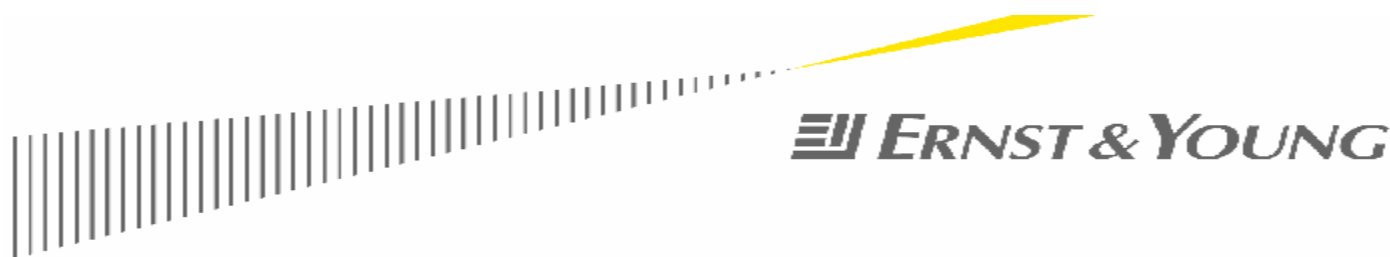




Development Fund for Iraq

Memorandum of Matters Arising From Audit
31 December 2007



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30 April 2008

Messrs.
International Advisory and Monitoring Board
Committee of Financial Experts
Development Fund for Iraq
Baghdad – Republic of Iraq

Dear Sirs,

In relation to our review of Development Fund for Iraq (the Fund) of 2007, we are now reporting to you certain matters which came to our attention during the course of the audit.

For the purposes of determining the timing and extent of our audit procedures required by International Standards on Auditing, we have conducted a review and evaluation of Internal Controls systems of the fund. Throughout this review we have noted some observations and recommendations that we are reporting to you for your kind attention and follow up.

This work is not primarily directed towards the discovery of weakness or the detection of fraud or other irregularities (other than those which would influence us in forming that opinion) and should not therefore be relied upon to show that no other weakness exist.

Our report is intended solely for the information and use of the Government of Iraq, the International Advisory and Monitoring Board of the Development Fund for Iraq, and The Committee of Financial Experts and should not be used for any other purpose. We do not, in giving our report, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our consent in writing.

We take this opportunity to thank the management and staff of all Iraqi Governmental entities for their co-operation during the course of the audit.

Yours faithfully,



Ernst & Young

Bishr Baker





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SYMBOLS LEGEND


The following symbols are used through the report:

Symbol Name	Symbol	Description
High Risk		A serious weakness which exposes the DFI to a material extent in terms of achievement of corporate objectives, financial results or otherwise impairs reputation. Immediate corrective action is recommended.
Medium Risk		A weakness which can undermine the system of internal control and/or operational efficiency and should therefore, be addressed. Corrective action is recommended generally within a short period of time.
Low Risk		A weakness which does not seriously detract from the system of internal control and/or operational effectiveness/efficiency but which should nevertheless be addressed by Management. Corrective action is recommended generally within a reasonable time.
Current Year Observation	NEW	Observation noted during current year review
Prior Year(s) Observation Has Been Resolved		In our opinion, satisfactory actions were taken to resolve prior year(s) observation
Repeated/updated Observation	OLD	In our opinion, observation from prior year(s) was not properly resolved.

MATTERS RELATED TO MINISTRY OF FINANCE CURRENT AND PRIOR YEAR


Matters Related to Ministry of Finance Current and Prior Year

1. POLICIES AND PROCEDURES MANUAL

Observation	Recommendation	Risk Level	Status
<p>We noted that DFI does not have formal detailed policies and procedures to cover all areas of its operations. The MOF periodically issues accounting instructions to set out the procedures to be applied in performing certain tasks. However, these instructions are not comprehensive as they do not cover all the aspects of the DFI's operations. Furthermore, these instructions have not been formally codified in the form of a comprehensive policies and procedures manual, which is readily available for reference by the staff involved in the DFI activities.</p>	<p>We recommend that the DFI develops a comprehensive policies and procedures manual to cover all DFI operational, administrative, accounting and financial activities.</p> <p>The manual should also be reviewed on a periodic basis to ensure that it is updated and relevant for providing operational, administrative, accounting and financial guidance to the DFI's staff.</p> <p>In addition, detailed monitoring procedures should be developed and applied by the DFI to ensure proper and consistent implementation of the policies and procedures manual.</p>		OLD


Matters Related to Ministry of Finance Current and Prior Year

2. AUTHORIZATION OF DISBURSEMENTS FROM THE DFI ACCOUNT

Observation	Recommendation	Risk Level	Status
<p>The payments of the DFI funds are authorized by H. E. Prime Minister together with H. E. Minister of Finance or their representatives. Payments are made through allocating funds that represent the maximum limit of payments to cover financing requirements through the DFI account. These allocations usually range between U.S. \$ 300 million and U.S. \$ 800 million for each allocation. The period to be covered by these allocations is not predetermined and the allocations are not immediately withdrawn from the Federal Reserve Bank of New York (FRBNY).</p> <p>Afterwards, payments orders to transfer the funds from the FRBNY account to the CBI are carried out. These transfers are made out of the allocations of the Ministry of Finance at the FRBNY solely based on written approval by the MOF's Director General of the Accounting Department, with no limit to the amount to be transferred. Given the funds available in the DFI account, this may be considered to be excessive authority.</p> <p>Considering the DFI's significant weaknesses in internal control systems, there is no adequate controls to either prevent or detect the risk of unauthorized payments being made on a timely basis.</p>	<p>We recommend that the DFI develop an authorization manual to govern all DFI transactions, including payments from the FRBNY account to the CBI account, to ensure that adequate controls have been put in place.</p> <p>Authorization manual shall include the authorities and limits granted to Director General of the Accounting Department and each staff member involved in the DFI operations, and where appropriate, dual or more signatories requirements.</p>		OLD

Matters Related to Ministry of Finance Current and Prior Year

3. BUDGET PREPARATION

Observation	Recommendation	Risk Level	Status
<p>During our review of the procedures followed by the budget section relating to the review of the departmental budgets, we noted that the budget section does not refer to the prior year budgets and actual expenditure in order to challenge the proper preparation of effective budgets prepared by the various Governmental entities.</p> <p>An effective evaluation of budgets prepared by the Governmental entities and determination of important control procedure to ensure that the needs of each department are consistent with the activities, past performance and plans for the forthcoming year. This includes assessing performance in prior year against budget to determine whether there were significant over or under spending.</p>	<p>The departmental budgets review process undertaken by the budget section is a significant part of the Finance Department's activities relating to the follow up and review of Government expenditures. Accordingly, it is our belief that the DFI key management should give special attention to the budget compilation and review process undertaken by the budget section to ensure that adequate control procedures exist in such process.</p> <p>A contemporary budget preparation and review environment would include, but it is not limited to:</p> <ul style="list-style-type: none"> • Review by the budget section of procedures undertaken by various entities to prepare their annual budgets. The budget section then ensures that adequate controls have been put in place by the various departments to facilitate an accurate budget preparation and, hence, reduce the time spent by the budget section in their review process of these budgets. • The budget section shall establish a process to identify transfers between different expenditure categories. This information would enable the budget section to identify expenditure items that have been over budgeted by any particular department in prior years and which are being used to finance the expenditure of other unapproved spending, if any. • The budget section shall establish a database of all 		OLD


Matters Related to Ministry of Finance Current and Prior Year

3. BUDGET PREPARATION

Observation	Recommendation	Risk Level	Status
	<p>departmental budgets and expenditures for each entity for the purpose of establishing a benchmark for each expenditure item in relation to the activities and size of the related entity. Such a database would enable the budget section to review entity's performance on a periodical basis (e.g. monthly) and investigate any significant variances compared to the benchmark. Such a database would also enable the budget section to identify areas of risk and opportunities for cost saving.</p> <ul style="list-style-type: none">• The review by the budget section of entity's budgets shall include a comparison of prior year budgets and actual expenditure. Such review would highlight effectiveness of budget preparation process and in addition to any significant changes or developments compared to the prior year.		


Matters Related to Ministry of Finance Current and Prior Year

4. ACCOUNTING SYSTEMS

Observation	Recommendation	Risk Level	Status
<p>The current governmental accounting system relating to accounting procedures, including management information systems and internal control procedures, are no longer suitable for the current size and structure of the DFI, and have not been updated in line with the modern technologies and best practices available.</p> <p>The Iraqi Government is currently undertaking an overall change in the computerized accounting system of the Accounting Department.</p>	<p>We recommend that the DFI undertakes a review of the accounting systems and processes and internal controls related to the DFI at MOF, CBI, SOMO and related ministries; with a view to improving efficiency of operations and effectiveness of controls. This should include, as a minimum:</p> <ul style="list-style-type: none"> • Policies and procedures manual. • Control procedures in connection with the other sections of the accounting department. • Review of the accounting department's documentation and filing procedures. • Review of the operating departments' system of internal controls. • Consider providing online access to automated system to the internal audit department. • Establishment of procedures for follow up of budget preparation and compliance. • <p>Given the above, we recommend that the DFI consider developing or sourcing an integrated Accounting and Reporting Package together with Management Information Systems (MIS) and Financial Information Systems (FIS) which fully meet the requirements of the DFI operations at all locations.</p>		OLD


Matters Related to Ministry of Finance Current and Prior Year

5. DFI ACCOUNTING RECORDS

Observation	Recommendation	Risk Level	Status
<p>We noted that the DFI accounting records are based on information obtained from the CBI, and monthly statements sent by the CBI to the MOF. This information is limited to the transactions of the DFI's main account at the FRBNY.</p> <p>As a result, the DFI does not maintain a complete set of accounting records to support the financial statement and the related notes disclosures for the year ended 31 December 2007. The statement of cash receipts and payments is compiled from the monthly statement of cash receipts and payments of the DFI's main bank account managed by the CBI, the DFI's sub-account maintained by the U.S. Agencies, the FRBNY bank statements, other financial information maintained by the Ministry of Finance, and confirmations received from other parties.</p> <p>During 2007, The MOF has established a designated database for DFI to collect all transactions and accounting records in. MOF is working on reconciling DFI opening balances.</p>	<p>We strongly recommend that the MOF keep complete set of accounting records to account for all DFI approved transactions that are reconciled with bank statements obtained from the CBI.</p> <p>In addition, Periodic reconciliations shall also be performed between the MOF and CBI. Differences shall be investigated, reported and resolved on a timely manner.</p> <p>Also, we recommend that the COFE follows up on development and enhancement of the DFI accounting records to be separately maintained from MOF records, which are maintained in accordance with the government accounting system. The DFI's accounting records should be maintained in accordance with the cash basis under International Public Sector Accounting Standards.</p> <p>In the meantime, the MOF shall continue to develop the DFI's database to support all figures reported in the financial statements and related disclosures. Employees shall also receive appropriate training to carry out the preparation of the DFI's financial statement in accordance with the cash basis under International Public Sector Accounting Standards.</p>		OLD


Matters Related to Ministry of Finance Current and Prior Year

6. DFI ACCOUNTING RECORDS

Observation	Recommendation	Risk Level	Status
<p>We noted during our audit that the DFI's overall internal control system is not effective, due to the following main factors:</p> <ul style="list-style-type: none"> • Formal code of business conduct and ethics is not established. • Comprehensive policies and procedures manual to be developed for all areas of the DFI's operations. • Organizational chart to be re-structured. DFI is currently managed by separate departments at Central Bank of Iraq under the supervision of the Ministry of Finance. However, there is no designated executive and financial controller to take responsibility for the direction of the DFI's overall activities. • DFI does not have a formal risk management process to assess the risks of its operations and to continuously monitor the risk exposures and reduce the risks to acceptable levels. • DFI personnel need more extensive training to be able to properly execute their responsibilities given the nature and complexity of the DFI's transactions. • Human resource policies and practices relating to employee training, evaluation, counseling, promoting, and compensation need to be developed • No internal audit departments dedicated for the DFI. Audit procedures carried by the internal audit departments in both the CBI and the MOF are limited and only cover part of the DFI operations. 	<p>We recommend that the DFI undertake a detailed review of the DFI's overall internal control systems and develop a plan and timetable to address the various above mentioned internal control related issues.</p> <p>In addition, we recommend that an executive be appointed and made responsible for directing the overall activities of the DFI at all locations, including the MOF, CBI, SOMO, spending ministries, Kurdistan Region, etc. Consideration may also be given to establishing an executive committee (involving executives from the key locations) to oversee the DFI operations and report to the Committee of Financial Experts (COFE) and the IAMB on a periodic basis.</p> <p>In addition, we recommend that an executive be appointed and made responsible for directing the overall activities of the DFI at all locations, including the MOF, CBI, SOMO, spending ministries, Kurdistan Region, etc. Consideration may also be given to establishing an executive committee (involving executives from the key locations) to oversee the DFI operations and report to the Committee of Financial Experts (COFE) and the IAMB on a periodic basis.</p>		OLD


Matters Related to Ministry of Finance Current and Prior Year

7. REPORTING AND FINANCIAL STATEMENTS PREPARATION

Observation	Recommendation	Risk Level	Status
<p>During the course of our audit, we noted that the MOF and the CBI do not prepare a complete set of DFI's statement of cash receipts and payments as part of the monthly management reporting process. The CBI currently prepares a monthly report including the cash receipts and cash payments of the main DFI account only, excluding the sub-account managed by the U.S. Agencies.</p> <p>In addition, we noted that there are no formally documented policies and procedures for the preparation of the DFI's financial statements and the related disclosures.</p> <p>Moreover, the MOF does not maintain records for all financial information that should be reported and disclosed in the DFI's statement of cash receipts and cash payments as required by the International Public Sector Accounting Standards /Financial Reporting on Cash basis.</p> <p>During 2007, The MOF has established a designated database for DFI to collect all transactions and accounting records in. MOF is working on reconciling DFI opening balances.</p>	<p>We recommend that the COFE shall follow up with both the CBI and the MOF to prepare a full set of the DFI's statement of cash receipt and cash payments in accordance with the cash basis under International Public Sector Accounting Standards.</p> <p>We further recommend that a formally documented policies and procedures to be developed for the preparation of the DFI's financial statement and its related disclosures.</p>		OLD


Matters Related to Ministry of Finance Current and Prior Year

8. LONG OUTSTANDING CASH MARGINS AT JP MORGAN CHASE BANK

Observation							Recommendation	Risk Level	Status																																																																						
<p>During the course of our audit, we noted a large number of long outstanding cash margin balances with JP Morgan Chase for letters of credit that were opened through the Trade Bank of Iraq (TBI) for the benefit of the Iraqi ministries that are financed by the DFI.</p> <p>The following are examples of these outstanding balances as of 31 December 2007 according to the confirmation received from JP Morgan Chase.</p> <table><tr><th>L/C #</th><th>Ministry</th><th>L/C Amount (U.S. \$)</th><th>Outstanding Amount (U.S. \$)</th><th>L/C Opening Date</th><th>L/C Validation Date</th><th>Date of Last Payment</th></tr><tr><td>160/2003</td><td>Health</td><td>1,350,000</td><td>181,811</td><td>19/1/2004</td><td>28/4/2004</td><td>29/12/2004</td></tr><tr><td>220/2004</td><td>Electricity</td><td>3,867,559</td><td>203,161</td><td>2/3/2004</td><td>11/2/2005</td><td>13/10/2005</td></tr><tr><td>225/2004</td><td>Communication</td><td>300,000</td><td>48,900</td><td>19/3/2004</td><td>9/8/2004</td><td>4/3/2005</td></tr><tr><td>226/2004</td><td>Electricity</td><td>7,412,370</td><td>799,896</td><td>17/3/2004</td><td>31/12/2006</td><td>4/3/2005</td></tr><tr><td>1222/2004</td><td>Health</td><td>1,870,457</td><td>374,091</td><td>16/12/2004</td><td>1/4/2005</td><td>5/6/2005</td></tr><tr><td>1306/2004</td><td>Oil</td><td>14,319,721</td><td>14,391,721</td><td>17/3/2005</td><td>4/2/2006</td><td>None</td></tr><tr><td>1316/2004</td><td>Agriculture</td><td>615,284</td><td>615,284</td><td>19/2/2005</td><td>20/10/2006</td><td>None</td></tr><tr><td>1345/2004</td><td>Health</td><td>145,040</td><td>69,276</td><td>28,2,2005</td><td>28/11/2005</td><td>13/10/2005</td></tr><tr><td>1453/2004</td><td>Agriculture</td><td>3,900,000</td><td>3,900,000</td><td>1/2/2005</td><td>1/9/2005</td><td>None</td></tr></table> <p>The above are only examples, as JP Morgan Chase confirmation includes a large number of similar old outstanding balances as of 31 December 2007.</p>							L/C #	Ministry	L/C Amount (U.S. \$)	Outstanding Amount (U.S. \$)	L/C Opening Date	L/C Validation Date	Date of Last Payment	160/2003	Health	1,350,000	181,811	19/1/2004	28/4/2004	29/12/2004	220/2004	Electricity	3,867,559	203,161	2/3/2004	11/2/2005	13/10/2005	225/2004	Communication	300,000	48,900	19/3/2004	9/8/2004	4/3/2005	226/2004	Electricity	7,412,370	799,896	17/3/2004	31/12/2006	4/3/2005	1222/2004	Health	1,870,457	374,091	16/12/2004	1/4/2005	5/6/2005	1306/2004	Oil	14,319,721	14,391,721	17/3/2005	4/2/2006	None	1316/2004	Agriculture	615,284	615,284	19/2/2005	20/10/2006	None	1345/2004	Health	145,040	69,276	28,2,2005	28/11/2005	13/10/2005	1453/2004	Agriculture	3,900,000	3,900,000	1/2/2005	1/9/2005	None	<p>We recommend that the MOF and CBI coordinate with the TBI and the respective ministries to analyze the current status of each outstanding letter of credit cash margin and follow up to resolve all old outstanding balances.</p> <p>Also, we recommend that CBI and MOF shall follow up with the TBI and beneficiary ministries to ensure letters of credit are executed on a timely basis.</p>		OLD
L/C #	Ministry	L/C Amount (U.S. \$)	Outstanding Amount (U.S. \$)	L/C Opening Date	L/C Validation Date	Date of Last Payment																																																																									
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1453/2004	Agriculture	3,900,000	3,900,000	1/2/2005	1/9/2005	None																																																																									


Matters Related to Ministry of Finance Current and Prior Year

9. CASH MARGIN AT CORRESPONDING BANKS

Observation	Recommendation	Risk Level	Status
<p>During our audit, we noted that the CBI and the MOF do not maintain any records of the outstanding cash margins paid from the DFI on behalf of the Iraqi ministries.</p> <p>According to the confirmations received from JP Morgan Chase and Citibank; the outstanding cash margin balances at these banks were U.S. \$ 2,474,616 thousand and Euro 140,883 thousand U.S. \$ 412,943 thousand and Euro 86,873 thousand respectively as of 31 December 2007.</p> <p>The letters of credit cash margins at the corresponding banks are not included as part of the DFI cash balances as they are not controlled by the DFI and restricted for the payment of the outstanding letters of credit to the suppliers. However, the cash margins are considered DFI assets and any extra cash at the end of the letter of credit is to be refunded to the DFI account.</p>	<p>We recommend that the DFI maintain complete records of the cash margin transfers to the TBI's corresponding banks and all related transactions, as these cash margins are considered as part of the DFI assets until being paid to suppliers.</p>		OLD


Matters Related to Ministry of Finance Current and Prior Year

10. LETTERS OF CREDIT ISSUED FOR SELF-FINANCING ENTITIES

Observation	Recommendation	Risk Level	Status
<p>We noted that self-financing governmental entities reporting to some ministries are transferring funds to the MOF current account at the CBI, and the letters of credit (LCs) are then being opened from the DFI funds at the FRBNY.</p> <p>During the year ended 31 December 2007, payments were made from the DFI funds to cover letters of credit for certain self-financing government entities that are not covered by the federal state budget, which is financed by the DFI, amounting to U.S. \$ 890,824 thousand. Conversely, the MOF received advance payments from these ministries to fund the payments of their letters of credit amounting to U.S. \$ 1,169,524 thousand, which have not been deposited in the DFI accounts. These advances were deposited in the MOF account at the CBI account number (301116).</p> <p>The following are examples of these institutions:</p> <ul style="list-style-type: none"> • General Company for Irrigations/Ministry of Industry • General Company for Agricultural Supplies/Ministry of Agriculture. • South Oil Company / Ministry of Oil 	<p>We recommend that arrangements to be made for the self financing entities to open their letters of credit directly through the Trade Bank of Iraq or other banks and maintain its data related to receipts and payments in electronic form to facilitate controlling them.</p> <p>During 2008, MOF issued instructions to all self financing entities to open their letter of credit directly.</p>		OLD


Matters Related to Ministry of Finance Current and Prior Year

11. DFI DISBURSEMENTS FOR THE IRAQI MINISTRIES

Observation	Recommendation	Risk Level	Status
<p>Certain payments from the DFI account at the FRBNY are transferred to the MOF current account at the CBI to be paid at a later date to the Iraqi ministries, related entities, and Kurdistan region in Iraqi Dinars in accordance with the allocated budget for each ministry. In the DFI's statement of cash receipts and payments, these transfers are reported immediately as cash payments, before actually being paid to the intended ministries and related entities.</p> <p>Transfers from the DFI's account at the FRBNY amounted to U.S. \$ 26,700 Million during 2007, while the total payments from the MOF to the ministries and related entities and Kurdistan Region amounted to U.S. \$ 30,518 Million.</p> <p>The MOF current bank account at the CBI No. (70009) is used to deposit transfers from DFI and transfers relating to MOF own transactions that are not related to the DFI. The payments from this account that are related to DFI are not separately recorded. As a result, it is not possible to identify the total payments related to the DFI the beginning, and the ending cash balances related specifically to the DFI.</p> <p>During March 2008, MOF has made the necessary arrangements to open a separate account at CBI to deposit transfers from DFI bank account in the FRBNY.</p>	<p>We recommend that the MOF consider opening a separate DFI sub-bank account at the CBI to deposit transfers from DFI bank account in the FRBNY, that are designated to finance the Iraqi ministries and related entities. This would assist in identifying the amounts paid from the DFI account and the remaining balance out of total transfers received from the DFI account at the end of each period. This would also enhance tracking all payments made to the respective Iraqi ministries and related entities, as well as managing the available cash balances and enhancing the reconciliation process with the beneficiary ministries.</p> <p>We also recommend that the MOF prepares clear and complete documentation to define all sources of cash receipts and types of payments relating to the DFI.</p>		OLD


Matters Related to Ministry of Finance Current and Prior Year

12. RECONCILIATION BETWEEN THE MOF AND OTHER MINISTRIES

Observation	Recommendation	Risk Level	Status
During the course of our audit, we noted that the MOF does not carry out monthly reconciliations of the payments transferred from the DFI to the ministries and government entities between the MOF records and the records of the other ministries and government entities records.	<p>We recommend that the MOF carry out monthly reconciliations with the records of the ministries and other government entities for payments transferred to cover their operating and capital costs, according to the budget allocated to each ministry. This will help the MOF ensure that all payments made to the ministries were properly recorded in the MOF records and would enhance the control over those payments.</p> <p>We also recommend the MOF to send confirmations to the respective ministries and other government entities on a periodic basis in order to ensure the receiving and proper recording of amounts that have been funded, as well as to identify and reconcile any differences arising.</p>		OLD


Matters Related to Ministry of Finance Current and Prior Year

13. RECONCILIATION OF THE MOF'S CURRENT ACCOUNT AT THE CBI

Observation	Recommendation	Risk Level	Status
<p>The MOF's current account held at the CBI in Iraqi Dinar represents the main account of the MOF that is being used to finance the ministries and related entities and Kurdistan Region in accordance with the allocated budget for each ministry to cover their operating and capital expenditures in Iraqi Dinars.</p> <p>During the course of our audit, we noted that the reconciliation carried out by the MOF for its current account No. (70009) held at the CBI is not being properly performed, as this reconciliation only compares the transactions per the CBI statement of account to the MOF statement of account and determines the outstanding amounts without reconciling the balances.</p>	<p>We recommend that the MOF prepares the reconciliation of the MOF current account in a proper manner which aimed to properly reconcile the outstanding amounts as recorded by the CBI and the MOF.</p> <p>We further recommend that the MOF's current account at the CBI reconciliation should be carried out on a periodic basis, e.g. monthly, and all reconciling items should be investigated, reported and resolved on a timely manner.</p> <p>In addition, the reconciliation should be reviewed and approved by independent personnel from the preparer of the reconciliation.</p>		OLD


Matters Related to Ministry of Finance Current and Prior Year

14. CBI TRANSFERS TO THE MOF'S CURRENT IQD ACCOUNT

Observation	Recommendation	Risk Level	Status
<p>During the course of our audit, we noted that there is currently no written agreement between the MOF and the CBI of to the arrangements of financing the MOF's Iraqi Dinar current account at the CBI from the DFI.</p> <p>The CBI is financing the MOF's current account, held at the CBI, by withdrawing the amounts from the DFI account at the FRBNY in U.S. \$ and then transferring an equivalent amount in Iraqi Dinar to the MOF's current account at the CBI. The exchange rate used is the CBI formal exchange rate on the date of transfer minus IQD 15 for each U.S. \$ 1 as commission charged by the CBI.</p>	<p>We recommend the MOF and the CBI to reach an agreement setting out the arrangements to be followed to finance the MOF's current account in Iraqi Dinars. This agreement shall also include the date of exchange rate to be applied by the CBI to purchase the U.S. \$ from DFI and basis of commission to be charged to MOF.</p>		OLD



Matters Related to Ministry of Finance Current and Prior Year

15. PAYMENTS FROM DFI SUB-ACCOUNT MANAGED BY U.S. AGENCIES

Observation	Recommendation	Risk Level	Status
<p>During the course of our audit, we noted that no party is responsible for monitoring the U.S. Agencies sub account for checking the accuracy of payments and tracing the amounts to the contract terms. Payment orders are issued from the U.S. Agencies and sent to the CBI for the contracts that are executed for the benefit of the Iraqi ministries and other U.S. Agencies after approval by the MOF. There is no evidence of a review being carried out on these contracts and the related supporting documentation.</p> <p>During 2007, the MOF has started sending statements with the payments carried out from DFI sub-account to the ministries and other governmental institutions in order to ensure the receipt of goods or services.</p>	<p>In addition to the above mentioned procedures, we recommend that the following procedures be performed by MOF:</p> <ul style="list-style-type: none"> • Follow up the receipt of the confirmations from the ministries and other governmental entities to check the receiving of goods by the respective ministries. • Ensure that all payments are in congruence with supporting documents. • Ensure that payments have been recorded properly by the respective ministries. • Reconcile amounts paid with the CBI and FRBNY records. • Ensure that all payments are in compliance with the contract terms. • Ensure that all contracts' invoices have been stamped as "PAID", in order to avoid any duplicate payments. 		OLD


Matters Related to Ministry of Finance Current and Prior Year

16. SUSPENDED PAYMENT

Observation	Treatment Method	Risk Level	Status
During the course of our audit, we noted that an amount of U.S. \$ 46,000,000 was paid to Inter-Arab Investment Guarantee Corporation for partial settlement of the total amount of U.S. \$ 120,983,000 that is due to the Corporation based on the agreement with Ministry of Finance signed during December 2005. However, this payment has been recorded by the Ministry of Finance as a suspended advance payment, due to the fact that there is no allocation for such payment in the 2006 budget, and until the completion of further investigation and approvals.	The amount was properly classified during 2007.		


Matters Related to Ministry of Finance Current and Prior Year

17. UNITED NATIONS' COMPENSATION FUND

Observation	Recommendation	Risk Level	Status
<p>According to UNSCR 1483 (2003), the proceeds of export sales of oil and oil products shall be deposited into the Oil Proceeds Receipts Account (OPRA) at FRBNY and immediately thereafter 95% is required to be deposited in the DFI account at the FRBNY and the remaining 5% is to be deposited in the United Nations' Compensation Fund that was established in accordance with UNSCR 687 (1991) and subsequent relevant resolutions as a result of the Iraqi invasion of Kuwait during 1990.</p> <p>We noted the MOF has no information about the following matters:</p> <ul style="list-style-type: none"> • Amount of disbursements made from the Compensation Fund to each beneficiaries and payments details and supporting documents. • The balance available at the Compensation Fund as of 31 December 2007. • The remaining outstanding amounts due to the United Nations Compensation Fund that should be deposited in the Compensation Fund subsequent to 31 December 2007. • The estimated date of the final payment to the Compensation Fund. <p>During 2007, MOF requested from Iraqi Council of Ministers to resolve this matter.</p>	<p>We recommend the MOF to follow up with the Government of Iraq in order to take necessary actions to address the above issues and maintain sufficient information about the United Nations Compensation Fund for the purpose of making suitable disclosure in the notes to the DFI's financial statements.</p> <p>Following the meeting with IAMB and COFE, we received a letter from the United Nations providing us with the following information:</p> <ul style="list-style-type: none"> • Balance available at the Compensation fund : U.S.\$ 360 million. • The remaining outstanding amounts due to United Nations Compensation Fund : U.S.\$ 28,950 million. • As of December 31, 2007 about U.S. \$ 23,430 million had been paid out to award recipients. • At the present rate of Iraqi oil sales, it would take approximately 17 years for the compensation award to be fully paid. 		<p>OLD</p>


Matters Related to Ministry of Finance Current and Prior Year

18. PASSWORD SECURITY NOT IMPLEMENTED

Observation	Recommendation	Risk Level	Status
We noted that there is no main menu to access the Accounting Database Application of the DFI at the Accounting Department of Ministry of Finance; moreover, the only way to access the Application is by running the source code through Microsoft Access 2003. Furthermore, anyone can access and run the Application because the password control has not been implemented, and all users have unrestricted access to application.	We recommend suitable security controls be implemented immediately to ensure access to data is restricted to authorized users only.		NEW


Matters Related to Ministry of Finance Current and Prior Year

19. SEGREGATION OF DUTIES

Observation	Recommendation	Risk Level	Status
We noted that the programmer has unrestricted access to Accounting Database Application, and therefore; the programmer is in a position to make unauthorized or erroneous changes to data files.	We recommend to constantly review the segregation of duties in IT department and separate incompatible duties where possible. In our view, the current lack of segregation arose as initially IT was the only department with skills and knowledge to operate the Application. However, Programmers access to update data should be restricted. In addition, any data files needed for program testing should be copied into the test area.		NEW


Matters Related to Ministry of Finance Current and Prior Year

20. PROGRAM DOCUMENTATION PROCEDURES

Observation	Recommendation	Risk Level	Status
We noted that the Accounting Department at MOF does not document any changes made into their Application. Also, the process of locating information about the programmed code is not efficient. To find a certain change, the whole program must be reviewed, and finding details of the latest change is time consuming.	<p>We recommend detailing of all changes made to the Application be recorded in a block of narrative at the top of the program code as well as in the relevant part of the code itself. This step will provide quick and easy reference to work previously carried out and its position in the program, which will increase the efficiency of the programming function.</p> <p>We suggest also using a control form, displaying the history of revisions made to Application's programs within the Application, and be maintained as part of the System documentation. This form should include the programmer name, the program number, the date and purpose of the modification, the user request number to which it relates, and a description of the modification.</p>		NEW


Matters Related to Ministry of Finance Current and Prior Year

21. USER PROGRAM CHANGE REQUEST PROCEDURES

Observation	Recommendation	Risk Level	Status
<p>We noted no standard procedures for users to follow when initiating and controlling requests for Application development and maintenance; such requests are often verbally communicated.</p> <p>Without formal written Application development and maintenance procedures, there is a risk that, some program changes may not be valid, or some program changes may not be adequately tested before being implemented.</p> <p>To help ensuring these control objectives are met, documented evidence of users' requirements and written authority for program changes should be developed.</p>	<p>We recommend designing forms to provide standard documentation for all user requests. These forms should be prenumbered and include, at a minimum, the following details:</p> <ul style="list-style-type: none"> • Name of the user initiating the request. • Date of the request. • Specifications of changes required. • Required completion date for request. • Authorization of request by user department head. • Authorization of request by data processing management; the completed user request forms should be filed in numerical sequence. Periodic checks of the sequence would enable data processing management to identify any requests not completed for follow up by management. <p>Management shall ensure that standard documentation is used across all changes in order to provide evidence for change requests with the required authorization, testing, and approvals.</p>		NEW


Matters Related to Ministry of Finance Current and Prior Year

22. ACCESS TO SOURCE CODE

Observation	Recommendation	Risk Level	Status
We noted that the programmer has access to an Application's source code. Where administrative, development and support functions are not segregated; there is a risk that the programmer could make unauthorized changes to program parameters or process data without being detected.	We recommend prohibiting programmer access to source code to minimize the risk of unauthorized changes. Access to source code should be monitored under close supervision of Management.		NEW


Matters Related to Ministry of Finance Current and Prior Year

23. COMPUTER SECURITY

Observation	Recommendation	Risk Level	Status
<p>In reference to direct access devices on the end user computer, the following was noted:</p> <ul style="list-style-type: none">Floppy drives are enabled.CD-ROM drives are enabled.USB ports are enabled.End user has administrator privileges on his/her computer. <p>With the uncontrolled use of external media as well as administrative privileges, the Department risks increasing the potential for the spread of viruses. Furthermore, installation of unauthorized programs as well as the copying of sensitive and confidential information may occur.</p>	<p>We recommend considering disabling all direct access devices on user workstations. Moreover, user should not be given administrator privileges on computer. Additionally, should a solid business case exist based on a formal risk assessment, Management should consider enabling certain drives / ports and granting power user privileges on computers exclusively to those justified in the business case. In such a case, approvals and authorizations should be obtained from the appropriate level of Management.</p>		NEW


Matters Related to Ministry of Finance Current and Prior Year

24. OPERATING SYSTEM UPDATE

Observation	Recommendation	Risk Level	Status
We noted that Application's computer operating system is not updated with the most recent operating system update patches. Therefore, it will lead to the risk of exploitation of known security vulnerabilities in systems which are not sufficiently protected by updated operating system patches.	We recommend following up, test, and deploy most recent operating system update patches in order to safeguard the Application's computer assets regularly.		NEW

Matters Related to Ministry of Finance Current and Prior Year


25. COLLECTION OF AMOUNTS RESTRICTED ABROAD

Observation	Recommendation	Risk Level	Status
During the course of our audit, we noted that an amount of U.S. \$ 10,886,400 of the petroleum export sales was seized based on a seizure order issued by Court of Roma – Italy on 23 March 2006 as a result of a lawsuit against the Iraqi Ministry of Planning. The Government of Iraq believes that the court order violates UNSCR 1483 (2003).	We recommend the MOF coordinate with the Ministry of Justice and the Ministry of Foreign Affairs to follow up on this matter and take whatever action required and justified to recover this seized amount.		OLD

MATTERS RELATED TO CENTRAL BANK OF IRAQ CURRENT AND PRIOR YEAR


Matters Related to Central Bank of Iraq Current and Prior Year

26. DELEGATION & AUTHORITY MANUAL

Observation	Recommendation	Risk Level	Status
<p>Payment orders through the DFI account, issued by the Ministry of Finance, are carried out by the Investment Directorate in the CBI by issuing payment orders approved by three employees from middle management at the CBI. A summary of payment orders is then prepared, indicating payment orders numbers, Ministry of Finance approval numbers and the beneficiary, in order to be approved by the proper management level in the CBI.</p> <p>The CBI's authorized signatories list, however, does not include a formal authority matrix that specifies the role of each CBI's authorized signatory and their approved limits to authorize the execution of banking transactions of DFI.</p>	<p>We recommend the following:</p> <ol style="list-style-type: none"> 1. The MOF shall develop an authorization matrix to govern all DFI transactions to ensure that adequate and appropriate controls have been put in place. 2. The authorization matrix shall specify the authorized managerial levels, authorized activities and the authorization limit for each type of DFI activities and transactions, including cash transfers and payments. 3. The types of authorities are as follows: <ul style="list-style-type: none"> •Initiate •Review •Approve 4. The authorization matrix of the DFI shall be reviewed and approved by the COFE, the IAMB and the Government of Iraq. 5. Based on the internal control best practices, no individual should have the sole authority to sign and execute bank payment transactions above a pre-determined limit. All transactions above this limit should therefore be signed by two or more signatories based on the approved authorization matrix. 		OLD

Matters Related to Central Bank of Iraq Current and Prior Year

27. REPORTING THE RECOVERED AND REFUNDED AMOUNTS

Observation	Recommendation	Risk Level	Status																																																						
<p>During our audit of the DFI’s statements in the CBI’s records, we noted that some of the deposited amounts in the DFI account at the FRBNY do not have sufficient supporting documents, except for the SWIFT confirmation from FRBNY. The deposited amounts mainly are recovered from letters of credit cancellation, interest on cash margins or excess of funding over the required amount.</p> <p>The following schedule shows examples of amounts that were deposited in the DFI account during 2006 without sufficient supporting documents:</p> <table><tr><th>Date of Deposited In DFI</th><th>Amount U.S. \$</th><th>Description</th></tr><tr><td>22/1/2007</td><td>822,461</td><td>No information</td></tr><tr><td>6/2/2007</td><td>889,606</td><td>No information</td></tr><tr><td>20/2/2007</td><td>18,004</td><td>Receipts related to Rafidain Bank</td></tr><tr><td>23/2/2007</td><td>10,658</td><td>No information</td></tr><tr><td>16/3/2007</td><td>24,415</td><td>No information</td></tr><tr><td>4/4/2007</td><td>248</td><td>No information</td></tr><tr><td>4/4/2007</td><td>1,068,488</td><td>No information</td></tr><tr><td>17/4/2007</td><td>100,065</td><td>No information</td></tr><tr><td>17/4/2007</td><td>212,134</td><td>No information</td></tr><tr><td>24/4/2007</td><td>40</td><td>No information</td></tr><tr><td>7/5/2007</td><td>2,999,973</td><td>No information</td></tr><tr><td>8/6/2007</td><td>167,330</td><td>Receipts related to MOF</td></tr><tr><td>13/6/2007</td><td>8,999,970</td><td>No information</td></tr><tr><td>2/7/2007</td><td>1,471,697</td><td>No information</td></tr><tr><td>19/7/2007</td><td>2,010,186</td><td>No information</td></tr><tr><td>1/8/2007</td><td>1,463,298</td><td>Receipts related to resettle debt</td></tr><tr><td>1/8/2007</td><td>1,550,972</td><td>Transferred from CitiBank</td></tr></table>	Date of Deposited In DFI	Amount U.S. \$	Description	22/1/2007	822,461	No information	6/2/2007	889,606	No information	20/2/2007	18,004	Receipts related to Rafidain Bank	23/2/2007	10,658	No information	16/3/2007	24,415	No information	4/4/2007	248	No information	4/4/2007	1,068,488	No information	17/4/2007	100,065	No information	17/4/2007	212,134	No information	24/4/2007	40	No information	7/5/2007	2,999,973	No information	8/6/2007	167,330	Receipts related to MOF	13/6/2007	8,999,970	No information	2/7/2007	1,471,697	No information	19/7/2007	2,010,186	No information	1/8/2007	1,463,298	Receipts related to resettle debt	1/8/2007	1,550,972	Transferred from CitiBank	<p>We recommend that all deposited amounts are adequately supported to assist in determining the nature of the receipts in order to properly classify these amounts in the financial statement.</p>		OLD
Date of Deposited In DFI	Amount U.S. \$	Description																																																							
22/1/2007	822,461	No information																																																							
6/2/2007	889,606	No information																																																							
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Matters Related to Central Bank of Iraq Current and Prior Year	
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27. REPORTING THE RECOVERED AND REFUNDED AMOUNTS

Observation				Recommendation	Risk Level	Status
1/8/2007	14,742,595	No information	<p>These recovered amounts were included in other receipts in the DFI statement of cash receipts and payments. As the recovered amounts include refundable cash margins, recording the recovered amounts in other receipts, rather than offsetting against related letter of credit payments in the same period, overstates the cash receipts and payments balances.</p>			
29/8/2007	102,686	No information				
29/8/2007	750,000	No information				
29/8/2007	455,000	No information				
4/9/2007	39,286	Receipts from Toku				
6/9/2007	30,653	No information				
14/9/2007	287	Receipts from ABN AMRO Bank				
27/9/2007	15,000,000	No information				
28/9/2007	905	No information				
2/10/2007	6,134	No information				
1/11/2007	1,689,094	No information				
30/11/2007	682,805	No information				
3/12/2007	1,605,562	No information				
10/12/2007	10,000,000	No information				
17/12/2007	2,593,451	No information				
17/12/2007	93,414	Receipts related to MOF				
18/12/2007	3,944,410	No information				
24/12/2007	4,999,972	Dividends from Arabic Iraqi Company –Dubai				
27/12/2007	161,000	No information				


Matters Related to Central Bank of Iraq Current and Prior Year

28. DFI RECORDS AT THE CENTRAL BANK

Observation	Recommendation	Risk Level	Status
<p>The DFI's bank accounts at the FRBNY are managed by the CBI on behalf of the MOF and included as part of the CBI's accounting records.</p> <p>As of 31 December 2007, there is an un-reconciled difference of U.S. \$ 4.025 million between the balance recorded by the DFI and the related balance (maintained for control purposes) in the CBI records.</p> <p>This difference does not affect the DFI's statement of cash receipts and payments, as this statement was compiled directly from the Excel sheets database maintained by the CBI, the FRBNY statement and other external sources.</p>	<p>We recommend that the CBI properly reconciles the remaining difference of U.S. \$ 4.025 million and arranges for the appropriate adjustments to be made to resolve this difference.</p> <p>We further recommend that the CBI maintains separate records for the DFI with complete and detailed documentation for each transaction. These records should then be reconciled with the FRBNY bank statement and the MOF records on a timely basis and any differences should be investigated, reported and resolved.</p> <p>Once this process is properly established, the DFI financial statement should be prepared directly from the DFI accounting records, rather than the current Excel sheets database maintained by the investment directorate at the CBI.</p>		OLD


Matters Related to Central Bank of Iraq Current and Prior Year

29. DATA ENCRYPTION AND CONFIDENTIALITY

Observation	Recommendation	Risk Level	Status
<p>During our audit, we noted that several payment requests for oil exports are sent by the CBI's Oil Export Department to the corresponding banks of the CBI through internet mail.</p> <p>This practice may result in security concerns over the integrity and confidentiality of the data as internet mail may not have the encryption and security protection required for such payment requests.</p>	<p>To ensure the protection of confidentiality and integrity of data, we recommend that all payment requests with corresponding banks must be encrypted through CBI secured mailing system or by using SWIFT electronic transfer system.</p>		OLD



Matters Related to Central Bank of Iraq Current and Prior Year

30. INTEREST CALCULATION FOR REPURCHASE AND TREASURY BILLS INVESTMENT

Observation	Recommendation	Risk Level	Status
During our audit in the CBI, we noted that the investment department did not regularly recalculate the interest income from the Repurchase and Treasury bills investment related to DFI, and in the cases when the interest is recalculated, this procedure is neither documented nor reviewed by a supervising employee.	We recommend that all interest received from any source should be recalculated to confirm this is in accordance with the investment agreement, and signed as being reviewed and approved by an authorized person.		OLD


Matters Related to Central Bank of Iraq Current and Prior Year

31. AUTHORIZED SIGNATORIES ON THE DFI BANK ACCOUNT

Observation	Treatment Method	Risk Level	Status
<p>Based on our review of the confirmation received from the FRBNY on 10 January 2007, we noted the names of the following authorized persons continued to be listed even though they retired from the CBI during 2006.</p> <ul style="list-style-type: none">• Former Deputy Governor.• Former General Manager of the Investments Directorate.• Former Manager of the Investment Directorate.• Former Manager in the Letters of Credit Directorate.	<p>During 2007, the CBI informed the FRBNY to cancel the authorization of persons previously mentioned.</p>		


Matters Related to Central Bank of Iraq Current and Prior Year

32. CLASSIFICATION OF DFI'S CASH RECEIPTS AND CASH PAYMENTS

Observation	Recommendation	Risk Level	Status
<p>During the course of our audit, we noted that the CBI maintains an Excel database for all the DFI cash receipts and cash payments, where we noted the following:</p> <ul style="list-style-type: none"> • Cash payments are not classified in the CBI database in accordance with the presentation of each category of cash receipts and cash payments in the DFI financial statement. • The CBI database is missing clarification information such as the MOF's payment order number, letter of credit number, beneficiary's name, the destination account number where the money was transferred and the description of each transaction. • Some errors were encountered in the 'details' field of the database, e.g. the name of the ministry. • Some receipts were misclassified, e.g. the interest received from JP Morgan Chase that was classified as other receipts instead of being classified as interest received. 	<p>We recommend that the CBI develop procedures to ensure the DFI cash receipts and cash payments are properly recorded and classified in accordance with the presentation of the DFI annual financial statement, which has been prepared in accordance with International Public Sector Accounting Standards / Financial Reporting on Cash basis.</p>		<p>OLD</p>


Matters Related to Central Bank of Iraq Current and Prior Year

33. INTEREST PAID ON CASH MARGINS

Observation	Recommendation	Risk Level	Status
<p>During our audit on cash receipts, we noted that interest payments received from JP Morgan Chase on funds deposited as cash margins against opened Letters of Credit amounted to U.S. \$ 128,379 thousand during 2007 and the cash margin balances were U.S. \$ 2,474,616 and Euro 140,883 as of 31 December 2007, as stated in the confirmation received from JP Morgan Chase.</p> <p>Interest payments are transferred to the DFI on a quarterly basis. However, there is no documented evidence that the interest received is recalculated to ensure the accuracy and reasonableness of the amount of interest received.</p> <p>These interest payments are recorded in the monthly statement of cash receipts and payments prepared by the CBI, although the source of these payments is not documented.</p> <p>In addition, we noted that no interest was recorded in the DFI cash receipts against the cash margins held at Citibank amounting to U.S. \$ 321,589,553 as of 31 December 2006.</p>	<p>We recommend that the CBI re-computes all interest received from the correspondent banks on timely basis to ensure the amount is fairly stated.</p> <p>Additionally, we recommend that CBI has to follow up with Citibank in order to clarify the reasons behind not booking interest on the cash margin held with.</p>		OLD

Matters Related to Central Bank of Iraq Current and Prior Year


34. PAYMENTS FROM THE DFI SUB-ACCOUNT

Observation	Recommendation	Risk Level	Status
During the course of our audit, we noted that a detailed monthly statement is not being prepared by the CBI to record the details of the cash payments from the DFI sub-account at the FRBNY managed by the U.S. Agencies. The CBI only prepares a summary letter on a daily basis showing the cash receipts and cash payments of the sub-account.	We recommended that the CBI prepares a detailed monthly statement for all payments made from the DFI sub-account showing the amounts paid, payment order numbers and the beneficiary name, in addition to the description of the nature of the transaction.		OLD

**MATTERS RELATED TO SOMO AND MINISTRY OF OIL CURRENT AND PRIOR
YEAR**


Matters Related to SOMO and Ministry of Oil Current and Prior Year

35. IMMUNITY

Observation	Recommendation	Risk Level	Status
In accordance with UNSCR 1483 (2003), certain Member States have taken legal steps, as considered necessary, to ensure immunity from legal proceedings for the purchase of petroleum and petroleum products originating in Iraq, until title passes to the initial purchaser, so as not to be subject to any form of prior judicial, administrative or arbitral lien or judgment. This immunity expires on 31 December 2008 unless the United Nations Security Council decides otherwise.	We recommend the Government of Iraq to consider what action is required to ensure the continuity of the immunity over the petroleum and petroleum products or to find out and assess any alternative procedures to protect the Member States.		OLD


Matters Related to SOMO and Ministry of Oil Current and Prior Year

36. COMPLETENESS OF PETROLEUM AND PETROLEUM PRODUCTS SALES

Observation	Recommendation	Risk Level	Status
<p>The IAMB recommended in March 2004 the expeditious installation of a comprehensive oil metering system in Iraq and in accordance with standard oil industry practices. Oil metering is a key factor to achieve financial transparency and accountability over oil resources in Iraq. While the Iraqi Government supports oil metering, progress has been slow.</p> <p>Some metering has been installed at oil terminals, but there continues to be no metering in the oil fields. Because of the absence of an overall comprehensive system of controls over oil, there are un-reconciled differences between oil extraction, production, export sales and internal usage.</p> <p>During January 2007, we noted that new metering systems were installed at the loading points only, but still no metering systems have been installed at the oil wells, storage facilities and refineries.</p> <p>These systems need to be calibrated in accordance with Committee of Calibration and measurement.</p>	<p>We recommend installation of Comprehensive metering systems for all oil industry related entities and expeditious installation and calibration processes for entities already received the metering systems.</p>		<p>OLD</p>


Matters Related to SOMO and Ministry of Oil Current and Prior Year

37. PETROLEUM PRODUCTS SALES

Observation	Recommendation	Risk Level	Status
<p>During the course of our audit, we noted that the State Oil Marketing Company (SOMO) policy is to sell fuel oil through cash advances made by customers before shipping. Cash received from export sales of petroleum products during the year ended 31 December 2007 amounting to U.S. \$ 770,165,984 has been deposited in bank accounts controlled by SOMO.</p> <p>According to UNSCR 1483 (2003), 95% of the proceeds of export sales of petroleum and petroleum products should be deposited in the DFI account. Accordingly, the cash receipts in the DFI financial statement for the year ended 31 December 2007 and the cash balance as of 31 December 2007 are understated by U.S. \$ 731,657,685.</p> <p>Also, we noted that according to SOMO's records, the export sales of petroleum products excluding barter transactions during the year ended 31 December 2007 amounted to U. S. \$ 923,915,546, while the total proceeds deposited into local banks amounted to U.S. \$ 770,165,984. We were not provided with reconciliation for the difference of U.S. \$ 153,749,562 between the total sales and total collections.</p>	<p>We recommend, in order to comply with UNSCR 1483 (2003), SOMO should arrange to deposit the proceeds of export sales of petroleum products in the DFI account on a timely basis.</p> <p>We further recommend SOMO to reconcile all advances received with the related sales ledger and sales invoices on a monthly basis. Any reconciling differences should be investigated, reported and cleared on a timely basis.</p>		OLD

Matters Related to SOMO and Ministry of Oil Current and Prior Year


38. BARTER TRANSACTIONS

Observation	Recommendation	Risk Level	Status
<p>During the course of our audit, we noted that SOMO engaged in barter transactions with the Syrian Government for exports of petroleum and petroleum products. Barter transactions consist mainly of exports of fuel oil in exchange for petroleum products, and exports of petroleum in exchange for electricity and petroleum products. The total barter transactions during 2007 amounted to U.S. \$ 217,391,457 According to UNSCR 1483 (2003), 95% of the proceeds of export sales of petroleum and petroleum products should be deposited in the DFI accounts. As these were non-cash transactions, these barter transactions are not recorded in the DFI's statement of cash receipts and payments.</p> <p>Also, according to the agreement between SOMO and the Syrian Government, when the amount due from the Syrian Government exceeds U.S. \$ 10,000,000 for more than three months, a cash payment covering 75% of the due amount should be transferred to the other party. However, during the year, we noted that the amount due from the Syrian Government exceeded U.S. \$ 10,000,000 for more than three months and no cash transfer was received during 2007.</p> <p>Total amount due from the Syrian Government as of 31 December 2007 according to SOMO's records amounted to U.S. \$ 302,390,176. This amount has not been confirmed by the Syrian Government.</p>	<p>We recommend SOMO to send a statement of barter transactions on a monthly basis to the Syria Government, in order to minimise any disputes that may arise with respect to any amounts relating to exchanged products.</p> <p>In addition, we recommend SOMO to request a confirmation of the balance outstanding from the Syria Government on a monthly basis and reconcile this confirmation to SOMO's records. Any reconciling differences should be investigated, reported and cleared on a timely basis.</p>		OLD

**MATTERS RELATED TO CONTRACTS ADMINISTERED BY U.S. AGENCIES
DURING THE CURRENT AND PRIOR YEAR**


Matters Related to Contracts Administered By U.S. Agencies During the Current and Prior Year

39. U.S. AGENCIES OUTSTANDING CONTRACTUAL COMMITMENTS

Observation	Recommendation	Risk Level	Status
<p>We noted that the U.S. Agencies did not maintain a complete database of outstanding contractual commitments for contracts signed by the former CPA.</p> <p>During our audit for the year ended 31 December 2006, we received Excel sheets extracted from the database showing detailed contracts information (i.e. contract number, contractor name, awarded date, date of completion, closeout date, contract value, amount paid, outstanding balance, contract status, related Ministry, etc). During or audit of these contracts, we noted the following:</p> <ul style="list-style-type: none"> • Certain contracts closing dates are in 2007 but they are shown as completed contracts as of 31 December 2006 (i.e. DFIWAT-06-C-0021). • U.S. Agencies did not furnish us with contracts database as at 31 December 2007. <p>Based on the above, the controls to ensure the completeness of the contract database and the commitments outstanding balance at 31 December 2007 need to be improved.</p>	<p>We recommend that the U.S. Agencies that are responsible for administering and closing DFI funded contracts should ensure that the database contains all DFI funded contracts signed by the former CPA, together with any other new contracts, and that the status of all contracts are fairly stated in the contracts database.</p>		OLD


Matters Related to Contracts Administered By U.S. Agencies During the Current and Prior Year

40. U.S. AGENCIES CONTRACTS DATABASE

Observation	Recommendation	Risk Level	Status
<p>We noted that the contracts database being used by the contracting department is very simple and does not have any access privileges. Consequently, any of the contracting officers can access the contracts database to add, delete or change data without leaving an audit trail.</p> <p>In addition, the contracts database is not integrated with the disbursements database.</p>	<p>The U.S. Agencies should develop security procedures to properly control and monitor access to the database and ensure any additions, deletions or other changes are made only by authorized officers.</p> <p>We further recommend that the U.S. Agencies consider integrating the contracts and disbursements databases.</p>		OLD


Matters Related to Contracts Administered By U.S. Agencies During the Current and Prior Year

41. PROJECTS HANDOVER TO THE GOVERNMENT OF IRAQ

Observation	Recommendation	Risk Level	Status
<p>The U.S. Agencies have been performing an administrative function on behalf of the Government of Iraq or the beneficiary ministry and following up payments to contractors. For this purpose, the U.S. Agencies use the DD250 form as a control to ensure receiving and inspection of materials or services. However, we noted that this form is not being signed by the representative of the Government of Iraq or the beneficiary ministry.</p> <p>During the progress of the projects, U.S. Agencies issue letters to the Ministry of Finance to settle the due balance to each contractor. After the completion of the projects, the U.S. Agencies hand over the projects to the beneficiary ministry. We note that the beneficiary ministry does not sign any formal documents to confirm receiving the projects from the U.S. Agencies.</p>	<p>We recommend that the U.S. Agencies inform the Government of Iraq representatives of the progress of the contracts to ensure all contracts and services administered by the U.S. Agencies are appropriately handed over to the Government of Iraq. This will help the Government of Iraq to have more information about the status of the projects made for the benefit of the ministries. The DD250 form should be signed by the representative of the Government of Iraq or the beneficiary ministry to confirm this control is being carried out.</p> <p>Also, the beneficiary ministry should sign the project hand over letter from the U.S. Agencies to confirm receipt of the projects, thus increasing the documented controls over completed projects administered by the U.S. Agencies.</p>		OLD



Matters Related to Contracts Administered By U.S. Agencies During the Current and Prior Year

42. CASH ON HAND AND DISBURSEMENTS LIMITS

Observation	Treatment Method	Risk Level	Status
<p>We noted that the U.S. Agencies have no ceiling limits for either cash on hand and held in the U.S. Agencies vault or for cash payment transactions.</p> <p>During our audit, we noted certain high value cash payments transactions, e.g. payment of U.S. \$ 10 million on 1 January 2006 to one U.S. Agency in order for that U.S. Agency to pay its suppliers and contractors. We requested but did not receive the supporting documents for the amounts paid to the suppliers and contractors.</p>	<p>No payment transaction from was been performed out of cash on hand held with U. S. Agencies during 2007. However, during March 2008 the U. S. Agencies transferred all cash on hand to MOF's account at CBI.</p>		OLD


Matters Related to Contracts Administered By U.S. Agencies During the Current and Prior Year

43. DISBURSEMENT DOCUMENTS STAMPED AS PAID

Observation	Treatment Method	Risk Level	Status
We noted that the U.S. Agencies do not stamp the payments supporting documents (e.g. invoices) attached to the payment vouchers as "PAID" or otherwise defaced after the payment has been made. Therefore, there is a risk of duplicate payments being made for the same invoice.	During September 2007, the U. S Agencies started to stamp the payments supporting documents attached to the payment vouchers as "PAID".		


Matters Related to Contracts Administered By U.S. Agencies During the Current and Prior Year

44. CLOSED CONTRACTS WITH OUTSTANDING BALANCES

Observation	Recommendation	Risk Level	Status
We obtained a list from the U.S. Agencies includes contracts with "Closed Status". Based on our review, we noted that there are 2 contracts still having outstanding balances due to two suppliers amounting to U.S. \$ 2,581,128 for contracts number DFIWAT-06-M-0003 and DABV01-04-C-9019 as of 31 December 2006..	We recommend that the contract database and contracts files should be revised to ensure the completeness and accuracy of the information and to ensure management reports are up to date and fairly reflect the current status of the contracts.		OLD

Matters Related to Contracts Administered By U.S. Agencies During the Current and Prior Year

45. U.S. AGENCIES NEW CONTRACTS

Observation	Recommendation	Risk Level	Status																																																												
<p>The DFI sub-account was established at the FRBNY during 2004 to be managed by the U.S. Agencies and monitored by the Iraqi MOF. The purpose of this sub-account is to facilitate disbursements for contracts signed by the former Coalition Provisional Authority (CPA), requiring payments subsequent to 28 June 2004. U.S. Agencies management of the DFI sub-account expired on 31 December 2006.</p> <p>However, U.S. Agencies have signed new contracts during 2006 and which are still in progress during 2006. The total number of these contracts is 26, which include 19 contracts that were still in progress as of 31 December 2006, and amount to a total of U.S. \$ 41,741,783 as follows:</p> <table><tr><th>Award Date</th><th>Status</th><th>Contract number</th><th>Contract amount U.S. Dollar</th><th>Paid amount U.S. Dollar</th></tr><tr><td>3 February 2006</td><td>Completed</td><td>DFIWAT-06-M-0004</td><td>130,930</td><td>-</td></tr><tr><td>26 February 2006</td><td>In progress</td><td>DFIWAT-06-C-0008</td><td>34,900</td><td>-</td></tr><tr><td>15 March 2006</td><td>In progress</td><td>DFIWAT-06-C-0020</td><td>3,449,707</td><td>2,783,636</td></tr><tr><td>1 April 2006</td><td>In progress</td><td>DFIGRS-06-C-0001</td><td>1,421,000</td><td>1,002,000</td></tr><tr><td>10 April 2006</td><td>In progress</td><td>DFIWAT-06-C-0001</td><td>187,190</td><td>-</td></tr><tr><td>4 May 2006</td><td>Completed</td><td>DFIWAT-06-M-0001</td><td>63,000</td><td>-</td></tr><tr><td>20 May 2006</td><td>In progress</td><td>DFIWAT-06-C-0014</td><td>2,195,963</td><td>-</td></tr><tr><td>1 June 2006</td><td>In progress</td><td>DFIWAT-06-C-0017</td><td>989,688</td><td>94,500</td></tr><tr><td>6 June 2006</td><td>Completed</td><td>DFIWAT-06-C-0018</td><td>205,000</td><td>140,000</td></tr><tr><td>6 June 2006</td><td>Completed</td><td>DFIWAT-06-C-0019</td><td>20,000</td><td>16,700</td></tr><tr><td>6 June 2006</td><td>In progress</td><td>DFIWAT-06-C-0016</td><td>802,896</td><td>-</td></tr></table>	Award Date	Status	Contract number	Contract amount U.S. Dollar	Paid amount U.S. Dollar	3 February 2006	Completed	DFIWAT-06-M-0004	130,930	-	26 February 2006	In progress	DFIWAT-06-C-0008	34,900	-	15 March 2006	In progress	DFIWAT-06-C-0020	3,449,707	2,783,636	1 April 2006	In progress	DFIGRS-06-C-0001	1,421,000	1,002,000	10 April 2006	In progress	DFIWAT-06-C-0001	187,190	-	4 May 2006	Completed	DFIWAT-06-M-0001	63,000	-	20 May 2006	In progress	DFIWAT-06-C-0014	2,195,963	-	1 June 2006	In progress	DFIWAT-06-C-0017	989,688	94,500	6 June 2006	Completed	DFIWAT-06-C-0018	205,000	140,000	6 June 2006	Completed	DFIWAT-06-C-0019	20,000	16,700	6 June 2006	In progress	DFIWAT-06-C-0016	802,896	-	We recommend that the U.S. Agencies develop a plan for the completion of all outstanding contracts and to hand over these contracts to the beneficiary Iraqi ministry on a timely basis.		OLD
Award Date	Status	Contract number	Contract amount U.S. Dollar	Paid amount U.S. Dollar																																																											
3 February 2006	Completed	DFIWAT-06-M-0004	130,930	-																																																											
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6 June 2006	In progress	DFIWAT-06-C-0016	802,896	-																																																											


Matters Related to Contracts Administered By U.S. Agencies During the Current and Prior Year

45. U.S. AGENCIES NEW CONTRACTS

Observation					Recommendation	Risk Level	Status
12 June 2006	In progress	DFIWAT-06-C-0022	989,000	-			
14 June 2006	In progress	DFIWAT-06-C-0012	975,500	943,099			
17 June 2006	Completed	DFIWAT-06-C-0021	891,456	483,236			
17 June 2006	In progress	DFIWAT-06-C-0015	2,422,072	1,667,994			
8 July 2006	In progress	DFIWAT-06-C-0023	2,439,700	-			
11 July 2006	Completed	DFIWAT-06-M-0002	95,050	-			
13 July 206	In progress	DFIWAT-06-C-0024	2,615,000	769,000			
13 July 2006	In progress	DFIWAT-06-C-0025	185,238	-			
20 July 2006	In progress	DFIWAT-06-C-0026	1,749,363	-			
26 July 2006	In progress	DFIWAT-06-C-0027	4,621,937	1,341,120			
14 August 2006	Completed	DFIWAT-06-C-0003	110,000	32,500			
14 August 2006	In progress	DFIWAT-06-M-0003	1,609,230	132,405			
17 October 2006	In progress	DFIWAT-07-M-0001	6,992,988	6,194,078			
1 November 2006	In progress	DFIWAT-07-C-0001	372,550	-			
30 December 2006	In progress	DFIWAT-07-C-0002	6,172,425	-			
Total			41,741,783	15,600,268			


Matters Related to Contracts Administered By U.S. Agencies During the Current and Prior Year

46. HAND OVER OF U.S. AGENCIES DOCUMENTS TO THE BSA

Observation	Recommendation	Risk Level	Status
<p>During the course of our audit, we noted that on 11 December 2006, the U.S. Agencies submitted the contracts files and other supporting documents of the former CPA and the U.S. Agencies to the Iraqi Board of Supreme Audit (BSA).</p> <p>According to the BSA letter dated 25 February 2007 to the U.S. Agencies, the BSA informed the U.S. Agencies that they found financial and legislative violations, which lead the BSA to review all the submitted documents. As a result of these findings, and the Government of Iraq has retained its right to request compensation for any financial damage to the Iraqi budget due to any financial or administrative actions taken by the U.S. Agencies during the execution of the contracts.</p>	<p>We recommend the findings of the BSA are followed up to determine what action is required to be taken.</p>		OLD

Matters Related to Contracts Administered By U.S. Agencies During the Current and Prior Year


47. RECONCILIATION OF PAYMENTS MADE FROM DFI SUB-ACCOUNT

Observation	Recommendation	Risk Level	Status																								
<p>During the course of our audit, we noted that the CBI receives the MOF approval together with the U.S. Agencies statement that shows a summary of the payment order numbers requested by the CBI. The responsible person in the CBI then records this approval and supporting statement in a separate file. Subsequently, these orders are executed according to the payments orders issued by the U.S. Agencies.</p> <p>We noted that an official documented reconciliation is not being carried out periodically on a monthly basis by the CBI and MOF of the payments orders issued by the MOF and the payments made from the DFI sub - account at the FRBNY managed by the U.S. Agencies. Based on our review, we noted that the following retrieved amounts were not taken into consideration in the CBI and MOF records during the year 2006:</p> <table><tr><th colspan="2">Retrieval Date</th><th>Amount (U.S. \$)</th></tr><tr><td>1</td><td>29/1/2007</td><td>208,786</td></tr><tr><td>2</td><td>30/1/2007</td><td>48,,103</td></tr><tr><td>3</td><td>30/1/2007</td><td>87,602</td></tr><tr><td>4</td><td>30/1/2007</td><td>86,467</td></tr><tr><td>5</td><td>20/2/2007</td><td>99,980</td></tr><tr><td>6</td><td>13/3/2007</td><td>94,122</td></tr><tr><td>7</td><td>27/4/2007</td><td>130,852</td></tr></table>	Retrieval Date		Amount (U.S. \$)	1	29/1/2007	208,786	2	30/1/2007	48,,103	3	30/1/2007	87,602	4	30/1/2007	86,467	5	20/2/2007	99,980	6	13/3/2007	94,122	7	27/4/2007	130,852	<p>We recommend that the U.S. Agencies investigate the reasons for such a high number of retrieved amounts. We also recommend that the CBI carries out a periodic reconciliation on a monthly basis of the payment orders issued by the MOF and the payments made from the DFI sub-account at the FRBNY managed by the U.S. Agencies in order to ensure the accuracy of all payments from the account and to reconcile all outstanding amounts on a timely basis.</p>		OLD
Retrieval Date		Amount (U.S. \$)																									
1	29/1/2007	208,786																									
2	30/1/2007	48,,103																									
3	30/1/2007	87,602																									
4	30/1/2007	86,467																									
5	20/2/2007	99,980																									
6	13/3/2007	94,122																									
7	27/4/2007	130,852																									

GENERAL MATTERS ARISING FROM AUDIT


General Matters Arising from Audit

48. FOLLOW UP OF PREVIOUS MANAGEMENT LETTERS RECOMMENDATIONS

Observation	Recommendation	Risk Level	Status
<p>During our audit, we noted that the Board of Supreme Audit (BSA) followed up and requested the concerned parties to improve the weaknesses reported in the audit management letters issued by the external auditors.</p> <p>To date, we have noted that there is no formal action plan developed by the Central Bank of Iraq (CBI) and the Ministry of Finance (MOF) for timely follow up and implementation of the recommendations of prior period audits.</p> <p>We have however noted that a committee was constituted in February 2007 to take into consideration the recommendations of our management letter for the periods in order to enhance and develop the work procedures of the DFI. This committee is represented by the CBI, MOF, Ministry of Oil and the State Oil Marketing Company (SOMO). The committee held its first meeting during April 2007.</p> <p>We have not yet been provided with a copy of the charter setting out the roles and responsibilities of this committee.</p>	<p>We strongly recommend that action is to be taken to develop an action plan to address each of the points raised in the audit management letters.</p> <p>We further recommend that a status report is then prepared and reported on a periodic basis, either monthly or quarterly, highlighting the progress made and action still to be taken.</p>		OLD


General Matters Arising from Audit

49. INTERNAL AUDIT DEPARTMENT

Observation	Recommendation	Risk Level	Status
<p>During the course of our audit, we noted there is no internal audit department dedicated for the DFI. Audit procedures carried by the internal audit departments in both the Central Bank of Iraq (CBI) and the Ministry of Finance (MOF) are limited and only cover part of the DFI operations.</p> <p>The main objective of the Internal Audit Department should be to assist the DFI management to monitor the internal control systems over the DFI activities and focus on key issues or higher risk areas that require special attention to improve the controls over the accounting and operating activities of the DFI.</p>	<p>We recommend that consideration is given to developing the following for the DFI:</p> <ol style="list-style-type: none"> 1. Establish a dedicated internal audit department for the DFI. 2. Policies and procedures should be in accordance with the International Standards for the Professional of Internal Auditing as issued by the Institute of Internal Auditors (IIA). 3. Develop a risk-based audit work plan and internal audit programs approved by the COFE and the IAMB. 4. Develop an internal audit charter to clearly set out the organizational structure and to clarify authorities and responsibilities, including reporting. 5. Ensure that the internal audit staff has been trained properly and are qualified with appropriate levels of experience with the International Standards for the Professional of Internal Auditing. 6. Ensure that sufficient financial and operational resources are allocated to the internal audit department in order to enable the internal audit function to be effectively carried out. 		OLD


General Matters Arising from Audit

50. CORPORATE GOVERNANCE

Observation	Recommendation	Risk Level	Status
<p>Corporate Governance is the system by which entities are directed and controlled, in the interests of stakeholders.</p> <p>We consider the following to be essential elements of a Corporate Governance structure:</p> <ul style="list-style-type: none">• An active Board of Directors;• A proactive Audit Committee;• A sound internal control framework;• A relevant code of conduct defining ethical behavior;• Clear, enforced policies and procedures;• Effective management of risk;• An objective, well resourced internal audit function;• An independent effective external audit;• Systems that ensure transparent disclosure, effective communication and corporate accountability.	<p>We recommend that the MOF performs a review of the DFI current Corporate Governance framework to identify any areas where improvements are required.</p>		OLD


General Matters Arising from Audit

51. SERVICE LEVEL AGREEMENTS

Observation	Recommendation	Risk Level	Status
<p>Service level agreements are agreements between related entities to provide key services and deliverables according to a pre-determined timetable. These are established to ensure that inter-related activities between all related entities are carried out in an effective and timely manner.</p> <p>As there are many government entities involved in the DFI activities, the DFI may want to consider the implementation of service level agreements with the CBI, MOF, Trade Bank of Iraq (TBI), SOMO, and all other ministries.</p> <p>In this case, the service level agreement would document the nature of documents and information that are to be exchanged and the time by which such documents should be exchanged. The service level agreement would also include other key interactions between these parties. Once an agreement is executed between these parties, it would be the responsibility of a designated individual / heads of each party to ensure that the terms of the service level agreement are adhered to. The MOF should then, on a periodic basis, perform an assessment to ensure compliance with the service level agreements.</p>	<p>We recommend that the DFI management consider the merits of introducing and implementing service level agreements with the CBI, MOF, TBI, SOMO, and all other ministries.</p>		OLD

General Matters Arising from Audit

52. CONTROLS SELF ASSESSMENT

Observation	Recommendation	Risk Level	Status
<p>In recent years there has been a growing concern amongst large organisations that internal controls exceptions and breaches are not being escalated and resolved in a timely manner.</p> <p>Controls Self Assessment (CSA) is a relatively new and growing methodology which places the responsibility for compliance reporting in the department or organisation unit, supported by clear guidelines as to what is defined as an internal control exception and the timeframe for reporting and resolving such exceptions.</p> <p>This methodology is built on the following concepts:</p> <ul style="list-style-type: none"> • Exceptions and errors are clearly defined within the policies and procedures; • Instructions on the escalation of errors and exceptions, i.e. to who such matters are to be reported, and the time frame by which such matters have to be reported, are specified; • Actions to be taken by the person to whom such exceptions and errors are reported and the timeframe for resolution/escalation are also specified. <p>The application of CSA will mean that the responsibility for monitoring compliance with DFI's policies and procedures is entrusted to the individual departments on a full time basis. The role of the internal audit function would be to assess the effectiveness of the identification and reporting process.</p> <p>In the absence of clear specific guidance on what constitutes an</p>	<p>We recommend that management consider measures to implement a system of controls self assessment across all DFI activities and develop a structured framework to report all controls exceptions on a timely basis.</p>		<p>OLD</p>


General Matters Arising from Audit

52. CONTROLS SELF ASSESSMENT

Observation	Recommendation	Risk Level	Status
<p>internal control error or an exception, and specific policies and procedures on how these are to be escalated and resolved, the decision whether to escalate a potential internal control exception is determined by lower level staff. Such staff may, either through poor judgment or out of fear of reporting bad news, not report the internal control exceptions to senior management. The absence of specific procedures for staff in respect of internal control errors, including deadlines for resolution or reporting to the directors of department levels, increases the risk that reported internal control exceptions are not addressed.</p> <p>Finally in the absence of a structured reporting framework, the Director General of the Accounting Department does not receive a regular report on the current status of internal control compliance so that he is aware of any internal control issues which may arise and impact on the financial reporting.</p>			


General Matters Arising from Audit

53. AWARENESS OF CONTROLS

Observation	Recommendation	Risk Level	Status
<p>Given the complex nature of the DFI activities and the involvement of employees from different government entities, to the DFI should take action to raise the awareness of their employees of internal control and risk management concepts.</p> <p>Training of this type is an integral part of employee induction or career development programs. Such practices go a long way to improving the internal control environment of an entity.</p> <p>The objective is to help employees understand and appreciate the importance of internal control and risk management practices. This would assist the employees in complying with the DFI's policies and procedures and the Government of Iraq regulations in a more effective manner.</p> <p>A better understanding of internal controls and risk management practices by the employees would also contribute to improving the overall control environment within the DFI. The process would help employees understand the risks involved and consequently understand the importance of complying with laid down policies and procedures. Employees may also be encouraged to contribute suggestions to improvements in the internal control system as employees who are in direct charge of a particular function would be more able to identify relevant control weaknesses.</p>	<p>We recommend that management consider measures to increase the awareness of internal controls and risk management practices for all management and employees involved in the DFI's activities.</p>		OLD

General Matters Arising from Audit

54. FRAUD REPORTING

Observation	Recommendation	Risk Level	Status
<p>Fraud is a broad concept that refers generally to any intentional act committed to secure an unfair or unlawful gain. Financial fraud falls under four broad categories:</p> <ul style="list-style-type: none"> • Fraudulent financial reporting • Misappropriation of assets • Expenditures and liabilities for improper purposes (example: improper payment schemes) • Fraudulently obtained revenue and assets, and costs and expenses avoided. <p>We note that the DFI does not have a formally documented policy to deal with fraud should it arise, or to prevent a fraud from occurring.</p>	<p>We recommend that management consider the merits of establishing a “whistleblower” program which should provide employees and others a means of:</p> <ul style="list-style-type: none"> • Communicating concerns, anonymously if preferred, about potential violations of the Government of Iraq regulations, including unethical behavior and actual or suspected fraud, without fear of retribution. • Obtaining advice before making decisions that appear to have significant legal or ethical implications. <p>This program should operate independently of management. This independence can be achieved through administration of the program by establishing an independent party within the MOF, such as an ethics or compliance officer or internal auditor with appropriate experience and objectivity, who reports directly to the COFE.</p> <p>We further recommend that management assess (a) the current level of fraud awareness within the employees involved in the DFI activities and (b) the potential for a fraud occurring and being identified and reported. Current procedures should also be reviewed to assess their sufficiency in addressing the risk of fraud, and amendments should be made to ensure that identification and reporting of a fraud is as timely as possible.</p>		OLD