

STATE, FOREIGN OPERATIONS, AND RELATED PROGRAMS APPROPRIATIONS FOR 2009

HEARINGS BEFORE A SUBCOMMITTEE OF THE COMMITTEE ON APPROPRIATIONS HOUSE OF REPRESENTATIVES ONE HUNDRED TENTH CONGRESS SECOND SESSION

SUBCOMMITTEE ON STATE, FOREIGN OPERATIONS, AND RELATED
PROGRAMS

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the most effective way to do this, I would like to hear from you what kind of system would be a conducive to doing that, how much time it would take, and what would be the cost of such a system.

Mr. PAULSON. Thank you, Madam Chairwoman. I will first say that I am not sure that there is a single answer to your question. It depends on the needs of the institution. If you have a small staff and a low budget, then it may be more cost-effective to have a central unit of public affairs and communications. THURSDAY, APRIL 10, 2008.

FY 2009 INTERNATIONAL PROGRAMS BUDGET

WITNESS

HON. HENRY M. PAULSON, JR., SECRETARY, U.S. DEPARTMENT OF THE TREASURY

Ms. LOWEY. Good morning. The Subcommittee on State, Foreign Operations, and Related Programs will come to order. Today, we are very pleased to welcome Secretary Henry Paulson to discuss the Department of the Treasury's \$2.41 billion Fiscal Year 2009 budget request for contributions to international programs, an increase of \$941 million above the Fiscal Year 2008 appropriation.

Mr. Secretary, you have come to our Subcommittee at a time when many Members have serious concerns about the state of our domestic economy. Each of us has constituents who are reeling from record gas prices, falling home values, and shrinking job opportunities. Many of us also question aspects of the regulatory plan unveiled last week.

While this hearing is about Treasury's role on the international stage, these domestic issues, as you know, have a significant impact globally. I am very interested to hear your views on the effect of the current financial crisis on the global economy and the multilateral development banks, their risk exposure, and the potential liability for U.S. taxpayers. I hope your opening statement will shed some light on how the liquidity crisis is affecting developing nations' already limited access to credit and the role of international institutions in mitigating this risk.

Over the past several months, this Subcommittee has examined the effectiveness and coordination of U.S. bilateral foreign assistance. With that in mind, Mr. Secretary, I am interested in hearing why Treasury should have its own capacity to provide international technical assistance and why these programs should remain outside of the existing foreign aid infrastructure. Indeed, experience has shown that our assistance is most effective when it is well coordinated both within the United States government and with other donors.

As one of the lead negotiators with the G-8, and as the U.S. representative to the multilateral banks, I am interested in hearing the steps you are taking to represent U.S. development priorities during discussions with world leaders.

The United States has been supporting a reform agenda, and I believe that the World Bank is making progress in this area under its new leadership. I was pleased that the World Bank leadership endorsed the Volker Panel Report, which laid out concrete steps to address whistleblower protection, corruption investigation allegations, and the role of the Internal Investigations Unit at the Bank.

Mr. PAULSON. Thank you, Madam Chairwoman.

However, I remain concerned about continuing corruption allegations, including recent evidence of collusion in the India aid contractor programs.

Although both the World Bank and India are taking action on this issue now, it took three years for the Bank to admit charges. I would like to hear what Treasury is doing to encourage immediate implementation of the Volker recommendations, including the establishment of a strong whistleblower protection policy.

The Fiscal Year 2009 budget request includes a 16 percent increase in our contribution to the World Bank, and therefore Treasury oversight will be more important than ever.

Additionally, I am deeply bothered that the World Bank Group continues to disburse funding to Iran. In fact, while no new loans have been provided since 2005, disbursement of existing loans to Iran has increased in each of the last four years. It is perplexing that, despite United Nations sanctions against Iran, the World Bank has approved over \$1.3 billion in loans for Iran. While some of these loans are humanitarian in nature, many are for road and infrastructure projects. In addition, the Bank also provided loan guarantees to companies doing work in Iran in 2005.

I would like your thoughts on these policies and whether there are additional steps the U.S. should be taking to stop the flow of these disbursements, halt future investment guarantees, and dissuade European and Asian banks from investing in Iran.

The Treasury Department plays a critical role in stemming terrorist financing but cannot be successful when our allies leave their commitments unfulfilled. What is the Treasury Department doing to catalyze action in other countries, particularly Saudi Arabia, to prevent funds from reaching the hands of terrorists?

With respect to debt relief, I commend the administration for its commitment. However, I am concerned that we are not doing enough to ensure that these funds are reaching their intended recipients or being spent as envisioned. Many of us were outraged when we first learned of so-called "vulture funds," which prey upon poor countries, swooping in and buying their debt when it is about to be written off, only to sue for the original value of the debt plus interest, once it has been forgiven. These unforgivable actions have defrauded needy countries while lining the pockets of wealthy businessmen.

Mr. Secretary, what steps will the Treasury Department take in the coming year to address vulture funds and to ensure that debt relief for heavily indebted, poor countries is sustainable?

The Fiscal Year 2009 budget requests significant funds for global climate change, an issue that we all know this administration has had difficulty embracing, and I do commend you for your very important personal leadership and commitment to corporate environmental responsibility going back to your time at Goldman Sachs. I imagine that your commitment played a role in the funding requested for the Clean Technology Fund, and I hope you will share more details on this initiative.

However, I must note that I do not believe that eight years of backsliding on international climate change commitments can be rectified simply by throwing money at the problem. It is essential and I am sure you would agree, that the United States exercise

ship on curbing greenhouse gases and investing in alterative energy and clean technology here at home, if I may add, Secretary Paulson, I would like to close by noting that you have returned from China, where you were the most senior U.S. government official to visit since the Chinese government's violent crackdown in Tibet. Many of us have spoken out forcefully against the oppression of peaceful democratic activists in Tibet, and where its inaction and complicity in the genocide in Darfur, continued intransigence on United Nations resolutions that impose sanctions on Iran under resolution 1803. I have seen just today in the past, you have not raised concerns about these issues in conversations with the Chinese, illustrating what appeared to be a bifurcated policy within the administration towards China. State Department would press China on human rights concerns while the Treasury Department, which wields far greater leverage, would not engage on these issues. While I appreciate the distinct roles played by each agency, I fear that the Treasury Department's past silence has sent a message of inconsistency or, worse, indifference on many critical concerns. I was, therefore, pleased to hear that on your recent trip you did engage the Chinese government on the issue of Tibet. However, I hope this will not be an isolated incident and that you will continue to press the Chinese government on issues of concern, as we did. I bring this up to Secretary Paulson; I appreciate your being with us. I look forward to hearing your testimony. I look forward to working with you to ensure that our investments in the multilateral development banks address the development priorities of the 21st Century, and before we move to your testimony, let me turn to Mr. Wolf, the ranking Member, for his opening statement.

Thank you, Madam Chair. Mr. Secretary, welcome to the Committee. I think this is the second time I have ever been in his first speech before the British Parliament, William Wilberforce, who was the one who abolished the slave trade in England, talking to his colleagues and in talking to the leadership, the business leaders of England, said the following. He said to them, "Having heard all of this, you may choose to look the other way, but you can never again say you did not know." I work next to Mr. Walker, there is no one in this administration, and particularly you, and none in Congress who does not know about the nation's long-term financial outlook—in fact, when you were appointed, I really felt very good about it because I had heard you speak out on that issue, and I thought you were going to do something about it. Now I know David Walker, whom I know you know, who has left GAO to go and raise the consciousness of the country on this issue, said, "We have a tsunami of debt and spending that can swamp our ship state." Many think we are \$9 trillion in debt. We have \$53 trillion of unfunded obligations. I saw your quote last week, when the Social Security and Medicare Trustees Report recently came out, that it reinforced the dire consequences of our fiscal health. The Medicare Trustees Report concluded that consideration of reforms to ensure the financial security of Medicare must occur, stating, "the sooner the solutions are enacted, the more flexible and grad-

I know you know about the Social Security Report. It echoed the same sense of urgency, saying, "The projected trust fund deficit should be addressed in a timely way. Making adjustments sooner will allow them to spread over more generations."

The value of the dollar is dropping. In today's Washington Times, "Global Food Riots Turn Deadly Throughout the World."

What more evidence do we need? Congress, too, and the administration need to realize that our children and grandchildren cannot afford to have their leaders choose to look the other way.

Just last week, and I know you know about this because you had a representative there, there was a roundtable discussion held by Maya McGinnis and the Committee for a Responsible Federal Budget. It was a diverse group—Republicans and Democrats and independents and Wall Street people from business, finance, former CBO directors, former OMB directors, think tanks. Everyone there, but for one or two, expressed concern about the entitlement crisis that we are facing. What kind of country are we going to turn over to our children?

I was taken by the editorial page, if you saw it, in Newsweek last week. I think you know Pete Peterson. Do you know Pete Peterson? He said in that editorial—he was talking about the crisis and he ended by quoting Dietrich Bonhoeffer. I am sure you know who Dietrich Bonhoeffer is, the German pastor who was instrumental in the resistance movement against the Nazis. Dietrich Bonhoeffer said, and I quote, "The ultimate test of a moral society is the kind of world it leaves to its children."

Now, Jim Cooper and I have a bill in Congress with 80 co-sponsors. Senator Conrad and Senator Gregg and Senator Radanovich have a similar bill over on the Senate side. There are the votes to pass this in the House. I have been told there are votes to pass it in the Senate.

I have written the administration a number of times on the issue, and most of the time we do not even get an answer. But I urge you to be like Esther in the Bible. In such a time as this, with all of your knowledge and expertise, I hope you are going to pick this issue up. If you fail, you fail; but never to really try. We can pass this now. We can pass it. This would be a gift for the next president, whoever he or she is.

If you do not, and if the administration does not, I would predict, and I will never be able to really find out because I do not think we will be talking with each other once you leave, and you are in a different place, going back to New York or Chicago, I honestly believe, Mr. Secretary, one, I believe that you are probably one of the most competent people has been appointed to this spot.

As I was talking to Mr. Froemmer, your congressional relations person, I said, "The failure of Secretary Paulson to speak out and work on this is kind of like if a top brain surgeon in town failed to speak out on a problem, then the other brain surgeons are not going to deal with it."

You are the top brain surgeon on this issue, and I will predict if you leave here without forcefully addressing this issue, where ever you may go, you will live to regret it. You will sit on your rocking

Chair, and you will say, when you see the media reports next year and the year after, you will say, "You know, I could have dealt with that. I could have done something about that. I know I could have done something." I think you are going to say, "I am really sorry," you may not tell anybody else other than your close family, but you are going to say, "I am really sorry I did not pick this issue up."

So my request, we cannot force you to do it, but my request is that you will today begin to say, "Okay. We are going to work for the Cooper-Wolf Bill, we are going to work for the Conrad-Gregg Bill, we are going to put the resources of the administration, put the knowledge that you have and the expertise that the Department has behind this whereby we can do this, and we can do it." Dietrich Bonhoeffer said, not only for our generation but also for our children and our grandchildren."

With that, Madam Chair, I yield back the balance of my time.
[The information follows:]

As an example of these concerns, I have learned that the Inter-American Development Bank may have significant exposure to the crisis. According to an internal memo, dated January 26, 2008, the Bank reported almost \$300 million in losses in 2007, stemming largely from the subprime mortgage crisis.

This raises a whole host of questions, which I would like you to address. First of all, in your judgment, was the IDB investing in risky assets? What actions did Treasury take, as a member of the board, to change this investment strategy? Why was the IDB investing in U.S. subprime mortgages when a host of leaders were raising concerns about the ethical propriety of subprime lending, much less the growing risk of a collapse in this market? Does Treasury thinks this is a socially responsible and prudent investment of U.S. taxpayer dollars?

As the newly installed chairman of IDB's Board of Governors, what specific policies will you implement to ensure better oversight of IDB's investment portfolio and protect the institution in the future? Has Treasury undertaken a review of the investment portfolios of the other banks? What is the full exposure of the other institutions to this current crisis?

You have just overseen an unprecedented \$29 billion bailout of Bear Stearns. Should we expect American taxpayers to be on the hook for a bailout of the multilateral development banks?

Secretary PAULSON. Let me begin by saying, the meeting with the G-7 financial ministers begins tomorrow and takes place this weekend, and I just came from Miami with a meeting with the Inter-American Development Bank.

Let me begin by saying that, as we have talked with finance ministers around the world, the good news when you look at the developing markets, is this turmoil did not begin in the developing markets, and it really has had very little impact to date on the developing markets. I think you mentioned in your opening statement that the multilateral development banks need to be very vigilant and be able to look and figure out what role to play.

Now, in terms of your question about the IADB and subprime, this is a strong financial institution. Its triple A is not at all in jeopardy. This is something Treasury spent a fair amount of time on recently, that Chairman Luis Alberto Moreno has brought in an independent adviser to report to the board on this issue. That looks very contained and very manageable.

Ms. LOWBY. But there is a \$300 million loss.

Secretary PAULSON. Right now, I think, a marked-to-market loss on some of the securities in an overall portfolio that is in that neighborhood, yes. But, as I said, this is a relatively small portion of the overall assets, and he has retained an independent firm to report to him on that.

In terms of the World Bank and the others, I do not see any significant direct impact. I think the impact will be, to the extent there is an impact on the regions and the economies they serve because, as you know, weakness in one economy around the world ultimately impacts others. But, to date, I think in all of the meetings that I have had, and I met with the finance ministers of many of the Latin American countries, I have met with the finance min-

isters of the African countries, the Asian countries, for the most part, the economic situation outside of the U.S. is relatively strong.

Ms. LOWEY. But getting back to the banks, what is their exposure? You indicate that the Inter-American Development Bank is strong. What about the other banks?

Secretary PAULSON. As I said, as far as I know, this is not an issue for them.

Ms. LOWEY. Has Treasury done a review of their portfolio?

Secretary PAULSON. They are being reviewed, and there are processes in place in all of those banks to review their portfolio, as there is in the Inter-American Development Bank.

Ms. LOWEY. So, at this point, you are saying that there is no exposure, or are you saying that it is still under review? In the process of reviewing it.

Secretary PAULSON. You cannot be a bank by triple A securities, where you are buying mortgages and others, without there being some exposure, but this is not anywhere near comparable to what you have seen in some of the private sector financial institutions. This is something that is being looked at, and it is limited exposure. The IDB clearly has the most, and, as I said, they have got a process in place to deal with that.

Ms. LOWEY. So, you are in the process of reviewing it. I will turn this over to my colleague.

Secretary PAULSON. I am not in the process of review. I said, they are in the process of review, and their board of directors, their investment committee, their investment adviser in the process of reviewing it.

Ms. LOWEY. Well, if you can just keep me apprised of the results of this review.

Secretary PAULSON. We will continue to do that.

Ms. LOWEY [continuing]. That would be very helpful. Thank you.

Mr. WOLF. Thank you, Mr. Secretary, do you want to comment? I have some other questions. Can we get your support, active support, so you do not feel badly when you leave here?

Secretary PAULSON. I would say this. In terms of feeling badly, when I came down here, one of the reasons that I was attracted to come down here—I knew it was not going to be easy—was that the President had the courage to take on the Social Security issue. He asked me to undertake a fresh approach and to reach out to Members on both sides of the aisle in an attempt to start a process which could either be well along while we are here or completed when we were here.

Since I have been trained to run toward a problem rather than run away from a problem, while many people said to me, "You are tilting at a windmill"—not that this is not a very, very major issue, because I happen to think that entitlement reform is one of the two or three major issues, and it is one of the major issues we, as a country, face. So every time I have testified before the budget committees, I have made that point.

I made a huge effort to try to get people to come together and deal with this, and I had a lot of individual meetings where, behind closed doors, people said that something might be able to be done, but we could not get this together. In my judgment, there was not the political will in Congress to do this, and so the role we have

been playing right now has been continuing to talk about it, put out studies from Treasury that hopefully will depoliticize it and make it easier for the next administration to do.

Mr. WOLF. Well, Mr. Secretary, if I can—I only have so much time—there are 80 co-sponsors on this bill, and we are waiting for you to act, and you have not. You may have been part of the discussion over a year ago. Circumstances have changed. I read that Standard & Poor's and Moodys inferred that we could lose our triple A bond rating in 10 years. Is there a potential for that? Could I ask you, is there a potential for that?

Secretary PAULSON. I am not going to say there is a potential for that. I would say that the problem you have pointed to is a serious problem.

Mr. WOLF. But both of them said that we could lose our triple A rating. What would be the result in the United States if we lost our triple A bond rating?

Secretary PAULSON. Well, the way I describe the situation is that I am sure that this country will ultimately solve the problem, but the longer we wait, the less financial flexibility we have, and the greater price the younger generation will pay.

To get back to your issue, I have talked with the majority leader, the minority leader, with you, with Jim Cooper. I spent a lot of time with Kent Conrad and Judd Gregg. And you have some dead-on process, and I have got to tell you, I respect those ideas for progress. I do not think it is the Treasury secretary's role to sort of dictate to the House what the process should be for solving it, but I am happy to participate in any process you all want to put together. This is a serious problem, and your leadership has been exemplary, and I do hope we continue to talk when I leave. I care a lot about this, and all I can tell you is I have made a huge effort, and I am spending most of my time now on other things where there is a chance of getting them done, and they are more pressing in the short term.

I am sincerely disappointed that we could not get people to come together, because this should not be a political issue. This is an economic issue.

Mr. WOLF. Well, I do not think it is a political issue now. We have a large number of Democratic Members that are on it. Jim Cooper is a highly respected Member of the Congress. Congressman Hoyer has spoken out on behalf of this. Kent Conrad has been very sincere. I have been told there are the votes to pass this in the Senate. So we really need you to be engaged. Not to be engaged is to walk away. Just to put out a statement, and when you pull out your statement on the Social Security Medicare report, you said something to the effect of, I do not like playing solitaire. This is not solitaire. There are 80 Members up here who want to participate. They want to participate and want to work with you so we can really do what is best, and I do not believe it is a partisan issue, and I believe there are enough good men of faith on both sides of the aisle of all political backgrounds.

If you look at the cosponsorship that Jim has, I think he has Congressman Moran, and he has Congressman Tanner. He has a very broad cross-section. We really need you to weigh in. We need you to be a participant. You are not just another person.

the key brain surgeon in this town on this issue, and you carry a tremendous amount of credibility. I respect you highly. In fact, as I remember saying, when I heard you were going to be appointed, I referenced that Politico statement that was in the article. Finally we have someone who really understands this, and I know you have spoken out on it.

So we really need you to weigh in, and I would like you to submit for the record, or if you want to tell us verbally, what would the ramifications be if Standard & Poor's and Moodys are accurate. If you say someone is going to intervene, I do not know who they are. Because we have said, Jim and I have said to other Members, If you have a better idea that can pass, then we should be for it, but if you do not have a better idea that can pass, then this can pass. We have people like Bill Frenzel and Maya McGinnis, prominent, credible people in this town who have dealt with these issues.

Brookings believes it is very important. They helped us craft the bill. The Heritage Foundation's Stewart Butler helped us craft the bill. David Walker supports the bill. You are the quarterback. You are the key person. It is very difficult without you in, and the administration... I am not going to put you on the spot on this... I want to move on to another issue, but the administration is never reluctant to come up here and ask Members on both sides of the aisle, when they are looking for a vote on a free trade agreement, they had people down here over and over. They took people to Colombia. They are never reluctant to come up here when it is an issue with regard to Afghanistan or Iraq, and they ought not be reluctant to come up here on an issue that everyone knows about.

I just would end my question with this. I find this to be so powerful. If you recall, slavery was running rampant in Great Britain. The slave trade was an important part of their economy. No one in Parliament wanted to deal with that, and for Wilberforce to say to them, "Having heard all of this, you may choose to look the other way, but you can never again say you did not know." Mr. Secretary, history will never allow you to say you did not know! With that, I yield back.

Secretary PAULSON: I can just say to the Congressman, I appreciate your point of view. I will have no trouble looking in the mirror because of how much time I spent on this, and it was not just a matter of speaking out, and there are a lot of other congressional leaders that know how much time I spent on it.

So I appreciate your leadership, and I am going to respect you forever for the amount of time, and I am hopeful that you will get something done, and I thank you for your comments.

Ms. LOWRY: Ms. McCollum, I'd like to add my support.

Ms. MCCOLLUM: Thank you, Madam Chair. Secretary Paulson, I would like to thank you for joining us this afternoon. First, I want you to know I support the administration's request for the IDA-15 replenishment. My support is based on IDA's mission, its success, and because of its very impressive leadership with President Zoellick at the World Bank. President Zoellick is to be commended for picking up the pieces at the World Bank during a difficult time and leading the institution forward with a very successful IDA re-