



Office of Inspector General

October 15, 2014

Ms. Dana J. Hyde
Chief Executive Officer
Millennium Challenge Corporation
875 15th Street, NW
Washington, DC 20005

Dear Ms. Hyde:

The enclosed statement summarizes the Office of Inspector General's (OIG's) conclusions on the most serious management and performance challenges facing the Millennium Challenge Corporation (MCC). We based decisions on which challenges to report primarily on audits and analyses of MCC's operations. More challenges may exist in areas that we have not yet reviewed, and other significant findings may result from future work.

The Reports Consolidation Act of 2000 (Public Law 106-531) requires that agency performance and accountability reports include a statement prepared by each agency's inspector general summarizing the most serious management and performance challenges facing the agency and reporting the agency's progress in addressing those challenges. The enclosed statement will be included in MCC's fiscal year 2014 agency financial report.

We have discussed the management and performance challenges summarized in this statement with the responsible MCC officials. If you have any questions or wish to discuss the statement further, I would be happy to meet with you.

Sincerely,

/s/

Michael Carroll
Acting Inspector General

Enclosure: a/s

**Statement by the Office of Inspector General on the Millennium Challenge Corporation's
Most Serious Management and Performance Challenges
Fiscal Year 2014**

The Millennium Challenge Corporation (MCC) provides foreign aid to countries that meet its policy indicators of ruling justly, investing in people, and encouraging economic freedom. By 2014, 25 countries had met these requirements and been awarded approximately \$10 billion in compact agreements. The agreements are designed to reduce poverty and increase economic growth through projects in sectors such as agriculture, education, transportation, and water and sanitation. At the end of the fiscal year, MCC had eleven current compacts worth \$3.8 billion: Cabo Verde II, El Salvador II, Georgia II, Ghana II, Indonesia, Jordan, Malawi, Moldova, Philippines, Senegal, and Zambia. MCC continues to face its most serious management challenges in the following areas:

- Developing Compacts
- Implementing Compacts
- Sustaining Compact Benefits
- Managing Finances Efficiently

MCC has taken action to mitigate a serious challenge that was reported last year concerning its management of information technology.

Developing Compacts

MCC and its partner countries take approximately 2 years to develop compacts. They do preparatory analysis, project definition, project development and appraisal, compact negotiation and signing, and preparation for entry into force. Once a compact enters into force, the fixed, 5-year implementation period starts. The compact development process is collaborative, involving partner-country stakeholders and MCC.

A recent Office of Inspector (OIG) review identified the need for improvements in compact development, specifically in setting compensation for employees at Millennium Challenge Accounts (MCAs).

- In a July 2014 review,¹ OIG reported that MCC gave limited guidance to MCAs on compensation practices. Further, MCC did not follow its policy requiring that employment agreements for all key MCA personnel be maintained at headquarters and did not systematically share information on staffing practices at the MCAs. Finally, MCAs did not all hire key staff before entry into force, potentially delaying compact implementation.

¹ *Review of the Millennium Challenge Account Employee Compensation*, Report No. M-000-14-003-S, July 16, 2014.

Implementing Compacts

MCC and its partner countries, through MCAs, complete the compact implementation process over the 5-year compact term. Each MCA is staffed by a team of professionals in management, procurement, finance, monitoring and evaluation, and law and by specialists in sectors covered by the compact, such as infrastructure and agriculture. The MCA procures contractors to implement the compact projects and oversees them with the assistance of contracted specialists.

A recent audit of two projects in Namibia, the Education Project and the Tourism Project, illustrates challenges encountered during compact implementation.

- In this audit report,² OIG reported that although the education and tourism projects were achieving their compact goals, project implementation needed improvement. Auditors found that five of six schools visited had construction deficiencies, two of the six schools renovated with MCC funding were too small to accommodate current students, and teachers lacked training on science equipment provided by MCC. For the tourism project, the MCA had not conducted audits of environmental compliance by conservancy grantees, as required by the grants.

Sustaining Compact Benefits

To ensure that project benefits can be sustained over time, MCC requires that sustainability be part of compact design and development. Sustainability can take a number of forms, like requiring a partner country to increase its contributions to a road maintenance fund so that when the MCC-funded road is completed, the partner country has adequate funding for upkeep. A recent OIG audit³ showed that sustainability measures could be improved.

- OIG reported that the sustainability of certain project activities was at risk. Five of six renovated schools had construction deficiencies such as cracks in walls and foundations and leaking roofs that jeopardized their functionality. Also, the MCA provided governance training to current governing representatives, but did not implement a process for transferring training knowledge to future conservancy board members.

Managing Finances Efficiently

Strong financial management is critical to effective and efficient operations. MCC must not only manage its finances well but also see that MCAs do so.

MCC received an unqualified audit opinion on its fiscal year (FY) 2013 financial statements and demonstrated progress in improving its financial management practices. The audit report cited one material weakness and three significant deficiencies in internal control. One issue in particular represents an ongoing challenge to MCC's ability to prepare complete, reliable financial statements.

² *Audit of the Millennium Challenge Corporation-Funded Program in Namibia*, Report No. M-000-14-002-P, December 17, 2013.

³ Ibid.

- MCC's financial management system follows the guidance prescribed by the Federal Accounting Standards Advisory Board, whereas the independent MCAs established by recipient countries do not. MCC addresses this challenge by adjusting its grant liabilities at headquarters in order to bring the cash-basis reporting by MCAs in line with MCC's accrual basis. In 2012, MCC revised its grant accrual methodology, and it now estimates accruals by examining disbursement history, unused spending authority, and invoices received but not paid. MCC continues to accumulate disbursement data from MCAs for its data warehouse use. In developing its accrual estimates, MCC also continues to implement its accrual validation process. However, accumulating sufficient MCA disbursement data to reasonably validate grant accrual estimates is still challenging and time consuming. In addition, MCC further revised its grant accrual validation process in FY 2014. As we perform the current financial statement audit, we continue to examine MCC's method for estimating accruals.

Managing Information Technology

Since FY 2008, OIG has reported information technology (IT) management challenges that affect MCC. Last year, those challenges related to MCC's privacy program, IT governance, and IT security.

This year OIG does not consider IT a management challenge. Although OIG has not yet verified whether the weaknesses were fully corrected, MCC indicated it had taken final action on significant recommendations that affect the Corporation's privacy program⁴ and IT governance.⁵ In addition, a recent audit⁶ confirmed that MCC corrected significant IT security weaknesses that we previously reported.⁷

To keep the focus on IT in FY 2015, OIG plans to follow up on recommendations related to MCC's IT governance. In addition, OIG plans to conduct an audit of MCC's IT security, which will assess aspects of the Corporation's privacy program. Depending on the results of these audits, IT may be identified as a management challenge next year.

⁴ *Follow-up Audit of the Millennium Challenge Corporation's Implementation of Key Components of a Privacy Program for Its Information Technology Systems*, Report No. M-000-12-002-P, March 30, 2012.

⁵ *Risk Assessment of the Millennium Challenge Corporation's Information Technology Governance Over Its Information Technology Investments*, Report No. M-000-11-001-O, June 1, 2011.

⁶ *Audit of the Millennium Challenge Corporation's Fiscal Year 2014 Compliance With the Federal Information Security Management Act of 2002*, Report No. A-MCC-14-008-P, September 12, 2014.

⁷ *Audit of the Millennium Challenge Corporation's Fiscal Year 2013 Compliance With the Federal Information Security Management Act of 2002*, Report No. M-000-13-005-P, September 20, 2013, and *Audit of the Millennium Challenge Corporation's Fiscal Year 2012 Compliance With the Federal Information Security Management Act of 2002*, Report No. M-000-13-001-P, November 6, 2012.