Republic of Iraq
Decentralization and subnational service delivery in Iraq: status and way forward

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MIDDLE EAST AND NORTH AFRICA

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CURRENCY AND EQUIVALENT UNITS  
(Exchange Rate Effective as of 29 March, 2016)

US$ 1 = 1176 Iraqi Dinars  
1 Iraqi Dinar = .00085 US$

FISCAL YEAR

January 1 – December 31

ABBREVIATIONS AND ACRONYMS

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<tr>
<th>Abbreviation</th>
<th>Full Form</th>
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<tr>
<td>ARDP</td>
<td>Accelerated Regional Development Program</td>
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<tr>
<td>COR</td>
<td>Council of Representatives</td>
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<td>CPA</td>
<td>Coalition Provisional Authority</td>
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<td>CSC</td>
<td>Civil Service Commission</td>
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<td>FBSA</td>
<td>Federal Board of Supreme Audit</td>
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<td>GFS</td>
<td>Government Financial Statistics</td>
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<td>HR</td>
<td>Human Resources</td>
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<td>HRMIS</td>
<td>Human Resources Management Information System</td>
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<td>IFMIS</td>
<td>Integrated Financial Management Information System</td>
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<td>IGO</td>
<td>Inspector General Office</td>
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<td>ISIL</td>
<td>Islamic State of Iraq and the Levant</td>
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<td>IT</td>
<td>Information Technology</td>
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<td>KRG</td>
<td>Kurdistan Regional Government</td>
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<td>PFM</td>
<td>Public Financial Management</td>
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<td>PDP</td>
<td>Provincial Development Plan</td>
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<td>PR</td>
<td>Public Relations</td>
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<td>SOE</td>
<td>State-Owned Enterprise</td>
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<td>TAL</td>
<td>Transitional Administrative Law</td>
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<td>TB</td>
<td>Trail Balance</td>
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<td>TSA</td>
<td>Treasury Single Account</td>
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<td>USAID</td>
<td>United States Agency for International Development</td>
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Vice President: Hafez Ghanem  
Country Director: Ferid Belhaj  
Practice Manager: Hisham Waly  
Country Manager: Robert Bou Jaoude  
Team Leader: Rama Krishnan Venkateswaran
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EXECUTIVE SUMMARY: FINDINGS AND SYNTHESIS

Status of Decentralization: Political, Institutional and Fiscal Aspects

1. This assessment provides a snapshot of the current status of the decentralization process. It identifies policy and process reform measures that are necessary to strengthen service delivery by the 15 Governorates of Iraq. The assessment builds on the analytical and advisory reports previously prepared by the Bank (World Bank 2010) and others. It is intended to inform the World Bank country management on the steps required for the Iraqi government to maintain the momentum of the ongoing decentralization process. The assessment excludes the Kurdistan Regional Government (KRG), and is confined to the remaining fifteen Governorates.

2. This report examines decentralization through the lens of service delivery by the Governorates. Though decentralization is a multi-dimensional issue and can be assessed from several angles, this report aims to assess the current status of decentralization in Iraq from the point of view of the relevance and impact of decentralization in improving the delivery of services at the Governorate level. As such, it does not delve into the broader issues relating to decentralization in Iraq (for example on political decentralization) except to the extent that it impacts on service delivery systems. For the long term, it is important to acquire an in-depth understanding of the political economy of decentralization, as well as the impact of the macroeconomic situation on decentralization as these could be potential risk factors for the sustainability of decentralization in Iraq.

3. Iraq has achieved a significant level of political decentralization comprised of a partial federal and partial unitary state. The 2005 Constitution provides for a federal structure with respect to regional government(s) and a unitary structure with respect to the governorates. To date, no governorates that are not organized in a region have chosen to form a region. Authorities of regions are not subject to federal statutory changes; governorate authorities are determined by federal legislation. For governorates, the Constitution characterizes the governance structure as administrative decentralization.

4. The first major step toward a decentralized state predates the Constitution — with the election of governorate councils in 2005. Popular and open elections of governorate officials have given governorates a political presence and popular legitimacy. Councils elected in 2005 subsequently formed an association, and acted collectively to draft the major statute defining the roles, responsibilities and authorities of governorates through Law 21 (2008), namely, the Law on Governorates not Incorporated in a Region. Successive elections, each more openly organized and with high voter turnout, were held in 2009 and 2013. The popular election of governorate officials has also created the expectation among citizens that governorates are the primary authorities responsible for improving service delivery.
5. Historically, responsibility for basic service delivery has been lodged almost exclusively in central government ministries, but that arrangement is changing. Until recently, the only significant service delivery responsibility held by the Governorates has been the authority to prepare provincial development plans, as well as to design and implement capital projects to improve service delivery conditions. In 2006, elected governorate officials took the initiative to develop provincial strategies, prepare project plans, and implement investment projects prior to official recognition of such authority (in Law 21). Governorates now have had ten years of experience preparing strategies, designing projects, and implementing them. However, the impact of these development projects on improving the quality and quantity of basic services has been quite limited. Relative to capital funding for federal ministries, Governorates have had access to very limited investment funds.

6. The Second Amendment to the Law on Governorates not Incorporated in a Region (Law 19, 2013) provides for the devolution of “sub-directorates, departments, tasks and competencies of parts of eight federal ministries.” Devolution was supposed to have been carried out over a two-year period, to be completed by August 2015. A strong push by the new Prime Minister throughout 2015 has moved devolution forward with at least some of the affected Ministries, and the Governorates are now preparing plans to determine which functions will be devolved, and which functions will remain with the federal ministries. Generally, functions involving more than one Governorate and broad strategic planning remain at the federal level. Day-to-day service provision and investment programs contained within individual Governorates are being devolved. The Ministry of Housing, Municipalities and Public Works is the most advanced in this process, though no formal transfer of staff, facilities and budgets have taken place as of late 2015.

7. The progress achieved in the realm of political decentralization needs to be matched with institutional and fiscal decentralization. The periodic, successful election of Governorate officials provides a solid base for electoral and other political mechanisms for citizens to hold Governorate officials accountable for performance in service delivery, as well as for other functions normally demanded/expected by the citizenry. However, the following facts must be taken into consideration:
   - To date, elections are only for Governorate councils, and have not yet been implemented at the district and sub-district levels;
   - Formal mechanisms and structures are lacking for more localized demands for services and other concerns;
   - The devolution of significant functions will increase the pressures on governorate officials to improve service delivery, and eliminate the possibility of placing blame on the lack of authority over services. That will be more directly apparent where the quality and quantity of services vary significantly by district.

8. While legislative actions and more recent pressure from the Prime Minister have forced action on devolution of some service delivery functions, there has been limited attention to the

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1 These include the Ministries of Housing and Reconstruction, Municipalities and Public Works, Health, Education, Labor and Social Welfare, Sports and Youth, and Agriculture and Finance. With respect to the Ministry of Finance, devolution has meant only the creation of Finance Departments in the Governorates, and not a devolution of the Ministry of Finance authorities.
institutional and fiscal decisions required to achieve successful devolution, as well as to the capacity of the Governorates to absorb and manage staff, resources, and responsibilities many times greater than they currently possess.

- Human resources capacity for hiring, performance appraisals, and salary administration is limited and is not adequate for the thousands of devolved employees, as compared to the current staff size;
- Managerial expertise to oversee technical service delivery functions is very weak in the Governorates. It is unclear if management and supervisory personnel will be among the staff devolved;
- Although the Governorates have experience in developing provincial strategies, investment plans and projects, devolution will require planning and investment budget planning for entire service delivery functions, not just individual projects;
- Governorate experience in current or routine budget preparation and oversight for technical services delivery, including operation and maintenance requirements, is virtually non-existent.
- Financial management systems in the Governorates, primarily paper and spreadsheet based, are reasonably adequate to their current service delivery responsibilities. However, they are not up to the task of tracking and reporting on significantly increased expenditures for devolved services.

9. **If successfully carried out, a significant degree of institutional reassignment of service delivery functions to the Governorates will have been achieved. However, little attention has been given to fiscal decentralization.** To date, Governorates have had very weak budgetary authority. Authority over budget preparation and execution has been limited to the expenditures of the elected council, the Governor’s office and staff, as well as for the investment projects prepared by the Governorate and funded through a federal budget line. The 2013 amendments to Law 21 allocated a fixed $/barrel (or $/m³ for natural gas) for oil and gas produced or refined in the Governorate. The proposed 2015 amendments, not yet enacted in the Council of Representatives (CoR), change the per barrel of oil produced, per barrel of oil refined tax and per 150 cubic meter of gas produced tax to 5 percent (of the market selling price) and exclude double counting of extraction and refining. The 2013 allocations were never fully implemented. In addition, there seems to be a partial substitution of some of the oil and gas revenue allocations for some federal funds that otherwise would go to the Governorates receiving the oil and gas allocations. Furthermore, on the revenue side, budget shortfalls are likely to continue in the face of persistent low international oil and gas prices, escalating demands for increased defense spending as the government proceeds with reclaiming territory occupied by Islamic State of Iraq and the Levant (ISIL), consolidating the rule of law, and addressing urgent infrastructure and social protection issues in conflict areas.

10. **Although the devolution of service delivery functions is a major step in fiscal decentralization, neither discretionary controls over expenditures nor revenues is an apparent feature of the devolution process in Iraq.**
• If the discretion to make changes across and within devolved functions is not authorized, then only the authority to *administer, not to manage* centrally-determined service delivery quality and quantity levels has been devolved. It will be another form of administrative decentralization.

• If revenues previously associated with devolved functions transfer to the governorate level, but are still allocated in detail at the central level, the Governorates will not be able to change or manage priorities more appropriately to meet citizen demands and needs;

• No steps or policies have been taken to authorize Governorates to raise revenue through various taxes, fees, charges already authorized — *without* incurring a reduction in federal budget allocations;

• Recurrent budgetary allocations for serving local populations are driven by ministerial priorities and are negotiated as a component of the annual budget process. Transfers for investment spending are driven by specific project approval.

• There are no systematically designed vertical or horizontal equalizing transfers, and no service or project transfers intended to efficiently alter prices or create proper economic incentives.

• Iraq has not yet developed a framework and process for intergovernmental transfers that will allow for the Governorates to make discretionary choices about the quality and quantity of services in keeping with citizens’ preferences, as well as to develop own-source revenues without being penalized with reductions in federal budget allocations or transfers.

11. Revenue authority shows a pattern which is even more concentrated within the Central Government than is service delivery authority. For example, per capita Governorate revenues collected in Babel, Basra and Najaf equal less than one 10th of a percent of total per capita government revenue across the nation. For 2014 in Babel, it was less than one hundredth of a percent. From a national perspective, Governorate own-source revenue is inconsequential. However, if Governorates are provided authority over the revenues derived from self-funding services (user charges, fees and so forth based on services delivered) of the devolved functions of the ministries, this subnational revenue profile will change significantly.

12. Although a significant portion of the national budget is spent in the Governorates, a major portion of such spending is actually controlled by the Central Government. Governorates submit their proposed project investments for approval by the Ministry of Planning and funding through the Ministry of Finance in a line within the federal budget. This is generally referred to as the Accelerated Regional Development Program (ARDP). Funding levels for the regional development program initially were relatively high. For example, from 2006–2009, the Governorates and the KRG together were allocated 35 to 45 percent of the total federal investment budget to implement projects selected and developed within the Governorates (and the KRG). When federal budget shortfalls occur, ministry investment budgets are more protected at the expense of allocations to Governorate investments. In the 2016 federal budget, the regional development allocation to the KRG and the Governorates will amount to only 6 percent of all federal investment expenditures.
13. **Provincial investment planning, budgeting and execution offers an opportunity to focus attention on the potential to realize the benefits of devolution of significant service provision responsibility from the eight federal ministries.** The devolution of important services delivery functions has the potential to improve local service delivery, but it is tied closely to investments in deteriorated and insufficient infrastructure. The Provincial Development Plan (PDP) provides a good instrument for Governorates to address local development aspirations, and for the Central Government to reinforce efficient and accountable local service delivery.

14. **The decentralization model in Iraq is evolving.** Considering the diversity of the country, a monolithic approach is not likely to produce the intended outcomes. Asymmetric solutions are likely necessary at the Central and Governorate levels to adapt to differing regional capacities and social, cultural, economic and security environments. In all likelihood, the necessary structure for effective decentralization in Iraq will not be encompassed by as single decentralization model, it will likely require the development of separate sub-models which provided increased autonomy and discretion in a manner consistent with capacity. Though the current model of decentralization is focused around Governorates, it could also be useful to explore the feasibility of devolving to the local government level at the district/municipal levels as they are more directly involved in delivery of local services. While this could be a challenge in the short term due to weak institutional structures and capacities at the local level, in the medium term the Government could define clearly the roles and responsibilities of districts/municipalities vis-à-vis Governorates as well as empower the institutional structures at the district/municipal level as a third tier of the State responsible for service delivery.

**Recommendations**

15. **Decentralization in Iraq requires a strategic approach in order to move forward.** Decentralization in Iraq has moved forward in an ad hoc and fragmented fashion in the past. It now requires a clear strategic direction to enable the government to translate the broad national vision, as articulated in the Constitution, into tangible development results on the ground. Although decentralization has gathered some momentum in the past few months, there is the risk of losing this window of opportunity unless the government can seize this momentum and lay out a clear vision on the way forward. Organizing the decentralization reform process around the core objective of enhancing the Governorates ability to deliver services in an efficient and accountable manner will move the ongoing reform process forward and help the government to better connect with and meet the development demands of citizens.

16. **Strengthening local accountability should be the key to strengthening the service delivery performance of the Governorates.** International experience has shown that strengthening accountability is critical to improving service delivery as it strengthens the social contract between the citizens and the State. Specifically, improving service delivery performance requires the strengthening of accountability relationships between the state and service providers, citizens and the state, as well as between citizens and service providers. Translating this model into the Iraqi context requires the building and strengthening of three key accountability relationships that are currently weak. These accountability relationships, that is, between the citizens and the Provincial
Government, between the Provincial Government and the Central Government, and between the Central Government to Provincial Governments and the citizens) have a critical impact on service delivery. Therefore, strengthening service delivery at the governorate level through the government’s decentralization program would require specific operational steps to redefine and strengthen these accountability relationships.

17. Reforming and strengthening the preparation of the Provincial Development Plans offers a unique opportunity to enhance local accountability and potentially improve service delivery. The investment budget for the PDPs is the only budget over which the provincial Governor and the Provincial Council have discretionary authority with regard to the selection of projects for budgetary funding. Putting in place a robust model of consultation between the Governorates and the citizenry during the preparation of the PDPs will ensure that the PDPs reflect local development priorities in a realistic manner. Providing transparent and predictable financing for PDPs, as well as providing the flexibility to Governorates to use the financing provided in a discretionary manner without being constrained by centrally-determined priorities, will enable the Governorates to respond to local service delivery and development requirements in a timely and effective manner.

18. Putting in place a transparent and predictable flow of resources to the Governorates will strengthen fiscal decentralization. The present structure is an overly centralized model of resource allocation and transfer. Budget allocations to Governorates are dependent upon the Ministry of Finance and negotiation. In addition, there is little discretionary revenue at the provincial level. Recurrent budgetary allocations serving local populations are driven by ministerial priorities and are negotiated as a component of the annual budget process. A transparent structure for transferring budgetary resources to the Governorates as part of a reformed intergovernmental fiscal system is needed and will help ensure that resources are delivered as budgeted. The intergovernmental system cannot be managed on an ad hoc or negotiated basis. Rather, it must be based on understandable, stable and mutually-agreed upon fiscal rules. The system must be continuously reevaluated, but its resource elements should be sufficiently stable within overall macro-fiscal constraints to allow for the appropriate economic incentive for efficiency, effectiveness and self-sufficiency to take effect.

19. An annual capital grant is needed to provide resources to the Governorates on a predictable and transparent basis and to finance Provincial Development Plans. This grant pool should be funded at a level of real resources and should be allocated to each Governorate based on a formula to be determined by the government (based on factors such as population, land area, need, and fiscal capacity). Furthermore, this formula should remain fixed and stable. The pool should be structured to grow on an annual basis each year by a fixed percentage amount until it reaches an agreed portion of the total Central Government investment spending for the previous year. At that point, the share of natural resource taxes to the pool will be fixed, and the Governorates will receive annual distributions from this fixed proportionate pool on a formula basis.

20. The institutional foundations for decentralization need to be strengthened through a combination of short- and medium-term actions. As Governorates increasingly take on more service delivery responsibilities, the capacity of the Governorates to manage their new responsibilities efficiently will be a critical factor that will determine the future course of decentralization. Along
with transferring the responsibilities, staff and provision of financing, the capacities of the Governorate to manage the service delivery function need to be built up. Global experience has shown that rather than providing training and capacity building efforts in isolation and/or in a piecemeal manner, adopting a “learning by doing” approach where capacity support is provided in an integrated manner with financing and institutional development support to achieve mandated responsibilities provides better results in the public sector. Enabling the Governorates to implement the Provincial Development Plans through the provision of targeted capacity support can result in building institutional capacities of Governorates in a sustainable way. Therefore, the Central Government and international development agencies should align their capacity support initiatives in the Governorates with a view to enabling them to fulfill their service delivery responsibilities.

21. **Efficient systems for expenditure management for the Governorates need to be put into place to strengthen local service delivery.** The management of governmental financial systems at the central government and the public financial management (PFM) systems at the Governorates should be reviewed and reformed as needed at each stage of the budget cycle. This includes planning and budgeting, budget implementation, budget monitoring reporting, and audit and evaluation. The chart of accounts and budget classification across central and subnational government administrations should be reviewed and unified. In addition, the economic budget classifications and the revenue classifications used by the Central Government and the Governorates must be aligned. Measures to establish, develop, and improve treasury operations are needed to better meet fiscal targets, support program service delivery, and gather better information for control and analysis. Finally, establishing full expenditure authority over Governorate-assigned functions — including establishing priorities, programming the mix of production resources, controlling staffing and personnel decisions, eliminating perverse incentives associated with lapsing, and reduced budget allocations associated with attempts to economize — will help efficient expenditure management at the governorate level.

22. **Enabling effective local revenue mobilization will enhance local accountability and financial sustainability.** Governorates are generally not able to alter the yield of revenue instruments as they must be centrally approved and are centrally assigned by the Ministry of Finance. The legal framework for the definition of local revenue sources needs to be clearly defined. The administrative capacities of the Governorates also need to be strengthened to provide for the efficient and effective collection of local revenues.

23. **A coordinated and sequenced approach to decentralization is necessary in order to move forward.** Communication and coordination between various stakeholders is important in ensuring smooth, forward progress toward decentralization. To consolidate the gains made in the decentralization reform process so far and to enable a smooth progression forward, it is necessary for the government to lay out a set of steps to operationalize the devolution of powers and functions for the eight ministries enacted through Law 19 (2013). Following the direction of the Cabinet and the High Commission for Coordination among Regions, some ministries (such as the Ministry of Housing and Municipalities and Public Works) have started taking steps to transfer specific powers, functions, and resources to the Governorates. However, concerted action is required from other devolved ministries as well as other key ministries, such as Ministry of Finance and Ministry of Planning, to put in place the operational rules for implementing the provisions of Law 19 (2013). A
well-defined sequence of operating steps that will coordinate the roles of the various ministries/agencies at the central and governorate levels is necessary to ensure a smooth implementation of the decentralization process.

24. **A strengthened High Commission for Coordination among Regions and Governorates ("High Commission") should oversee and coordinate the implementation process for decentralization.** The various stakeholders need to have a shared vision of decentralization borne by a common understanding of the decentralization process. This requires an extensive communication campaign by the government or an appropriate agency, such as the High Commission. In addition, the various ministries/agencies of the Central Government and the Governorates require technical advice and support to enable them to address the various operational issues relating to transitioning through the process. The capacities of the High Commission need to be strengthened to address and carry out these critical responsibilities. Building upon the brief summary of international experiences included in this report, development Partners including the World Bank could support the Government of Iraq and its institutions to benefit from the knowledge and experience of other countries who have gone through similar circumstances by setting up knowledge and experience sharing programs.
1. OVERVIEW OF DECENTRALIZATION IN IRAQ

1.1 Introduction

1.1 Decentralization in Iraq is at a crossroads. Since the Constitution (2005) provided for decentralizing powers and functions for the Governorates, the government of Iraq has enacted several legal, policy and institutional reform initiatives, the intent of which is to shift political and administrative powers and responsibilities from the Central Government to the Governorates. Although this shift from a highly centralized state to a more decentralized political and administrative system has been occurring at an uneven pace, the momentum for the transition gained speed in 2013. Decentralization developed more quickly with the enactment of the Law 19 (2013). It identified eight sector ministries some of whose functions and responsibilities were expected to be transferred to the Governorates. In addition, it included the declaration of a two-year time period for implementing decentralization.

1.2 The legal and policy framework for decentralization is yet to be followed through with efficient implementation. The new Government of Prime Minister Haider Al-Abadi that took office in 2014 clearly identified decentralization as a core policy priority. Despite this, the implementation of decentralization has not progressed smoothly. Governorates are still not able to respond to citizen demands and delivery of service requirements in an efficient and effective manner. Demands by the citizenry for improved service delivery by the Governorates are becoming louder and more persistent. Therefore, both the Central and Subnational Governments are keen to operationalize the decentralization policy framework with the objective of improving service delivery by the Governorates.

1.3 The Government of Iraq and the World Bank would like to assess the current status of decentralization and its implications for improving service delivery at the Governorate level. Based on discussions between the Country Management Unit of the World Bank and the Government of Iraq, the Bank decided to undertake a rapid assessment of the current status of the decentralization process in Iraq. The findings of the assessment will be used to inform preparation of the Country Partnership Framework between the Government of Iraq and the World Bank, as well as the design of Bank-financed investment operations in Iraq, and the country dialogue more generally.
1.2 Rapid Assessment of Decentralization and Subnational Service Delivery in Iraq

1.4 **Objective:** The objective of the assessment is to take stock of the current state of decentralization in Iraq with a view to identifying factors that contribute to weak service delivery performance at the governorate level. The assessment will also make recommendations for policy and process reforms that are deemed necessary to moving forward the decentralization process, thereby helping to improve service delivery performance by the Governorates. The assessment builds upon the World Bank’s previous analytical reports (World Bank, 2010, 2014b) about Iraq and as such, it does not attempt a comprehensive assessment of decentralization in Iraq. Instead, the report focuses on service delivery at the governorate level and identifies those aspects/issues of the decentralization framework that can contribute to the improvement of service delivery performance at that level.

1.5 **Scope:** The scope of the assessment is confined to the fifteen Governorates not constituted as Regions. Therefore, it does not include the Governorates of the Kurdistan Regional Government (KRG). Due to the rapid nature of this assessment, the aim is to provide recommendations that could possibly be implemented in the short to medium term. Therefore, it does not provide any long-term policy reforms that will require in-depth analysis and extensive consultations with stakeholders. At the same time, the report also includes supplementary notes (included in the annexes) on two specific areas, specifically: (1) international experiences in the sharing of resource revenues; and (2) international experiences in fiscal decentralization. Both of these supplementary notes have been prepared based on specific client demand, and are expected to inform the longer-term policy dialogue relating to fiscal decentralization in Iraq.

1.6 **Methodology:** The assessment was carried out through a combination of desk reviews and field-level consultations. Based on an initial survey of existing analytical work relating to decentralization in Iraq, the World Bank task team identified a list of issues for field-level research. The Bank team carried out a one-week mission in Baghdad (November 1-7, 2015) during which discussions were held with a cross section of stakeholders that included Central Government Ministries, Provincial Governorates, the High Commission for Coordination among Regions and Governorates, as well as with international development partners. This was followed up with field-level data collection through local consultants. The draft report was validated through informal consultations with counterparts in Iraq.

1.3 Development of the Governorates’ Political and Service Delivery Authority

1.7 **Since 2003, Iraq has progressed toward a more decentralized governance framework, but the progress has been uneven:** the period 2005–2009 was marked by enthusiasm and leadership from the Governorate level stimulated by the political legitimacy achieved by the election of governorate councils. The period of 2009–2013 was characterized by discouragement ensuing from the uneven support from the central ministries. The current period of 2013–present has seen renewed decentralization prospects by statutory changes (2013), as well as the strong policy support of the al Abadi government in 2015. This overview focuses on the 2013–2015 period, and provides an update on Iraq’s progress toward a more decentralized system. It also presents a framework for support of that progress. Table A2.1 (see annexes) summarizes the key constitutional, statutory, and other main legal contributors to decentralization in Iraq.
1.8 The first major step toward decentralization under the Iraqi authority was the election of the governorate councils (for all 18 Governorates) in January 2005. The election overcame some stigma attached to occupation period advisory councils. In this one step of citizens choosing their own representatives, Iraq achieved a degree of political decentralization much more quickly than many other countries’ whose decentralization process is considered highly successful, such as Indonesia. This first major step in political decentralization, taken by Iraq even prior to the adoption of a new Constitution, has stood the test of time with a statutory basis adopted in 2008 and successful, subsequent elections in 2009 and 2013.

1.9 The new Constitution adopted overwhelmingly in a national referendum in late 2005 affirms a federal structure with locally elected councils that in turn select the local executive authority — which would be the Governor in the case of the Governorates. However, the federal nature of the structure refers only to regional governorates. Authorities of regions (only the KRG at present) are protected in the Constitution. For those Governorates not in a region, the Central Government has the constitutional authority to legislate Governorate authority and sources of revenue.

1.10 From 2005 through 2009, the elected governorate councils took two significant initiatives to fill in vague and somewhat contradictory references in the Constitution to a decentralized state: namely, the successful drafting and lobbying for passage of the Law on Governorates not Incorporated into a Region (Law 21, 2008), as well as the preparation of strategic plans for the development of the Governorates. Law 21 provides the statutory basis for governorate authority. Amendments in 2010, 2013 and 2015 (pending) have clarified some governorate authority, such as the legislative authority of governorate councils. They also mandated the devolution of key functions in eight federal ministries. Governorates also took the initiative to address demands from citizens for basic service improvement. As early as 2005, the Basrah Governorate started a strategic planning process that in 2006 expanded to all 18 Governorates. Specifically, the Governorates expanded this vague mandate into a strategic planning process that produced multi-year development and action plans consisting of capital projects to rehabilitate, replace or create new capacity for service delivery (USAID and RTI International 2007).

1.11 Parallel to the developments concerning the Governorates and investment planning process, the Council of Ministers included in the 2006 Budget an allocation (Accelerated Regional Development Program - ARDP) of a proportion of the federal investment budget to each Governorate for their discretionary use. Governorates have taken advantage of their strategic investment planning programs and the federal budget allocations to fund projects in their investment plans. However, project approval processes in the Ministry of Planning and regulations in the Ministry of Finance for access to funds have hampered the timely access by Governorates to allocations, and project execution has been weak. Governorates generally have been as effective at implementing investment projects as the central ministries.
1.12 The Governorates’ initiatives to write Law 21 and to improve service delivery through investment programs marked the initial high point for decentralization. Later, the 2009–2013 period was characterized by a degree of retrenchment. Much of what happened with governorate authority in the 2005–2007 period was Governorate initiated, thereby forcing central government officials to respond. Operational details were not really worked out, especially as to how governorate development plans turn into investment programs, and then individual projects. Details were also lacking with respect to access to funds to implement the projects. Both as a practical matter and perhaps because of some reluctance at the central level to see decentralization proceed too quickly, operational requirements and guidelines issued by the central ministries have tended to reduce the extent of actual discretion on the part of governorate officials.

1.13 From 2009 through 2015 (and in the proposed 2016 budget), funding allocations for governorate investment programs have fallen from the early significant share of the investment budget to 15 percent and less, especially after the fall in oil prices. Momentum for decentralization declined through the year 2013. Some of the decline is perhaps attributable to the central government deliberately slowing the pace of decentralization through the regulatory processes, and in part due to the practical operational issues that arose. The more serious limitation on Governorate-directed programs has been the decline in investment allocations to the Governorates. From 2006 through 2009, the KRG and the Governorates not incorporated in a region were allocated 35 to 45 percent of the total investment budget. In 2016, the investment budget allocation to the KRG and the Governorates will be less than 6 percent of total investments. Even if the oil and gas revenue allocation to producing and refining Governorates is taken into account, the total funds for investments for the KRG and the Governorates, as a share of total investments, will still be below 12 percent. (See table A2.2). In addition, the 2016 Budget includes a prohibition against the Governorates using any of the allocation to start new investment projects, possibly forecasting a worsening beyond 2016.

1.14 The year 2010 saw a few short lived initiatives to further decentralization. These were fueled by legislation to take a major step toward assigning service delivery responsibility and allocating funds to the Governorates. The 2010 Laws 18 and 20, respectively, devolved the Ministries of Labor and Social Affairs and Municipalities and Public Works to the Governorates. The initial excitement, however, was stifled when both laws were declared unconstitutional by the Supreme Court.\(^3\)

\(^2\) Based on the current version of the 2016 budget as approved by the Council of Ministers.

\(^3\) The Court did not rule on the legality or appropriateness of devolving ministerial authority to the Governorates, but to procedural issues as to how the laws were introduced (legislation has to be evaluated and approved by the Council of Ministers before passage by the Council of Representatives).
Box 1: Key Provisions of the Second Amendment of Law 21

The key provisions of the Second Amendment of Law 21 include the following:

1. Strengthens the authority of Governorate Councils as the “legislative and regulatory authority” with the right to issue local legislation in a manner to enable the Council to conduct its business in accordance with the principle of administrative decentralization;
2. Gives the Governor “direct power over the agencies … assigned to protection and preserving security in the Governorate (Articles 10.8 and 10.10);
3. Further formalizes federal budget allocations to Governorates sufficient to fulfill their functions in accord with population, level of deprivation and consistent with balanced development for different parts of the country;
4. Further specifies revenues generated by the Governorate to include service fees on services and investment projects, taxes and other fees and fines, sale of movable and immovable state property, half of the revenues of border ports;
5. Allocates $5.00 per barrel of crude oil produced in a Governorate, $5.00 from every barrel of crude oil refined in a Governorate; and $5.00 from every 150 m$^3$ of natural gas produced in the Governorate (Article 44)

Note: The Budget Law for 2016 changes the fixed $5 allocation to a 5 percent equivalent allocation.

1.15 Little happened to further the decentralization process between 2010 and 2013. After the Supreme Court action on the devolution of two ministries, the governorate councils elected in 2009 turned more inward and were less inclined to start new initiatives at the national level. Although there was a strong sense from 2010 that momentum for decentralization was stalled, 2013 saw a reversal. The Second Amendment to the Law on Governorates not Incorporated into a Region (Law 19, 2013) strengthened language to most provisions of the Law that had been challenged, such as council authority to legislate. Other language pertained to the assignment of significant security authority to the Governors, and augmented the allocation of resources to the Governorates, including enhanced authority to the Governorates to raise their own revenue.
The enactment of Law 19 (2013) gave a much-needed impetus to push the decentralization initiative forward. The most important article of Law 19 (2013) gradually transfers the “sub-directorates, departments, tasks, services and competencies of eight federal ministries.” The law creates a new High Commission for Coordination among the Governorates to manage this transfer. The High Commission is chaired by the Prime Minister, with the Minister for Governorate Affairs as the Secretary. Membership includes several ministries and representatives of all the Governorates. The 2013 amendments provide broad statements of policy, but few operational details. The devolution provision leaves the practical issues of how the devolution is to take place aside, including what functions, staff and budgets will be devolved and, over what time period, to the individual ministries — most of which did not want to be devolved. While the High Commission seems strongly supportive, it is a small organization with limited technical staff support and the authority apparently only to coordinate, not to require specific actions. As a result, very little happened in 2013 and 2014.

In 2015, the new Prime Minister gave a strong push to implementation of the 2013 devolution provision. Several of the Ministries coordinated by the High Commission began negotiation meetings to identify the functions to be devolved, as well as the mechanics of staff and budget assignments. However, by the August deadline, no agreements had been settled, and the time was extended to November 5, 2015, which has now passed.

A Third Amendment to the Law on Governorates not Incorporated into a Region has been approved by the High Commission and the Council of Ministers. This Third Amendment intends to force rapid devolution of some ministry functions and allow for a more gradual devolution of other ministry functions. It amends Article 45 (Law 21), the article that contains the devolution of federal ministries as follows: “The commission shall discharge its functions referred to in paragraph (1) above [coordinate the devolution of federal ministries] gradually as of the date this law comes into effect provided that some powers are delegated immediately, others within 6 months and other powers within one year and above. The powers that remain within the federal ministries’ powers must be specified.”

Substantial agreement has been reached on the devolution of the Ministry of Housing and Municipalities (including the five directorates of Municipalities, Water, Sewage, Urban Planning, and Planning and Follow up). Some 163 functions of the 5 directorates are understood to be devolved, and all parties agree that 107 functions are not to be devolved. A further 17 functions are still under debate. Implementation of these agreements should be underway for the remainder of 2015 and into 2016. Other ministries to be devolved at least in part indicate they have not started the process but there was no clear indication on when they would expect to complete the process.

Tellingly, the proposed 2016 budget does not take into account the devolution of any functions of any of the Ministries. The fiscal year (FY) 2016 budget does, however, provide (Article 34) the Minister of Finance with the power to transfer the financial allocations of departments which are no longer related to ministries to the related Governorates, including the transfer of all grades and titles as well. Thus, although the 2016 budget allocations do not transfer budgets of devolved functions, as decisions are reached, the Ministry of Finance can make the budget transfers during the 2016 budget year.

These include the Ministries of Housing and Reconstruction, Municipalities and Public Works, Health, Education, Labor and Social Welfare, Sports and Youth, and Agriculture. The wording of the Article seems to suggest Finance also, but apparently it has meant only the creation of Finance Directorates in the Governorates and not a devolution of the Ministry of Finance authorities.
1.21 **The current model of decentralization in Iraq is moving on a somewhat eclectic and haphazard fashion.** Variations in capacity across levels of government necessitate an asymmetric approach in direct service delivery assignment, particularly within the third tier of government. In any meaningful sense, decentralized service delivery is presently very weak. The institutional framework to support decentralized service delivery is also undeveloped. The model envisioned via existing law has its foundation in administrative deconcentration, with an emerging level of regional/local authority for service delivery/responsibility and a lesser level of emerging revenue authority. Decentralized expenditure authority can exist without decentralized revenue authority, but this existence is fraught with pitfalls and requires a systematic commitment to the provision of resources necessary for local choice in a manner that allows meaningful local expenditure discretion.

1.4 **Decentralization: Issues that need to be considered in moving forward**

1.22 **Significant policy changes have been made in 2013 and 2015 that can substantially move decentralization forward to the subnational levels, if key issues are addressed.** However, decentralization policy does not appear to be matched by appropriate fiscal arrangements. The 2016 Budget’s protection of central ministry investment budgets by slashing allocations to governorate investments undermines the belief by governorate officials in the seriousness of policy reforms. In addition, it engenders heightened citizen dissatisfaction with public service levels — dissatisfaction that is directed at governorate officials more than at central government officials.

1.23 **The proposed decentralization policy changes are not yet matched at the operational level.** The High Commission has the major responsibility for ensuring that the 2013 and 2015 amendments to Law 21 are implemented. However, it still is a small group composed mainly of officials from the ministries, the regions and the Governorates. It seems to lack the authority and the staff to address a variety of concerns, for example, possible legal issues related to whether the devolution amendments to transfer staff to the governorates, particularly senior staff at the Director level and above, contradict the organic statutes of individual ministries or other laws. There is great possibility for confusion regarding reporting lines of authority for devolved staff.

1.24 **Ministerial functions to be devolved are being identified on a functional basis, but lack clarity about the structure to be devolved.** Specifically, a function can be one such as: “managing and organizing the administrative and technical staff, and transferring and relocating them [except for the departments’ managers in the governorate”] in each of the five Ministry of Municipalities Directorates. These Directorate functions being devolved are to be transferred to the Governorates. However, it is not clear if the supervisory or management personnel, who have in the ministry exercised that function, are to be transferred. If senior managers of a directorate are not transferred, then the devolution of the function assigns authority and responsibility to the Governorate — but not the experienced management personnel to carry out the function.
1.5 Moving the Decentralization Agenda Forward: Strengthening the Accountability Framework

1.25 Decentralization in Iraq requires a strategic approach in order to move forward. Although Iraq has taken several steps toward decentralization, what seems to be missing is a clear strategic vision that lays out the objectives and intended outcomes. Decentralization has moved forward in an ad hoc and fragmented fashion in the past. This seems to have affected the smooth progression of the government’s intention to translate the broad national vision articulated in the Constitution into tangible development results on the ground. Although decentralization has gathered some momentum in the past few months, there is a risk of losing this window of opportunity — unless the governments seizes this opportunity and lays out a clear vision for the way forward.

1.26 There needs to be a shared vision regarding decentralization among the various stakeholders. Decentralization is a multi-dimensional process and requires a common understanding of the outcomes and processes by the various stakeholders involved. In Iraq, although the Constitution and the legal framework spelled out the broad layout of the decentralization reform process, there is still a lack of clarity among key stakeholders regarding their respective roles. For instance, discussions by the Bank team with several stakeholders revealed a difference in perception between key Ministries and the Governorates on the scope of devolution of powers and responsibilities. In a diverse economic, political and social country such as Iraq, it is important for the Central Government to reach out to the various constituents involved in the decentralization process both within the government and outside. Likewise, it is essential that the government communicate effectively the expected outcomes and benefits to the country as a result of this process. The High Commission for Coordination among Provinces and Regions should take the lead and put in place a robust communications strategy for the decentralization effort.

1.27 Improving the delivery of services by Governorates needs to be the principal driver of decentralization in Iraq. Although decentralization may be motivated by various considerations (administrative, financial, and political, to name a few), a key outcome that it should achieve is enhancing the ability of the State to deliver services to citizens in an accountable and responsive manner. This is very pertinent in the case of Iraq as evidenced by the consistent demand of citizens for better delivery of services. The intent of the 2005 Constitution was to enable the State to move from the highly centralized governance model of the pre-2003 years to a model of shared powers and responsibilities that would enable the Governorates to respond to the service delivery needs and priorities of their constituents. However, the fragmented approach to decentralization has prevented the country from actualizing the philosophy of the Constitutional mandate. Therefore, organizing the decentralization reform process around the core objective of enhancing the Governorates ability to deliver services in an efficient and accountable manner will move the ongoing reform process forward. In this way, it will also help the Governorates to better connect with the development demands of the citizenry.
1.28 **There are significant gaps in the existing institutional and financial structures that prevent the Governorates from delivering services in an efficient and effective manner.** Despite the devolution provisions of Law 19 (2013), the Governorates continue to face a variety of constraints that impede their ability to deliver services. The institutional structures of the devolved ministries continue to operate in the deconcentrated mode. Furthermore, there are no clear plans for the transfer of staff, no clear guidelines for the reporting and accountability relationships of devolved staff to the Governorates and former parent Ministries, and no clarity in the organization of the civil service under the decentralized context. Although the Governorates prepare their Provincial Development Plans through a system of consultation at the district and sub-district levels, the final choice of projects and their implementation continues to be essentially a centrally driven process. The flow of resources from the Central Government to the Governorates through the investment and recurrent budgets does not provide discretion and flexibility to the Governorates that would reflect their local priorities in the preparation and execution of their annual work programs. This situation continues to be significantly affected by the liquidity pressures and the financing priorities of the Central Government. These have in turn affected the ability of the Governorates to effectively address local service delivery priorities.

1.29 **Strengthening accountability for service delivery could provide the strategic framework for strengthening decentralization in Iraq.** International experience has shown that strengthening accountability is critical to improved service delivery as it strengthens the social contract between the citizens and the State. The World Bank Group’s *World Development Report* (2004) analyzed the factors that contribute to effective service delivery by the public sector. It determined that improving service delivery performance requires the strengthening of accountability relationships between the State and service providers, citizens and the State and between citizens and service providers. Translating this model into the Iraqi context requires the building and strengthening of three key accountability relationships that are currently weak in Iraq. These relationships have a critical impact on service delivery, and include those specifically between the citizens and the Provincial Government, between the Provincial Government and the Central Government and between the Central Government to Provincial Governments and citizens. Therefore, strengthening service delivery in the Governorates through the government’s decentralization program would require specific operational steps to redefine and strengthen these accountability relationships.
1.30 Strengthening accountability for service delivery requires strengthening the institutional and financial aspects of decentralization. Strengthening the institutional capacities of the Governorates will require: (i) clear assignment of service delivery responsibilities to the Governorates; (ii) clarity in functional and reporting relationships between devolved staff in the sector ministries and the Governorates; and (iii) restructuring of organizational structures and systems that will provide the necessary incentives and motivation to staff in the long run in terms of career progression and skill building. Institutional development also includes strengthening the social contract between the Governorate and their citizens through robust citizen engagement and transparency in government plans and programs. In addition to existing institutions such as the High Commission for Coordination among Governorates that play a critical role, the need for similar such institutions to ensure a robust institutional framework for decentralization and service delivery at the Governorate level needs to be explored. Similarly, on the financial side, providing the Governorates with discretionary resources in a transparent and predictable manner will enable them to address local development priorities in an effective and accountable manner. Public financial management (PFM) and oversight systems also need to be put in place and strengthened to provide efficient and accountable execution of plans and programs. Whatever fiscal transfer arrangements are put in place will need to be designed in ways that balance legitimate governorate spending demands that are consistent with devolved functions, and with the continuing provision of public goods by the central government. Furthermore, this must be done in ways that are responsive to Iraq’s macro-fiscal situation, currently highly circumscribed by civil war and weak international oil and gas prices.

1.31 The Provincial Development Plans (PDPs) formulated by the Governorates offer a good platform to bring the various accountability elements together. The investment budget for the PDPs is the only budget where the provincial Governor and the Provincial Council have discretionary authority with regard to the selection of projects for budgetary funding. Governorates have 10 years of accumulated experience in these processes. However, in the current system, Central ministries are heavily involved in the final choice of projects and their approval leaves little discretion for Governorates in selecting and implementing projects. All projects must be consistent with the national development plan. Reforming the PDP process and enabling Governorates to respond effectively to citizen priorities could strengthen local accountability.

1.32 Reforming the current system of PDP preparation and implementation offers a unique opportunity to strengthen the capability of the Governorates to deliver services. Creating a robust model of consultation between the Governorates and citizens during the preparation of the PDPs will ensure that the PDPs reflect local development priorities in a realistic manner. Providing transparent and predictable financing for the PDPs — as well as the flexibility to the Governorates to use the financing provided in a discretionary manner without being constrained by centrally-determined priorities — will enable the Governorates to respond to local service delivery and development requirements in a timely and effective manner. Providing an adequate complement of staff at the Governorate level with clearly defined functional responsibilities and reporting relationships, as well as strengthening the execution capacities of the Governorates by creating PFM and oversight will enable the Governorates to implement PDPs in an efficient and accountable way. Furthermore, the devolution of functions from several ministries affords the opportunity for development planning at the governorate level to become a comprehensive investment mechanism across different services.
1.33 Adopting a “learning-by-doing” approach is necessary to enable the Governorates to manage their service delivery responsibilities in an efficient, effective and accountable manner. As the Governorates increasingly take on more service delivery responsibilities, the capacity of the Governorates to effectively manage their new responsibilities will be a critical factor that will determine the future course of decentralization. Along with transferring the responsibilities, staff and provision of financing, the capacities of the Governorates to manage the service delivery function need to be developed. International experience has shown that rather than providing training and capacity building efforts in isolation and/or in a piecemeal manner, adopting a “learning-by-doing” approach provides better results in the public sector. Such “learning-by-doing” should also entail capacity support in an integrated manner along with financing and institutional development support to help the Governorates meet their mandated responsibilities. Furthermore, by enabling the Governorates to implement the PDPs through the provision of targeted capacity support can result in building institutional capacities of Governorates in a sustainable way. Therefore, the Central Government and international development agencies should align their capacity support initiatives in the Governorates with a view to enabling them to fulfill their service delivery responsibilities.

1.34 A coordinated and sequenced approach to operationalize decentralization will be necessary in order to move forward. To consolidate the gains made in the decentralization reform process so far and to enable a smooth progression in the future, it will be necessary for the government to lay out a set of steps to operationalize the devolution of powers and functions for the eight ministries created under Law 19 (2013). Following the direction of the Cabinet and the High Commission for Coordination among Regions, some ministries (such as the Ministry of Municipalities and Public Works) have started taking steps to transfer specific powers, functions, and resources to the Governorates. However, concerted action is required from other devolved ministries as well as other key ministries, such as Ministry of Finance and Ministry of Planning, to put in place the operational rules for implementing the provisions of Law 19. A well-defined sequence of operating steps that will coordinate the roles of the various ministries/agencies at the central and Governorate levels is necessary to ensuring a smooth implementation of the decentralization process.

1.35 The High Commission seems to be an appropriate institution to oversee and coordinate the process. It has representation of the key actors from both central ministries and the Governorates, and it has the Prime Minister’s authority as Chair. However, the High Commission’s role, at least to date, does not seem to include the authority to require central ministries to fulfill the law’s requirements. The High Commission needs to steer the decentralization process forward by playing an active role in coordinating among central ministries and agencies, as well as between the Central Government and the Governorates.
The technical and staff capacities of the High Commission need to be strengthened to enable them to effectively coordinate the decentralization process. The High Commission does not appear to have the technical capacity and staff resources to support the negotiation process between the various stakeholders related to decentralization, and to address other operational issues that have to be solved. The High Commission needs to develop within itself core capacities both in the policy and operational aspects of decentralization so that they can provide sound technical advice to the Government at the Central and Governorate levels on implementing decentralization. Donor partners could possibly support the High Commission to take an inventory of its current capacities and provide technical assistance and capacity building support to enable the High Commission to strengthen its competencies in the financial, administrative, legal and policy aspects of decentralization. South South Learning Exchanges between other developing countries could be considered so that the High Commission can learn from the experiences of other developing countries who have experience in managing the decentralization process.

1.36  The political economy of the decentralization reform process needs to be better understood. Decentralization is a complex political process and a good comprehension of the history and process of decentralization reform is critical to understanding the incentives and motivations of the various stakeholders. Discussions with various stakeholders during the mission gave a glimpse of the variance in perspectives and expectations among different stakeholders with regard to the process and intended outcomes of decentralization. Understanding these underlying incentives, motives that drive various stakeholders to support or oppose decentralization reforms and the resultant institutional dynamics through a systematic political economy analysis will be very useful in charting the long-term course for decentralization reforms in Iraq. Since undertaking a political economy analysis is outside the scope of this report, we recommend that such an analysis be carried out by the Bank and/other development partners in collaboration with the Government of Iraq in the near future.

1.38  The decentralization model in Iraq is evolving. Considering the diversity of the country a monolithic approach is likely to fail. Asymmetric solutions are likely necessary at the Central and Governorate levels to adapt to differing regional capacities and social, cultural, economic and security environments and also due to the widely varying capacities and conditions at the district/municipal levels. In all likelihood, the necessary structure for effective decentralization in Iraq will not be encompassed by as single decentralization model and will likely require the development of separate sub-models which provided increased autonomy and discretion in a manner consistent with capacity. Going beyond the current model of decentralization that is focused at the Governorate level, it may be useful to consider the feasibility of devolving powers and responsibilities to the district/municipal level as they are the tier of the State closest to the citizens. However, the weak institutional structure at the district/municipal level and the absence of a clear assignment of powers, responsibilities and resources to the districts/municipalities prevent the latter from functioning effectively as the third tier of the State. Iraq could learn from the experience of countries such as Indonesia who strengthened their local governments through a series of interconnected policy measures (such as providing discretionary financial resources to local governments through formula based fiscal transfers and strengthening local service delivery by clearly defining institutional roles and responsibilities). Further studies and analysis are required to explore the modalities of devolving powers and functions to district/municipalities.
2. INSTITUTIONAL ASPECTS OF STRENGTHENING SERVICE DELIVERY BY THE GOVERNORATES

2.1 The Government of Iraq has begun the process of devolving some functions to the provincial governments. The institutional challenge will be to build on the core organizational structure and capacities currently found in the Governorates, and ultimately create more autonomous provincial governments capable of sustained service delivery. Provincial governments will have extensive service provision responsibilities, and will be directly accountable through a locally appointed governor as chief executive. Specifically, the provincial governments will be accountable to an elected provincial council with legislative powers within its mandate, and, in turn, to all residents of the province. For this to happen, the Governorates will have to: (i) prepare and coordinate public investment plans on a much wider basis than before; (ii) develop greatly expanded budget preparation and implementation capabilities; and (iii) manage and motivate many times more staff than they presently control, covering all the services transferred to provinces, districts and sub-districts. All of this will have to be supported by new accountability mechanisms, re-orienting service delivery departments toward the governor and the elected council, and outwardly to citizens.

2.2 This chapter discusses the capacity building challenges that lie ahead. It begins by describing the existing administrative arrangements centered on the Governor’s office. Then it looks at what needs to be done to handle the service delivery functions and the provincial level staff of the eight ministries that are being identified for transfer to the Governorates. Finally, it considers the longer-term future, when provincial administrations could become a more distinct and autonomous layer of subnational government in Iraq, including their own provincial civil services and distinct planning and budget systems.

2.1 Existing Structure of Provincial Governments

2.3 There is some variation in organizational structure and staffing between provinces. The Bank team was able to visit Wasit Province, and met with Basrah Province staff in Baghdad. Table 1 shows the organizational structures of the Governor’s Office in Wasit Province and also in Basrah Province.

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*Source: World Bank mission notes.*

**Box 2: Salient Features of the Organizational Structure of the Wasit and Basrah Governorates**

*based on field observations*

- **Organization of the Governor’s Office:** In Wasit, there are two Vice-Governors assisting the Governor, though they do not appear to have separate departments under them, as is the case in Basrah. Governors also have senior advisers, generally on contract, reporting directly to them.

- **Planning:** The Planning Department in Wasit is divided into a Strategic Planning Division, a Follow-up Division, an Information Technology (IT) Division, an Administrative Division, and a Poverty Support Division. In Basrah, the Planning Department has an Administrative Division, a Follow-up and Evaluation Division, a Sustainable Development Division, a Sector Planning Division, and a Plan and Resource Management Division. It is not known how many professional staff exist in each of these divisions, or how much interaction they have had so far with the centrally managed service delivery ministries in the province. However, structurally, both Governorates’ Planning Departments seem to be organized to play a larger role.

- **Budgeting and Accounting:** Both Governorates have Budget Departments. In Basrah, a single department covers both the recurrent and investment budgets, whereas in Wasit there are separate departments. In Basrah, accounting is a separate department, as is audit. In Wasit, audit and accounting appear to be folded into the two budget departments.

- **Personnel Management:** Wasit has a separate Human Resource (HR) Department reporting to the Governor. How the Basrah Governorate handles personnel management is unclear because there is no separate department identified in its organizational structure. Possibly, personnel matters are shared between the Governor’s Office and the Budget Department.

- **Relations with Districts and Sub-districts:** Basrah has a distinct department for Districts and Sub-districts, with separate divisions for each district. In Wasit, it is unclear how district and sub-district relations are handled, although the Media and Public Relations (PR) Department is organized by District.

- **Service Delivery Sectors:** Both Wasit and Basrah have a Sector Division within their Planning Departments. In addition, Basrah has a Department of Sectors reporting directly to the Governor, within which can be found the Health and Education Directorates. This would suggest that provincial governments have gone some way toward creating a management structure for broader service delivery.
2.4 **Critical departments for successful decentralization are those which will be central to the management of the devolved functions and staff of the eight ministries.** These are the Planning Department, the Budget Departments, the Human Resources Department, the Engineering Department for project design, and the Contracts Department for project implementation. The Audit Department is likely to be important for financial control. The team was not able to visit each of these departments, but their present capacities appear to be closer in scale to the presently limited, formal governorate functions. Nevertheless, they are the foundation for an expanded governorate administration as decentralization unfolds. However, this will entail a major expansion of the tasks to be performed and the resources they have to carry them out, as they are starting from a very small base.

2.5 **The Planning Department prepares the Provincial Development Plan, comprised mostly of investment projects.** It submits it in the first instance to the Governor and the Provincial Council. Thereafter, it is sent to the Ministry of Planning in Baghdad, which checks the plan for alignment with national planning parameters and project eligibility guidelines. Engineers help design investment projects, and the Contracts Department plays a critical role in project implementation. Projects are included in the Governorate’s Investment Budget, and ARDP funding from Baghdad is made available by the Ministry of Finance in the course of the year (although sometimes the funding is late because of delayed Ministry of Planning approval of projects, and delays in issuance of annual requirements on access to and reporting on fund disbursements by the Ministry of Finance). The money is paid into the Governorate’s Investment Budget bank account at one of the state-owned commercial banks, out of which project expenditures are met. The Governorate Office is required to follow government-wide procurement and financial management rules and processes.

2.6 **The Provincial Budget Department acts as a provincial treasury in that it manages the provincial bank accounts and controls cash by regulating the flow of payments, both for the recurrent and the investment budgets.** The Second Amendment to Law 21 includes in the devolution provision the creation of a governorate-level Finance Department (or Directorate) in each province to encompass the increased treasury responsibilities. Currently, there is no automation; existing provincial budget departments operate using an essentially manual system, supported by spreadsheets. If releases are late or less than the approved budget provides for, the Budget Department pays only the most urgent bills and allows arrears to accumulate to protect cash for salaries. As budgets have become tighter with falling oil prices, spending on operating costs, other than salaries, and on investment projects has declined. The Budget Department reports monthly to the Ministry of Finance, submitting budget execution records in support of drawdowns. Annual budgets drawn up by the Provincial Budget Department are submitted to the Provincial Council for approval, but the ultimate decision-maker is the Ministry of Finance in Baghdad. The Ministry of Finance makes the decisions because the provincial budgets are merely one component of the national budget, which must conform with the country’s macro-fiscal targets. Furthermore, they cover only the very limited direct activities of the Governor’s office and the council, with all service delivery functions currently paid out of the central government line ministry budgets. In this context, the governorate budget departments have no experience of putting together comprehensive service delivery budgets.
2.7 **Presently, the Human Resources Departments in the Governorates handle only the staff of the Governorate administration.** They are responsible for their pay and grading, subject to Ministry of Finance guidelines. If staffing levels require increasing, the Governorate submits its requests for additional posts to the Ministry of Finance as part of its annual budget submission. Total staff numbers are moderate, about 750 for Wasit, and somewhat higher for Basrah. Salaries are paid in cash envelopes, and not electronically into staff bank accounts. Personnel files for individual officers are held by the HR Department only for Governorate staff. Appointments and promotion decisions are made locally. However, again, they are subject to central government regulations, which require vacant positions before new staff can be recruited or existing staff promoted. A mostly seniority-based pay and grading system operates across the Governorates. Both Governorate staff and those working for central government ministries delivering services in the province are currently members of a single public service of the government of Iraq.

2.8 **An acceptable payroll system at the governorate level does not exist.** This is currently managed by the finance department, and salaries (and other related benefits) are paid mostly in cash (and not by electronic transfer of funds to employees’ bank accounts). This process entails significant risk to cash collection from the bank and distribution to staff. Anecdotal evidence suggests that Iraq’s state-owned banks do not have the required infrastructure to serve thousands of bank accounts of government employees and arrange for the transfer of funds to these accounts on a timely basis. However, it appears that all suppliers and contractors are paid through checks.

2.9 **Ministry units in the province are required by law to inform the Governor of their plans and program activities.** However, the Governor, under present arrangements, has little leverage in the choice of the sector investment projects in the Governorate other than his powers of persuasion. Plans and investment projects of the line ministries delivering services at the provincial level are negotiated directly with their headquarters and in turn with the Ministry of Planning in Baghdad, as are operational budgets. Presumably this will change for the devolved functions as Governors will have formal institutional authority over the devolved functions. Governors are the most politically visible figures in the government at the provincial level, and are popularly expected to make a difference. This will present a challenge for them, since they have few levers to pull.

2.10 **As line ministry functions at the provincial level are transferred to the Governorates, the management responsibilities will increase greatly.** The team was not able to obtain estimates of the total staff numbers expected to be transferred to the Governorates once the decentralization process is completed. However, this could entail a tenfold or more increase in the ultimate payroll, given that eight ministries will be transferring their service delivery staff, and that many of the transferred functions are expected to be staff intensive, such as those pertaining to health and education. The next section looks at what needs to be done to handle this substantial increase in managerial responsibilities.
2.2 Institutional Impacts of Decentralization

2.11 The decentralization process has already started. As noted, Law 19 (2013) and a Third Amendment to Law 21 (2008) currently under consideration have accelerated the process of devolving some functions and responsibilities from the Central Ministries to Governorates. An immediate issue is how these devolved functions and responsibilities will be coordinated with functions remaining in the central ministries. The challenge before the government is to put in place an appropriate institutional setting that fosters a cooperative and coordinated working arrangement between the central and provincial elements of devolved functions. Governors will also need to create a new management structure so that the heads of former central ministry units report and take instructions from the Governor rather than ministry headquarters in Baghdad. At the moment, there is no overall plan for the decentralization of services, with negotiations proceeding at different speeds with different line ministries. Therefore, decentralization is likely to be a process spread over several years rather than a “big bang” event.

2.12 As transferred functions are identified, Governors will need to quickly build a management team to handle the new service delivery responsibilities. Regarding the transfer of functions and staff, Governors may adopt a “carry-on as normal” policy for service delivery. In one sense, this would be the correct thing to do. Existing services reflect national policies and follow long practiced management routines, with which staff are familiar. Severing the connection with vertical reporting obligations and transferring them to the Governors is likely to be disruptive enough in itself. Therefore, in the short run, changing service delivery policy and programs is unlikely to be an option. Indeed, the underlying assumption behind the shift in reporting responsibilities is that services will remain guided by national policies and standards. However, once the initial transfer period is over, Governors will want to address what are seen to be deficiencies in service delivery through the means at their disposal, including the provincial budget, staff dispositions, and management changes. In the short term, tight budgets, which reflect both reduced oil revenues and the need to fund large defense expenditures, will limit their ability to take advantage of greater management autonomy.

2.13 Once the functions to be devolved are agreed upon by the Ministries and the Governorates, then the issue becomes whether the devolved functions form coherent organizational structures in themselves. Alternatively, they could be smaller units abstracted from larger structures that may not be either provincially or functionally organized. Until the process of identifying the functions and staff to be transferred is further advanced, it is hard to be sure whether what will be moved to provincial control comprises organizationally coherent entities or something less well formed. For example, some services delivered at the provincial level may be closely integrated with nationally based support units, located in Baghdad, for example. These will have to be identified, and suitable arrangements worked out. Alternatively, they may share some internal services with parts of the ministry which, though located in the province, will not be transferred because they are engaged in national programs.
2.14 The functions to be transferred are still being negotiated, and it is hoped that issues of organizational coherence will be considered in the process. In this context, the High Commission has a critical role to play, ensuring that managerially coherent structures are moved to Governorates to match their newly transferred service delivery responsibilities. Unfortunately, the Bank team did not have an opportunity to talk to central government ministries (except the Ministry of Housing, Municipalities and Public Works) about the way service delivery functions at the provincial level are organized. Nonetheless, the Governorates should be prepared to look critically at what is being proposed for transfer. They should demand adjustments, if justified, to ensure that the functions that get transferred from a ministry are matched with sufficient organizational capacity and resources. Governors will need to be ready, either through their own office personnel departments or by engaging consultants, to review transferred services and ensure that management structures are in place for them to function without undue delay. The Basrah Governorate’s organization chart, for example, shows what seem to be already formed health and education sector directorates. Even if they are only shells at this point, they could be expanded with staff transferred from central government service delivery ministries. Governors will have to create new departments within their existing structures which correspond with the transferred service delivery functions, and ensure that each one is headed by a management team drawn both from the transferred administrators and professionals, and perhaps existing Governorate staff in which the Governor has confidence.

2.15 Whether the transfer of functions happens over an extended period or more quickly, the Governorates will need to increase their budget and personnel departments to handle a rapid increase in the scale of their functions. They will have to move from making budgets and managing the personnel of, what is by the government of Iraq standards, a single, modestly sized department to running a large and complex organization with multiple functions across sectors. For example, if the transfer of education and health ministries to the Governorates involves the transfer of primary and secondary schools, healthcare, clinics and hospitals, this could entail thousands of teachers and health workers being added to the Governorate payrolls. A critical issue will be whether the transferred functions will come with sector planning, budget and HR management staff. If such staff currently exist in the provincial establishments of the central ministries, they should be transferred along with their service delivery colleagues.

2.16 As a practical matter, consideration should be given to verifying staff numbers as part of the staff transfer process. If there are substantial payroll irregularities (such as staff paid at inflated scales, ghost workers [fictitious names inserted for fraudulent purposes], retirees or deceased workers still drawing regular salaries from the central government ministries, then such problems will need to be addressed before payroll responsibility can be assumed by the provinces. Therefore, Governors may want to verify the staffing rolls before accepting responsibility for their payrolls. It would be better to verify this first, while staff records are kept centrally and are still the responsibility of the line ministry. The alternative would be to find out later that provinces have been saddled with payrolls that do not match authorized staffing lists, and that the transfer has inadvertently legitimized payroll irregularities, making it too late to correct them. In this context, the Central Government, notably the concerned line ministries and the Ministry of Finance, should determine the extent to which staffing and payroll irregularities are an issue, and work out how best to deal with them. A sample payroll audit of the first ministry identified for service delivery function transfer to provinces could be the place to start.
2.17 **Ensuring that staffing lists and payrolls are accurate before people are transferred is only the first step in managing staff resources effectively.** When staff have been transferred, it will be important to record staff numbers and grades, and integrate them into the provincial payroll system. Once Governors have become familiar with the service delivery functions that have been transferred to the provinces and the staff that go with them, some may wish to modify organizational structures and staffing levels, and review and upgrade job descriptions (which may presently be little more than job titles).

2.18 **Governorate management structures need to be adjusted.** There will be a range of inter- and intra-departmental problems to resolve, and the Governor will want to deal with what may be seen as service delivery dysfunctions and related performance problems. The Governor will need to be sure that there are management structures in place in each of the functional grouping areas, and that an overall management team will report directly to him (or through the two Vice-Governors that Wasit has, each of whom would take several functional groupings). These functional grouping areas would in turn become departments of the new provincial government. On this vital issue, Governors are likely to need significant external management consultancy support.

2.19 **Governorate planning units will see their responsibilities greatly expanded.** Presently, the planning department under the governor is responsible only for preparing the Provincial Development Plan. At the moment, this is a parallel system because service delivery units of the central ministries in the provinces separately prepare plans which are submitted upwards for consolidation in national sector plans and then funded through the national investment budget. Once service delivery functions and staff have been transferred to the provinces, the routing of these sector provincial plans and projects logically must flow through the Governor to the provincial council for incorporation in a greatly enlarged PDP. Whether PDPs can still be funded through an augmented ARDP or in some other way remains to be determined, as does the role of the Ministry of Planning in reviewing PDPs. Ultimately, the existing planning departments under the Governor will have their workload greatly expanded, and must build capacity to match this. They would also need to be institutionally linked to the Provincial Finance Departments to ensure coherence and coordination between planning, budgeting and execution. How successfully they do this will partly depend on whether any provincial level planning staff currently in the service delivery ministries are transferred as well. This would enable the Governorate to create function-specific planning cells that would work closely with the planning department in the Governor’s office. Similar arrangements need to be in place to design the individual projects which will comprise the expanded PDPs. The transfer of functions should also be accompanied by sufficient project design and implementation specialists to ensure that the provincial planning system will work.

2.20 **As the decentralization process gets under way, Governorate planning staff should work with the Ministry of Planning to update planning manuals, procedural instructions, guidance and other training materials.** In turn, the Ministry of Planning needs to play an active role in providing guidance to the provincial governments as to how the existing PDP process will need to change.
2.21 Provincial budget departments, whether with separate or combined recurrent and investment mandates, will also see their workload greatly increase. Even under the current constrained fiscal situation, they will need to prepare and execute annual budgets greatly exceeding in scale the budgets they current manage for the Governorate alone. Their role will change too. Under the current system, the Governorates are petitioners, along with other users, for additional Ministry of Finance resources, preparing budget submissions in accordance with the Ministry’s guidelines. Once service delivery functions have been transferred and the norms for funding are established, governorate budget offices will need to take the lead in financial management. Specifically, they will need to balance their development and service delivery priorities with central budget transfers, as well as other supplementary financing sources such as locally generated revenues. This will require building up the systems, process and capacities for public financial management at the governorate level. It will be very important for the Ministry of Finance to work closely with the High Commission to ensure that the transfer of functions proceeds at a pace consistent with provincial governments’ financial management capabilities, and that all efforts are made to build the requisite financial management capacity.

2.22 A similar challenge confronts the Governorates on the personnel management side. It is not clear the extent to which personnel records are computerized across the government, and whether an integrated Human Resources Information Management System (HRMIS) exists. If staff of the transferred functions are to report to the Governor, their personnel files containing all records of their employment in the Iraqi civil service (letter of appointment, vital statistics, postings, grades, promotions, performance appraisal reports, discipline, and so on) will need to be transferred as well. Governorates will have little chance of implementing successful personnel policies unless a computerized HR management system is installed to handle the vastly increased volume of information. This calls for a review of existing practices, and for priority to be given to putting such a system in place. It should maintain standards consistent with what has been adopted by the central government so that staffing reports can be submitted by all provinces on a common basis.

2.23 In addition to personnel files, provincial service delivery records management systems will have to be transferred. This means transferring over to the provincial government filing systems that up to now have been part of the Baghdad-based central ministry systems. If offices are unchanged, many will not have to be physically moved very far, but file lists and file registries will have to be reconfigured. In this context, the opportunity may be taken for a broader review of records management across the Government of Iraq, with a view to developing a modernization strategy.

2.24 Offices and asset registries need to be set up. Many, if not most, staff are likely to remain in the same offices, but in some cases (especially if not all of the functions of a central ministry in the province are transferred), buildings will be required. In addition, physical assets such as vehicles, equipment and facilities will need to be provided. Existing asset registries need to be set up or updated.

2.25 Not all of the central government ministry staff working at the provincial level in the 8 ministries will transfer to provincial administrations and report to the Governor. There will remain staff working under central control staff on national programs or in national facilities located in particular provinces. Presently, such staff often share the same offices as central ministry staff working on service delivery. Over time, and as resources permit, provincial civil service staff will benefit from being located in distinct provincial government offices to underline their institutional separateness.
2.26  Governorates, Central Ministries and the High Commission will have to communicate the changes to stakeholders. The understanding of decentralization and its impacts may be differently understood according to the type of stakeholders. Unless there is a common understanding of the government’s policy of decentralization, there is the risk of different stakeholders taking up positions for or against decentralization that are not necessarily based on facts. Therefore, the Central Government, or mandated institutions such as the High Commission, need to undertake a communications campaign that will explain the policy goals of decentralization as well as the implementation details. For example, in the case of communications by central ministries, this will need to be done in a way that makes clear both what will happen to individual staff of line ministries delivering services, how their new reporting arrangements will work, and the reasons for the new policy. Staff need to know how they personally will be affected. Any misconceptions that arise will need to be dealt with and assurances may need to be given as well. If the decentralization policy is not operationally clear to those affected, then staff may become disillusioned and resist integration. Explained in a positive way, decentralization stands a greater chance of achieving its full potential. Thus, a change management strategy should be developed, with the High Commission taking the lead in advising provinces about how to develop a change management plan.

2.27  The role of the High Commission needs to be strengthened for ensuring a coordinated implementation of the decentralization process. The High Commission for Coordination among Regions and Governorates has played a critical role in furthering the progress of decentralization at the policy level. However, at this time, the implementation of Law 19 is entering a crucial phase. The Central Ministries need technical and operational advice for the transfer of powers and functions, and the Provincial Governorates need operational support for managing the transition so as to become fully functional subnational governments. Therefore, the High Commission needs to put in place a sustainable capacity building framework that would provide technical and operational advisory support to operating units required to achieve a smooth implementation of the decentralization process. The High Commission needs to have access to specialist technical advice in the various aspects of decentralization and public sector management, either by recruiting specialists on its own or by contracting such support so that they can fulfill their functions as a Decentralization Secretariat for the whole of the government. In turn, they will need to involve the central management agencies of the government of Iraq more directly in the process than seems to presently be the case. The participation of the Ministry of Finance, the Ministry of Planning and the Civil Service Commission (expected to be created), will be crucial.
2.3 Looking Ahead: Longer-Term Decentralization Developments

2.28 **Iraq has a deep-seated culture of centralized reporting to Baghdad, and this will take time to change.** Simply shifting staff to provincial rolls and making them formally report to the Governor will not result in an immediate change in bureaucratic culture. Nor will giving the Governor direct powers over service delivery unit hiring, promotion, staff discipline, plans and budgets necessarily change performance overnight. Staff rules will continue to be determined from Baghdad with their issuance likely shifting from the Ministry of Finance to a Federal Civil Service Commission. A law providing for this is being considered in the legislature. Plans now assembled by the Governor for not just his office but for all service delivery agencies, perhaps in the form of an enlarged PDP, will still be submitted to the Ministry of Planning for approval. The Ministry of Finance in Baghdad may still require budgets to be submitted to it, and to be implemented in accordance with centrally determined financial regulations and procurement rules. For the short term, the emphasis inevitably will be on managing the transfer with a minimum of disruption, putting staff onto provincial payrolls, determining the relationship between provincial units and sector ministries, and matching proposed expenditures with likely resources transferred to provinces under new fiscal-federal arrangements.

2.29 **The existing accountability of Governors to their respective councils will be more extensive and more complex with the devolution of functions.** This means arrangements for the presentation, scrutiny and approval of the whole provincial budget, regular fiscal reporting through the year, the production of annual revenues and expenditure accounts, and auditing, and individual program reports. These are to be submitted in due course with performance information from the main service delivery departments. The provincial Council, for its part, will need to organize itself to effectively scrutinize these reports and hold the Governor and his executive responsible for their performance. At the same time, mechanisms for horizontal accountability could usefully be devised, such as independently carried out and published beneficiary surveys, citizen report cards, and other feedback mechanisms. These would be used to provide citizens a voice and to hold their provincial governments to account. Budgets prepared by the Governor and submitted to the Council for approval should be published documents. In-year fiscal reports and end-of-year accounts and financial statements should be published documents as well. Similarly, service delivery departments should publish annual reports about their activities and results.

2.30 **Citizen engagement needs to be strengthened to enhance accountability relationships.** As Governorates increasingly are devolved to take on more service delivery responsibilities, they need to be in a position to gauge local citizen preferences and to be responsive to such preferences. Formal modes of consultations need to be put in place to ascertain citizen preferences, as well as systems for sharing of information to enhance transparency and accountability. Provincial Development Plans should be made in a participative manner. Mechanisms for the sharing of information and oversight through enhanced systems of reporting and audits should be included in the PDP preparation process as well.

2.31 **A provincial civil service will need to emerge over time.** Currently, staff working at the service delivery level in the provinces see themselves as employees of the national civil service, even if the vast majority of them are destined to serve out their careers within the province of their first appointment. The logic of decentralization is the emergence, in due course, of a professional merit-based provincial civil service to deliver policies, programs and projects. This civil service will also be responsible for discharging the mandates of the provincial government to national standards, consistent with rules and regulations that have been nationally agreed.
2.32 **Of interest here is the new Federal Civil Service Law, now on its way to the legislature.** Reportedly, the bill provides for a Federal Civil Service Commission (CSC) and provincial-level CSCs, seemingly validating the move toward separate provincial civil services. Such civil services are unlikely to deviate greatly from the federal civil service with regard to HR regulations and pay and grading policies and practices. However, the possibility might occur for some variation in pay and allowances, particularly for difficult to recruit skill categories to reflect different labor market conditions across the country.

2.33 **Arrangements could also be developed for the exchange of staff on a secondment basis.** This could include the possibility of central government staff, particularly in higher grades, serving at the provincial level, and vice versa. Similar arrangements could be made for training, which provincial governments will have to invest in if they are to build a cadre of skilled and motivated professionals.

2.34 **A Provincial Financial Management Law should be considered.** As the decentralization process gets under way, and revenue flows, mandates and reporting lines become clearer, legislation should be drafted setting forth financial management principles, key processes, standards, as well as the roles and responsibilities at the provincial level. These would include the power to issue regulations. They would also detail how provincial governments should report their revenues and spending to the central authorities in Baghdad. The law could also cover auditing arrangements and transparency requirements. Such a law should be harmonized with any existing or prospective financial management law for the federal government, so that all levels of government operate within a common financial management framework of standards and reporting requirements.

2.35 **New institutional structures will be necessary to strengthen the sustainability of the decentralization process.** As decentralized structures and systems take root, Iraq will need stable and comprehensive institutional structures to sustain the decentralized system. Iraq already has a robust legal framework that delineates the political relationships between the various tiers. However, new structures for managing the fiscal and financial relationships between the central and subnational governments will need to be designed and put in place. Such institutional structures (for example some countries have institutions such as Finance/Fiscal Commissions) will be needed to ensure an equitable sharing of national resources, as well as for ensuring smooth intergovernmental fiscal relations.

**2.4 Recommendations**

**Short Term**

1. Build Governorate management teams to handle transferred service delivery responsibilities, drawing on newly transferred service delivery ministry professionals and managers, and existing governorate staff.
2. Ensure that transferred service delivery units are coherent and complete organizational entities, capable of functioning effectively once reporting lines have been switched from Baghdad to the province. Ensure that arrangements are made for central ministry support activities to continue.
3. Large service delivery ministries, such as education and health, may need to be considered as special cases, and task forces established to plan for their transfer.
4. Staff numbers and payroll information should be verified before transferring staff to provincial government rolls, particularly if there is a risk of payroll fraud and/or other staff irregularities. The High Commission should ensure that accurate staff lists, grades and payroll information are transferred to the Governorates.

5. Decentralization will entail amalgamation of two separate planning systems — the PDPs prepared by the governorate planning departments and sector investment plans prepared by central ministries in the provinces. Existing governorate planning staff will need to be augmented by any provincial level central ministry staff transferred with their service delivery counterparts. The Ministry of Planning should work with provincial planning departments to clarify new planning processes, and upgrade planning manuals and procedures, as appropriate.

6. Governorates will need to expand the capacity of their budget units to cope with the preparation and execution of much larger annual budgets once the decentralization process gets under way. Treasury management will have to be greatly strengthened, and the financial management system automated, likely through an extension of the Integrated Financial Management Information System (IFMIS) project. Financial management regulations and procedures will have to be updated accordingly.

7. Governorates will also have to update their personnel management systems to accommodate a tenfold or more increase in employees. Critical issues for attention concern the accuracy of staff and payroll information for the newly acquired staff, and the transfer of their personnel files.

8. Decentralization will also entail the transfer and reconfiguration of records management systems, as well as physical assets and their accompanying registers.

9. Governorates will have to develop a change management plan to communicate the rationale and changes to both transferred and existing staff.

10. The technical capacities of the High Commission will need to be strengthened so as to enable them to provide the necessary technical and operational guidance to the central and subnational governments to navigate the decentralization process more effectively. The High Commission should in turn put in place a sustainable framework for capacity building at the Governorate level that will provide technical assistance and advisory support to operating units.

11. Other central management agencies, notably the Ministry of Finance and the Ministry of Planning (and the proposed new Civil Service Commission), will need to be actively involved in the decentralization process so that the transfer of functions now being identified become part of a more comprehensive decentralization strategy.

Medium Term

12. Provincial level accountability systems will need to be deepened and developed, with all budget submissions, execution reports, and end-year accounts published. Council capacity to scrutinize budget reports will similarly have to be enhanced.

13. Once there is clarity on roles, responsibilities and revenue flows, a Provincial Financial Management Law should be drafted covering principles of public financial management (PFM) standards, roles, responsibilities and accountabilities. These will also need to be harmonized with any changes made to the Federal Government Financial Management Law.

14. Design new suitable institutional structures for the equitable sharing of national revenues and for smooth intergovernmental fiscal relations.
3. STRENGTHENING FISCAL DECENTRALIZATION TO IMPROVE SERVICE DELIVERY BY THE GOVERNORATES

3.1 **Iraq is only just beginning its decentralization process and many of the necessary structures and systems are incomplete or nonexistent.** Although the government of Iraq has put in place several policy and procedural steps to begin the process of political and administrative decentralization, intergovernmental fiscal relations and service delivery remain highly centralized. By directing the devolution of functions from eight ministries to the Governorates, the 2013 amendments to Law 21 (of 2008) began a path toward what may ultimately become a meaningful devolution of authority.

3.2 **At present, Iraq’s form of decentralization is administrative decentralization, combining deconcentration and delegation with Constitutionally-established political decentralization and political accountability mechanisms.** This political decentralization is hampered in its effectiveness by the lack of pronounced and structured administrative and fiscal decentralization. The result is that the current Iraqi system is incapable of achieving the efficiency, effectiveness and accountability benefits promised by effective decentralization.

3.3 **In analyzing the Iraqi context, we consider the current state of decentralization to the Governorates within the context of important structural issues along four fiscal decentralization pillars: budget authority, expenditure assignment, revenue assignment and the intergovernmental transfer system.** The framework provided a comprehensive foundation for assessing the extent to which the Governorates have the authority and capacity to effectively meet the demands of their citizens, manage their budgets, allocate resources, and generate revenues. Each of these pillars is strongly connected to the others, so while every effort has been made to effectively follow these categories, the interconnected nature of effective fiscal decentralization results in some overlap.
3.1 Governorate Budget Authority – Status and Framework Issues

3.4 Effective service delivery, whether it is for roads, sanitation, education or health, requires budgetary authority. In order to achieve the efficiency, public responsiveness and public satisfaction gains of decentralization, authority must be exercised by an entity which balances local accountability to the population with accountability to regional and national objectives. Presently in Iraq, the Governorates, districts and sub-districts have extremely weak budgetary authority. Without the authority and mechanisms of local accountability, effective decentralization is not possible. Devolution of service delivery responsibilities is a vehicle for positive movement toward decentralization — but only if supporting structural elements are in place.

3.5 The Constitution (Article 122) states that provinces are to have independent finances. However, they are heavily dependent on the Central Government. Governorate finances consist of the “budget granted” to the Governorate by the central government as prepared by the Ministry of Finance and approved by the Council of Representatives. The Governorates also derive revenues from their own sources including from: (i) services it provides and returns from investment projects and revenues; (ii) duties; (iii) fines; (iv) donations and grants; and (v) sale and lease of property. The Governorate budgets (from the Republic budget) are transferred to the Governorates by the Ministry of Finance (after the Ministry subtracts strategic costs).

3.6 The total spending envelope for both the recurrent and investment budgets is negotiated between the Governorates and the Central Government, largely as a residual of ministerial spending plans. Its foundation is broadly guided by the population of the Governorate, a petro-dollar formula, and local revenue-sharing agreements between Governorates. The ultimate approval resides within the Ministry of Planning and the Ministry of Finance. However, the subnational governments can influence the Ministry of Finance and budget outcomes.

3.7 Governorates have virtually no expenditure authority related to the recurrent budget over functions operating within a particular Governorate. This is the case even for the 8 ministries that are undergoing decentralization. Functional spending in Iraq is dominated by social protection and defense. General public services including local ones amount to only 4.6 percent of budget expenditures. However, much of the ministerial spending within functions is directly delivered to local populations (see figure A3.1).
3.8 **Direct expenditure authority is highly concentrated.** Table A3.1 shows the level of expenditure authority exercised by the Governorates and Governorate Councils over their budgets as compared to total consolidated government spending in Iraq. Governorate spending is approximately 6 percent, with nearly all of that accounted by the Governor’s Office for general management. These budgets also require approval by the Ministry of Finance, resulting in severely limited discretion with respect to magnitude and control. Substantial Governorate capacity expansion will therefore be required.

3.9 **For the investment budget, the Ministry of Planning reviews and approves the list of investment projects proposed by each Governorate for funding approval by the Ministry of Finance.** The Governorate has the authority to plan, execute and approve disbursement of funds related to these Governorate priority projects (as approved by the Ministry of Planning and the Ministry of Finance). Subnational jurisdictions (Governorates) have a limited authority to reallocate across investment projects provided they remain within the approved budget limits.

3.10 **Exactly how the responsibility for devolved functions will be partitioned between the Central Government and Governorates is still evolving.** The current operating (recurrent) budget of the Governorates does not include the resources allocated to departments and offices of the central government ministries operating within the Governorate. Currently, the Governorates prepare the operating budget for their departments and assist the Council in preparation of the budget for Council operations. These are in turn presented to the Ministry of Finance. The Ministry then has final determination on staffing, wages and salaries. This entails quite limited actual service delivery activity, as most service spending is channeled through the ministries. Devolving functions stands to alter this arrangement.

3.11 **Intergovernmental asymmetry exists across regions in Iraq.** Fifteen Provinces function under a common intergovernmental structure which is more integrated with the central government. The three provinces in the KRG have status under the Constitution as a regional government. Asymmetry also exists within this structure at the sub-Governorate level. The current intergovernmental structure allows for asymmetry in the assignment of responsibilities across levels of local government. The Governorates have the authority to assign/delegate functions to districts and sub-districts based on local capacities and preferences.

3.12 **Governorates have discretion in programming and executing their investment budgets. However, these too require the approval by the Ministry of Planning and financing by the Ministry of Finance.** The limited budget authority of the Governorates over recurrent and investment spending is evident in a comparison of resource allocation across administrative entities. Governorates (outside of the KRG) accounted for only 5.3 percent of recurrent and capital expenditures in 2015 (see table A3.2).

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5 The Constitution permits any of the other fifteen governorates either singly or in self-selected groups to form regions, but none have done so to date.
6 Such asymmetry is appropriate in an environment of differing administrative and fiscal capacities. Assignments are tailored to meet those capacities.
7 There is a provision for additional discretion through the use of oil/gas revenue shares, however, projects are of limited scale. Additional discretion may be forthcoming for investment projects by self-financing devolved functions, but presently these are under ministerial control.
3.13 **Asymmetry is also factored into the developing model of devolved functions.** While ministries are establishing lists of functions to be devolved to the Governorates, the Governorates are not compelled to assume these responsibilities; they can be reassigned back to the central government. Given the differing fiscal/administrative capacities and levels of development across the nation, reassigning responsibilities back to the central government may be the preferred choice of some Governorates. This allows adaptation to the differing contextual issues within each Governorate.

3.14 **For Governorate officials to be reasonably accountable to local populations, they must possess actual budgetary decision-making authority, including authority over staffing.** While it seems that the Governorates have limited ability to propose new hiring of employees, such hiring must currently be within the budget allocation and consistent with the different line grades established by the Ministry of Finance. The ability to discipline service delivery staff is also presently lacking. The result is that staff function in a dual subordinate role to the ministries and the Governorates. As such, this staff is likely to be most responsive to the entity which controls their employment and compensation. Dual subordination produces uncertainty in lines of accountability and may reduce responsiveness to local authority. Reporting and supervisory relationships should be clearly established and reinforced through corresponding and personnel fiscal responsibilities.

**Expenditure Assignment**

3.15 **Governorate expenditure assignment is in flux.** The existing law provides for a subnational role in both shared service responsibility with the central government and specific areas of subnational authority. However, the details of this expenditure authority have not been established. Currently, responsibility is primarily shared. However, policy, budget development, financing and execution is dominated by the central government.\(^8\)

3.16 **At present, all Governorate expenditures (even for the office budgets of the Governor’s office and Governorate Council) are provided for through the central government budget, which is approved and monitored by the Ministry of Finance.** In general, despite the fact that a reliable census has not been completed since 1957,\(^9\) budget allocations are based primarily upon past spending, population and a petro-dollar formula. Budget execution is also tightly controlled across functions and economic articles. To the degree that past spending determines current allocations, disincentives exist for economizing. Beyond this, any resources that are unspent at the end of the fiscal year are then offset for future year allocations, encouraging spending.

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\(^8\) This is purported to be changing in the areas of devolved functions. However, ministries are still in the process of determining which functions will be assigned to the Governorates, and the formalities of budget authority over those services have not been established.

\(^9\) Population estimates were established by the United Nations in 2007 and by the official Government of Iraq in 2009.
3.17 **Law 21 (2008), the Law on Governorates not Incorporated into a Region, devolves responsibility for strategic direction and associated planning instruments to the Governorate Councils.** It further stipulates that budget allocations from the central government will support strategic plans. However, it does not give the Governorate Councils any leverage to influence planning and resource allocation by the line ministries through which the vast majority of services are provided. Subsequent amendments in 2010 and 2013 reinforced that authority, but did not make substantive changes.

3.18 **The Governorates have essentially no discretion for recurrent budget items financed through the Central Government budget.**\(^{10}\) Presently, this central control extends to the eight ministries that are currently devolving functions, but presumably will change with devolution of some of those functions. The Governorate investment budget is the only area where there is presently some discretion\(^ {11}\). The Governorate has the authority to approve the disbursement of funds related to investment projects, however these projects must be approved by the Ministry of Planning and Ministry of Finance.

3.19 **Budget execution within the Governorates is dominated by the Central Government through the direct provision of services by the line ministries.** The Governorates have only informal persuasive powers over these allocations. The Governorates have little ability to alter the mix of services, staffing or the mix of inputs (production function) for services provided\(^ {12}\).

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\(^{10}\) It is not uncommon for economic article spending to be heavily concentrated and controlled. In times of scarcity, the wage bill is often protected, further reducing discretionary spending. Concentration of expenditures within the personal services and social support articles (compensation for employees and social, pension and retirement benefits) has been growing over the last few years in Iraq. In 2015, it constituted approximately three-fourths of all spending (see table A3.3). This concentration is normally significantly higher for the Governorates (outside of the investment budget), and therefore more tightly constraining of expenditure flexibility at this level. However, because Governorate salaries and social benefits are largely paid through the central government budget, salaries are a smaller portion of Governorate budgets, particularly for those with oil revenue distributions (see tables A3.4 and A3.5). For the Najaf and Wasit Governorates, salaries and social benefits range from 20 to 40 percent of expenditures, while for Basra salaries and social benefits range from 16 to 20 percent (and salaries are less than 2 percent). For the Governorates, the largest categories of spending tend to be goods and services and non-recurrent, net acquisition of non-financial assets (capital investments). These proportions are a function of the highly constrained scope of Governorate budgets, rather than any indicator of enhanced flexibility.

\(^{11}\) Districts and sub-districts are even more constrained than the Governorates. However, they have some autonomy in making spending allocations between approved projects as long as they remain within the allocated budget limit for all projects.

\(^{12}\) The Ministry of Finance can allow reallocations of up to 5 percent of resources, but this is a ministerial function. For the Governorate and Council operating budgets, more discretion is available in budget development. However, these must still be approved by the Ministry of Finance, although they reflect a very small portion of spending. The Governorates have more discretion in staffing, within guidelines and maximums (positions and compensation) determined by the Ministry of Finance.
3.20 Coordinated investment planning is more developed than coordinated recurrent spending\(^{13}\). However, it is also not truly reflective of a decentralized process. Governorate projects must be approved by the Ministry of Planning and the Ministry of Finance as they are funded by central government resources, but administered at the Governorate level.\(^{14}\) The capital investment budget allocations for the Central Government, the Governorates and the KRG show that the bulk of spending comes directly from the central government budget (see table A2.2). For 2015, 88 percent of investment spending was directly controlled through the central government budget (excluding the KRG). Without the oil revenue share to the Governorates, the central government share would be 92 percent.

3.21 Given the scale of centralization of spending in Iraq and the scope of direct ministerial spending control in the Governorates, budget execution shortfalls in the Central Government have very significant consequences for Governorate level services. Table A3.2 shows past execution rates by ministry within Iraq. Execution rates between 25 and 70 percent have not been uncommon. Indications are that the situation may have even deteriorated in 2014. The inability to execute line ministry budgets has direct negative implications to the service recipients, government employees and suppliers in Governorates throughout Iraq. It also significantly impinges on local discretion and complicates accountability and local governing capacity.

3.22 The allocation and disbursement of budget resources for subnational governments (from central sources) have not been predictable in the recent past. Budgetary resources to subnational governments should be available and released as budgeted. Otherwise planning, prioritization, responsiveness, and management are defeated. The Ministry of Finance’s stated policy is to disburse a percentage of the investment budget for each of the Governorates at the beginning of the fiscal year and then make subsequent disbursements throughout the year, until the entire budgeted amount of funds has been disbursed. It appears, however, that these disbursements have frequently deviated from a fixed or predictable schedule. Recently, it has been the case that initial disbursements have been delayed until late in the second quarter of the fiscal year, seriously complicating project programming. This points to the need for more realistic budget planning processes, both at the center and for the provinces.

3.23 For the recurrent budget, disbursements (authorizations) are made monthly and based on cash availability. Since the warrant system is centralized within the control of the Ministry of Finance, potential overspending of cash is highly controlled. However, commitment controls are not as robust and the development of arrears can occur unchecked. This is a function of being unable to fulfill appropriations more than a function of ineffective line management. Also, the uncertainty of funds availability creates significant inefficiencies and potential service gaps. It is worth noting that in 2015, the Governorates did not receive the allocated resources for all economic articles that had been identified in the budget. This is a significant problem for a decentralized regime. Even if subnational jurisdictions had the ability to make spending decisions, such decisions would be hampered by an inability to adequately predict and depend upon fiscal transfers.

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13 As part of the investment planning process, the Governorate submits its five-year provincial development plan (PDP) to the Ministry of Planning for approval. The Governorate then, annually, compiles a prioritized project list (PPL) and submits it to the Ministry of Planning for individual project approval. Approved project lists are then submitted to the Ministry of Finance for recommended inclusion in the Central Government investment budget.

14 For Governorates with oil or gas production/refinement, the petro account allows for additional Governorate programming of investment spending. Similar investment supplements occur for provinces with irrigation programs.
3.24 **Revenue shortfalls or policy changes require mid-year expenditure adjustments.** It is common for such adjustments to be on an ad hoc basis rather than rationally determined. As noted, with regard to ministerial budget execution rates, overly optimistic revenue estimates have tended to necessitate mid-year budget retrenchment in past years. In decentralized structures, subnational jurisdictions are better able to identify critical needs. Presently, budget adjustments are controlled by the Ministry of Finance and stipulate reductions across functions and economic articles. The Governorates have very limited roles in ministerial execution adjustment. Further, the Governorates have more, but still limited, control over execution reallocations within their limited budgets. As table A3.6 shows, the need for adjustment during execution has been significant.\(^{15}\)

3.25 **Both recurrent and investment budget allocations lapse at the end of the year.** This produces perverse incentives to spend as much as possible within the year to avoid losing the allocation. This often results in expenditure choices that are driven by expediency rather than need, and could also generate perverse incentives in spending. To address these issues, giving more subnational control of expenditures at the margin, as well as putting in place medium-term budgeting and expenditure frameworks at the subnational level with the attendant PFM rules, could be considered. In times of resource deficiencies, however, budget cuts at the Governorate level are centrally managed by the Ministry of Finance. This lessens the effectiveness of the use of scarce resources by separating choice from local preferences.

### Revenue Assignment

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\(^{15}\) The Iraqi Federal Budget Act No. 2 of 2015 (the Budget Act) does make an attempt at improving fiscal management. One of the key provisions authorizes the Ministry of Finance to act as the central ledger for revenue and spending, while also requiring all Iraqi ministries to record and report all revenues realized and expenditures incurred. This is intended to improve the central response to cash flow difficulties. Additionally, exemptions on employee income taxes that have been in place since 2008 are likely to be repealed. New sales taxes on car purchases, transport, tickets, cellular phone SIM cards, the internet, and the sale of cigarettes and tobacco have been put in place to diversify the revenue base. The net effect may offset some of the losses incurred by decreasing oil prices. An alternative vehicle to smooth revenue fluctuations is an expansion in the size of the oil reserve. For subnational finance, it will be necessary to develop Governorate revenue sources. Furthermore, some of the extensions noted may have been better reserved as subnational instruments.
3.26 The current provisions for Governorate revenues are both inadequate and fragmented. Beyond shared proceeds from oil and gas production and refinement, in-bound airport fees, border entry duties and religious pilgrimage assessments, local revenue sources are fragmented and of low yield. Accountability and transparency can be enhanced by a subnational revenue system, which includes revenue instruments of sufficient yield and local discretion to command the attention of the population. The lack of access by the Governorates to significant broad-based revenue instruments impairs accountability\(^\text{16}\).

3.27 Governorates require meaningful source revenues of their own if decentralization is to be achieved. There are provisions that require revenue from local sources to be shared between the Governorates\(^\text{17}\). Structures which pool subnational, own-source collections for distribution to the Governorates defeat the purpose of own source revenues. They create serious disincentives for subnational revenue execution. Own-source, subnational revenue authority has been subject to differing interpretations. Despite these differing interpretations, certain Governorates have successfully developed some revenue from their own sources\(^\text{18}\).

3.28 Presently, Governorate revenue collections have little influence on resources allocated to Governorate service provision. This limits incentives for local revenue mobilization; however, some of this detrimental incentive is relieved to the degree that fees collected for self-financing services provide for increased local service levels.

\(^{16}\) Legal provisions for Governorate revenue have been evolving. However, by all accounts, these provisions require enabling regulation by the Central Government. This enabling regulation has not been forthcoming. Therefore, there is no provision for a level of local discretion in setting tax rates or bases needed to qualify as a local revenue source. The Governorates need discretion over the decision of whether to adopt a revenue instrument. They also require discretion to establish the rate and/or base of the instrument. While it appears that there may be more discretion for fees and charges (although even here, there is reference to approval by the ministries), there are no significant discretionary local revenue sources presently available to the Governorates.

\(^{17}\) The Governorates have a finance committee which is responsible for collecting both local revenues and (predominantly) central government revenues, and depositing these funds into central government accounts. The mandate for this committee and its specific roles and responsibilities are unclear. It will be important for own-source revenue capacity to be increased to support local choice.

\(^{18}\) While some Governorates have been able to establish local revenue sources, they are generally not able to alter the yield of these revenue sources as they must be centrally approved and are centrally assigned by the Ministry of Finance.
3.29  **Revenue authority shows a pattern which is even more concentrated within the Central Government than is expenditure authority.** Per capita Governorate revenues collected in Basra, Babel and Najaf equal less than one tenth of a percent of total per capita government revenue across the nation. In Babel, for 2014, it was less than 100th of a percent (see table A3.7). From a national perspective, Governorate own-source revenue is inconsequential. Without revenue authority, expenditure authority is rather meaningless. However, if as suggested above, the Governorates are provided authority over the revenues derived from self-funding services of the devolved function of ministries, this subnational revenue profile will change significantly.

3.30  **Law 130 (the Law of Municipality Revenues) of 1963 established the initial base of revenues to support provincial service delivery.** The initial revenue authority included fees, charges and fines. The defined base evolved to include new construction, slaughter houses, advertising, businesses, professional services, hotels and nightclubs, tobacco, alcohol and soft drinks. In most cases, revenue collection provided local resources, with exceptions for tobacco, matches, and alcohol. The Coalition Provisional Authority (2004) reconfirmed the local authority to impose taxes and fees.

3.31  **Article 44 of Law 21 (2008) provides additional subnational authority to collect revenue** for Governorate-provided services, from duties and fines (“in accordance with the Constitution and federal laws in force”), from donations and grants to Governorates, and from the sale (and lease) of movable or immovable property of the State. The 2013 amendments to this law allowed for fees on services and investment projects, including “taxes, fees and fines imposed by federal and local laws applicable in the Governorate.” These included: (i) the sale and lease of state-owned movable and immovable property; (ii) taxes imposed by the Governorate Council on companies to compensate for environmental pollution and infrastructure degradation; (iii) donations and gifts; (iv) one-half of border crossing fees/duties; (v) 5 dollars for each barrel of oil produced in the Governorate; (vi) 5 dollars for each barrel of oil refined; and (vii) 5 dollars for each 150 cubic meters of gas produced.

3.32  **Recent changes in the legal framework have impacted the local revenue mobilization of the Governorates.** The 2015 amendments expand revenue authority to fees for any service provided by the Governorate. The amendments reduced the local share of border crossing fees/duties to 25 percent. They also changed the tax on the per barrel of oil produced, per barrel of oil refined tax, and per 150 cubic meter of gas produced tax to 5 percent (of the market selling price, and excluded double counting of extraction and refining). They included a provision defining stated tax authority as the authority to impose local taxes (as regulated in law), fees and fines in accord with valid local laws. The objectives of the subnational governments may differ from that of the national government, so service pricing may interfere with national policy objectives. The local incentive may be to use service fees as instruments of revenue generation and care must be exercised to assure that the pursuit of that objective does not produce negative equity and efficiency outcomes. Still, the capacity for increased Governorate own-source financing is significant with the devolved functions.

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19 Self-financing services offer potential economic benefits through price signaling that is often difficult to achieve in the public sector. The difficulty is not simply due to the inability to levy charges. Rather, it is due to the need to establish a charge structure which appropriately covers the level of marginal benefit which accrues to the service recipient. For public services, this is often quite different from the cost of actually producing a service. One of the basic rationales for public provision of a service is the accrual of benefits to those other than the direct service recipient. In such circumstances, if the service recipient is faced with paying the full cost of providing the service, the level of aggregate consumption will be less than what is optimal from a social perspective.
3.33  **Law 10 of 2010, provided authority to the Najaf Governorate to impose a pilgrim’s tax.** As noted in the expenditure assignment section, the budget law of 2016 authorizes the Governorates to implement ministerial projects below 10 billion dinars, and to transfer the resources to the Governorate account. It also authorizes the Ministry of Finance to transfer the budget allocations of departments devoted to Governorates to the governorate accounts, along with employment grades and titles. In addition, it provides for the authority to impose tariffs and new service fees “according to the instructions produced by the minister or the governor or the head of entities not-related to the ministry” to cover approved budget expenditures of the entity.

3.34  **This framework provides less than specific revenue authority; what is provided is quite non-general and specific to oil-producing regions, regions with border activity and those (such as Najaf) with somewhat unique revenue bases.** It does not provide for specific broad-based access to local revenues. In fact, since the establishment of the Coalition Provincial Authority in 2004, each successive prime minister has refused to allow Governorate tax authority. In 2010, the Council of Ministers determined that Basra’s attempt to levy a surcharge on passports and identity cards was an extra-Constitutional act. The Constitution provides authority only on the condition that it is consistent with federal law. The Supreme Court has recognized local revenue authority. However, the execution of this authority is limited by specific enabling law. The result is quite inconsequential, own-source Governorate revenue (see table A3.8).

3.35  **The subnational revenue position is evolving quite slowly.** The 2010 budget law introduced derivation-based sharing for customs and in-bound air travel, as well as fixed distributions of oil production/refinement and natural gas production. Over time, additional authority has been added for fees and charges related to services or investment facilities providing services and budget allocations for evolved services (although this is not revenue), including changes to a fixed percentage for oil production/refinement and natural gas production. These are, however, narrow and volatile bases. The Governorates lack access to broad-based revenue sources, such as through derivation-based sharing of income taxes, excise taxes or consumption taxes. They also lack the ability to access broad-based taxes of their own (such as income, payroll, sales or property taxes in a manner in which they control the rate or definition of the base). Revenue options must generally be defined, authorized or approved from above.

3.36  **Revenue diversity is an issue throughout the Iraqi structure.** In recent years, oil revenue has ranged from over 95 percent of total revenue to approximately 85 percent for 2015 (see figure A3.2). Volatility must be managed through stabilization funds. Alternatively, volatility can be managed through diversification of revenue sources. Tax and other non-tax sources of revenue have grown significantly over the past three years (see figure A3.3). It is important to develop a tax payment infrastructure beyond oil as an element of moving to a more mature state. This is particularly important if local revenue bases are to be developed. Local access to revenue is enhanced by the central development of tax bases. Presently, effective non-oil national and local tax structures have not been developed.

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20 Most revenue collected by the Governorates is transferred to the Central Government (these collections are not shown in table A3.8). Central government revenue administration is supported by a Governorate unit’s administration of central government taxes. Quotas are established for expected levels of Governorate collection and revenues transferred to the central treasury are credited against these quotas.

21 The oil and natural gas basis has been made more volatile by pegging the distribution to a percent of the market price, rather than a fixed per unit distribution.
3.37 Capacity to collect local own-source revenue is lacking in the Governorates. The Governorates have tax collection responsibilities which are executed through the provincial finance committees. However, this authority is exercised under the supervision of the Central Government and is predominantly directed at collecting central government revenues. Fee and charge revenues are presently collected by the directorates for self-funded operations, and are deposited into Governorate accounts. A first step toward achieving revenue self-sufficiency is to establish an administrative unit capable of establishing and executing the evolving revenue authority accruing to the Governorates.

3.38 The dominant sources of Governorate revenues are unequally distributed across regions. The result is significant horizontal disparities in Governorate access to revenue. Reliance on such concentrated bases is an inferior foundation for basic subnational revenue authority. Ideally, the Governorates would be provided access to commonly found revenue bases related to their resident population and economic activity. Reliance on these bases would provide proper signaling to the government and population, and foster fiscal concern for proper stewardship and development of the economic capacity of the Governorate. The current reliance on narrow base components will require an increased use of transfers from the Central Government to compensate for the unequal access to revenue by the Governorates. This will occur at the same time as natural resource-endowed Governorates reap a windfall gain for the existence of a national asset at the expense of the national treasury.

3.2 Intergovernmental Transfers

3.39 The intergovernmental structure in Iraq is opaque and negotiated. Negotiated budgets not only open the door to soft budget constraints, but also foster uncertainty on the part of subnational jurisdictions. Subnational central government budget allocations and revenue distributions are subject to change from one year to the next, negatively impacting incentives. Resource certainty can be enhanced by fixed rules for subnational shared revenues and transfers, and by transparent mechanisms for establishing subnational budget allocations.

3.40 Article 121 of the Constitution states that “Regions and Governorates shall be allocated an equitable share of the national revenues sufficient to discharge their responsibilities and duties, but having regard to their resources, needs and the percentage of their population.” This Article provides the foundation for a stable sharing structure. However, such stability does not exist in the current system for Governorates outside of the Kurdistan Regional Government. Economic incentives for fiscal stewardship should be incorporated into the intergovernmental system to ensure that the “sufficient” criteria is not operationalized as a subjective, negotiated transfer.

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22 The expanded Article 44 also calls for the creation of a Department of Financial Affairs to organize the Governorate’s public budget, consistent with federal financial policy. The Department would be responsible for managing two separate bank accounts of the Governorate (one for investment and one for current expenditures), and for financial transfer of departments (devolved functions) in accordance with Article 45.

23 Oil/gas production and refinement, in-bound air traffic and border duties.

24 Natural resource extractions and border entry fees are generally regarded as poor sources of local revenue. They create windfall gains to subnational jurisdictions in manners unrelated to value-adding activities of local populations. Local derivation-based distributions from these sources should be limited to amounts needed to provide for required infrastructure to support natural resource extraction or border activities, as well as to offset pollution and/or congestion effects.
3.41 **For Governorates outside of the KRG, the transfer pool is a lump sum dedicated to investment projects.** The basis for the distribution is population and deprivation. It is used to fund the Governorate investment budget. This is augmented considerably for some Governorates through shared oil revenue transfers. The result is significant per capita variations in the level of investment resources across the Governorates (see table A3.9)

3.42 **Stability in an intergovernmental system requires concomitant stability and predictability in budget allocations.** There are wide variations in budget execution among the Governorates (figure A3.4). This is juxtaposed against the relatively stable budgetary environment of the KRG region. While this figure reflects only the limited Governorate budgets, it is likely indicative of ministry execution gaps as well. Stability and predictability is important for all regions if subnational Governorates are to effectively manage resources and provide services to the public.

3.43 **Fiscal transfers and allocations to provinces remain essentially ad hoc in nature.** Recurrent budgetary allocations serving local populations are driven by ministerial priorities and are negotiated as a component of the annual budget process. Transfers are implicitly purposeful because they are a consequence of approved spending. However, this is more reflective of a central budget process with deconcentrated administration than it is decentralization. Transfers for investment spending are driven by specific project approvals. However, this has little to do with the need for purposeful transfers. There are no systematically designed vertical or horizontal equalizing transfers. Furthermore, there are no service or project transfers intended to efficiently alter prices or create proper economic incentives.

3.44 **Both vertical and horizontal balance is missing in the Iraqi transfer framework.** Budget allocations to the Governorates are dependent upon the Ministry of Finance and negotiation. There is little discretionary revenue at the provincial level. Elements of derivation-based resource sharing exist in the form of per-barrel distributions from oil production, as well as for customs and in-bound air traffic. However, these are problematic candidates for such revenue sharing. Border regions should not benefit from entry into or out of a nation beyond that needed to accommodate border traffic and infrastructure. Likewise, natural resource endowments are generally better thought to convey national wealth. The result is significant horizontal disparities in Governorate access to revenue as identified in the discussion of revenue assignment. Intergovernmental transfers are essential for achieving both vertical and horizontal balance. Appropriately structured transfers are the essential bridge between expenditure responsibility and more limited revenue authority. The design of the transfer system is conditioned by both expenditure and revenue assignments.
### 3.3 Provincial Development Plans as a Vehicle for Decentralization

**3.45** A fully developed provincial development planning process would be a significant step forward in the decentralization process. However, there are several issues associated with the Provincial Development Plans that limit their present contribution to decentralization, and will need to be reformed. The most important factors are that they require the approval of the Ministry of Planning, and that their financing is determined by the Ministry of Finance. As such, they are quite limited in scope. Although they receive authorization by the Governor (and Governorate Council), their ultimate scale is controlled from above. These plans could however function as a catalyst to decentralization if they were to be/have: (i) fully determined and administered by the Governorates; (ii) financed by an independent, objective and stable financing source; (iii) integrated maintenance considerations; and (iv) provided Central Government shared financing for Central Government priorities. The PDP should be entirely determined by the Governorate, with complete awareness of financing and maintenance requirements.

**3.46** Natural resources revenues could be used to put in place an Annual Capital Grant for the Governorates that would provide them with resources on a predictable and transparent basis. As an illustration of its possible structure, this pool could be funded at a level of real resources in its first year that is equal to the entirety of budgeted resources for Governorate PDPs in the previous year. This would then be multiplied by 1.x (with x to be a positive number established based on fiscal projections of affordability). Negotiations would proceed with the High Commission, and revenues would be sufficient to ensure that each Governorate received an allocation in the budget year at least equal to the real level allocated in the current year. This pool should be allocated to each Governorate based on a formula to be determined (based on factors such as population, land area, need, and fiscal capacity). In addition, this formula should remain fixed and stable. The pool should be structured to grow on an annual basis by a fixed percentage until it reaches an agreed portion of total central government investment spending for the previous year. At that point, the share of natural resource taxes to the pool will be fixed, and Governorates will receive annual distributions from this fixed proportionate pool on a formula basis.

**3.47** Operations and maintenance expenditures should be adequately funded to ensure the sustainability of capital investments. Due to perverse incentives associated with a separation of capital and recurrent financing and attendant decision making, subnational jurisdictions should face the responsibility for maintaining facilities for which they make capital investment choices. As decentralization progresses, the Governorates should use a portion of their investment pool allocation for maintenance (without additional support from the Central Government), and maintenance expenditures should be included in project costs.
3.4 Devolving Functions as a Vehicle for Decentralization

3.48 Devolving the functions of the eight ministries has the potential to dramatically increase the budget authority of the Governorates. Ideally, this authority would be matched by revenue authority. However, because own-source revenue authority is not likely to emerge at the same rate as functions are devolved, there needs to be an alternative, objective vehicle to funding the Governorate takeover of these functions. This requires attention to assuring that effective incentives for Governorate efficiency and effectiveness are in place. It also requires a certainty of entitlement to a specific fixed allocation of resources for each function devolved. Indeed, this allocation should not be subject to negotiation or arbitrary alteration. Furthermore, each Governorate should be confident that: (i) it will receive the resources as specified and in a timely manner; and (ii) no additional negotiated resources for any function will be received to offset or augment the use of these resources beyond those received under fixed rules for unrelated and separately accountable purposes (such as for capital spending or maintenance)\(^\text{25}\).

3.49 Suitable institutional arrangements need to be put in place to establish the resource pool for transfers to the Governorates. The resource transfer pool for assumed functions is constituted separately from the pool for investments. However, it will largely come from the same source, namely, natural resources revenues. Getting this pool correct is a more complicated undertaking, as the scale of devolved functions will vary quarterly and across Governorates\(^\text{26}\). The evolving nature of devolved functions requires that the transfer system be dynamic, while also maintaining objectivity and certainty. At the same time, while transfers to governorates need to be rule driven and fair, they also need to be determined in a way that is consistent with the country’s overall macro-fiscal situation (currently very tight), and that take into account the resources needed by the federal government to fulfill its essential public functions.

3.50 Simultaneous to establishing the pool size, the allocation to individual Governorates must be determined. It is important that this allocation mechanism be fixed and stable to assure that Governorates face incentives for efficient service delivery. Article 106 of the Constitution calls for a public commission to examine federal revenues, and to ensure the appropriate sharing in various forms of these revenues among the federal government, the regions and the Governorates. One possible model is the Fiscal and Financial Commission in South Africa, which is designed to be an independent and unbiased constitutionally-mandated advisory institution\(^\text{27}\). It may be useful for Iraq to consider such an institution as a model because it is mandated to provide advice and recommendations on all financial and fiscal matters across all levels of government.

3.5 Recommendations

Short-Term Recommendations

1. Mechanisms of coordination (and control) are needed to ensure that the pursuit of local priorities by subnational jurisdictions does not exclude proper attention to national priorities. This generally requires that the national government retain responsibility for basic levels of redistributive programs or that it provide financing for basic levels of priority services. Fiscal incentives, created though a

\(^{25}\) In order for the Central Government to provide such objective budgetary support, there are three requirements: (i) establishment of a resource transfer pool; (ii) defining a formula for allocating resources from this pool to the Governorates to supply a function; and (iii) assuring minimum services.

\(^{26}\) For a more detailed discussion of challenges associated with resource sharing, see the ODI Draft Working Paper, International Experiences in Resource Revenue Sharing.

\(^{27}\) [http://www.ffc.co.za/](http://www.ffc.co.za/)
properly structured intergovernmental fiscal transfer system and mechanisms of shared service financing, function better in ensuring that national priorities are maintained at the same time that the subnational jurisdiction tailors spending to local preferences.

2. Local revenue mobilization needs to be strengthened. Specific steps in the short term could include the following:
   a. Clearly identify and define Governorate revenue authority in law and regulation.
   b. Establish a target for own-source revenue sufficiency.
   c. Assist the Governorates in mobilizing and managing local revenues by providing technical support services.
   d. Allow districts and sub-districts access to the most localized of revenue instruments (such as fees and service charges).

3. Design and implement an intergovernmental fiscal transfer system that is equitable and efficient, and takes into consideration the development needs of the Governorates. Transfer systems require a greater level of sophistication on the part of Central Governments, as well as attention to the implications of the economic incentives conveyed to subnational jurisdictions within the structure design. Likewise, they require the establishment of reporting requirements and mechanisms to assure that resources intended to support a particular function are indeed used in support of that function. This would require more elaborate analysis of the economic, fiscal and financial management systems both at the central and subnational levels, as well as more consultation and discussions with various stakeholders.

4. To achieve the greatest level of social welfare for a fixed level of resources, the Governorates must be allowed to make marginal budget reallocations both across functions and activities and between economic articles. At the same time, though, controls must be in place to ensure that the Governorates do not shift resources away from important categories of spending that would in turn essentially require that the Central Government step in to replace those resources. This will require a strengthened Governorate PFM system that includes both defined authority and systems of coordination between levels of government. It will also be necessary to establish a structure that assures the maintenance of national priorities within the context of local autonomy and that takes into account both the development needs of the Governorates, the residual functions of the federal government, and the country’s overall macro-fiscal situation.

5. Strengthen expenditure management in the Governorates through the following steps:
   a. Focus local expenditure authority on functions that have a direct benefit to local populations, and establish a model of further decentralization of authority to the district and sub-district levels as service benefits become more localized.
   b. Establish a detailed coordinating position between the Governorates and the ministries for the elements of devolved functions. There should be coordinated planning for recurrent and investment spending for which the Ministry of Finance and Ministry of Planning do not have veto authority over Governorate priorities. This can be eased through fiscal inducements whereby subnational jurisdictions also have significant revenue authority.
   c. Establish a target for Governorate control over expenditure functions and move progressively toward identifying and defining functions to satisfy that target. The present expenditure responsibility of the Governorates is approximately 5.3 percent. A reasonable target for a devolved structure needs to be progressively established, and should be based on local conditions and experiences.
d. Eliminate perverse incentives associated with lapsing and reduced budget allocations resulting from attempts to economize. Provide for objective means for financing functions.

e. Establish full expenditure authority over Governorate-assigned functions, including establishing priorities, programming the mix of production resources and controlling staffing and personnel decisions. To ensure that this is achieved, devolve staff along with their devolved functions. Authority should extend to any mid-year adjustment necessary to bring resource inputs and outputs back into balance.

6. The Governorates need to have control at the margins for the level of resources available to finance their budget. This will require local resources to be retained locally (and some level of national resources also be retained locally), and not returned to the central government, as currently is the case. The Governorates should have the ability to retain own source revenues to use on local priorities, otherwise all incentives for revenue mobilization are eliminated.

7. Stability and predictability of revenues, an ability to determine the overall budget envelope on the margin, and accountability to the population for the level and quality of services provided are vitally required.

8. The PDP should be entirely determined by the Governorate based on consultation with citizens, with complete awareness of financing and maintenance requirements.

9. Natural resource revenues should be used to put in place an Annual Capital Grant for Governorates. Due to the perverse incentives associated with a separation of maintenance and capital decision-making, subnational jurisdictions should face the responsibility for maintaining facilities for which they make capital investment choices.

10. Intergovernmental fiscal transfers should be transparent and predictable. A transparent structure for transferring budgetary resources to the Governorates is needed to ensure that resources are delivered as budgeted. The system must be continuously reevaluated, but its resource elements should be sufficiently stable to allow the appropriate economic incentive for efficiency, effectiveness and self-sufficiency to take effect. An often suggested period of stability is 5 years before any significant restructuring.

11. The Government of Iraq could draw lessons from the experience of similar countries that have gone through the process of fiscal decentralization. The two annexes to this report provide a brief introduction to international experiences in resource revenue sharing and fiscal decentralization. Building upon these, a longer term knowledge exchange program could be set up to help the Government of Iraq, its institutions and personnel to benefit from the knowledge and experience of other countries who have gone through similar circumstances.

3.6 Recommendations for the Medium Term

12. Article 106 of the Constitution calls for a public commission to examine federal revenues, and to ensure the appropriate sharing of various forms of these revenues among the federal government, the regions and the Governorates. One possible model is the Financial and Fiscal Commission in South Africa, which is designed to be an independent and unbiased Constitutionally-mandated advisory
institution. It may be useful for Iraq to consider such an institution as it is mandated to provide advice and recommendations on all financial and fiscal matters across all levels of government.

13. Minimum acceptable service standards need to be defined. The legal basis for Governorate expenditure authority needs to be firmly established as well. This would allow for the local jurisdiction to expand their expenditure portfolio consistent with the population’s desires to any field that does not conflict with national authority or national law.

14. Establish coordinating mechanisms to ensure that the exercise of subnational expenditure authority does not conflict with national objectives (national priorities and merit goods). Establish national (Central Government) roles for providing for the financing of services for which a national priority suggests there should be a minimum level of consumption or universal access. These characteristics do not negate Governorate provisions, but they require mechanisms of coordinated compliance between levels of government. The High Commission, in an expanded purview or recast as a Fiscal Commission, could aid in establishing proper mechanisms.

15. Given the complexity of the issues relating to fiscal decentralization, it would be useful to carry out a more detailed and comprehensive analytical work on fiscal decentralization that could provide recommendations for informing the long term strategy on decentralization.

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28 http://www.ffc.co.za/
4. PUBLIC FINANCIAL MANAGEMENT ASPECTS OF IMPROVING SERVICE DELIVERY BY THE GOVERNORATES

4.1 Key Challenges and Analysis

4.1  The Government of Iraq’s PFM system has typically focused on central government finances. Given the priority accorded to ensuring macroeconomic fiscal stability and the magnitude of central government revenues and expenditures, this is quite understandable. However, as funds are increasingly channeled through subnational government structures and decentralized financial arrangements, there is a need to improve PFM mechanisms which link central to subnational government structures. First, a key aspect of sound PFM is the management of intergovernmental financial systems, including accounting for intergovernmental financial flows linkages, managing subnational fiscal risks, and the monitoring and reporting of subnational revenues and expenditures. Second, the internal budgeting and financial management systems, as well as the procedures of subnational public administration structures should be viewed as part of the national PFM system.

4.2  The general budget cycle provides a logical reference point for the Ministry of Finance to analyze how PFM under fiscal decentralization arrangements should be integrated into an assessment (and possible subsequent reforms of decentralized administrative structures). In order to ensure efficiency and accountability, the government must clarify the respective roles, responsibilities and powers for each subnational jurisdiction. A major step in this direction is the devolution of functions from the 8 ministries, although the operational details are yet to be worked out. The management of governmental financial systems at the central government level (and, the internal PFM systems of subnational entities) should be reviewed and reformed as needed at each stage of the budget cycle, including planning and budgeting, budget implementation, budget monitoring, reporting, and audit and budget evaluation.

Current Status of PFM Systems in the Governorates

4.3  According to the provisions of Article (3) of Chapter 3 of the amended Law of the Ministry of Finance No (92) of 1981, the Ministry of Finance shall “(a) monitor and update the coding structure every three years as from the date of being published or whenever necessary; and, (b) distribute the structure across ministries, levels of government, independent agencies, and other departments.” The Iraqi budget coding structure is unified with Government Financial Statistics (GFS 2001) serving as the core of the coding classification structure. The budget coding structure captures all information pertaining to budget formulation, execution and reporting, together with enabling data for fiscal statistics and for statutory financial accounting.
4.4 The current chart of accounts includes administrative, economic, functional, geographical, and local coding. In order to enable a coordinated functioning of the PFM systems at the Governorate level with those at the central government level, the government financial chart of accounts and budget classification across the central and subnational government administrations should be reviewed and unified. Specifically, administration, location, and project segments may need to be revised. In addition, the economic budget and revenue classifications used by the central and subnational administrations must be aligned. Since a number of functions will be deconcentrated to the governorate and sub-governorate levels, it will be essential to ensure that appropriate user information be made readily available.

4.5 The availability of information about the utilization of all public financial resources at the subnational level is not adequate. Although the collection and consolidation of subnational government statistics is common in many countries with advanced PFM systems, the manual based system(s) currently found in the government of Iraq’s administrative structures may prove to be an overwhelming obstacle to effective consolidation. Systematic collection of subnational administration finance data requires consistency in the governmental financial chart of accounts and budget classifications across the central and subnational government administrations. In addition, the economic budget classifications and the revenue classifications used by the central and subnational administrations must be aligned.

4.6 No Treasury Single Account (TSA) is in place at either the national or the local governmental levels. Cash management is required to ensure that the government has sufficient cash available to meet its financial obligations as they fall due, and to invest temporary surpluses to generate interest income. However, these are not linked to the Ministry of Finance’s main TSA account with the Central Bank of Iraq. There is no mechanism in place to sweep/reverse sweep overnight balances held by budget units in various government bank accounts into a main TSA. Therefore, the Ministry of Finance does not obtain reliable information regarding the total amount of cash available to the government at any given point in time. When the Ministry of Finance is able to schedule it, cash operations need to move to a TSA structure at the Central Bank. The bank accounts of the federal government ministries and agencies, including the Governorates, are currently maintained with the state-owned commercial banks (particularly the Al Rashid and Al Rafidain banks). These accounts are used to receive Ministry of Finance cash releases and to make payments for budget expenditures.

4.7 At present, the Governorates’ recurrent and investment expenditures follow a complex hybrid structure of centrally-governed controls over expenditures versus devolved authority to from the central government to the Governorates. Recurrent expenditures for the governorate councils and the Governors’ offices and departments are fully managed by the Governorates, while investment budget expenditures are managed by the Governorates and the central government, depending on the nature of the expenditure. For instance, the Governorates are responsible for managing the investment budget under the provincial development, marshes revival, and poverty reduction programs. As central ministry functions are devolved, the magnitude of governorate management of recurrent expenditures will increase to many times their current responsibilities.

4.8 The Governorates maintain two bank accounts to receive the federal budget proceeds for recurrent and investment budget allocations. One account is used for recurrent expenditures (salaries, and operating costs) for governorate officials and staff only, and the other is used for investment projects under provincial development, marshes revival, and poverty reduction programs. The two accounts are replenished on a monthly basis by the Ministry of Finance, based on the request of the Governorates with the necessary supporting documents (Trial Balance [TB], schedule of payments, bank reconciliation and statements). See figure 1.
4.9 The Iraqi Ministry of Finance’s IFMIS System Requirement Study (2014) estimated that there are approximately 76,743 monthly transactions. The current most reliable figures detailing government transactions are provided in Table 2 below. Approximately, 48,109 transactions, or 62 percent of all transactions, are undertaken at the ministerial level, with the remaining 26,739, or 38 percent, provided at the Governorate level. The total volume of monthly transactions does not appear to be overwhelming in light of the size of the Iraqi public administration. As some functions are devolved from the national (Ministry) to the governorate level, the volume of transactions at the Governorate level should increase significantly. It is not clear whether there are appropriate financial and control systems at the governorate level which can easily accommodate an increase in the transaction processing volumes.
<table>
<thead>
<tr>
<th>Summary of Expenditure Transaction</th>
<th>Total Monthly Entries</th>
<th>Average Number of Daily Entries</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total of All Ministries</td>
<td>48,109 (62%)</td>
<td>2,187</td>
</tr>
<tr>
<td>Total of Governorate</td>
<td>26,739 (38%)</td>
<td>1,215.4</td>
</tr>
<tr>
<td>Overall Total</td>
<td>76,743</td>
<td>3,488.3</td>
</tr>
</tbody>
</table>


4.10 **Similar to all government agencies in Iraq, the Governorates follow the Law of Financial Administration and Public Debt No. 94, 2004, and the unified accounting bylaw issued in 2011 by the Iraqi Federal Board of Supreme Audit (FBSA).** The Governorates follow the cash basis of accounting by which resources and uses of funds are recorded when cash is received or when payments are made. The Governorates use manual-based accounting systems supported with Excel and Word applications to generate basic regular and ad hoc financial reports, such as trial balance, bank reconciliations, and monthly details of revenue and expenditures. Automated accounting systems are believed to reduce human error, and improve record keeping and reporting. The installation of such automated systems in Iraq would eventually lead to better decision making. Therefore, implementing an automated accounting system at the national and subnational government administration levels is a priority.

4.11 **A modern internal audit function is lacking in the public administration sector in Iraq (national and subnational).** The internal audit function, which is a vital part of a PFM system and core to a country’s accountability framework, appears to be fragmented and ineffective. The current scope of the internal audit function is similar to that of a financial controller, whereby ex-ante verification is performed by the internal audit department before payment is made to the beneficiaries. A risk-based approach is not applied to ensure that audit activities concentrate on areas of high or material risk. The internal audit function is almost exclusively restricted to the compliance and regularity of transactions. No system seems to be in place for distribution of the reports to concerned entities or the Audit Bureau. There is little evidence of follow-up on recommendations.

4.12 **The scope of the Inspector General’s Office (IGO) needs to be extended to the Governorates.** The IGO follows the Law of Inspector General issued by virtue of Order No. 57 of 2004, including its relevant instructions and orders that establish duties and responsibilities, confidentiality, reporting, professional standards, and quality assurance. Currently, IGOs exist only at the central governmental level. With the increased flow of resources and responsibilities to the Governorates, the role and functions of the IGO will assume critical importance in strengthening the oversight and accountability of governorate finances. Steps would need to be taken to enable internal audit functions at the governorate level, as well as to put in place regular IGO reviews at the governorate level once the additional powers and responsibilities are transferred from the central government to the Governorates.
4.13 The external audit function needs to be strengthened at the Governorate level. With the additional powers and resources that will be transferred to the Governorates, it will be important to strengthen the external audit function performed by the Federal Board of Supreme Audit (FBSA) to enhance the oversight and accountability of public spending. According to Article 2 of Law 31 (2011), “the Board shall carry out an extremely wide range of tasks, including: (i) Making an extensive mission of auditing the accounts and activities of all public bodies, including evaluating their performance and investigating all matters related to the efficient use of public money; and (ii) embarking on a mission to investigate corruption, fraud, waste, abuse and inefficiency in matters related to the receipt, disbursement and use of public money.” The audit is carried out by the audit commission teams that exist in all governmental entities (including the Governorates) and state-owned enterprises (SOEs). The scope and frequency of external audits by the FBSA should be extended to the Governorates, especially during the first years of devolution.

4.14 Officials need skills to procure construction services and inputs in a cost-effective and open manner. Such skills will be necessary to oversee appropriate implementation of projects and to ensure proper maintenance and servicing of the new infrastructure or buildings that have been completed. The principal findings with respect to subnational infrastructure development currently in Iraq include: (i) an inadequate knowledge at the subnational level as to how to develop, implement and integrate transparent project prioritization procedure(s); (ii) limited knowledge at subnational levels of government with respect to project financial analysis; and (iii) a lack of integration of recurrent and capital expenditures in not only prioritizing and understanding the full financial implications of the investment project, but also in integrating future operational, depreciation and maintenance expenses in the medium-to-long term budget forecasts.

4.15 At present, it does not appear that investment projects are reviewed as a total financial/economic package with capital outlays, future recurrent operating expenditures, and amortization and depreciation at the subnational level. Anecdotal evidence suggests that some projects may have been designed with inadequate budget space provided for the provision of operational costs. The investment and recurrent budgets of investment spending do not yet appear to be seamlessly integrated within the overall spending envelope. It is important that capital outlays and their respective operational expenses be integrated into the annual budget, the long-term capital investment plan, and the medium-term expenditure framework. Project feasibility evaluation should also be assigned to the entity with the best capacity to carry out this task.

4.16 Supporting these decentralized areas of public financial management may require developing different skills throughout the public administration service. For example, skills need to be developed in public sector accounting, as well as in designing, costing, and managing policy-determined budgets. These skills all necessitate a heavier investment in computerization and associated IT skills.

4.2 Recommendations

- The management of intergovernmental financial systems and the internal PFM systems of the subnational entities should be reviewed and reformed as needed at each stage of the budget cycle — including planning and budgeting, budget implementation, budget monitoring reporting, and audit and budget evaluation. It is recommended that a detailed assessment of the PFM systems and

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29 The FBSA covers all government bodies every year, and SOEs every three years.
processes at the governorate level be undertaken so that the current state of the system and its capacities can be analyzed, and attendant gaps and weaknesses identified.

- **The chart of accounts and budget classification across the central and subnational government administrations should be reviewed and synchronized.** In addition, the economic budget and revenue classifications used by the central and subnational administrations must be aligned.

- **The role of subnational government treasuries is currently limited to issuance of monthly limits, commitment controls, as well as payments for subnational governmental budget expenditures.** Current cash management practices (triaging payments) deliver effective cash outflow control. However, to some extent it undermines budget policies, adversely affecting suppliers and service delivery, and in some cases may lead to the amassing of arrears. Measures to establish, develop, and improve treasury operations are needed to better meet fiscal targets and support program service delivery. Such measures are also needed to gather better information for control and analysis purposes.

- **In order to improve the fiscal management of the Governorates, automation of financial management systems could be considered.** Hence it will be useful to consider including Governorates within the scope of any future and wider implementation of IFMIS currently about to be introduced at the Central Government level.

- **With the transfer of additional powers and resources to the Governorates, the external audit function performed by the FBSA should be strengthened to improve oversight of public expenditure management at the governorate level.** It is recommended that the scope and frequency of external audits by the FBSA also be extended to the Governorates.

- **Supporting these decentralized areas of public investment management may require the development of skills both at the Central Government and Governorate levels.** For example, skills will need to be developed for public investment project appraisal, project monitoring and evaluation, as well as for designing, costing, and managing policy-determined, medium-term budgets. Technical assistance should also be considered to develop a cadre of technical specialists at the governorate level that can provide project development, appraisal, financial analysis and planning expertise.

- **Multi-year investment and procurement plans have not been fully developed at the subnational level, thereby hindering the effective execution of multi-year investments.** As a result, linkages between procurement and investment planning are underdeveloped. As such, it is recommended that basic training be provided to Governorates on topics such as medium-term budgeting, development of capital investment planning, and project prioritization.

- **Project implementation guidelines should be developed and disseminated to subnational government entities.** Many countries provide concrete training and actions with respect to project development, project appraisal, project selection criteria, and project monitoring and evaluation.
5. DECENTRALIZATION OF MUNICIPAL SERVICES

5.1 Current Status, Issues and Recommendations

The government of Iraq is faced with significant challenges hampering its ability to provide citizens with reliable basic services, including municipal services. Although there are macro-level constraints (for example, political and macro-fiscal constraints), this section focuses on the current institutional and financing aspects of municipal service delivery, and the impact on service delivery as a result of the recent developments in decentralization of municipal services. As noted, in order to develop effective and efficient service delivery systems, there is a need to focus on building the institutional systems, ensuring the predictability of financing and developing sound accountability mechanisms. Although positive steps are being taken toward devolution of municipal services, they have yet to translate into improved service delivery.

The methodology of this review consists of in-country meetings with staff and a review of prior reports by the World Bank, donors, and the government. Staff included those from the Ministry of Municipalities and Public Works, the Ministry of Finance, the United States Agency for International Development (USAID) and the Taqadum and Tarabot projects, as well as staff and officials from the Salahaddin Governorate Council. Individuals included: Mr. Muhammed Muhsin Sayed, Director General of the Directorate of Regional and Local Development of the Ministry of Planning, and Mr. Torhan Almofty, Head of Provincial Coordination Secretariat in the Prime Minister’s Office. In-country consultants who gathered data from two Governorates also aided this effort.

The municipal, water and sanitation sector is governed by a complex institutional framework. It is predominately managed by two ministries, including (see Table 3) the Ministry of Water Resources and Irrigation, and the Ministry of Municipalities and Public Works. The Mayoralty of Baghdad has its own status and is empowered to prepare and implement plans for municipal and water projects. Coordination mechanisms connecting various ministries and subnational governance administration structures are not very well developed. Although the Ministry of Municipalities and Public Works is in charge of the planning and development of many of the subnational municipal, water and sanitation projects, the final approval for such projects is given by the Ministry of Planning, and by the Ministry of Finance for the budget.

30 Mr. Yalmaz Shahbaz Abbas, Deputy Minister and his technical team including General Director for Municipal Services, General Director for water, General Director for sewage.
31 Ms. Amal Badeea, Head of the Recurrent Budget section in the Budget Department in the Ministry of Finance, Ms. Layla Shalal, Head of the Decentralization section in the Accounts Department in the Ministry of Finance.
32 The Ministry of Municipalities and Public Works was created when the Ministry of Interior was subdivided by the Coalition Provisional Authority (Order Number 33 of September 9, 2003). Subsequently, this Ministry was merged with the Ministry of Construction and Housing to establish the current Ministry of Construction and Housing and Municipalities and Public Works. The Ministry is the national policymaker for the provision of all municipal services.
Table 3: Functional Responsibilities of the Municipal, Water and Sanitation Sector (excluding the KRG)

<table>
<thead>
<tr>
<th>Organization</th>
<th>Functions and Responsibilities</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Federal and Regional Level</strong></td>
<td></td>
</tr>
<tr>
<td>Council of Ministers</td>
<td>• The Council of Ministers is empowered to oversee the implementation of plans and policies.</td>
</tr>
<tr>
<td>Ministry of Water Resources and Irrigation</td>
<td>• Water planning and allocation; operation and maintenance for bulk water, flood control and mitigation.</td>
</tr>
<tr>
<td></td>
<td>• Water source quality, standards and monitoring of ground and surface water.</td>
</tr>
<tr>
<td>Ministry of Municipalities and Public Works</td>
<td>• Planning and implementation of water and wastewater projects in 15 Governorates (outside of Baghdad and the KRG)</td>
</tr>
<tr>
<td></td>
<td>• Water/wastewater quality monitoring and establishment of technical standards.</td>
</tr>
<tr>
<td><strong>Governorates</strong></td>
<td></td>
</tr>
<tr>
<td>Governorates</td>
<td>• Propose projects and set allocations for the implementation of projects.</td>
</tr>
<tr>
<td></td>
<td>• For Governorates not incorporated into the region, the Governorate council can issue local laws.</td>
</tr>
<tr>
<td>Municipalities</td>
<td>• Develop and manage water projects on its own or jointly with other municipalities.</td>
</tr>
<tr>
<td></td>
<td>• Exclusive right for sale of raw/treated water in the municipality.</td>
</tr>
<tr>
<td>District and Sub-district (water and sanitation department)</td>
<td>• Operation and maintenance of water and waste treatment facilities.</td>
</tr>
</tbody>
</table>


5.3 **The organization of the State in the level below the Governorate is very weak.** The reference to Municipalities in Iraq is different from the standard use of the term in other countries where it connotes an elected third tier of the State. However, in Iraq “Municipalities” are the deconcentrated arm of the Ministry of Municipalities. This is a common misconception in Iraq that the districts (qada’as) are sometimes translated as municipalities with a territorial and political connotation, and with service delivery authority. This is confounded by the Municipalities Directorates of the Ministry of Housing and Municipalities that are in fact service delivering entities (water, sewers, drainage, streets, roads, etc.) which are responsible for overseeing the network of 265 Municipalities. These Directorates are being devolved from the central Government to the Governorates, which in fact will transfer the service delivery functions from the line Ministry to the Governorates. The Directorates have departments in the Qadas and Offices in the sub-districts (nahiya). There are district administrators (qaim al qam) and sub-district administrators (mudiyar nahiya). In some Governorates, the Governorates have actually organized elections for those offices at least at the district level. In others, they are appointed. Law 21 specifies elected councils who then appoint the executive at those two lower levels, but nationally the provision has never been implemented. Municipality Directorates have budget allocations from the central Government, while municipalities have a mix of own revenues and grants from the Ministry of Finance. It is estimated that about 40,000 employees work in the Ministry of Municipalities and Public Works, with more than 90 percent of its staff based in the Governorates.

5.4 **The structure of the Ministry of Municipalities and Public Works includes five directorates with the following responsibilities:**
I. **The General Directorate of Municipalities.** Service delivery is done through a network of Municipalities (also known as Municipal Institutions) in the Governorates/Districts for core services including: land development engineering; construction, diversion, maintenance and improvement of streets, intersections, bridges, and sidewalks; street cleaning, garbage collection; traffic control; and construction of service facilities (markets, stores, public parks, and garages). Service delivery also includes the provision of construction permits, and the allocation of land for commercial, industrial, and housing purposes. Municipal institutions own and manage properties throughout the Governorates, and lease them to others based on Law (32) of the year 1986 for the sale and lease of public assets, as amended.

II. **The General Directorate of Water** is responsible for making available safe water for drinking for all Governorates except for the Mayoralty of Baghdad. It is also responsible for implementing, managing and maintaining water projects for reconstruction and maintenance of water networks.

III. **The General Directorate of Sewage** is responsible for implementing, managing, and maintaining sewerage projects and associated networks.

IV. **The General Directorate of Urban Planning** is responsible for preparing: city plans, designs and urban studies; structural designs for governorates based on development indicators and natural and human resources available in each area; and rural and urban development studies.

V. **The General Directorate of Planning and Monitoring** is responsible for monitoring and follow up for implementation of plans, and preparing regular monitoring reports. It also monitors the implementation of construction projects, and prepares annual and strategic plans.

5.5 **The Directorates of the Ministry of Municipalities and Public Works in the Governorates have collaborate closely with the Governorate and reports officially to the Ministry of Municipalities.** This relationship is changing with the devolution process as the directorates will report directly to the Governorate. The relationship with the line Ministry is still not clear. The Directorates core budget comes from the Ministry (both recurrent and sector investment). They also collaborate with the Governorates for the implementation of the investment budget allocated for the Accelerated Regional Development Program (ARDP). This has contributed to weak accountability and poor service delivery. To implement its investment budget, the Directorates and Municipalities have the option of contracting private service providers or using their own staff (temporary and/or permanent) to deliver services.

5.6 **The municipal, water and sanitation sector is highly centralized.** In terms of investment spending, the approval and funding of projects are highly dependent on the approval of the Ministry of Planning (for project planning approval) and the Ministry of Finance (to ensure that the project fits within the budget envelope). According to the General Director of Water in the Ministry of Municipalities and Public Works, there are currently no water/sanitation utilities in charge of service delivery, and the operation and maintenance of water/sanitation services is largely the responsibility of the various directorates in the sector ministries. The Iraqi public administration system, as it pertains to the municipal, water and sanitation sector, does not allow for any autonomy in decision-making at the subnational level.
5.7 **The financing and flow of funds for municipal services follows a hybrid structure** in which the budget is controlled centrally by the Ministry of Municipalities and Public Works, which is in turn responsible for preparing annual budget plans in coordination with the Ministry of Finance and the Ministry of Planning. In addition, budget execution for authorized recurrent and investment expenditures is done at the level of the Directorates/Municipalities, as they receive their approved budget (released periodically by the Ministry of Finance) directly into their bank accounts at the district level. Budget allocation for municipal services depends on the Ministry’s negotiation with the Ministry of Finance, with little discretion at the municipal level. Recurrent budgetary allocations for municipalities are driven by the line ministry’s priorities and negotiated as part of the annual budget process. Directorates and municipalities maintain records of expenditures which are then reconciled with the Ministry of Finance for replenishment of the bank accounts up to their approved budget.

5.8 **The flow of resources to municipalities for the investment and recurrent budgets does not provide discretion and flexibility to municipalities** to reflect their local priorities in the preparation and execution of their annual work programs as these remain a central function. This affects municipalities and Governorates in effectively addressing local service delivery priorities and in achieving the desired accountability structure. A transparent and timely flow of funds is required for the municipalities to operate effectively.

5.9 **Revenue collection for services rendered at the Municipality level is done by the Municipalities/Directorates.** However, local revenues are limited. Municipalities and Directorates of the Ministry of Municipalities and Public Works in Iraq are directly responsible for a range of public services for which fees collected do not cover the cost of providing the services (for example, water), or for which fees are normally not charged, such as local street maintenance and lighting. These are normally funded from local revenues or intergovernmental transfers. Currently, there is no apparent relationship between the costs to provide and deliver services and local revenues generated from local fees or taxes. Further, collection efforts on fees in place are poor at best. A realistic assessment of the cost of the delivery of water services and the financing gap in water service delivery could provide an opportunity for local governments to collect revenues. Currently, the financing gap is covered through the government budget which provides no incentives for the municipalities to collect revenues, and allows for poor accountability for services. Although fees charged by the water and sewer directorates are very low, this does not mean that consumers do not pay extra/more for water. Consumers incur costs to deal with the intermittent supplies that are often of poor quality through private purchase, water fetching, pumping, and other means to supplement their piped water supplies. This blanket subsidization of water is costly and hinders progress in the sector, while providing incentives to use excessive volumes of water.

5.10 **Financial management systems in Governorates are basic** (that is, paper and spreadsheet based), which may be adequate for limited operations. However, with the devolution of functions and plans to increase local autonomy, there will be a need to strengthen financial management at the Governorates level. This will include installing automated systems to manage key financial management functions such as record keeping, reporting, billing, collection, enhanced internal controls, and so on. The present efforts to introduce the Integrated Financial Management Systems (IFMIS) at the central government level should consider the possibility of rolling out such systems over time to the Governorates in the future and therefore build flexibilities into the design of the system.
Accountability to citizens is weak. While this review did not include a detailed examination of the current status of citizen engagement in the budget process, it is important to highlight that one of the fundamental problems in Iraq is that the institutions lack accountability mechanisms with citizens. As such, the citizenry are unable to obtain information, voice demands, and/or influence policy makers and public servants through formal channels. A related issue is the lack of professionalism in the civil service as a result of appointments made based on connections rather than merit. As a result, it is quite possible that the professional ethics that in other countries underpin good service delivery may be weak and may need to be reinforced.

5.2 Status of Progress toward Devolution of Municipal Functions

The Ministry of Municipalities and Public Works has been one of the first Ministries to devolve powers and functions to the Governorates. Municipal and Water Services is one of the eight sector ministries to be devolved to the Governorates in accordance with Law 19 (2013). To expedite the implementation of Law 19, the Council of Ministers issued Decree Number 304 on August 4, 2015 requiring sector ministries to form working committees to complete the transfer of authorities within three months ending on November 5, 2015. The Council’s Decree provided for a phased approach so that some authorities would be transferred within the next six months, other would transfer after one year or more, while the non-transferred authorities would remain in the line ministries.

One hundred and sixty-three functions were formally transferred in September 2015 after the issuance of Decree Number; 107 functions were retained within the Ministry. The Minister of Construction and Housing and Municipalities and Public Works officially announced the functions devolved to the Governorates. This decree came after the Ministry officials collaborated with representatives from the Governorates and discussed the implementation mechanisms for Provision 45 of Law 19 of year 2013 and in accordance with the Council of Ministers’ Decree Number 304 of August 5, 2015. The process of determining which functions to devolve was done in close coordination and with the support of a USAID Governance Strengthening Project/Taqadum, which worked with seven provinces and three out of the eight Ministries targeted for devolution, Ministry of Municipalities and Public Works, Ministry of Health and Ministry of Education.

One hundred and seven functions were retained within the Ministry. Some of the functions retained by the Ministry include managing ongoing contracts already signed with the ministry, while providing the Governor’s office with monthly progress and financial reports; and managing loans and grants externally financed by donors such as the World Bank and the Japan International Cooperation Agency with the Project Implementation Unit at the Ministry.
5.15 Seventeen contentious functions remain to be determined. The perception of capacity at the Governorate level varies. Their readiness to immediately take over all of the functions will require detailed assessments and capacity building. The current approach of gradual devolution of functions appears to be reasonable. However, it has caused conflict because the Governorates believe that they already have adequate capacity. One key contentious issue concerns appointing, transferring, and firing the General Directors of the Ministry in each of the Governorates. The Ministry is concerned with immediate changes to the General Directors for political reasons if the Governorates have such authority. Furthermore, the Ministry will retain the functions of planning and policies, so retaining the same Director Generals is perceived to be important to the Ministry to safeguard capacity. The Ministry proposed a solution to resolve this issue which is to have the Governors nominate three individuals and send the names to the council members of the Governorate to select one name. This name would then be submitted to the Minister who would have 15 days to accept or reject the nominated person. Another contentious issue is the training and evaluation of staff. It was agreed to keep this function within the Ministry for one year only.

5.16 Implementation of the transfer of functions has started and the following mechanisms were agreed upon: (i) delivery and receipt of movable and immovable property; (ii) delivery of the staff database and inventory of employees' salaries; (iii) completion of the implementation of ongoing Ministry contractual projects; (iv) transfer of knowledge and expertise from the ministry to the provinces, and provision for capacity building for the staff of sub-directorates in the provinces to support the implementation of the functions that will be successfully transferred; and (v) implementation of the Ministry’s planning and public policy in coordination with the provinces. The deconcentrated structure of the Ministry helped in the implementation of the transition to a decentralized structure, as some of the functions devolved to the Governorates were in the past delegated to them by the Ministry. The Ministry expects to continue providing the Governorates with technical assistance, and may assume some of the devolved functions if the Governorates ask them to do so.

5.17 The process of transferring employees is underway. There is a need to agree on the mechanism to transfer the database for employees and take stock of and transfer their salaries as well. An official report of the information will be shared with the Governorates to take record of such information and compare it with the branch directorates for endorsement and usage. It was also agreed to take an inventory of transferable and nontransferable assets and deliver the inventory report to the committees represented by the Governor’s office. The Ministry issued instructions to carry out an inventory of all assets, names of employees and their salaries in order to prepare for transferring them to the Governorates.

5.3 Issues Affecting the Effective and Accountable Delivery of Municipal Services

5.18 While Municipalities have had years of experience providing local services, the quality and quantity of such services have been limited. The following section highlights some of the key factors impacting the delivery of municipal services.
5.19  A systematic approach to establishing adequate institutional, fiscal and accountability arrangements is currently lacking in Iraq, thereby hindering the government’s ability to improve service delivery. The legal framework provides the Governorates with the authority to manage service delivery for the devolved ministries, but fiscal and institutional arrangements have yet to reflect the same. While citizen expectations of municipal service delivery are high, the devolution process was not done based on a strategic approach. Rather, it was implemented with random steps and poor communication with all stakeholders.

5.20  Other concerns include a lack of a sound fiscal transfer system, and unclear reporting and accountability relationships between the Municipalities with citizens, Governorates, and the Ministry of Municipalities and Public Works. There is a need for clear guidelines for reporting and accountability relationships of staff in the Municipalities with officials in the Governorates and with the line ministry. Although Iraq has achieved a significant level of political decentralization as evidenced by the election of the governorate councils which started in 2005 and continues to date, elections have not been held at the municipality level. Furthermore, formal mechanisms and structures are lacking for local demands for municipal and local services. The devolution of municipal functions was contentious in a number of areas, including the function of appointing and removing General Directors. In order for the devolution of municipal functions to be successful, the Municipalities must have a clear structure, and reporting and accountability arrangements.

5.21  A clear and transparent system for a predictable flow of funds to the Governorates, districts and municipalities for delivering municipal services is lacking. Currently, the activities of the Ministry of Municipal Services are financed mainly through the investment budget, and reconstruction of regions and Governorates, with the latter being allocated and implemented by the Governorates. The 2016 budget has not transferred the investment budget for municipal services to the Governorates. Also, the Governorates do not have a system for transferring municipalities’ budget.

5.22  Greater coordination in the municipal and water/sanitation sector between national and provincial planning processes and the annual budget formulation process is necessary to improve service delivery. The Governorates need to be included in the decision-making process. Technical assistance should be introduced to harmonize budget procedures, and to align procurement, disbursement, and project monitoring procedures. Technical assistance should also be supported to introduce a transparent project selection, gate-keeping (filtering) system, so that selected projects can more readily dovetail into the National Development Plan.

5.23  The institutional arrangements required with the transition from a central to a decentralized structure remains a work in progress. There is a need to reevaluate the roles and responsibilities of staff, identify capacity gaps and develop a new institutional structure for the Governorates. The new governorate structure is under preparation by the Governorates. It will be reviewed by the provincial council and then submitted to the Council of Ministers and the Council of Representatives. (The Institutional Implications Chapter elaborates further on the details related to institutional challenges and recommendations.)
The devolution of municipal functions to the Governorates will increase pressure on officials to improve service delivery. However, there has been limited attention to the institutional arrangements required to improve service delivery especially the management capacity at the Governorate level. The Governorates do not foresee the need to build technical sectoral capacity due to the current deconcentrated structure of municipalities, which upon devolution will be reporting directly to the Governor. A detailed capacity assessment of the Governorates is required to assess the current capacities and validate management constraints, which will increase as the Governorates assume the newly devolved functions. The key initial needs will likely be in the capacity to manage the planning function, public financial management systems, and human resources. In addition, sound accountability and audit arrangements will be required to ensure the efficient use of funds.

5.4 Recommendations for Strengthening Municipal Service Delivery

Putting in place a transparent and predictable flow of resources to Municipalities will improve service delivery. An annual Capital Grant Scheme that provides municipalities with resources in a predictable and transparent manner is needed to improve local service delivery. The Provincial Development Plan (PDP) shall be strengthened and used to address local demands for municipal services. It can enhance local discretion and authority, provide transparent and predictable financing for municipal services, and afford flexibility to address fluid local demands in a timely manner.

Reorganize the Ministry of Municipalities and Public Works to shift its focus away from project implementation toward management of national policies and strategic plans. The Ministry will also need to support the Governorates with appropriate institutional and financial arrangements to deliver services. In addition, support will be needed for the development of revised institutional arrangements for the Governorates to enable them to manage the newly added functions, including municipal services.

Strengthening budget execution at the municipal level is necessary to enhance the efficiency of public spending. The subnational public administration should be strengthened to: (i) ensure that disbursement activities can be properly implemented to minimize project implementation delays; (ii) ensure that the internal audit function is fully operational; and (iii) develop basic public financial management systems (accounting, reporting, and auditing and monitoring systems) so that projects can be tracked through the full project cycle. Capacity building of staff is best strengthened through on-the-job training (that is, learning by doing), and complemented by technical training courses in the areas of planning, budgeting, accounting, cash management, internal controls, and human resource management. (Please refer to chapter 4 for a related discussion on capacity building of PFM systems at the governorate level).

An institutional and financial assessment of the systems and capacities of Governorates to deliver municipal services could be useful in order to document the baseline levels, and to develop a comprehensive capacity building plan with the objective of strengthening subnational government systems. An institutional assessment of the systems and capacities can be useful obtain a comprehensive baseline understanding of the strengths and weaknesses of public sector management practices at the local levels. Such assessments are a useful and common approach used by governments to improve its performance and enhance the delivery of municipal services and accountability to citizens, as well as to build strong partnerships with key stakeholders including central government agencies.
REFERENCES


56


______.2010.”Intergovernmental Fiscal Management in Iraq: Challenges and Options for a Petroleum-Dependent Economy.”


ANNEXES

A. International Experience in Fiscal Decentralization

B. Good Practices in Resource Revenue Sharing
Table A2.1: Constitutional, Statutory and Other Legal and Regulatory Instruments Key to Decentralization in Iraq

<table>
<thead>
<tr>
<th>Legal - Regulatory Precedent</th>
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</tr>
</thead>
</table>
| **Law 130 (“Law of Municipality’s Revenues”), 1963** | **Fiscal and Financial Management**  
- The purpose was to identify, collect, and enforce a variety of revenues in the provinces to support a service delivery base.  
- Includes fees, charges and fines.  
- New construction, slaughter houses, advertising, businesses, professional services, hotels and nightclubs, tobacco, alcohol, and soft drinks may be subject to this law.  
- Revenues collected in the province remained in the province with few exceptions (for example, tobacco, matches, alcohol, soft drinks and auctions).  
- Comprehensive nature of the law, with its administrative components, could offer a framework for revenue collection structures for subnational government structures. |

| **Iraq Financial Management Law, 2004** | **Fiscal and Financial Management**  
- This law regulates the arrangements governing the preparation, adoption, recording, management, execution and reporting of the federal budget and related issues including public borrowings, guarantees, internal controls, accounting and auditing.  
- **Section 9, Clause 8:** Permits the virement of funds: no more than 5 percent of funds can be vired; inter-spending unit transfers are not permitted; virement source and destination accounts must be in the same budget category. |

| **Transitional Administrative Law (TAL), 2004**<sup>33</sup> | **Political Decentralization**  
- **Article 4** establishes that the system of government in Iraq shall be republican, federal, democratic, and pluralistic, and powers shall be shared between the federal and regional governments, governorates, municipalities, and local administrations.  
- **Article 55:** Governorates have the right to form a Governorate Council, name a Governor, and form municipal and local councils. |

| **Coalition Provisional Authority (CPA) Order 71, 2004**<sup>34</sup> | **Political Decentralization**  
- **Section 2** gives the power to the Governorate Council to appoint the governor (and similarly district and sub-district councils to appoint the executive at those levels), subordinating the Governor to the Council.  
- Councils were authorized to approve or veto appointments of Directors General and other senior local ministerial officials in the Governorate.  
- Set the direction for the authority of the Governorate in the appointment of senior ministry officials in the Governorate.  
- **Fiscal Decentralization**  
- Set the direction for the authority to impose taxes and fees.  
- **Service Delivery Decentralization**  
- Set the direction for:  
  - the authority to review and revise central ministry projects within the governorate;  
  - the authority to monitor public service provision by the central ministries in the provinces; and  
  - the authority to plan and execute projects independent of central ministries. |

| **Iraqi Constitution, Political Decentralization** |  |

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<sup>34</sup> Coalition Provisional Authority Order Number 71: Local Government Powers. [www.iraqcoalition.org/regulations](http://www.iraqcoalition.org/regulations). All references to Order 71 are to this source.
### Table A2.1: Constitutional, Statutory and Other Legal and Regulatory Instruments Key to Decentralization in Iraq

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</table>
| **2005**<sup>35</sup>       | - The Constitution affirms a federal structure with locally elected councils who in turn select the local executive authority – the Governor in the case of Governorates.  
- Article 114 leaves to the central legislative authority to further specify the limits of local government authority, the responsibilities carried out exclusively by local officials, and the responsibilities carried out in coordination with central government ministries.  
- Article 115 provides support for a broader interpretation of the powers and authority of regions and governorates not incorporated into the regions. All powers not stipulated in the exclusive powers of the federal government belong to the authorities of the regions and governorates that are not organized in a region.  
- Article 116 provides that the federal system in the Republic of Iraq is made up of a decentralized capital, regions and governorates, as well as local administrations.  
- Article 122 specifies that governorates are to have broad administrative and financial authorities to enable them to manage their affairs in accordance with the principle of decentralized administration. |
| **Law 21, 2008**<sup>36</sup> (“The Law of Governorates not Incorporated into a Region”) | - Article 62 empowers the Council of Representatives (CoR) to approve the general budget; and authorizes the CoR to submit and close the accounts for approval.  
- Article 106 describes the formation of a public commission composed of officials and experts from the federal government, regions and governorates “to audit and appropriate federal revenues.” Responsibilities of this commission include assuring a fair and equitable distribution of grants and other funds from outside Iraq, and to guarantee that federal funds are appropriated to the regions and governorates in agreement with established percentages.  
- Article 112 assigns the responsibility to manage the exploitation of oil and gas to the federal government, and the producing regions and governorates. The article also assigns to the federal government the responsibility to distribute the revenues from oil and gas proportionate to population. |

### Fiscal Decentralization

- Article 31.1: Governors prepare the governorates’ general budget (the

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<sup>36</sup> (2008). Law of Governorates not Incorporated into a Region: An Annotated Text. USAID and RTI International. Research Triangle Park, NC. All references to the original Law 21 are to this source.
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<th>Key Decentralization Provisions</th>
</tr>
</thead>
<tbody>
<tr>
<td>administrative units and offices of the governorate, not including the budgets of federal line ministries providing services) and submit them to the Governorate Council.</td>
<td></td>
</tr>
<tr>
<td><strong>Article 7.5:</strong> The Council approves the draft general budget and submits it to the federal Ministry of Finance to “ensure its uniformity with the federal budget.” The general budget also includes the administrative units and offices of the governorate at the district and sub-district levels. Subsequent amendments to Law 21 made no changes to this provision.</td>
<td></td>
</tr>
<tr>
<td><strong>Article 44:</strong> Provides for local revenue generation authority to be devolved to the provinces. Hence, this Article provides for the transfer of fiscal authority (both legislatively and administratively).</td>
<td></td>
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<tr>
<td>o Provides for federal budget allocations</td>
<td></td>
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<tr>
<td>o Generation of revenues in the provinces, and</td>
<td></td>
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<tr>
<td>o Authority of local decision-makers to allocate funding within provinces.</td>
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<tr>
<td><strong>Service Delivery Decentralization</strong></td>
<td></td>
</tr>
<tr>
<td><strong>Article 7.4:</strong> This provision, through the initiative at the governorate level and subsequently accepted through incorporation into the Five Year National Development Plan, enables the governorates to prepare investment plans and to execute projects within the governorate.</td>
<td></td>
</tr>
<tr>
<td><strong>Article 7.15:</strong> Formalized what governorates had already asserted, and accepted by central authorities, mainly the Ministry of Planning and National Development and the Ministry of Finance – the preparation of development strategies and investment plans, and the implementation of investment projects within the governorate.</td>
<td></td>
</tr>
<tr>
<td><strong>Political Decentralization</strong></td>
<td></td>
</tr>
<tr>
<td>Reducing the time period in which council members who have been removed can appeal their removal (Law 21, Article 6.2, as amended by Law 15 of 2010).</td>
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</tr>
<tr>
<td>Changing the jurisdiction for a governor to challenge his removal from the Federal Supreme Court (Law 21, Article 7.8, as amended by Law 15, 2010).</td>
<td></td>
</tr>
<tr>
<td>Clarifying, both by the abrogation of CPA Order 71, and by replacing the language in Article 55 (Law 21) with new language making it clear that the Law on Governorates applies not only to governorate councils and their appointees but also to district and sub-district councils.</td>
<td></td>
</tr>
<tr>
<td>Modifying the Council of Representatives’ authority to dissolve the councils (Law 21, Article 20.2) in a two-step process in which the council first has the opportunity to consider and respond to the COR’s objection (objection on the grounds of contravening the Constitution or applicable laws).</td>
<td></td>
</tr>
<tr>
<td><strong>Law 19, 2013, Second Amendment of the Law of Governorates not Incorporated in a Region (Law 21)</strong></td>
<td></td>
</tr>
<tr>
<td><strong>Political Decentralization</strong></td>
<td></td>
</tr>
<tr>
<td>Articles 10.8 and 10.10: Strengthen the authority of the Councils as the “legislative and regulatory authority” with the right to “issue local legislations in a manner to enable the Council to conduct its business in accordance with the principle of administrative decentralization”; and give the Governor “direct power over the agencies assigned to protection and preserving security in the governorate.”</td>
<td></td>
</tr>
<tr>
<td><strong>Fiscal Decentralization</strong></td>
<td></td>
</tr>
<tr>
<td>Article 11 formalizes federal budget allocations to governorates sufficient to fulfill their functions in accordance with population, level of deprivation and consistent with balanced development for different parts of the country (amends Article 44 in Law 21).</td>
<td></td>
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<tr>
<td>Article 44 specifies revenues generated by the governorate to include service fees...</td>
<td></td>
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</tbody>
</table>
Table A2.1: Constitutional, Statutory and Other Legal and Regulatory Instruments Key to Decentralization in Iraq

<table>
<thead>
<tr>
<th>Legal - Regulatory Precedent</th>
<th>Key Decentralization Provisions</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>on services and investment projects, taxes and other fees and fines, sale of movable and immovable state property, half of the revenues of border ports (replaces Article 44 in Law 21).</td>
</tr>
<tr>
<td></td>
<td>▪ <strong>Article 44</strong> allocates $5.00 per barrel of crude oil produced in a governorate, $5.00 from every barrel of crude oil refined in a governorate; and $5.00 from every 150 m$^3$ natural gas produced in the governorate (Subsequently amended to 5 percent).</td>
</tr>
<tr>
<td><strong>Service Delivery Decentralization</strong></td>
<td></td>
</tr>
<tr>
<td></td>
<td>▪ <strong>Article 45</strong> establishes a High Commission for Coordinating among the governorates with membership from several ministries, governors and chairmen of governorate councils (replacing a previous High Commission with only Governors representing the provinces). The High Commission is responsible for the gradual “transfer of sub-directorates, departments, tasks, services and competencies” of the seven federal ministries (replaces Article 45 in Law 21).</td>
</tr>
<tr>
<td><strong>Law 10, 2010</strong></td>
<td><strong>Fiscal and Financial Management</strong></td>
</tr>
<tr>
<td></td>
<td>▪ <strong>Article 2.2</strong>, recognized the authority of the Najaf Governorate to impose a pilgrim’s tax on religious tourists, consistent with Advisory Opinion No. 16, recognizing the authority of provincial councils to raise local revenues.</td>
</tr>
<tr>
<td><strong>Law 18, 2010</strong></td>
<td><strong>Service Delivery Decentralization</strong></td>
</tr>
<tr>
<td></td>
<td>▪ <strong>Devolved the Ministry of Labor and Social Affairs to the governorates</strong>. One governorate, Karbala, wrote a local ordinance to receive the staff, budget and properties of the two ministries. In 2010, the Supreme Court declared the law unconstitutional on technical grounds related to how the law was introduced and passed.</td>
</tr>
<tr>
<td><strong>Law 20, 2010</strong></td>
<td><strong>Service Delivery Decentralization</strong></td>
</tr>
<tr>
<td></td>
<td>▪ <strong>Devolved the Ministry of Municipalities and Public Works</strong>, transferring staff, budget and property to the governorates. In 2010, the Supreme Court declared the law unconstitutional on technical grounds related to how the law was introduced and passed.</td>
</tr>
<tr>
<td><strong>Annual Budget Law 2013</strong></td>
<td><strong>Fiscal Decentralization</strong></td>
</tr>
<tr>
<td></td>
<td>▪ States that unused grants and aid from the amounts allocated to state departments and public sector companies shall be calculated by the end of fiscal year (FY) 2012. On this basis, surplus amounts or amounts paid in excess shall be regarded as an advance payment made on the account of the grant allocated to a department or unit in FY2013.</td>
</tr>
<tr>
<td><strong>Annual Budget Law 2015</strong></td>
<td><strong>Political Decentralization</strong></td>
</tr>
<tr>
<td></td>
<td>▪ <strong>Articles D.1 and D.2</strong> enhance the Governor’s position, relative to the Council.</td>
</tr>
<tr>
<td></td>
<td>▪ Assigns the authority to implement the investment plan, funded through the budget allocation, to the Governor.</td>
</tr>
<tr>
<td></td>
<td>▪ The Council is responsible for oversight and monitoring the implementation of investment projects.</td>
</tr>
</tbody>
</table>

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37 The law was overturned by the Supreme Court on the technical grounds that legislation was drafted by the Council of Representatives rather than by the Council of Ministers. The ruling did not address the constitutionality of devolving federal powers or authority to the Governorates.

38 The law was overturned by the Supreme Court on the technical grounds that legislation was drafted by the Council of Representatives rather than by the Council of Ministers. The ruling did not address the constitutionality of devolving federal powers or authority to the Governorates.
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</thead>
<tbody>
<tr>
<td>Third Amendment to the Law on Governorates not Incorporated in a Region (Law 21) (approved by the High Commission and Council of Ministers, not voted yet in COR)</td>
<td>- Intends to force more rapid devolution of some ministry functions and allow for a more gradual devolution of other ministry functions. It amends Article 45 of Law 21, which contains the devolution of federal ministries: “The commission shall discharge its functions referred to in paragraph (1) above [coordinate the devolution of federal ministries] gradually as of the date this law comes into effect provided that some powers are delegated immediately, others within 6 months and other powers within one year and above. The powers that remain within the federal ministries’ powers must be specified.”</td>
</tr>
<tr>
<td>Annual Budget Law 2016</td>
<td>Fiscal Decentralization</td>
</tr>
<tr>
<td>- Article 13 authorizes the assignment to the governorates to implement ministerial projects below 10 billion dinars and to transfer ministry funds to the governorate account.</td>
<td></td>
</tr>
<tr>
<td>- Article 34 authorizes the Minister of Finance to transfer the financial allocations of the departments which are no longer related to a ministry to the related governorate, and transfer all grades and titles as well.</td>
<td></td>
</tr>
</tbody>
</table>
Table 2.2. Capital Investment Budget: Federal, Regional and Governorates ($bn), 2006 - 2015

<table>
<thead>
<tr>
<th>Year</th>
<th>KRG</th>
<th>Governorates</th>
<th>Federal</th>
<th>Total</th>
<th>KRG%</th>
<th>Governorates %</th>
<th>Federal %</th>
</tr>
</thead>
<tbody>
<tr>
<td>2006</td>
<td>0.5</td>
<td>2</td>
<td>3.7</td>
<td>6.2</td>
<td>8.1%</td>
<td>32.3%</td>
<td>59.7%</td>
</tr>
<tr>
<td>2007</td>
<td>1.6</td>
<td>2.1</td>
<td>6.4</td>
<td>10.1</td>
<td>15.8%</td>
<td>20.8%</td>
<td>63.4%</td>
</tr>
<tr>
<td>2008</td>
<td>2.5</td>
<td>3.3</td>
<td>7.2</td>
<td>13</td>
<td>19.2%</td>
<td>25.4%</td>
<td>55.4%</td>
</tr>
<tr>
<td>2009</td>
<td>2</td>
<td>2.2</td>
<td>8.6</td>
<td>12.8</td>
<td>15.6%</td>
<td>17.2%</td>
<td>67.2%</td>
</tr>
<tr>
<td>2010</td>
<td>2.8</td>
<td>2.6</td>
<td>13.4</td>
<td>18.8</td>
<td>14.9%</td>
<td>13.8%</td>
<td>71.3%</td>
</tr>
<tr>
<td>2011</td>
<td></td>
<td></td>
<td></td>
<td>22.4</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2012</td>
<td></td>
<td></td>
<td></td>
<td>28.4</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2013</td>
<td>4.6</td>
<td>2.4</td>
<td>42.7</td>
<td>49.7</td>
<td>9.3%</td>
<td>4.8%</td>
<td>85.9%</td>
</tr>
<tr>
<td>2014**</td>
<td></td>
<td></td>
<td></td>
<td>51.8</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2015</td>
<td>4.8</td>
<td>2.6</td>
<td>30.9</td>
<td>38.3</td>
<td>12.5%</td>
<td>6.8%</td>
<td>80.7%</td>
</tr>
<tr>
<td>2015 oil</td>
<td>1.5</td>
<td>1.5</td>
<td>0.0%</td>
<td>100.0%</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2015 total</td>
<td>4.1</td>
<td>30.9</td>
<td>39.8</td>
<td>10.3%</td>
<td>10.3%</td>
<td>77.6%</td>
<td></td>
</tr>
</tbody>
</table>

*Published sources differ depending on use of official MOF data versus other sources and exchange rates used. Figures should be used as reasonable approximations. An official budget was not passed for 2014, so detailed figures for breakout of investment funds are not readily available.


Note: KRG= Kurdistan Regional Government; MOF= Ministry of Finance; USAID= United States Agency for International Development.

Table A2. 3: Development Budget Improvement Action Plan
<table>
<thead>
<tr>
<th>Diagnostic</th>
<th>Description/Remedy</th>
<th>Tasks</th>
</tr>
</thead>
</table>
| Enhance subnational capital investment plans | Developing organizational capacity | ▪ Develop rules, procedures, and documentation for providing feasibility study analysis procedures;  
▪ Develop prioritization procedures and applicable weighting (adjustments) to measure project priority.  
▪ Central and subnational governments should agree on a standardized baseline feasibility study package. |
| Training of line agencies | | ▪ Introducing life-cycle investment projects requires training project investment managers about how to introduce data, and analyze results.  
▪ Develop data input files, create management output files, develop performance indicators, and train managers on using the investment project module. |
| Improve Project Feasibility Analysis | Project Feasibility Analysis | ▪ Develop effective project feasibility and appraisal guidelines.  
▪ Develop project feasibility (appraisal) documents for investment projects.  
▪ Feasibility documents at a minimum should include: social impact, demographic analysis, estimated capital outlays, estimated maintenance and operational expenses over a 5-10 year period. |
| Establish Basic Asset Register and Development (Investment) Database | | ▪ A consolidated (unified) asset register and database should be coordinated with the relevant agencies, ministries and departments. In addition to the basic data described below, the data base should include such descriptions as asset condition grade, asset performance grade, and expected replacement date. |
| ▪ Improve quality of financial projections.  
▪ Ensure that all project costs are included in the medium-term budget framework | Financial Projections | ▪ Assist relevant entities in determining long-term financial requirements for management of the asset portfolio based on the strategies and targets outlined in the asset management plan, including: 1) Long-term cost streams for operations, maintenance, renewal, acquisition, and disposal activities; 2) Forecasts of income and balance sheet, asset valuation and depreciation; and 3) A summary of key assumptions made in the financial forecasts. |
Figure A3. 1: 2013 Recurrent Expenditures by Functional Classification

Source: Ministry of Finance, Iraq.
Table A3.1 Governorate Spending as a Percent of Total Consolidated Government Spending -- Recurrent and Investment

<table>
<thead>
<tr>
<th></th>
<th>FY2013 (%)</th>
<th>FY2015 (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Local Councils in the Provinces</td>
<td>0.02</td>
<td>0.16</td>
</tr>
<tr>
<td>Local and General Management in the Provinces</td>
<td>6.27</td>
<td>5.12</td>
</tr>
<tr>
<td>Investment Commissions at the Provinces</td>
<td>0.02</td>
<td>0.02</td>
</tr>
<tr>
<td>Total</td>
<td>6.31</td>
<td>5.30</td>
</tr>
</tbody>
</table>

Source: Ministry of Finance, Iraq.
<table>
<thead>
<tr>
<th>Administrative Category</th>
<th>2013 Budget</th>
<th>2014 Budget</th>
<th>2015 Budget</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Council of Representatives</strong></td>
<td>570,055,000,000</td>
<td>501,448,520,821</td>
<td>689,230,372,000</td>
</tr>
<tr>
<td><strong>Presidency</strong></td>
<td>99,625,000,000</td>
<td>56,885,964,099</td>
<td>85,099,851,000</td>
</tr>
<tr>
<td><strong>Council of Ministers</strong></td>
<td>3,322,698,000,000</td>
<td>1,870,416,838,773</td>
<td>5,967,900,526,000</td>
</tr>
<tr>
<td><strong>Foreign Affairs</strong></td>
<td>604,360,000,000</td>
<td>346,221,035,945</td>
<td>425,734,376,000</td>
</tr>
<tr>
<td><strong>Finance</strong></td>
<td>22,897,702,000,000</td>
<td>16,359,128,441,622</td>
<td>17,643,630,038,000</td>
</tr>
<tr>
<td><strong>Interior</strong></td>
<td>9,929,494,000,000</td>
<td>7,908,557,170,714</td>
<td>13,052,558,944,000</td>
</tr>
<tr>
<td><strong>Labor and Social Affairs</strong></td>
<td>1,068,740,000,000</td>
<td>1,200,465,881,261</td>
<td>1,597,621,029,000</td>
</tr>
<tr>
<td><strong>Health</strong></td>
<td>6,750,431,000,000</td>
<td>3,641,601,970,927</td>
<td>5,417,292,295,000</td>
</tr>
<tr>
<td><strong>Defense</strong></td>
<td>9,206,856,000,000</td>
<td>4,516,334,641,116</td>
<td>10,780,537,028,000</td>
</tr>
<tr>
<td><strong>Justice</strong></td>
<td>567,125,000,000</td>
<td>487,561,861,664</td>
<td>489,113,119,000</td>
</tr>
<tr>
<td><strong>Education</strong></td>
<td>8,811,060,000,000</td>
<td>7,279,660,219,940</td>
<td>7,372,790,858,000</td>
</tr>
<tr>
<td><strong>Youth and sport</strong></td>
<td>533,478,000,000</td>
<td>106,186,376,664</td>
<td>260,815,541,000</td>
</tr>
<tr>
<td><strong>Trade</strong></td>
<td>6,362,887,000,000</td>
<td>4,928,918,541,897</td>
<td>3,426,923,776,000</td>
</tr>
<tr>
<td><strong>Culture</strong></td>
<td>390,235,000,000</td>
<td>120,713,295,527</td>
<td>104,981,528,000</td>
</tr>
<tr>
<td><strong>Transportation</strong></td>
<td>1,474,043,000,000</td>
<td>115,211,289,004</td>
<td>53,216,165,000</td>
</tr>
<tr>
<td><strong>Municipalities and public works</strong></td>
<td>2,705,930,000,000</td>
<td>457,409,194,891</td>
<td>1,129,769,142,000</td>
</tr>
<tr>
<td><strong>Housing and Reconstruction</strong></td>
<td>1,636,842,000,000</td>
<td>133,844,428,676</td>
<td>619,321,583,000</td>
</tr>
<tr>
<td><strong>Agriculture</strong></td>
<td>1,057,847,000,000</td>
<td>248,010,654,460</td>
<td>888,788,198,000</td>
</tr>
<tr>
<td><strong>Water resources</strong></td>
<td>1,336,748,000,000</td>
<td>205,204,957,006</td>
<td>532,308,048,000</td>
</tr>
<tr>
<td><strong>Oil</strong></td>
<td>21,509,513,000,000</td>
<td>545,437,463,696</td>
<td>14,999,593,200,000</td>
</tr>
<tr>
<td><strong>Planning and Development Cooperation</strong></td>
<td>76,058,000,000</td>
<td>44,556,834,303</td>
<td>56,223,960,000</td>
</tr>
<tr>
<td><strong>Industry and Minerals</strong></td>
<td>1,064,323,000,000</td>
<td>46,818,699,945</td>
<td>156,927,715,000</td>
</tr>
<tr>
<td><strong>Higher Education</strong></td>
<td>3,606,061,000,000</td>
<td>2,311,885,742,761</td>
<td>2,757,663,560,000</td>
</tr>
<tr>
<td><strong>Electricity</strong></td>
<td>7,946,498,000,000</td>
<td>1,031,697,821,625</td>
<td>4,910,116,608,000</td>
</tr>
<tr>
<td><strong>Science and Technology</strong></td>
<td>229,533,000,000</td>
<td>140,566,711,662</td>
<td>1,524,455,420,000</td>
</tr>
<tr>
<td><strong>Communications</strong></td>
<td>165,037,000,000</td>
<td>13,811,604,376</td>
<td>35,941,028,000</td>
</tr>
<tr>
<td><strong>Environment</strong></td>
<td>74,800,000,000</td>
<td>54,103,291,822</td>
<td>65,698,228,000</td>
</tr>
<tr>
<td><strong>Displacement and Migration</strong></td>
<td>238,060,000,000</td>
<td>107,991,662,981</td>
<td>2,595,784,312,000</td>
</tr>
<tr>
<td><strong>Human rights</strong></td>
<td>32,389,000,000</td>
<td>20,095,506,488</td>
<td>16,914,910,000</td>
</tr>
<tr>
<td><strong>Kurdistan Regional Government</strong></td>
<td>14,406,735,000,000</td>
<td>2,280,784,567,164</td>
<td>14,817,474,990,000</td>
</tr>
<tr>
<td><strong>Directories unrelated to ministries</strong></td>
<td>9,313,702,000,000</td>
<td>1,178,143,822,760</td>
<td>6,504,246,446,000</td>
</tr>
<tr>
<td><strong>Local Councils in the Provinces</strong></td>
<td>21,234,000,000</td>
<td>-</td>
<td>187,701,394,000</td>
</tr>
<tr>
<td><strong>Local and General Management in the Provinces</strong></td>
<td>8,673,373,000,000</td>
<td>-</td>
<td>6,115,379,624,000</td>
</tr>
<tr>
<td><strong>Investment Commissions at the Provinces</strong></td>
<td>29,337,000,000</td>
<td>-</td>
<td>21,252,184,000</td>
</tr>
<tr>
<td><strong>Iraqi Security Commission</strong></td>
<td>13,524,000,000</td>
<td>-</td>
<td>4,206,145,000</td>
</tr>
<tr>
<td><strong>The Independent Supreme Commission for Election</strong></td>
<td>375,349,000</td>
<td>-</td>
<td>0.00%</td>
</tr>
<tr>
<td><strong>Supreme Council of Judiciary</strong></td>
<td>370,318,000,000</td>
<td>296,663,949,696</td>
<td>396,073,871,000</td>
</tr>
<tr>
<td><strong>Tourism</strong></td>
<td>65,426,000,000</td>
<td>69,120,152,867</td>
<td>85,682,884,000</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>138,424,608,000,000</td>
<td>58,625,459,117,353</td>
<td>119,462,429,549,000</td>
</tr>
</tbody>
</table>

Source: Ministry of Finance, Iraq.
Table A3. 3 Government of Iraq (expenditures by year- Iraqi dinars)

<table>
<thead>
<tr>
<th></th>
<th>2013</th>
<th></th>
<th>2014</th>
<th></th>
<th>2015</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>$</td>
<td>%</td>
<td>$</td>
<td>%</td>
<td>$</td>
<td>%</td>
</tr>
<tr>
<td>Compensation for employees</td>
<td>33,830,281,000,000</td>
<td>40.6%</td>
<td>28,437,628,036,032</td>
<td>49.0%</td>
<td>38,550,630,236,000</td>
<td>49.3%</td>
</tr>
<tr>
<td>Use of goods and services</td>
<td>14,075,193,000,000</td>
<td>16.9%</td>
<td>5,836,809,656,297</td>
<td>10.1%</td>
<td>6,437,389,836,000</td>
<td>8.2%</td>
</tr>
<tr>
<td>Interest, subsidies and grants</td>
<td>7,349,292,000,000</td>
<td>8.8%</td>
<td>9,380,851,872,153</td>
<td>16.2%</td>
<td>12,343,115,172,000</td>
<td>15.8%</td>
</tr>
<tr>
<td>Social benefits, pensions, and retirement benefits</td>
<td>15,790,866,000,000</td>
<td>19.0%</td>
<td>14,363,878,004,996</td>
<td>24.8%</td>
<td>19,624,200,554,000</td>
<td>25.1%</td>
</tr>
<tr>
<td>Other</td>
<td>12,270,374,000,000</td>
<td>14.7%</td>
<td>606,291,547,874</td>
<td>1.0%</td>
<td>1,293,056,635,000</td>
<td>1.7%</td>
</tr>
</tbody>
</table>

Source: Ministry of Finance, Iraq.
### Table A3. 4 Economic Composition of Recurrent Government Expenditures (in per capita terms)

<table>
<thead>
<tr>
<th></th>
<th>Iraq (Total)</th>
<th>Basra</th>
<th>Wasit</th>
<th>Najaf</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Budgeted per Capita</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Compensation for employees</td>
<td>1,053,739</td>
<td>1,200,768</td>
<td>3,415</td>
<td>3,415</td>
</tr>
<tr>
<td>Use of goods and services</td>
<td>438,411</td>
<td>200,511</td>
<td>55,899</td>
<td>94,001</td>
</tr>
<tr>
<td>Grants, subsidies, and interest</td>
<td>228,914</td>
<td>400,018</td>
<td>9,909</td>
<td>2,667</td>
</tr>
<tr>
<td>Social benefits (including pensions)</td>
<td>491,851</td>
<td>611,251</td>
<td>39,760</td>
<td>29,298</td>
</tr>
<tr>
<td>Other expenditures</td>
<td>382,195</td>
<td>40,276</td>
<td>7,545</td>
<td>7,601</td>
</tr>
<tr>
<td>Net acquisitions of non-financial assets</td>
<td>48,512</td>
<td>0</td>
<td>92,093</td>
<td>59,321</td>
</tr>
<tr>
<td><strong>Total Recurrent Budget</strong></td>
<td>2,595,111</td>
<td>2,437,266</td>
<td>208,622</td>
<td>196,303</td>
</tr>
</tbody>
</table>

**Source:** Total – Ministry of Finance, Governorate data provided by individual Governorates.

**Note:** Population numbers based on 2009 data.

### Table A3. 5 Economic Composition of Government Expenditures (as a percent of total recurrent expenditures)

<table>
<thead>
<tr>
<th></th>
<th>Iraq (Total)</th>
<th>Basra</th>
<th>Wasit</th>
<th>Najaf</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Budgeted per Capita</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Compensation for employees</td>
<td>40.60%</td>
<td>49.27%</td>
<td>1.64%</td>
<td>1.74%</td>
</tr>
<tr>
<td>Use of goods and services</td>
<td>16.89%</td>
<td>8.23%</td>
<td>26.79%</td>
<td>47.89%</td>
</tr>
</tbody>
</table>

70
Grants, subsidies, and interest   8.82%  16.41%  4.75%  1.36%  0.00%  0.00%  0.00%  0.00%
Social benefits (including pensions)  18.95%  25.08%  19.06%  14.92%  9.07%  2.77%  2.53%  1.60%
Other expenditures  14.73%  1.65%  3.62%  3.87%  19.49%  11.60%  15.63%  8.61%
Net acquisitions of non-financial assets  1.87%  0.00%  44.14%  30.22%  35.21%  1.91%  4.50%  0.14%
Total Recurrent Budget  100%  100%  100%  100%  100%  100%  100%  100%

Source: Ministry of Finance, Governorate data provided by individual Governorates.
Note: Population numbers based on 2009 data.

Table A3. 6 Budget Execution Rates by Governorate

<table>
<thead>
<tr>
<th>Governorate</th>
<th>2010</th>
<th>2011</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>%</td>
<td>%</td>
</tr>
<tr>
<td>KRG</td>
<td>80</td>
<td>100</td>
</tr>
<tr>
<td>BAGHDAD</td>
<td>91</td>
<td>48</td>
</tr>
<tr>
<td>THI-QUA</td>
<td>75</td>
<td>71</td>
</tr>
<tr>
<td>MISSAN</td>
<td>73</td>
<td>47</td>
</tr>
<tr>
<td>ANBAR</td>
<td>52</td>
<td>100</td>
</tr>
<tr>
<td>MUTHANNA</td>
<td>50</td>
<td>76</td>
</tr>
<tr>
<td>KERBLA</td>
<td>48</td>
<td>57</td>
</tr>
<tr>
<td>BABIL</td>
<td>39</td>
<td>41</td>
</tr>
<tr>
<td>SALA AL-DIN</td>
<td>25</td>
<td>84</td>
</tr>
<tr>
<td>NAJAF</td>
<td>23</td>
<td>78</td>
</tr>
<tr>
<td>WASSIT</td>
<td>22</td>
<td>65</td>
</tr>
<tr>
<td>KIRKUK</td>
<td>22</td>
<td>37</td>
</tr>
<tr>
<td>NINEWA</td>
<td>14</td>
<td>24</td>
</tr>
<tr>
<td>DIYALA</td>
<td>12</td>
<td>34</td>
</tr>
<tr>
<td>BASRAH</td>
<td>11</td>
<td>8</td>
</tr>
<tr>
<td>QADISIYA</td>
<td>9</td>
<td>61</td>
</tr>
</tbody>
</table>

Source: Data obtained from Iraqi Budget Execution Report, United Nations joint analysis.
### Table A3. 7 Per Capita Governorate Revenue as a Percentage of Total Government Revenue

<table>
<thead>
<tr>
<th></th>
<th>Basra</th>
<th>Babel</th>
<th>Naja</th>
<th>Average*</th>
</tr>
</thead>
<tbody>
<tr>
<td>FY2013</td>
<td>0.05186%</td>
<td>0.01071%</td>
<td>0.05003%</td>
<td>0.03753%</td>
</tr>
<tr>
<td>FY2014</td>
<td>0.13520%</td>
<td>0.00796%</td>
<td>0.05670%</td>
<td>0.06662%</td>
</tr>
</tbody>
</table>

*Average is the simple average across these three provinces. It is not weighted by province population.

**Source:** Total revenue – Ministry of Finance, Governorate revenue – individual Governorates.

**Note:** Population based on 2009 data.

### Table A3. 8 Comparison of Iraq Budget Revenue (including capital) (Iraqi dinars)

<table>
<thead>
<tr>
<th></th>
<th>Ministry of Finance</th>
<th>Basra</th>
<th>Babel</th>
<th>Najaf</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>per Capita</td>
<td>Budget</td>
<td>per Capita</td>
<td>Actual/Budget</td>
</tr>
<tr>
<td>2013</td>
<td>119,296,663,096,000</td>
<td>4,925,500,000</td>
<td>1,927</td>
<td>270%</td>
</tr>
<tr>
<td>2014</td>
<td>105,266,034,056,436</td>
<td>11,328,213,920</td>
<td>4,433</td>
<td>100%</td>
</tr>
</tbody>
</table>

**Source:** Total – Ministry of Finance, Governorate data provided by individual Governorates.

**Note:** Population based upon 2009 data.
Figure A3. 2 Oil Receipts as a Percentage of Total Iraqi Revenue

Oil receipts as a percentage of total Iraq revenue

Source: Based on data collected by the Task team from Ministry of Finance, Baghdad.
Figure A3. 3 Non-Oil Related Sources of Total Iraqi Revenues

Source: Based on data collected by the Task team from Ministry of Finance, Baghdad.

Table A3. 9 Investment Budget and Petro$ Share Allocations by Governorate for 2015

<table>
<thead>
<tr>
<th>Governorates</th>
<th>Investment Share $m</th>
<th>Petro$ share $m</th>
<th>Investment Budget + Petro$</th>
<th>Investment Budget Share%</th>
<th>Petro$ Share%</th>
<th>Total Investment + Petro$ Share%</th>
<th>Population Share 2009</th>
</tr>
</thead>
<tbody>
<tr>
<td>Anbar</td>
<td>139</td>
<td>1</td>
<td>140</td>
<td>5.1%</td>
<td>0.1%</td>
<td>3.3%</td>
<td>4.5%</td>
</tr>
<tr>
<td>Babylon</td>
<td>160</td>
<td>8</td>
<td>168</td>
<td>5.9%</td>
<td>0.5%</td>
<td>4.0%</td>
<td>5.4%</td>
</tr>
<tr>
<td>Baghdad</td>
<td>357</td>
<td>39</td>
<td>396</td>
<td>13.2%</td>
<td>2.6%</td>
<td>9.4%</td>
<td>22.4%</td>
</tr>
<tr>
<td>Basrah</td>
<td>231</td>
<td>896</td>
<td>1127</td>
<td>8.5%</td>
<td>59.5%</td>
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*Note:* KRG= Kurdistan Regional Government.

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**Figure A3. 4 Budget Execution Rates by Governorate**

![Budget Execution Rates by Governorate](image)

*Source:* Data obtained from Iraqi Budget Execution Report, United Nations joint analysis.

*Note:* KRG= Kurdistan Regional Government.
Chapter 5 Annexes

Annex C– Functions Transferred from the Ministry of Municipalities and Public Works to the Governorates

The General Functions for the Five Directorates of the Ministry of Municipalities that are transferred to the Governorates:

1- Human resource management including authority to transfer, relocate staff, and evaluation and disciplinary sanctions, except for the General Directors in the governorates.
2- Employing staff on a temporary and/or permanent basis, and authority to manage promotions and incentives according to the annual budget law and its instructions.
3- The formation of investigative committees, approving recommendations
4- Prosecuting in legal cases according to the jurisdictions granted to the governors.
5- Formulating, elaborating, and approving contracts for the projects and works of the governorate, and ratifying the authorizations, contracts, and written pledges.
6- Claiming the property of lands for projects.
7- Preparing the investment budget of the non-strategic projects of the governorate.
8- Preparing the operational budget of all the directorates of the governorate.
9- Financial management (accounts, reports, auditing, and monitoring) at the governorate level.
10- Developing short- and mid-term plans.

The Specific Functions of the General Municipalities Directorate that are transferred to the Governorates.

1- The purchase and supply of materials, vehicles and equipment to operate the public facilities.
2- Exercising powers regarding the rent and sale of the municipalities’ immovable properties.
3- Renting the industrial lands for the professional and the owners of factories according to Decision 64 in 1990 and its Amendment 38 in 1999, and Law 20 in 1998 and its amendment Law 35 in 2000.
4- Building public facilities, markets, parking garages, bridges intersections, slaughter houses and cattle fields according to planning and environmental regulations; opening and widening the streets and their approaches, turns, classification, and building them in light of the Master Plan.
5- Building and managing manufacturing stations and landfill sites, as well as waste recycling factories.
6- Setting the depth and width of the sides on the streets, rivers, water springs, and public places.
7- Determining the building materials that are not allowed to be used in some buildings to save lives, and to sustain the aesthetic privacy of some cities.
8- Determining the wages charged by the owners of the public markets for fruits, vegetables, seeds, and palm dates sold according to the valid laws.
9- Collecting the fees and fines according to applicable laws.
10- Managing and disposing the movable properties except for the cash deposits of the Ministry.

The Functions of the Water General Directorate of Municipalities that are transferred to the Governorates.

1- Building water filtration complexes for potable water, and extending the water grids to the districts and sub-districts.
2- The purchase and supply of materials (except the sterilization and filtration materials) and the vehicles and equipment required to operate the water filtration stations and complexes.
3- Collecting the water fees according to the valid laws.
4- Providing water meters.
5- Following up on the implementation of the standards, decisions, and plans in the governorate.
6- Supervising the implementation of the works and plans of the departments and sections of the water directorate in the governorate.
7- Managing and disposing the movable properties, except for the cash deposits of the Ministry.

The Functions of the Sewage General Directorate of Municipalities that are transferred to the Governorates.

1- Collecting the sewage fees according to the valid laws.
2- The purchase and supply of materials and the vehicles and equipment required to operate the sewage stations and complexes.
3- The implementation of the sewage and storm grids.
4- Conducting surveys and studies on the status of the sewage service in the governorate.
5- Conducting the quality management works for river water in order to make it meet the specifications by conducting periodic tests.
6- The sewage directorate shall follow up on the implementation of the standards, decisions, and plans in the governorate.
7- The sewage directorate shall supervise the implementation of the works and plans of the departments and sections of the water directorate in the governorate.
8- Managing and disposing the movable properties except for the cash deposits of the Ministry.

The Functions of the Urban Planning General Directorate that are transferred to the governorates.

1- Giving the planning opinion adopted in the proposed sites for the public and private sectors projects that are within the master plan boundaries according to the ratified uses, as well as giving the planning opinion for the municipality departments regarding granting building licenses according to the ratified uses.
2- Giving the planning opinion adopted in the requests for projects sorting for the public and private sector projects that are outside the municipal and master plan boundaries, and refer it the committee for allocating investment and development projects according to the ratified uses, as well as giving the planning opinion for the strategic projects and refer it through to the committee.
3- The preparation and amendment of the sorting schemes of the lands according the uses set in the ratified sectoral and detailed designs, and ratifying them according to the adopted regulations.
4- The preparation and amendment of sectoral and detailed according to the uses set in the ratified master plans.
5- Preparing the studies related to rural development.
6- Managing and disposing the movable properties except for the cash deposits of the Ministry.
7- The preparation and amendment of master plans of the cities according to the regulations, and authorizing the governors to sign the final ratification.
8- The preparation of the structural plans of the governorate according to the regulations and in coordination with the related parties under the supervision of the directorate of urban planning in the governorate. It should be endorsed by the general directorate to ensure coordination with the plans of the neighboring governorates.
9- The preparation of studies related to natural and aesthetic areas and parks at the governorates.
10- The preparation of studies and modern designs of urban upgrading for the heritage sites and city centers and old cities at the governorate level, and in coordination with the general directorate of urban planning in the Ministry.

The Functions of Planning and Monitoring General Directorates that are transferred to the governorates.

1- Unifying the suggestions of amending the plans in coordination with the related directorates in the governorate.
2- Setting a detailed work plan, the implementation responsibilities, and the objective follow up for the projects in the governorate.
3- Implementing the required studies and reviewing the projects and plans expressing the needs of most of the governorate departments.
4- Putting the plans in light of the results of each implementation, following up on the reports in the governorate.
5- Collecting and categorization of the data and statistical information related to the activities of the governorate in order to benefit from them in the fields of planning, monitoring, and providing the Central Statistical Office with the needed data.
6- Coordination and supervision of the statistics departments and the information systems in the directorates belonging to the Ministry of Municipalities and Public Works in the governorate in order to unify the data and show the relation among them.
7- Conducting studies and research, and implementing plans and programs that help to achieve the goals of the directorate in coordination with the other directorates in the governorate.
8- The preparation of elementary studies and assessment of the statistical data.
9- Following up on the implementation of the plans in the governorate.
10- The monitoring and following up of the special reports of the potable water in the governorate.
11- The following up and monitoring of the special reports about collecting the solid waste and putting them in landfills in the governorate.
12- The following up of the environmental effect of the Ministry and governorate`'s projects through factory tests for all the projects in the governorate.
13- Managing the movable properties, except for the cash deposits of the Ministry.