

OBJECTIVES AND GENERAL TERMS OF REFERENCE
AUDIT OF MCC RESOURCES
MANAGED BY MCA- [insert Country]

I. BACKGROUND

[Insert relevant Country background text here]

II. TITLE

Audits of the Fund Accountability Statements¹ of MCC resources managed by MCA-[insert Country] under the Compact, pre-Compact and/or supplemental agreement between the MCC and the MCA-[insert Country] will cover the Base Audit Period [insert date] to [insert date] and the six month Option Audit Periods ended [insert date], [insert date] and [insert date] (included under each of three (3) six-month Option Periods).

III. OBJECTIVES

The objective of this engagement is to conduct financial audits of the MCC resources managed by MCA-[insert Country] under the Compact, pre-Compact and/or supplemental agreement between the Millennium Challenge Corporation, representing the U.S. Government, and the Government of [insert Country] from [insert date] to [insert date], [insert date] to [insert date] and [insert date] to [insert date] in accordance with U.S. Government Auditing Standards issued by the Comptroller General of the United States and the “Millennium Challenge Corporation Guidelines for Financial Audits Contracted by Foreign Recipients” (*MCC Audit Guidelines*) issued by the MCC Inspector General (IG).

The fund accountability statement is the basic financial statement to be audited that presents MCA-[insert Country]’s revenues, costs incurred, cash balance of MCC-provided funds, and assets and technical assistance directly procured by MCC for MCA-[insert Country]’s use. All currency amounts in the fund accountability statement, cost-sharing schedule, schedule of computation of indirect cost rate, and the report findings, if any, must be stated in U.S. dollars. The Auditors must indicate the exchange rate(s) used in the notes to the fund accountability statement.

A. Audit of Funds Provided by MCC

A financial audit of the funds provided by MCC must be performed in accordance with *U.S. Government Auditing Standards* and accordingly include such tests of the accounting records as deemed necessary under the circumstances. The specific objectives of the audit of the MCC-provided funds are to:

- Express an opinion on whether the fund accountability statement for the MCC-funded programs presents fairly, in all material respects, revenues received and costs incurred for the period audited in conformity with the terms of the Compact, pre-Compact and/or supplemental agreement and related ancillary agreements and generally accepted accounting principles or other comprehensive basis of accounting (including the cash receipts and disbursements basis and modifications of the cash basis), including supplemental schedules to reflect accruals for items, such as accounts

¹ A fund accountability statement is the basic financial statement to be audit. It is described in Section III of the statement of work. An example is provided on pages 39-41 of the *MCC Audit Guidelines*.

payable and other related expenses.

- Evaluate and obtain a sufficient understanding of MCA-[insert Country]'s internal controls related to the MCC-funded programs, assess control risk, and identify reportable conditions, including material internal control weaknesses. This evaluation must include the internal controls related to required cost-sharing contributions.
- Perform tests to determine whether MCA-[insert Country] complied, in all material respects, with the Compact, pre-Compact and/or supplemental agreement, and applicable laws and regulations related to MCC-funded programs. All material instances of noncompliance and all illegal acts that have occurred or are likely to have occurred must be identified. Such tests must include the compliance requirements related to required cost-sharing contributions, if applicable. Specifically, the auditor shall perform tests to determine whether MCA-[insert Country] complied, in all material respects, with the Procurement Guidelines and the Fiscal Accountability Plan in effect during the audit period.
- Determine if MCA-[insert Country] has taken adequate corrective action on the prior audit report recommendations of [insert date if applicable].

Auditors must design audit steps and procedures in accordance with U.S. *Government Auditing Standards*, Chapter 4, to provide reasonable assurance of detecting situations or transactions in which fraud or illegal acts have occurred or are likely to have occurred. If such evidence exists, the Auditors must immediately contact the MCC Inspector General and must exercise professional judgment in pursuing indications of possible fraud and illegal acts so as not to interfere with potential future investigations or legal proceedings.

IV. AUDIT SCOPE

The Auditor must use the following steps as the basis for the audit programs and the review. They are not considered all-inclusive or restrictive in nature and do not constitute relief from exercising professional judgment. The steps must be modified to fit local conditions and specific program design, implementation procedures, and agreement provisions which may vary from program to program. Any limitations in the Terms of Reference must be communicated as soon as possible to the MCC Inspector General.

The term of the contract will be for a Base Period of approximately [six] months and three (3) six-month Option Periods. The Client shall determine in its sole discretion whether to exercise an Option Period regardless of the performance of the Auditor; provided that the Client shall obtain the consent of MCC and the MCC Inspector General prior to exercising any Option.

A. Pre-Audit Steps

Following is a list of documents applicable to different MCC-funded programs. The auditor must review the applicable documents considered necessary to perform the audit:

1. The Compact or pre-Compact agreement between MCC and MCA-[insert Country].
2. Supplemental agreements between MCC and the Government of [insert Country], between MCA-[insert Country] and its agents (e.g., Fiscal Agent and Procurement Agent), and plans called for under the Compact, pre-Compact and/or supplemental agreement. Plans and procedures supplementing such plans might include: Governance Agreement, Bank Agreement(s), Disbursement Agreement, Fiscal Agent Agreement, Fiscal Accountability

Plan, Financial Plan, Procurement Agent Agreement, Procurement Plan, Procurement Guidelines, Implementing Entity Agreement(s), M&E Plan, Implementation Plan(s), and Work Plans for the relevant Project or Project Activity, among others.

3. The agreements between MCA-[insert Country] and contractors and grantees, and any other entities implementing Compact funded activities on MCA-[insert Country]'s behalf.²,
4. Implementation letters, and written procedures approved by MCC and/or MCA-[insert Country].
5. The subagreements between MCA-[insert Country] or other implementing entities and their sub-implementing entities, as applicable.
6. All program financial and progress reports; charts of accounts; organizational charts; accounting systems descriptions; procurement policies and procedures; and receipt, warehousing and distribution procedures for materials, as necessary, to successfully complete the required work.

B. Fund Accountability Statement

A "fund accountability statement" is a financial statement that presents, MCA-[insert Country]'s revenues, costs incurred, cash balance of funds (after considering reconciling items), and assets and technical assistance directly procured by MCC. The fund accountability statement must be presented in U.S. dollars and the exchange rate(s) used must be disclosed in a note to the fund accountability statement.

The auditor must examine the fund accountability statement for MCC-funded programs including the budgeted amounts by category and major items; the revenues received from MCC for the period covered by the audit; the costs reported by MCA-[insert Country] as incurred during that period. The fund accountability statement must include all MCC-provided assistance funds identified by each specific program or agreement. The revenues received, less the costs incurred, after considering any reconciling items, must reconcile with the balance of cash on hand and/or in bank accounts. The fund accountability statement must not include cost-sharing contributions provided from MCA-[insert Country]'s in cash or in-kind.

The Auditors may prepare or assist MCA-[insert Country] in the preparation of the fund accountability statement from the books and records maintained by MCA-[insert Country] but MCA-[insert Country] must accept the responsibility for the statement's accuracy before the audit commences.

The opinion on the fund accountability statement must be in accordance with SAS No. 62 (AU623). The fund accountability statement must separately identify those revenues and costs applicable to each specific agreement funded by MCC. The audit must evaluate program implementation actions and accomplishments to determine whether specific costs incurred are allowable, allocable, and reasonable under the agreement terms, and to identify areas where fraud and illegal acts have occurred or are likely to have occurred as a result of inadequate internal control. At a minimum, the Auditors must:

² In a typical MCC Compact with a host country, the Accountable Entity established by the host country to implement the Compact agreement, i.e., MCA-[insert Country], is the direct recipient of MCC funds. In turn, the MCA entity may establish agreements with Covered Providers--either host country or foreign entities receiving MCC-provided funding in excess of a specified dollar threshold, as well as entities receiving less than the specified dollar thresholds--to implement the Compact activities. The MCC Inspector General has developed a separate standard statement of work for non-U.S. Covered Providers to use for financial audits required of them by the host country Accountable Entity.

1. Review direct and indirect costs billed to and reimbursed by MCC and costs incurred but pending reimbursement, identifying and quantifying any questioned costs. *All* costs that are not supported with adequate documentation or are not in accordance with the Compact and related agreement terms must be reported as questioned. Questioned costs that are pending reimbursement must be identified in the notes to the fund accountability statement as not yet reimbursed.

Questioned costs must be presented in the fund accountability statement in two separate categories (a) *ineligible costs* that are explicitly questioned because they are unreasonable; prohibited by the Compact and related agreements or applicable laws and regulations; or not program related; and (b) *unsupported costs* that are not supported with adequate documentation or did not have required prior approvals or authorizations. All questioned costs resulting from instances of noncompliance with the Compact and related agreement terms and applicable laws and regulations must be included as findings in the report on compliance. Also, the notes to the fund accountability statement must briefly describe the questioned costs and must be cross-referenced to the corresponding findings in the report on compliance.

2. Review general and program ledgers to determine whether costs incurred were properly recorded. Reconcile direct costs billed to and reimbursed by MCC to the program and general ledgers.
3. Review the procedures used to control the funds, including their channeling to contracted financial institutions or other implementing entities. Review the bank accounts and the controls on those bank accounts. Perform positive confirmation of balances, as necessary.
4. Determine whether disbursement requests made to MCC and any MCA-[insert Country] advances of funds to sub-implementing entities were justified with documentation, including reconciliations of funds advanced, disbursed, and available. The Auditors must ensure that all funding received by MCA-[insert Country] from MCC was appropriately recorded in MCA-[insert Country]'s accounting records and that those records were periodically reconciled with information provided by MCC.
5. Determine whether program income was added to the funds used to further eligible program objectives, to finance the non-MCC share of the program, or deducted from program costs, in accordance with the terms of the Compact and related agreements.
6. Review procurements to determine whether sound commercial practices including competition were used, reasonable prices were obtained, and adequate controls were in place over the qualities and quantities received. Assess whether the procurements were in accordance with the Procurement Guidelines, approved Procurement Plan, and the Fiscal Accountability Plan.
7. Review direct salary charges to determine whether salary rates are reasonable for that position, in accordance with those approved by MCC, when such approval is required, and supported by appropriate payroll records. Determine if overtime was charged to the program and whether it is allowable under the terms of the Compact and related agreements. Determine whether allowances and fringe benefits received by employees were in accordance with the agreements and applicable laws and regulations. The Auditors must question unallowable salary charges in the fund accountability statement.
8. Review travel and transportation charges to determine whether they are adequately supported and approved. Travel charges that are not supported with adequate documentation or not in

accordance with the Compact and related agreements and regulations must be questioned in the fund accountability statement.

9. Review assets (e.g., supplies, materials, vehicles, equipment, food products, tools, etc.) procured by MCA-[insert Country]. The Auditors must determine whether assets exist or were used for their intended purposes in accordance with the terms of the Compact and related agreements, and whether control procedures exist and have been placed in operation to adequately safeguard the assets. As part of the procedures to determine if assets were used for intended purposes, the Auditors must perform end-use reviews for an appropriate sample of all assets based on the control risk assessment (see section IV.C. of this statement of work). End-use reviews would normally include site visits to verify that assets exist or were used for their intended purposes in accordance with the terms of the Compact and related agreements. When conducting end-use reviews, the Auditors must ensure that assets are marked in accordance with grant or contract requirements. The cost of all assets whose existence or proper use, in accordance with the terms of the Compact and related agreements, cannot be verified must be questioned in the fund accountability statement.
10. Review technical assistance and services. The Auditors must determine whether technical assistance and services were used for their intended purposes in accordance with the terms of the Compact or any pre-Compact and/or related agreements. The cost of technical assistance and services not properly used in accordance with the agreements must be questioned in the fund accountability statement.

In addition to the above audit procedures, if technical assistance and services were contracted by MCA-[insert Country] from a non-U.S. contractor, the Auditors must perform additional audit steps of the technical assistance and services under this statement of work, unless MCA-[insert Country] has separately contracted for an audit of these costs. When testing for compliance with the Compact and related agreement terms and applicable laws and regulations, the Auditors must not only consider the agreements between MCA-[insert Country] and MCC but also the agreements between MCA-[insert Country] and non-U.S. contractors providing technical assistance and services. The agreements between MCA-[insert Country] and the non-U.S. contractors must be audited using the same audit steps described in the other paragraphs of this section, including all tests necessary to specifically determine that costs incurred are allowable, allocable, reasonable, and supported under the Compact and related agreement terms.

If technical assistance and services were *not* contracted by MCA-[insert Country] from a non-U.S. contractor, the Auditors are still responsible for determining whether technical assistance and services were used for their intended purposes in accordance with the terms of the Compact and related agreements. However, the Auditors are not responsible for performing additional audit steps for the *costs incurred* under the technical assistance and services agreements, since either MCC or a cognizant U.S. government agency is responsible for contracting for audits of these costs.

11. Any funds managed by MCC as part of a Compact, pre-Compact or supplemental agreement will not be subject to the detailed audit procedures described below, but summary information must be displayed in the consolidated fund accountability statement. "Managed by MCC" refers to any situation in which a formal agreement requires MCC to procure goods, works and services and/or to make payments against the delivery of such goods, works and services, pursuant to the objectives of the relevant Compact or supplemental agreement. Audit treatment of funds managed by MCC shall be as follows:

- a. MCC will provide to MCA-[insert Country] summary information on procurements conducted by MCC on behalf of MCA-[insert country].
- b. MCC will provide the MCA-[insert Country] with the total value of third party payments made by MCC on behalf of MCA-[insert Country].
- c. The MCA-[insert Country] shall prepare the fund accountability statement adding the MCC third party payments on behalf of MCA-[insert Country] to the bottom of it and providing a grand total.
- d. MCC third party payments amount should be footnoted, "MCA-[insert Country] expenditures paid to a third party by MCC. These third party payments are added to the fund accountability statement for the purpose of providing full disclosure of MCA-[insert Country] expenditures for the audit period. The scope of the MCA-[insert Country] Accountable Entity Audit *does not* cover funds managed by MCC on behalf of MCA-[insert country]. The audit of these of expenditures will take place in the annual MCC Financial Audit.

12. Any questioned costs identified through audits of MCA-[insert Country]'s covered providers must be reported in the audit of MCA-[insert Country] since all uses of funds, whether by covered providers or by MCA-[insert Country] itself, will appear in MCA-[insert Country]'s fund accountability statement. Any internal control findings identified through audits of MCA-[insert Country]'s covered providers must be reported in the audit of MCA-[insert Country] if the internal control deficiencies could adversely affect the ability of MCA-[insert Country] to record, process, summarize, and report financial data consistent with the assertions of MCA-[insert Country]'s management in the fund accountability statement. Finally, any compliance findings identified through audits of MCA-[insert Country]'s covered providers must be reported in the audit of MCA-[insert Country] if the compliance deficiencies, alone or cumulatively, have a direct and material effect on the amounts in MCA-[insert Country]'s fund accountability statement.

C. Internal Controls

The Auditors must review and evaluate MCA-[insert Country]'s internal controls related to MCC-funded programs to obtain a sufficient understanding of the design of relevant control policies and procedures and whether those policies and procedures have been placed in operation. The U.S. Government Accountability Office's *Standards for Internal Controls in the Federal Government* (GAO/AIMD-00-21.3.1; 1999) may be helpful in assessing recipient internal controls. The auditor's understanding of the internal controls must be documented in the audit documentation file.

Prepare the report required by the *MCC Audit Guidelines*, identifying the reportable conditions that are significant deficiencies in the design or operation of the internal controls, and the reportable conditions considered to be material weaknesses. Material weaknesses are reportable conditions in which the design or operation of the specific internal control elements do not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material in relation to the fund accountability statement being audited may occur and not be detected within a timely period by management performing its normal functions. Reportable conditions, including material weaknesses, must be set forth in the report as "findings" (see paragraph 5.1.d of the *MCC Audit Guidelines*). Reportable conditions involve matters coming to the auditor's attention relating to significant deficiencies in the design or operation of internal controls that, in the auditor's judgment, could adversely affect MCA-[insert Country]'s ability to record, process, summarize, and report financial data consistent with the assertions of management in the fund accountability statement.

The major internal control components to be studied and evaluated include, but are not limited to, the controls related to each revenue and expense account on the fund accountability statement. The Auditors must:

1. Obtain a sufficient understanding of the internal controls to plan the audit and to determine the nature, timing and extent of tests to be performed.
2. Assess inherent risk and control risk, and determine the combined risk. Inherent risk is the susceptibility of an assertion, such as an account balance, to a material misstatement assuming there are no related internal control policies or procedures. Control risk is the risk that a material misstatement, that could occur in an assertion, will not be prevented or detected on a timely basis by the entity's internal control policies or procedures. Combined risk (sometimes referred to as detection risk) is the risk that the auditor will not detect a material misstatement that exists in an assertion. Combined risk depends upon the effectiveness of an auditing procedure and its application by the auditor.
3. Summarize the risk assessments for each assertion in the audit documentation. The risk assessments must consider the following broad categories under which each assertion should be classified: (a) existence or occurrence; (b) completeness; (c) rights and obligations; (d) valuation or allocation; and (e) presentation and disclosure. At a minimum, the audit documentation files must identify the name of the account or assertion, the account balance or the amount represented by the assertion, the assessed level of inherent risk (high, moderate, or low), the assessed level of control risk (high, moderate, or low), the combined risk (high, moderate, or low), and a description of the nature, extent, and timing of the tests performed based on the combined risk. The summarized audit documentation must be cross-indexed to the supporting audit documentation files that contain the detailed analysis of the fieldwork. If control risk is evaluated at less than the maximum level (high), then the basis for the auditor's conclusion must be documented in the audit documentation files.

If the control risk is assessed at the maximum level for assertions related to material account balances, transaction classes, and disclosure components of financial statements when such assertions are significantly dependent upon computerized information systems, the Auditors must document in the audit documentation files the basis for such conclusions by addressing (i) the ineffectiveness of the design and/or operation of controls, or (ii) the reasons why it would be ineffective to test the controls.

4. Evaluate the control environment, the adequacy of the accounting systems, and control procedures. Emphasis must be placed on the policies and procedures that pertain to MCA-[insert Country]'s ability to record, process, summarize, and report financial data consistent with the assertions embodied in each account of the fund accountability statement. This evaluation must include, but not be limited to, the control systems for:
 - a. ensuring that charges to the program are proper and supported;
 - b. managing cash on hand and in bank accounts;
 - c. procuring goods and services;
 - d. managing inventory and receiving functions;
 - e. managing personnel functions such as timekeeping, salaries, and benefits;

- f. managing and disposing of assets (such as vehicles, equipment, and tools, as well as other assets) purchased either by the program or directly by the MCC; and
- g. ensuring compliance with Compact and related agreement terms and applicable laws and regulations that collectively have a material impact on the fund accountability statement.

The results of this evaluation must be contained in the audit documentation section described in Section IV.E of this statement of work dealing with the review of compliance with Compact and related agreement terms and applicable laws and regulations and presented in the compliance report.

- 5. Evaluate internal controls established to ensure compliance with cost-sharing requirements, if applicable, including both provision and management of the contributions.
- 6. Include in the study and evaluation other policies and procedures that may be relevant if they pertain to data the auditor uses in applying auditing procedures. This may include, for example, policies and procedures that pertain to non-financial data that the auditor uses in analytical procedures.

In fulfilling the audit requirement relating to an understanding of the internal controls and assessing the level of control risk, the auditor must follow, at a minimum, the guidance contained in AICPA SAS Nos. 55, 60, 78 and 94 (AU110, AU319, AU324 and AU325), respectively entitled *Consideration of Internal Control in a Financial Statement Audit*, *Communication of Internal Control Related Matters Noted in an Audit*, *Consideration of Internal Control in a Financial Statement Audit: An Amendment to SAS 55*, and *The Effect of Information Technology on the Auditor's Consideration of Internal Control in a Financial Statement Audit*, as well as SAS No. 74 (AU801) entitled *Compliance Auditing Considerations in Audits of Governmental Entities and Recipients of Governmental Financial Assistance*, and SAS No. 99 entitled *Consideration of Fraud in a Financial Statement Audit*.

D. Compliance with Agreement Terms and Applicable Laws and Regulations

In fulfilling the audit requirement to determine compliance with Compact, pre-Compact and/or related agreement terms and applicable laws and regulations related to MCC-funded programs, the Auditors must, at a minimum, follow guidance contained in AICPA SAS No. 74 (AU801) entitled *Compliance Auditing Considerations in Audits of Governmental Entities and Recipients of Governmental Financial Assistance*. The compliance review must also determine—on audits of awards that present cost-sharing budgets on an annual basis and on close-out audits of awards that present cost-sharing budgets on a life-of-project basis—whether cost-sharing contributions were provided and accounted for in accordance with the terms of the agreements. The auditor's report on compliance must set forth as findings all material instances of noncompliance, defined as instances that could have a direct and material effect on the fund accountability statement.

The auditor's report must include all conclusions that a fraud or illegal act either has occurred or is likely to have occurred. In reporting material fraud, illegal acts, abuse, or other noncompliance the Auditors must place their findings in proper perspective. To give the reader a basis for judging the prevalence and consequences of these conditions, the instances identified should be related to the universe or the number of cases examined and be quantified in terms of U.S. dollar value, if appropriate. In presenting material irregularities, illegal acts, or other noncompliance, Auditors must follow the reporting standards contained in Chapter 5 of U.S. *Government Auditing Standards*. Auditors may provide less extensive disclosure of irregularities and illegal acts that are not material in either a quantitative or qualitative sense. Chapter 4 of U.S. *Government Auditing Standards* provides guidance on factors that may influence Auditors' materiality judgments. If the auditor concludes that sufficient evidence of irregularities or

illegal acts exists, they must immediately contact the MCC Inspector General, and must exercise due professional care in pursuing indications of possible irregularities and illegal acts so as not to interfere with potential future investigations and/or legal proceedings.

In planning and conducting the tests of compliance, the Auditors must:

1. Identify the requirements of the Compact and related Compact documents and pertinent laws and regulations and determine which of those, if not observed, could have a direct and material effect on the fund accountability statement. The Auditors must:
 - a. list all standard and program-specific provisions contained in the Compact and related agreements that cumulatively, if not observed, could have a direct and material effect on the fund accountability statement;
 - b. assess the inherent and control risk that material noncompliance could occur for each of the compliance requirements listed in 1.a. above;
 - c. determine the nature, timing and extent of audit steps and procedures to test for errors, fraud, and illegal acts that provide reasonable assurance of detecting both intentional and unintentional instances of noncompliance with the Compact and related agreement terms and applicable laws and regulations that could have a material effect on the fund accountability statement. This must be based on the risk assessment in 1.b. above; and
 - d. prepare a summary audit documentation file that adequately identifies each of the specific compliance requirements included in the review, the results of the inherent, control, and combined (detection) risk assessments for each compliance requirement, the audit steps used to test for compliance with each of the requirements based on the risk assessment, and the results of the compliance testing for each requirement. The summary audit documentation file must be cross-indexed to detailed audit documentation files that adequately support the facts and conclusions contained in the summary audit documentation file.
2. Determine if payments have been made in accordance with the Compact, pre-Compact and/or related agreement terms and applicable laws and regulations.
3. Determine if funds have been expended for purposes not authorized or not in accordance with applicable agreement terms. If so, the auditor must identify these costs as questioned in the fund accountability statement.
4. Identify any costs not considered appropriate, classifying and explaining why these costs are questioned.
5. Determine whether assets, whether directly procured by MCA-[insert Country] or directly procured by MCC for MCA-[insert Country]'s use, exist or were used for their intended purposes in accordance with the Compact, pre-Compact, and/or related agreements. Ensure that assets are marked in accordance with agreement requirements. If not, the cost of such assets must be questioned.
6. Determine whether any technical assistance and services, whether procured by MCA-[insert Country] or directly procured by MCC for MCA-[insert Country]'s use, were used for their intended purposes in accordance with the Compact, pre-Compact, and/or related agreements. If not, the cost of such technical assistance and services must be questioned.

7. Determine if the amount of cost-sharing funds was calculated and accounted for as required by the Compact, pre-Compact, and/or related agreements or applicable cost principles.
8. Determine if the cost-sharing funds were provided according to the terms of the Compact, pre-Compact, and/or related agreements and quantify any shortfalls.
9. Determine whether those who received services and benefits were eligible to receive them.
10. Determine whether MCA-[insert Country]'s financial reports (including those on the status of cost-sharing contributions) and claims for advances and reimbursement contain information that is supported by the books and records.

E. Follow-Up on Prior Audit Recommendations

The Auditors must review the status of actions taken on findings and recommendations reported in any pre-award review and prior audits of MCC-funded programs. Chapter 4 of the U.S. *Government Auditing Standards* under the section entitled *Considering the Results of Previous Audits and Attestation Engagements*, states: "Auditors should consider the results of previous audits and attestation engagements and follow up on known significant findings and recommendations that directly relate to the objectives of the audit being undertaken." As well, the Chapter states, "Auditors should use professional judgment in determining (1) prior periods to be considered, (2) the level of work necessary to follow up on significant findings and recommendations that affect the audit, and (3) the affect on the risk assessment and audit procedures in planning the current audit." They must do this to determine whether the auditee has taken timely and appropriate corrective actions. Auditors must report the status of uncorrected material findings and recommendations from any pre-award survey and prior audits that affect the financial statement audit.

The Auditors must review and report on the status of actions taken on prior findings and recommendations in the summary section of the audit report. The Auditors must refer to the most recent audit report for the same award (for a follow-up audit), or other MCC-funded awards and any pre-award survey (for an initial audit). When corrective action has not been taken and the deficiency remains unresolved for the current audit period and is reported again in the current report, the Auditors need to briefly describe the prior finding and status and show the page reference to where it is included in the current report. If there were no prior findings and recommendations, the Auditors must include a note to that effect in this section of the audit report.

F. Other Audit Responsibilities

The Auditors must perform the following steps:

1. Hold entrance and exit conferences with MCA-[insert Country]. The MCC country representative and MCC Inspector General must be notified of these conferences in order that their representatives and any other MCC representatives that have an interest may attend.
2. During the planning stages of an audit, communicate information to the auditee regarding the nature and extent of planned testing and reporting on compliance with laws and regulations and internal control over financial reporting. Such communication must state that the Auditors do not plan to provide opinions on compliance with laws and regulations and internal control over

- financial reporting.³ Written communication is preferred. Auditors must document the communication in the audit documentation files.
3. Institute quality control procedures to ensure that sufficient competent evidence is obtained through inspection, observation, inquiries, and confirmations to afford a reasonable basis for an opinion regarding the financial statements under audit. While Auditors may use their standard procedures for ensuring quality control, those procedures must, at a minimum, ensure that:
 - audit reports and supporting audit documentation files are reviewed by an auditor, preferably at the partner level, who was not involved in the audit. This review must be documented in the audit documentation files;
 - all quantities and monetary amounts involving calculations are footed and cross-footed; and
 - all factual statements, numbers, conclusions and monetary amounts are cross-indexed to supporting audit documentation files.
 4. Ascertain whether MCA-[insert Country] ensured that audits of its Covered Providers were performed to ensure accountability for MCC funds passed through to the Covered Providers (see paragraph 1.6 of the *MCC Audit Guidelines*). If audit requirements for Covered Providers were not met, the Auditors must disclose this in the auditor's report on the fund accountability statement and consider qualifying their opinion.
 5. Obtain a management representation letter in accordance with AICPA SAS No. 85 (AU333), SAS No. 89, and SAS No. 99 signed by MCA-[insert Country]'s management. See Example 4.1 of the *MCC Audit Guidelines* for an illustrative management representation letter.
 6. Evaluate the supplemental information prepared and provided to recognize accrual activity such as expenses incurred, but not yet paid, for and portion of the outstanding advances that are actually assets at the end of the period.

V. AUDIT REPORTS

The Auditors must submit one hard copy and one electronic copy (in .pdf format) of the final audit report to the MCC Inspector General. In turn, the MCC Inspector General will incorporate the Auditor's report into an audit report issued by the MCC Inspector General which report will include any Inspector General recommendations addressed to the MCC. To make it easier for Auditors to comply with the *MCC Audit Guidelines*, the format and content of the audit reports must follow the illustrative reports in Chapter 7 of the *MCC Audit Guidelines*. The audit report must specify the correct award number of each award covered by the audit. The report must contain:

- A. a title page,⁴ table of contents and a transmittal letter and summary which includes: (1) a background section with a general description of the MCC-funded programs audited, the period covered, the program objectives, a clear identification of all entities mentioned in the report, a

³ The auditors only express an opinion on the fund accountability statement, and the indirect cost rate and general purpose financial statements, if applicable, as indicated in Chapter 3 of the *MCC Audit Guidelines*.

⁴ Closeout audits must specify they are closeout audits on the title page. A closeout audit is an audit for an award that expired during the period audited.

section on the follow-up of prior audit recommendations, and whether MCA-[insert Country] has a provisional indirect cost rate authorized by MCC; (2) the objectives and scope of the financial audit, and a clear explanation of the procedures performed and the scope limitations, if any; (3) a brief summary of the audit results on the fund accountability statement, questioned costs, internal controls, compliance with the Compact and related agreement terms and applicable laws and regulations, and the status of prior audit recommendations; and (4) a brief summary of MCA-[insert Country]'s management comments regarding their views on the audit results and findings.

B. the auditor's report on the fund accountability statement must identify any questioned costs not fully supported with adequate records or not eligible under the terms of the Compact and related agreements. The report must be in conformance with the standards for reporting in Chapter 5 of the U.S. *Government Auditing Standards* and must include:

1. The auditor's opinion on whether the fund accountability statement presents fairly, in all material respects, program revenues, and costs incurred for the audited period in accordance with the terms of the Compact, pre-Compact, and/or related agreements, and in conformity with generally accepted accounting principles or other basis of accounting. This opinion must clearly state that the audit was performed in accordance with U.S. *Government Auditing Standards* or specific alternative standards, if applicable (see paragraph 2.9.d of the *MCC Audit Guidelines*). Any deviations from these standards, such as noncompliance with the requirements for continuing professional education and external quality control reviews, must be disclosed (See Example 7.1.A of the *MCC Audit Guidelines*).
2. The fund accountability statement identifying the program revenues, costs incurred, and assets and technical assistance directly procured by MCC for the audited period (in the summary format outlined by this Terms of Reference). The statement must also identify questioned costs not considered eligible for reimbursement and unsupported, if any, including the cost of any assets and technical assistance directly procured by MCC whose existence or proper use in accordance with agreements could not be verified. All questioned costs resulting from instances of noncompliance with the Compact and related agreement terms and applicable laws and regulations must be included as findings in the report on compliance. Also, the notes to the fund accountability statement must briefly describe all questioned costs and must be cross-referenced to any corresponding findings in the report on compliance (see Example 6.1 of the *MCC Audit Guidelines*). All questioned costs in the notes to the fund accountability statement must be stated in U.S. dollars. The U.S. dollar equivalent must be calculated at the exchange rate applicable at the time the dollars were converted to local currency by MCA-[insert Country].
3. Notes to the fund accountability statement, including a summary of the significant accounting policies, explanation of the most important items of the statements, the exchange rates during the audit period and foreign currency restrictions, if any. In addition, a note to the fund accountability statement must state whether any interest on MCC-provided funds was returned to MCC or otherwise used in accordance with the terms of the Compact and related agreements.

C. the auditor's report on internal control. The auditor's report must include as a minimum: (1) the scope of the auditor's work in obtaining an understanding of the internal controls and in assessing the control risk, and; (2) the reportable conditions, including the identification of material weaknesses in MCA-[insert Country]'s internal controls. Reportable conditions must be described in a separate section (see paragraphs 5.2 through 5.4 of the *MCC Audit Guidelines*).

This report must be made in conformance with SAS No. 60 and the standards for reporting in Chapter 5 of U.S. *Government Auditing Standards*.

- D.** the auditor's report on MCA-[insert Country]'s compliance with the Compact, pre-Compact, and/or related agreement terms, specifically including the Procurement Guidelines and the Fiscal Accountability Plan, and applicable laws and regulations related to MCC-funded programs. The report must follow the guidance in SAS No. 74. Material instances of noncompliance must be described in a separate section (see paragraphs 5.2 through 5.4 of the *MCC Audit Guidelines*). All questioned costs resulting from instances of noncompliance must be included as findings in the report on compliance. Also, the notes to the fund accountability statement that describe questioned costs must be cross-referenced to any corresponding findings in the report on compliance.

The auditor's report must include all conclusions, based on evidence obtained, that a fraud or illegal act either has occurred or is likely to have occurred. This report must include an identification of all questioned costs, if any, as a result of fraud or illegal acts, without regard to whether the conditions giving rise to the questioned costs have been corrected and whether MCA-[insert Country] does or does not agree with the findings and questioned costs.

In reporting material fraud, illegal acts, or other noncompliance, the Auditors must place their findings in proper perspective. To give the reader a basis for judging the prevalence and consequences of these conditions, the instances identified must be related to the universe or the number of cases examined and quantified in terms of U.S. dollar value, if appropriate. In presenting material fraud, illegal acts, or other noncompliance, Auditors must follow the reporting standards contained in Chapter 5 of U.S. *Government Auditing Standards*. Auditors may provide less extensive disclosure of irregularities and illegal acts that are not material in either a quantitative or qualitative sense. Chapter 4 of U.S. *Government Auditing Standards* provides guidance concerning factors that may influence Auditors' materiality judgments. If the Auditors conclude that sufficient evidence of irregularities or illegal acts exist, they must contact the MCC Inspector General and exercise due professional care in pursuing indications of possible irregularities and illegal acts so as not to interfere with potential future investigations and/or legal proceedings.

- E.** the auditor's comments on the status of prior audit recommendations. The Auditors must review and report on the status of actions taken on findings and recommendations reported in prior audits and any pre-award survey recommendations. When corrective action has not been taken and the deficiency remains unresolved for the current audit period and is reported again in the current report, the Auditors need only briefly describe the prior finding and show the page reference where it is included in the current report. If there were no prior findings and recommendations, a note to that effect must be included in this section of the audit report.

The findings contained in the reports on internal controls and compliance related to MCC-funded programs must include a description of:

- the condition (what is);
- the criteria (what should be);
- the cause (why it happened);
- the effect (what harm was caused by not complying with the criteria); and
- a *recommendation* that corrects the cause and the condition, as applicable.

It is recognized that material internal control weaknesses and noncompliance found by the Auditors may not always have all of these elements fully developed, given the scope and objectives of the

specific audit. The Auditors must, however, at least identify the condition, criteria and possible effect to enable management to determine the cause and take timely and proper corrective action.

Findings which involve monetary effect must:

1. Be quantified and included as questioned costs in the fund accountability statement and in the auditor's report on compliance.
2. Be reported without regard to whether the conditions giving rise to them were corrected.
3. Be reported whether MCA-[insert Country] does or does not agree with the findings or questioned costs.
4. Contain enough relevant information to expedite the audit resolution process (e.g., number of items tested, size of the universe, error rate, corresponding U.S. dollar amounts, etc.).

The reports must also contain, after each recommendation, pertinent views of responsible recipient officials concerning the auditor's findings and actions taken by MCA-[insert Country] to implement the recommendations. If possible, the auditor should obtain written comments. When the Auditors disagree with management comments opposing the findings, conclusions, or recommendations, they should explain their reasons following the comments. Conversely, the Auditors should modify their report if they find the comments valid.

Any evidence of fraud, illegal acts or abuse that have occurred, or are likely to have occurred, must be included in a separate written report if deemed necessary by the MCC Inspector General. This report must include an identification of all questioned costs as a result of abuse, irregularities or illegal acts, without regard to whether the conditions giving rise to the questioned costs have been corrected or whether MCA-[insert Country] does or does not agree with the findings and questioned costs.

VI. INSPECTION AND ACCEPTANCE OF AUDIT WORK AND THE REPORT

The Auditor shall conduct an **Exit Interview** with MCA-[insert Country] after the completion of fieldwork to discuss its preliminary audit findings and allow MCA-[insert Country] to correct and clarify any misunderstandings that may have arisen during fieldwork, and to request formal, written comments for inclusion into the Draft Audit report. After the Draft Audit report has been prepared, the MCA-[insert Country] management responses to the findings have been incorporated, and the Draft Audit report has been routed through the Auditor's formal in-house review process, it shall be sent to the MCC Inspector General.

The MCC Inspector General will review the Draft Audit report, and provide suggestions to the Auditor for consideration and incorporation into the report. A formal **Exit Conference** will be convened with the MCA-[insert Country] to present and discuss the MCC IG reviewed Draft Audit report. After conducting the formal Exit Conference and incorporating all formal written comments from MCA-[insert Country] and after all MCC Inspector General suggestions have been addressed and incorporated into the Audit report, the Auditor shall forward the Final Audit report to the MCC Inspector General for its approval and acceptance.

The MCC Inspector General is responsible for assuring that the work performed under this statement of work complies with U.S. *Government Auditing Standards* and the "Millennium Challenge Corporation Guidelines for Financial Audits Contracted by Foreign Recipients" issued by the MCC Inspector General (IG). To accomplish this objective, the MCC Inspector General will perform desk reviews on every draft

audit report, and may review audit documentation files prior to approving draft audit reports or perform quality control reviews of the audit documentation files after the audit has been completed.

For the IG's review of audit documentation files, the Auditors must ensure that all audit records related to the audited agreements are available to enable IG Auditors to accomplish and support their review. To this end, the IG Auditors must have access to all pertinent audit documentation files and records of MCA-[insert Country] and its Covered Providers and be authorized to make excerpts, photocopies, and transcripts as deemed necessary by the IG.

If the MCC Inspector General does not accept the report because of deficiencies in the work, the Auditors must perform any additional audit work requested at no additional cost to MCC, MCA-[insert Country] or the U.S. Government.

VII. RELATIONSHIPS AND RESPONSIBILITIES

While the Compact agreement is between the MCC and the host country, and MCA-[insert Country] as the host country's implementing entity, in order for the MCC Inspector General to exercise its quality control responsibilities over audits of U.S. funds, the IG program coordinator for this contract is Richard Taylor @ (202) 712-4884 and MCCFA@USAID.gov.

The Auditors will work in coordination with, [Insert Accountable Entity Point of Contact name and title]. The liaison for audit concerns will be Richard Taylor, Director, MCC Financial Audit Division, of the MCC Inspector General or his/her designee, and the liaison for information and assistance from the MCC will be the MCC country representative or his/her designee.

The MCC country representative may meet with the public accounting firm at the beginning of the audit to explain any financial/compliance areas of concern contained in the statement of work that they want emphasized and provide any advice concerning the performance of the audit. The MCC country representative shall provide the following information to the Auditors for the entrance conference:

1. a list of all disbursements made by the MCC to MCA-[insert Country] under the Compact; and
2. summary information on procurements conducted by MCC on behalf of MCA-[insert country]; and
3. the total value of third party payments made by MCC on behalf of MCA-[insert Country].

MCC may also provide written comments on the draft audit report concerning the facts and conclusions contained in the report in order to obtain the best possible end product. The MCC country representative may also attend the exit conference for the same purpose. However, the MCC country representative comments on the draft report and at the exit conference will not be binding on the public accounting firm.

The auditor must properly maintain and store the audit documentation files for a period of five years from the completion of the audit. During this five-year period the Auditors must immediately provide the audit documentation files when requested by the MCC Inspector General. Auditors that are nonresponsive or do not provide timely responses to questions raised by the MCC country representative or MCC Inspector General shall be temporarily or permanently excluded from performing additional audits of MCC-funded programs.

VIII. TERMS OF PERFORMANCE

The effective date of this contract will be the date of the signature of MCA-[insert Country]'s authorized representative.

The Base Period audit must begin as soon as practicable after the signing of the audit contract, and from the audit start date, the Auditors must submit to MCC Inspector General: (a) a complete audit program, written in English, within 14 calendar days, after the signing of the contract, (b) an indexed draft audit report written in English within 45 calendar days after signing the contract, and (c) a final audit report that includes revisions incorporating MCC Inspector General comments within 90 calendar days after the Base Audit Period end date.

Each Option Period audit will require that the Auditors submit to MCA [insert country] and MCC Inspector General: (a) a complete audit program, written in English, thirty (30) calendar days prior to the end of each Option Audit Period, (b) an indexed draft audit report written in English within 60 calendar days after each Option Audit Period end date, and (c) a final audit report that includes revisions incorporating MCC Inspector General comments within 90 calendar days after each Option Audit Period end date.

It is the responsibility of MCA-[insert Country] to ensure that all records are available, all accounting entries and adjustments are made, and all other necessary steps are taken to make possible for the Auditors to perform the work necessary to be able to present the final audit report to the MCC Inspector General within 90 calendar days after the end of the audited period. In order for the Auditors to meet this Compact requirement, MCA-[insert Country] will need to close its books and have its fund accountability statement ready for audit within 14 calendar days after the audit cutoff period. Further, in order to deliver the final audit report to the MCC Inspector General within 90 calendar days after the audit cutoff period, the Auditors will need to have conducted interim testing well before the audit cutoff date and begin final testing while MCA-[insert Country] is still in the process of closing its accounting records.

Deliverables

Deliverables which must be submitted to the MCC Office of Inspector General at MCCFA@USAID.gov:

1. **Planning Document.** This deliverable shall include a detailed Audit Program with clearly established milestones for completing the audit.
2. **Draft Audit Report.** This deliverable shall include an indexed draft audit report to include an opinion on the financial statements, report on the internal controls, and report on Compact compliance and supplemental agreements to MCC Inspector General.
3. **Final Audit Report.** This deliverable shall include a final audit report to include an opinion on the financial statements, report on internal control, and report on compliance with Compact and supplemental agreements.

Type of Contract

This contract is considered a fixed price contract.

Terms of Payment

For each period (either Base Period or one of three Option Periods) payment will be provided in three phases upon successful completion of the three deliverables described in the Terms of Reference. The payment schedule will be as follows:

1. 20 percent of the fixed price amount for the current period (either Base Period or one of three Option Periods) paid upon successful completion and acceptance by the MCC Inspector General of Deliverable 1, titled Planning Document;
2. 40 percent of the fixed price amount for the current period (either Base Period or one of three Option Periods) paid upon successful completion and acceptance by the MCC Inspector General of Deliverable 2, titled Draft Audit Report; and
3. 40 percent of the fixed price amount for the current period (either Base Period or one of three Option Periods) paid upon successful completion and acceptance by the MCC Inspector General of Deliverable 3, titled Final Audit Report.

MCA - [insert Country]

SECTION V
TERMS OF REFERENCE - APPENDIX A

MCA-[INSERT COUNTRY] PLANNED RE-DISBURSEMENTS

MCA-[insert Country] has estimated the re-disbursements which are to be audited during both the Base Period and each of three (3) six month Option Periods as follows:

Contract Period	Period to be Audited	Planned Re-disbursements for Period To Be Audited
Effective Date of the Contract to [insert date]	[insert date] to [insert date]	[\$ Insert Amount Here]
[insert date] to [insert date]	[insert date] to [insert date]	[\$ Insert Amount Here]
[insert date] to [insert date]	[insert date] to [insert date]	[\$ Insert Amount Here]
[insert date] to [insert date]	[insert date] to [insert date]	[\$ Insert Amount Here]

These numbers represent MCA-[insert country]’s planned re-disbursements for illustrative purposes only, to assist Auditors in preparing their Financial Proposals. Actual re-disbursements will be determined by actual program expenses, and any variation from these planned re-disbursements will have no bearing on final the lump-sum fixed price paid to the Auditor by MCA-[insert Country]. After the effective date of the contract, there will be no negotiation of the Proposal Price, either in total or per option or base period, regardless of actual re-disbursements to be audited.