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U.S. HOUSE OF REPRESENTATIVES

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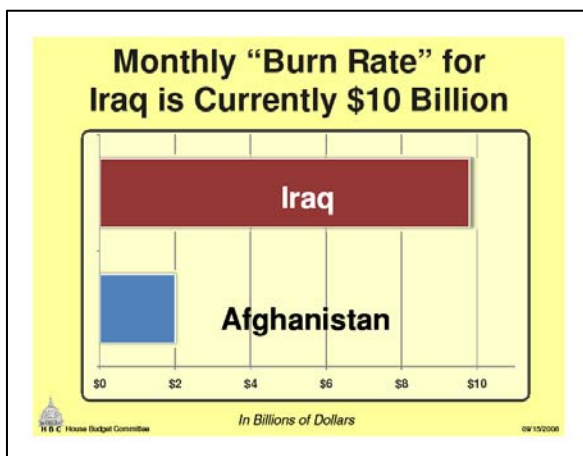
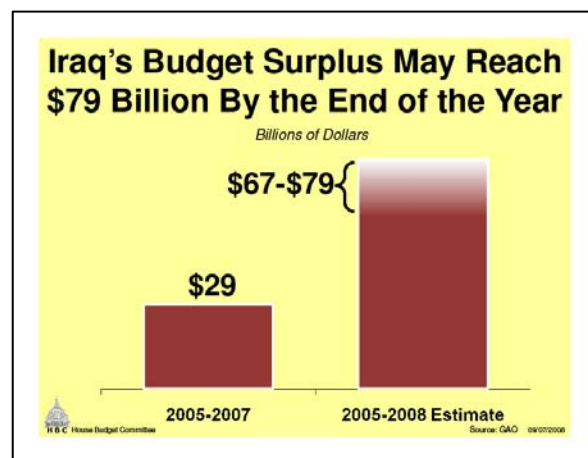
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October 2, 2008

Iraq's Budget Surplus

On September 16th, the House Budget Committee held a hearing on Iraq's budget surplus. Members questioned Joseph Christoff of the U.S. Government Accountability Office (GAO) and other witnesses about GAO's August 2008 report, which concluded that Iraq's budget surplus will increase dramatically this year. GAO found that Iraq's cumulative budget surplus for 2005-2007 was \$29 billion and its surplus could reach as much as \$79 billion by the end of 2008. These numbers are in stark contrast to the Congressional Budget Office's (CBO) latest estimates of the U.S. federal budget. CBO estimates that the budget deficit for the United States will exceed \$400 billion for 2008 – making it the second largest deficit in U.S. history – with an even bigger deficit projected for 2009.

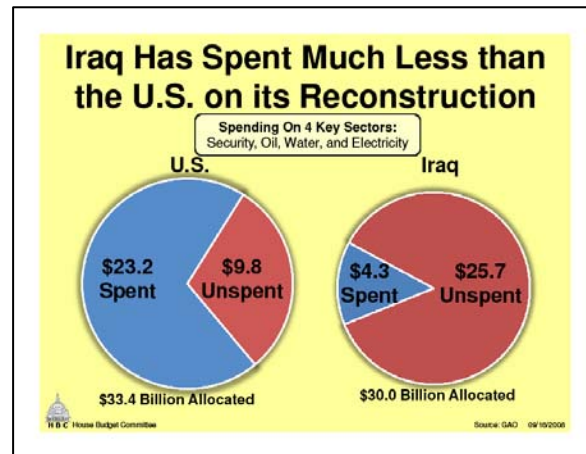
While the United States is committing \$10 billion a month for Iraq, Iraq has budget surpluses that may reach \$79 billion this year. Contrary to the Administration's predictions at the war's start, Iraq has been unable to finance its own reconstruction and security. Since 2003, the United States has provided \$653 billion for the Iraq war, reconstruction, and security – that comes out to \$10 billion per month. About \$50 billion of the total U.S. funding for Iraq has gone to reconstruct buildings and infrastructure and to train Iraq's security forces. In addition, Iraq has allocated \$50 billion of its own resources to these efforts, but it has spent much less than that amount so far. Other nations have pledged \$16 billion in grants and loans, with only \$7 billion of that amount having been provided to date.



According to GAO, the key factors responsible for Iraq's burgeoning surplus are steep increases in oil revenues and its inability to spend significant amounts on reconstruction and security. The chief reasons for Iraq's inability to spend significant amounts of its budget resources are persistent violence, corruption, and smuggling, and a shortage of trained budget and procurement professionals.

Recently, Iraq's oil exports began rising with world oil prices, and its revenues and budget surpluses are growing. Iraq has the world's third largest oil reserves. Crude oil export sales account for 90 percent of its revenues. Iraq's oil revenues for 2008 will be double the average for 2005-2007. This growth in revenues is a major reason that Iraq's cumulative surplus may reach \$79 billion by the end of 2008, as estimated by GAO.

Iraq has failed to effectively carry out plans and maintain reconstruction projects initiated with U.S. help. As part of the total U.S. funding of \$653 billion to date, the United States has contributed about \$50 billion for Iraq's reconstruction and security forces training, and Iraq has dedicated about \$50 billion of its own money. However, Iraq has not actually spent most of its own funding, which is contributing to Iraq's budget surplus. For example, GAO reported that, looking at *four key sectors – security, oil, water, and electricity* – while the United States has spent 70 percent of the \$33 billion it allocated, Iraq has spent only 14 percent of the \$28 billion it allocated for these same four key sectors. As GAO testified, Iraq has no difficulty spending its budgets for such operating expenses as personnel salaries. However, Iraq spends very little of its capital budget – just 28 percent in 2007. Without continuing capital investments by Iraq, projects that Iraq started with the United States are at risk and are faltering.



Witnesses discussed the reasons for Iraq's inability to spend its budgets effectively. Major problems include a shortage of trained budget staff, weak procurement and budgeting systems, and continued violence and sectarian strife. Dr. Lawrence Korb of the Center for American Progress testified that most of Iraq's budget and government professionals were removed from office at the start of the Iraq War due to their political affiliation, and that many of them have left the country. Their expertise is missing and has not been replaced. Witnesses at the hearing testified that violence also continues to present problems in maintaining oil pipelines and transportation. Furthermore, as Christopher Blanchard of the Congressional Research Service told Members, the Iraqi government has been unable to reach an oil revenue-sharing arrangement acceptable to all of Iraq's key parties.

Going forward, the United States seeks to require Iraq to pay more of the cost of its own reconstruction and security. As Mr. Christoff and Mr. Blanchard testified, the House and Senate moved this year to require equal cost-sharing between Iraq and the United States for all reconstruction projects costing more than \$750,000. In addition, the United States is improving the coordination and performance of the financial management assistance that several U.S. agencies are offering to Iraq.