

# Development Fund for Iraq Interim Results

January 1, 2006 to June 30, 2006



**IAMB Meeting October 30, 2006**

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# 2006 Audit Scope of Work



# Co-develop Expectation

- Understand your needs and apply all possible procedures to exceed your expectations
- Perform an effective and efficient audit in accordance with International Standards on Auditing (IAS) and the International Organization of Supreme Audit Institutions (INTOSAI) Standards in Government Auditing
- Provide valuable recommendations to improve the weaknesses in the internal control systems and corporate governance
- Follow up the status of the implementation of prior year audit recommendations

## Co-develop Expectation - Cont.

- Visit all Iraqi ministries receiving funds from the DFI
- Timely communications about emerging issues affecting the financial statements, operations, and/or internal controls
- Timely completion of our work and issuance of our reports
- Translation of all report to Arabic within reasonable time

We are ready to meet any other expectations related to the 2006 audit.

# 2006 Audit Deliverables



# Scope of the Interim Work

- Review the DFI interim statement of cash receipts and payments for the period from January 1, 2006 to June 30, 2006.
- We have conducted the review in accordance with International Standard on Review Engagement 2410, “Review of Interim Financial Information Performed by the Independent Auditor of the Entity”.

# Interim Work Locations

- Central Bank of Iraq (CBI)
- Ministry of Finance (MOF)
- U. S. Agencies
- State Oil Marketing Organization (SOMO)



# DFI Statement of Cash Receipts and Payments

|                             | <i>January 1 to June<br/>30, 2006</i>   | <i>July 1 to December<br/>31, 2005</i>  |
|-----------------------------|---|---|
|                             | <i>U.S. \$ 000'</i>                     | <i>U.S. \$ 000'</i>                     |
| <b>Cash Receipts</b>        |   |   |
| Export sales of petroleum   | 12,569,474<br><i>269,875,421 Barrel</i> | 12,704,059<br><i>254,189,610 Barrel</i> |
| UN Oil for Food program     | -                                       | 62,321                                  |
| Proceeds from frozen assets | 9,473                                   | 286,750                                 |
| Interest received           | 172,068                                 | 126,354                                 |
| Other receipts              | 195,075                                 | 345,904                                 |
| <b>Total Cash Receipts</b>  | 12,946,090                              | 13,525,388                              |

## DFI Statement of Cash Receipts and Payments – Cont.

|  | <i>January 1 to<br/>June 30,<br/>2006</i> | <i>July 1 to<br/>December 31,<br/>2005</i> |
|--|---|--|
| <b>Cash Payments</b>                         | <i>U.S. \$ 000'</i>                       | <i>U.S. \$ 000'</i>                        |
| Transfers to the Ministry of Finance         | 5,900,000                                 | 7,750,000                                  |
| LCs for the benefit of Iraqi ministries      | 4,598,139                                 | 4,435,174                                  |
| Contracts administered by U.S. Agencies      | 140,644                                   | 116,603                                    |
| Iraqi external debt repayments               | 398,986                                   | 159,315                                    |
| Other payments                               | 17,216                                    | 112,027                                    |
| <b>Total Cash Payments</b>                   | <b>11,054,985</b>                         | <b>12,573,119</b>                          |
| <b>Excess of cash receipts over payments</b> | <b>1,891,105</b>                          | <b>952,269</b>                             |
| Proceed from matured Treasury bills          | 1,967,991                                 | -  |
| Outstanding Treasury bills                   | (1,954,861)                               | (1,967,991)                                |
| Cash, beginning of period                    | 4,314,696                                 | 4,922,518                                  |
| <b>Cash, end of period</b>                   | <b>6,218,931</b>                          | <b>4,314,696</b>                           |

# Outstanding Information Required to Issue the Final Review Report

- Receiving the details of the cash receipts from export sale of petroleum products from SOMO.
- Receiving the supporting documents of the Iraqi debt payment of U.S.\$ 46 million for Inter-Arab Investment Guarantee Corporation.
- Receiving the supporting documents required to complete the review of the U.S. Agencies payments. *(Will be available during November)*

# Outstanding Information Required to Issue the Final Review Report – Cont.

- Signed letter of representation.
- Approval of the DFI financial statement by the Minister of Finance.

## Key Issues

- The DFI accounting records are maintained by the MOF as part of its records; no separate records for the DFI.
- The MOF records does not include complete set of accounting records to support the DFI's financial statement figures and the related notes disclosures.
- The DFI's interim statement of cash receipts and disbursements was compiled from:
  - Monthly statements of the DFI's main account prepared by the CBI,
  - DFI's sub-account maintained by the US Agencies and the CBI,
  - FRBNY statements,
  - MOF manual records and Access Data Base.

## Qualifications

## Key Issues – Cont.

## Qualifications

- Weak internal controls over the completeness of the export sales of petroleum and petroleum products
- Cash received from export sales of petroleum products have been deposited in SOMO bank accounts instead of the OPRA as required by UNSCR 1483
- Total export sales of petroleum products during the period from January 1, 2006 to June 30, 2006 amounted U.S. \$ 323 million. However we did not receive yet the total proceeds from the sales of petroleum products.
- The U.S. Agencies list of contractual commitments as of June 30, 2006 is incomplete.

## Key Issues – Cont.

## Qualifications

- The MOF paid U.S. \$ 221 million from DFI accounts for LCs of certain self financing Iraqi Ministries that are not covered by the DFI budget
- On the other hand, the MOF received advances of U.S. \$ 535 million from the ministries to cover their LCs. This amount has not been deposited in the DFI accounts; it was deposited in the MOF account.
- As a result, the DFI cash payments balance during the period is overstated by U.S. \$ 221 million.
- Such transactions shall be made directly by the ministries through the TBI.

## Key Issues – Cont.

- The MOF does not maintain separate bank account for the DFI at the CBI.
- All cash transfers during the period from DFI account at FRBNY to the MOF account at the CBI of U.S. \$ 5,900 million were recorded directly as cash payments in the DFI financial statement; *before transferring the cash to the intended Iraqi Ministries*
- Total amounts transferred to the Iraqi Ministries and related entities during the period amounted to U.S. \$ 6,840 million, (Exceed the receipts by U.S. \$ 940 million)



## Key Issues – Cont.

- Recall that in the prior period, the total amounts transferred from the DFI account at the FRBNY to the MOF account at the CBI exceed the total amounts transferred by the MOF to the Iraqi Ministries and related entities by U.S. \$ 1,008 million.
- There is no reconciliation between the amounts transferred from the DFI account at the FRBNY to the MOF account at the CBI.

## Key Issues – Cont.

- SOMO was engaged in barter transactions with the Syrian Government valued at US \$ 52.5 million (US \$ 51 million for petroleum, US \$ 1.5 million for petroleum products) in exchange for electricity and petroleum products.

# Other Issues and Findings

- The exported quantity of petroleum per South Oil Production Company records is more than exported quantity per SOMO's records by 991 thousand barrel during the period.
- Recall that there was a difference of 846 thousands barrel during the prior period.
- Reconciliations between Oil Production Companies and SOMO are not performed.

## Other Issues and Findings

- An amount of US \$ 10,886,400 of petroleum export sales proceeds was seized based on Court of Roma – Italy seizure order on March 23, 2006 as a result of a lawsuit against the Iraqi Ministry of Planning.
- The Iraqi Government is following up the collection of this amount and believes that the court order violates UNSCR 1483 related to the immunity of the petroleum and petroleum products originating in Iraq

## Other Issues and Findings

- There is a difference of U.S. \$ 207,000 between the total amount transferred to the Compensation Fund per the United Nations confirmation (U.S. \$ 661,551,000) and the CBI records (U.S. \$ 661,758,000).
- This difference has not been reconciled yet.

**Follow up of prior period Recommendations  
to Improve the  
DFI Internal Control System**

# MOF Accomplishment during the period

- The DFI's statement of cash receipts and payments for the period has been approved by the Director General of the MOF Accounting Department.
- Based on our recommendations, the MOF used an Excel data base to compile and prepare the DFI's statement of cash receipts and payments.
- The MOF prepared a reconciliation between the MOF and the CBI records related to the DFI.
- However, most of prior period audit recommendations have not been implemented yet.

## Board of Supreme Audit

- The Board of Supreme Audit (BSA) assigned a coordinator to assist Ernst & Young team in following up the information required from different parties.
- BSA is following up the observations reported in the prior year management letters.
- Regular meetings are being held with the BSA to follow up the progress of the audit.
- All 2006 audit issues will be communicated with the BSA on timely basis.



# Action Plan for Improvements

- An action plan should be prepared to implement the recommendations of the prior period management letters to improve the DFI internal controls.
- Appointment of a Director to the DFI to oversee the implementation of the action plan in all locations.
- The action plan should include clear assignment of the responsibilities for the implementation of each of the recommendations.
- Also, the action plan should include a time frame for the implementation of each of the recommendations.

## Action Plan for Improvements – Cont.

➤ The action plan should be implemented by the following parties to improve the DFI's accounting and internal control system:

- Central Bank of Iraq (CBI)
- Ministry of Finance (MOF)
- U. S. Agencies
- State Oil Marketing Organization (SOMO)
- Ministry of Oil
- All other Iraqi Ministry
- Kurdistan Region ministries

# DFI 2006 Audit

Plan for the Next Period

# DFI 2006 Audit Progress

The DFI 2006 audit will be conducted in two stages:

➤ Stage 1: Interim audit work that will be performed prior to the year end. This stage we will include:

- Planning of the 2006 audit
- Substantive testing of the cash receipts and payments.
- Testing oil export sales at SOMO
- Testing the Oil Proceeds Receipt Account
- Visiting part of the Iraqi Ministries
- Testing payments from U.S. Agencies sub-account

We already commenced the first 4 parts of Stage 1.

## 2006 Audit Progress – Cont.

- Stage 2: Final audit work that will be performed after year end. This stage we will include:
  - Update and wrap up of all testing performed during the interim audit
  - Receiving third party confirmations.
  - Visiting the remaining Iraqi Ministries and update interim work
  - Completing the test oil export sales at SOMO
  - Completing the test of Oil Proceeds Receipt Account

The following slides include summary of the work that will be performed for each part of the scope of work.

# Audit of DFI Financial Statements

- Planning and updating our understanding of the DFI's internal controls and accounting processes
- Testing cash receipts from oil export sales
- Testing cash receipts from other sources
- Testing cash disbursements from DFI
- Review the reconciliations between the MOF and other parties (*CBI, SOMO, Iraqi ministries and US Agencies*)
- Testing the cash balances at the FRBNY at end of the period

# Testing the Disbursements of the U.S. Agencies

- Verification of handover of DFI sub account from the U.S. Agencies to the Iraqi Government
- Planning and understanding internal controls over disbursements made by the US Agencies / Purchasing & Contracting Office (PCO)
- Testing of cash disbursements per CBI records
- Testing of cash disbursements per PCO record
- Testing of outstanding commitments
- Review the PCO reconciliations with CBI & MOF
- Testing the PCO cash balances at year end

# Testing Oil Export Sales

- Document key internal controls over the bidding on, and awarding of, export sales contracts
- Document key internal controls for capturing revenue from oil export sales and subsequent deposits in DFI
- Obtain list of SOMO export sales ledger and agree with the amount deposited in the FRBNY
- Review all exports sales of petroleum and a sample of petroleum products sales
- Review the reconciliation of export sales at SOMO with oil production companies



# Testing Oil Proceeds Receipt Account (OPRA)

- Match the amounts deposited in the OPRA with the export sales of petroleum as recorded by SOMO
- Recalculate the transfers from the OPRA pursuant to the UNSCR 1483 (95% to DFI & 5% to the Compensation Fund)
- Agree the payments from the OPRA to the cash deposited in the DFI and the cash transferred to the Compensation Fund
- Obtain a confirmation from the United Nations regarding the amounts transferred from the OPRA to the Compensation Fund

# Visiting all Iraqi Ministries

- Visiting all ministries and Kurdistan Region and understand the internal controls over the disbursements made from the DFI's fund
- Testing the DFI's funds disbursed by the Iraqi ministries
- The extent of the testing in each ministry will be based on our professional judgement based on the materiality level of the DFI financial statement. The test will cover the major capital expenditures financed by DFI.
- Review the reconciliation of the total DFI's funds received by the ministries with the disbursed funds per DFI records

# Timing of Issuance of the Draft Reports

- We expect to issue our draft audit and agreed upon procedures reports for the year ending December 31, 2006 by April 30, 2007.
- This timing is based on the assumption that we will receive all the information that we need from the MOF and all ministries and other parties by February 15, 2007.