American strategy for Iraq consists of three basic tenets: clear, hold, and build. U.S. ground forces have been successful in clearing and holding key areas in Iraq; however, the last tenet, build, as of February 2007 has been the most complicated to implement. Army Field Manual (FM) 3-0, Operations, states that ground forces should conduct stability operations to establish civil security and control, restore essential services, support local governance, and promote economic and infrastructure development. Most Army units in Iraq have been relatively successful at restoring essential services by using the Commander’s Emergency Response Program (CERP), which has netted many positive short-term gains. However, Army tactics to foster local governance and economic development have produced mixed long-term results. In addition, no clear linkage has existed between small-unit short-term goals and State Department and U.S. Agency for International Development (USAID) long-term development goals.

This article highlights some tactical concepts developed and applied in Tal Afar and Ar Ramadi that, if successfully sustained, could lead to a stable Iraq and offers guidelines for future U.S. nation-building efforts. To this end, the Army must counter political disenfranchisement and economic depression to address insurgency’s grass-root causes and eliminate extremist ideology.

Support Local Governance

Iraq has 18 provinces, and the new Iraqi constitution gives the provinces certain powers for political and economic development; however, neither the Iraqi constitution nor U.S. policies address the powers of the local governments in detail. Shifting the focus of political reconciliation and reform to the local level gives the average Iraqi more ownership of the political process. As the saying goes, “All politics is local.” As Alexander Hamilton wrote in Federalist Paper 17, the “people maintain stronger affection, esteem, and reverence toward sub-unit government owing to its public visibility in the day-to-day administration of criminal and civil justice.”

PHOTO: Tal Afar’s 14th-Century, Ottoman-era castle (currently the district government center) dominates the city’s landscape, evoking its long history of civilization and conflict. (DOD, CPT Lewis Messinger)
The Tal Afar district government. In 2006, Tal Afar’s local district government consisted of a mayor and a council appointed by the provincial council. However, it did not reflect the 13 clearly defined internal city neighborhoods with different ethnic mixes of Sunnis and Shi’ites, or the sub-districts of Abu Maria, Zuma, Avgani, and Rab’ea. Had the council organized to do this, it would have mitigated many conflicts and much distrust. Though reorganizing the Tal Afar council was impractical at the time, such a reorganization effort was vital in developing sub-district governments in Ar Ramadi in Al Anbar Province.

Once the district government assumed power, it was critical to develop an extensive training program to allow the council to act as a true governing body. Some of the most important functions of any legislative body are developing parliamentary procedures, drafting legislation, and enacting budgets. Unlike the Iraqi Army, Iraqi Police, and provincial government, the district government had no strategy to operate independently. This created the illusion that it was a “figurehead government” in which the local mayor and council appeared to have power and authority, but in fact exercised none.

From February to March 2006, the Tal Afar district council was a governing body in name only. Calls for its dissolution and the establishment of a new council to serve the people forced it to start performing its duties. The council began to address the issue of compensation for battle damages and formed committees to discuss human rights violations and the district’s operating budget. By November 2006, the district council managed $4 million worth of compensation payments, passed a $29 million operating budget, investigated excessive use of force by the Iraqi Police, and enacted local ordinances, including traffic and fuel distribution codes and zoning for industrial development. As the council began to work on more issues, the people’s confidence in the local government increased.

The Jazeera council in Ar Ramadi. At the height of Al-Qaeda’s domination of Ar Ramadi, the provincial, district, and sub-district governments completely collapsed. However, once 1st Brigade, 1st Armored Division security operations drove Al-Qaeda from the city, a new government began to emerge. The provincial government re-established itself, but it refused to meet in Ar Ramadi because the director generals (DG) were corrupt and complicit with Al-Qaeda. The Sheikh Awakening, a Sunni revolt in Ar Ramadi led by Sheikh Sattar Abu Risha, was the first critical development in governance and set the conditions for clearing the area of Al-Qaeda.

In December 2006, in response to the dismal services the existing district government provided, the leaders of the Sheikh Awakening and the Albu Thiayb tribe discussed forming a new council just north of Ar Ramadi. They also hoped to organize the tribes for reconciliation and economic development instead of allowing reconstruction projects to move forward on a case-by-case basis. Each of the four cooperating tribes had a representative on the new council to discuss coalition project allocation, develop governing bylaws, address security and development issues, and seek recognition from the provincial government in order to receive funds for infrastructure improvement.

Word of the council spread to the other tribes in Jazeera. The coalition urged them to end their support for Al-Qaeda. As a reward, they would have a seat on the council and be eligible to receive coalition assistance in the form of reconstruction projects. The conditions for joining the council were—

- End any allegiance to Al-Qaeda.
- Reduce attacks against coalition forces and Iraqi Security Forces by at least 50 percent.
- Provide recruits for local Iraqi Security Forces.

By February 2007, all the tribes in the Jazeera area had endorsed the council. Iraqis that were once hostile to the coalition became cooperative and helped clear Al-Qaeda out of northern Ar Ramadi. After the council expanded, it began working with the coalition on large reconstruction projects and concepts to promote economic development. The key to the Jazeera council’s success was the fact that it was fully democratic and each tribe had a representative on it.

From February to March 2006, the Tal Afar district council was a governing body in name only.
Developing a budget. After a U.S.-sponsored contract that supplied the local Tal Afar government with support personnel ended, coalition forces began to train Iraqis in budgetary procedures. In 2006, a decentralized funding process required each department in the local government to seek funds for personnel and operational support from a separate national ministry. Unfortunately, the national ministers used a centralized funding matrix that did not meet local funding needs and did not consult with the legislative and executive bodies that oversaw the day-to-day operations of the government.

The Tal Afar government desperately needed an operating and maintenance budget. City department directors had no clear idea how many people worked for their departments, how many supplies they needed to run their offices, or how much it would cost to operate them. They were not accustomed to developing a budget because everything had been centralized previously. As a result, many government offices rarely had enough money to hire new workers, purchase equipment, or make repairs. The entire budgetary system in Iraq was dysfunctional, and we had to address this problem in order to empower local governments.

Federalism is not only political, but fiscal. As the International Monetary Fund (IMF) noted, fiscal federalism is important for the development of countries moving from a unitary or totalitarian regime to a democratic model. As explained by author Vito Tanzi:

The needs of the citizens and taxpayers for public sector activities are better known to the local government officials than those who represent the central government. The reason is that contiguity provides more information while distance reduces the amount of information necessary to make good decisions. This argument is assumed strong enough to neutralize the advantages that economies of scale in the production of public goods and public services and in the generation of tax revenue may give to arrangements that keep more power in the hands of the central government.2

After the district directors briefed the district council and Tal Afar city directors on the budget, they presented their budget request to the district council. This allowed the district council to better understand the city’s operations and funding requirements and the serious shortfalls the city had been operating under for so many years (see Figure 1). The council approved the budget on 8 August 2006, and the mayor signed his endorsement at a public hearing. The local government had acted as a unified body.

The provincial council in Mosul had received about $203 million for capital projects from the Ministry of Finance. The Deputy Commanding General of the 101st Airborne Division proposed giving each district a percentage of this amount

<table>
<thead>
<tr>
<th>Directorate</th>
<th>Amount ($USD)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Education</td>
<td>15,827,525.00</td>
</tr>
<tr>
<td>Youth and Sports</td>
<td>43,276.00</td>
</tr>
<tr>
<td>Propane Distribution</td>
<td>212,195.33</td>
</tr>
<tr>
<td>Agriculture</td>
<td>86,980.08</td>
</tr>
<tr>
<td>Primary Health Clinics</td>
<td>2,741,743.77</td>
</tr>
<tr>
<td>Civil Defense (fire department)</td>
<td>4,239,086.00</td>
</tr>
<tr>
<td>Municipal Services</td>
<td>923,920.55</td>
</tr>
<tr>
<td>Water</td>
<td>568,520.96</td>
</tr>
<tr>
<td>Granary (Silo)</td>
<td>302,302.00</td>
</tr>
<tr>
<td>Sewerage</td>
<td>127,858.80</td>
</tr>
<tr>
<td>Gas Station (petroleum fuels)</td>
<td>138,858.67</td>
</tr>
<tr>
<td>Electricity</td>
<td>1,830,233.33</td>
</tr>
<tr>
<td>Census</td>
<td>54,160.67</td>
</tr>
<tr>
<td>Agriculture Bank</td>
<td>69,287.75</td>
</tr>
<tr>
<td>Veterinary Clinics</td>
<td>158,643.45</td>
</tr>
<tr>
<td>Rafidan Bank</td>
<td>86,266.60</td>
</tr>
<tr>
<td>Communications</td>
<td>481,647.47</td>
</tr>
<tr>
<td>Irrigation</td>
<td>127,858.50</td>
</tr>
<tr>
<td>Tal Afar Hospital</td>
<td>983,137.00</td>
</tr>
<tr>
<td>Tal Afar Tax Department</td>
<td>119,968.80</td>
</tr>
<tr>
<td>Tal Afar Mayor and City Council Executive Budget</td>
<td>380,014.78</td>
</tr>
</tbody>
</table>

Total: $29,503,485.20

NOTE: Exchange ratio is $1500 ID = $1 USD

Figure 1. Tal Afar district budget.
based on the percentage of the provincial population inside its borders. The Tal Afar district was home to 11 percent of the people in Nineveh Province, entitling it to $22 million in capital improvement funds. The district then developed a practical plan for the projected $22 million. (Al Anbar Province received a similar amount of money from the Ministry of Finance.)

Tal Afar’s receipt of these funds reduced the demand for CERP funds, which allowed U.S. forces to focus CERP money on larger projects with long-term economic and infrastructure benefits. (If each CERP project had been added as a line item to the Tal Afar budget proposal, the local government could have accurately forecast future maintenance costs as well.)

**The need for a tax base.** While no one wants to pay taxes, taxes are unavoidable if governments are to function. As the 19th century economist Millicent Fawcett notes, “The legitimate functions of government are . . . the protection of life and property, and the maintenance of the equal freedom of all. These functions cannot be performed without incurring a considerable expense. To meet this expense, taxation is necessary; a great interest has always been felt in the question of how taxes should be levied.”

The district government’s ministry structure currently does not allow it to generate revenue through taxes or service fees to provide incentives to establish a business; maintain, reconstruct, or modernize Iraq; or invest in education. In addition, no property or sales tax exists to generate revenue. The provincial council has to finance the entire city budget.

If the city had taxed the $74 million in U.S.-sponsored CERP and Iraqi government-funded projects at 5 to 10 percent, it would have generated from $3.7 million to $7.4 million in revenue. The city could have put that tax revenue into interest-bearing accounts in either state or private banks. The tax office collects sales taxes on homes, automobiles, and other big purchases that can increase the amount of money for district operations and make them more responsive to the needs of the people.

Figure 2 depicts an example of fiscal federalism, “a system of transfer of payments or grants by which the federal government shares its revenues with the lower levels of government.” Iraq’s district, provincial, and national governments can follow this model and get a clearer read on the nation’s budgetary needs. However, in order for this process to be successful, Iraq must modify its tax and revenue laws.
Economic and Infrastructure Development

Successful counterinsurgency and nation building require security and political reconciliation, but they also require economic growth. As Milton Friedman reminds us, “Economic freedom is also an indispensable means toward the achievement of political freedom.” Once the local population in Iraq begins to focus more on wealth creation, the incentives to participate in hostile acts lessen because the risks of doing so increase and the rewards diminish. Re-establishing state-owned enterprises, investing in private enterprises, and creating capital will help make this happen in Iraq.

Re-establishing state-owned enterprises. In the U.S., several cities have base industries that define the local economies. For instance, consider the automakers GM, Ford, and Chrysler in Detroit; Boeing and Microsoft in Seattle; and Xerox and Kodak in Rochester, New York. When these industries suffer, their suffering affects the city’s entire economy. In Iraq, the base industries were all state-owned enterprises necessary to maintain the economy, but the U.S. declined to invest in state-owned enterprises in Iraq, preferring instead that private investors do so. However, as the security situation in Iraq worsened and these facilities fell into disrepair, private investors were unwilling to risk capital on such ventures. As a result, thousands of unemployed Iraqis joined the insurgency for economic reasons rather than ideological ones. An approach that provided modest investment to restart the state-owned enterprises and subsequently privatize them in phases might have avoided some of the conditions for economic and political chaos.

For example, in Tal Afar, the chief state-owned enterprise was the granary. The two primary mutually supporting industries were agriculture and transportation. The granary supported 25 milling companies in the area and thousands of farmers from the western portion of the province. It was decided in late March to early April of 2006 that this local economic engine would have to be repaired and re-opened for business to revive the economy. U.S. forces and the local Iraqi government determined that it would take $1.16 million to make the granary ready for production. Once repaired, it would create a market for local farmers’ grain crops, create a demand for machinists to repair farm and factory equipment, and increase the demand for...
truckers to move grain products from Tal Afar to markets in Mosul and elsewhere. The granary could employ thousands of people directly and indirectly. Funds were approved for the refurbishment of the granary, and by the spring of 2007, it was returning to production capacity.

In contrast, the primary industry in Ar Ramadi was an old glass factory. Efforts to restore that facility began in late 2006. The factory provided employment for thousands of Iraqis and was important to many other service-sector industries that existed during the old regime. Once the glass factory was out of production, the main economic engine of Ar Ramadi shut down. The glass factory could have been an example of gradual privatization. With foreign support and mentorship from such corporations as Corning Glass, the plant could have become a viable production facility for glass products sold domestically, regionally, and possibly even internationally.

**Lack of investment opportunities.** In the spring of 2006, an Iraqi executive asked coalition forces for financial assistance to build an asphalt plant in Tal Afar to work on coalition road projects. He stated that the project would cost about $1.2 million and that he and his partners could finance about $750,000 of that amount. He sought $500,000 from the coalition. Implementing the proposal would generate jobs in the construction of the plant and its daily operations, and the plant would provide needed asphalt at a lower price than asphalt brought in from Mosul. However, U.S. policies prohibited using CERP funds to invest in a private enterprise. Still, with over $3 million in road projects being developed and proposed, the coalition wanted to hatch a plan to help the executive build his plant.

The business center offered to work with the banks to secure a loan for the plant, but the Iraqi executive rejected the idea of a loan because he did not want to pay the high interest rate the government banks asked. The business center proposed selling shares of stock in the plant to local investors to raise the necessary capital, and Iraq’s chief accountant proceeded to explain to the businessman the risks and rewards of issuing stock and how the business center could help market the plant to local contractors. The Iraqi government was planning $10 million in coalition-approved road projects and the provincial council managed a $37 million reconstruction fund and a $203 million Development Fund for Iraq in Mosul.

Had the Iraqis sold stock to generate the $500,000 and the plant received a minimum of $5 million in contracts for asphalt, the owners of the plant would have received a 1,000-percent return on their money, and each investor a good return as well. Had this worked, more opportunities would have opened for private investors to invest in start-up companies tied to reconstruction efforts. Had the coalition loaned funds to the company at an interest rate of 8 to 10 percent, the return would have been $40,000 to $50,000. Had U.S. forces been able to invest in the company at $1 per share and the price of each stock rose to $2 to $5, the coalition might have earned up to $2.5 million for future reconstruction projects. Had it put money from shares in the asphalt plant into a private bank account at 10 percent, it would have gained an additional $100,000 to $250,000 for future use. Encouraging more Iraqis to take private ownership of the economy could have helped stabilize the area. The policies that prevented investment in private businesses seem to have been a strategic mistake.

**The banking industry and credit.** The banks in Tal Afar offered no incentive to the people to put their money in the bank. They paid no interest on money deposited into savings accounts because the bank itself had no money to provide loans and earn interest. Had the banks provided a modest 3 percent interest rate on savings accounts and used depositors’ money to provide loans at 8 percent, each $1,000 deposited in the bank would have earned $80: a $50 profit for the bank and a $30 gain for the account holder. If the same account supported another loan, it would have produced another $82.40 in interest. In Tal Afar, population 100,000, the banks and the people could have generated thousands and possibly millions of dollars of interest from basic savings accounts used to provide loans. Had the coalition put a large part of its CERP dollars into private or state banks that

---

**The policies that prevented investment in private businesses seem to have been a strategic mistake.**
paid interest, it could have generated more capital to use for reconstruction and helped the Iraqi government raise and invest capital at the local level. In addition, it would have convinced residents that the banks were safe, just as similar actions taken by the government during the Great Depression restored faith in the U.S. banking system.

Other issues discouraged Iraqis. Most in Tal Afar and Ar Ramadi complained to the coalition about the lack of capital to establish privately owned enterprises. The biggest obstacle for investors in Tal Afar and Ar Ramadi was the absence of a legal system to protect property rights, solve disputes concerning investing and lending, and no institution in place to evaluate and grant financial credit. Micro-financing and lending were difficult. Financial institutions did not expect to receive a return on their money. There was no legal action to take if borrowers did not repay their debts. (Still, the Nineveh Business Center in Mosul gave out $1 million in loans and earned around $800,000, with only a few minor defaults and a repayment rate of over 95 percent.)

Success would have been possible with the establishment of credit within the Iraqi banking industry because, as economist Millicent Garrett Fawcett explains, “the real service credit performs is that it enables an increased quantity of wealth of a country to be used productively as capital. It encourages the productive employment of wealth. Scarcely anyone, for instance, retains a considerable sum of money in his own keeping; people keep just sufficient money to pay their daily personal expenses; all their money above this amount is generally deposited in a bank, and there used for productive purposes.”

Two proposals addressed the issue of credit at the micro-level in Tal Afar and Ar Ramadi: start-up loans for U.S.-funded projects and micro-loans for low-income individuals.

The coalition would guarantee or co-sign a start-up loan for individuals or businesses that received CERP-funded projects and micro-loans for low-income individuals.

The coalition would guarantee or co-sign a start-up loan for individuals or businesses that received CERP-funded projects. Local state banks or semi-privately owned business centers would issue the loans. Contractors would be eligible for a loan of up to 10-15 percent of any total project awarded that was less than $25,000. Loan requests for larger amounts would require approval from the board of directors of the banks or business center and an approval statement by the coalition forces.

In the summer of 2006, the USAID designated the city of Tal Afar as a site for a Micro-Finance Institute. The Micro-Finance Institute would have started with a loan balance of $500,000 to provide loans of $2,500 or less to poor people without a source of income; in Iraq these are often women. (This was similar to the Micro-Loan Program developed by Muhammed Yunus of the Grameen Bank in Bangladesh.) The notion of this program was extremely popular to many Iraqis because it fell within the parameters of Islam. Unfortunately, USAID ended its funding for Tal Afar at the end of the summer of 2006.

Efforts to establish a microfinance institution in Ar Ramadi came to naught due to lack of funding and because similar efforts were underway in Fallujah and other sections of Al Anbar Province. We should dramatically expand the concept of micro-finance and integrate it into city action plans for key cities in Iraq.

**Conclusion**

The recent surge has created conditions of security in Baghdad and Al Anbar Province that give the Iraqi government “breathing room” to address the political and economic problems plaguing the nation. U.S. military and provincial reconstruction teams have been fanning out to meet with local leaders to find solutions to many of Iraq’s systemic problems. It is imperative to provide support and financial assistance for local governments and businesses in Iraq to build a strong foundation for this newly democratic nation. 

**NOTES**

6. Fawcett, 186.