787 | 6,181 | 2,491 |
| 2007 | 6,224 | 2,415 | 3,846 | 2,208 | 10,070 | 4,623 |
| 2008 | 11,282 | 2,617 | 9,831 | 5,854 | 21,113 | 8,471 |
| | | | | | | |
| **Expended as Percent Budgeted** | | | | | | |
| 2006 | | 46% | | 31% | | 40% |
| 2007 | | 39% | | 57% | | 46% |
| 2008 | | 23% | | 60% | | 40% |

Source: MOF reports on budget execution, updated as of April 2009.

*Notes:
Marsh lands rehabilitation program included as federal expenses.
Provincial capital allocations originally classified under MOF operational expenses for 2006.
Figures for 2008 include the supplemental budget.
Planned amounts exclude amounts carried over from previous year's unspent budget allocations.

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**Table 4. Sectoral Distribution of Capital Projects in 10 Provinces,* 2006**

| Sector | Amount (in thousands of U.S. dollars) | Percent |
|---|---|---|
| Drinking water and water resources | 83,431 | 15.9% |
| Health care | 81,513 | 15.5% |
| Municipalities | 79,807 | 15.2% |
| Elementary education | 66,062 | 12.6% |
| Sewage and sanitation | 54,714 | 10.4% |
| Roads and bridges | 45,179 | 8.6% |
| Provincial capital city | 44,690 | 8.5% |
| Power generation and distribution | 38,127 | 7.2% |
| Higher education | 11,721 | 2.2% |
| Others | 6,018 | 1.1% |
| Communications | 3,298 | 0.6% |
| Sports and youth | 2,885 | 0.5% |
| Agriculture | 1,586 | 0.3% |
| Intermediate and vocational education | 1,470 | 0.3% |
| Local management | 1,246 | 0.2% |
| Trade | 1,093 | 0.2% |
| Garbage collection and disposal | 960 | 0.2% |
| Security | 891 | 0.2% |
| Environment | 619 | 0.1% |
| Urban planning and development | 540 | 0.1% |
| Parks and other recreation facilities | 226 | 0.0% |
| Islamic foundations for social, religious, and welfare affairs (Awqaf) | 138 | 0.0% |
| Court buildings | 99 | 0.0% |
| **Total** | **526,313** | **100.0%** |

Sources: Provincial Reconstruction Teams and USAID Local Governance Program Staff

* The 10 provinces are Babil, Baghdad, Basrah, Diyala, Karbala, Maysan, Najaf, Ninawa, Salah ad Din, and Wasit.

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