THE WORLD BANK IRAQ TRUST FUND
WITHIN THE
INTERNATIONAL RECONSTRUCTION FUND FACILITY
FOR IRAQ

January 14, 2004

Middle East Department
MNCO2
Middle East and North Africa Region

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### ABBREVIATIONS AND ACRONYMS

<table>
<thead>
<tr>
<th>Abbreviation</th>
<th>Full Form</th>
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<tbody>
<tr>
<td>CIC</td>
<td>Council for International Coordination</td>
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<td>CPA</td>
<td>Coalition Provisional Authority</td>
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<td>FMR</td>
<td>Financial Management Report</td>
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<td>G7</td>
<td>Group of Seven Industrialized Countries</td>
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<td>IBRD</td>
<td>International Bank for Reconstruction and Development</td>
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<td>IDA</td>
<td>International Development Association</td>
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<td>IFC</td>
<td>International Finance Corporation</td>
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<td>IRFFI</td>
<td>International Reconstruction Fund Facility for Iraq</td>
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<td>ISRB</td>
<td>Iraq Strategic Review Board</td>
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<td>ITF</td>
<td>Iraq Trust Fund (World Bank)</td>
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<td>IMF</td>
<td>International Monetary Fund</td>
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<td>MENA</td>
<td>Middle East and North Africa</td>
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<td>MoPDC</td>
<td>Ministry of Planning and Development Cooperation</td>
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<td>PEP-ME</td>
<td>Private Enterprise Partnership for the Middle East</td>
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<td>PSD</td>
<td>Private Sector Development</td>
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<td>SBFF</td>
<td>Small Business Financing Facility (IFC)</td>
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<td>SOE</td>
<td>State-Owned Enterprise</td>
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<td>UN</td>
<td>United Nations</td>
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<td>UNDG</td>
<td>United Nations Development Group</td>
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<td>UNDP</td>
<td>United Nations Development Programme</td>
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<td>US</td>
<td>United States</td>
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I. INTRODUCTION

1. The following is a description of the proposed World Bank Iraq Trust Fund (ITF) which would operate within the International Reconstruction Fund Facility for Iraq (the Facility). The Bank would act as administrator of the ITF but is not expected to contribute to the ITF. However, when Bank lending resumes, ITF funds may be used to cofinance Bank-supported activities.

2. Mandate. At their April 12, 2003 meeting, the Group of Seven Industrialized Countries (G7) finance ministers and central bank governors recognized the need for a multilateral effort to rebuild and develop Iraq and for UN and Bank assistance. UN Security Council Resolution 1483 (May 22, 2003) noted the statement of the G7 and called for the international financial institutions to assist the people of Iraq in reconstruction and to facilitate assistance by the broader donor community. In response, on June 24, 2003, the UN hosted a meeting of some 50 states which, collectively, became known as the Liaison Group. The Liaison Group in turn requested a small number of major donors, known as the Core Group, to convene a Donors’ Conference. The Liaison Group also asked the Bank and the UN to assess Iraq’s needs, and to design a multi-donor trust fund to coalesce donor support around Iraq’s priority reconstruction needs.

A. Needs Assessment

3. The Bank and the UN, with support from the Iraqi national officials and the IMF, conducted a Needs Assessment during the period June through August 2003 in order to define Iraq’s reconstruction and transition requirements. The Needs Assessment was finalized following consultations in Dubai and Madrid with the Core Group, representatives of Iraq’s Governing Council, Iraqi sector ministries and the Coalition Provisional Authority (CPA). The final document was presented at the October 23-24 Donors’ Conference in Madrid and endorsed by the donors present and representatives of the Iraqi Governing Council. The Needs Assessment covers 14 sectors and cross-cutting themes, and identifies investment needs and priorities for the short and the medium term.

1 The Core Group comprised the European Union (Commission and Presidency); Japan; US; CPA; United Arab Emirates, with the IMF, the Bank and the UN as observers. Following the decision to hold the Donors’ Conference in Madrid, Spain was invited to join the Group. There is currently a proposal to expand the Core Group to donors who contribute over US$150 million of grant reconstruction assistance.

2 The Needs Assessment sectors are: education; health; employment creation; water and sanitation; transport and telecommunications; electricity; housing and land management; urban management; agriculture, water resources and food security; finance; state-owned enterprises; investment climate; mine action; and government institutions. Cross-cutting themes include: macroeconomics; economic management; human rights; gender; and the environment. Other sectors, such as cultural heritage, drugs and crime, were also assessed with UN support outside of the joint UNDG/World Bank process.
B. The International Reconstruction Fund Facility for Iraq

4. In parallel with the Needs Assessment, the Bank and the UNDG designed the International Reconstruction Fund Facility for Iraq (the Facility). The Facility aims to help donors channel their resources and coordinate their support for reconstruction and development activities in Iraq, in line with the priority areas emerging from the Needs Assessment as validated by the Iraqi authorities. The Facility complements other forms of donor support, including bilateral assistance. The structure, governance, and modalities of the Facility were designed in close consultation with the Core Group, other donors, and Iraqi national authorities over the period August through December 2003 at meetings held in Washington, D.C., Brussels, New York, Dubai, Madrid, and Amman.

5. The Facility encompasses two trust funds: the World Bank Iraq Trust Fund (ITF) to be administered by the Bank, and the UN Development Group Iraq Trust Fund (UNDG Trust Fund) to be administered by the United Nations Development Programme (UNDP), on behalf of itself and Participating UN Organizations. The Bank and the UNDG would utilize their complementary strengths to address the requirements identified in the Needs Assessment, each in accordance with its operational policies. Close coordination and avoidance of duplication would be achieved through a common governance structure, including a joint Donor Committee, a UN/World Bank Facility Coordination Committee, and a joint Secretariat. A more complete description of the Facility is provided in paras.16 and 38-46.

C. The Madrid Donor Conference

6. On October 23-24, 2003, high-level representatives from over 70 states and from a large number of multilateral organizations and NGOs met at the Madrid Donors’ Conference. Donors pledged about US$32 billion. In well-attended sector sessions, relevant sections of the Needs Assessment were discussed. The majority of donors was not able to provide details on the timing or mode of their assistance. Since Madrid, several donors have expressed their intention to contribute to the Facility and are looking forward to receiving a proposed work program for the ITF and the UNDG Iraq Trust Fund before making their allocations. A proposed initial work program for the ITF is included in the Bank’s Interim Strategy Note which is presented to the Executive Directors of the Bank simultaneously with this proposal for the ITF. Detailed work program proposals are to be presented to the donors in February, following completion of consultations with Iraqi authorities in January.

II. RATIONALE FOR THE WORLD BANK IRAQ TRUST FUND

A. Economic and Political Background

7. State of the Economy: Since the early 1980’s, Iraq has undergone three wars and a decade of economic sanctions. During this time, the country’s economy, infrastructure, and civic institutions deteriorated significantly. Income per head, which had peaked at over US$3,600 in the early 1980s on the back of sharp rises in the real price of oil, fell to a low of around US$300 in the early 1990s, before recovering (partly as a result of the Oil-for-Food
Program) to between US$480 and US$630 in 2003. Although data are unavailable, it is clear that there is widespread poverty.

8. Illiteracy rate (age 15 and above) is estimated at 60%, compared to MENA average of 35%. Life expectancy at birth is 63 years, compared to MENA average of 69 years. Under-5 mortality has increased from 60 per 1,000 in 1979 to 133 in 2001, compared to 33 in Jordan and 107 in Yemen. Maternal mortality (per 100,000 live births) is 300, compared to 41 in Jordan. Power generating capacity is currently estimated at 3,300 MW, compared to 9,295 MW in 1990, and demand significantly exceeds supply.

9. As the figures above vividly illustrate, Iraq presents a picture of social and economic degradation from decades of a tightly centralized command economy, where the state dominated industry, agriculture, and trade; where public resources were skewed towards military spending and food and energy subsidies; and where prices played little role in resource allocation. Medium and large industry is nationalized, with state-owned enterprises (SOEs) operating below capacity, if at all.

10. The growth of the Iraqi economy has relied heavily on oil. After three decades of growing production (1950-1980), damage to the oil industry during the Iran-Iraq and Gulf wars combined with transport problems and damaged industrial sites have decreased production. With its balance of payments falling short, Iraq resorted to foreign borrowing, resulting in massive debt that now threatens fiscal sustainability and future access to finance.

11. **Political Situation**: The CPA and the Governing Council have approved a plan for a transition to a sovereign Iraqi government by the end of June 2004. Under the current plan, approved in mid-November 2003, caucuses in Iraq’s 18 provinces would select a transitional assembly, which would then elect an executive branch, select ministers, and serve as a legislative body. The new transitional administration would assume full responsibility for governing Iraq by June 30, 2004. The assembly would draft a new constitution to lead to a fully elected government by the end of 2005. However, some of the features of the plan are still under discussion, with the possibility of compromises to broaden political support for the plan.

**B. Medium-Term Reconstruction Needs**

12. The Needs Assessment estimates the overall stock of medium-term reconstruction needs to be on the order of US$35.8 billion for mainly physical reconstruction, technical assistance, and training needs, plus additional operation and maintenance costs associated with new investments across the 14 sectors. In addition, for those sectors outside the UN/World Bank Needs Assessment, including security and oil, the CPA has estimated the cost of reconstruction needs as an additional US$19.4 billion over the coming years. Recurrent costs are not included in the Needs Assessment because they are to be covered by the Iraqi budget.

13. The US$35.8 billion (plus the US$19.4 billion addressed separately by the CPA) does not necessarily represent the financing gap because, over time, Iraqi government revenues or private sector financing is expected to increasingly cover the required investments, thereby reducing the need for external donor support. This is based on the assumption that, in a stable
environment, oil productivity and output will increase with the investment that will take place; general economic recovery will result in rising direct and indirect tax revenues; and an improved investment climate will result in significant financing from both domestic and international private investors.

14. In the meantime, however, Iraq has large reconstruction and new investment needs. Until the point when domestic revenues and private investment largely cover these expenditures, Iraq’s needs can be met in the short to medium term through a combination of direct budgetary support, CPA investment, bilateral assistance, and the Facility. Given the difficulties of bilateral funding at the early post-conflict stages, the Facility is expected to be a significant source of external finance for addressing priority needs quickly and flexibly. The main source of immediate investment financing is the US$18.6 billion contribution by the United States to be administered by a Program Management Office, reporting to the CPA Administrator.

III. THE FACILITY

A. Operating Principles

15. While recognizing that the current situation in Iraq presents unique challenges and constraints, the Facility will operate, to the extent possible, based on the principles which normally apply to multi-donor trust funds in a post-conflict situation. The arrangements aim to ensure, in particular, that:

   (a) Each project approved for funding is part of a priority program of reconstruction and development activities validated by the Iraqi authorities, based on the Needs Assessment and formulated in consultation with donors and other partners.

   (b) The activities financed by the donor community are implemented as much as possible by the Iraqis themselves, under the ownership and leadership of the Iraqi authorities, with the aim of helping to develop sustainable local capacity.

   (c) Implementation and funding modalities will: (i) provide for transparency and accountability; (ii) facilitate efficient and prompt delivery; and (iii) support the progressive development of a unified budget and a coherent public expenditures process.

   (d) A unified donor coordination and funding structure will avoid the emergence of gaps and duplication in funding, inconsistency in policy advice, and will ensure sustained budget expenditure planning.

16. Consistent with the above principles, the Facility provides for joint coordination and monitoring mechanisms. Close coordination would be achieved through a joint Donor Committee and a UN/World Bank Facility Coordination Committee. The Donor Committee would oversee the activities of the Facility as a whole and endorse its overall priorities. The Facility Coordination Committee would serve as the administrative body for the Bank and UNDG to work together to ensure coherence and coordinated planning, monitoring, and reporting between UNDG and Bank activities.
17. By sharing information and coordination, the ITF and the UNDG Iraq Trust Fund will work in close partnership with the Iraqi national authorities in order to ensure that gaps are filled and overlaps avoided and that there is consistency and coherence between Facility-financed activities and overall Iraqi priorities and budget.

**B. Interface Between Iraqi National Authorities and the Facility**

18. Iraqi-led development assistance coordination is carried out by two entities in particular: the Iraqi Strategic Review Board (ISRB) and the Ministry of Planning and Development Cooperation (MoPDC). Their responsibilities are as follows:

(a) The ISRB provides overall policy guidance for donor assistance and will have the final approval authority on recommendations from the MoPDC and Ministry of Finance on allocation of international assistance to Iraq.

(b) The MoPDC is the interlocutor with the donor community and, in that context, will serve as the Interim Iraqi Administration’s primary liaison with the Facility. The MoPDC ensures that resources are applied against Iraq’s prioritized needs and that they are equitably distributed. The MoPDC is expected to work closely with the Ministry of Finance to ensure conformity with the overall budgetary framework. The MoPDC will have an endorsement/refusal role with respect to proposals seeking funding from the Facility (para. 26).

(c) The ISRB and MoPDC, in consultation with the interim ministers and under the guidance of the Governing Council, will define a Priority Program based on the Needs Assessment, and will revise it as necessary in light of changes in the Iraqi budget, resources, and economic circumstances.

(d) The Council for International Coordination (CIC) will be chaired by the MoPDC and will provide advice and support to the Minister of Planning and Development Cooperation on coordination issues. Its current composition may be enlarged to include donors, civil society representatives and other key partners involved in the reconstruction of Iraq. Local aid groups may also be established to assist in sectoral coordination.

19. The diagram below reflects the interface of the Facility with the Iraqi donor coordination structure.
IV. THE WORLD BANK IRAQ TRUST FUND

A. Legal Framework

20. Operational Policy 14.40 (Trust Funds) requires the Bank to administer trust funds under applicable Bank policies and procedures. The Bank's policy on Dealing with De Facto Governments (Operational Policy 7.30) would preclude the Bank from providing grants from the ITF to the Governing Council and/or any of its ministries. This is because, in the current circumstances, not all of the factors to be considered under Operational Policy 7.30 for making new grants exist.³ For the Governing Council and/or its ministries to be considered as recipients

³ The conditions are:
(i) whether the new loan or grant would expose the Bank to additional legal or political risks associated with the country’s financial obligations and obligations to carry out the project;
(ii) whether the government is in effective control of the country and enjoys a reasonable degree of stability and public acceptance;
(iii) whether the government generally recognizes the country’s past international obligations, in particular any past obligations to the Bank;
(iv) the number of countries (particularly neighboring) that have recognized the government or dealt with it as the government of the country; and
(v) the position of other international organizations toward the government.
of ITF resources, a waiver of the application of the provisions of Operational Policy 7.30 is required. In requesting approval for the Bank to administer the ITF, management is seeking the concurrence of the Executive Directors for this waiver.

21. Operational Policy 7.30, among other things, aims to protect the Bank from undue and unusual risks that arise when member countries undergo government changes outside their constitutional framework. De facto situations increase the risk that the government in power may not be able to carry out project activities, and that subsequent governments may repudiate any incurred, stop paying the Bank or discontinue previously agreed activities.

22. In the case of Iraq, these risks are significantly mitigated because financial assistance is provided in the form of grants rather than loans. Also, the grants would be for near-term reconstruction, rehabilitation and development activities that fall within the mandate of the Governing Council and the CPA under Security Council Resolution 1511 and its predecessors. In addition, the explicit call from the Security Council in paragraph 20 of that Resolution to work with the Governing Council further assures the Bank that dealing with the Governing Council in the context of financing reconstruction and development projects in Iraq has the support of the international community.

23. Further, the Bank, as administrator of the ITF, needs to ensure that grant recipients, whether they are the Governing Council, its ministries, or other public or private entities in Iraq, are able to carry out project activities and use ITF funds properly, and that the Bank is able to supervise such activities adequately. Were the Governing Council or one of its ministries to be considered as a recipient under an ITF grant agreement, the Bank would need to be satisfied that it is appropriately empowered to enable it to achieve the objectives of the project for which an ITF grant would be made. This gradual devolution of power is explicitly referred to in paragraph 5 of Resolution 1522 which provides that “the administration of Iraq will be progressively undertaken by the evolving structures of the Iraqi interim administration.”

B. Use of ITF Funds and Eligible Expenditures

24. The ITF would finance eligible operations in all sectors and cross-cutting themes identified in the Needs Assessment (with the exception of mine action), with particular emphasis on areas where the Bank has comparative advantage. The ITF would not finance humanitarian relief, peace-keepers, or other security, military, or political interventions.

25. Recipients of grants from the ITF would need to meet the Bank’s eligibility criteria, including financial viability. Recipient entities responsible for implementing activities financed from the ITF could be inside or outside Iraq, and include Iraqi ministries, governorates and municipalities, private entities, NGOs, UN agencies, or international financial institutions (IFIs). In the case of IFIs, the Bank would serve as the fiscal agent. In such cases, the Bank would not have any responsibility for the use of funds provided to IFIs, and such IFIs would employ their own financial management, procurement, monitoring, and other fiduciary arrangements regarding the use of funds provided to them.
26. As shown in the chart below, potential recipients, in consultation with Bank staff, submit their program/project proposals to MoPDC which vets them to determine whether they are consistent with priority needs and appropriate for channelling to the Facility. The Facility Coordination Committee determines the eligibility of each proposal for funding from the Facility and channels it to either Trust Fund. For proposals that come to the ITF, the Bank proceeds with appraisal and appraisal review meeting. For satisfactorily appraised operations, the Bank, as the ITF Administrator, and the recipient negotiate and sign a grant agreement that spells out the terms and conditions under which funds will be made available to recipient entity. The grant agreement will govern the actual use and disbursement of funds. It will specify measurable indicators to monitor implementation progress. It will also contain detailed financial management, procurement, monitoring, and other fiduciary arrangements to ensure that funds are used for eligible expenditures.

Two categories of expenditures would be eligible for financing under such grant agreements:

(a) **investment and capital expenditures**, including incremental recurrent costs directly related to the supported investment and capital expenditures. This expenditure category would finance capital investments under the agreed Priority Program. Supported activities could be in sector-wide programs, stand-alone investment projects, or umbrella programs of small projects and activities that meet a common development objective;

(b) **technical assistance and training** that would fund programs for Iraq’s public and private sector entities and could also cover training programs to build the capacity of Iraqi organizations and individuals to contribute to reconstruction. This component would cover financing for a Feasibility Fund to enable potential
recipients to employ consultants to help them do analytical work and prepare projects.

C. Donor Contributions to the ITF

28. As a multi-donor trust fund, the ITF will commingle all donor contributions into a common pool. All contributions, and correspondingly all payments out of the ITF, would be on grant basis. The minimum contribution would be US$1 million, reflecting the fact that there are various fixed costs associated with processing and reporting on each contribution and smaller contributions would not be cost-effective. Donor contributions would be held in US dollars. For contributions received in a currency other than US dollars, the Bank would, upon receipt of the funds, convert them into US dollars and transfer them to the Bank’s US dollar-denominated IBRD cash account “T.”

29. A donor may state a preference that its contribution be used to support one or more of the 14 sectors and cross-cutting themes defined under the Needs Assessment with the exception of mine action for which no funds from the ITF may be allocated. In the event that a donor’s preference cannot be accommodated, the Bank may allocate the contribution to other sectors with the agreement of the donor.

30. The ITF Administrator would not guarantee that total spending in the broad sector(s) concerned would match or exceed the level of the contribution for which a sectoral preference had been indicated. Given the large volume of reconstruction needs in each sector in Iraq, over-subscription is not expected. Reports to the Donor Committee would include information on the amount of spending from the ITF on the broad sector(s) concerned.

31. Whenever possible, the Participating UN Organizations and the World Bank, in consultation with the appropriate Iraqi authorities, will promote donor visibility on information, project materials and at project sites.

D. Duration of the ITF

32. Unless otherwise agreed by the donors and the Bank, the ITF arrangement would terminate on the earlier of: (i) December 31, 2007; or (ii) such date as the funds contributed by donors will have been fully disbursed. The proposed duration is deemed appropriate given the magnitude of the political transition issues involved and Iraq’s massive reconstruction needs.

33. Agreements entered into among the Bank, the Monitoring Agent (paras. 49-53), and/or other third parties would not be affected by the termination of the ITF, and the Bank would be entitled to continue permitting withdrawals of funds in respect of such agreements as if the ITF had not been terminated. Any remaining funds, including any applicable investment income, would be returned to the donors on a pro-rata basis, and the Bank’s functions will be considered terminated. Within six months following such termination, the Bank would furnish to the donors an unaudited financial statement with respect to the aggregate amount contributed by all donors.
V. POTENTIAL FINANCING OF ACTIVITIES PROPOSED UNDER THE BANK’S INTERIM STRATEGY FOR IRAQ BY THE WORLD BANK IRAQ TRUST FUND

34. The Interim Strategy Note that is presented to the Board together with the ITF proposal outlines the World Bank Group’s work program for Iraq for the next six to nine months. The Interim Strategy Note focuses on the actions the Bank will take during the current interim period, addressing emergency needs as opportunities arise while undertaking economic and sector work that will set the building blocks for the broad policy issues to be addressed. IDA and IBRD lending to Iraq is predicated on a number of threshold issues: the security situation; the legal issue of Iraq’s government; and settlement of Iraq’s arrears to the Bank. The Bank is operating under the assumption that staff travel to Iraq will be unlikely until the second part of 2004.

35. Within the framework of the Iraqi national budget and the Priority Program, it is proposed that the ITF help finance a portion of the work program (capacity building and emergency operations) identified in the Interim Strategy Note and presented in the box below. During the December 2003 Amman meeting, the Bank discussed the draft strategy and program with the Iraqi Minister of Planning and Development Coordination and received his endorsement for the approved work program. The work program outlined in the Interim Strategy Note is to be discussed in greater detail throughout January 2004 in meetings in Washington, D.C., New York, and Amman.

36. The work program identified in the Interim Strategy Note initiates activities on three tracks, as described below and shown in the box that follows.

(a) **Build Iraqi institutional capacity.** A Multi-Sector Institutional Capacity Building Program would be one of the first activities to be financed by the ITF. The program has two aspects. The first is to build overall institutional capacity to obtain skills and knowledge to undertake the reforms needed for Iraq’s reconstruction and transition to a stable, productive economy. The second is to build a good understanding of the implementation requirements for internationally (and Bank) financed activities; institutionalizing this “know how” in the Iraqi entities; and establishing systems and procedures to ensure transparency and accountability. Specific activities would include:

- Training Iraqi officials in (i) procurement, financial management, monitoring and evaluation, and environmental and social safeguards; and (ii) other aspects of the project cycle (identification, preparation, analysis, appraisal, financing, and implementation);
- Conducting public procurement and financial accountability reviews;
- Providing sector or activity-specific training by the Bank Group or external institutions; and
- Preparing an Operational Manual for project preparation and implementation.
(b) *Prepare and implement emergency operations to address urgent needs.*\(^4\) These operations would aim at meeting Iraq’s current priorities in two areas:
- Generating employment and kick-starting economic activity; and
- Restoring essential infrastructure and services.

(c) *Lay the groundwork for Iraq’s medium-term program.* This component would begin supporting the transition from central planning to a market economy, through policy advice and capacity building for sectoral and structural reforms and analytical work, and by establishing the preparatory work for larger scale development projects.

37. It is expected that these three categories of activities would continue throughout the life of the ITF but at differing intensity; i.e., a heavier emphasis would be placed on capacity building and emergency operations in the initial period (of about two years) with sectoral and structural reforms and larger scale reconstruction projects coming on line more intensively over the second half of the ITF’s life.

### Interim Strategy Work Program

| Capacity Building (to be financed out of the ITF) |  
|-------------------------------------------------|---|
| Multi-Sector Institutional Capacity Building Program | US$5-10 million |

| Emergency Operations to Address Urgent Needs (to be financed out of the ITF) |  
|-----------------------------------------------------------------------------|---|
| Emergency Primary/Secondary Education | 100 |
| Emergency Community-Based Rural Infrastructure | 100 |
| Emergency Infrastructure Reconstruction | 200-400 |

*Project amounts during the interim period are contingent on the availability of ITF resources. If necessary, for example, the Emergency Infrastructure Reconstruction Project could be phased.*

### Analytical and Policy Work to Lay the Groundwork for the Medium-Term Program (to be financed out of the Bank’s budget)

- Poverty and Safety Nets
- Incentive Framework for a Market Economy
- Energy Pricing
- Policy Advice for SOE Restructuring, Investment Climate, and Financial Sector
- TA for Health Policy, Health Finance, and Public Health

### Reviews and Analyses for the Bank to Ensure that Trust Fund Objectives Are Met (to be financed out of the Bank’s budget)

- Procurement and Financial Accountability Reviews
- Core Economic Monitoring
- Social Development Analysis

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\(^4\) The recently approved US$200 million IFC operation–Iraq Small Business Finance Facility–is designed to kick-start economic activity by (i) providing micro and small business lending to revive the private sector and thus job creation; and (ii) building the capacity of participating financial institutions. It is likely to seek financing from the ITF. In restoring essential infrastructure and services, a sectoral programming approach, when appropriate, would be adopted with discrete activities at the subsectoral level that can be expanded as circumstances improve.
VI. **Governance Structure of the Facility and Respective Roles**

38. To ensure coordination between the two trust funds, the arrangements consist of a Facility Coordination Committee and a Donor Committee, both supported by a joint Secretariat.

A. **The Donor Committee**

39. For purposes of efficiency, the Donor Committee will be kept to a manageable size. The Committee will comprise donors whose paid-in contributions or binding commitments to either or both of the Trust Funds amount to a minimum of US$10 million per donor. In addition, two seats would be given to representatives of other contributing donors who do not meet this threshold according to a procedure to be decided upon by the Committee. The Bank, UNDG, IMF, and the Iraqi Strategic Review Board will have observer status. The Donor Committee may be expanded to include other observers.

40. The Donor Committee will be responsible for endorsing overall priorities for and providing strategic guidance to the Facility’s two Trust Funds. The Committee will review progress of the Facility’s operations and ensure reporting to all its donors. The Donor Committee will also ensure coherence and collaboration between the Facility and Iraq’s Priority Program, maintaining close collaboration with Iraqi authorities to ensure flexible adaptation of the Facility to changes in the Priority Program. The Donor Committee will meet on a semi-annual basis in such location as it may decide.

B. **The UN/World Bank Facility Coordination Committee**

41. The UN/World Bank Facility Coordination Committee (the Facility Coordination Committee) will include representatives from the Bank and UNDG. The IMF will have observer status.

42. The primary responsibility of the Facility Coordination Committee will be to review, for purposes of conformity with the Facility’s objectives, make recommendations, and coordinate the overall programs of activities to be financed by both Trust Funds. It will ensure that such programs are coordinated with those funded from the national budget and bilateral donors. When requested to do so, the Facility Coordination Committee will also advise donors on the most appropriate allocation of their resources, based on needs, priorities, and absorptive capacities. The Committee will liaise closely with Iraqi counterparts, on a continuing basis, to ensure coherence of the activities financed with Iraqi priorities. The Bank and the UNDG Trust Funds will each, according to their internal governance structures, have full authority in the allocation of funds within their agreed purpose and the Priority Program.

43. The Facility Coordination Committee will review all reports prepared or passed by the Secretariat on the activities of both Trust Funds in connection with their submission to the Facility’s donors. The Committee will make a formal report and bring recommendations to the Donor Committee at every meeting of the latter.
44. The Committee will meet at least on a monthly basis in Amman during the interim period, and then in Baghdad. On an exceptional basis it may also meet by teleconference, or in such location other than Baghdad as it may decide. Reports and recommendations of the Committee and minutes of its meetings will be prepared by the Secretariat and shared with the Facility’s donors.

C. The Secretariat

45. The Secretariat will be staffed by representatives of the Bank and UNDG and report to the Facility Coordination Committee. In the interim period, the Secretariat will be based in Amman and move to Baghdad when security improves. Its responsibilities will be informational, administrative, and secretarial. Members of the Donor Committee may assign and cover the cost of their national staff to the Secretariat staff (to be decided by the Donor Committee).

46. The Secretariat will answer inquiries from donors. It will handle logistical arrangements for meetings of both the Facility Coordination Committee and the Donor Committee as well as take minutes and distribute them. In addition, the Secretariat will disseminate to all donors in the Facility and to the MoPCD the following:

(i) The reports noted in paras. 63-65 below; and

(ii) Information, recommendations and requests from the Facility Coordination Committee and the MoPDC, the Ministry of Finance, and other Iraqi national authorities as to Iraqi policy, sector programs, and project requirements.

VII. ADMINISTRATION OF THE WORLD BANK IRAQ TRUST FUND

A. ITF Administrator

47. The Bank, as the ITF Administrator, and the UNDP, as the UNDG Trust Fund Administrator, will each be responsible for establishing and maintaining appropriate records and accounts to identify the contributions to their respective trust funds, the commitments to be financed out of the contributions, and the receipt and disbursement of funds. The Bank and UNDP will use a standardized format in drafting their reports, on the activities financed by their respective trust funds, and these will be consolidated into one report. The Secretariat to the Facility will disseminate the consolidated reports to the members of the Donor Committee and the Facility Coordination Committee to ensure transparency, thereby contributing to closer coordination at all levels.

48. The ITF Administrator would have the authority to deny ITF funding to any activity where in its view significant doubts arise as to whether the funds concerned will be effectively utilized for the agreed purpose. The ITF Administrator would regularly monitor the utilization of funds and supervise the work of the Monitoring Agent.
B. Monitoring Agent

49. Iraqi ministries have not worked with the Bank for three decades. Individual and institutional capacity needs strengthening. The Bank is not present in the country, and even when the Baghdad office reopens, it will operate with a skeleton staff for the immediate future. In order to ensure that contribution funds are disbursed only for the purposes of ITF and according to applicable Bank procedures, the Bank, as Administrator of the ITF, would engage a suitably qualified and experienced independent firm (the Monitoring Agent) to monitor expenditures related to the activities financed from the ITF.

50. The Monitoring Agent would report to the Bank and be responsible for: (i) pre-screening and supporting the Bank in monitoring the procurement of goods, services, and other items; (ii) pre-screening and recommending withdrawal applications for the Bank’s approval and payment; (iii) supporting the Bank in monitoring all expenditures financed from the ITF; and (iv) pre-screening the financial management capacity of potential grant recipients.

51. The Monitoring Agent would be selected and retained by the Bank on the basis of terms of reference/scope of work agreed by the Facility Coordination Committee and the Bank. The selection and recruitment of the Monitoring Agent by the Bank, and the procurement of goods and services to be used by the Monitoring Agent in the performance of its obligations, will take place on an untied basis and in accordance with the Bank’s applicable policies.

52. The Bank would have the authority to change the terms of reference/scope of work of the Monitoring Agent and, where justified, to replace the Monitoring Agent with another firm or agency. The contract of the Monitoring Agent would also provide for scaling down or phasing out the services as and when conditions in Iraq allow it. The Bank would inform the MoPDC, the Facility Coordination Committee, and the donors of changes in the terms of reference/scope of work of the Monitoring Agent. The Bank would perform ex-post evaluations of the activities undertaken by the Monitoring Agent, and would, upon completion of the activities financed under the ITF, arrange for an independent review of the performance of the Monitoring Agent and report its findings to the donors.

53. Funds from the ITF would be used by the Bank to: (i) pay the reasonable fees, travel, and other reimbursable costs of the Monitoring Agent; and (ii) pay the cost of goods, services, and other items of expenditure in furtherance of ITF’s activities.

C. Supervision

54. The Bank, as the ITF Administrator, will supervise ITF-funded operations in accordance with the Bank’s applicable policies and procedures. While staff travel to Iraq is restricted, supervision of recipient-executed operations, including NGOs, will be carried out through consultants and the Monitoring Agent. Each ITF-funded operation will include a results-based supervision plan that reflects realities on the ground (para. 61). Responsibility for supervision of ITF-funded operations that are being executed by other IFIs and UN agencies will remain with those agencies.
D. Terms and Conditions of Grants Made out of the ITF

55. Terms and conditions pursuant to which funds will be made available to the recipient entities that will be set out in grant agreements will include, without limitation, requirements related to procurement, environmental and social safeguards, financial management, reporting, and monitoring.

56. **Procurement.** In the interest of expeditious assistance, procurement provisions would be as flexible as possible with due consideration for economy and efficiency while still maintaining safeguard measures to ensure that funds are used only for the purposes specified in the respective grant agreements. The procurement of goods, works, and services would be made in accordance with the “Guidelines for Procurement under IBRD Loans and IDA Credits” and “Guidelines for the Selection and Employment of Consultants by World Bank Borrowers,” as may be amended from time to time.

57. **Disbursements.** Disbursements for activities to be financed from the ITF will be made in accordance with the appropriate policies and procedures of the Bank.

58. Disbursements related to recipient-executed ITF grants will be made using the most appropriate Bank mechanisms, taking into consideration the nature of the projects and the related risks. Such disbursement mechanisms may include making direct payments to suppliers or contractors, providing Special Commitments to support letters of credit, reimbursement of expenditures made from the recipient’s own funds, or by making Special Account advances to enable expenditures to be paid by the recipients. In accordance with Bank procedures, the recipient will need to provide documentation to support the expenditures. The Monitoring Agent would pre-screen all withdrawal applications before sending them to the Bank.

59. Financial Monitoring Reports (FMRs) would be produced on a quarterly basis, starting the second quarter after the project becomes effective.

60. **Environmental and Social Safeguards.** The investment activities financed from the World Bank Iraq Trust Fund would be carried out in accordance with environmental and social screening and assessment guidelines as called for under Operations Policy 8.50.

61. **Monitoring and Evaluation.** The ITF Administrator and the UNDG Trust Fund Administrator would provide the Facility Donor Committee and the MoPDC a consolidated report which would describe the progress under each of the two Trust Funds over the previous six-month period. The ITF report would include, inter alia, progress towards reaching project objectives and the ITF’s development impact as defined in the supervision plan (paras. 54 and 64).

62. **Financial Covenants.** As required under regular Bank lending operations, a grant agreement with a recipient would obligate the recipient, among other things, to maintain an appropriate and adequate financial management system, including records and accounts, and prepare financial statements adequate to separately reflect the operations, resources, and expenditures related to the activity financed under the grant from the ITF. The grant agreement
would obligate the recipient to have the accounts, records, and financial statements of the grant to be audited for each fiscal year by a qualified auditor acceptable to the ITF Administrator in acceptable scope and standards. The audit report along with the related financial statements would be submitted to the ITF Administrator not later than six months after the end of each fiscal year. A grant recipient would be obligated to retain until at least one year after submitting the last audit report all records and supporting documents for grant expenditures. Upon request of a donor, a copy of the audit report and financial statements would be provided.

63. **Reporting.** The Bank shall maintain separate records and ledger accounts in respect of the funds deposited by the donors with the Bank under the ITF. Within ninety (90) days of each March 31, June 30, September 30, and December 31, the Bank will prepare, on a cash basis, an unaudited statement of receipts, disbursements, and fund balance with respect to the ITF and forward a copy to each donor. Each such statement will be expressed in United States dollars, the currency in which the ITF funds shall be maintained by the Bank. In addition, within one hundred and eighty (180) days of the completion of all disbursements relating to activities financed from the ITF, the Bank will prepare on a cash basis an unaudited financial statement of receipts, disbursements, and fund balance with respect to the ITF and forward a copy to each donor.

64. The Bank will furnish the donors:

   (a) on a semi-annual basis, a consolidated report describing the operations of the ITF (including contributions, disbursements, and implementation progress) in the preceding six months (paras. 54 and 61); and

   (b) on an annual basis, a management assertion, together with an attestation from the Bank’s external auditors, concerning the adequacy of internal control over cash-based financial reporting for trust funds as a whole.

65. The Bank will cause a financial statement audit of the ITF to be performed by the Bank’s external auditors on an annual basis. The costs of such an audit, including the internal costs of the Bank with respect to such an audit, shall be charged to the ITF. The Bank shall provide each donor with a copy of the auditors’ report.

66. The Bank, as Administrator of the ITF, will maintain close consultation and coordination with the donors. The Bank will provide each donor to the ITF with semi-annual reports on its quarterly ex-post evaluation of the activities undertaken by the Monitoring Agent. Within six months of completion of the activities, or of full disbursement of the contributions, whichever comes later, the Bank will provide a final progress report to each donor, together with a copy of the independent review of the performance of the Monitoring Agent. Upon request by any donor, the Bank will send to such donor the draft and final reports received by the Bank from the Monitoring Agent on the activities financed by the contributions.
E. The Bank’s Cost Recovery

67. The Bank’s cost recovery would be determined on a yearly basis and will consist of two components. On a semi-annual basis, the Bank would notify the Donor Committee of the amounts used for such purposes:

(i) The Bank’s administrative fee would be 0.4% for technical assistance projects and 0.2% for investment and for cofinanced operations. The fee would be deducted from contributions to the ITF at the time they are allocated for such activities. The Bank will invest contribution funds pending their disbursement in accordance with the Bank’s policies and procedures for the investment of trust funds administered by the Bank. Investment income earned on the contribution funds would be deposited into the account to be used for purposes of the ITF.

(ii) In addition to the above administrative fee, the Bank would also charge actual full costs of its support to the following to the ITF:

(a) ITF Management Team (manager, financial specialist, other expertise specifically related to the management of the ITF, and administrative assistant);
(b) The Monitoring Agent: the cost of the Bank’s contract and the cost of independent review of the Monitoring Agent’s performance;
(c) The Bank’s contribution to the joint Secretariat of the Facility (the UNDG and the Bank will share costs 50:50); and
(d) Bank staff and consultants involved in activities (analysis, appraisal, supervision, and other project-specific activities) undertaken solely to carry out the Bank’s responsibilities under the ITF.

VIII. Benefits and Risks

A. Benefits

68. The proposed Facility, by bringing together donors to finance a coherent program of priority expenditures within a unified budget, would help avoid the dangers often seen in post-conflict situations: politicization of program support, duplication of donor effort, and overburdening of country officials by donor missions and information requests. The Facility would promote a coordinated approach to Iraqi reconstruction. The criterion that proposed reconstruction activities be within the Priority Program would help avoid fragmentation of the national budget; rather it would help align it with the Priority Program. The Facility, through the oversight of the Donor Committee and regular reporting, would promote transparency and accountability of reconstruction assistance.

69. The pledges at the Madrid Conference demonstrated that there is strong international support for helping to bring Iraq to economic recovery, macroeconomic and fiscal stability, and attainment of the MDGs. The Facility, which is likely to be the largest post-conflict multi-donor
trust fund, would provide the critical mass in financing to generate economies of scale. In addition, the Facility would provide an innovative structure by bringing together the UN and the ITF under one roof, so their distinct comparative advantages can be closely coordinated to enhance the effectiveness and efficiency of the reconstruction effort.

B. Risks

70. As in any post-conflict country, the current situation in Iraq poses risks for operations. First, security will be a key consideration in implementing projects and in protecting the assets created by ITF financing (para. 74). Continued security threats could, in turn, cause erosion of donor commitment and the channeling of their funds elsewhere. Continuous consultation and information sharing with the different stakeholders will be essential in order to avoid the potential disengagement of international partners. Until staff are able to travel to Iraq, the Bank will need to rely heavily on Iraqi consultants; the Office in Amman and other field offices in the region; videoconferencing facilities; and especially the continued presence and engagement of the Monitoring Agent with ongoing projects.

71. Second, establishment of economic and fiscal stability and full restoration of public services could be difficult in view of the challenging political transition Iraq faces. The success of ITF activities is inextricably intertwined with the success of the political process. Reconstruction assistance will need to support the political process and respond to the legitimate demand of the Iraqi people for quick results on the ground while building the institutional and human capacity for economic recovery and sustainable growth and poverty reduction. Also, ITF administration will need to be flexible enough to manage contingencies and deal with potential setbacks such as delays in decision-making by the Iraqi authorities and conflicting demands at different levels of government and within civil society.

72. A third set of risks revolve around the fiduciary aspects of project implementation. The Bank and the Iraqi recipients will need to learn and understand each other’s procedures and way of doing business. In the case of the Bank, it will then assess the risks and identify ways to manage the risks. All this will require an intensive and rapid effort on the part of the Bank. There is a mitigating factor, however. In contrast to many post-conflict countries, Iraq had a legal and procedural framework for procurement and financial management. There are many similarities, for instance, between Jordanian and Iraqi public procurement and institutional arrangements. Furthermore, personnel in Iraqi ministries and the private sector have capacity that can be strengthened with training and on-the-job mentoring.

73. From the onset, our goal will be to structure our capacity building programs, so that the Iraqi Government (provisional, transitional or permanent) can rapidly become fully in charge of fiduciary aspects of projects. We are organizing training programs, using the ILO Center in Turin and other centers. During the discussions in Amman in early 2004, the Iraq team will work with Iraqi counterparts to detail a preliminary training program that will range from an initial one-week training seminar covering procurement, financial management, and disbursement to 3-4 week-long training programs on the complete project cycle. The training to be conducted in Arabic will combine classroom instruction with case studies, hands-on practice exercises, and tutorials. In addition, at least, in the beginning, we would expect certain
procurement or financial management to exceed the emerging capacity level of Government; In those cases, we would advise Government to retain the services of procurement agents or financial management specialists on a competitive, international basis, in order to provide short-term technical assistance and also transfer of know-how.

74. A fourth risk relates to implementation delays and disbursement lags resulting from weak capacity. Bank experience in other post-conflict countries shows that constraints in reconstruction are often due not to lack of funds, but rather to difficulties in developing and implementing time-bound investment programs. The planned capacity building training on the design and implementation of projects is expected to mitigate this risk. Also, in assessing proposals for ITF funding, consideration will be given to those operations that are simple, relatively easy to implement, and have strong Iraqi ownership.