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Iraq holds the world's third-largest proven oil reserves, and revenues from the sale of oil resources are the engine of Iraq's national economy and the lifeblood of its national budget. Iraq's state-owned oil production and marketing system ensures that revenue from the export and sale of Iraqi oil accrues to the Iraqi government, and the Iraqi people's elected representatives are now responsible for administering that revenue to meet the country's considerable development needs. Iraq's energy resources and potential export revenues offer the country an undeniable opportunity for economic growth, if conditions prevail that allow those resources to be developed efficiently and if Iraqi leaders manage export revenues effectively. This statement analyzes the recent U.S. policy debate over Iraq's current budget surplus, reviews relevant recent developments in Iraq's oil and natural gas sector, and discusses factors that may affect the oil sector's ability to continue to serve as an engine of economic growth and public revenue for Iraqis.

## Current Revenue Arrangements

Iraq's State Oil Marketing Organization (SOMO) is responsible for the sale and export of Iraqi crude oil. Under the terms of United Nations Security Council resolution

(UNSCR) 1483 (and renewed through subsequent Security Council resolutions), revenue from Iraq's oil exports is deposited into an Iraq-controlled account at the Federal Reserve Bank of New York (FRBNY). Five percent of the funds are reserved for a United Nations Compensation Fund for reparations to the victims of the 1990 Iraqi invasion and occupation of Kuwait. The remaining 95% is deposited into the Development Fund for Iraq (DFI) account at the FRBNY and is then transferred to an Iraqi Ministry of Finance account at the Central Bank of Iraq for further distribution to Iraqi government ministries.

Under the terms of UNSCR1546 (and renewed by subsequent resolutions), the DFI is monitored by an International Advisory and Monitoring Board (IAMB), which provides periodic reports on Iraq's oil export revenue, Iraq's use of its oil revenues, and its oil production practices. According to the IAMB, as of December 31, 2007, $23.43 billion had been disbursed from the United Nations Compensation Fund; Iraq owes $28.95 billion to the Fund. The IAMB estimates that "at the present rate of Iraqi oil sales, it would take approximately 17 years for the compensation award to be fully paid."[1] As of June 2008, the balance in the DFI was approximately $17 billion.

UNSCR 1790 of December 18, 2007, extended the IAMB monitoring of the DFI until December 31, 2008. In October 2006, the Iraqi cabinet approved the creation of an oversight body known as the Committee of Financial Experts (COFE) to monitor oil revenue collection and administration. The president of the COFE inaugurated its activities in April 2007, and the committee currently is working alongside the IAMB on audit procedures. When the mandate of the IAMB expires in December, the COFE will assume its duties. Immunity provisions contained in standing UN Security Council

[1] Ernst & Young, Development Fund for Iraq — Summary of Audit Results for the year ended December 31, 2007, May 12-13, 2008.

resolutions prevent Iraqi funds deposited in the DFI from being subject to property attachment motions in lieu of legal judgments rendered against the former Iraqi regime. Many observers expect those immunity provisions to be renewed in a new UN resolution, and the IAMB has encouraged the Iraqi government to pursue continued immunity protection.

**Iraq's Budget Surplus: Sources and Management**

Revenue projections for governments that rely on oil exports are based on variables such as price and export volume, which may be subject to significant or rapid changes in domestic or global market conditions. Iraq's recent surpluses have accumulated based in large part on rapid increases in oil prices over the last year and higher levels of oil production and exports attributable to improved security. The August 2008 Government Accountability Office (GAO) report on Iraq's budget surplus illustrates these relationships by laying out several revenue projections for Iraq's potential 2008 surplus based on variable price and export levels.[2]

At present, Iraq's steady oil export levels and a relative decline in world oil prices from recent highs have moved revenue projections closer to the more pessimistic assumptions outlined in the GAO report: The GAO's lower estimate for Iraq's 2008 budget surplus assumed Iraq would export an average of 1.89 million barrels per day and that the average price received would be $96.88 per barrel. As of September 10, 2008, the U.S. State Department reported that Iraq's Basra Light Crude was priced at $100.15 per barrel and that Iraq was exporting 1.93 million barrels of oil per day. Coupled with Iraq's recently adopted Supplemental Budget of $22 billion, these market trends suggest

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[2] Government Accountability Office, GAO-08-1031 - Stabilizing And Rebuilding Iraq: Iraqi Revenues, Expenditures, and Surplus, August 2008.

that Iraq's 2008 budget surplus may remain well below the upper limit projected in the August 2008 GAO report, pending the result of expenditures through the rest of 2008.

## Table 1. Iraq: Key Oil Indicators

| Oil Production (current weekly avg.) | Oil Production (pre-2003) | Oil Exports (current) | Oil Exports (pre-2003) | Oil Revenue (2006) | Oil Revenue (2007) | Oil Revenue (2008, to date) |
|---|---|---|---|---|---|---|
| 2.48 million barrels per day (mbd) | 2.5 mbd | 1.93 mbd | 2.2 mbd | $31.3 billion | $41 billion | $50.5 billion |

**Note:** Figures in the table from the U.S. Department of State "Iraq Weekly Status Report," September 10, 2008. 'Oil Revenue' is net of a 5% deduction for reparations to the victims of the 1990 Iraqi invasion and occupation of Kuwait, as provided for in U.N. Security Council Resolution 1483.

The U.S. Department of the Treasury and the International Monetary Fund have expressed confidence that, over time, Iraq's oil revenues are likely to be sufficient to meet the country's development needs, if underlying conditions remain favorable for the expansion of oil production and if revenues are managed effectively. However, the IMF warned in a January 2008 report that Iraq's public finances have been "fragile" in recent years and added that, in light of considerable operations and reconstruction needs, the Iraqi government has "little room for fiscal slippage" until oil output increases. The IMF report explains how higher oil prices have compensated for missed oil production expansion targets that undermined revenue generation and how these factors otherwise would have "depleted" the $9.9 billion balance in the Development Fund for Iraq "by the end of 2007." [3]

While reports about Iraq's current and projected budget surplus have raised questions in Congress about the relative overall size of Iraqi and U.S. expenditures, shortcomings in Iraqi revenue management practices and capabilities also have contributed to the accumulation of surpluses. According to U.S., Iraqi, and international observers, these shortcomings have prevented capital investment budgets from being

[3] International Monetary Fund, Country Report No. 08/17, "Iraq: Request for Stand-By Arrangement and Cancellation of Current Arrangement—Staff Report," January 2008, p. 9.

spent effectively thus far and may continue to hinder reconstruction progress if left unaddressed. The U.S. Department of Defense (DoD) June 2008 Measuring Security and Stability in Iraq report noted “marginal improvement” in the Government of Iraq’s ability to spend its resources, although the report concluded that “budget execution rates continue to be relatively low, limiting Iraq’s ability to increase economic development and deliver essential services to its citizens.”[4] Among the “considerable challenges” facing efforts to improve the performance of Iraq’s ministries identified in the report were “cumbersome budgetary approval and complex funding processes”, limited experience among available staff, and the “limited availability of resident contractors.”

The U.S. State Department made similar assessments in July 2008. According to the Department’s latest Section 2207 Report on Iraq Relief and Reconstruction, impediments to effective budgetary expenditure in Iraq “persist at all levels.”[5] The report concluded that “continued assistance is needed to address impediments to capital budget execution.”[6] The Special Inspector General for Iraq Reconstruction (SIGIR) reported in July 2008 that U.S. funded ministerial capacity development programs had been hindered by “weak coordination” among multiple agencies that “tended to implement their own programs with little prioritization of projects or coordinated planning.” The SIGIR concluded that U.S. investments in capacity building are “at risk” unless more integrated programming is implemented.[7]

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[4] U.S. Department of Defense (DoD), Measuring Stability and Security in Iraq - June 2008, Report to Congress in accordance with the Department of Defense Appropriations Act 2007 (Section 9010, P.L. 109-289), p. 10.

[5] U.S. Department of State, Section 2207 Report on Iraq Relief and Reconstruction, July 2008, Report to Congress in accordance with the National Defense Authorization Act for Fiscal Year 2006 (U.S. Policy in Iraq Act, Section 1227, P.L. 109-163).

[6] U.S. Department of State, Section 2207 Report on Iraq Relief and Reconstruction, July 2008.

[7] Special Inspector General for Iraq Reconstruction (SIGIR) Report 08-020, “Key Recurring Management Issues Identified in Audits of Iraq Reconstruction Efforts,” July 2008.

In light of these assessments, both the U.S. and Iraqi governments have undertaken initiatives in recent months to improve public financial management and the coordination of U.S. assistance programs. Iraq has issued new decrees and reformed administrative bodies to grant greater contracting authority to ministries and provinces.[8] Iraq's 2008 Budget Law allows provinces and government agencies to carry over their unused budget authority into the current fiscal year. The U.S. Embassy in Baghdad and the commanders of Multi-National Forces-Iraq also have reorganized the management of existing U.S and coalition budget assistance programs to improve coordination.

> "Efforts to improve ministerial performance face considerable challenges. The central government and provincial ministries lack a civil service cadre trained to manage the work within their ministries. Some senior managers have the requisite expertise to manage the activities within their ministries, but almost all that do are near retirement age. Mid-level managers have some experience, but most lack modern management training. Provincial civil servants have limited links to the central ministries, which exacerbates their lack of leadership and vision. Communication is poor within and between ministries. There is no common strategic plan to address these issues. Additionally, many civil servants continue to fear corruption charges, while intimidation and assassination remain threats, whether at the hand of criminal or sectarian elements."
> **U.S. Department of Defense, Measuring Security and Stability in Iraq, Report to Congress, June 2008, pp. 3-4.**

In late June 2008, the interagency Public Finance Management Assistance Group (PFMAG) began its work. The PFMAG's civilian-military Policy and Operations Committees now direct the activities of paired teams of Action Officers and Treasury Technical Assistance Advisors who work alongside Iraqis, collecting and analyzing data and helping to re-engineer and expedite payments and other budgetary

[8] A Central Contracts Committee has now replaced Iraq's former contract approving authority. Decrees issued since January 2008 granted Governors and selected Ministers and Heads of Agencies authority to enter into contracts worth $50 million. The ministries selected were Defense, Interior, Oil, Trade, Health, Electricity, Industry and Minerals, Water Resources, Municipalities, and Public Works. Agencies not attached to ministries have been granted a $30 million contract approval ceiling. Iraq's governorates can now approve contracts worth up to $10 million. SIGIR Report 08-020, "Key Recurring Management Issues Identified in Audits of Iraq Reconstruction Efforts," July 2008.

processes.[9] These activities build on existing programs such as USAID's National Capacity Development Program (more commonly known by the name *Tatweer*, the Arabic word for development), the U.S. Embassy Iraq Transition Assistance Office (ITAO) Ministerial Capacity Development Program, and the work of the Multi-National Security Transition Command-Iraq (MNSTC-I) Embedded Advisory and Functional Capability Teams. Coalition partners, such as the United Kingdom's Department for International Development (DFID), participate in PFMAG decision-making, and U.S. officials report that expanded PFMAG coordination with international bodies such as the IMF and World Bank is planned.

**Recent Developments in Iraq's Oil Sector**

The concept of federalism has been incorporated into Iraq's constitution and law, and Iraqi attitudes toward the oil sector often correspond with regional differences of opinion about the proper role and power of the national government and regional and governorate authorities to make oil policy and revenue decisions. However, the constitution's ambiguity about the roles and powers of federal, regional, and governorate authorities has contributed significantly to the ongoing impasse over these issues. Articles 111 and 112 of the Iraqi constitution state that Iraq's natural resources are the property of "all the people of Iraq in all regions and governorates," and that "the federal government, *with the producing governorates and regional governments*, shall undertake the management of oil and gas extracted from present fields (italics added)." These provisions were included as a means of ensuring consensus among Iraqis and the adoption of the constitution.

[9] Information provided to CRS by U.S. Treasury Attaché, Baghdad, Iraq, September 13, 2008.

Further complicating matters are Article 115, which provides regional authorities the power to override federal law in the event of conflicts with regional legislation, and Article 110, which grants powers to Iraq's federal government to formulate "foreign sovereign economic and trade policy" and regulate "commercial policy across regional and governorate boundaries" similar to those granted to the United States Congress by the commerce clause of the U.S. Constitution. According to the U.S. Department of Defense, Iraq's Constitutional Review Commission "continues to review almost 50 amendments addressing the authority of the federal government and governorates," including provisions addressing "the extent of governorate powers under Article 115" and the "status and management of oil and gas."[10]

To date, draft legislation to establish a new framework for the development of Iraq's hydrocarbon sector has not been placed on the parliament's legislative calendar because of continuing political differences between the national government and the Kurdistan Regional Government (KRG) over their relative powers and other constitutional issues, such as the administrative status of the city of Kirkuk. KRG Prime Minister Nechirvan Barzani and Iraqi Prime Minister Nouri al Maliki met in April and June 2008 to negotiate terms for moving forward on the draft hydrocarbon laws, Kirkuk, and other outstanding issues. According to Barzani, a political committee has been formed to continue negotiations on the framework legislation.[11] The June 2008 Measuring Security and Stability in Iraq report states that the Chairman of the Iraqi Council of Representatives Oil and Gas Committee does not plan to proceed with a first reading of the draft legislation until the federal government and the KRG reach a political

[10] U.S. Department of Defense, Measuring Stability and Security in Iraq - June 2008, p. 3.
[11] Kurdistan Regional Government (KRG), Press Release: "PM Barzani announces political committee to discuss Iraqi federal hydrocarbons law," June 28, 2008.

agreement on the hydrocarbon sector.[12] The previous report in March 2008 observed that the Iraqi government "continues to distribute oil revenues equitably to the provinces in the absence of this comprehensive legislation."[13]

Iraqi, U.S., and other international observers have expressed concern that the potential for renewed violence and the atmosphere of unresolved political tension prevailing in Iraq may not be conducive to careful consideration of hydrocarbon sector legislation or to inclusive decision making about long-term oil development contracts. Nevertheless, in the absence of new oil legislation and regulation, the Ministry of Oil and the KRG have moved forward with hydrocarbon sector investment and development. New national and KRG contracts have contributed to the persistence of an atmosphere of political controversy surrounding the hydrocarbon sector. In turn, several international companies have chosen to pursue investment opportunities in Iraq in an uncertain legal environment. This includes China's National Petroleum Corporation, which recently modified a Saddam-era production contract into a 20-year service contract to improve production in southern Iraq's Al Ahdab oilfield. Similarly, Shell has launched negotiations to develop systems for capturing and marketing associated natural gas in Iraq's southern oilfields; the gas currently is being wasted at a cost estimated by the Iraqi government to be $40 million per day.[14] The KRG has signed over twenty production sharing agreements with international oil companies, but the limited amount of oil currently being produced in KRG territory is not exported.

Overall, the Ministry of Oil has set a goal of nearly doubling current oil production to 4.5 million barrels per day within 5 years, and expanding production

[12] U.S. Department of Defense, Measuring Stability and Security in Iraq - June 2008, p. 3.
[13] U.S. Department of Defense, Measuring Stability and Security in Iraq - March 2008, p. 4.
[14] *Reuters*, "Iraq approves preliminary gas deal with Shell," September 7, 2008.

thereafter to 6 million barrels per day within 10 years. To reach these goals, the Ministry of Oil is moving forward with plans to conduct an international bidding round for the development of six major oil fields, with contract awards expected some time in 2009. A pre-qualification round held in early 2008 attracted strong interest from U.S. and international bidders: 41 firms were qualified, including six unnamed state-owned firms.[15] However, the recent collapse and cancellation of an interim process to award short-term service contracts for production expansion demonstrates the difficulty Iraq's government and international bidders may have in reaching mutually agreed contract terms and gaining public support in the absence of new legislation and political consensus.

**Factors Affecting Iraq's Oil Revenue Potential**

As Iraq and the United States look to the future, four key factors may affect the Iraqi oil sector's ability to continue to provide adequate financial resources to the Iraqi people. The first and most fundamental of these factors is the security of the country. General insecurity and infrastructure attacks have hindered efforts to rehabilitate and develop Iraq's oil sector since 2003. Oil sector corruption also has contributed to the insecurity of the country, according to U.S. officials. For example, according to DoD, until mid-2007, corruption and siphoning at the refinery at Bayji resulted in "as much as 70% of the fuel processed" being sold on the black market at a value of up to $2 billion a year.[16] U.S. military leaders have made clear statements about the potential reversibility of the recent security gains that have enabled oil output to increase since 2007. During that time, U.S. and Iraqi investments in infrastructure security for oil production facilities

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[15] *Reuters*, "Firms pre-qualified for Iraq long-term oil deals," June 30, 2008.
[16] U.S. Department of Defense, Measuring Stability and Security in Iraq - June 2007, p. 13.

and pipelines have contributed to increased export levels, and U.S. and Iraqi officials are expanding existing projects to extend these gains.

Second, Iraqis face the challenge of coming to a greater degree of political consensus about the powers and responsibilities of various levels of government in determining national energy policy and about various issues related to energy development. This includes reaching agreements about the degree and terms of foreign participation and models for revenue sharing. In late 2007, the KRG finalized its own regional oil and gas investment law and signed new production sharing agreements with several international companies, including U.S.-based Hunt Oil.[17] Some analysts believe that the Kurdish moves signal the KRG's intention to begin large scale oil development activities regardless of progress on federal legislation. The KRG has stated its opposition to proposals to require federal approval of its existing or future contracts, but notes that it is committed to revenue sharing as defined in the constitution and the draft revenue sharing law. As noted above, these issues remain the subject of ongoing negotiation.

In September 2007 a State Department spokesman stated the Administration's view that the KRG deals "elevate tensions between the Kurdish regional government and the Government of Iraq," and "aren't particularly helpful" to the extent that they hinder consideration of a national oil law.[18] Iraqi government officials from other parties have reacted negatively to the impasse and the KRG's recent activities. On September 8, 2007, Iraqi Oil Minister Hussein al Shahristani stated that the national government considers contracts signed by the KRG to have "no standing".[19]

[17] Bloomberg News, "Dallas Oil Company Approved to Drill in Kurdistan," September 10, 2007.
[18] U.S. Department of State Daily Press Briefing, Tom Casey, Deputy Spokesman, Washington, DC, September 28, 2007.
[19] Ben Lando, "Deeper Than an Oil Law in Iraq," UPI, September 10, 2007.

Tensions appeared to escalate further after Minister Al Shahristani warned international oil companies that the national government would not allow the export of oil produced under KRG contracts.[20] The KRG responded by accusing Minister Al Shahristani of mismanaging the Oil Ministry budget and restated its opinion that its contracts were both constitutional and legal.[21] In November 2007, 60 Iraqi oil sector leaders wrote to the Council of Representatives to state that the KRG's unilateral signing of contracts constituted a "deliberate and dangerous action" and had no "legal or political standing whatsoever."[22] At least 120 members of the Council of Representatives from a wide range of political parties endorsed a January 2008 joint statement underscoring their opposition to the KRG contracts.[23] The Ministry of Oil has since refined its position slightly to emphasize its opposition to contracts signed by the KRG after February 2007. Contracts signed before February 2007 with firms currently producing oil for domestic consumption would be considered valid after review and potential amendments.

Third, fluid global market conditions ultimately determine the demand for Iraq's energy resources, the revenue potential of those resources, and the availability of domestic and external investment capital. As noted earlier, recent declines in global oil prices have lowered this year's surplus revenue projections for Iraq. However, the abundance of energy resources in Iraq and their relative ease of production will likely sustain the attractiveness of Iraq's oil sector to international investors over the long-term. The U.S. Embassy's Iraqi Transition Assistance Office estimated in 2007 that Iraq's oil

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[20] Platts Commodity News, "Iraq's Shahristani Says Hydrocarbon Law not Expected Soon," November 15, 2007.
[21] Kurdistan Regional Government, "KRG responds to Dr Shahristani's threats to international oil companies," November 20, 2007.
[22] Radio Free Europe Documents and Publications, "Iraq: Baghdad, Kurds At Odds Over Oil Deals," November 30, 2007.
[23] Ned Parker, "Iraqi Political Factions Jointly Pressure Kurds," Los Angeles Times, January 14, 2008; and, UPI, "Iraq Factions Join Against Kurd Oil Deals," January 15, 2008.

sector could require $100 billion in investment to meet the Iraqi government's production goals.

In light of Iraq's transition from conflict and in light of strong economic growth in the more stable countries of the Persian Gulf region, Iraq may struggle relative to its neighbors in attracting international investment and expertise to assist in its non-energy related reconstruction. DoD has reported that projects for critical ministries require "multi-year, large-scale strategic infrastructure upgrades" that may require the involvement of international firms; those firms could remain reluctant to engage in Iraq.[24]

Lastly, Iraqi leaders are working to address what the U.S. government and international auditors have described as significant weaknesses in Iraq's current public financial management practices. The United States has financial advisory programs in place for many of Iraq's key ministries, including with civilian leaders of security ministries. However, these programs remain limited in scope and funding in spite of their recently reorganized coordination. From Iraq's perspective, the availability of significant oil revenues is fortunate in light of the country's remaining development needs. In addition to planned physical infrastructure investments, investment in human capital and management assistance may prove equally important.

**Options for U.S. Policy**

As Iraqi officials and their coalition partners preside over the latter half of the so-called "Year of Transition in Iraq", U.S. spending on large-scale reconstruction projects is coming to a close: the State Department reports that the funds available in the Iraq Relief and Reconstruction Fund have been almost entirely obligated or expended as of early September 2008.

[24] U.S. Department of Defense, Measuring Stability and Security in Iraq - June 2008, p. 10.

Pending legislative proposals in both houses of Congress reflect broad and growing sentiment that seeks to require the Iraqi government to pay more of the cost of reconstituting Iraq's security forces and providing for reconstruction needs. Proposed defense authorization language in both houses would reduce authorized spending from the Iraq Security Forces Fund (ISFF) relative to the Administration's request ($2 billion) and last year's bridge fund ($1.5 billion).[25] The Appropriation Committees require "equal cost-sharing" for all reconstruction projects above $750,000 in report language as well as prohibiting the use of these funds for salaries for Iraqi military personnel.[26] Senate authorizers would prohibit using ISFF monies for "large-scale" infrastructure above $2 million; House authorizers would prohibit the use of ISFF funds for any facilities construction and argue that "the Iraqi Government is well able to afford to finance its own infrastructure needs at this point."[27]

As noted above, U.S. and international auditors have not expressed doubt about the Iraqi government's *ability to afford* taking on more of the costs of its reconstruction and security sector development, if oil production expands and export conditions remain favorable. Those auditors and observers have expressed significant doubts about the Iraqi government's current *ability to expend available funds at a sufficient rate or level of efficiency* to maintain the complex, long-term, and large-scale programs required. By most public accounts, Iraqis in many areas of the country remain somewhat dissatisfied with the scope and pace of ongoing reconstruction programs, particularly with regard to

[25] The Senate recommends $200 million while both the House authorization bill and the previously-enacted supplemental appropriations act (P.L.110-252) provide $1 billion.
[26] Section entitled "Iraq Security Forces" in P.L. 110-252 and report language on p. S4337, Congressional Record, May 19, 2008.
[27] Sec. 1616 in S. 3001 as reported and S.Rept. 110-335, p. 428; see also Sec. 1512 in H.R. 5658 as passed by the House. Section 1613 in S. 3001 as reported by the Senate lists equipment, supplies, services, and training as the only types of expenses that can be funded in the ISFF; Sec. 1616 applies the prohibition to any "large-scale infrastructure projects" above $2 million.

the delivery of essential services such electricity and water. Midway through the "Year of Transition", DoD warned that:

> "Future progress in essential services could be at risk since the U.S. will transition large-scale infrastructure projects to the Iraqis to fund and execute. While the Government of Iraq acknowledges it has the revenues to support these projects, budget and program execution rates indicate that the Government lacks the ability to execute programs on the scale required."[28]

As such, Members of Congress concerned about relative scope and effectiveness Iraqi contributions to reconstruction and security goals may wish to consider options to encourage or enable the Iraqi government to improve its public financial management capabilities. As described above, Administration officials have already taken steps to improve the coordination and performance of U.S. financial management assistance programs in Iraq by creating the interagency Public Financial Management Assistance Group (PFMAG). Congress can influence the operations of the PFMAG and its constituent programs through consideration of pending appropriations and authorization legislation or through the exercise of targeted oversight and evaluation.

Existing U.S. programs to improve the performance and capabilities of the security forces of allied governments in the Middle East also offer potential models for the structuring future of the U.S. assistance and advisory relationships with Iraq. Significant U.S. foreign assistance programs for Israel and Egypt are funded through annual appropriations of Foreign Military Financing, Economic Support Fund, and other assistance, and the annual appropriations process offers opportunities for Members of Congress to evaluate progress toward stated bilateral goals and respond to changing political and economic conditions. Alternatively, long-standing U.S. security assistance programs for Saudi Arabia are financed through Saudi government purchases of U.S.

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[28] DoD, Measuring Stability and Security in Iraq - June 2008, p. vi.

training and services through the Foreign Military Sales program. Iraq has begun using the FMS program for its acquisition needs, and may soon make large arms purchases worth up to $11 billion according to arms sale proposals recently notified to Congress by the Administration. The U.S. Army Corp of Engineers, which is currently carrying out U.S. funded reconstruction work in Iraq, carried out construction projects in Saudi Arabia on a contract basis during the 1970s and 1980s, funded by Saudi government oil revenues.

Similar direct or contract-based bilateral assistance programs could help Iraq complete its transition and reconstruction and would likely make U.S.-Iraqi relations subject to more conventional congressional concerns about human rights, the end use of U.S. military equipment, the regional military balance, and the efficiency and transparency of contract assistance programs. Increasing confidence within Iraq's political leadership and competition among some Iraqi political groups to harness popular nationalist sentiment may limit the attractiveness or utility of official bilateral assistance efforts over time, making contract-based solutions with U.S. or other international partners more appealing or effective.

**Conclusion**

Thank you for the invitation to testify and I look forward to your questions.