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The Effectiveness of Profit Sharing in Reducing the US Federal Budget Deficit

Asst. Prof. Ali Abdulkadhim Dadoosh
ali.abd2102p@coadec.uobaghdad.edu.iq

Abstract: The policy of profit distribution between central banks and governments is a common practice worldwide. However, its mechanisms and details vary from one country to another. The primary objective is to contribute to increased public revenue, and it is important to understand this practice and its effects on the government budget and monetary policy.

Profit distribution does not literally mean dividing profits, as it is either a direct division of profits between the central bank and the government or the transfer of part (or all) of the profits to the state's public treasury after deducting the necessary reserves and expenses for the central bank. Moreover, the legal frameworks regulating this policy vary from country to country based on laws and regulations, which affects how profits are distributed and their size.

Iraq suffers from a persistent budget deficit, leading to significant domestic debt—more than 75% of the debt is owed to the Central Bank of Iraq. The Iraqi government relies on oil revenues to finance the public budget, causing a major imbalance in the country's economic performance. Conversely, monetary policy has achieved important successes in confronting crises, in addition to accumulating annual profits during the period 2015-2024. Hence, a profit distribution policy could serve as a financial buffer to diversify sources of public revenue and/or finance the budget deficit, increase revenue, attract investments, and consequently, boost productive sectors in the country.

Key words: Profit distribution policy, Central bank profits, Public budget deficit, Public debt, Iraqi economy, Monetary Finance.

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Introduction:

Monetary policy, along with fiscal policy, is one of the most important tools that countries rely on to stimulate and revitalize the economy, in addition to planning future visions to keep pace with continuous global economic developments. With established economic theories and the

emergence of ideas from specialized individuals and researchers, it has become necessary to present these ideas for discussion and implementation.

Many diverse ideas have emerged in the realm of economic policies, especially monetary policy, as it is the primary tool for addressing economic and non-economic crises that occur globally. Among the most important ideas that have emerged is the attempt to develop monetary theory into Modern Monetary Theory (MMT), making it more flexible in financing governments. The policies of monetary financing and quantitative easing, among other tools and policies of central banks, have been used to resolve crises (the 2008 financial crisis and the 2020 health crisis).

Some countries were compelled to add or amend laws regarding central banks as a measure to confront crises. Addressing crises depends on the financial capacity of governments, and this is provided by central banks in the context of deficits and public debt. **One of these central banks is the Federal Reserve Bank, which in 1993 added an important provision of profit distribution (profit-sharing) with the US Treasury Department to finance increasing public expenditures, especially after the US deficit and public debt rose to record levels.**

Iraq suffers from a persistent public budget deficit except in some years when surpluses were achieved due to high oil prices. In light of the rentier nature of its economic performance and reliance on oil revenues, with a lack of economic diversification, any economic or non-economic crisis, whether external or internal, means a negative impact on public revenues. Then, there is recourse to domestic debt (monetary financing) and external debt from international financial institutions to finance the deficit. This deficit has specifically exacerbated domestic debt, which has negative consequences for the current state and future of the Iraqi economy.

In light of this, we propose a policy of profit-sharing by the Central Bank of Iraq to finance the budget deficit, or one of the other instruments of profit distribution mentioned in the research. Or, alternatively, transferring part of the profits to a special fund for financing and investing the debt, which would lead to an increase in public revenues.

Importance: The policy of profit distribution between central banks and their governments is used by developed countries, particularly the United States, providing additional financial space and capacity for governments to address economic and non-economic crises that require increased spending for mitigation.

Problem: The policy of profit distribution faces legal, administrative, and regulatory problems. On the other hand, the government's reliance on the traditional budget method (line-item budgeting) does not allow for the use of this policy in Iraq.

Hypothesis: The hypothesis is based on the profit-sharing policy in the United States and its potential applicability in Iraq to address financial problems arising from both economic and non-economic crises.

Objective: The research aims to explain the profit-sharing policy between the Federal Reserve and the US Treasury Department and then present a proposal for applying this policy in the context of Iraq.

Literature Review

1- Concept of Profit Distribution Policy

The division of earnings, as per Section 7 of the Federal Reserve Banks Act, is divided between (The Fed) themselves, the Board of Governors of the Fed System, and the U.S. Treasury. The main stages of the profit distribution process are as follows:

A. Profit Calculation: The Federal Reserve Banks' profits are calculated annually by combining all revenues, such as interest on assets, operating costs, and credit losses.

B. Profit Reserve: A portion of the profits is allocated to the Federal Reserve Bank's surplus fund. The size of the profit reserve is intended to remain high, enhancing the stability of the Federal Reserve Bank.

C. Maximum Profit: The law sets a ceiling for reserve funds, and any funds exceeding this ceiling are transferred to the Board of Governors of the Fed System.

D. Surplus Profit Division: The surplus profits are divided by the Board of Governors of the Federal Reserve System into four parts:

✓ The first half is allocated to the U.S. Treasury.

✓ A quarter of the second half is given to the Federal Reserve Banks.

✓ A quarter of the second half is allocated to the Board itself to finance its activities.

✓ A quarter of the second half is deposited in the profit reserve.

E. Distribution of Fed Profits: The profits of the Fed's are distributed to the shareholders of the bank, who are member banks of the system.

2- Objectives of Federal Reserve Bank Profit Distribution

a) Ensuring the Stability of the Fed's System: The profit reserve contributes to ensuring the ability of the Federal Reserve Banks to deal with economic fluctuations.

b) Distributing Profits to System Member Banks: This distribution supports the stability of the banking system.

c) Funding the Activities of the Board of Governors: The funds allocated to the Board finance its activities, including research and banking supervision.

d) Allocating Funds to the Public Treasury: The funds allocated to the public treasury support the activities of the federal government.

Results and Discussion

3- Analysis of the Federal Reserve Bank's Profit Distribution Policy

3-1 Profits and Excess Funds at Reserve Banks :

3-1-1 Shareholder Profits

3-1-1-1 Amount of Profits: After paying or providing all necessary expenses for the Federal Reserve Bank, shareholders of the bank are entitled to annual profits on paid-in capital shares at a rate equal to the lesser of: For a shareholder with consolidated total assets exceeding $10,000,000 trillion, it’s the lesser of:

➢ (%6) the rate that is equal to the high yield of 10-year Treasury bonds issued in the last auction held before payment of these profits.

➢ (%6) or less for a shareholder with consolidated total assets of $10,000,000 trillion.

3-1-1-2 Cumulative Profits: The right to receive profits under subparagraph (a) is cumulative.

3-1-1-3 Inflation Adjustment: The Board of Governors of the Federal Reserve System annually adjusts the dollar amounts of consolidated total assets specified under subparagraph (a) to reflect the change in the GDP price index, published by the Bureau of Economic Analysis.

3-2 Transfer of Net Profits to Surplus Fund

That portion of the net profits of each Fed that remains after satisfying profit claims under subparagraph (1)(a) in full must be deposited in the bank's surplus fund.

3-3 Restrictions on Excess Funds

Generally, they are determined as follows: [1]

A. Total amount of excess funds at Federal Reserve Banks shall not exceed $6,825,000 trillion.

B. Transfer to the General Fund: Any excess funds at Federal Reserve Banks that exceed—or would cause them to exceed—the limit set out in subparagraph (a) are transferred to the Board of Governors of the Federal Reserve System for transfer to the Secretary of the Treasury for deposit into the General Fund of the Treasury.

3-4 Amendment of Profit Distribution (Transfer) Policy for Fiscal Year 2000 (Updated)

A. The Fed shall transfer a total amount of $3,752,000 trillion from their excess funds to the Board of Governors of the Federal Reserve System for transfer to the Secretary of the Treasury for deposit into the General Fund of the Treasury in fiscal year 2000.

B. The Board determines the amount each of these banks must pay in that fiscal year and future years.

C. The surplus fund is prohibited from being replenished during the fiscal year 2000, and no Federal Reserve Bank may replenish its surplus fund by the amount of any transfer by that bank under paragraph (1).

4- Using Profit Distribution to Finance Government Deficit

The net profits that the United States obtains from the Federal Reserve Banks are used, at the discretion of the Secretary of the Treasury, to supplement the gold reserve held against outstanding United States bonds or are applied to reduce outstanding debt on United States bonds under regulations determined by the Secretary of the Treasury.

If a Federal Reserve Bank is dissolved or liquidated, any remaining surplus after payment of all debts and profit requirements as previously stipulated, and the face value of the shares, is paid to the United States government (the Treasury Department), becomes its property, and is applied similarly [2]**.**

Federal Reserve Banks, including their capital and surpluses, and the income derived from them, are exempt from federal, state, and local taxes, except for real estate taxes. Table (1) below shows the amounts of divided profits and their contribution to financing the public budget deficit in the United States for the period (2008-2022):

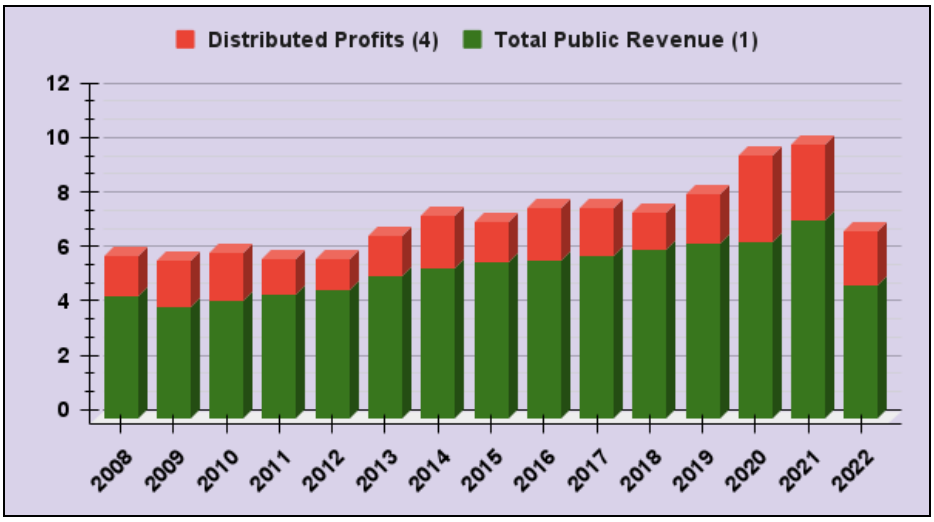
Table (1): Funding the US Deficit through Distributed Profits for the Period (2008-2022) (Trillions)

Year	Total Public Revenue (1)	Total Public Expenditure (2)	Deficit (3)	Distributed Profits (4)	Ratio 4/1
2008	4.509	5.484	(0.975)	1.500	33.2
2009	4.085	5.992	(1.907)	1.752	42.8
2010	4.329	5.982	(1.653)	1.752	40.4
2011	4.536	6.050	(1.514)	1.324	29.1
2012	4.731	6.048	(1.317)	1.129	23.8
2013	5.270	6.036	(0.766)	1.458	27.6
2014	5.507	6.217	(0.710)	1.945	35.3
2015	5.764	6.407	(0.643)	1.455	25.2
2016	5.829	6.646	(0.817)	1.905	32.6
2017	5.969	6.904	(0.935)	1.766	29.5

2018	**6.207**	**7.299**	**(1.092)**	**1.388**	**22.3**
2019	**6.461**	**7.689**	**(1.228)**	**1.789**	**27.6**
2020	**6.489**	**9.438**	**(2.949)**	**3.215**	**49.5**
2021	**7.320**	**10.029**	**(2.709)**	**2.752**	**37.5**
2022	**4.900**	**6.270**	**(1.370)**	**2.010**	**41.0**

Source :1- The Federal Reserve, Monetary policy Report (2008-2023). https://fiscaldata.treasury.gov/datasets/monthly-treasury-statement/outlays-of-the-u-s-government. 2- US fiscal deficit data from: US Department of Treasury and Office of Management and Budget, 'Financial Report of the United States Government', Bureau of the Fiscal Service (Report 2008–2022). https://fiscaldata.treasury.gov/americas-finance-guide/federal-spending. Ratios calculated by the researcher(Figure 1) .

Figure (1) Total Revenue and Distributed Profits



It is observed that the US government resorts to financing the public budget deficit by borrowing money through **the sale bonds, Treasury bills, and other securities, such as mortgage-backed securities, credit and liquidity facilities, etc**. Consequently, the public debt is the accumulation of this borrowing with the associated interest due to investors who purchased these securities. **Since the federal government suffers from a persistent deficit,** which is common, the public debt grows more than the deficit **[3] .**

In addition to the aforementioned deficit financing, the profit-sharing policy allows the US government to finance its fiscal deficit. It reached approximately $975 billion in 2008 and increased to approximately $2.949 trillion in 2020 due to the health shock that led to a rise in public spending. **Given decreased public revenues, the highest amount for profit sharing was resorted to, which accounted for about 49.5% of total public revenues, helping significantly in financing expenditures allocated for emergencies and the process of containing the health crisis at that time.**

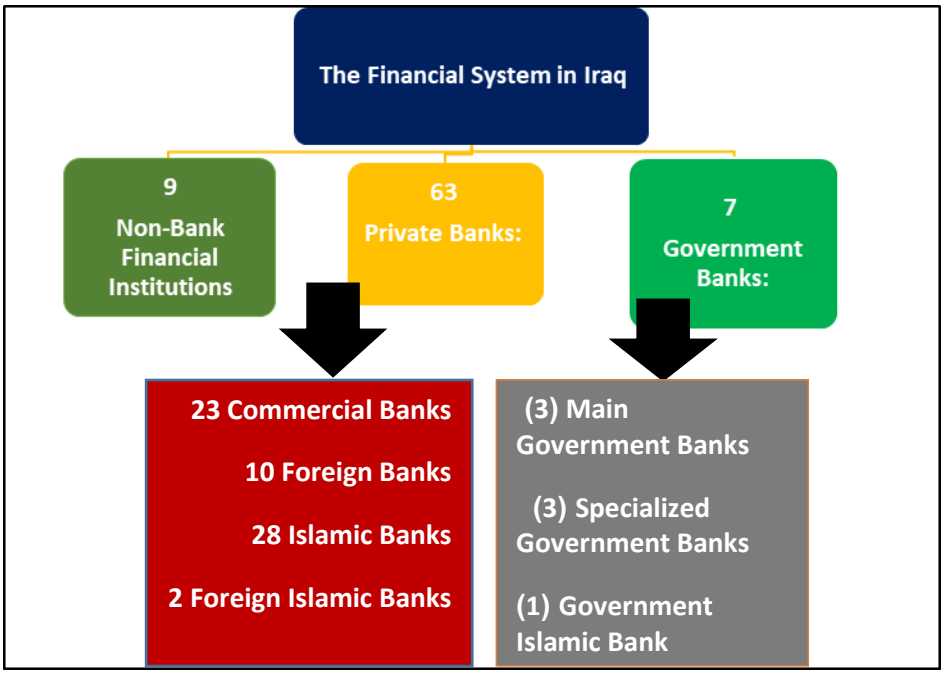
5- The Reality of the Financial System in Iraq after 2003

The financial system is viewed as an interactive and interconnected system (a set of responsive inputs connected through processes to achieve specific goals and measuring the extent to which these goals are achieved). The financial system is a collection of different markets, or a group of financial institutions, whose function is to balance savings and investments. The financial system is one of the most important indicators of the government, where it shows its financial and economic capacity.

In Iraq, the financial system typically encompasses all financial institutions, markets, individuals, laws, regulatory procedures, and technologies through which financial and cash assets such as treasury bills, bonds, and stocks are traded. In contemporary and advanced societies, the role of the financial system is essential in ensuring the transfer of surplus financial resources from savers to borrowers for investment or consumption. In other words, it makes funds available for lending and borrowing to all, as well as providing financial means and tools that contribute to enhancing the country's economic development (financial), thereby raising the standard of living of the society members. Over the past few years, the Central Bank of Iraq has initiated steps to build a sound, strong, and stable financial system, recognizing its significant role in achieving financial and economic stability. This has encouraged the Bank to make financial stability the primary stated goal within its 2016-2020 strategy.

Chart (1) shows that the financial system in Iraq includes approximately 70 banks and 9 non-bank financial institutions. The financial system is dominated by government banks, which own more than 78% of the total assets of the banking sector. However, in return, these banks suffer from significant weaknesses in operations and banking services due to many diverse reasons, including the lack of incentive for employees to develop their activities or contribute to financial innovation (financial technology). This lack of incentive is due to continued payment of their salaries and wages whether or not they contribute to development, as well as bureaucracy and other reasons.

(Chart 1) Structure of the Financial System in Iraq as of 2023



Source: Researcher based on data from the Financial Stability Report of the Central Bank of Iraq, 2023.

Private banks, despite the increase in their total assets to more than 21%, have not been able to stimulate the overall economic sectors—which is the basis of their banking operations. This is because they have relied on the window of selling foreign currency throughout the period (2004-2022) for the existence of guaranteed profits, in addition to the weak investment environment and the total reliance on imported goods and services to meet the entire local demand in the country.

6- Mechanism for Financing the Deficit and Managing Public Debt in Iraq after 2003

The public budget has been affected by the structural imbalances of the Iraqi economy. It relies on oil revenues for approximately 92-96% of its revenue, which fluctuates periodically depending on geopolitical situations, as well as other economic factors such as global supply and demand for

energy. From this perspective, the financial, military, and health crises that occurred in 2008, 2014, and 2020, respectively, directly impacted the Iraqi economy. This resulted in a decrease in oil revenues in the face of increased public expenditures to address the crises, thus creating a fiscal deficit in certain years.

The Iraqi government also resorted to the Central Bank, specifically through discounted bills (monetary finance), to finance the accumulated deficit, leading to public debt. This measure addressed the aforementioned crises, but due to poor planning and sound management of spending, as well as the imbalance in the production structure—the weak flexibility of the production system—and the reliance on imported goods to meet local consumer demand, it has led to an increase in public debt in Iraq **[4]** .

Undoubtedly, government spending in Iraq relies mainly on oil revenues, in addition to other revenues represented by tax revenues (customs, etc.) and fees. Direct and indirect taxes, customs duties, fines, as well as capital revenues, state property rental revenues, and transfer revenues and government services to other entities, as well as other unclassified revenues. The proportion of these revenues does not exceed 3-4% of the total public revenues at best **(Iraqi Public Budget Law, Article 1, first).**

The process of financing the public budget deficit in Iraq is through domestic borrowing, especially from commercial banks and financial institutions within the country, as well as the government issuing bonds and bills to government banks that are discounted at the Central Bank of Iraq, which is called (monetary financing). External borrowing is through loans granted by (the World Bank, the International Monetary Fund, the Japan International Cooperation Agency, the French Development Agency, as well as issuing foreign bonds). Table (2) shows the size of the public budget (actual expenditures and revenues) in Iraq during the period (2015-2024):

Table (2): Public Budget in Iraq during the Period (2015-2024) (Trillion Dinars)

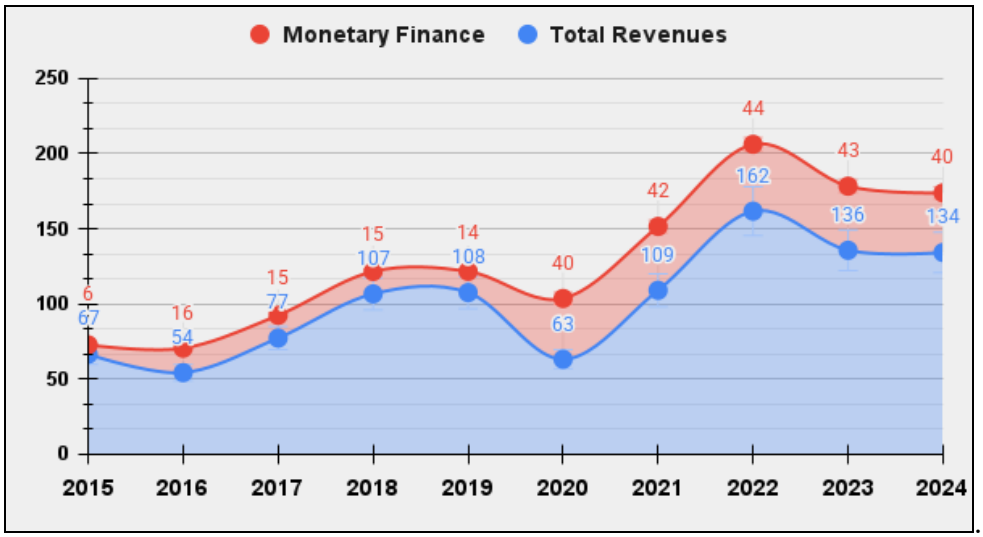
Year	Total Revenues	Total Expenditures	Surplus/Deficit	Monetary Finance [1]	Monetary Finance as % of Total Revenue
2015	66.569	70.498	(3.929)	6.225	9.3
2016	54.341	67.106	(12.765)	16.225	29.8
2017	77.307	75.543	1.764	15.125	19.5
2018	106.687	80.961	25.726	14.925	13.9
2019	107.566	111.723	(4.157)	14.125	13.1
2020	63.199	76.082	(12.883)	40.452	64.0
2021	109.081	102.847	6.234	42.452	38.9
* 2022	161.697	116.959	44.738	44.450	27.4
2023	135.681	142.435	(6.754)	42.632	31.4
** 2024	134.215	156.345	(22.130)	39.654	29.9

Source: Iraqi Ministry of Finance, Economic Department, Technical Information Section, various years for the period (2015-2024 Q1). * The budget law was not ratified in 2020 and 2022 for various reasons. Ratios calculated by the researcher. Preliminary Data. [5]

[1] Monetary Finance : This refers to discounted bills (cash amounts) paid by Central Bank of Iraq indirectly finance the budget deficit through the secondary market.
For more information, please refer to: (Dadoosh, Ali Abdul Kadhim, "The Impact of Monetary Financing on the Public Budget: International Experiences with a Focus on Iraq," PhD dissertation, University of Baghdad, College of Administration and Economics, Department of Economics, p. 131, 2024)."

The public budget recorded a deficit in the years (2015, 2016, 2019, 2020, and 2023) due to military, financial, and health crises. With increased public spending and the accumulation of deficits in the public budget, in addition to the failure to invest the financial surpluses that were achieved in many years, which amounted to more than 80,332 trillion dinars, this led to the exacerbation of the total public debt (domestic and external) with its interests, causing an imbalance in the basis of the operation of public finance in Iraq .Figure (2)

Figure (2) Total Revenues and Monetary Finance in Iraq



The percentage of monetary financing (discounted bills) to total revenues was calculated as it has become clearly included in the public budget, specifically within the deficit financing item. Therefore, it has reached record rates. In 2020, it reached about 64% of total public revenues due to the repercussions of COVID-19, the disruption of international trade, and the collapse of oil prices. These amounts are recorded in the domestic debt items belonging to the Central Bank of Iraq, government banks, and others. Table (3) shows the structure of domestic and external public debt during the period (2015-2024):

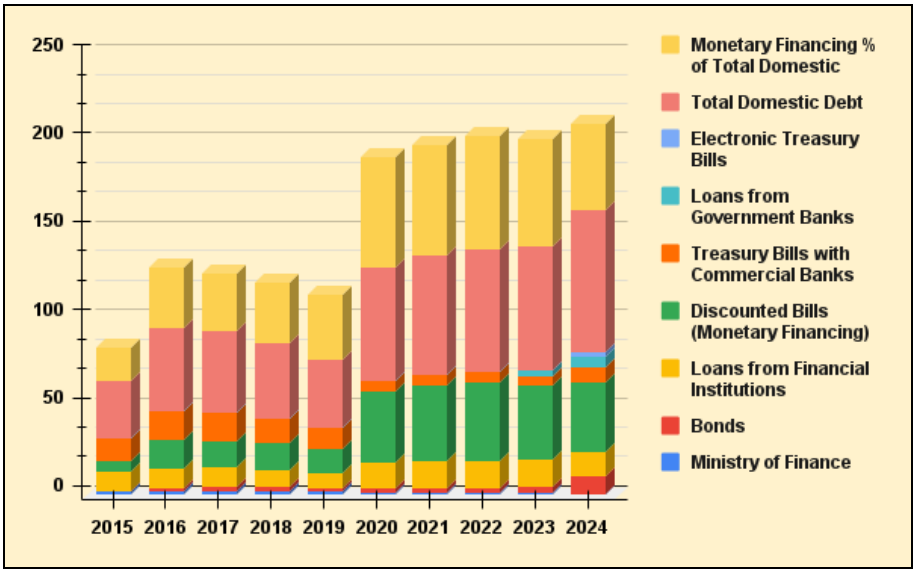
Table (3): Structure of Domestic and External Public Debt in Iraq during the Period (2015-2024) (Trillion Dinars)

Year	Ministry of Finance Debt	Bonds	Loans from Financial Institutions	Discounted Bills (Monetary Financing)	Treasury Bills with Commercial Banks	Loans from Government Banks	Electronic Treasury Bills	Total Domestic Debt	Monetary Financing % of Total Domestic Debt	External Public Debt	Total Public Debt*
2015	2.355	0	10.461	6.225	13.086			32.127	19.3	46.791	78.918
2016	2.355	1.696	10.546	16.225	16.538			47.360	34.2	46.662	94.022
2017	2.155	2.682	10.546	15.125	16.069			46.577	32.5	49.499	96.076
2018	1.955	2.953	9.501	14.925	13.487			42.821	34.9	49.775	92.596
2019	1.755	1.921	8.651	14.125	11.877			38.329	36.9	31.905	70.234
2020	1.555	1.916	14.668	40.452	5.653			64.244	63.0	29.823	94.067
2021	1.555	2.097	15.962	42.452	5.843			67.909	62.5	26.550	94.459
2022	1.555	2.031	15.778	44.450	5.677			69.491	64.0	24.345	93.836
2023	1.255	3.291	15.261	42.632	5.106	3.000		70.545	60.4	22.589	93.134
2024	0.755	9.834	13.381	39.654	9.021	5.900	2.030	81.006	49.0	19.536	99.356

Source: 1-Central Bank of Iraq, Statistical Website available at: https://cbiraq.org/SubCategoriesTable.aspx?SubCatID=101 . 2- Iraqi Ministry of Finance, Public Debt Department, Various years, total external public debt. Total public debt calculated by the researcher.

The rise in the volume of debt in general, especially domestic debt, is noticeable, reaching about 81 trillion dinars during November 2024, which is a record level and negatively affects the reality of the Iraqi economy, especially on the currency issued and inflation. Conversely, external debt is decreasing due to its connection to a specific schedule according to Iraqi crude oil sales, as higher oil prices directly helped in its decline(Figure 3) .

Figure (3) The Structure of Domestic Debt in Iraq



The ratio of monetary financing to total domestic debt, which is the basis of the research, increased from 19.3% in 2015 to about 64% in 2022, which means that the government relies heavily on monetary financing. **It has become an item written in the public budget to finance the deficit, and this is a clear interference in the independence of the Central Bank of Iraq.**

7- Proposal for a Profit-Sharing Policy of the Central Bank to Finance the Deficit in Iraq

The profits of the CBI are the result of managing its assets and reserves, whether in local or foreign currency. These profits differ from tax revenues or oil revenues, as they are the result of financial activity. Using these profits to finance the deficit or public debt requires careful study to ensure that the stability of the macro economy and the independence of the central bank are not harmed. Hence, the experiences of developed countries, particularly the United States, can be benefited from, as stated in the Federal Reserve Act No. 7 on profit sharing.

7-1 Types of Profits of the Central Bank of Iraq

a) Market Operations Profits: These are the profits resulting from buying and selling foreign currencies and government bonds.

b) Investment Profits: These are the profits resulting from investing the central bank's reserves in various financial instruments.

c) Other Profits: These are the profits resulting from other activities carried out by the central bank, such as fees for services provided to banks, etc.

According to Article (6) of the CBI Law of 2004, the bank must, within (3) months from the end of each fiscal year, determine its net profits available for distribution or its net losses. If the bank incurs operating losses for any fiscal year, the loss shall first be charged against the general reserve and then against capital within 3 months from the end of any fiscal year. The bank's board of directors shall distribute net profits as follows: [6].

(%80) of the net profits available for distribution to the general reserve account of the Central Bank of Iraq until the value of the amount in this account reaches 10% of the total assets of the Central Bank of Iraq.

The remainder of the net profits available for distribution shall be transferred to the emergency reserve account.

On December 23, 2015, the Board of Directors of the Central Bank of Iraq decided to amortize the net operating loss as of December 31, 2014, which amounted to 1,996,29 trillion dinars from the general reserve. On September 29, 2016, the Board of Directors decided to amortize the net operating loss as of December 31, 2015, which amounted to approximately 617.229 billion dinars from the general reserve. Table (4) below shows the volume of profits of the CBI during the period (2015-2023), according to what is stated in the financial statements reports:

Table (4): Profit/Loss and General Reserve of the Central Bank of Iraq during the Period (2015-2023)

Year	Revenues	Expenditures	Profit/Loss	General Reserve	Emergency Reserve
2015	(681.715)	347.893	(1.029.608)	1.462.461	1.089.690
2016	50.290	87.385	(37.095)	845.232	1.089.690
2017	4.185.091	172.815	4.224.332	477.425	1.089.690
2018	1.745.387	166.661	1.578.726	3.304.037	1.796.342
2019	3.177.425	154.786	3.022.639	4.598.391	2.119.931
2020	16.886.168	212.151	16.674.017	4.309.866	2.547.799
2021	1.390.141	178.740	1.211.401	15.315.943	5.299.371
2022	3.444.554	313.601	3.130.953	14.540.071	5.605.351
** 2023	6.338.090	462.450	5.875.640	11.550.273	6.107.901

Source: Central Bank of Iraq, Financial Data, Financial Statements for the years 2016-2023.

The Board of Directors also decided on March 29, 2018, to transfer the retained earnings for 2017, which amounted to approximately 4,224.332 trillion dinars, to the general reserve and emergency reserve accounts, taking into account the impact of applying the financial reporting standard No. 9 on the opening balances of retained earnings for 2018, which amounted to 2.344 trillion dinar .[7]

Thus, the Central Bank of Iraq annually transfers its net profits to the general and emergency reserve accounts. The highest profits were achieved in 2020, with more than 16 trillion dinars. As a result, the general and emergency reserve accounts were strengthened by more than 15 and 5 trillion dinars, respectively.

It is observed that the good management of the central bank has achieved important profits that have helped in the stability of monetary variables in general and inflation rates in particular except during the COVID period and its aftermath. In return, the public budget was affected by a large deficit, especially during the triennial budget (2023-2025), which generated a large domestic debt that reached 81 trillion dinars by the end of 2024. **All of this can be remedied by resorting to a profit-sharing policy in accordance with the best mechanisms outlined in paragraph (7-3).**

7-2 Legal and Regulatory Framework for a Profit-Sharing Policy

7-2-1 Central Bank of Iraq Law: The law determines the powers and objectives of the central bank. Any profit sharing must be compatible with this law or a modification must be made, such as adding a paragraph on profit-sharing with the government by the legislative authority, in order to be consistent and enforceable.

7-2-2 Independence of the Central Bank: The independence of the central bank must be maintained, and any political or financial pressures that may affect its decisions should be avoided.

7-2-3 Core Objectives: Profit sharing should not compromise the central bank's ability to achieve its core objectives, which are maintaining price stability and financial system stability.

7-2-4 Sharing Mechanism: The profit-sharing mechanism should be clear and transparent, and it should be established by law, as mentioned above.

7-3 Mechanisms for Profit Sharing with the Government

7-3-1 Direct Transfer of Profits to the Public Treasury

- **Mechanism**: A portion of the central bank's profits is directly transferred to the state's public treasury account.
- **Advantages**: A simple and clear mechanism that contributes to financing the deficit or public debt.
- **Disadvantages**: May affect the central bank's independence and may create an incentive for the government to pressure the central bank to increase its profits.
- **Caveat**: This mechanism should be used cautiously, with a ceiling on transfers, and ensuring that it does not affect the central bank's ability to achieve its objectives[8] .

7-3-2 Purchase of Government Bonds by the Central Bank

- **Mechanism**: The government issues government bonds, and the central bank purchases them using a portion of its profits.
- **Advantages**: An effective mechanism for financing the deficit or public debt, and contributes to public debt management.
- **Disadvantages**: May lead to an increase in the amount of money in circulation and may affect inflation if not managed carefully.
- **Caveat**: This procedure should be carried out cautiously and within the framework of the agreed-upon monetary policy.

7-3-3 Direct Use of Profits to Reduce Public Debt

- **Mechanism**: The central bank directly uses a portion of its profits to purchase and retire a portion of the public debt.
- **Advantages**: Contributes to directly reducing public debt.
- **Disadvantages**: May have a limited effect in the short term if the size of the public debt is large.
- **Caveat**: This procedure should be carried out transparently and coordinated with the Ministry of Finance[9] .

7-3-4 Transfer of a Portion of Profits to a Special Fund for Debt Financing

- **Mechanism**: A special fund for public debt financing is created, and a portion of the central bank's profits is transferred to this fund.
- **Advantages**: A more transparent mechanism that contributes to the efficient management of public debt.
- **Disadvantages**: May require complex legal and administrative procedures to establish a new fund.
- **Caveat**: This fund should be subject to oversight and audit, and its funds should be used effectively.

7-4 Basic Controls and Criteria for Profit-Sharing Policy

A. Coordination with the Ministry of Finance: Profit sharing should be carried out in full coordination with the Ministry of Finance and within the framework of the state's overall economic policy.

B. Transparency and Disclosure: All profit-sharing operations should be transparent, and fully disclosed to the public.

C. Review and Audit: All profit-sharing operations should be subject to review and audit by the competent authorities.

D. Maintaining Reserves: The central bank must maintain an adequate level of foreign reserves to ensure the stability of the exchange rate.

E. Avoiding Inflation: Profit sharing should not lead to an increase in inflation, and liquidity should be managed wisely.

8- Conclusions and Recommendations

The sharing of central bank profits with the government to finance the deficit or public debt is a sensitive and complex issue that requires careful study of all legal, economic, and social aspects. The main goal should be to achieve a balance between financing the government and maintaining macroeconomic stability and the independence of the Central Bank of Iraq.

Profit sharing with the government to finance the deficit or public debt may be necessary in some cases, but it should be done very cautiously, within a clear legal and regulatory framework, and taking into account the core objectives of the Central Bank of Iraq as established in its 2004 law.

Based on the above, the researcher recommends that the best mechanism is to transfer a portion of profits to a special fund for financing public debt, with strict controls in place to ensure that these funds are used effectively and transparently. A specific profit-sharing percentage should be determined, perhaps between (40-50%) of the total profits of the Central Bank of Iraq. I also emphasize the need for full coordination with the Ministry of Finance, requiring a shift from the traditional line-item budgeting to a more developed approach **(such as program and performance budgeting),** and effective communication with the public to ensure the support of these measures from all parties, with data published quarterly and audited by a specialized international auditing firm.

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