

DEVELOPMENT FUND FOR IRAQ

Report of Factual Findings

In Connection With

Oil Proceeds Receipts Account

For the period from

July 1, 2005 to December 31, 2005



Private and confidential

July 10, 2006

**To Government of Iraq
To International Advisory and Monitoring Board
of Development Fund for Iraq**

REPORT OF FACTUAL FINDINGS - OIL PROCEEDS RECEIPTS ACCOUNT

We have performed the procedures agreed with you and set out in Appendix A of the attached report with respect of oil proceeds receipts account of Development Fund for Iraq. Our engagement was undertaken in accordance with International Standard on Related Services (ISRS) No. 4400, engagements to perform agreed-upon procedures regarding financial information. The procedures were performed solely to assist the International Advisory and Monitoring Board (IAMB) and the Iraqi Government (IG) in evaluating the Development Fund for Iraq's compliance with United Nations Security Council Resolution (UNSCR) 1483 paragraph 20 and 21, for the period from July 1, 2005 to December 31, 2005. The Government of Iraq is responsible for the Development Fund for Iraq's compliance with UNSCR 1483.

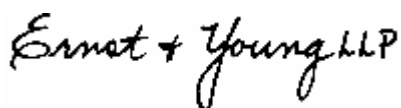
We report our findings in sections 1 to 3 in the attached report.

Because the procedures, which are detailed in Appendix A to this report, do not constitute an audit or a review made in accordance with International Standards on Auditing or International Standards on Review Engagements, we do not express any assurance.

Had we performed additional procedures or had we performed an audit or review made in accordance with International Standards on Auditing or International Standards on Review Engagements, other matters might have come to our attention that would have been reported to you.

Our report is solely for the purpose set forth in the first paragraph of this report and for the information of IAMB and IG and is not to be used for any other purpose or by any other parties. We do not accept or assume responsibility for any other purpose or to any other person who may receive this agreed upon procedures report. This report relates only to the accounts and items specified in Appendix A of the attached report, and does not extend to any financial statements of Development Fund for Iraq taken as a whole.

Yours faithfully
Ernst & Young



Baghdad, Iraq

**DEVELOPEMNT FUND FOR IRAQ
REPORT OF FACTUAL FINDINGS
IN CONNECTION WITH OIL PROCEEDS RECEIPTS ACCOUNT**

1. EXPORT SALES RECORDED BY SOMO TO DEPOSITS AT THE OPRA

1.1 PROCEDURES PERFORMED

We obtained from the Federal Reserve Bank of New York (FRBNY) statements of transactions for the period from July 1, 2005 to December 31, 2005 and we agreed the amounts of export sales of petroleum, petroleum products and natural gas, as recorded by the Iraqi State Oil Marketing Organization (SOMO), to the amounts deposited in the Oil Proceeds Receipts Account (OPRA).

1.2 FINDINGS

SUMMARY OF OIL EXPORT SALES

- We found that no export sales of natural gas took place in Iraq during the period from July 1, 2005 to December 31, 2005, due to the absence of infrastructure for the export of natural gas.
- We found that the total export sales and barter transactions of petroleum and petroleum products for the period from July 1, 2005 to December 31, 2005, were made through letters of credit (LCs) and barter transactions, as recorded by the Iraqi State Oil Marketing Organization (SOMO), and were as follows:

	U.S.\$		
	Export Sales	Barter	Total
Petroleum	12,872,584,674	68,989,566	12,941,574,240
Petroleum Products	218,681,669	9,575,351	228,257,020
Total	13,091,266,343	78,564,917	13,169,831,260

- We found that the amount of export sales made through LCs includes interest received of U.S.\$ 95,464 for delayed bank transfers, and is net of paid demurrage claims of U.S.\$15,418,783 incurred during the period from July 1, 2005 to December 31, 2005.
- We found that sales invoice no. B/2005/263 amounting to U.S.\$ 106,208,092, with interest of U.S.\$ 28,763, recorded by SOMO deposited in the OPRA on October 3, 2005 through letter of credit number 05/227, was not listed on the OPRA statement received from FRBNY. We have requested but not yet received from FRBNY clarification for this amount.
- We found that SOMO issued a debit note of U.S.\$ 434,957 to one of its customers as a price adjustment for discharging part of the lifting at a port other than the scheduled destination.

- We found that proceeds from export sales of petroleum for the period from July 1, 2005 to December 31, 2005 were deposited into the OPRA account approximately 30 days after the lifting, in accordance with the terms of LCs as follows:-

Deposited in OPRA for the period:

	U.S.\$
July 1, 2005 to December 31, 2005	11,373,233,119
Subsequent to December 31, 2005	1,499,351,555
	<u>12,872,584,674</u>

- We found that net cash advances received for, and proceeds of, export sales of petroleum products during the period from July 1, 2005 to December 31, 2005 amounted to U.S.\$ 211,421,722.
- The export sales of petroleum products, excluding barter sales, during the period from July 1, 2005 to December 31, 2005 were as follows:

	U.S.\$
Export sales of petroleum products	218,681,669
Total proceeds deposited at local banks	211,421,722
Difference	<u>7,259,947</u>

- As shown in the above table there is un-reconciled difference of U.S.\$ 7,259,947 between the total sales and total collections during the period from July 1, 2005 to December 31, 2005. We did not receive a reconciliation or analysis of this difference.
- We found that the net cash advances of U.S.\$ 211,421,722 were not deposited into the OPRA in accordance with UNSCR 1483, with the funds being deposited in SOMO bank accounts at the Trade Bank of Iraq, Rafidain Bank and a Jordanian branch of an Iraqi bank.
- We found that SOMO engaged in barter transactions with the Syrian Government for export of petroleum and petroleum products. Barter transactions were mainly in the form of exporting petroleum in exchange for electricity and petroleum products, and exporting fuel oil in exchange for petroleum products.
- We founds that the total amount of bartered petroleum and petroleum products with the Syrian Government for the period from July 1, 2005 to December 31, 2005 was U.S.\$68,989,566 and U.S.\$9,575,351, respectively.
- We found that as barter transactions are non cash transactions, no cash was deposited at the OPRA, nor the DFI account and Compensation Fund.

- Following is a summary of the monthly barter transactions of petroleum and petroleum product with the Syrian Government for the period from July 1, 2005 to December 31, 2005:

	U.S.\$		
	Petroleum	Petroleum Products	Total
July	13,990,742	1,169,971	15,160,713
August	20,329,033	1,246,072	21,575,105
September	4,162,777	3,467,042	7,629,819
October	18,130,550	3,341,774	21,472,324
November	12,376,464	313,704	12,690,168
December	-	36,788	36,788
	68,989,566	9,575,351	78,564,917

2. TRANSFERS FROM OPRA TO DFI ACCOUNT AND COMPENSATION FUND

2.1 PROCEDURES PERFORMED

- We recalculated the amounts transferred from the OPRA account, pursuant to the allocation requirements of UNSCR 1483 paragraphs 20 and 21.
- We agreed the calculation for the transferred amount with the actual transferred amounts to the DFI account and the Compensation Fund.

2.2 FINDINGS

- We found that the proceeds of export sales of petroleum and petroleum products were deposited into the Oil Proceeds Receipts Account (OPRA) and, immediately thereafter, 95% was deposited in the DFI account at the FRBNY and the remaining 5% was deposited in the Compensation Fund in accordance with UNSCR 1483. The Compensation Fund was established in accordance with UNSCR 687 and subsequent relevant resolutions, as a result of the Iraqi invasion of Kuwait during 1990.
- We found that the proceeds resulting from export sales of petroleum, deposited in the OPRA and, immediately thereafter, , 95% was deposited in the DFI account at the FRBNY and the remaining 5% was deposited in the Compensation Fund, during the period from July 1, 2005 to December 31, 2005 were as follows:

Period of export:

	U.S.\$		
	OPRA	DFI	Compensation Fund
July 1, 2005 to December 31, 2005	11,373,233,119	10,804,571,463	568,661,656
Prior to July 1, 2005	2,014,394,657	1,913,674,924	100,719,733
	13,378,627,776	12,718,246,387	669,381,389

U.S.\$ 2,014,394,657 represents proceeds of export sales of petroleum during the period prior to July 1, 2005 which were deposited in the OPRA during the period from July 1, 2005 to December 31, 2005.

- We recalculated the amount to be transferred from OPRA account to the DFI account and the Compensation fund pursuant to the allocation requirements of UNSCR 1438 paragraph 20 and 21 for the period from July 1, 2005 to December 31, 2005 to be as follows:

	<u>Amount U.S.\$</u>
Transferred to DFI account (95%)	12,603,134,284
Transferred to the Compensation Fund (5%)	663,322,857
Total deposits in OPRA account per FRBNY confirmation	<u>13,266,457,141</u>

- We found that the recalculated amount transferred from the OPRA was in accordance with the allocation requirement of UNSCR 1438 paragraphs 20 and 21.

3. TRANSFERS TO COMPENSATION FUND

3.1 PROCEDURES PERFORMED

- We obtained confirmation from the United Nations regarding the amounts transferred from the OPRA account to the Compensation Fund during the period from July 1, 2005 to December 31, 2005.
- We agreed the amount transferred from the OPRA to the Compensation Fund as stated in the FRBNY statement of transactions with the confirmation received from the United Nations.

3.2 FINDINGS

- We agreed the amount transferred from OPRA account to the Compensation Fund with the confirmation received from the United Nations, and noted the following difference:

	<u>U.S.\$</u>
Total transfers per FRBNY statement of transactions	663,322,857
Total amount deposited at the Compensation Fund according to United Nations confirmation	668,634,700
Difference	<u>5,311,843</u>

- We found this difference relates to the 5% proceeds of invoice number B/2005/263 amounting to U.S.\$106,208,092, together with interest of U.S.\$ 28,763 and that amounts of U.S.\$ 5,310,404 and U.S.\$ 1,438 were deposited at the Compensation Fund on October 3, 2005, but not listed on the OPRA statement of transactions received from the FRBNY. We have requested but not yet received from FRBNY clarification for this amount.

Appendix A

SCOPE OF WORK

In accordance with the agreed upon scope of work set out in our engagement letter dated March 12, 2006, the procedures to be performed in connection with the OPRA account held on behalf of the Central Bank of Iraq at the FRBNY are as follows:

1. Obtain from the FRBNY statements of transactions for the period from July 1, 2005 to December 31, 2005; agree the amounts of export sales of petroleum, petroleum products and natural gas, as recorded by the Iraqi State Oil Marketing Organization, to the amounts deposited in the OPRA account.
2. Recalculate the amounts to be transferred from the OPRA account, pursuant to the allocation requirements of UNSCR 1483 paragraphs 20 and 21, and agree these payments to the cash deposited in the DFI account and to the cash transferred to the Compensation Fund.
3. Obtain a confirmation from the United Nations regarding the amounts transferred from the OPRA account to the Compensation Fund during the period from July 1, 2005 to December 31, 2005.