

Millennium Challenge Corporation

Public Financial Management Due Diligence Guidance



MILLENNIUM
CHALLENGE CORPORATION
UNITED STATES OF AMERICA

Due Diligence Methodology

Fiscal Agent

Introduction

The Fiscal Agent due diligence process is the procedure MCC undertakes to assess the capability of a proposed government entity to fulfill the roles and responsibilities of a Fiscal Agent. When an eligible country proposes the use of an internal entity to serve as fiscal agent, the MCC will perform an examination, or due diligence assessment, to ensure that the proposed entity has the capacity to handle the financial management requirements of the compact. In this context, “capacity” means the ability to provide reasonable assurance that compact funds

1. will be used for the intended purposes
2. will achieve good value for the money spent
3. will be accounted for properly and in accordance with MCC requirements

This document describes the functions and structures a proposed entity must have to meet the MCC requirements. Eligible countries can use these guidelines, in conjunction with the Country System Assessment Questionnaire, to determine which, if any, internal entity has the capacity to serve as the compact’s fiscal agent.

There are eight areas of financial management functioning that need to be assessed:

1. Legal structure of the proposed entity
2. Staffing
3. Budgeting
4. Automated accounting system
5. Accounting policies and procedures
6. Funds control and funds flow processes
7. Financial reporting processes
8. Auditing

Item 4, the automated system, will also require a special assessment performed by a firm that has the technical skills and abilities to perform a thorough analysis of the automated system’s structure, functions and controls. MCC will contract and pay for the firm to do this work.

The proposed entity will be assessed by means of the questionnaire and one or more site visits from Fiscal Accountability staff of the Department of Compact Development at MCC, who will work in conjunction with financial management personnel from the proposed entity to develop a joint assessment.

Financial management requirements

Legal structure of the proposed entity

The fiscal agent serves as an agent/advisor to the MCA on financial management issues. The two entities will sign a Fiscal Agent Agreement that outlines the responsibilities of both.

The MCA, as the accountable entity, has overall authority over the fiscal agent which, as an agent to the MCA, has the obligation to perform its duties in the best interest of the MCA. For example, the MCA will have the authority to hire and release personnel working for the fiscal agent, as well as oversee its work. It is important to consider these relationships when deciding on an appropriate candidate as the internal fiscal agent.

Staffing

The services of the fiscal agent will be required for approximately one year prior to entry into force, for five years during the implementation of the compact, and for a period subsequent to compact end for wrapping up the financial activities of the compact. This means that any additional personnel hired to work on compact activities for the fiscal agent may not be permanently needed by the internal entity. These staffing issues should be considered when selecting a proposed internal fiscal agent.

Budgeting systems

There are two budget issues the internal fiscal agent will contend with. The first is the compact budget. While the MCA will establish the budget for the compact projects during the period of compact development, once established, the internal fiscal agent will be required to manage the budget throughout the life of the compact. This means having the ability to establish a budgetary system in an automated accounting system, reprogram the budget as appropriate, ensure budget limits are not exceeded, and report on budget execution.

The second issue relates to the eligible country's national budget. The MCC grant, while not provided directly to the eligible country, represents a resource that the eligible country has available to it. As such, MCC requires the eligible country to reflect compact money as a source and use of funds. The fiscal agent will work with the appropriate government entity or entities to ensure that compact funds are properly presented in the national budget.

Accounting policies and procedures

The proposed entity must have an established accounting function with written policies and procedures, and a mechanism to ensure that the policies and procedures are followed by employees. The policies and procedures should cover topics such as

- ★ the required qualifications of the staff hired to perform the work and job descriptions for each position
- ★ roles and responsibilities of personnel within the unit
- ★ management's policy regarding fraud and corruption and the importance of integrity among the workforce
- ★ management's policy on the importance of strong internal controls
- ★ official travel policy
- ★ manuals and desk procedures for various accounting functions and transactions
- ★ basic accounting structures, including the chart of account, processing logic etc.
- ★ documentation of the automated accounting system
- ★ management and control of fixed assets

Funds control and funds flow processes

The funds control process is a critical duty of the fiscal agent. The control of compact funds to ensure that no commitment is made except according to the compact financial plan and that no payment is made except in accordance to commitments made is essential to the success of the compact. The fiscal agent must have mechanisms in place to ensure that funds are properly controlled and expended for compact purposes only. Furthermore, the proposed entity must have the capability to segregate MCC funds from other donor and eligible country funds. In order to do this, the MCA must have the ability to open a separate bank account in the name of the MCA with the signatory authority over the account assigned to the proposed fiscal agent.

Another important function of the fiscal agent is to make payments on behalf of the MCA. These payments range from salary payments for MCA and implementing staff to payments to contractors working on the implementation of compact projects. The MCC requires that all payments be made in a timely manner, that is that employees are paid according to the requirements of employment agreements and that vendors are paid within 30 days of receipt of a valid invoice. The fiscal agent must ensure that procedures are in place to accomplish this requirement.

Financial reporting processes

A number of stakeholders require financial information from the fiscal agent. As mentioned above under budgeting, compact funding should be reported in the national budget of the eligible country. The fiscal agent must have

the ability to provide the information to the appropriate authorities in the required format to ensure the financial information can be properly reflected.

MCC requires a number of reports from the fiscal agent. These reports must be submitted on a quarterly basis and in accordance with MCC's fiscal year end, which is September 30. The accounting system used by the proposed entity must have the flexibility to incorporate these reporting requirements into its systems. Examples of reports will be provided during the due diligence process.

Auditing

All compacts funded by the MCC must be audited every six months during the five years of the compact implementation period. The audits are performed in accordance with audit guidelines of the Office of the Inspector General of the U. S. Agency for International Development (USAID) and by local audit firms approved by USAID. It is essential, then, that the selected audit firm have access to auditable books to records and systems of the proposed internal fiscal agent. These audits will be in addition to any audits that might be required by the country's supreme audit institution.

Country System Assessment Questionnaire

Country: _____

Preparer: _____ Position: _____

Proposed Entity to perform financial management of the compact: _____

Instructions: This questionnaire is designed to help MCC gain an understanding of the structure, functions and abilities of the Entity proposed to service as Fiscal Agent. Please answer each question completely. Please provide a detailed explanation of any question that is answered “yes” or “no;” that is, provide all the information you believe is necessary to give a thorough answer.

Subject	Response	Overall Assessment	Remediations Needed
1. The Entity – serves as the Fiscal Agent to the MCA. Must take instruction from the MCA on a variety of financial management issues.			
1a. Describe the legal structure of the Entity. How was the Entity created? To what extent can the Entity act independently from other government entities?			
1b. If the Entity has previously implemented projects funded by external donors, please describe the project and the implementation structure in detail.			
1c. As the Accountable Entity for compact implementation, the MCA will have authority over the Fiscal Agent. Examples include the ability to direct work, hire and fire personnel, and evaluate performance. What problems, if any, will there be in the MCA having such authority?			
1d. How has the current management of the Entity been selected? How frequently does top management change?			
1e. Who and what agency does the management of the Entity currently report to?			

Subject	Response	Overall Assessment	Remediations Needed
1f. The Entity, as the Fiscal Agent will be held liable for improper payments. Please explain if this requirement will pose a problem.			
1g. The Entity will have responsibility for local bank accounts dedicated to the Compact. Will this arrangement pose a problem for the Entity?			
2. Staffing – must be sufficient and dedicated to perform financial management tasks during the compact period.			
<p>2a. Provide an organigram showing the existing staff and the reporting relationships among the staff of the Entity as it is currently structured. Please provide details answers to the following:</p> <ul style="list-style-type: none"> • Is the accounting function adequately staffed for its current workload? • Are the accounting staff adequately qualified and experienced? • Do all staff have written position descriptions? • Is staff performance evaluated on a regular basis? • Does the Entity have a training policy for staff? 			
2b. Provide an organigram showing the proposed staff and the reporting relationships among the staff of the Entity as it would need to be structured to support the compact.			
2c. Describe any problems that might exist regarding the hiring of staff for limited term appointments, that is, only for the duration of the compact.			
2d. What will be the basis of compensation of newly hired employees? Are salaries commensurate with the private sector? Please provide an example.			
2e. Will current staff be dedicated to work on the compact? If so, please provide current CV's of any staff who will work on the compact			
2f. Describe any organic labor laws that might prevent the ability to remove or place sanctions against an employee.			
3. Budgeting – management of the MCC compact budget; integration of MCC funding into the National Budget			
3a. The budget developed by the MCA will be implemented by the fiscal agent. Please explain how the proposed system will ensure that no obligation will be incurred and no disbursements made unless provided for in the budget and unless uncommitted funds exist.			

Subject	Response	Overall Assessment	Remediations Needed
3b. MCC requires that the MCA, through its fiscal agent, provide an analysis of the funds it needs to commit and cash it needs to disbursement on a rolling quarterly basis for the upcoming four quarters and on an annual basis for the remaining years of the compact. Please explain how the proposed Entity will handle that requirement in the system.			
3c. Describe how the MCC funded will be reflected in the National Budget. What information will be reflected and how frequently will it be required?			
3d. Describe how the Entity will provide the information needed for inclusion in the National Budget.			
4. Automated accounting system – an accounting system that can maintain compact data in the MCC-required format for reporting			
4a. Does the Entity have an automated accounting system that can maintain compact financial information in the format required by MCC? If yes, see question 4b.			
<p>4b. Describe how the automated accounting system can handle the following requirements:</p> <ul style="list-style-type: none"> • Recording of a commitment at the time a contract or purchase order is executed. • Recording of an expenditure when a payment request is approved. • Accounting on a cash basis. • Maintaining information on foreign currency gains and losses. • Maintaining a chart of accounts to allow for reporting on assets, liabilities, income and expenses of compact activities. • Tracking at the project, activity, subactivity, task and object of expenditure. • Reporting on monthly, quarterly, semiannually and annually. 			
4c. How flexible is the accounting system in terms of implementing new requirements? Provide an example of a recent change to the accounting system's structure.			
4d. Please provide system documentation showing the current accounting string.			

Subject	Response	Overall Assessment	Remediations Needed
4e. The Entity's automated accounting system must be assessed by an outside consultant of MCC's choosing, who will perform a due diligence assessment of the system's functionality. Will this requirement pose a problem?			
4f. Describe the automated systems control over user access to the system. Is there an audit trail of all users involved in transactions? Explain if the system can designate/limit user access by function, role or other criteria.			
4g. Describe how the system data is protected unauthorized access.			
4h. Describe how the system is backed up. Discuss frequency, method, storage, etc.			
4i. Describe how the software is kept up to date, with system patches, upgrades, and the like. Describe the most recent upgrade process and how it was carried out.			
4j. Describe the number and experience of the personnel involved in maintaining the automated accounting system.			
4k. The automated system must have the ability to import and export information to other systems. Please explain in detail the system's capability to handle this requirement.			
5. Accounting policies and procedures			
Policies and internal controls			
5a. What accounting standards are currently followed? What is the basis of accounting? (Cash, accrual, etc.)?			
5b. Does the Entity have an up-to-date accounting procedures manual that provides guidance on both routine and infrequent accounting functions? If yes, please provide a copy. If no, please explain how guidance is provided to system users and managers.			
5b.1 What changes will be made to document the financial management requirements related to the compact?			
5c. Are there controls to ensure that all transactions are properly prepared, authorized and implemented? Describe the controls in place.			

Subject	Response	Overall Assessment	Remediations Needed
<p>5d. Describe how the Entity has separated the following functions with regards to ordering, receiving, accounting for, and paying for goods and services:</p> <p>i. authorization to create or execute a transaction; ii. recording the transaction; iii. custody of the assets/documentation involved in the transaction</p>			
<p>5d. Describe the process for reconciling bank accounts to the general ledger cash balances and to budget appropriations. Who performs them? Who reviews them? How are reconciling items handled? How often are reconciliations performed?</p>			
<p>5e. What policies and procedures are in place to ensure that employees are held accountable for their actions?</p>			
<p>5f. What steps are taken to protect the Entity from conflicts of interest (real and apparent) and undisclosed related party transactions?</p>			
<p>5g. Are employees encouraged to report accounting errors and irregularities to the proper management authorities? How are these employees protected from potential retribution?</p>			
<p>5h. What procedures are in place to review internal controls periodically to ensure they are working as intended? How are corrections made?</p>			
Physical protection of assets			
<p>5i. Describe how physical assets, including cash, computers and other IT equipment, and supplies are physically protected from theft or abuse.</p>			
<p>5j. What policies and procedures ensure that fixed assets are periodically inventoried and compared to control records?</p>			
<p>5k. What security measures are in place to ensure physical assets are protected during non-work hours and weekends?</p>			
<p>5l. What policies exist governing the use of Entity assets by employees for personal use?</p>			
<p>5m. Describe the types and coverage levels of insurance maintained by the Entity</p>			

Subject	Response	Overall Assessment	Remediations Needed
5n. Are key documents properly stored and protected?			
Payroll and personnel policies			
5o. Are all employees covered by an employee contract, position description or other document that clearly states the salary and benefits the employee is entitled to receive? If yes, please provide a sample contract, PD, etc.			
5p. What is the system for evaluating performance? Can employees be fired for poor performance?			
5q. How does the Entity ensure that <ul style="list-style-type: none"> • Only existing employees are paid • All employees are paid the correct amount • All required tax withholdings are paid to the appropriate authorities 			
5r. The Entity will be responsible for processing employee payments. Will that pose a problem?			
5s. What policies, laws, and/or codes of conduct are in place to assure the ethical behavior of employees?			
5t. What training in ethics is provided to employees and management?			
5u. What measures are in place to protect employees who report unethical behavior or corruption?			
6. Funds control and Funds Flow Processes			
Cash management			
6a. The MCC will use a Common Payment System through the US Treasury to make payments to most vendors. Funds will be transferred directly to vendor accounts. Will this payment system pose a problem for the Entity?			
6b. For local payments, a bank account, in the name of the MCA with the fiscal agent as the authorized signatory, will be established. Will the Entity have a problem with that arrangement?			

Subject	Response	Overall Assessment	Remediations Needed
6c. How will the Entity ensure that MCC's funds are segregated from other cash resources?			
6d. Will there be a problem in returning any interest earned in the local bank account to the MCC?			
Payments			
6e. Describe how the following invoicing and payment activities are carried out: <ul style="list-style-type: none"> • Obtaining purchase orders and receiving reports from the ordering Entity • Comparing invoice details to the PO and receiving report • Checking accuracy of invoices • Authorizing payment of invoices • Rejecting invoices that are improper • Ensuring that duplicate payments do not happen 			
6f. Describe how the Entity will comply with the MCC requirement to pay vendors within 30 days of receipt of a valid invoice.			
6g. Describe the handling and filing of all documents related to the payment process. Are documents readily available for audit purposes?			
6h. For payments made through local checking accounts, how are check-books, cancelled checks and voided checks protected?			
6i. Describe the controls in place to ensure that invoices are coded properly for entry into the accounting system.			
6j. What funding and banking systems are currently used to make payments?			
7. Financial Reporting			
7a. Will the proposed Entity be capable of preparing MCC required reports? Please review the attached report samples and provide an answer that references each required report.			

Subject	Response	Overall Assessment	Remediations Needed
7b. Does the system have the capability to prepare reports on a real-time basis? If not, on what basis are reports prepared?			
7c. MCC requires that financial reports be available within 14 days of the end of a month, quarter or year end. Please explain the system's ability to meet this requirement.			
7d. What is the system's ability to produce ad hoc reports?			
7e. How will the fiscal agent ensure that financial information related to the compact is available to the general public?			
8. Auditing			
8a. Is there an internal audit function in the proposed Entity? If so, how often are audits conducted? How and how timely are findings resolved?			
8b. How large is the audit function? To whom does it report?			
8c. The MCC requires an audit of the compact program every six months during the life of the compact. The audit firms are competitively procured from a list of firms approved by the Office of the Inspector General of the US Agency for International Development. The audits are paid for with compact funds. Please explain if this will be a problem.			
8d. Will the compact be subject to audits performed by a governmental agency, such as a supreme audit institution?			