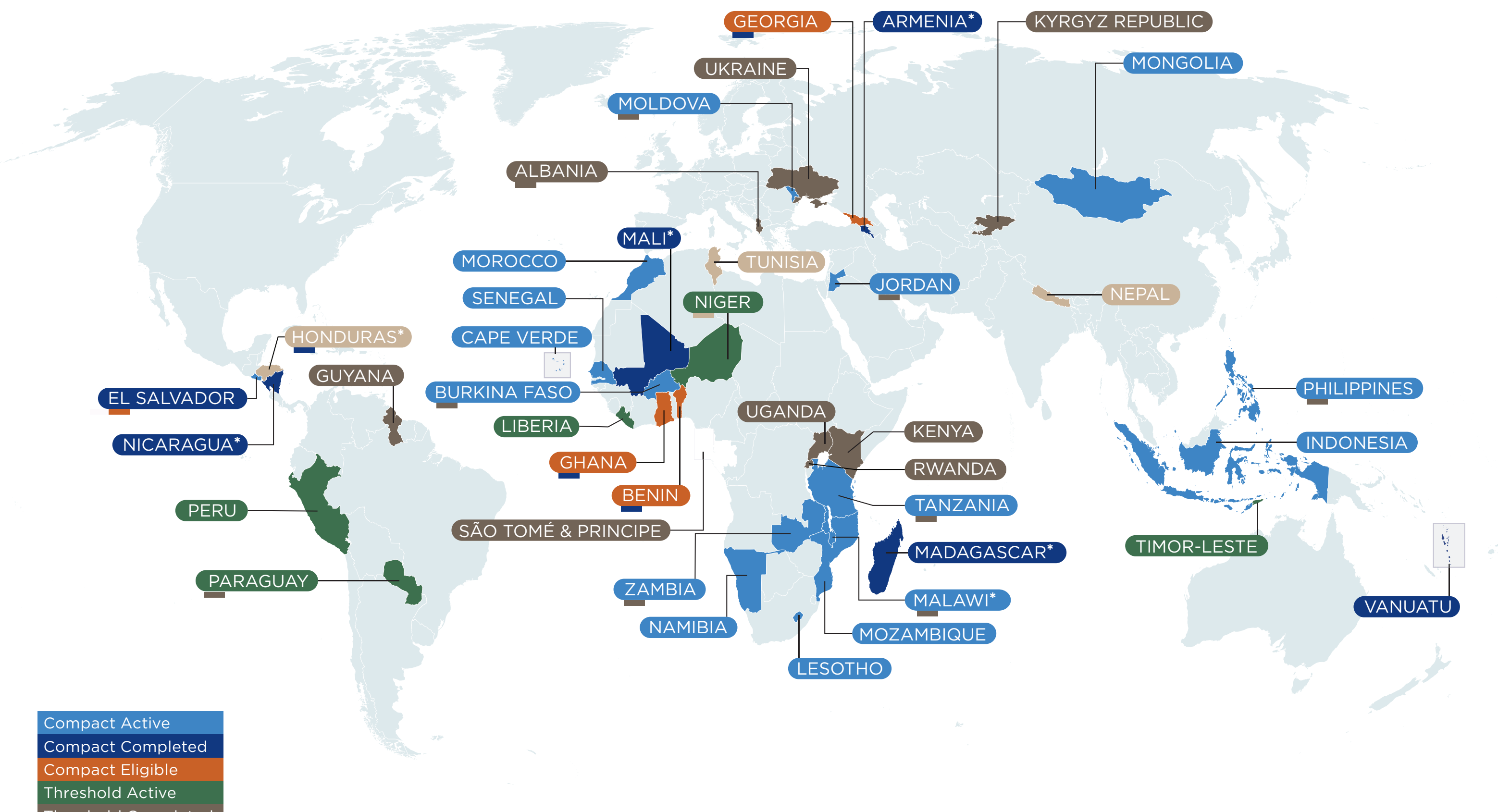
Agency Financial Report
Fiscal Year 2013

October 1, 2012–September 30, 2013

MILLENNIUM
CHALLENGE CORPORATION
UNITED STATES OF AMERICA



Country name badge and map color denote current status, rectangular badges denote previous or additional status.

*MCC's Board of Directors put on hold, suspended or terminated a portion of assistance due to events or government actions inconsistent with MCC's eligibility criteria.

MCC Partner Countries — Compacts and Threshold Programs

MCC has worked with partners in the countries shown on the map above to help reduce poverty through economic growth.

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Introduction

The Millennium Challenge Corporation's (MCC's) Agency Financial Report (AFR) for fiscal year (FY) 2013 provides fiscal and high-level performance results that enable the President, Congress and the American people to assess MCC's performance for the reporting period October 1, 2012, through September 30, 2013. It provides an overview of MCC's programs, accomplishments, challenges, and management's accountability for the resources entrusted to MCC. This report was prepared in accordance with the requirements of the Office of Management and Budget's (OMB's) Circular No. A-136, *Financial Reporting Requirements.*

MCC has chosen to produce an AFR and an Annual Performance Report (APR). MCC will include its FY 2013 APR in the Corporation's Congressional Budget Justification, which it will post on MCC's website on February 17, 2014. Together, the AFR and APR present the results of the annual assessment of MCC's program leadership and stewardship of the resources entrusted to it. They provide a comprehensive snapshot of the most important financial information related to MCC's programs. MCC also issues an Annual Report and other documents regarding its activities to its Board of Directors, to stakeholders, and to the public on its website.

Organization of This Report

This Agency Financial Report includes a message from the Chief Executive Officer (CEO), followed by three sections and appendices:

- **Management's Discussion and Analysis** describes MCC's mission and organizational structure; strategic goals and highlights of accomplishments; analysis of the financial statements and stewardship information; systems, controls and legal compliance; and other management information and initiatives.
- **Financial** contains a message from the Vice President, Department of Administration and Finance and Chief Financial Officer (CFO), the financial statements and notes, and the independent auditor's report.
- **Other Information** includes the Office of Inspector General's summary of top management challenges, MCC management's response to those challenges and MCC's Improper Payments Information Act (as amended by the Improper Payments Elimination and Recovery Act) Report.
- **Appendices** include a list of acronyms used in this report (Appendix A), a summary of MCC's compact and threshold programs (Appendix B), MCC's country selection process and criteria (Appendix C) and a list of useful websites for additional information about MCC (Appendix D). The website list includes the web addresses for all hyperlinked documents in the text of this report.

For more information about MCC, visit its website at: http://www.mcc.gov

MCC Welcomes Your Comments

MCC welcomes comments and suggestions regarding this report.
Please contact MCC at:

https://www.mcc.gov/pages/contact

or

875 Fifteenth Street, NW
Washington, DC 20005-2221
(202) 521-3600.

The Millennium Challenge Corporation is an innovative and independent U.S. foreign aid agency that is helping lead the fight against global poverty.

December 16, 2013

Message from the Millennium Challenge Corporation's Chief Executive Officer

I am pleased to present the Millennium Challenge Corporation's (MCC's) 2013 Agency Financial Report (AFR). MCC is an independent United States foreign assistance agency that is fighting global poverty through economic growth. MCC most effectively manages limited development resources by partnering only with countries committed to practicing sound democratic and economic governance, that then design and lead their own development projects. MCC requires that these projects spur economic growth and deliver tangible and sustainable results to raise incomes of the poor.

This commitment to evaluating what works and does not work in development defined MCC this past fiscal year with the October 2012 release of our first five independent impact evaluations. Focusing on farmer training activities in Armenia, El Salvador, Ghana, Honduras, and Nicaragua, these evaluations revealed critical lessons on how we can improve our operations, as well as independent evaluations moving forward. We are already using the evaluation results to redesign programs across other MCC compacts, illustrating our commitment to accountability, learning, transparency, and evidence-based decision-making.

In addition to releasing the findings of our first impact evaluations, five more compacts reached completion this past fiscal year in Lesotho, Mongolia, Morocco, Mozambique, and Tanzania; the latest compact with Georgia that focuses exclusively on education, was signed; our redesigned Threshold Program was launched with the signing of a Threshold Program Agreement with Honduras; and major achievements in data transparency with the unveiling of MCC's data and evaluation catalogs, resulting in MCC being ranked first among international donors by Publish What You Fund's Aid Transparency Index.

All these milestones—from closed compacts to independent evaluations—reflect MCC's commitment to delivering sustainable economic growth. The financial and performance information presented in this AFR helps to tell the story of MCC's impact on reducing global poverty, and is fundamentally complete and reliable.

I am proud to report that in fiscal year 2013, MCC received an unqualified or "clean" opinion on its financial statements for the third year in a row. The opinion rendered by MCC's auditors reaffirms our dedication to fulfilling our fiduciary responsibility to the American people in managing the resources entrusted to us in compliance with applicable laws and rigorous accounting standards.

We take seriously the independent auditor's identification of one modified repeat material weakness in internal controls over financial reporting; we will continue to take aggressive action to resolve this weakness. Please see my annual assurance statement, also included in this report, for more information regarding this weakness and MCC's compliance with appropriate financial laws and regulations.

I invite our key stakeholders to continue following MCC's work, sharing critical feedback, and holding us accountable to make progress in the fight against global poverty. This is how MCC will further contribute evidence-based learning to U.S. global development efforts and make a measurable and tangible difference in the lives of the world's poor.

/ s /

Daniel W. Yohannes
Chief Executive Officer

Management's Discussion and Analysis

Mission and Organizational Structure

Mission

The Millennium Challenge Act of 2003, contained in Title VI, Division D, of Public Law 108-199 (the Consolidated Appropriations Act, 2004), established MCC as a wholly-owned Government corporation as defined by the Government Corporation Control Act. MCC's mission is to reduce poverty by supporting sustainable economic growth in developing countries that create and maintain sound policy environments. MCC selects only those countries committed to strengthening good governance, encouraging economic freedom and promoting investments in people as demonstrated through independent assessments. Through the country-created Millennium Challenge Account (MCA), MCC provides assistance to stimulate economic growth and alleviate poverty. To ensure accountability, MCC rigorously plans, tracks and monitors results to determine the long-term effect of investments.

Individual countries develop assistance programs to build their own capacity for delivering solutions to their citizens. These programs have focused on policy, institutional and infrastructure improvements in such sectors as agriculture and irrigation; transportation (e.g., roads, bridges, ports); water supply and sanitation; access to health; finance and enterprise development; anticorruption initiatives; land rights and access; and access to education.

MCC's programs complement other U.S. and international development programs. MCC works closely with the Department of State and the United States Agency for International Development (USAID) to develop and implement its programs. Strengthening the next generation of emerging markets that will trade and do business with American companies can lead to job creation in the United States. As emerging economies prosper, they become more stable and secure, which promotes America's national security interests.

MCC provides assistance through two types of large-scale grants to eligible countries:

- A ***compact*** is a large, five-year grant to a country that meets MCC's eligibility criteria. It funds specific programs targeted at reducing poverty and stimulating economic growth. To obtain a compact, a country identifies its priorities and develops a proposal in broad consultation with civil society; MCC teams then work in close partnership to help the country refine a program. When MCC awards a compact, the country sets up a local accountable entity (MCA) to manage and oversee all aspects of implementation.
- A ***threshold program*** is a country-driven partnership that aims to assist a country to become eligible for an MCC compact by supporting policy and institutional reforms that target binding constraints to economic growth. MCC uses a rigorous, structured diagnostic process to develop threshold programs, followed by program design and implementation.

Appendix B provides a summary of MCC compact and threshold programs.

Values

MCC articulated a set of corporate values in FY 2013 to serve as the foundation of MCC's corporate culture and improve agency performance through enhanced staff engagement and team effectiveness. MCC's values define how individuals and the institution behave on a daily basis in pursuit of the mission. The values guide how MCC and MCC staff make decisions, set priorities, address challenges, manage tradeoffs, recruit and develop staff, and work together with country partners and stakeholders. Taken together, MCC's values are **CLEAR**:

Embrace **C**ollaboration

We work together toward clear, common goals with a spirit of creativity and teamwork. We believe that bringing different perspectives to the table leads to finding the best solutions.

Always **L**earn

We question assumptions and seek to understand what works, what doesn't and why. We recognize that failing to reach a goal can be an important source of learning, and we apply and share those lessons broadly.

Practice **E**xcellence

We envision MCC as a leader in global development, and we have high standards for ourselves, our partner countries, and the investments we make. We bring out the best in ourselves and in each other to advance the fight against global poverty.

Be **A**ccountable

We own our actions, are honest about our limits and missteps, and hold ourselves and each other responsible for good performance. We are transparent and explain our decisions.

Respect Individuals and Ideas

We are inclusive, act with humility and value diverse ideas. We listen to each other and foster strong working relationships with our colleagues at MCC, in our partner countries and in the development community.

Country Selection Process

The hallmark of MCC's country selection process is transparency. MCC uses a four-step process to select countries as eligible for assistance:

1. ***Identify Candidate Countries.*** MCC identifies candidate countries for the fiscal year based on per capita income and whether they are legally eligible to receive U.S. economic assistance.
2. ***Publish MCC's Selection Criteria and Methodology.*** MCC submits a report to Congress describing the criteria and the methodology and including the indicators that MCC's Board of Directors will use to select eligible countries.

3. ***Publish MCC Country Scorecards.*** Before the MCC Board meets to select compact-eligible countries, MCC publishes its country performance scorecards on its public website for all candidate countries and countries that would be candidates but for legal prohibitions.

4. ***Selection of Compact-Eligible and Threshold-Eligible Countries.*** From the pool of candidate countries, the MCC Board selects eligible countries according to the methodology described above and submits a report to Congress no later than five days after the determination. These countries are then eligible to begin developing compact proposals for MCC's consideration.

Appendix C describes the selection process and the criteria in detail. For FY 2013, MCC used 20 criteria, which fall under one of three categories: Ruling Justly, Investing In People, and Encouraging Economic Freedom. The table below summarizes MCC's selection criteria.

MCC Selection Criteria

Ruling Justly	Investing In People	Encouraging Economic Freedom
• Civil Liberties • Political Rights • Control of Corruption • Government Effectiveness • Rule of Law • Freedom of Information	• Immunization Rates • Public Expenditures on Health • Primary Education Expenditure • Girl's Education – Primary Education Completion (Lower Income Countries only) – Secondary Education Enrollment (Lower Middle Income Countries only) • Child Health • Public Expenditure on Primary Health – Child Health – Natural Resource Protection	• Business Start-up • Land Rights and Access • Trade Policy • Regulatory Quality • Inflation • Fiscal Policy • Access to Credit • Gender in the Economy

If you are reading a paper copy of this document, you will find the *Guide to the MCC Indicators and the Selection Process for Fiscal Year 2014,* at the following MCC website address: http://www.mcc.gov/documents/reports/reference-2013001142401-fy14-guide-to-the-indicators.pdf.

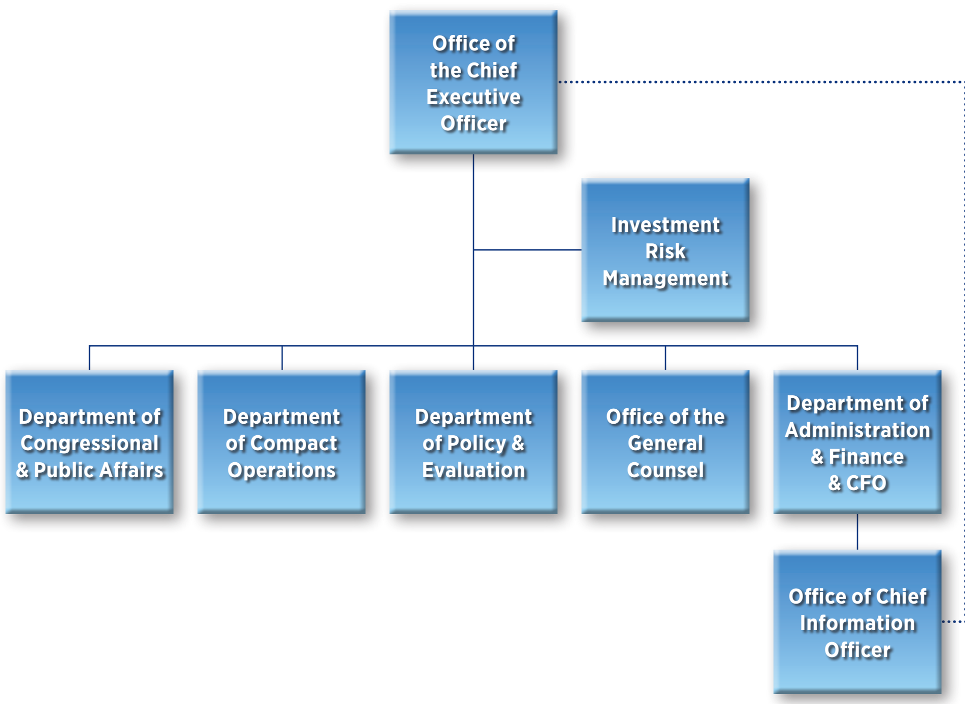
MCC's guiding principle is that aid is most effective when it reinforces good governance and investments in people that promote economic growth. In making its determinations, MCC's Board of Directors considers three factors: (1) policy performance as defined by policy indicators and supplemental information, (2) the opportunity to reduce poverty and generate economic growth in the country and (3) the funds available to MCC. MCC identifies countries eligible to receive MCC funds through a rigorous evaluation process prior to the MCC Board making its selections. This process uses indicators to assess countries' policy environments and determine in which countries MCC funding will be effective in reducing poverty and promoting economic growth.

The country selection process is continuous; MCC reviews all of its performance indicators annually to ensure it is using the best measures, making changes or refinements to identify better indicators or improved sources of data.

Further, MCC evaluates its partner countries' policy performance throughout implementation of the compact or threshold program in coordination with the Department of State, USAID and the U.S. embassies. MCC can warn a country, or suspend or terminate its eligibility, for a significant policy decline or policy reversal or a pattern of actions inconsistent with the eligibility criteria.

Organizational Structure

The CEO, part of the nine-member Board of Directors, manages MCC. The Secretary of State, the Secretary of the Treasury, the U.S. Trade Representative, and the USAID Administrator serve on the Board along with four private sector representatives appointed by the President of the United States with the advice and consent of the U.S. Senate. The Secretary of State is the Chair of the Board and the Secretary of the Treasury is the Vice Chair. MCC's organization chart is shown below.



MCC has six departments:

1. The **Office of the Chief Executive Officer** is responsible for the overall management of MCC. Principal officers include the CEO, the Chief of Staff, the Senior Advisor, the Deputy Chief of Staff, the Executive Secretary and the Senior Investment and Risk Officer.

The Office of the Chief Executive Officer provides executive leadership and strategic direction for the agency; coordinates activities and communications across departments; manages the agency's portfolio investment and risk assessment; manages the Investment Management Committee; and manages the official correspondence, scheduling and interagency information for the CEO.

2. The **Office of General Counsel** provides advice to MCC's Board of Directors and MCC staff on all legal issues affecting MCC, its programs, policies and procedures; advises the Department of Policy and Evaluation (DPE) on all aspects of country eligibility, the Threshold Program and other policy initiatives; provides legal advice to transaction teams developing compact programs; addresses and resolves legal issues associated with compact development; conducts and evaluates due diligence on country proposals; conducts compact negotiations and assists with legal aspects of compact implementation; provides advice to the Department of Administration and Finance and CFO on all issues affecting the internal operations of MCC, including personnel law, government contracts, fiscal law, information technology (IT), and corporate records management; advises the Department of Congressional and Public Affairs on matters of statutory interpretation, interagency agreements and communications, and other public initiatives; performs the function of Corporate Secretary to the MCC Board of Directors; and manages MCC's ethics program, providing related training and guidance to staff.

3. The **Department of Congressional and Public Affairs** manages MCC's relationship with the U.S. Congress, other U.S. Government agencies, the media, universities, non-governmental organizations, think tanks, the private sector, and other key groups interested in MCC's mission. This department handles all media inquiries and interview requests, manages the MCC speaker's bureau, coordinates all public events, serves as a liaison to the staff of MCC's Board of Directors, maintains MCC's public and internal websites and disseminates information to the public via statements, press releases and speeches.

4. The **Department of Administration and Finance and Chief Financial Officer** plans and directs all activities related to financial management and budgeting; manages MCC's human resources; oversees IT infrastructure and services; enters into and manages all MCC contracts, acquisitions and grants; preserves personnel and physical security; coordinates and manages MCC's facilities and provides administrative services; maintains official corporate records; coordinates audit interactions with the Inspector General and the Government Accountability Office; and coordinates and ensures timely and relevant reporting of performance data on compact programs. There is a "dotted" line relationship between the Chief Information Officer and the CEO.

5. The **Department of Compact Operations (DCO)** manages the day-to-day operational relationships with countries eligible to develop compacts and with countries that have signed compacts with MCC and are implementing or closing out compact programs; assists partner countries to develop, prioritize and appraise investments to address constraints to economic growth; identifies, in partnership with countries, potential areas for collaboration with other development agencies and the private sector; provides technical and regional expertise to ensure rigorous oversight of U.S. Government resources during compact implementation; and promotes MCC core standards of accountability by providing technical expertise in education, fiscal accountability, infrastructure, agriculture, land policy, procurement, environmental and social performance, gender integration, private sector engagement, and health.

   DCO divides the management of the MCC compact portfolio into two regional divisions ("Africa" and "Europe, Asia-Pacific and Latin America") and two technical divisions (Sector Operations and Infrastructure, Environment and Private Sector). DCO oversees the MCC staff residing in MCC missions in compact countries. Washington-based DCO specialists travel to compact countries to offer technical support.

6. The **Department of Policy and Evaluation** is responsible within MCC for the institutional oversight of policy and best practices related to country eligibility, policy improvement and reform, economic analysis, monitoring and evaluation, and learning from evidence. DPE manages MCC's country selection process, country monitoring, the Threshold Program and independent evaluation. It is co-responsible with the DCO for economic analysis and monitoring and evaluation of MCC compacts. DPE formulates strategies that leverage MCC impact with other U.S. Government agencies, the international development community and nongovernmental organizations.

MCC is a small government corporation with its headquarters in Washington, DC. The table below shows staffing levels since FY 2010.

MCC Staffing — Full Time Equivalent (FTE)*

	FY 2013	FY 2012	FY 2011	FY 2010
Headquarters	268	259	251	251
Overseas	25	30	31	33
Total Employees	**293**	**289**	**282**	**284**

**Staffing report based on Standard Form (SF)-113A and SF-113G reporting of FTE calculations based on quarter 4 of each fiscal year.*

Performance Goals, Objectives, and Results

MCC will provide an Annual Performance Report as part of its Congressional Budget Justification, which will be available February 17, 2014. A high-level summary of MCC's strategic direction and performance during FY 2013 follows.

Strategic Direction

MCC's mission is to reduce poverty by supporting sustainable economic growth in selected developing countries that demonstrate a commitment to sound policy in the areas of democratic governance, economic freedom and investment in people. This is a long-term mission, focused on addressing issues of persistent poverty and underdevelopment in lower and lower-middle income countries facing critical challenges of capacity, resources and institutional weakness. MCC seeks through its programs to demonstrate the effectiveness of linking foreign development assistance to demonstrable economic outcomes by concentrating on four key principles outlined in MCC's Strategic Plan 2011–2015:

1. **Results matter** — success is measured by results, not inputs.
2. **Policies matter** — good policies are critical to achieving sustainable economic growth.
3. **Country ownership matters** — country partner responsibility for results is essential for achieving sustainable development and reducing dependence on foreign assistance.
4. **Accountability matters** — without accountability there is no true responsibility and without transparency there is no accountability.

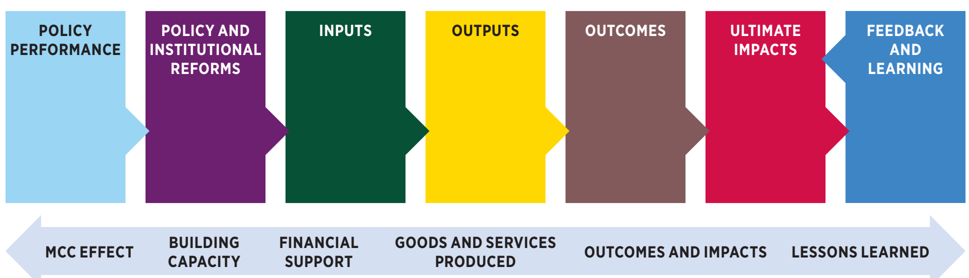
To implement these principles, MCC identified the following broad themes for the five-year period covered by its strategic plan:

1. Apply effective instruments for results tracking that will support transparent results' reporting.
2. Focus on policy reform as the best guarantor of sustainable development.
3. Leverage MCC's assets by working with partners to enhance the impact and reach of MCC programs, especially with the private sector.
4. Integrate gender and social assessment into all aspects of program design and implementation.
5. Ensure that MCC has the organizational capacity to respond effectively to evolving challenges.

Prior to the beginning of each fiscal year, MCC carries out an exercise focused on identifying priority areas of concentration for that fiscal year. These areas of concentration elaborate upon, but do not replace the overarching principles. The process for identifying them is both top-down and bottom-up. Informed by feedback from staff at all levels, the senior management team meets to discuss experiences over the past year in relation to the strategic plan and the previous year's goals and priorities. It determines what the specific areas of attention should be for the coming year. Each department carries out an intensive departmental planning exercise to clarify its detailed goals and objectives. Senior management reviews the plans to ensure that the corporate and departmental goals and priorities are clear and integrated effectively. These goals and priorities serve as the basis for individual performance planning as well as for management of the agency's business during the course of the year.

MCC's Approach to Performance Measurement

MCC is committed to delivering results throughout the entire lifecycle of its investments. From before investments begin to their completion and beyond, MCC's robust and comprehensive "Continuum of Results" framework seeks to measure, collect and report on policy reforms associated with MCC compact eligibility and program investments, inputs and outputs that indicate whether projects are on track, interim outcomes as programs reach completion, and impacts as measured through independent evaluations. The figure below shows the continuum framework; the table on the next page explains each step along the continuum.



MCC's Continuum of Results	
Step	**Description**
Policy Performance	The first result along the continuum is often the MCC Effect, when countries enact policy reforms to improve performance on MCC's indicators. Eligibility for an MCC compact is regarded as a seal of approval, signaling to private investors that the country is well governed and open for business. MCC has the option to suspend or terminate funding if a partner country's policy performance deteriorates significantly. This option to halt funding, which to date MCC has used in response to governance concerns, creates an incentive for ongoing policy and implementation performance that is key to delivering on the entire continuum of results.
Policy and Institutional Reforms	During compact development, MCC and partner countries look closely at the policy and institutional environment to assess areas that might limit investments' impact and sustainability and work with partner countries to plan appropriate policy and institutional reforms. These can be changes to national policies, laws, regulations, or even ways of doing business, and often focus on building capacity within existing national institutions.
Inputs	MCC's primary input is financial support for investments that promote poverty reduction and economic growth. MCC also contributes technical/professional support for oversight and policy dialogue. MCC and its partner countries use analyses of key constraints to growth, cost-benefits and beneficiaries to identify which investments have the biggest impact in terms of raising local incomes and generating long-term returns measured in economic benefits. To safeguard MCC investments, partner countries must adhere to international standards in financial management and procurement. Where necessary, they use external financial and procurement agents.
Outputs	Outputs measure the goods or services produced by a program such as kilometers of roads or irrigation canals built, farmers trained or land titles issued. MCC and its partner countries use monitoring and evaluation plans to establish targets and track progress on outputs. Transparent reporting on these outputs is key for accountability and for making mid-course corrections as needed.
Outcomes	Outcomes measure the medium-term effects of a program, such as increased traffic volume on improved roads, new business investments, increased production of high value crops, increased access to electricity or clean water, or increased school attendance. MCC and partner countries use monitoring and evaluation plans to track outcomes since they are the drivers of the increased income that MCC ultimately aims to achieve.
Ultimate Impacts	The ultimate result MCC is committed to producing—and being able to attribute to its investments—is increased incomes among poor people in developing countries. MCC wants to know if incomes went up because of an MCC investment, what worked best to increase incomes and if the increases were achieved in a cost-effective way. Where the potential to learn is greatest, MCC uses independent impact evaluations to answer these questions, often comparing results from the people who participated in MCC-funded programs to those who did not. This indicates whether gains were the direct result of MCC's investment. MCC also uses performance evaluations to answer qualitative questions, such as how is a project being implemented and whether expected results are occurring.
Feedback and Learning	MCC applies lessons learned to maximize development effectiveness. This involves working with partner countries to identify and address implementation challenges, keep current investments on track and inform the design and implementation of future investments. MCC is committed to transparently sharing the results of all evaluations, even when they reveal that MCC investments did not achieve planned targets. This is essential for both accountability and learning. MCC has opened its portfolio to scrutiny and is testing a variety of implementation and evaluation approaches. MCC's experience will foster learning internally, within the U.S. Government and globally both about what programs work best to increase incomes, and what evaluation approaches work best to measure impact.

Building on the foundation of strong monitoring systems and self-evaluations, MCC-financed independent evaluations are the most rigorous mechanism for fulfilling MCC's commitment to accountability and learning. It is common in the development community to focus on inputs (such as funds dedicated to farmer training) and outputs (such as the number of farmers trained), and increasingly on some intermediate outcomes (such as the rate that trained farmers apply the improved cultivation techniques). MCC frequently takes this focus another step further by using evaluation to determine if a link exists between these outcomes and the ultimate impact on household incomes. Independent evaluations test the assumptions underlying the program logic and are the primary mechanisms for measuring whether or not that link exists.

MCC invests in two different types of independent evaluations: impact and performance. Impact evaluations make it possible to know whether the MCC investment caused the observed impacts specifically or whether the impacts were the result of external factors that affected program participants and non-participants, such as increased market prices for agricultural goods, national policy changes or favorable weather conditions. Impact evaluations compare what happened with the MCC investment to what would have happened without it, through use of a counterfactual.

If you are reading a paper copy of this document, you will find MCC's complete monitoring and evaluation data by sector report at the following MCC website: http://www.mcc.gov/pages/results/m-and-e

Performance evaluations also are valuable tools for estimating the contribution of MCC investments to changes in trends for outcomes, including household income. Performance evaluations are useful for comparing changes in the situation before and after MCC's investment and provide details on how an investment might have contributed to changes in outcomes and, very importantly, why or why not.

In early FY 2013, MCC published the results of the first five impact evaluations, revealing critical learning on how MCC can improve operations and independent evaluations moving forward. As of the end of FY 2013, MCC is investing in more than 140 independent evaluations across all sectors, including impact and performance evaluations.

Compact Program Amounts and Results

Since MCC began operations, 25 countries have received funding through 27 compacts (Cape Verde and Georgia have signed two compacts each) and 22 countries have received funding through 24 threshold programs (Albania and Paraguay each signed two). Burkina Faso, Honduras, Indonesia, Jordan, Malawi, Moldova, Philippines, Tanzania, and Zambia have signed both compacts and threshold programs. MCC issues Quarterly Status Reports that provide a comprehensive qualitative and quantitative snapshot of each compact project, its commitments and expenditures, and its activities.

In FY 2013, MCC added a new compact with Georgia, and closed compacts in Lesotho, Mongolia, Mozambique, Morocco, and Tanzania. The table on the next page displays signed grant totals, net of deobligated amounts, for each country through September 30, 2013.

MCC Compact Grants at End of Fiscal Year 2013 (in thousands)	
Compact Country	**Grant Amount**
Armenia[1]	$ 176,550
Benin[1]	301,810
Burkina Faso	480,944
Cape Verde[1]	108,512
Cape Verde II	66,230
El Salvador[1]	449,567
Georgia[1]	387,179
Georgia II*	140,000
Ghana[1]	536,289
Honduras[1]	204,015
Indonesia	600,000
Jordan	275,100
Lesotho[1]	362,551
Madagascar[1]	85,895
Malawi*	350,700
Mali[1]	435,628
Moldova	262,000
Mongolia[1]	284,911
Morocco[1]	697,500
Mozambique[1]	506,924
Namibia	304,478
Nicaragua[1]	112,703
Philippines	433,910
Senegal	540,000
Tanzania[1]	698,136
Vanuatu[1]	65,404
Zambia*	354,758
TOTAL	**$ 9,221,694**

**These compacts have not entered into force.*
[1]These compacts have been completed.

MCC aggregates results in key sectors to measure progress in those areas across compacts. Currently, MCC calculates aggregate results on a quarterly basis in five categories: roads, agriculture and irrigation, water and sanitation, education, and property rights and land policy (land).

Each category contains several measures or common indicators. In June 2013, MCC revised its measures for two sectors. For agriculture and irrigation, MCC added an indicator for enterprises assisted. MCC defines enterprises as producer, processing and marketing organizations; water users associations; trade and business associations; and community-based organizations receiving assistance. An enterprise may be a single individual. MCC deleted hectares under production as an agriculture and irrigation indicator.

For land, MCC added an indicator for land administration offices established and deleted urban parcels mapped and rural hectares formalized. MCC works with the development community to re-assess its indicators. MCC may complete early process-level indicators, such as contract dollars disbursed, more quickly than other indicators. The actual construction of the road, for example, will take more time and will be a more relevant indicator as time passes.

The table on the next page presents MCC's program results by sector on select indicators as of June 30 of 2013, 2012 and 2011. Previous data for discontinued indicators are included as reference. The table aggregates country-specific targets and performance data by sector. It represents only a fraction of the performance data that MCC collects and assesses on a quarterly basis. MCC and MCC's partner MCAs collaborate to establish these targets. MCC assesses performance data across all compact programs on a quarterly basis and, where necessary, takes action to address deficiencies, mitigate risks and ensure that the compacts use U.S. taxpayer funding effectively and responsibly.

Beginning in FY 2014, future MCC Agency Financial Reports will present performance data on a fiscal year basis. The MCC website posts additional data on these five categories in the results pages on its website at the address shown in Appendix D, Useful Websites.

Program Results by Sector on Select Indicators for FYs 2013, 2012, and 2011

			Actual			Performance on Targets (Based on Cumulative Target for That Year)			
Sector	Indicator	Cumulative Target Through FY 2013	June 30, 2013	June 30, 2012	June 30, 2011	June 30, 2013	June 30, 2012	June 30, 2011	Countries Tracked
Roads	Value of signed contracts for road works (dollars in millions)	$2,126	$2,329	$1,794	$1,361	110%	117%	87%	Armenia Burkina Faso Cape Verde El Salvador Georgia Ghana Honduras Mali Moldova Mongolia Mozambique Nicaragua Philippines Senegal Tanzania Vanuatu
	Kilometers of roads under works contracts	3,610	3,719	3,168	2,802	103%	90%	88%	
	Kilometers of roads completed	3,003	1,929	1,595	1,247	64%	96%	117%	
Agriculture and Irrigation	Hectares under new or improved irrigation	254,714	138,753	116,460	8,257	54%	97%	10%	Armenia Burkina Faso Cape Verde El Salvador Georgia Ghana Honduras Madagascar Mali Moldova Morocco Mozambique Namibia Nicaragua Senegal
	Value of agricultural and rural loans (dollars in millions)	$84	$85	$83	$73	102%	134%	145%	
	Number of farmers trained	233,861	244,481	202,351	186,395	105%	96%	95%	
	Hectares under production	NA	NA	3,677	132,894	NA	127%	101%	
	Enterprises assisted	3,288	3,733	NA	NA	114%	NA	NA	
Water and Sanitation	Value of signed contracts for water and sanitation works (dollars in millions)	$400	$447	$285	$142	112%	110%	61%	El Salvador Georgia Ghana Jordan Lesotho Mozambique Tanzania
Education	Number of students participating	201,525	200,380	244,762	145,016	99%	91%	75%	Burkina Faso El Salvador Ghana Mongolia Morocco Namibia
	Facilities completed	844	839	805	406	99%	95%	57%	
	Value of signed contracts for construction and/or equipping of educational facilities (dollars in millions)	$164	$166	$115	$75	101%	93%	92%	

Program Results by Sector on Select Indicators for FYs 2013, 2012, and 2011

Sector	Indicator	Cumulative Target Through FY 2013	Actual			Performance on Targets (Based on Cumulative Target for That Year)			Countries Tracked
			June 30, 2013	June 30, 2012	June 30, 2011	June 30, 2013	June 30, 2012	June 30, 2011	
Land	Number of stakeholders trained	25,562	26,867	19,301	18,001	105%	74%	72%	Benin Burkina Faso Ghana Lesotho Madagascar Mali Mongolia Mozambique Namibia Nicaragua Senegal
	Urban parcels mapped	NA	NA	169,524	62,273	NA	60%	58%	
	Rural hectares formalized	NA	NA	1,514,818	353,246	NA	63%	84%	
	Land administration offices established	200	168	NA	NA	84%	NA	NA	

Analysis of MCC's Financial Statements

At the end of the fiscal year, MCC prepared four basic financial statements with notes to the financial statements and presented them to the USAID Office of Inspector General (OIG) for audit by an independent accounting firm. The Financial Section of this report contains the financial statements and notes, and the auditor's report. The following analysis provides a high-level summary of MCC's Balance Sheet, Statement of Net Cost, Statement of Changes in Net Position, and Statement of Budgetary Resources.

Balance Sheet

Assets

As of September 30, 2013, MCC reported total assets of $4.8 billion, a decrease of approximately 13 percent from FY 2012's total assets of $5.5 billion. MCC's Fund Balance with Treasury (FBWT) constitutes the vast majority (97 percent) of total assets. FBWT decreased $710 million due to differences in Appropriations Received and Gross Outlays. Appropriations Received decreased due to the FY 2013 sequester and across-the-board rescission. Gross Outlays increased primarily due to increased outlays associated with five countries whose compacts closed in FY 2013.

Other assets include Advances, Property, Plant and Equipment (PP&E), and Accounts Receivable. Intragovernmental Advances decreased substantially because Saõ Tomé and Principe completed its threshold program in FY 2013. Nongovernmental advances decreased slightly from FY 2012 due to net decreases in MCA-issued advances for compacts.

MCC has very few capital assets in relation to total assets because it does not own its facilities or other real property and does not have capital leases. MCC established its capitalization thresholds at $200,000 for IT equipment and $50,000 for other fixed assets. As of September 30, 2013, MCC reported fixed assets of approximately $2.1 million, which were mainly leasehold improvements for enhancements made to leased office space at MCC headquarters in Washington, DC. This amount decreased $1.2 million from FY 2012 due to amortization of leasehold improvements. Accounts receivable decreased by $6.7 million primarily because MCC recaptured cost payments made as part of Ghana's Agriculture Credit Program.

Liabilities

As of September 30, 2013, MCC had $223 million in liabilities, which represented amounts owed to its grantees, vendors, contractors, trading partners, and employees. Total liabilities increased by approximately 71 percent from FY 2012's total liabilities of $130 million. Grant liabilities comprise more than $209 million, or nearly 94 percent, of MCC's total liabilities. Grant liabilities nearly doubled from FY 2012, due primarily to net increases related to four compacts. MCC closed three of those compacts in September 2013 and increased the spending authority for the fourth compact.

Net Position

MCC's overall net position as of September 30, 2013, was $4.5 billion, a decrease of $828 million or nearly 16 percent from FY 2012. The available appropriations reported in MCC's positive net position represent the resources necessary to fund future compacts and demonstrate the lag between appropriation, commitment, and expenditure of compact funds.

Statement of Net Cost

This statement shows MCC's net cost of operations, as a whole, by the major programs or appropriation fund categories. The table below describes each program.

MCC Appropriation Fund Categories

Category	Source/Purpose
Compact	Funds approved by Congress, apportioned by OMB, and obligated by MCC to cover compacts between MCC and partner countries. Note: Under authority contained in section 609(g) of the MCC Act, MCC provides Compact Implementation Funds when it signs a compact to speed compact implementation by the partner country. OMB apportions grant funds for grants and cooperative agreements.
609(g) *(refers to section of MCC Act)*	Funds approved by Congress and apportioned by OMB to fund contracts or grants for facilitating the development and/or implementation of a compact between MCC and a partner country.
614(g) *(refers to section of MCC Act)*	Funds approved by Congress that the CEO may use to contract with any nongovernmental organization (including a university, independent foundation or other organization) in the United States or in a candidate country and, where appropriate, directly with a governmental agency of any such country that is undertaking research aimed at improving data related to eligibility criteria under this title with respect to the country.
Threshold	Funds appropriated by Congress, apportioned by OMB, and used by MCC to help countries to become eligible for MCC compact assistance.
Due Diligence	Funds apportioned by OMB and used by MCC to cover costs associated with assessing compact proposals developed by eligible countries and providing compact implementation oversight.
Audit	Funds appropriated by Congress and apportioned by OMB for audits of MCC operations and programs. The USAID OIG is responsible for conducting MCC audits.
Administrative	Funds appropriated by Congress and apportioned by OMB for operating expenses.

During FY 2013, MCC incurred $1.7 billion in net program costs, divided among the seven programs as shown in the table below and the chart to the right. Net program costs increased by $372 million, or 28 percent, from FY 2012. The primary reason for the increase was a net increase of Compact Program costs of $391 million. With the exception of Administrative Costs, which increased slightly in FY 2013, costs for the other funds decreased.

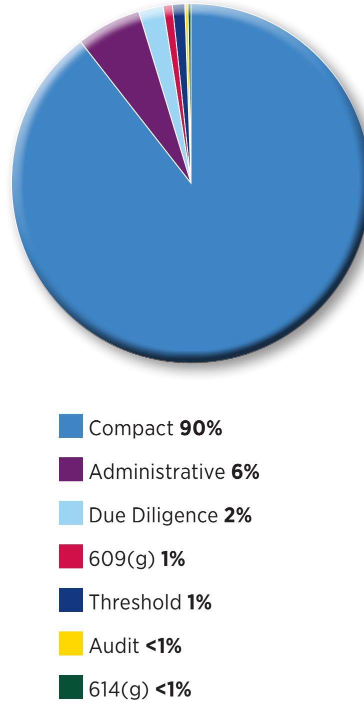
MCC Net Program Costs (Dollars in Thousands)

Program	FY 2013	FY 2012	% Change	Explanation for Change
Compact	$ 1,521,124	$ 1,129,720	35%	Increase in compact net costs
609(g)	16,633	21,734	–23%	Changes in contract and grants for facilitating development and/or implementation of compacts
614(g)	1	220	–99%	Research in contract eligibility not required in FY 2013
Threshold	9,677	16,371	–41%	Decrease in USAID activity (phasing out its Threshold program)
Due Diligence	35,525	41,478	–14%	Less cost than anticipated
Audit	3,730	5,165	–28%	Less cost than anticipated
Administrative	96,561	96,306	1%	
TOTAL	**$ 1,683,251**	**$ 1,310,994**	**28%**	

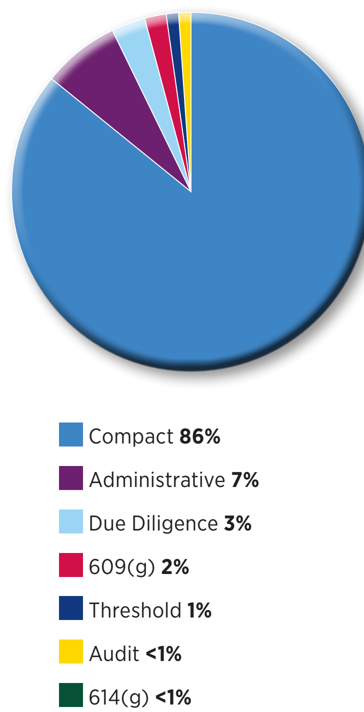
As the chart in the top right shows, 90 percent of MCC's expenditures were for compact activities. Administrative and audit program costs were approximately six percent of MCC's costs, while due diligence costs were only two percent. The remaining categories combined were approximately two percent.

As the chart in the bottom right shows, compact activities accounted for most of MCC's net program costs for FY 2012, with approximately 86 percent of the costs dedicated to compact activities. Administrative costs were the next largest expenditure.

FY 2013 Net Program Costs



FY 2012 Net Program Costs



Statement of Changes in Net Position

This statement shows the change in net position during the reporting period. MCC's net position at September 30, 2013, was $4.5 billion, a decrease of $828 million from September 30, 2012. Net position is affected by changes to its two components: Cumulative Results of Operations and Unexpended Appropriations. As of September 30, 2013, Cumulative Results of Operations amounted to $3 million, a decrease of nearly $8 million, or 72 percent, from September 30, 2012. This balance is the cumulative difference, for all previous fiscal years, between funds available to MCC from all financing sources and the net costs of MCC. The second component of net position, Total Unexpended Appropriations, amounted to $4.5 billion, a decrease of $820 million, or 15 percent, from FY 2012. This net decrease was the result of a decrease in Appropriations Used in FY 2013 of $1.7 billion, which was driven primarily by compact activity.

Statement of Budgetary Resources

This statement and related disclosures provide information about how budgetary resources were made available as well as their status at the end of the period. It is the only financial statement derived predominantly from an entity's budgetary general ledger in accordance with budgetary accounting rules. The Statement of Budgetary Resources reflects the format prescribed by OMB Circular No. A-136, *Financial Reporting Requirements.* The total amount displayed for the status of budgetary resources equals the total budgetary resources available to MCC as of September 30, 2013.

For 2013, MCC had total budgetary resources of $2.7 billion, an increase of $497 million, or 23 percent, from FY 2012. A total of $853 million of budgetary resources were provided through FY 2013 Congressional appropriation and $1.8 billion were carried forward from appropriations in prior years.

Analysis of MCC's Systems, Controls and Legal Compliance

Systems

MCC has no plans to operate its own financial systems and plans to further utilize service providers. Currently, the Department of the Interior's Interior Business Center (IBC) is MCC's financial management shared services provider for financial and payroll systems. MCC is responsible for overseeing IBC and ensuring that financial systems and internal controls are in place to fulfill legislated and regulatory financial management requirements.

Controls

The MCC CEO's annual Assurance Statement and the annual Assurance Statement of Management Controls over Financial Reporting submitted by MCC's service provider follow this section.

Internally, at least annually, MCC assesses the vulnerability of its programs and systems in alignment with the Federal Managers' Financial Integrity Act (FMFIA) and its implementing guidance, OMB Circular No. A-123, *Management's Responsibility for Internal Control,* as well as the associated guidelines issued by the Chief Financial Officers Council. OMB Circular No. A-123, Appendix A, "Internal Control over Financial Reporting," provides guidance to Federal managers on improving the accountability and effectiveness of Federal programs and operations by establishing, assessing, correcting and reporting on internal control over financial reporting. Appendix A allows for modified implementation to fit the circumstances, conditions and structure of each entity. As such, through MCC's commitment to prudent financial management and internal controls, during FY 2013, the second year of its three-year phased-in improvement plan, MCC continued its efforts to reassess, improve and enhance its financial, systems, program and performance information.

The information presented in this report meets the Circular's and Appendix A objectives, and is fundamentally complete and reliable as required by OMB. The annual assurance statement required by FMFIA concludes that MCC can provide unqualified assurance that its overall internal control over the effectiveness and efficiency of operations and compliance with applicable laws and regulations was operating effectively and can provide qualified assurance that its internal control over financial reporting was operating effectively.

December 11, 2013

FY 2013 Assurance Statement from CEO

The Millennium Challenge Corporation's (MCC's) management is responsible for establishing and maintaining effective internal control and financial management systems that meet the objectives of the Federal Managers' Financial Integrity Act of 1982 (FMFIA). MCC conducted an assessment of the effectiveness of internal control in achieving effective and efficient operations and compliance with applicable laws and regulations in accordance with Office of Management and Budget (OMB) Circular No. A-123, *Management's Responsibility for Internal Control.*

FMFIA Sections 2 and 4

The vulnerability of MCC programs and systems was assessed in accordance with FMFIA and OMB guidance. Based on the annual assessment, MCC can provide qualified assurance that MCC's accounting systems and internal controls comply with provisions of OMB Circular No. A-123, *Management's Responsibility for Internal Control,* and for section 2 (Internal Accounting and Administrative Controls) of FMFIA. MCC can also provide reasonable assurance that it is fully compliant with section 4 (Financial Systems) of FMFIA. Taken as a whole, MCC can provide reasonable assurance that its overall internal control over the effectiveness and efficiency of operations and compliance with applicable laws and regulations as of June 30, 2013, was operating effectively.

Internal Control over Financial Reporting

The effectiveness of internal control over financial reporting was assessed, which includes safeguarding assets and compliance with applicable laws and regulations in accordance with the requirements of Appendix A of OMB Circular No. A-123. Based on the results of this assessment and the independent auditor's report, MCC can provide qualified assurance that its internal control over financial reporting as of June 30, 2013, was operating effectively.

MCC recognizes the one material weakness identified in the auditor's report related to Inefficient and Ineffective Integration of Data, Processes and Controls within the Financial Management Systems. The report also identified three significant deficiencies: (i) Validation Control over Grant Accrual Estimates Needs to be Strengthened; (ii) Monitoring of Millennium Challenge Account Audits Needs to be Strengthened; and (iii) Information Systems Controls Need Improvement. MCC will continue to enhance its internal controls to address the noted deficiencies. Specific enhancements in fiscal year 2014 will include:

- Commencing a business process to reengineer efforts geared toward enhancing MCC financial reporting and program management information needs;
- Correcting underlying causes for financial management system errors and limitations;
- Developing improved methods for posting accounting transactions, i.e., grant accruals;
- Strengthening the relationship with our shared services provider, the Interior Business Center;
- Continuing to improve financial reporting and management review processes;
- Continuing to improve upon our grant accrual and validation procedures;
- Continuing to work with the USAID Office of the Inspector General to improve our MCA audit programs; and
- Lastly work to improve Information Systems Controls.

/ s /

Daniel W. Yohannes
Chief Executive Officer

FY 2013 Assurance Statement from Service Provider

MCC's service provider issued the following Statement of Assurance.

United States Department of the Interior
Office of the Secretary

Interior Business Center

October 18, 2013

Ms. Chantale Y. Wong
Millennium Challenge Corporation
875 Fifteenth Street NW
Washington, DC 20005

Ms. Wong:

The purpose of this letter is to provide assurance that the Oracle Federal financial application controls remained unchanged for the period July 1, 2013, through September 30, 2013.

You were previously notified that KPMG LLP examined the description of the Oracle financial application controls at the Department of the Interior (Department), National Business Center (IBC). The results of their review and analysis were provided in a Service Organization Control Report (SSAE16) covering the period July 1, 2012, through June 30, 2013. A copy of the report was provided to you under separate cover.

The SSAE 16 review was conducted for the purpose of expressing an opinion as to whether (1) IBC's description of the Oracle application controls presents fairly in all material respects the aspects of the IBC controls that may be relevant to a user organization's internal control; (2) the controls included in the description were suitably designed to achieve the control objectives specified in the description if those controls were complied with satisfactorily; and (3) such controls had been placed in operation as of June 30, 2013. KPMG also performed testing procedures designed to determine the effectiveness of the specified controls in meeting control objectives specified by the IBC.

This letter provides representations and assurances related to Oracle financial application controls at the IBC for the period July 1, 2013, through September 30, 2013. This time period was not covered by the SSAE 16 examination report previously provided. To the best of our knowledge and belief, there have been no subsequent events that would have a significant effect on user organizations that have not been disclosed to you. The controls that have been placed in operation as of June 30, 2013, did not change for the period of July 1, 2013, through September 30, 2013. The description of controls in the FY 2013 SSAE 16 examination report presents fairly the aspects of IBC controls that were in place as of September 30, 2013.

Ms. Chantale Y. Wong
October 18, 2013
Page 2 of 2

The IBC also conducted an assessment of the effectiveness of internal control over financial reporting for customers where the IBC processes your financial transactions, which includes safeguarding of assets and compliance with applicable laws and regulations in accordance with the requirements of Appendix A of OMB Circular A-123 and the CFO Council's Implementation Guide dated July 31, 2005, as implemented by the Department. The assessment focused on the specific IBC financial business processes such as financial reporting, revenue management, funds management, and procurement in place as of June 30, 2013. As of that date, the IBC noted no material or significant deficiencies verified through A-123 Appendix A financial transaction testing. Thus, the IBC asserted internal controls over financial reporting were suitably designed and operating effectively. The procedures and management controls for processing financial transactions have not changed since June 30, 2013. As a result, the IBC continues to assert substantial compliance with financial accounting and reporting controls in place from July 1, 2013, through September 30, 2013.

If you have any questions on this assurance statement, please contact Dean N. Martin, Interior Business Center Audit Liaison, on 303-969-5195.

Sincerely,

James W. Beall, CPA
Chief Financial Officer, Interior Business Center

If you are reading a paper copy of this report, the full text of the Interior Business Center Annual Assurance Statement of Internal Controls is available at: http://www.mcc.gov

Summary of Material Weaknesses, Non-Compliance and Corrective Actions

The Independent Auditor's Report identified one material weakness in internal control related to Ineffective and Inefficient Interrelationship Among Software, Personnel, Procedures, Controls and Data within MCC's Financial Management Systems. The report also identified three significant internal control deficiencies. These deficiencies are:

(1) Validation Control over Grant Accrual Estimates Needs to be Strengthened,

(2) Monitoring Control over Funds Provided to Millennium Challenge Accounts (MCAs) Needs Improvement and

(3) Information Systems Controls Need Improvement.

MCC will continue to enhance its internal controls to address the noted deficiencies. Specific enhancements in fiscal year 2014 will include:

- Commencing a business process to reengineer efforts geared toward enhancing MCC financial reporting and program management information needs;
- Correcting underlying causes for financial management system errors and limitations;
- Developing improved methods for posting accounting transactions, i.e., grant accruals;
- Strengthening the relationship with our shared services provider, the Interior Business Center;
- Continuing to improve financial reporting and management review processes;
- Continuing to improve upon our grant accrual and validation procedures;
- Continuing to work with the USAID Office of the Inspector General to improve our MCA audit programs; and
- Working to improve Information Systems Controls.

Legal Compliance

MCC complies with all applicable Federal statutes and regulations. Key legal requirements include:

Prompt Payment Final Rule

The Prompt Payment Final Rule (*Code of Federal Regulations,* Title 5, Part 1315) requires Federal agencies to pay commercial obligations within certain periods and to pay interest penalties when payments are late. With certain exceptions, payments to vendors are due within 30 days of the later of (1) receipt of properly prepared invoices or (2) the receipt of goods or services. For amounts owed and not paid within the specified payment period, agencies are required to pay interest on the amount owed at a rate established by the Department of the Treasury. MCC measures the percentage of all payments made within the specified timeframes out of all payments subject to the Prompt Payment Final Rule. In FY 2013, MCC's prompt payment performance exceeded 99 percent. MCC is taking steps to reduce the likelihood of future unnecessary interest payments.

Debt Collection Improvement Act of 1996

The Debt Collection Improvement Act requires all Federal agencies to refer for collection to the Department of the Treasury's Financial Management Service past due, legally enforceable, non-tax debts that are more than 180 days delinquent. During FY 2013, MCC had no debt to refer to the Department of the Treasury.

Improper Payments Information Act (as amended by Improper Payments Elimination and Recovery Act of 2010)

The Other Information section of this report contains MCC's Improper Payments Information Act report. MCC's risk assessment did not identify any funds that met the OMB threshold of significant erroneous payments, but MCC tested four of its funds to determine if it could identify any significant improper payments. MCC did not identify any improper payments from the sample of disbursements tested. However, MCC self-identified and reported two improper payments totaling nearly $5.3 million due to data entry errors; the errors were corrected and the funds were subsequently collected. MCC considered the errors an isolated incident and implemented corrective actions to prevent future occurrences.

Federal Information Security Management Act (FISMA) of 2002

In FY 2013, MCC continued to improve and enhance implemented security controls in compliance with FISMA and to increase the protection of agency systems and information. MCC revamped the security authorization process by publishing and implementing a comprehensive risk monitoring process that meets FISMA compliance requirements. MCC will fully implement its FISMA program in 2014. In addition, MCC worked with the Department of Homeland Security (DHS) to implement the DHS Continuous Diagnostic Monitoring program. Lastly, MCC is in the process of outlining a comprehensive corrective action plan for the audit findings.

Privacy Act of 1974

In 2013, MCC published and implemented an update to the Privacy Policy that outlines a comprehensive incident response plan. In addition, the agency conducted a thorough review of the logical information technology storage infrastructure to ensure compliance with the policy. MCC also implemented compliance monitoring services for its cloud storage solutions. In 2014, MCC will improve on privacy training and institute metrics to monitor results of the training program.

Other Management Information, Initiatives and Issues

MCC has identified seven areas that merit special attention as part of its commitment to achieving its five-year goals. Each department considers these areas when identifying specific goals, targets and measures of success in support of MCC's commitment to achieving its strategic objectives. The seven areas are:

1. **Differentiating the MCC model** — focusing on those elements of the MCC business model that offer the opportunity to significantly improve the way in which foreign development assistance is delivered.

2. **Communicating information and results** — reinforcing MCC's commitment not only to produce results but also to ensure that MCC is holding itself accountable for results and that its results are widely available to anyone interested in development assistance.

3. **Managing, sharing and applying knowledge** — ensuring that MCC is able to learn from its own experience and that of other actors in the global development community, adapt business practices based on lessons learned and remain at the cutting edge of applying best practices.

4. **Promoting transparency of information** — committing MCC to disseminating information about its business practices, investment decisions, implementation progress, and to learning about what works and what does not work in broad and readily accessible venues and formats.

5. **Implementing strategic staffing** — enabling MCC to optimize its limited staff resources and to respond flexibly and effectively to changing portfolios and technical/sector demands.

6. **Ensuring project sustainability** — maximizing value for money from MCC funding by focusing on enhancing the long-term viability of projects, processes and institutions promoted in MCC compacts, including through strategic partnerships.

7. **Addressing organizational challenges** — creating flexible and efficient administrative processes to support a highly motivated, creatively incentivized, and institutionally supported agency in a constrained budget environment.

Limitations of the Financial Statements

The principal financial statements have been prepared to report the financial position and results of operations of the entity, pursuant to the requirements of 31 U.S.C. 3515 (b). While the statements have been prepared from the books and records of the entity in accordance with generally accepted accounting principles (GAAP) for Federal entities and the formats prescribed by OMB, the statements are in addition to the financial reports used to monitor and control budgetary resources, which are prepared from the same books and records. The statements should be read with the realization that they are for a component of the U.S. Government, a sovereign entity.

Financial Section

Message from the Vice President, Department of Administration and Finance and Chief Financial Officer

December 16, 2013

The Millennium Challenge Corporation (MCC) remains firmly committed to delivering the highest standards of financial accountability, transparency and reporting in support of the Corporation's focused mandate to reduce poverty through economic growth. Our Agency Financial Report (AFR), a key component in delivering on our commitment, discloses and reports on our key performance and financial outcomes for the fiscal year. The report is the result of a rigorous year-round process of evaluation and improvement supported by MCC and compact personnel in countries around the world.

Accountability and transparency are at the very core of MCC—they are the same attributes we ask of our country partners. Their achievement requires continuous, ongoing effort. During 2013, MCC made great strides toward improved accountability by addressing systems and internal control weaknesses identified through previous audits. In particular, MCC confirmed that its financial system complies with Federal financial management system requirements. We improved our validation and reconciliation of financial transactions. We have strengthened our regular reviews of key financial reports, improved our transaction processing and established a team to review financial policies and procedures to ensure that they reflect current procedures which achieve MCC's financial objectives.

Transparency has been an important focus for the Corporation and today MCC is at the forefront of transparency in delivering aid. We launched data.mcc.gov where the public can access data in machine readable format that shows financial performance, country selection, and country household survey impact evaluation information. Due to our efforts, MCC is ranked #1 among 67 international donors according to the Publish What You Fund's Aid Transparency Index.

I am extremely proud of the improvements and enhancements we have made as we continue to ensure accountability and transparency in the Corporation's performance and financial reporting. As a continuing result of our focus and efforts, I am pleased to report that, for the third consecutive year, the Millennium Challenge Corporation has received an unmodified "clean" audit opinion on its financial statements. I am also pleased to report that MCC continues to maintain a robust system of controls.

While we have accomplished much, MCC's financial processes and practices still have room for improvement. Our independent auditors identified one material weakness and three significant deficiencies. The details of which are contained in this report. I have reviewed and concurred with each of the auditor's findings. In addition, I appreciate their recommendations, and will continue to use them as basis for action as we extend our efforts to address the underlying causes to eliminate them.

I appreciate the continued support of the entire Corporation, with special thanks to the Office of Inspector General and the independent auditor, as we continue to work together in our quest for excellence in financial management.

/ s /

Chantale Yokmin Wong
Vice President, Department of Administration and Finance
and Chief Financial Officer

Financial Statements

The principal financial statements have been prepared to report the financial position and the results of operations of the Millennium Challenge Corporation (MCC). The financial statements have been prepared from MCC's books and records in accordance with formats prescribed by the Office of Management and Budget (OMB) in OMB Circular No. A-136, *Financial Reporting Requirements* (revised on October 21, 2013). The financial statements should be read with the understanding that they are for a component of the U.S. Government, a sovereign entity. The Agency has no authority to pay liabilities not covered by budgetary resources. Liquidation of such liabilities requires enactment of an appropriation. Comparative data for fiscal year (FY) 2013 and FY 2012 has been included. MCC is presenting the following financial statements and additional information:

- Balance Sheet
- Statement of Net Cost
- Statement of Changes in Net Position
- Statement of Budgetary Resources
- Notes to Financial Statements
- Independent Auditor's Reports of the Millennium Challenge Corporation's Financial Statements, Internal Controls, and Compliance for the Periods Ending September 30, 2013 and September 30, 2012.

Note that totals may vary slightly due to rounding.

Balance Sheet

As of September 30, 2013 and September 30, 2012 (in thousands)		
Assets	**FY 2013**	**FY 2012**
Intragovernmental:		
Fund Balance with Treasury *(Note 2)*	$ 4,611,354	$ 5,321,289
Advances *(Note 3)*	38	1,708
Total Intragovernmental	**4,611,392**	**5,322,997**
Accounts Receivable, Net *(Note 4)*	814	7,489
General Property, Plant, and Equipment, Net *(Note 5)*	2,124	3,368
Advances *(Note 3)*	138,669	154,253
Total Assets	**$ 4,752,999**	**$ 5,488,107**
Liabilities		
Intragovernmental:		
Accounts Payable *(Note 1L)*	$ 442	$ 215
Other Liabilities	889	716
Total Intragovernmental	**1,331**	**931**
Accounts Payable *(Note 1L)*	6,436	16,757
Federal Employee and Veteran Benefits Payable	15	14
Other Liabilities:		
Accrual — Grant Liabilities (Note 7)	209,259	106,410
Accrued Funded Liabilities	6,433	6,293
Total Liabilities	**223,474**	**130,405**
Net Position		
Unexpended Appropriations — All Other Funds	4,526,375	5,346,633
Cumulative Results of Operations — All Other Funds	3,150	11,069
Total Net Position	**4,529,525**	**5,357,702**
Total Liabilities and Net Position	**$ 4,752,999**	**$ 5,488,107**

The accompanying notes are an integral part of these statements.

Statement of Net Cost

For the Years Ended September 30, 2013 and September 30, 2012 (in thousands)		
Program Costs *(Note 9)*	**FY 2013**	**FY 2012**
Compact Program Costs	$ 1,521,124	$ 1,129,720
609 (g) Program Costs	16,633	21,734
614 (g) Program Costs	1	220
Threshold Program Costs	9,677	16,371
Due Diligence Program Costs	35,525	41,478
Audit Costs	3,730	5,165
Administrative Costs	96,561	96,306
Net Cost of Operations	**$ 1,683,251**	**$ 1,310,994**

The accompanying notes are an integral part of these statements.

Statement of Changes in Net Position

For the Years Ended September 30, 2013 and September 30, 2012 (in thousands)	FY 2013	FY 2012
Cumulative Results of Operations:		
Beginning Balances	$ 11,069	$ 4,890
Budgetary Financing Sources:		
Appropriations Used	1,672,986	1,314,837
Other Financing Sources:		
Donations and Forfeitures of Property *(Note 8)*	320	275
Imputed Financing	2,026	2,061
Total Financing Sources	**1,675,332**	**1,317,173**
Net Cost of Operations	**(1,683,251)**	**(1,310,994)**
Net Change	**(7,919)**	**6,179**
Cumulative Results of Operations	**3,150**	**11,069**
Unexpended Appropriations:		
Beginning Balance	5,346,633	5,763,269
Budgetary Financing Sources:		
Appropriations Received	898,200	898,200
Other Adjustments	(45,472)	—
Appropriations Used	(1,672,986)	(1,314,837)
Total Budgetary Financing Sources	**(820,258)**	**(416,637)**
Total Unexpended Appropriations	**4,526,375**	**5,346,633**
Net Position	**$ 4,529,525**	**$ 5,357,702**

The accompanying notes are an integral part of these statements.

Statement of Budgetary Resources

For the Years Ended September 30, 2013 and September 30, 2013 (in thousands)	FY 2013	FY 2012
Budgetary Resources:		
Unobligated Balance Brought Forward, October 1	$ 1,760,688	$ 1,264,708
Recoveries of Prior Year Unpaid Obligations	57,623	11,068
Appropriations *(Note 1E)*	852,728	898,200
Total Budgetary Resources	**$ 2,671,039**	**$ 2,173,976**
Status of Budgetary Resources:		
Obligations Incurred	$ 1,165,631	$ 413,288
Unobligated Balance, End of Year:		
Apportioned	1,454,851	1,760,688
Unapportioned	50,557	—
Total Unobligated Balance, End of Year	1,505,408	1,760,688
Total Budgetary Resources	**$ 2,671,039**	**$ 2,173,976**
Change in Obligated Balance:		
Unpaid Obligations, Brought Forward, October 1	$ 3,559,785	$ 4,609,454
Obligations Incurred	1,165,631	413,289
Outlays (Gross)	(1,562,108)	(1,451,890)
Recoveries of Prior Year Unpaid Obligations	(57,623)	(11,068)
Obligated Balance, End of Year	**$ 3,105,685**	**$ 3,559,785**
Budget Authority and Outlays, Net:		
Budget Authority, Gross	$ 852,728	$ 898,200
Budget Authority, Net	**$ 852,728**	**$ 898,200**
Outlays, Gross	$ 1,562,108	$ 1,451,890
Agency Outlays, Net	**$ 1,562,108**	**$ 1,451,890**

The accompanying notes are an integral part of these statements.

Notes to the Financial Statements (As of September 30, 2013 and September 30, 2012)

Note 1 — Summary of Significant Accounting Policies

A. Reporting Entity

The Millennium Challenge Act of 2003, as amended, contained in Title VI, Division D of Public Law 108-199 (the Consolidated Appropriations Act of 2004) established MCC as a wholly-owned Government corporation, as defined by the Government Corporation Control Act. MCC's mission is to reduce poverty through grants by supporting sustainable, transformative economic growth in developing countries that maintain sound policy environments.

B. Reporting by Operational Components

MCC reports the results of its operations, as a whole, by its major programs or appropriation fund categories, which consist of the following:

- **Compact** — Compact funds comprise large, 5-year grants for countries meeting MCC's eligibility criteria
- **609(g) of the Millennium Challenge Act of 2003** — 609(g) funds cover contracts or grants that facilitate the development of a compact between MCC and a partner country
- **614(g) of the Millennium Challenge Act of 2003** — 614(g) funds comprise research contracts to improve data related to eligibility criteria. The contracts may be with a university, independent foundation, government entity, or other organization in the United States or a candidate country where such entity or country is undertaking research to improve data related to eligibility criteria under this title
- **Threshold** — Threshold programs are smaller grants awarded to countries that come close to meeting the eligibility criteria for compacts
- **Due Diligence** — Due Diligence funds support the cost of assessing compact proposals and providing compact implementation oversight
- **Audit** — Audit funds cover audits of MCC operations and programs. The U.S. Agency for International Development (USAID) Office of Inspector General (OIG) performs and manages MCC programmatic and financial audits
- **Administrative** — Administrative funds cover MCC's operating expenses

C. Basis of Accounting and Presentation

The accompanying financial statements have been prepared in accordance with generally accepted accounting principles (GAAP) in the United States of America and accounting standards issued by the Federal Accounting Standards Advisory Board (FASAB) in the format prescribed by the Office of Management and Budget (OMB) Circular No. A-136, *Financial Reporting Requirements* (revised on October 21, 2013). FASAB is recognized by the American Institute of Certified Public Accountants as the official accounting standards-setting body for United States Government entities. The financial statements present the financial position, net cost of operations, changes in net position, and budgetary resources of MCC, as required by the Chief Financial Officers (CFO) Act of 1990, the Government Management Reform Act of 1994, and the Government Corporation Control Act (31 United States Code [U.S.C.] §9106).

The accounting structure of Federal activities is designed to reflect both the accrual and budgetary basis of accounting. Under the accrual method of accounting, revenues are recognized when earned and expenses are recognized when a liability is incurred, without regard to receipt or payment of cash. The accompanying Balance Sheet, Statement of Net Cost, and Statement of Changes in Net Position are prepared using the accrual method of accounting. The Statement of Net Cost reports MCC's gross cost less earned revenues to arrive at net cost of operations. MCC has no earned revenue. Budgetary accounting facilitates compliance with legal constraints and controls over the use of Federal funds. Budgetary accounting principles are designed to recognize the obligation of funds according to legal requirements, which may be prior to the occurrence of an accrual-based transaction. The Statement of Budgetary Resources is prepared in accordance with budgetary accounting rules. In accordance with OMB Circular A-136 requirements, the Statement of Budgetary Resources presentation was significantly restructured compared to its presentation for FY 2012 in order to better align with the FY 2013 reporting format of the SF-133, *Report on Budget Execution and Budgetary Resources.* Due to this change, the FY 2012 Statement of Budgetary Resources has been reformatted compared to what was reported in FY 2012. The result is a change in format only; the underlying supporting information is unchanged.

While the financial statements have been prepared from the books and records of MCC in accordance with the formats prescribed by OMB, these financial statements are in addition to the financial reports used to monitor and control budgetary resources, which are prepared from the same books and records.

Intradepartmental transactions and balances have been eliminated from the Balance Sheet, Statement of Net Cost, and Statement of Changes in Net Position. The Statement of Budgetary Resources is reported on a combined basis; therefore, intradepartmental balances have not been eliminated.

MCC's financial statements should be read with the realization that they are for a component of the Federal Government, a sovereign entity, whose liabilities not covered by budgetary resources cannot be liquidated without the enactment of an appropriation, and that the payment of all liabilities other than for contracts can be abrogated by the Federal Government acting in its capacity as a sovereign entity.

D. Use of Estimates in Preparing Financial Statements

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions, and exercise judgment that affects the reported amounts of assets, liabilities, net position, and disclosure of contingent liabilities as of the date of the financial statements, as well as the reported amounts of financing sources, expenses, and obligations incurred during the reporting period. These estimates are based on management's best knowledge of current events, historical experience, actions MCC may take in the future, and on various other assumptions that are believed to be reasonable under the circumstances. The Notes to the Financial Statements include information to assist the reader in understanding the effect of changes in assumptions on the related information.

E. Budgetary Basis of Accounting

MCC's programs and activities are funded through no-year appropriations. Appropriations are recognized as an accrual-based financing source at the time they are used to pay program or administrative expenses, except for expenses to be funded by future appropriations. These funds are available for obligation without fiscal year limitation and remain available until expended. OMB apportions MCC program and administrative funds on an annual basis pursuant to statutory limitations in the annual appropriations bill. OMB segregates the apportionment of funds for Compact programs, 609(g) programs, 614(g) programs, Threshold programs, Due Diligence programs, Audit oversight, and Administrative programs. Because of the no-year status of MCC appropriations, unobligated Due Diligence, Audit, and Administrative funds are not returned to the U.S. Department of the Treasury (Treasury). Unobligated balances as of September 30, 2013, for these three categories of funds are transferred to the program fund category for future obligation until expended.

F. Grant Liabilities Accrual Methodology

MCC approves spending authority for a country-specific Millennium Challenge Account (MCA) on a quarterly basis. In reviewing the grant accrual methodology, it was determined that "unused spending authority" is the upper limit of the accrual. It was also determined that the "MCA In-house Invoices" is the lower limit of the accrual. Within these upper and lower limits, MCC is discounting unused spending authority by using a rolling average of actual disbursements to calculate the grant liabilities accrual.

G. Fund Balance with Treasury

Fund Balance with Treasury (FBWT) represents the aggregate amount of MCC's accounts with Treasury available to pay current and future liabilities and finance authorized purchases, except where prohibited by law. Treasury processes all cash receipts and disbursements on behalf of MCC. MCC's fund balances with Treasury represent no-year funds maintained in appropriated accounts. MCC's records are reconciled with those of Treasury on a monthly basis.

H. Advances

MCC provides grants through a country-specific MCA. This local accountable entity is responsible for managing and overseeing the development projects funded by the grants. MCC tracks the MCA's progress on a monthly basis. MCC receives a periodic reporting of advances from MCAs through monthly reporting of actual operating advances via the Monthly Commitments and Disbursements Report. Based on these reports, MCC adjusts advance and expense balances accordingly.

I. Accounts Receivable, Net

Accounts receivable reflect overpayments of payroll, travel, and other MCC current and former employee expenses. Accounts receivable also reflect substantiated disallowed MCA expenditures. Receivables that exist with foreign countries are considered sovereign debt. Public accounts receivable are presented net of an allowance for doubtful accounts, which is based on analyses of debtors' ability to pay, specific identification of probable losses, aging analyses of past-due receivables, or historical collection experience.

J. General Property, Plant, and Equipment, Net

MCC's general property, plant, and equipment (PP&E) consists of capitalized general equipment costs. MCC's capitalization threshold is $50,000 for all assets, except for information technology (IT) equipment, for which the capitalization threshold is $200,000. The basis for recording purchased PP&E is the full cost of the acquired asset, including all costs required to bring the asset to the form and location suitable for its intended use.

Leasehold improvements are depreciated using the straight-line method of depreciation over the estimated useful lives of improvement (usually between 8 and 10 years), depending on the years in the lease agreement. All other general PP&E is depreciated using the straight-line method over an estimated useful life of 5 years.

K. Liabilities

Liabilities represent the probable and measurable future outflow or other use of resources as a result of past transactions or events. Liabilities covered by budgetary resources are those liabilities for which Congress has appropriated funds or for which funding is otherwise available to pay amounts due. Liabilities not covered by budgetary or other resources represent amounts owed in excess of available Congressionally-appropriated funds or other amounts, where there is no certainty that the appropriations will be enacted. The Federal Government, acting in its sovereign capacity, can annul liabilities of MCC arising from any transaction or event, other than contracts.

L. Accounts Payable

Accounts payable represent amounts due to Federal and non-Federal entities for goods and services received by MCC that have not been paid at the end of the accounting period. Intragovernmental Accounts Payable represents payable transactions with other Federal Government agencies (e.g., USAID, U.S. Department of the Interior, etc.), while non-Federal Accounts Payable represents transactions with non-Federal entities.

M. Other Liabilities — Intragovernmental

Accrued Payroll

Accrued payroll consists of salaries, wages, and other compensation earned by the employees but not disbursed as of September 30, 2013. The liability is estimated for reporting purposes based on historical pay information.

Employee Retirement Benefits

MCC's employees participate in either the Federal Employees Retirement System (FERS) or the Civil Service Retirement System (CSRS). FERS was established by Public Law 99-335. Pursuant to this law, most U.S. Government employees hired after December 31, 1983, are covered by FERS and Social Security. FERS consists of Social Security, a gross annuity plan, and a Federal Thrift Savings Plan (TSP). MCC and the employee contribute to Social Security and the gross annuity plan at rates prescribed by law. In addition, each year MCC is required to contribute to the Federal TSP a minimum of one percent of the gross pay of employees covered by this system, match voluntary employee contributions up to three percent of the employees' gross pay, and match one-half of contributions between three and five percent of the employees' gross pay, for a maximum MCC contribution of 5 percent of pay. For FERS employees, MCC also contributes the employer's share of Medicare.

Federal employees hired prior to January 1, 1984, were allowed to elect whether they desired to participate in FERS (with Social Security coverage) or remain in CSRS. For employees covered by CSRS, MCC contributes seven percent of their gross pay toward their retirement benefits. A matching contribution of seven percent is required and is automatically deducted from the employees' gross pay. Employees under CSRS may participate in the TSP, but will not receive MCC's automatic or matching contributions.

Federal employee benefit costs paid by the U.S. Office of Personnel Management (OPM) and imputed by MCC are reported on the Statement of Net Cost. Contributions for FERS, CSRS, and other retirement benefits are insufficient to fund the programs fully and are subsidized by OPM. MCC imputes its share of the OPM subsidy, using cost factors provided by OPM, and reports the full cost of the programs related to its employees.

N. Federal Employee and Veteran Benefits Payable

Federal Employee and Veteran Benefits Payable consist of salaries, wages, leave, and benefits earned by employees but not disbursed at the end of the reporting period.

Actuarial Federal Employees Compensation Act

The Federal Employees Compensation Act (FECA) (established by Public Law 103-3) provides income and medical cost protection to covered Federal civilian employees injured on the job, employees who have incurred work-related occupational diseases, and beneficiaries of employees.

Claims incurred for benefits for MCC employees under FECA are administered by the Department of Labor (DOL) and later billed to MCC. MCC's actuarial liability for workers' compensation includes any costs incurred but unbilled as of year-end, as calculated by DOL, and not funded by current appropriations.

O. Other Liabilities — Public

Accrued Annual Leave

A liability for annual and other vested compensatory leave is accrued as earned and reduced when taken. The value of employees' unused annual leave at the end of each fiscal quarter is accrued as a liability. At the end of each fiscal quarter, the balance in the accrued annual leave account is adjusted to reflect current pay rates and leave balances. To the extent that current or prior year appropriations are not available to fund annual leave earned but not taken, funding will be obtained from future financing sources. Sick leave and other types of non-vested leave are expensed when used and, in accordance with Federal requirements, no accruals are recorded for unused sick leave.

Custodial Liabilities

Under current policies and procedures, MCC disburses funds for Compact and pre-Compact projects and activities upon the presentation of a valid invoice. However, under certain conditions, MCC will fund countries by advancing funds on an as-needed basis to cover basic needs. Such funds provided to the countries are required to be deposited in interest-bearing accounts, if legally feasible, until disbursed. The interest earned on these accounts is remitted to MCC by the MCA, and is then returned to Treasury's General Fund.

P. Net Position

Net position is composed of unexpended appropriations and cumulative results of operations. Unexpended appropriations are funds appropriated by Congress to MCC that are still available for expenditure. Cumulative results of operations represent the net differences between financing sources and expenses since MCC's inception.

Q. Judgment Fund

Certain legal matters to which MCC can be named as a party may be administered and, in some instances, litigated and paid by other Federal agencies. In general, amounts paid for Federal Tort Claims Act settlements or awards pertaining to these litigations are funded from a special appropriation administered by Treasury called the Judgment Fund. Although the ultimate disposition of any potential Judgment Fund proceedings cannot be determined, MCC management expects that any liability or expense that might ensue would not be material to MCC's financial statements.

R. Parent/Child Relationships with Other Federal Agencies

Allocation Transfers

MCC is a party to allocation transfers as a transferring (parent) entity with USAID, which serves as the recipient (child) entity. Allocation transfers are legal delegations by one Federal entity of its authority to obligate budget authority and outlay funds to another Federal entity. A separate fund account (allocation account) is created in Treasury as a subset of the parent fund account for tracking and reporting purposes. All allocation transfers of balances are credited to this account, and subsequent obligations and outlays that are incurred by the child entity are charged to this allocation account, as they execute the delegated activity on behalf of the parent entity. Generally, all financial activity related to these allocation transfers (e.g., budget authority, obligations, outlays) is reported in the financial statements of the parent entity, from which the underlying legislative authority, appropriations, and apportionments are derived.

Therefore, there are amounts reported in MCC's Balance Sheet, Statement of Net Cost, Statement of Changes in Net Position, and Statement of Budgetary Resources for which the activity is performed by USAID acting as the child in this financial relationship.

S. Contingencies

A loss contingency is an existing condition, situation, or set of circumstances involving uncertainty as to possible loss to MCC. The uncertainty ultimately should be resolved when one or more future events occur or fail to occur. The likelihood that the future event or events will occur confirms the loss; the incurrence of a liability can range from probable to remote. Statement of Federal Financial Accounting

Standards (SFFAS) No. 5, *Accounting for Liabilities of the Federal Government,* as amended by SFFAS No. 12, *Recognition of Contingent Liabilities from Litigation,* contains the criteria for recognition and disclosure of contingent liabilities.

MCC could be a party to various administrative proceedings, legal actions, and claims brought by or against it. With the exception of pending, threatened, or potential litigation, a contingent liability is recognized when a past transaction or event has occurred, a future outflow or other sacrifice of resources is more likely than not to occur, and the related future outflow or sacrifice of resources is measurable. For pending, threatened, or potential litigation, a contingent liability is recognized when a past transaction or event has occurred, a future outflow or other sacrifice of resources is likely to occur, and the related future outflow or sacrifice of resources is measurable.

T. Intragovernmental Transactions and Relationships

Intragovernmental transactions are transactions in which only Federal entities are parties to the transaction. MCC has intragovernmental relationships with various Federal entities. Transactions with the public are transactions in which one party to the transaction is a Federal entity and the other is a non-Federal entity.

If a Federal entity purchases goods or services from another Federal entity and sells them to the public, the exchange revenue is classified as with the public, but the related costs are classified as intragovernmental. The purpose of the classification is to enable the Federal Government to consolidate financial statements from all Federal entities to provide consolidated financial statements for the Federal Government as a whole.

Note 2 — Fund Balance with Treasury

MCC's FBWT balance is comprised of only General Funds, which primarily consist of no-year appropriated funds.

Fund Balance with Treasury as of September 30, 2013 and September 30, 2012 (in thousands)

Fund Balances	September 30, 2013	September 30, 2012
General Funds	$ 4,611,354	$ 5,321,289
Total	**$ 4,611,354**	**$ 5,321,289**

The Status of Fund Balance with Treasury is primarily the total fund balance as recorded in the general ledger for unobligated and obligated balances:

- **Unobligated Balance** – *Available* — The amount remaining in appropriated funds available for obligation in future fiscal years

- **Unobligated Balance** – *Unavailable* — The amount remaining in appropriated funds used only for adjustments to previously recorded obligations
- **Obligated Balance** – *Not Yet Disbursed* — The cumulative amount of obligations incurred for which outlays have not been made
- **Non-Budgetary Fund Balance with Treasury** — Comprised of amounts in General Fund Proprietary Receipts, Proceeds of Sales, Personal Property, and Undistributed Intragovernmental Payment funds.

Status of Fund Balance with Treasury as of September 30, 2013 and September 30, 2012 (in thousands)

Status of Fund Balance with Treasury	2013	2012
Unobligated Balance		
Available	$ 1,454,851	$ 1,760,688
Unavailable	50,557	—
Obligated Balance not yet Disbursed	3,105,684	3,559,785
Non-Budgetary FBWT	262	157
Reconciling Items	—	659
Total	**$ 4,611,354**	**$ 5,321,289**

Note 3 — Advances

As of September 30, 2013, MCC reported intragovernmental advances totaling $38 thousand, and public advances totaling $138,669 thousand. As of September 30, 2012, the amounts reported were $1,708 thousand and $154,253 thousand, respectively. The $15,584 thousand net decrease in public advances is composed primarily of the net effect of Compact closures, the addition of new Compacts, and fluctuations in Advance balances in ongoing Compacts.

Note 4 — Accounts Receivable, Net

Total receivables at September 30, 2013 and September 30, 2012 were $814 thousand and $7,489 thousand, respectively. The Accounts Receivable balance represents net valid claims by MCC to cash or other assets of other entities. Accounts Receivable Due from the Public is the total of miscellaneous debts due to MCC from employees and/or smaller reimbursements from other non-federal entities. A periodic evaluation of public accounts receivable is performed to estimate any uncollectible amounts based on current status. An allowance for doubtful accounts is recorded, for Accounts Receivable Due from the Public, to bring Accounts Receivable to its Net Realizable Value in accordance with SFFAS No. 1, *Accounting for Selected Assets and Liabilities.*

Note 5 — General Property, Plant, and Equipment, Net

MCC reports depreciation expense using the straight-line method over an asset's estimated useful life, beginning with the month the asset is placed in service. General PP&E is presented net of accumulated depreciation.

Status of General Property, Plant, and Equipment, Net as of September 30, 2013 (in thousands)	Estimated Useful Life	Cost	Accumulated Depreciation	Book Value
General PP&E				
Leasehold Improvements	8–10 years	$ 10,924	$ 8,836	$ 2,088
Other General PP&E	5 years	139	103	36
Total		**$ 11,063**	**$ 8,939**	**$ 2,124**

Status of General Property, Plant, and Equipment, Net as of September 30, 2012 (in thousands)	Estimated Useful Life	Cost	Accumulated Depreciation	Book Value
General PP&E				
Leasehold Improvements	8–10 years	$ 10,924	$ 7,619	$ 3,305
Other General PP&E	5 years	139	76	63
Total		**$ 11,063**	**$ 7,695**	**$ 3,368**

Note 6 — Leases

MCC leases office space in two adjacent locations in Washington, D.C. These operating leases are on 10-year (Bowen Building) and 8-year (City Center Building) lease terms that terminate on May 25 and May 26, 2015, respectively.

MCC also has short-term leases for one corporate vehicle (through September 28, 2015) and 14 copier machines (through September 29, 2017). The future lease payments due are depicted below.

Future Lease Payments Due — Buildings (in thousands)	Asset Category		
	Bowen Building	City Center	Totals
FY 2014	$ 5,590	$ 2,186	$ 7,776
FY 2015	2,349	912	3,261
Total Future Lease Payments	**$ 7,939**	**$ 3,098**	**$ 11,037**

Future Lease Payments Due — Equipment (in thousands)			
	Asset Category		
	Vehicle	Copier	Totals
FY 2014	$ 11	$ 44	$ 55
FY 2015	11	44	55
FY 2016	—	44	44
FY 2017	—	44	44
Total Future Lease Payments	**$ 22**	**$ 176**	**$ 198**

Note 7 — Accrual – Grant Liabilities

In September 30, 2013 and September 30, 2012, MCC had grant liabilities of $209,259 thousand and $106,410 thousand, respectively. The $102,849 thousand increase in grant liabilities was the result of the fluctuations related to changes in the compact portfolio in FY 2013.

Note 8 — Donated Services

On occasion, MCC may utilize donated services from other Federal agencies, individuals, and private firms in the course of its normal business operations. The approximate fair market value of donated services was $320 thousand for FY 2013 and $275 thousand for FY 2012.

Note 9 — Intragovernmental Costs

The below illustrates the value of exchange transactions between MCC and other Federal entities, as well as non-Federal (public) entities. Intragovernmental costs relate to transactions between MCC and other Federal entities. Public costs relate to transactions between MCC and non-Federal entities.

Intragovernmental Costs (in thousands)	2013	2012
Compact Programs		
Intragovernmental	$ 7,068	$ 6,531
Public	1,514,056	1,123,189
Total Compact Costs	**1,521,124**	**1,129,720**
609(g) Programs		
Intragovernmental	3,875	6,554
Public	12,758	15,180
Total 609(g) Costs	**16,633**	**21,734**
614(g) Programs		
Intragovernmental	—	—
Public	1	220
Total 614(g) Costs	**1**	**220**
Threshold Programs		
Intragovernmental	936	1,491
Public	8,741	14,880
Total Threshold Costs	**9,677**	**16,371**
Due Diligence Programs		
Intragovernmental	4,173	5,210
Public	31,352	36,268
Total Due Diligence Costs	**35,525**	**41,478**
Audit Programs		
Intragovernmental	3,554	3,313
Public	176	1,852
Total Audit Costs	**3,730**	**5,165**
Administrative Programs		
Intragovernmental	16,857	18,980
Public	79,704	77,326
Total Administrative Costs	**96,561**	**96,306**
Total Program Costs	**$ 1,683,251**	**$ 1,310,994**

Costs have been reflected by MCC-funded programs. Threshold program costs have dropped because MCC has signed no new Threshold agreements since FY 2010, and there was no new Threshold funding in FY 2013. MCC is in the process of establishing new Threshold programs, which will be implemented in FY 2014.

Note 10 — Undelivered Orders at the End of the Period

Undelivered orders at the end of the period totaled $3,021,121 thousand and $3,582,170 thousand as of September 30, 2013 and September 30, 2012, respectively.

Undelivered Orders at September 30, 2013 and September 30, 2012 (in thousands)

Programs	2013	2012
Compact	$ 2,826,652	$ 3,399,289
609(g)	26,885	24,358
614(g)	4	4
Threshold	25,349	31,423
Due Diligence	90,702	81,432
Audit	1,657	711
Administrative	49,872	44,953
Total	**$ 3,021,121**	**$ 3,582,170**

Note 11 — Explanation of Differences Between the Statement of Budgetary Resources and the Budget of the U.S. Government

The table below documents the material differences between the FY 2012 Statement of Budgetary Resources and the actual amounts reported for FY 2012 in the Budget of the Federal Government. Since the FY 2013 financial statements will be reported prior to the release of the Budget of the Federal Government, MCC is reporting for FY 2012 only. Typically, the Budget of the Federal Government with the FY 2013 actual data is published in February of the subsequent year. Once published, the FY 2013 actual data will be available on the OMB website at: www.whitehouse.gov/omb.

Explanation of Differences Between the Statement of Budgetary Resources and the Budget of the U.S. Government (in millions)

	Budgetary Resources	Obligations Incurred	Net Outlays
Statement of Budgetary Resources	$ 2,174	$ 413	$ 1,452
Deductions	1	1	1
Budget of the U.S. Government	**$ 2,173**	**$ 412**	**$ 1,451**

The $1 million difference for Budgetary Resources, Obligations Incurred, and Net Outlays is due to rounding. The Budget of the U.S. Government is reported by budget object class, which is rounded to the nearest million.

Note 12 — Reconciliation of Net Cost of Operations to Budget

SFFAS No.7, *Accounting for Revenues and Other Financing Concepts for Reconciling Budgetary and Financial Accounting,* requires a reconciliation of proprietary and budgetary accounting information. Accrual-based measures used in the Statement of Net Cost differ from the obligation-based measures used in the Statement of Budgetary Resources. The below note reconciles the net obligations derived from the Statement of Budgetary Resources and net costs of operations derived from the Statement of Net Cost by identifying key items that affect one financial statement but not the other for September 30, 2013 and September 30, 2012, respectively.

Reconciliation of Net Cost of Operations to Budget for the Year Ending September 30, 2013 (in thousands)

Resources Used to Finance Activities		FY 2013 Reported Program Costs	
Budgetary Resources Obligated		Gross Costs	
Obligations Incurred	$ 1,165,631		
Recoveries of Prior Year Unpaid Obligations	(57,623)	Net Program Costs	$ 1,683,251
Other Financing Sources	2,346		
Total Resources Used to Finance Activities	$ 1,110,354		
Total Resources Used to Finance Items Not Part of the Net Cost of Operations	$ 564,978		
Total Components of Net Cost of Operations that will Not Require or Generate Resources	7,919	Less: Earned Revenue	—
Net Cost of Operations per the Budget	**$ 1,683,251**	**Net Cost of Operations per the Statement of Net Cost**	**$ 1,683,251**

Reconciliation of Net Cost of Operations to Budget for the Year Ending September 30, 2012 (in thousands)

Resources Used to Finance Activities		FY 2012 Reported Program Costs	
Budgetary Resources Obligated		Gross Costs	
Obligations Incurred	$ 413,289		
Recoveries of Prior Year Unpaid Obligations	(11,068)	Net Program Costs	$ 1,310,994
Other Financing Sources	2,336		
Total Resources Used to Finance Activities	$ 404,557		
Total Resources Used to Finance Items Not Part of the Net Cost of Operations	$ 909,179		
Total Components of Net Cost of Operations that will Not Require or Generate Resources	1,244	Less: Earned Revenue	—
Advance Liquidation Adjustment	(3,986)		
Net Cost of Operations per the Budget	**$ 1,310,994**	**Net Cost of Operations per the Statement of Net Cost**	**$ 1,310,994**

Independent Auditor's Report

OFFICE OF INSPECTOR GENERAL

AUDIT OF THE MILLENNIUM CHALLENGE CORPORATION'S FINANCIAL STATEMENTS, INTERNAL CONTROLS, AND COMPLIANCE FOR THE PERIOD ENDING SEPTEMBER 30, 2013 AND 2012

AUDIT REPORT NO. M-000-14-001-C
December 13, 2013

WASHINGTON, DC

Financial information contained in this report may be privileged. The restrictions of 18 USC 1905 should be considered before any information is released to the public.

Office of Inspector General

December 13, 2013

Mr. Daniel Yohannes
Chief Executive Officer
Millennium Challenge Corporation
875 15th Street, NW
Washington, DC 20005-2203

Subject: Audit of the Millennium Challenge Corporation's Financial Statements, Internal Controls, and Compliance for the Period Ending September 30, 2013 and 2012 (Report No. M-000-14-001-C)

Dear Mr. Yohannes:

Enclosed is CliftonLarsonAllen LLP's, final report on the subject audit. The Office of Inspector General (OIG) contracted with the independent certified public accounting firm of CliftonLarsonAllen LLP, to audit the financial statements of the Millennium Challenge Corporation (MCC) for the period ending September 30, 2013. The contract required that the audit be performed in accordance with United States Generally Accepted Government Auditing Standards, Office of Management and Budget (OMB) Bulletin 14-02, Audit Requirements for Federal Financial Statements, and the GAO/PCIE Financial Audit Manual.

The Independent Auditors expressed an unqualified opinion on MCC's FY 2013 Financial Statements. The report stated that the financial statements referred to above present fairly, in all material respects, the net position of MCC as of September 30, 2013, and its net cost, changes in net position and budgetary resources for the fiscal year then ended, in conformity with accounting principles generally accepted in the United States of America.

In its audit of MCC's fiscal year 2013 financial statements the auditor's identified one issue that was considered a material weakness and three other issues that were considered significant deficiencies. These matters are listed below and are detailed in the auditor's report.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of an entity's financial statements will not be prevented, or detected and corrected on a timely basis.

U.S. Agency for International Development
Office of Inspector General
1300 Pennsylvania Ave, NW
Washington, DC 20523
http://oig.usaid.gov/

Material Weakness

- Ineffective and Inefficient Integration of Data, Processes, and Controls within the Financial Management Systems (Modified Repeat Finding)

A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Significant Deficiencies

- Validation Control over Grant Accrual Estimates Needs to be Strengthened (Modified repeat Finding)

- Monitoring of MCAs Audits Needs to be Strengthened (Modified Repeat Finding)

- Information Systems Controls Need Improvement

The auditors did not note any instance of material non-compliance with laws and regulations.

In carrying out its oversight responsibilities, the OIG reviewed CliftonLarsonAllen LLP, Internal Audit Report and audit documentation. This review, as differentiated from an audit in accordance with U.S. Generally Accepted Government Auditing Standards was not intended to enable the OIG to express, and we do not express, opinions on MCC's financial statements, or internal control; or on MCC's compliance with other laws and regulations. CliftonLarsonAllen LLP is responsible for the attached auditor's report, dated December 11, 2013, and the conclusions expressed in the report. However, our review disclosed no instances where CliftonLarsonAllen LLP, did not comply, in all material respects, with applicable standards.

To address the material weakness and significance deficiencies in internal controls reported by CliftonLarsonAllen LLP, we are listing below the findings with 11 recommendations to MCC's management:

<u>Material Weakness</u>

Ineffective and Inefficient Integration of Data, Processes, and Controls within the Financial Management Systems (Modified Repeat Finding)

Recommendations

With regards to the core financial system, we recommend that MCC:

1. Perform a comprehensive review and determine whether the SSP's financial management system is meeting MCC financial management and reporting needs. As part of this review, management should continue to evaluate whether:

    a. a separate grants management system that focuses on program and financial administrations that interfaces with the core financial system is needed, or

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b. to establish alternatives to recording numerous data lines in the Oracle AP module which is manual intensive and prone to errors.

2. Investigate and correct the underlying causes for the system errors and limitations that prevent or delay the recording, processing, and summarizing of accounting transactions. Key issues that remain unresolved should be escalated immediately rather than back-log the problem. MCC should ensure that errors and open tickets are resolved appropriately and timely by the SSP and that routine MCA accounting activities (such as the NA/NA fund transactions) are recorded in Oracle within the specified timeline. Moreover, manual adjusting journal entries should be used for limited transactions like unusual one-time entries or correcting entries.

3. In collaboration with the SSP, formalize in writing the system's issues and resolution process. This will include developing a standardized remedy ticket listing with relevant and historical information.

4. Continue to streamline the Monthly Commitments and Disbursements Report (MCDR) recording and adjustment process. With regards to supervisory reviews, we recommend that MCC:

5. Implement an effective management review of its accounting and financial reporting processes using the comprehensive review process to ensure that all transactions for the accounting period are accurately and completely reflected in the financial statements, beginning balances agreed to ending balances, and reconciling items are recorded timely. Such management reviews should be performed monthly or quarterly and at year-end timely.

6. Further review SSP data entries relating to MCA payment processing and related adjustments. Perform reconciliation of AP on a monthly basis and proactively resolve all differences.

<u>**Significant Deficiencies**</u>

Validation Control over Grant Accrual Estimates Needs to be Strengthened (Modified Repeat Finding)

Recommendations:

We recommend that MCC:

7. Develop and implement a logical and supportable look back validation process to assess the reasonableness of the grant accrual estimate, and then perform a grant accrual look back analysis on a quarterly basis for a sufficient period of time to develop a pattern or trend. The look back analysis and the results should provide MCC sufficient information to explain unusual variances between actual and estimates, or support updating the current grant accrual methodology. Such periodic assessment of the adequacy of the grant accrual methodology should be documented and supported by data analysis. Note that the accrued liability amount is subject to the risks that actual subsequent disbursement amount may be significantly different from management's estimate. When this occurs, management should further analyze the drivers/factors to ensure the validity and reasonableness of the estimation methodology.

8. Update the Expense Accruals Policy and Procedures to reflect the change in the methodology. At a minimum, the policy and procedures should include the following:

    a. documentation of the procedures and flow of information used in developing grant accrual estimates;
    b. a discussion of who (position title) is responsible for each step of the estimate as well as the review and approval process followed;
    c. the model used, the rationale for selecting the specific methodology, and, for programs with sufficient historical data, the degree of calibration within the projected spending model; and
    d. the sources of information, the logic flow, and the mechanics of the model, including the formulas and other mathematical functions.

9. Develop audit procedures for the MCA audit to compare spending authority amount granted against actual MCA expenses, and investigate and document significant variances. MCC should maintain a library of historical MCA financial data. This information may be used by MCC to validate or enhance its current methodology.

10. Continue to enhance the accrual methodology by:

    a. stratifying the MCAs based on variances in their spending rates and/or stages in the compact's life cycle;
    b. developing and implementing a process to ensure that compacts that are partially managed by MCC are fully addressed within the grant accrual process.
    c. addressing situations where the MCA exceeds its quarterly spending authority;
    d. addressing situations where the compact has expired and there is no spending authority and disbursements are still occurring;
    e. obtaining detailed document level breakdown of expenses to be used to compare against the accrual estimates;
    f. reviewing the disbursement patterns by compact to identify those with large fluctuations to determine the cause so that adjustments can be made in developing the spending plan or in how the grant accrual is calculated to improve the accuracy of the grant accrual estimate; and
    g. other factors as deemed necessary to achieve an acceptable precision of the accrual estimate.

Monitoring of MCA's Audits Needs to be Strengthened (Modified Repeat Finding)

Recommendation:

11. Continue the collaboration between the USAID OIG and the MCC management to improve timeliness of the MCA audits; adequacy of the MCA audit procedures; monitoring and reviewing the quality and performance of the MCA audits; and tracking and conducting follow-up of corrective action plans with the MCAs timely.

5

Information Systems Controls Need Improvement (Modified Repeat Finding)

Recommendation:

We are not repeating our recommendations which are included in the USAID OIG Report titled "Audit of Millennium Challenge Corporation's Fiscal Year 2013 Compliance with Federal Information Security Management Act of 2002," Audit Report M-000-13-005-P, dated September 20, 2013.

The OIG acknowledges MCC's management decisions for all 11 recommendations. Please inform us when final action has been achieved.

We appreciate the cooperation and courtesies extended to our staff and to the staff of CliftonLarsonAllen LLP, during the audit. Please contact Fred Jones at (202) 216-6963, if you have any questions concerning this report.

Sincerely,

/s/
Robert L. Fry
Acting Deputy Assistant Inspector General
for Audit
Millennium Challenge Corporation

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MILLENNIUM CHALLENGE CORPORATION

September 30, 2013

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CliftonLarsonAllen

CliftonLarsonAllen LLP
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INDEPENDENT AUDITORS' REPORT

To the Inspector General
U.S. Agency for International Development

To the Board of Directors
Millennium Challenge Corporation

In our audits of the fiscal years (FY) 2013 and 2012 financial statements of the Millennium Challenge Corporation (MCC), we found:

- The financial statements are presented fairly, in all material respects, in accordance with accounting principles generally accepted in the United States of America (U.S.);
- One material weakness and three significant deficiencies in internal control over financial reporting; and
- No instance of reportable noncompliance with certain provisions of laws, regulations, contracts, and grant agreements tested.

The following sections and Exhibits discuss in more detail: (1) these conclusions, (2) Management's Discussion and Analysis (MD&A), other required supplementary information (RSI), and other information included with the financial statements, (3) management's responsibility, (4) our responsibilities, (5) management's response to findings, and (6) the current status of prior year findings.

REPORT ON THE FINANCIAL STATEMENTS

We have audited the accompanying financial statements of MCC, which comprise the balance sheets as of September 30, 2013 and 2012, and the related statements of net cost and changes in net position, and the combined statements of budgetary resources, for the years then ended, and the related notes to the financial statements. The objective of our audits was to express an opinion on the fairness of these financial statements.

Management's Responsibility for the Financial Statements

MCC management is responsible for the (1) preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the U.S., (2) preparation, measurement, and presentation of the RSI in accordance with accounting principles generally accepted in the U.S., (3) preparation and presentation of other information in documents containing the audited financial statements and auditors' report, and consistency of that information with the audited financial statements and the RSI; (4) design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

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Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the U.S. and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement. We also conducted our audits in accordance with Office of Management and Budget (OMB) Bulletin No. 14-02*, Audit Requirements for Federal Financial Statements,* (OMB Bulletin 14-02).

An audit of financial statements involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the auditors' assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit of financial statements also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion on the Financial Statements

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of MCC as of September 30, 2013 and 2012, and its net costs, changes in net position, and budgetary resources for the years then ended, in accordance with accounting principles generally accepted in the U.S.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the U.S. require that MCC's MD&A and other Required Supplementary Information (RSI) be presented to supplement the financial statements. Such information, although not a part of the financial statements, is required by the Federal Accounting Standards Advisory Board (FASAB), who considers it to be an essential part of financial reporting for placing the financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the MD&A and other RSI in accordance with auditing standards generally accepted in the U.S., which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the financial statements, and other knowledge we obtained during our audit of the financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

All other information exclusive of the financial statements, MD&A and other RSI as listed in the table of contents contains a wide range of information, some of which is not directly related to the financial statements. This information is presented for purposes of additional analysis and is not a required part of the financial statements or RSI. The information has not been subjected to the auditing procedures applied in the audit of the financial statements, and accordingly, we do not express an opinion or provide any assurance on it.

REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

Report on Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered MCC's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of MCC's internal control or on management's assertion on internal control included in the MD&A. Accordingly, we do not express an opinion on the effectiveness of MCC's internal control or on management's assertion on internal control included in the MD&A.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, we identified certain deficiencies in internal control described below that we consider to be a material weakness and significant deficiencies.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of MCC's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiencies summarized below and described in Exhibit 1 to be a material weakness.

Ineffective and Inefficient Integration of Data, Processes and Controls within the Financial Management Systems

A *significant deficiency* is a deficiency, or combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the deficiencies summarized below and described in Exhibit 2 to be significant deficiencies.

Validation Control over Grant Accrual Estimates Needs to be Strengthened

Monitoring of MCAs Audits Needs to be Strengthened

3

Information Systems Controls Need Improvement

Also, as required by OMB Bulletin 14-02, we compared the material weakness identified during the audit with the material weakness included in the MCC's Federal Managers Financial Integrity Act (FMFIA) report that relate to financial reporting. We noted no exception.

Report on Compliance and Other Matters

As part of obtaining reasonable assurance about whether MCC's financial statements are free from material misstatement, we performed tests of MCC's compliance with certain provisions of laws, regulations, contracts, and grant agreements that have a direct effect on the determination of material amounts and disclosures in the financial statements. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported in accordance with *Government Auditing Standards*, issued by the Comptroller General of the United States or OMB Bulletin 14-02.

Management's Responsibility for Internal Control and Compliance

MCC management is responsible for (1) evaluating the effectiveness of internal control over financial reporting based on criteria established under the FMFIA, (2) providing a statement of assurance on the overall effectiveness on internal control over financial reporting, and (3) ensuring compliance with other applicable laws, regulations, contracts, and grant agreements.

Auditors' Responsibilities

We are responsible for: (1) obtaining a sufficient understanding of internal control over financial reporting to plan the audit, (2) testing compliance with certain provisions of laws and regulations that have a direct and material effect on the determination of material amounts and disclosures in the financial statements and applicable laws for which OMB Bulletin 14-02 requires testing, and (3) applying certain limited procedures with respect to the RSI included with the financial statements.

We did not evaluate all internal controls relevant to operating objectives as broadly established by the FMFIA, such as those controls relevant to preparing statistical reports and ensuring efficient operations. We limited our internal control testing to testing controls over financial reporting. Because of inherent limitations in internal control, misstatements due to error or fraud, losses, or noncompliance may nevertheless occur and not be detected. We also caution that projecting our audit results to future periods is subject to risk that controls may become inadequate because of changes in conditions or that the degree of compliance with controls may deteriorate. In addition, we caution that our internal control testing may not be sufficient for other purposes.

We did not test compliance with all laws and regulations applicable to MCC. We limited our tests of compliance to selected provisions of laws and regulations that have a direct effect on the determination of material amounts and disclosures in the financial statements and those required by OMB Bulletin 14-02 that we deemed applicable to MCC's financial statements for the fiscal year ended September 30, 2013. We caution that noncompliance with laws and regulations may occur and not be detected by these tests and that such testing may not be sufficient for other purposes.

MANAGEMENT'S RESPONSE TO AUDIT FINDINGS

Management's response to audit findings identified in our report is presented in Exhibit 4. We did not audit MCC's response and, accordingly, we express no opinion on it.

STATUS OF PRIOR YEAR'S CONTROL DEFICIENCIES AND NONCOMPLIANCE ISSUES

We have reviewed the status of MCC's corrective actions with respect to the findings included in the prior year's Independent Auditors' Report, dated November 12, 2012. The status of prior year findings and recommendations is presented in Exhibit 3.

PURPOSE OF THE REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND THE REPORT ON COMPLIANCE AND OTHER MATTERS

The purpose of the Report on Internal Control over Financial Reporting and the Report on Compliance and Other Matters sections of this report is solely to describe the scope of our testing of internal control and compliance and the result of that testing, and not to provide an opinion on the effectiveness of MCC's internal control or on compliance. These reports are an integral part of an audit performed in accordance with *Government Auditing Standards* in considering MCC's internal control and compliance. Accordingly, these reports are not suitable for any other purpose.

CLIFTONLARSONALLEN LLP

CliftonLarsonAllen LLP

Arlington, Virginia
December 11, 2013

EXHIBIT 1

MATERIAL WEAKNESS

1. Ineffective and Inefficient Integration of Data, Processes, and Controls within the Financial Management Systems (Modified Repeat Finding)

GAO *Standards for Internal Control in the Federal Government* states that internal control is not one event, but a series of actions and activities that occur throughout an entity's operations and on an ongoing basis. Control activity, which is one of the standards for internal control, may be applied in a computerized information system environment, or through manual processes. Information system control should be installed at an application's interfaces with other systems to ensure that all inputs are received and are valid, and outputs are correct and properly distributed. Some control activities include: controls over information processing, management of human capital, proper execution of transactions and events, accurate and timely recording of transactions and events, and appropriate documentation of transactions. Monitoring, which is another standard for internal control, is performed continually and is ingrained in the agency's operations. It includes regular management and supervisory activities, comparisons, reconciliations, and other actions people take in performing their duties.

Accounting is a systematic process of identifying, recording, measuring, classifying, verifying, summarizing, interpreting and communicating financial events. These financial events are ultimately presented in financial statements through the financial reporting process. Each step in the accounting process is an integral part of the financial reporting process.

A financial management system includes the core financial system and the financial portions of mixed systems necessary to support financial management, including automated and manual processes, procedures and controls, data, software, and support personnel dedicated to the operation and maintenance of system functions.

MCC continued to design and implement internal control to improve its accounting and financial reporting processes. For example, in FY 2013, MCC required the Millennium Challenge Account entities (MCAs) to perform and submit monthly reconciliation of compact disbursements report (MCDR) with those recorded in MCC's financial systems and resolve the identified variances with the MCC's shared service provider (SSP) timely. In addition, MCC established some accounting transaction models to be followed when performing routine manual accounting entries to ensure that they are done correctly. Moreover, MCC has successfully exported its core system's trial balance (TB) into a spreadsheet used to prepare the financial statements and eliminated significant manual cutting and pasting of the systems' TB into the FS spreadsheets. However, MCC continues to face a huge challenge in its accounting and reporting processes primarily due to its financial management systems' limitations, and the sheer volume of financial activities that are complex and require manual attentions and reviews to compensate for the systems' limitations. As a result, the accounting and financial reporting processes, as a whole, is inefficient, and the risks that internal controls are not effective to prevent, detect, and correct errors timely is high, increasing the reasonable possibility of a material misstatement in the financial statements.

We presented all our findings to MCC management in written notices of findings and recommendations (NFRs) and obtained their written responses to our NFRs. We have summarized and grouped those findings into systemic issues below:

a. MCC uses a SSP to process its accounting transactions. The SSP's core financial system current configurations prevent MCC from recording significant transactions in a systematic and correct manner. Issues with Oracle posting model and related version upgrades continue to exist. Our review of the September 30, 2013 SSP's open system ticket report, which tracks financial system issues, identified issues that remain unresolved for an unreasonable period of time. Due to the volume and variety of transactional financial events that MCC must record relating to its grantees; MCC frequently has to prepare manual journal vouchers and system's adjustments at the back end of the transactions to correct errors such as the differences between the a) Purchase Order (PO) and General Ledger (GL) module, b) Accounts Payable (AP) and GL module, c) incorrect postings, d) system module interface errors, and e) others. This system deficiency, combined with MCC and/or SSP's inadequate and untimely reviews and corrective actions, negatively impact MCC's ability to record transactions timely, properly, and accurately. Although MCC applied compensating controls to detect and correct these errors, with the sheer volume and complexity of these transactions (automated and manual), there is a high risk that errors will not be detected and corrected timely or not detected at all. Our audit identified instances where this situation occurred. Moreover, this system deficiency results in inefficiencies and negatively impacts MCC's limited staff resources.

   The government-wide policies and standards issued pursuant to FMFIA, states that agencies are responsible for managing their financial management system even when they utilize a service provider to implement, operate and maintain the systems. Agencies must ensure that their financial management systems meet applicable Federal requirements and are adequately supported throughout the systems' life cycle. Furthermore, agencies must monitor the service provider's performance and ensure that service failures are resolved promptly.

b. Although MCC has made strides in improving its financial reporting process by implementing certain quality control review processes in response to prior year's findings, much still needs to be done. MCC's accounting and financial statements preparation process continue to be susceptible to errors even though a number of functionalities have been automated. MCC uses the Oracle federal financial management system (Oracle) to generate its financial statements. Manual journal voucher (JV) entries are posted directly into Oracle to correct errors and/or post adjustments. Oracle then automatically generates the financial statements from these data inputs. Our audit identified instances where MCC missed posting manual journal entries, or posted correcting journal entries that resulted in further errors in Oracle at June 30, 2013 and September 30, 2013. Some of these missing manual journal entries or erroneous correcting journal entries are described in c below.

c. In reviewing the financial statements and performing our internal control testing, we identified errors and control deficiencies that led us to question the effectiveness and timeliness of supervisory reviews. For example,
   - Advances balance at June 30, 2013 was overstated by $119 million which was the first quarter accrual that was not reversed in the subsequent two quarters. MCC uses manual journal entry to reverse the accrual. MCC detected and corrected the error in September 2013.

1-2

- Compact related expenses of approximately $2.4 million from several MCAs were erroneously reported as Accounts Payable due to SSP recording errors within Oracle.
- Undelivered order (UDO) amount disclosed in the notes to the financial statements was erroneously recorded in the "Compact" portion of UDO overstating the amount disclosed by $50 million.
- Incorrect cost classification as "with the public" and negative program cost of approximately $1.4 million were presented in the note disclosure due to the absence of a trading partner code being entered in oracle at the time of entry.
- The SSP initiated JVs were not always tracked in the MCC consolidated JV log and did not have approval from authorized MCC personnel.
- MCC does not always validate the propriety of the SSP's open ticket resolution. The remedy ticket listing maintained to keep track of open ticket system's issues is overly broad and difficult to know the exact status of any issue without extensive follow-up. Furthermore, issues resolved are removed from the listing without any history tracking; that is, what was the original issue; how was the issue resolved; how extensive was the issue; and whether the resolution corrected the issue.
- JVs have inaccurate or inadequate explanation and/or supporting documentation.
- MCC and the SSP, separately and unknowingly, made correcting entries in an effort to correct same transactions incorrectly posted in Oracle. This resulted in further errors in the accounts that required an extensive effort from both the SSP and MCC to resolve.

Recommendations

With regards to the core financial system, we recommend that MCC:

1. Perform a comprehensive review and determine whether the SSP's financial management system is meeting MCC financial management and reporting needs. As part of this review, management should continue to evaluate whether:
    a. a separate grants management system that focuses on program and financial administrations that interfaces with the core financial system is needed, or
    b. to establish alternatives to recording numerous data lines in the Oracle AP module which is manual intensive and prone to errors.

2. Investigate and correct the underlying causes for the system errors and limitations that prevent or delay the recording, processing, and summarizing of accounting transactions. Key issues that remain unresolved should be escalated immediately rather than back-log the problem. MCC should ensure that errors and open tickets are resolved appropriately and timely by the SSP and that routine MCA accounting activities (such as the NA/NA fund transactions) are recorded in Oracle within the specified timeline. Moreover, manual adjusting journal entries should be used for limited transactions like unusual one-time entries or correcting entries.

3. In collaboration with the SSP, formalize in writing the system's issues and resolution process. This will include developing a standardized remedy ticket listing with relevant and historical information.

4. Continue to streamline the Monthly Commitments and Disbursements Report (MCDR) recording and adjustment process.

With regards to supervisory reviews, we recommend that MCC:

5. Implement an effective management review of its accounting and financial reporting processes using the comprehensive review process to ensure that all transactions for the accounting period are accurately and completely reflected in the financial statements, beginning balances agreed to ending balances, and reconciling items are recorded timely. Such management reviews should be performed monthly or quarterly and at year-end timely.

6. Further review SSP data entries relating to MCA payment processing and related adjustments. Perform reconciliation of AP on a monthly basis and proactively resolve all differences.

EXHIBIT 2

SIGNIFICANT DEFICIENCIES

1. Validation Control over Grant Accrual Estimates Needs to be Strengthened (Modified Repeat Finding)

MCC reported approximately $1.5 billion in compact grant related expenditures and an accrued grant liability of $209 million for expenditures incurred by the Millennium Challenge Accounts (MCAs) but not yet paid by MCC at September 30, 2013. MCC applied its new grant accrual methodology for the first time at September 30, 2012.

MCC's new accrual methodology is calculated based on an MCA's unused spending authority. MCC uses the MCA's "in-house invoices" as the floor and the spending authority request as the ceiling in calculating the accrued liability. MCA's in-house invoices are actual invoices held by the MCA waiting to be submitted to the SSP for processing. The spending authority request by MCAs includes expenses that were incurred but not yet reported. MCC approves the quarterly spending authority request in advance for each MCA. The unused spending authority at the end of the quarter is used in the accrual calculation for each MCA. MCC uses the MCA disbursement rate against the spending authority along with the disbursement rates for the last three quarters to determine an average rate. The average rate is then subtracted against 100 percent to arrive at a rate that is applied to the unused spending authority in calculating the grant accrual estimate for the MCA.

In FY 2013, MCC continues to refine its accrual methodology and started to accumulate data store to validate its methodology. For example, MCC separately evaluated the accruals for compact agreements that were expiring in FY 2013. Moreover, MCC performed follow-up inquiries with MCAs whose accrual estimates were not within their expectations. Through these reviews, MCC notified an MCA and the MCC Department of Compact Operations in writing, of spending authority request that seemed to be way overstated when compared to the actual results. However, MCC still has not validated some significant assumptions in its accrual methodology and still needs to continue to develop its historical data store to support its assumptions and validation.

Some of MCC's bases for validating the reasonableness of the grant accrual was inadequate and could not be supported. For example, MCC is relying on an assumption that in-house invoices and accrued expenses are being paid within the next 30 days in its grant accrual methodology. Given the exceptions we noted in our tests, MCC needs to perform additional validation to ensure that this assumption is still correct; otherwise, the analysis of the accrual to actual may be off and could impact MCC's decisions to adjust the accrual when such an adjustment may not be warranted. We found evidence that a significant portion of those costs would not be paid until the following months.

In addition, although MCC's current methodology does not require further analysis on a quarter when the difference (in total) between the disbursements and the accrual calculation is less than 10%, our tests showed, when we compared quarterly accruals to the subsequent month's disbursements, that the quarterly fluctuations on a number of the MCAs individually were over +/- 50% and as high as +/- 350%.

FASAB Federal Financial Accounting Technical Release (TR) 12, *Accrual Estimates for Grant Programs,* states that "As part of agencies' internal control procedures to ensure that grant accrual estimates for the basic financial statements were reasonable, agencies should validate grant accrual estimates by comparing the estimates with subsequent grantee reporting." "Preparing reliable and timely accrual estimates for grant programs must be a joint effort between the budget, financial, and program offices at each agency." "Agencies should document and maintain support for the data and assumptions used to develop grant accrual estimates. The documentation will facilitate the agency's review of the assumptions, a key internal control, and will facilitate the auditor's testing of the estimates."

In addition, MCC Expense Accrual Policy and Procedures, dated March 2011, do not reflect the current grant accrual methodology implemented in September 2012. In developing its policy and procedures, MCC should include various practical scenarios in its grant accrual calculation, such as how the spending accrual ceiling will be determined when compacts are partially managed by MCC; addressing situations where the compact has expired and there is no spending authority and disbursements are still occurring; advances being included in the spending authority requests and subsequent disbursements as expenses; and others.

TR 12 also states that: "Documented procedures are important to communicate relevant information on the grant accrual estimation to employees and management as well as other interested parties, such as auditors. As an agency experiences employee turnover, these documented procedures can provide vital information for new employees on how to complete reliable, well supported grant accrual estimates. Such documentation may be used to establish consistent procedures for developing grant accrual estimates across grant programs with similar characteristics."

Recommendations

We recommend that MCC:

7. Develop and implement a logical and supportable look back validation process to assess the reasonableness of the grant accrual estimate, and then perform a grant accrual look back analysis on a quarterly basis for a sufficient period of time to develop a pattern or trend. The look back analysis and the results should provide MCC sufficient information to explain unusual variances between actual and estimates, or support updating the current grant accrual methodology. Such periodic assessment of the adequacy of the grant accrual methodology should be documented and supported by data analysis. Note that the accrued liability amount is subject to the risks that actual subsequent disbursement amount may be significantly different from management's estimate. When this occurs, management should further analyze the drivers/factors to ensure the validity and reasonableness of the estimation methodology.

8. Update the Expense Accruals Policy and Procedures to reflect the change in the methodology. At a minimum, the policy and procedures should include the following:

    a. documentation of the procedures and flow of information used in developing grant accrual estimates;
    b. a discussion of who (position title) is responsible for each step of the estimate as well as the review and approval process followed;
    c. the model used, the rationale for selecting the specific methodology, and, for programs with sufficient historical data, the degree of calibration within the projected spending model; and

d. the sources of information, the logic flow, and the mechanics of the model, including the formulas and other mathematical functions.

9. Develop audit procedures for the MCA audit to compare spending authority amount granted against actual MCA expenses, and investigate and document significant variances. MCC should maintain a library of historical MCA financial data. This information may be used by MCC to validate or enhance its current methodology.

10. Continue to enhance the accrual methodology by:

    a. stratifying the MCAs based on variances in their spending rates and/or stages in the compact's life cycle;
    b. developing and implementing a process to ensure that compacts that are partially managed by MCC are fully addressed within the grant accrual process.
    c. addressing situations where the MCA exceeds its quarterly spending authority;
    d. addressing situations where the compact has expired and there is no spending authority and disbursements are still occurring;
    e. obtaining detailed document level breakdown of expenses to be used to compare against the accrual estimates;
    f. reviewing the disbursement patterns by compact to identify those with large fluctuations to determine the cause so that adjustments can be made in developing the spending plan or in how the grant accrual is calculated to improve the accuracy of the grant accrual estimate; and
    g. other factors as deemed necessary to achieve an acceptable precision of the accrual estimate.

2. Monitoring of MCAs Audits Needs to be Strengthened (Modified Repeat Finding)

OMB Circular A-123, *Management Responsibility for Internal Control,* states that monitoring the effectiveness of internal control should occur in the normal course of business. In addition, periodic reviews, reconciliations or comparisons of data should be included as part of the regular assigned duties of personnel. Periodic assessments should be integrated as part of management's continuous monitoring of internal control, which should be ingrained in the agency's operations. If an effective continuous monitoring program is in place, it can level the resources needed to maintain effective internal controls throughout the year.

An adequate monitoring system oversees the design, implementation, and effectiveness of controls in mitigating risks. This monitoring system can be structured as an ongoing assessment program (for instance, supervisory reviews of day to day financial operations and reporting) or as a point in time program when a point in time assessment is required (for instance, MCA audits).

When a country is awarded a grant (compact), it sets up its own local MCA accountable entity to manage and oversee all aspects of implementing the compact. The MCAs, as the grantees of MCC's funds, are responsible for submitting financial, programmatic and compliance documentation to MCC in accordance with their compact agreements with MCC and other administrative requirements. MCC, as the grantor, is responsible for reviewing and monitoring the MCA's compliance with the compact agreement and other administrative requirements. MCC needs to continue to strengthen its monitoring controls over the MCA audits.

MCAs are required to obtain an annual (or semi-annual as agreed upon) financial audit of the MCC funds by an independent auditor. We reviewed the most recent audits for 15 MCAs, which accounted for a total of 15 MCA audit reports. Similar to last year's finding, 9 out of 15 (or 60 percent) audit reports were not received timely or were already due but not yet received as of November 15, 2013, our test date. There were 7 audit reports that were submitted late, ranging from 1 month to 4 months late, and 2 audit reports due but not yet received that were over seven months late as of the test date.

A financial audit of the MCA Fund Accountability Statement conducted by an independent auditor in accordance with *Government Auditing Standards* issued by the Comptroller General of the United States, provides an assurance to MCC that the MCA's revenues received, costs incurred, and commodities and technical assistance directly procured by the MCC are not materially misstated, and that tests of MCA's internal control and compliance with compact terms and applicable laws and regulations related to MCC funded programs were performed. The MCA financial audit is a key MCC internal control over monitoring of MCA's control over financial reporting and compliance and its reliance on MCA's financial reports. Accordingly, MCC should ensure that these audits are performed and submitted timely, reviewed timely, and corrective actions, if any, are implemented timely.

A timely audit involves the timely engagement of an audit firm by the MCA, an agreed upon timeline that ensures that the deliverables are provided within the deadlines, quality deliverables from the audit firms, and timely responses from the MCA and the audit firms. We understand that both USAID OIG and MCC are working together to minimize the delays in the MCA audits, but more can be done to address the root causes of these delays.

Recommendation

11. Continue the collaboration between the USAID OIG and the MCC management to improve timeliness of the MCA audits; adequacy of the MCA audit procedures; monitoring and reviewing the quality and performance of the MCA audits; and tracking and conducting follow-up of corrective action plans with the MCAs timely.

3. Information Systems Controls Need Improvement (Modified Repeat Finding)

All business processes today are impacted in some respects by information systems applications, policies, and controls. Information system is key to financial information collection, classification, allocations, and reporting.

Information systems controls must be in place to ensure that critical data, transactions and programs are processed in a timely manner. These include controls over MCC's general support system used to gain access to the contractor owned financial applications. Our evaluation of the general and application controls of MCC's key information technology infrastructure identified the following control weaknesses, taken together, constitute a significant deficiency.

Security Management

- MCC needs to strengthen personnel out-processing procedures. MCC personnel exit checklists were not maintained in the Staff Track and Reconciliation System (STARS) for as required in the MCC Exit Policy and Clearance Procedures. Additionally, while the new exit process had been announced and the technology implemented, the process had not been adopted by the stakeholders involved: Human Resources, Contracts, and Office of Security.

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- MCC did not properly assess system risks for the fiscal year. For example:
    - MCC did not have an Authorization to Operate (ATO) for the MCC MIS system, even though the system is currently in the production environment.
    - MCC had not maintained a current ATO for the MIDAS application. The ATO expired on March 5, 2013, but the system was still in the production environment.
    - MCC had not performed an annual risk assessment for the MIDAS or MCC MIS systems.

- MCC needs to ensure all personnel receive security awareness training. MCC did not track users who failed to participate in the daily Tips of the Day. In addition, MCC did not establish a required number of tips a user must view each month or year.

- MCC did not fully implement NIST Special Publication 800-53, Revision 3 into its information system security policies. MCC was in the process of updating the Policy; however, it was not finalized.

Contingency Planning

- MCC needs to update the disaster recovery plan to reflect lessons learned. The MCC Disaster Recovery Plan had not been updated to reflect lessons learned from the disaster recovery tests that occurred in December 2012.

Access Controls

- MCC needs to periodically review network accounts. MCC did not perform quarterly reviews of MCCNet group memberships as required by the MCC Access Control Procedures. In addition, MCC did not review service accounts that had never logged into system.

- MCC needs to strengthen audit and accountability controls. MCC was not reviewing or analyzing domain and server audit records for indications of inappropriate or unusual activity.

Configuration Management

- MCC needs to strengthen security controls surrounding patch and configuration management. MCC had procedures in place that use vulnerability scanning software to assist in detecting and reporting security vulnerabilities. However, our evaluation identified critical and high vulnerabilities on MCC hosts that MCC did not identify through its scans.

- MCC did not effectively track and maintain their asset inventory. MCC's asset management is largely a manual process. The manual nature of the asset inventory allowed multiple, incorrect or delayed entries in the asset inventory.

- MCC's change management procedures did not describe types of changes and levels of testing applied to the changes prior to approval by the Configuration Control Board.

These findings highlight MCC's lack of compliance with the NIST publications, OMB Circulars, and FISMA requirements as listed below:

OMB Circular A-130, *Management of Federal Information Resources,* Appendix III, states "Agencies shall implement and maintain a program to assure that adequate security is provided for all agency information collected, processed, transmitted, stored, or disseminated in general support systems and major applications."

The Federal Information Security Management Act of 2002 (FISMA) requires that each agency develop an agency-wide information security program that includes:

- Periodic assessments of risk, including the magnitude of harm that could result from the unauthorized access, use, disclosure, disruption, modification, or destruction of information and information systems that support the operations and assets of the organization;
- Policies and procedures that are based on risk assessments, cost-effectively reduce information security risks to an acceptable level and address information security throughout the life cycle of each organizational information system;
- Plans for providing adequate information security for networks, facilities, information systems, or groups of information systems, as appropriate;
- Security awareness training to inform personnel of the information security risks associated with their activities and their responsibilities in complying with organizational policies and procedures designed to reduce these risks;
- Periodic testing and evaluation of the effectiveness of information security policies, procedures, practices, and security controls to be performed with a frequency depending on risk, but no less than annually;
- A process of planning, implementing, evaluating, and documenting remedial actions to address any deficiencies in the information security policies, procedures, and practices of the organization;
- Procedures for detecting, reporting, and responding to security incidents; and
- Plans and procedures for continuity of operations for information systems that support the operations and assets of the organization.

By not effectively implementing and enforcing IT policies and procedures, there is an increased risk that financial and sensitive information may be inadvertently or deliberately misused and may result in improper disclosure or theft without detection.

Recommendation

We are not repeating our recommendations which are included in the USAID OIG Report titled "Audit of Millennium Challenge Corporation's Fiscal Year 2013 Compliance with Federal Information Security Management Act of 2002," Audit Report M-000-13-005-P, dated September 20, 2013.

EXHIBIT 3

STATUS OF PRIOR YEAR FINDINGS AND RECOMMENDATIONS

As required by *Government Auditing Standards* and OMB Bulletin 14-02, we have reviewed the status of MCC corrective actions with respect to the findings and recommendations included in MCC's Report on Internal Control for FY 2012. The following analysis provides our assessment of the progress MCC has made through September 30, 2013 in correcting the noted deficiencies.

FY 2012 Findings	FY 2012 Summary of Recommendations	FY 2013 Status
I. Material Weakness: Ineffective and Inefficient Interrelationship among Software, Personnel, Procedures, Controls and Data within MCC's Financial Management Systems	1. Perform a comprehensive review and determine whether the service provider's financial management system is substantially in compliance with the federal financial management system's requirements and meeting MCC financial management and reporting needs. As part of this review, management should determine if a separate grants management system that focuses on program administrations that interfaces with the core financial system is needed.	Open
	2. Investigate and correct the causes for the underlying system errors and limitations that prevent or delay the recording, processing, and summarizing of accounting transactions.	Open
	3. Review USSGL transactions posting models so that all routine accounting transactions are included in the normal accounting processes.	Closed
	4. Hard code key cells in the excel spreadsheets used in preparing and generating the financial statements to prevent unintentional or inadvertent changes.	Closed
	5. Limit access and ability to make changes to the workbook to a few personnel. Assign a staff and a designate as primarily responsible and accountable for the workbook.	Closed
	6. Create a log to document changes to the workbook, the date of change, the person making the change, and the changes made.	Closed

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	7. Investigate the use of alternative approaches such as the use of a financial statement generation software tool or other financial management system that can interface with the trial balance or the core financial system and automatically generate the financial statements.	Closed
	8. Develop a comprehensive financial statements review process that detail specific review steps performed, results of such reviews, steps taken to resolve discrepancies noted, and related management resolution.	Closed
	9. Implement an effective management review using the comprehensive review process developed in recommendation 8.	Open
	10. Cross-train MCC financial staff on the financial statements preparation process to ensure that there is more than one person knowledgeable and can prepare the financial statements.	Open but will be reported as management letter comment in FY 2013.
2. Significant Deficiency: Validation Control over Grant Accrual Estimates Needs to be Strengthened	11. Perform a grant accrual look back analysis on a quarterly basis for a sufficient period of time to develop a pattern or trend.	Open
	12. Update the Expense Accruals Policy and Procedures.	Open
	13. Continue to enhance the accrual methodology.	Open
	14. Develop audit procedures for the MCA audit to compare authority request amount against actual expenses.	Open
3. Significant Deficiency: Monitoring Control over Funds Provided to MCAs Needs	15. MCC management collaborates with USAID to clarify and document management roles, responsibilities, and performance standards and the USAID OIG oversight roles with regards to MCA audits.	Closed

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Improvement *A. Audit Reports*		
	16. Evaluate resources, capability, and ability to monitor and review the quality and performance of the audits and the audit firms to track and conduct follow-up of corrective action plans with the MCAs in a timely manner.	Closed
B. Final Quarterly Financial Report (QFR)	17. Utilize the QFRs and monthly reconciliations as monitoring tools over the MCA's financial reporting process and MCC's validation of its financial records.	Closed
	18. Ensure the MCA reconciliations are provided to MCC and reviewed to investigate material variances and make corrections, if any.	Closed
	19. Require the MCA audit firms to test the design and effectiveness of the MCA's internal control over the QFRs and the monthly reconciliation, and to test the accuracy of the balances and reconciliation.	Open but will be reported as management letter comment in FY 2013.
	20. Develop and implement reconciliation procedures to complete the reconciliation between the MCA's final QFR and MCC's records.	Closed
	21. Timely assess the MCA's need for the remaining compact funds so that could be de-obligated within the timeline in the policy and procedures after the contract expires.	Closed
	22. Develop and implement a financial management policy that separates the programmatic close-out process from the financial close-out process. This policy should clearly lay out the expected timing for de-obligation.	Closed
4. Significant Deficiency: Information Systems Controls Need Improvement	23. We did not include recommendations in our audit report. Our recommendations were included in a separate USAID OIG Report titled "Audit of Millennium Challenge Corporation's Fiscal Year 2012 Compliance with Federal Information Security	Status of the findings and recommendations were reported separately in USAID OIG Report titled "Audit of Millennium Challenge Corporation's

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	Management Act of 20012," Audit Report M-000-13-001-P, dated November 6, 2012.	Fiscal Year 2013 Compliance with Federal Information Security Management Act of 2002," Audit Report M-000-13-005-P, dated September 20, 2013.

EXHIBIT 4

MANAGEMENT'S RESPONSE TO FINDINGS

MILLENNIUM
CHALLENGE CORPORATION
UNITED STATES OF AMERICA

December 11, 2013

Mia Leswing, CAP, CISA, CGFM, Partner
CliftonLarsonAllen, LLP
4250 N. Fairfax Drive
Suite 1020
Arlington, VA 22203

Robert Fry
Acting Deputy Assistant Inspector General/Audit
Millennium Challenge Corporation
1401 H Street, NW, Suite 770
Washington DC 20005

Dear Ms. Leswing and Mr. Fry:

In response to the audit findings and recommendations provided in your financial statement audit report MCC has the following comments:

Material Weakness: Ineffective and Inefficient Integration of Data, Processes, and Controls within the Financial Management Systems (Modified Repeat Finding)

Recommendations from the auditors regarding the core financial system:

1. Perform a comprehensive review and determine whether the SSP's financial management system is meeting MCC financial management and reporting needs. As part of this review, management should continue to evaluate whether:

2. Investigate and correct the underlying causes for the system errors and limitations that prevent or delay the recording, processing, and summarizing of accounting transactions. Key issues that remain unresolved should be escalated immediately rather than back-log the problem. MCC should ensure that errors and open tickets are resolved appropriately and timely by the SSP and that routine MCA accounting activities (such as the NA/NA fund transactions) are recorded in Oracle within the specified timeline. Moreover, manual adjusting journal entries should be used for limited transactions like unusual one-time entries or correcting entries. (Modified repeat recommendation)

    a. a separate grants management system that focuses on program and financial administrations that interfaces with the core financial system is needed, or
    b. to establish alternatives to recording numerous data lines in the Oracle AP module which is manual intensive and prone to errors. (Modified repeat recommendation)

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3. In collaboration with the SSP, formalize in writing the system's issues and resolution process. This will include developing a standardized remedy ticket listing with relevant and historical information. (New recommendation)

4. Continue to streamline the Monthly Commitments and Disbursements Report recording and adjustment process.

Recommendations from the auditors regarding supervisory reviews:

5. Implement an effective management review of its accounting and financial reporting processes using the comprehensive review process to ensure that all transactions for the accounting period are accurately and completely reflected in the financial statements, beginning balances agreed to ending balances, and reconciling items are recorded timely. Such management reviews should be performed monthly or quarterly and at year-end timely. (Modified repeat recommendation)

6. Further review SSP data entries relating to MCA payment processing and related adjustments. Perform reconciliation of AP on a monthly basis and proactively resolve all differences. (New recommendation)

Response from MCC:
MCC concurs with recommendation 1 - 6.

Significant Deficiency: Validation Control over Grant Accrual Estimates Needs to be Strengthened (Modified Repeat Finding)

Recommendations from the auditors:

7. Develop and implement a logical and supportable look back validation process to assess the reasonableness of the grant accrual estimate, and then perform a grant accrual look back analysis on a quarterly basis for a sufficient period of time to develop a pattern or trend. The look back analysis and the results should provide MCC sufficient information to explain unusual variances between actual and estimates, or support updating the current grant accrual methodology. Such periodic assessment of the adequacy of the grant accrual methodology should be documented and supported by data analysis. Note that the accrued liability amount is subject to the risks that actual subsequent disbursement amount may be significantly different from management's estimate. When this occurs, management should further analyze the drivers/factors to ensure the validity and reasonableness of the estimation methodology. (Modified repeat recommendation)

8. Update the Expense Accruals Policy and Procedures to reflect the change in the methodology. At a minimum, the policy and procedures should include the following: (Modified repeat recommendation

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a. documentation of the procedures and flow of information used in developing grant accrual estimates;
b. a discussion of who (position title) is responsible for each step of the estimate as well as the review and approval process followed;
c. the model used, the rationale for selecting the specific methodology, and, for programs with sufficient historical data, the degree of calibration within the projected spending model; and
d. the sources of information, the logic flow, and the mechanics of the model, including the formulas and other mathematical functions.

9. Develop audit procedures for the MCA audit to compare spending authority amount granted against actual MCA expenses, and investigate and document significant variances. MCC should maintain a library of historical MCA financial data. This information may be by MCC to validate or enhance its current methodology.

10. Continue to enhance the accrual methodology by:
   a. stratifying the MCAs based on variances in their spending rates and/or stages in the compact's life cycle;
   b. developing and implementing a process to ensure that compacts that are partially managed by MCC are fully addressed within the grant accrual process.
   c. addressing situations where the MCA exceeds its quarterly spending authority;
   d. addressing situations where the compact has expired and there is no spending authority and disbursements are still occurring;
   e. obtaining detailed document level breakdown of expenses to be used to compare against the accrual estimates;
   f. reviewing the disbursement patterns by compact to identify those with large fluctuations to determine the cause so that adjustments can be made in developing the spending plan or in how the grant accrual is calculated to improve the accuracy of the grant accrual estimate.; and
   g. other factors as deemed necessary to achieve an acceptable precision of the accrual estimate.

Response from MCC:
MCC concurs with recommendation 7 - 10.

Significant Deficiency: Monitoring of MCAs Audits Needs to be Strengthened (Modified Repeat Finding)

Recommendation from the auditors:

11. Continue the collaboration between the USAID OIG and the MCC management to improve timeliness of the MCA audits; adequacy of the MCA audit procedures; monitoring and reviewing the quality and performance of the MCA audits; and tracking and conducting follow-up of corrective action plans with the MCAs timely.

Response from MCC:

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MCC concurs with recommendation 11.

Significant Deficiency: Information Systems Controls Need Improvement (Modified Repeat Finding)

Recommendation from the auditors:

12. Repeat recommendations from the FISMA Report.

Response from MCC:
MCC concurs with recommendations from the FISMA Report.

Sincerely,

Chantale Yokmin Wong
Vice President, Administration and Finance and
Chief Financial Officer

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U.S. Agency for International Development
Office of Inspector General
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Other Information

Management Challenges Identified by the Inspector General

Office of Inspector General

NOV 26 2013

Mr. Daniel W. Yohannes
Chief Executive Officer
Millennium Challenge Corporation
875 15th Street, NW
Washington, DC 20005

Dear Mr. Yohannes:

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). Our decisions on which challenges to report were based primarily on audits and analyses performed on 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 2013 agency financial report.

We have discussed the management and performance challenges summarized in this statement with responsible MCC officials. If you have any questions or wish to discuss the statement further, please contact me or Tim Cox, Acting Deputy Inspector General, at 202-712-1150.

Sincerely,

Michael Carroll
Acting Inspector General

Enclosure: a/s

U.S. Agency for International Development
1300 Pennsylvania Avenue, NW
Washington, DC 20523
http://oig.usaid.gov

STATEMENT BY THE OFFICE OF INSPECTOR GENERAL ON THE MILLENNIUM CHALLENGE CORPORATION'S MOST SERIOUS MANAGEMENT AND PERFORMANCE CHALLENGES

Fiscal Year 2013

MCC faces its most serious management challenges for achieving its goals in three areas: managing for results, financial management, and information technology management.

MANAGING FOR RESULTS

MCC provides foreign aid to countries that meet its policy performance indicators of ruling justly, investing in people, and encouraging economic freedom. To date, 25 countries have met these requirements and been awarded more than $9 billion through compact agreements used to reduce poverty and increase economic growth through programs in agriculture, roads, education, health, and tourism. During fiscal year (FY) 2013, MCC had 16 active compacts in its portfolio: Burkina Faso, Cape Verde, Georgia, Indonesia, Jordan, Lesotho, Malawi, Moldova, Mongolia, Morocco, Mozambique, Namibia, Philippines, Senegal, Tanzania, and Zambia, which together were awarded more than $6 billion for projects. MCC faces challenges in ensuring that these compacts achieve planned results. These challenges occur in the context of compact development, compact implementation, and project sustainability.

Compact Development

It takes MCC and a partner country about 2 years to complete the compact development process. During that time, they conduct analyses; define, develop, and appraise a project; negotiate and sign a compact; and prepare for the compact's entry into force. Upon entry into force, the fixed 5-year implementation period starts.

A recent review and audit both noted the need for improvements in compact development. In its review of MCC's compact modifications, OIG reported that MCC significantly modified project activities in 9 of the 23 compacts in place at that time.[1] OIG specifically reported incomplete planning in 6 of the compacts, which were significantly modified because MCC underestimated construction quantities and unit costs during planning. As a result, costs increased during compact implementation, and the compacts had to be modified to reduce the project scope.[2] Meanwhile, OIG's audit of MCC's funding of activities in Mongolia determined that MCC had to revise goals for the number of new property rights registrants downward by 29 percent after it discovered that the data it relied on during planning was not accurate.[3]

[1] OIG defined significant modifications as a cumulative change in project costs of at least $10 million, or a 25 percent change in either the estimated economic rate of return or estimated number of beneficiaries.
[2] "Review of the Millennium Challenge Corporation's Compact Modifications," Report No. M-000-12-006-S, July 20, 2012.
[3] "Audit of the Millennium Challenge Corporation's Funding of Activities in Mongolia," Report No. M-000-12-001-P, March 22, 2012.

1

Compact Implementation

MCC and the partner country complete compact implementation through a Millennium Challenge Account (MCA) over the 5-year compact term. The MCA is staffed by a team of management, procurement, finance, monitoring and evaluation, and legal professionals, as well as specialists for the specific sectors in the compact, such as infrastructure and agriculture. The MCA procures contractors' services to carry out the compact's projects.

Three recent audits and reviews have noted the need for improvement in compact implementation in the areas of completing timely feasibility studies and designs, managing contractor performance, and resettling people affected by projects.

- OIG reported that the project activities in Mozambique might not achieve their revised goals because contractors were late in providing studies, designs, and cost estimates needed to procure construction contractors. In addition, some construction contractors were not meeting their deadlines and were not properly using advance payments for mobilization.[4]

- OIG reported that MCC significantly modified 30 percent of its compacts because of implementation challenges, and those compacts did not or will not achieve planned results as initially envisioned as a result. In several cases, these implementation challenges arose from poor project management or oversight.[5]

- Many projects that MCC funds involve resettlement (i.e., moving people or acquiring their property). MCC requires MCAs to implement resettlement activities and provide appropriate compensation to people who lose land, assets, or access to resources due to an MCC-funded project. In this audit, OIG found problems with resettlement activities in an MCC-funded road construction project in Ghana. OIG identified concerns with MCC's assessment of livelihood restoration, timely compensation to people affected by the project, and shortcomings with documentation on resettlement payments. In El Salvador, the second country OIG visited, people affected by resettlement were generally satisfied with the process and their compensation.[6]

Sustainability

To make sure project benefits can be sustained over time, MCC requires that sustainability considerations be accounted for within compacts. Sustainability can take a number of forms, such as requiring a partner country to increase its contributions to a road maintenance fund so

[4] "Audit of the Millennium Challenge Corporation's Programs in Mozambique," Report No. M-000-13-003-P, January 31, 2013.
[5] "Review of the Millennium Challenge Corporation's Compact Modifications," Report No. M-000-12-006-S, July 20, 2012.
[6] "Audit of the Millennium Challenge Corporation's Resettlement Activities," Report No. M-000-13-002-P, December 6, 2012."

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when a completed MCC-funded road is turned over to the country, adequate funding is available for its care. OIG audits and reviews consider the sustainability of MCC-funded projects and examine whether adequate provisions are in place. Two recent reports show that MCC's efforts to ensure sustainability could be improved.

- The sustainability of an MCC-funded fruit tree productivity project in Morocco was at risk because olive trees may receive less maintenance than outlined in the project's design. Maintenance activities were to be performed over a 2-year contract period to help the trees become viable. However, development of the technical planting details took longer than anticipated, which then delayed planting and reduced the amount of time contractors had for maintenance. In addition, the audit questioned farmers' ability to maintain the trees following the 2-year period in which maintenance was to be provided.[7]

- Funds made available by the Senegalese Government were inadequate to provide annual maintenance for an MCC-funded roads project. Similarly, the long-term sustainability of MCC-funded irrigation works was also at risk due to inadequate maintenance services and funding. OIG reported that MCC is taking action to ensure that adequate funding is available to maintain the investments in roads and irrigation.[8]

FINANCIAL MANAGEMENT

Financial management is critical to developing reliable financial information and to ensuring that operations are effective and efficient, including the use of an entity's resources. Significant MCC activities, liabilities, and expenses occur in compact programs implemented by various MCAs across the globe.

While MCC received an unqualified opinion on its FY 2012 financial statements, the audit report reported on one material weakness and three significant deficiencies in internal control. Two issues in particular indicate ongoing challenges to MCC's ability to prepare complete, reliable financial statements.

- MCC's financial management system follows the guidance prescribed by the Federal Accounting Standards Board, whereas the independent MCAs established by recipient countries do not. MCC addresses this challenge by adjusting its grant liabilities at the MCC level, in order to bring the cash basis reporting by MCAs to MCC's accrual basis. Last year, MCC revised its accrual methodology, and it currently uses disbursement history, unused spending authority, and invoices received but not paid to estimate accruals. However, MCC continues to have challenges with accumulating adequate relevant historical data to accurately estimate accruals. Further, MCC's new accrual validation process has not been fully

[7] "Audit of the Millennium Challenge Corporation-Funded Fruit Tree Productivity Project in Morocco," Report No. M-000-12-005-P, June 15, 2012.

[8] "Audit of the Millennium Challenge Corporation-Funded Program in Senegal," Report No. M-000-13-001-S, March 18, 2013.

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implemented. The auditors will continue to examine accrual estimation methodology during the current financial statement audit.

- MCC's accounting department continues to rely on some manual financial reporting processes. This continues to be a control deficiency because manual processes are more vulnerable to human error.

INFORMATION TECHNOLOGY MANAGEMENT

Since FY 2008, OIG has reported information technology (IT) management challenges that affect MCC. For FY 2013, OIG continues to consider MCC's Privacy and IT Governance Programs to be serious management challenges. In addition, OIG considers IT security to be a new challenge going into FY 2014.

Privacy Program

During FY 2012, OIG followed up on MCC's implementation of selected recommendations in a July 2010 audit report on MCC's Privacy Program.[9] The follow-up audit concluded that five recommendations had not been implemented fully and identified a number of new weaknesses. Therefore, OIG made 24 recommendations to strengthen the program.[10]

By the end of FY 2013, MCC completed final action on 20 of the 24 recommendations. Three of the four outstanding recommendations address training, which is an important component of a privacy program. Therefore, OIG continues to consider the shortcomings within MCC's Privacy Program as a management challenge. MCC plans to take final action on the training-related recommendations by November 2013.

IT Governance

In January 2011, OIG reported that weaknesses in MCC's IT governance process led MCC to spend more than $6.9 million for a system that only partially met its needs.[11] Six months later, in June 2011, an OIG contracted audit reported that similar weaknesses may (1) increase IT project costs, (2) lengthen deployment, and (3) deliver solutions that do not satisfy business needs.[12]

OIG made 32 recommendations in two reports to help MCC achieve an appropriate level of IT governance and control. In response, MCC developed a 17-month plan to improve IT

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[9] "Audit of the Millennium Challenge Corporation's Implementation of Key Components of a Privacy Program for its Information Technology Systems," Report No. M-000-10-003-P, July 9, 2010.
[10] "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.
[11] "Audit of the Millennium Challenge Corporation's Implementation of Selected Key Project Controls for the MCC Integrated Data Analysis System," Report No. M-000-11-002-P, January 31, 2011.
[12] "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.

management, with the final phase to be completed by December 2012. However, MCC requested an extension until February 2014 in completing final action on two significant recommendations that address the management of information used for making decisions.

IT Security

In an FY 2013 report, an OIG contracted audit found that while MCC generally had policies for its IT security program, implementation was not effective enough to preserve the integrity of MCC's information systems.[13] The lack of implementation potentially exposes MCC to unauthorized access, use, disclosure, disruption, modification, or destruction. Consequently, the audit identified numerous areas in MCC's IT security program that can be improved and made 14 recommendations.

OIG considers IT security to be a new challenge because of the number of IT security weaknesses this year, taken together with the nine recommendations from past years that have not been implemented.

[13] "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.

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Management's Response to the Inspector General's Assessment of Challenges Facing MCC

TO: Tim Cox
Acting Deputy Inspector General

FROM: Chantale Y. Wong / s /
Vice President, Department of Administration and Finance and Chief Financial Officer

DATE: December 11, 2013

SUBJECT: Management's Response to Statement by the Office of Inspector General (OIG) on MCC's Most Serious Management and Performance Challenges Fiscal Year 2013

In its *FY 2013 Statement of MCC's Most Serious Management and Performance Challenges,* the OIG identified three areas of concern:

1. Managing for Results, specifically compact development, compact implementation and sustainability
2. Financial Management
3. Information Management Technology

MCC concurs that these broad areas cited are challenges for our organization. Because the majority of the audits and reviews that the OIG relies on for its FY 2013 statement were completed in FY 2012 or earlier, MCC has either taken or is in the process of taking aggressive action to improve our performance. We appreciate that the OIG recognized our efforts to date, and we welcome your continued involvement as we improve and enhance our ability to perform MCC's mission effectively.

Specific comments on the three areas of concern are as follows:

Managing for Results

Compact Development

The Office of Inspector General (OIG) cites incomplete planning as one reason for major compact modifications. MCC recognizes the need for thorough due diligence of projects and proper planning. We also recognize that that planning is an ongoing process and modifications may be necessary even in the best-planned project. As the OIG acknowledged in the *Review of the Millennium Challenge Corporation's Compact Modifications,* MCC has taken concrete steps to ensure that staff are following best practices to reduce the number of major compact modifications. For example, in January 2012 MCC released new Compact Development Guidelines to emphasize up-front project preparation and diligence.

MCC recognizes the importance of addressing the management challenges outlined in these audit reports. MCC works to prevent major program modifications through rigorous project preparation and close supervision of program oversight. Implementation challenges of the kinds reported in the audit reports are common given the complexity of large projects, whether in the United States or overseas. As mentioned above, MCC is working to reduce the risks those challenges present. Overall, MCC works to prevent major program modifications through rigorous project preparation and close supervision of program oversight.

Compact Implementation

The management of contractors during project implementation is a significant challenge in any context. The accountable entities of partner country governments continue to make improvements in tackling this universal challenge. For instance, in response to some of the conditions noted in the OIG's report on programs in Mozambique, MCC worked with accountable entity staff to ensure that contractor performance oversight plans were developed and implemented.

Resettlement issues raised in the *Audit of the Millennium Challenge Corporation's Resettlement Activities* include recommendations that have helped support MCC's ongoing efforts to integrate internationally-accepted standards of environmental and social sustainability into the design and implementation of compacts. These efforts have included a comprehensive review of resettlement activities in MCC's portfolio, steps to improve knowledge sharing and the formal adoption of the International Finance Corporation's (IFC) Performance Standards on Environmental and Social Sustainability as part of a June 2012 revision of MCC's Environmental Guidelines. In the coming months, MCC will also issue updated guidance on resettlement and applying the IFC's Performance Standard on Land Acquisition and Involuntary Resettlement (IFC PS-5) throughout the MCC project lifecycle.

In the *Review of the Millennium Challenge Corporation's Compact Modifications,* the OIG stated, "… implementation challenges occurred when costs increased unexpectedly, the host government did not implement policy reforms that were critical to the success of a project, or contractors performed poorly." The statement provides the basis for the OIG's *FY 2013 Statement of MCC's Most Serious Management and Performance Challenges.* The OIG references this review and states that, "in several cases, these implementation challenges arose from poor project management and oversight." However, the "Implementation Challenges" section of the review cited by the FY 2013 statement includes only one claim, not several, where modifications were the result of poor management and oversight. Much more often MCC took action in response to the implementation challenges cited by the review, including unforeseen cost increases, lack of progress on key policy reforms or poor contractor performance.

Overall, the program modifications during implementation identified by the OIG demonstrate that MCC has been willing to make tough decisions and terminate funding for projects where increasing risks outweigh the potential benefit of proceeding as originally planned. When program modifications are necessary due to unforeseen market or other factors, MCC has a systematic approach for weighing risks and benefits of alternative courses of action to ensure that taxpayer resources are prudently managed. Given MCC's strict five-year implementation timeline and fixed funding levels for compact agreements, cost overruns resulting from changes in market conditions will inevitably lead to project modifications. In such situations, ensuring that scarce taxpayer resources are directed to activities with the greatest potential for impact demonstrates good management.

Sustainability

Sustainability is a key component of every MCC compact partnership. To accrue full and lasting benefits, MCC's investments cannot operate in static social and economic environments. As a principle of our approach to foreign assistance, MCC and its partner countries look closely at the environment in which MCC investments are made and plan reforms to policies that might limit the investment's impact and sustainability.

A key element of sustainability in infrastructure programs is ensuring that partner countries have adequate operations and maintenance funding planned in the years after project completion. As the OIG's report on programs in Senegal acknowledges, MCC and the Government of Senegal are taking the necessary action to ensure that sufficient road and irrigation project funding is set aside.

Financial Management

We note the OIG's acknowledgment that MCC continues to improve its financial management reporting capabilities in FY 2013. We have fully implemented a new grant accrual estimation process including validation processes to ensure the accuracy of the grant accrual. MCC has also made significant progress implementing a methodology for estimating advances to MCA grantees. These new estimation methodologies have been implemented while ensuring financial statements are presented in accordance with Generally Accepted Accounting Principles (GAAP).

In addition, MCC no longer relies solely on a manual financial reporting process. In FY 2013, MCC investigated alternative approaches for the compilation of the financial statements. MCC was successful in leveraging the Oracle Federal Financial (OFF) system out-of-the-box financial statement functionality. MCC is now producing financial statements out of OFF and is currently undergoing validation of these financial statements for full implementation and reliance in FY 2014. The addition of accounting staff at MCC has also enabled MCC to complete more thorough analysis and has enabled MCC management to perform increased, detailed reviews over the financial reporting process. Additionally, MCC has implemented several process improvements, including the addition of many internal controls over financial reporting. The implementation of additional internal controls has increased assurance that MCC is a good steward of funds and has increased transparency over financial reporting and the use of funds in achieving MCC's overall mission.

Information Technology Management

Privacy Program

During FY 2013, we strengthened our privacy program by implementing a revised MCC Privacy Policy and updated privacy training. Among many improvements, the Privacy Policy implemented a rigorous incident response program that encompassed MCC management decisions and proved effective during FY 2013. During FY 2013 and the first quarter of FY 2014, MCC closed the remaining five OIG recommendations that affected MCC's privacy program. In particular, MCC expanded the new hire and annual refresher training programs to include topics on applicable privacy laws; regulations and policies; restrictions on data collection; storage of personally identifiable information (PII); proper disposal and retention of PII; sanctions for misuse of PII; and rules governing the use of PII during telework or remote access. MCC's Director of Web Services also worked with accountable entities to revise the language of the disclaimers posted on primary websites to be consistent with the language of the accountable entities' websites. Having made significant improvements, MCC's senior assessment board determined that MCC's privacy program with respect to information technology systems is not a reportable condition pursuant to the Federal Managers' Financial Integrity Act of 1982.

IT Governance

MCC has hired a contracting firm that will remedy the final two OIG audit recommendations for IT governance. Specifically, the contractors are performing the work necessary to complete the enterprise information architecture planning and implementation project and to develop a plan that leverages data as indicated in the authoritative data source process and methodology.

IT Security

During the latter part of FY 2013 and the first quarter of FY 2014, MCC closed eight of the nine remaining FY 2012 audit recommendations. MCC expects to close the last remaining recommendation during the first quarter of FY 2014. In addition, MCC is on schedule to implement the 15 FY 2013 audit recommendations by August 2014.

Summaries of Financial Statement Audit and Management Assurances

Table 1. Summary of Financial Statement Audit

Audit Opinion	Unmodified Opinion
Restatement	No

Material Weaknesses	Beginning Balance	New	Resolved	Consolidated	Ending Balance
Ineffective and Inefficient Integration of Data, Processes, and Controls within the Financial Management Systems	1				1
Total Material Weaknesses	**1**				**1**

Table 2. Summary of Management Assurances

Effectiveness of Internal Control over Financial Reporting (FMFIA Section 2)

Statement of Assurance	Qualified

Material Weaknesses	Beginning Balance	New	Resolved	Consolidated	Reassessed	Ending Balance
Ineffective and Inefficient Integration of Data, Processes, and Controls within the Financial Management Systems	1					1
Total Material Weaknesses	**1**					**1**

Effectiveness of Internal Control over Operations (FMFIA Section 2)

Statement of Assurance	Unqualified

Material Weaknesses	Beginning Balance	New	Resolved	Consolidated	Reassessed	Ending Balance
None Cited	0					0
Total Material Weaknesses	**0**					**0**

Conformance with Financial Management System Requirements (FMFIA Section 4)

Statement of Assurance	System Conforms

Material Weaknesses	Beginning Balance	New	Resolved	Consolidated	Reassessed	Ending Balance
None Cited	0					0
Total Material Weaknesses	**0**					**0**

Improper Payments Information Act Report

The Improper Payments Information Act of 2002, as amended by the Improper Payments Elimination and Recovery Act of 2010, requires Federal agencies to annually report information on improper payments to the President and Congress through their Agency Financial Reports (or Performance and Accountability Reports). OMB Circular No. A-123, *Management's Responsibility for Internal Control,* Appendix C, "Requirements for Effective Measurement and Remediation of Improper Payments," Part I, defines an improper payment as any payment that should not have been made or that was made in an incorrect amount under statutory, contractual, administrative or other legally applicable requirements. Incorrect amounts are overpayments or underpayments made to eligible recipients (including inappropriate denials of payment or service, any payment that does not account for credits or applicable discounts, payments that are for the incorrect amount and duplicate payments). An improper payment also includes any payment that was made to an ineligible recipient or for an ineligible good or service, or payments for goods or services not received (except for such payments authorized by law). In addition, when an agency's review is unable to discern whether a payment was proper because of insufficient or lack of documentation, the agency must consider this payment as improper.

Risk Assessment

MCC conducted a risk assessment for each of its seven[1] funds. The assessment incorporated various risk factors as identified in OMB Circular No. A-123, Appendix C. Based upon the risk assessment, four funds, Compacts, 609(g), Administrative and Due Diligence, were considered to have a higher risk of improper payments due to the high volume of transactions and higher dollar amounts of disbursements. MCC conducted statistical sampling of these funds and determined an improper payment rate.

Statistical Sampling

The objective of sampling was to:

- Select a statistically valid random sample of sufficient size for each fund to support an estimate with a 90 percent confidence interval of +/– 2.5 percent around the estimate of the percentage of improper payments.
- Select a representative sample for each fund to reach a conclusion on the error rate by projecting the results of the sample to the population and calculating the estimated amount of improper payments made in those funds (gross total of both over and under payments (i.e., not the net of over and under payments)).

[1] *See page 22 for a description of each fund.*

> The sample size was determined using the sample size formula provided in OMB Circular No. A-123, Appendix C. MCC based the estimated percentage of erroneous payments on the improper payment error rate for FY 2012 determined from MCC's Financial Payment Data Report. Known rates are a good indicator of future rates, especially in cases where rates are currently low. To increase conservatism and coverage, MCC added one percent to the improper payment rate. This resulted in an increased sample size and allowed for greater assurance of the improper payment rate reported.

Using the sample size formula (adjusted to increase conservatism and coverage), MCC calculated that it needed a minimum of 45 samples to test during the FY 2013 Improper Payments Information Act reporting period. This sample size met the precision requirements specified in OMB Circular No. A-123, Appendix C. To obtain an even number of transactions to be tested, MCC increased the total minimum sample size to 48 transactions, or 12 samples for each of the four funds considered high risk.

MCC selected samples randomly from all accounting lines that composed the populations, with the exception of payroll and intra-governmental payment and collection (IPAC) transactions, so that each item had an opportunity for selection. MCC excluded transactions under $25,000 to focus emphasis on more material transactions and overpayments. Transactions under $25,000 did not have a significant impact on improper payment reporting thresholds.

Improper Payment Reporting

The risk assessment results did not identify any funds that met the OMB threshold of significant erroneous payments.[2] Although MCC did not meet the OMB threshold, MCC tested four of its funds to determine if it could identify any significant improper payments.

MCC did not identify any improper payments from the sample of disbursements tested. However, MCC self-identified and reported two improper payments in the total amount of $5,292,315 due to data entry errors; the errors were corrected and the funds were subsequently collected. MCC considered the errors an isolated incident and implemented corrective actions to prevent future occurrences.

MCC determined its programs were not susceptible to significant erroneous payments, so it did not include payment recapture audits in the scope of the FY 2013 review.

[2] *Defined by OMB as gross annual improper payments in the program exceeding (1) both 1.5 % of program outlays and $10,000,000 of all program or activity payments made during the fiscal year reported, or (2) $100,000,000 (regardless of the improper payment percentage of total program outlays).*

Corrective Actions

The overall total of $5,294,552 in improper payments (due to data entry errors and unnecessary interest payments) met OMB's category of Administrative and Documentation errors. MCC and IBC, its shared services provider, are improving payment processing and the integrity of the Oracle database management system by implementing the following corrective actions to reduce or eliminate this category of payment errors:

- Requiring an additional certifier for all payments in excess of $500,000 to validate payment requests; and
- Reviewing and processing invoices timely to avoid payment of interest charges (complying with the Prompt Payment Final Rule).

Appendices

Appendix A

Acronyms

Acronym	Definition
AFR	Agency Financial Report
AP	Accounts Payable
APR	Annual Performance Report
ATO	Authorization to Operate
CCAP	Comprehensive Corrective Action Plan
CEO	Chief Executive Officer
CFO	Chief Financial Officer
CSRS	Civil Service Retirement System
DCO	Department of Compact Operations
DHS	Department of Homeland Security
DPE	Department of Policy and Evaluations
DOL	Department of Labor
FASAB	Federal Accounting Standards Advisory Board
FBWT	Fund Balance with Treasury
FECA	Federal Employees' Compensation Act
FERS	Federal Employees' Retirement System
FISMA	Federal Information Management Security Act of 2002
FMFIA	Federal Managers' Financial Integrity Act of 1982
FS	Financial Statement
FTE	Full-time Equivalent
FY	Fiscal Year
GAAP	Generally Accepted Accounting Principles
GL	General Ledger
IBC	Interior Business Center (Department of the Interior)
IFC	International Finance Corporation
IPAC	Intragovernmental Payment and Collection
IT	Information technology
JV	Journal Voucher
MCA	Millennium Challenge Account
MD&A	Management's Discussion and Analysis
MCC	Millennium Challenge Corporation
OIG	Office of Inspector General
MCDR	Monthly Commitments and Disbursement Report
MIDAS	MCC Integrated Data Analysis System
MIS	Management Information System
NA	Not Applicable
NFR	Notice of Findings and Recommendations
NIST	National Institute of Standards and Technology
OFF	Oracle Federal Financial
OIG	Office of Inspector General
OMB	Office of Management and Budget

Acronym	Definition
OPM	Office of Personnel Management
PII	Personally-Identifiable Information
PP&E	Property, Plant, & Equipment
PO	Purchase Order
QRF	Quarterly Financial Report
RSI	Required Supplementary Information
SBR	Statement of Budgetary Resources
SF	Standard Form
SFFAS	Statement of Federal Financial Accounting Standards
SSAE 16	Statement on Standards for Attestation Engagements (No. 16 is Reporting on Controls at a Service Organization)
SSP	Shared Services Provider
STARS	Staff Tracking and Reconciliation System
STEM	Science, Technology, Engineering and Math
TB	Trial Balance
TR	Technical Release (FASAB Document)
TSP	Thrift Savings Plan
UDO	Undelivered Order
UNESCO	United Nations Educational, Scientific and Cultural Organization
UNICEF	United Nations Children's Fund
U.S.	United States
USAID	United States Agency for International Development
U.S.C.	United States Code
USSGL	United States Standard Ledger

Compacts

A compact is a multi-year agreement between MCC and a partner country to fund specific programs designed to reduce poverty and stimulate economic growth. Recognizing that sustainable development is achieved best by fostering country ownership, good policies and investment in people, MCC provides selected eligible countries the opportunity to identify their own priorities for achieving economic growth and poverty reduction.

Every MCC compact reflects its country's specific priorities and details program objectives, implementation methods and monitoring and evaluation strategies, while ensuring financial accountability, transparency and fair and open procurement processes. To date, MCC has signed 27 compacts totaling $9.2 billion. MCC issues Quarterly Status Reports that provide a comprehensive qualitative and quantitative snapshot of a compact project, its commitments and expenditures, and its activities.

Summary of MCC Compacts by Country

Armenia

This compact focused on increasing economic performance in the agricultural sector through strategic investments in rural roads and irrigated agriculture to provide communities and rural residents with reduced transport costs and better access to jobs, markets and social services. It increased productivity of 250,000 farmer households through improved water supply, higher yields, higher-value crops and a more competitive agricultural sector. In June 2009, MCC enacted a hold on funding for further road construction and rehabilitation because of Government of Armenia actions inconsistent with MCC principles promoting democratic governance. Armenia completed this compact in September 2011.

Benin

This compact sought to increase investment and private sector activity in Benin through four projects: (1) increasing access to land through more secure and useful land tenure, (2) expanding access to financial services through grants given to micro, small and medium enterprises, (3) providing access to justice by bringing courts closer to rural populations and (4) improving access to markets by eliminating physical and procedural constraints currently hindering the flow of goods through the Port of Cotonou. Benin completed this compact in September 2011. MCC selected Benin as eligible to develop a proposal for a second compact.

Burkina Faso

This compact is expected to (1) increase investment in rural productivity by improving land tenure security and land management, (2) increase the volume and value of agricultural production through investments in water management and irrigation, technical assistance to farmers and rural credit and (3) increase opportunities for farmers to sell agricultural goods and livestock by rehabilitating

Appendix B

Summaries of FY 2013 Compact and Threshold Programs

rural and primary roads. As an extension of Burkina Faso's successful MCC Threshold Program, the compact also funds the construction of three classrooms each at 132 "girl-friendly" schools for grades four through six.

Cape Verde I and II

The first compact helped Cape Verde achieve its national development goal of transforming its economy from aid-dependency to sustainable, private sector-led growth. The compact increased rural incomes of the poor by increasing agricultural productivity, integrating internal markets, reducing transportation costs and developing the private sector through greater private sector investment and financial sector reform. Cape Verde completed this compact in October 2010; it signed its second compact in February 2012.

The second compact is designed to reduce poverty through economic growth through two projects intended to increase household incomes by reforming two sectors identified as current constraints to economic growth: the water and sanitation sector and the land management sector. This compact builds off the success of the first compact and upholds high standards for accountability, transparency and achieving results.

El Salvador I and II

This compact sought to improve the lives of Salvadorans through strategic investments in education, public services, enterprise development and transportation infrastructure. Its Human Development Project increased employment opportunities for the region's poorest inhabitants and provided greater access to safe water and sanitation services. El Salvador completed this compact in September 2012; MCC approved a second compact with El Salvador in September 2013.

Georgia I and II

The first compact helped Georgians reduce poverty by renovating key regional infrastructure and improving the development of regional enterprises. The compact enhanced productivity in farms, agribusinesses and other enterprises that will increase jobs and rural income; rehabilitated a major highway; and improved energy and water security. Georgia completed this compact in April 2011; it signed its second compact in July 2013.

The second compact seeks to improve the quality of education in the science, technology, engineering and math (STEM) fields and increase the earning potential of Georgians through strategic investments from the start of a student's general education to graduation from technical training and advanced degree programs. The compact includes a focus on increasing women's participation in STEM professions. It builds on the success of Georgia's first compact, which supplemented Georgia's efforts to promote stability, good governance and private enterprise development in the years following the 2004 Rose Revolution.

Ghana

This compact reduced poverty by raising farmer incomes through private sector-led agribusiness development. MCC investments increased the production and productivity of high-value cash and food staple crops in some of Ghana's poorest regions and enhanced the competitiveness of Ghana's agricultural products in regional and international markets. Ghana completed this compact in February 2012; MCC selected Ghana as eligible to develop a proposal for a second compact.

Honduras

This compact sought to reduce poverty by increasing farmer productivity and entrepreneurship, and reducing transportation costs between targeted production centers and national, regional and global markets. In September 2009, MCC partially terminated the compact because of Government of Honduras actions inconsistent with MCC's eligibility criteria. Honduras completed this compact in September 2010.

Indonesia

This compact seeks to increase household incomes through three projects designed to (1) increase productivity, reduce energy costs and improve natural resource management, (2) reduce and prevent low birth weight, childhood stunting and malnourishment of children, and (3) improve provision of public sector growth-enhancing goods and services.

Jordan

This compact funds three integrated projects focused on improving water supply, wastewater collection and wastewater treatment and reuse. These projects are expected to improve water delivery, decrease costs of potable water and upgrade in-home water systems. They are also expected to increase the amount of wastewater collected for treatment and reduce the incidents of sewage overflow. Finally, the compact is expected to increase the volume of treated water that is available as a substitute for freshwater for non-domestic uses.

Lesotho

This compact was designed to have an economy-wide impact, affecting the entire population of Lesotho. It sought to increase water supplies for industrial and domestic use; alleviated the devastating effects of poor maternal health, HIV/AIDS, tuberculosis and other diseases by substantially strengthening the country's health care infrastructure and human resources for health capacity; and removed barriers to foreign and local private-sector investment. Lesotho completed this compact in September 2013.

Madagascar

This compact sought to raise incomes by assisting the rural population transition from subsistence agriculture to a market-driven growth. The compact included three projects to help rural Malagasy secure formal property rights to land; access credit and protect savings; and receive training in agricultural production, management and marketing techniques. In August 2009, MCC terminated this compact because of Government of Madagascar actions inconsistent with MCC's eligibility criteria.

Malawi

This compact is a single-sector program focusing on activities to revitalize Malawi's power sector. By reducing power outages and technical losses, enhancing the sustainability and efficiency of hydropower generation and improving service to electricity consumers, the compact intends to reduce energy costs to enterprises and households; improve productivity in the agriculture, manufacturing and services sectors; and preserve and create employment opportunities in the economy.

Mali

This compact sought to increase the productivity of agriculture and regional enterprises and serve as a catalyst for sustainable economic growth and poverty reduction through key infrastructure investments capitalizing on two of Mali's major assets, the Bamako-Sénou International Airport, a gateway for regional and international trade; and the Niger River, a valuable source for irrigated agriculture. In August 2012, MCC terminated the compact due to an undemocratic change in government.

Moldova

This compact will improve irrigation infrastructure and management; increase the production and marketing of high-value agricultural products; and rehabilitate part of the country's national road network. The highway is a key link for passenger travel and for internal commerce and trade; the repairs will reduce the time and cost to transport goods and services, and will reduce losses to the national economy resulting from deteriorated road conditions.

Mongolia

This compact sought to improve the ability of Mongolians to register and obtain clear titles to their land, expand vocational education in core technical skills and focus on the health and well-being of the labor force by reducing non-communicable diseases and injuries. The compact also promoted alternative energy and energy-efficient products to the market economy and constructed transportation infrastructure along sections of the critical north-south road corridor. Mongolia completed this compact in September 2013.

Morocco

This compact sought to increase productivity and improved employment in high-potential sectors including investments in fruit tree productivity, small-scale fisheries and artisan crafts. Investments in financial services also supported entrepreneurship, small business development and market growth. Morocco completed this compact in September 2013.

Mozambique

This compact sought to increase productive capacity in selected districts by reducing the poverty rate, increasing household income and employment, and reducing chronic malnutrition. Compact programs aimed to improve water systems, sanitation, access to markets, land tenure services and agriculture in the targeted districts. Mozambique completed this compact in September 2013.

Namibia

This compact aims to improve the quality of education and training for underserved populations and will capitalize on Namibia's comparative advantages, including large areas of semi-arid communal land suitable for livestock and diverse wildlife and landscapes ideal for eco-tourism. These projects are designed to increase opportunities in rural areas and increase incomes.

Nicaragua

This compact was designed to reduce transportation costs, improve access to markets, strengthen property rights, increase investment and raise incomes for farms and rural businesses. In July 2009, MCC partially terminated the compact because of political conditions in Nicaragua inconsistent with MCC's eligibility criteria. Nicaragua completed this compact in May 2011.

Philippines

This compact includes funds to repair 220 kilometers of the country's Samar Road. This road will improve access to markets and services for farmers, fishers, and small businesses in some of the poorest provinces in the Philippines. The compact also includes funds to expand community development projects and to computerize and streamline business processes in the Bureau of Internal Revenue to bolster the effectiveness of revenue collection and reduce opportunities for corruption.

Senegal

This compact is designed to reduce poverty and promote economic growth by unlocking the country's agricultural productivity, engaging in infrastructure projects to rehabilitate major national roads and investing in strategic irrigation and water resources management.

Tanzania

This compact sought to rehabilitate roads to connect communities with markets, schools and health clinics, and expanded economic opportunities by reducing transport costs. It improved the reliability and quality of electric power and extended electricity services to communities previously not served. It also funded water infrastructure improvements that will increase access to potable water and mitigate incidences of water-related disease, burdensome health care costs and decreased workforce productivity. Tanzania completed this compact in September 2013. In December 2012, MCC selected Tanzania as eligible to develop a proposal for a second compact.

Vanuatu

This compact improved the country's poor road conditions by constructing and sealing two national roads, the Efate Ring Road and the Santo East Coast Road. The compact benefited poor, rural agricultural producers and the tourism industry by reducing transportation costs and improving road conditions. Vanuatu completed this compact in April 2011.

Zambia

This compact seeks to address one of Zambia's most binding constraints to economic growth through infrastructure investment in Lusaka, the rapidly urbanizing capital. The compact will invest in water supply, sanitation and drainage infrastructure to decrease the incidence and prevalence of water-related disease; reduce productive days lost due to disease and time spent collecting water; and lower costs. It also will support the Government of Zambia's ongoing efforts to reform its water sector by strengthening partner institutions.

Threshold Programs: Improving Capacity, Reducing Corruption

The MCC Threshold Program is a country-driven partnership that aims to assist a country to become eligible for an MCC compact by supporting policy and institutional reforms that target binding constraints to economic growth. MCC develops threshold programs through a rigorous, structured diagnostic process followed by program design and implementation. The country's record implementing a threshold program will provide the MCC Board of Directors with important information about MCC's opportunity to reduce poverty and stimulate growth in that country and the threshold country partner's capacity and commitment to implementing policy and institutional reforms within the context of MCC's evidence-driven model. To date, MCC has signed 24 threshold program agreements with 22 countries.

Summary of MCC Threshold Programs

Albania I and II

The first threshold program focused on reducing corruption by reforming tax administration, public procurement and business administration. It sought to reduce bribes and bureaucracy related to starting a business, and to increase the national tax base. In October 2008, MCC signed a second threshold program with Albania.

The second program built upon the successes of the first and focused on anti-corruption through targeted reforms in the areas of public administration and judicial capacity building. Albania completed both programs.

Burkina Faso

This program focused on increasing the number of girls completing primary education. The program included the construction of "girl-friendly" schools, teacher training, take-home dry rations for girls who maintain a 90 percent school attendance rate, and literacy training center for mothers. Burkina Faso completed its threshold program; it signed an MCC compact in July 2008.

Guyana

This program sought to improve Guyana's fiscal policies and create a more business-friendly environment. The grant helped the Government of Guyana implement a new value-added tax system and develop ways to assist and educate taxpayers, while better planning and controlling spending. The program was designed to reduce the number of days and costs to start a business by modernizing and streamlining the business registration process. Guyana completed its threshold program.

Honduras

This three-year program aims to bring good governance practices to Honduras by improving public financial management and creating more effective and transparent public-private partnerships. It follows the successful implementation of the country's compact, which closed in September 2010. The threshold program will help the Government of Honduras save money in providing public services, improving the delivery of public services and reducing opportunities for corruption.

MCA-Honduras, a Honduran government organization set up under the previous MCC compact but now used by multiple donors, will manage the threshold program. The U.S. Treasury Office of Technical Assistance will implement a portion of the Public Financial Management Project, and MCC will oversee the implementation, monitoring and evaluation of the threshold program.

Indonesia

This program sought to immunize at least 80 percent of children under the age of one for diphtheria, tetanus and pertussis and 90 percent of all children for measles. The program also included a component aimed at curbing public corruption by reforming the judiciary. Indonesia completed its threshold program; it signed an MCC compact in November 2011.

Jordan

This program strengthened democratic institutions by supporting Jordan's efforts to broaden public participation in the political and electoral process, increasing government transparency and accountability and enhancing the efficiency and effectiveness of customs administration. Jordan completed its threshold program; it signed an MCC compact in October 2010.

Kenya

This program focused on reducing opportunities for corruption in public governance. The program targeted corruption in public procurement, the delivery of health care and the monitoring and evaluation of reforms. Kenya completed its threshold program.

Kyrgyz Republic

This program sought to increase the independence and effectiveness of the judicial system, develop a more functional and trusted police force, improve the government's capacity to investigate and prosecute corruption cases, educate the public and media on the dangers of corruption and strengthen the financial disclosure system. The Kyrgyz Republic completed its threshold program.

Liberia

This three-year program is promoting equal access to land and increased land security through better understanding of property rights issues and improved land administration. The program also focuses on improving girls' primary education enrollment and retention, and supports efforts to improve trade policy and practices, specifically in harmonizing tariffs, engaging regional and global bodies, and strengthening the regulatory environment. In December 2012, MCC selected Liberia as eligible to develop a compact.

Malawi

This program focused on combating corruption, enhancing oversight functions and building enforcement and deterrence capacity. The program strived to create more effective legislative and judicial branches of government, provide support for anti-corruption agencies, strengthen independent media coverage and expand the work of civil society organizations. Malawi completed its threshold program; it signed an MCC compact in April 2011.

Moldova

This program sought to reduce corruption in the public sector through reforms to the judicial, health, tax and customs systems. The reforms complemented Moldova's national strategy aimed at reducing corruption. Moldova completed its threshold program; it signed an MCC compact in January 2010.

Niger

This program focused on reducing public corruption within the health and education sectors; streamlining the process of starting a business; reducing the time and costs associated with land ownership transfer, land valuation, building permitting and notarization; and bolstering girls' education. In December 2009, MCC voted to suspend MCC's program with Niger based on Government of Niger actions inconsistent with MCC policies; MCC reinstated assistance under the program in December 2011. In August 2012, USAID began implementation of a $2 million program to complete and extend the activities of Niger's original threshold program. The program, approved by the MCC in March 2012, supports school-based strategies to improve academic performance and to increase girls' enrollment, retention and completion. In December 2012, MCC selected Niger as eligible to develop a compact.

Paraguay I and II

The first Paraguay threshold program focused on reducing corruption. The program sought to strengthen the rule of law by increasing penalties for corruption and building a transparent business environment. Additionally, it included a business development component aimed at reducing the number of days necessary to start a business.

In April 2009, MCC signed a second threshold program with Paraguay that built upon the successes of the first program. It focused on anti-corruption efforts in sectors that are especially prone to corruption and are of economic importance, such as customs, law enforcement, health care and the judiciary. The goal was not only to reduce opportunities for corruption and increase successful prosecution of wrongdoers, but also to improve public understanding and perception of these sectors, and reinforce the Government of Paraguay's commitment to combating corruption. Paraguay completed its second threshold program in July 2012.

Peru

This program sought to increase immunization rates of children in rural areas against diseases like measles, diphtheria, pertussis and tetanus in eight targeted regions, and assist Peru's Ministry of Health in strengthening information and vaccination management systems. The program also helped Peru combat corruption by working with the government and civil society organizations to improve internal controls, as well as analyze and simplify administrative processes to reduce opportunities for corruption. Peru completed its program in September 2012.

Philippines

This program sought to improve revenue administration and anti-corruption efforts by strengthening the Office of the Ombudsman and strengthening enforcement within three departments in the Department of Finance. The Philippines completed its threshold program; it signed an MCC compact in September 2010.

Rwanda

This program focused on strengthening civic participation and promoting civil liberties by providing training, technical support and grants to local and national civil society organizations, and supporting independent community radio stations to enhance citizen engagement. The program also reinforced Rwanda's efforts to support judicial capacity building legislative reforms and to improve overall public administration. Rwanda completed its threshold program.

Saõ Tomé and Principe

This program sought to increase revenue through improved tax administration and enforcement. The program also modernized Saõ Tomé and Principe's customs service to increase efficiency and reduce the time and cost of starting a business. Saõ Tomé and Principe completed this threshold program.

Tanzania

This program focused on four specific anti-corruption initiatives, including building the nongovernmental sectors' monitoring capacity; strengthening the rule of law for good governance; establishing a Financial Intelligence Unit; and curbing corruption in public procurement. Tanzania completed its threshold program; it signed an MCC compact in February 2008.

Timor-Leste

This program seeks to reduce corruption by building a network of functioning and effective anti-corruption institutions and actors strengthening capacity, increasing coordination and improving processes and procedures to deter and detect instances of corruption. The program also aims to improve access to immunization services by creating a more capable and effective community health system.

Uganda

This program focused on reducing corruption by improving public procurement and financial management practices, strengthening the role of civil society and building capacity to facilitate more effective follow-up of reported malpractices. Uganda completed its threshold program.

Ukraine

This program focused on reducing corruption by strengthening civil society's ability to monitor and expose it. The program also enabled the Government of Ukraine to increase monitoring and enforcement of ethical and administrative standards. Ukraine completed its threshold program.

Zambia

This program focused on reducing corruption and improving government effectiveness. The program funded three components aimed at (1) increasing control of corruption within the public sector, (2) improving public service delivery to the private sector and (3) strengthening border management of trade. Zambia completed its threshold program; it signed an MCC compact in May 2012.

Selection Indicators

MCC uses a variety of indicators within the categories of economic freedom, investing in people and ruling justly to determine country eligibility for compact assistance. It looks at several elements in choosing selection indicators, including:

- Development by a third party
- Linkage to policies that the government can influence within a 2–3 year horizon
- Linkage—theoretically or empirically—to economic growth and poverty reduction
- Use of an analytically rigorous methodology and objective and high-quality data
- Broad country coverage and comparability across countries
- Consistency in results from year to year

The table below lists the indicators and sources of information used to determine country eligibility for MCC compact assistance. The indicators are grouped by category.

Selection Indicators

Category	Indicator	Source
Encouraging Economic Freedom	Access to Credit Indicator	International Finance Corporation
	Business Start-Up Indicator	International Finance Corporation
	Fiscal Policy Indicator	International Monetary Fund
	Gender in the Economy Indicator	International Finance Corporation
	Inflation Indicator	International Monetary Fund
	Land Rights and Access Indicator	International Fund for Agricultural Development and International Finance Corporation
	Regulatory Quality Indicator	World Bank/Brookings Institution
	Trade Policy Indicator	The Heritage Foundation
Investing in People	Child Health Indicator	Columbia/Yale
	Girls' Primary Education Completion Rate Indicator (Lower Income Country only)	UNESCO
	Girls' Secondary Education Enrollment Ratio Indicator (Lower Middle Income Country only)	UNESCO
	Health Expenditures Indicator	World Health Organization
	Immunization Rates Indicator	World Health Organization/UNICEF
	Natural Resource Protection	Columbia/Yale
	Primary Education Expenditures Indicator	UNESCO

Appendix C

MCC Country Selection Process

If you are reading a paper copy of this document, you will find the Selection Indicators table at the following MCC website address: http://www.mcc.gov/pages/selection/indicators.

The table on the website is sorted by indicator, category, and source. You can click on individual indicators and sources for additional information.

If you are reading a paper copy of this document, you will find the website addresses for these documents in Appendix D.

Selection Indicators

Category	Indicator	Source
Ruling Justly	Civil Liberties Indicator	Freedom House
	Control of Corruption Indicator	World Bank/Brookings Institution
	Freedom of Information Indicator	Freedom House/Fringe
	Government Effectiveness Indicator	World Bank/Brookings Institution
	Political Rights Indicator	Freedom House
	Rule of Law Indicator	World Bank/Brookings Institution
	Voice and Accountability Indicator	World Bank/Brookings Institution

Use of Supplemental Information

MCC's Board of Directors also may take into account other quantitative and qualitative information. It uses supplemental information to inform its understanding of a country's policy performance relative to its peers, and MCC's ability to reduce poverty and generate economic growth in a country.

There are elements of the eligibility criteria set out in MCC's legislation for which there is either limited quantitative information or no well-developed performance indicator, so MCC may turn to supplemental sources for assessments of these policy issues. In addition, the Board may consider whether there are data gaps or lags in particular indicators that can be addressed by supplemental information.

Examples of the supplemental information used by MCC include the reports listed below.

- The U.S. Department of State's Human Rights Report
- The U.S. Department of State's Trafficking in Persons Report
- Transparency International's Corruption Perceptions Index
- Global Integrity Report
- Freedom House's Countries at the Crossroads
- The World Bank's World Development Indicators
- The World Bank's Doing Business Report
- The World Economic Forum's Global Competitiveness Report

Appendix D

Useful Websites

The following websites contain additional information related to MCC activities. This Appendix includes documents referenced in this report and will help readers who are reading a paper copy of this report locate the links embedded in the electronic version.

http://**www.mcc.gov**

MCC's website, which contains a wide variety of information about MCC's programs and activities.

http://**www.mcc.gov**/pages/about/reports#reports-par

The electronic version of the FY 2012 Agency Financial Report and previous reports, MCC's Annual Reports, and MCC's Congressional Budget Justification, which contain the Annual Performance Reports.

https://**www.mcc.gov**/pages/contact

Contact for comments or questions about the FY 2012 Agency Financial Report

http://**www.mcc.gov**/pages/results/m-and-e#me-by-sector

MCC's monitoring and valuation data by sector report

http://**www.mcc.gov**/documents/reports/reference-2013001142401-fy14-guide-to-the-indicators.pdf

Guide to the MCC Indicators and the Selection Process for Fiscal Year 2014

http://**www.mcc.gov**/pages/selection/indicators

MCC Selection Indicators

http://**www.mcc.gov**/pages/results/evaluations

MCC Independent Impact Evaluations

http://**www.state.gov**/j/drl/rls/hrrpt/index.htm

The U.S. Department of State's Human Rights Report

http://**www.state.gov**/j/tip/rls/tiprpt/index.htm

The U.S. Department of State's Trafficking in Persons Report

http://**www.transparency.org**/research/cpi/overview

Transparency International's Corruption Perceptions Index

http://**data.worldbank.org**/indicator

Global Integrity Report

http://**www.freedomhouse.org**/report/countries-crossroads/countries-crossroads-2012

Freedom House's Countries at the Crossroads

http://**data.worldbank.org**/indicator

The World Bank's World Development Indicators

http://**www.doingbusiness.org**

The World Bank's Doing Business Report

http://**www.transparency.org**/research/cpi/overview

The World Economic Forum's Global Competitiveness Report

http://**www.fasab.gov**

The Federal Accounting Standards Advisory Board website. The MCC prepares its financial statements in accordance with generally accepted accounting principles promulgated by FASAB.

http://**www.whitehouse.gov**/omb/financial_offm_circulars/

OMB's website, which contains Circulars No. A-123 and A-136 that MCC follows to prepare its FMFIA and financial reporting.

Reducing Poverty Through Growth

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