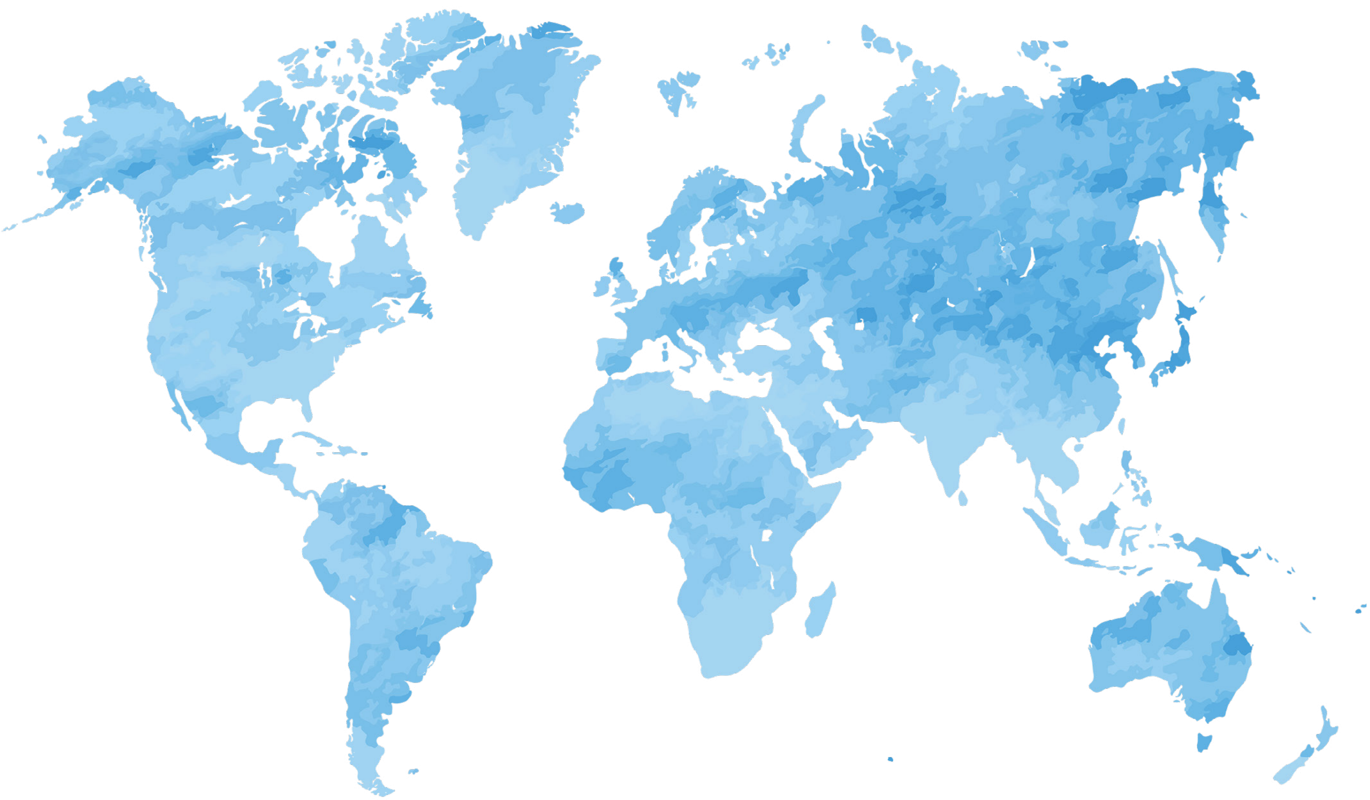
Millennium Challenge Corporation

Agency Financial Report

Fiscal Year 2017



October 1, 2016 – September 30, 2017

MILLENNIUM
CHALLENGE CORPORATION
UNITED STATES OF AMERICA

MCC Partner Countries — Compacts and Threshold Programs

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

Country name badge and map color denote current status (blends indicate multiple, concurrent status), rectangular badges denote previous status.

2010-002-0097-24

Agency Financial Report

Fiscal Year 2017

October 1, 2016 – September 30, 2017

Contents

Introduction

The Millennium Challenge Corporation's (MCC) Agency Financial Report (AFR) for fiscal year (FY) 2017 provides the results that enable the President, Congress, and the American people to assess MCC's performance for the reporting period beginning October 1, 2016, and ending September 30, 2017. In particular, the AFR provides an overview of MCC's programs, accomplishments, challenges, and management's accountability over the resources entrusted to MCC. This report was prepared in accordance with the requirements of the Office of Management and Budget (OMB) Circular No. A-136, *Financial Reporting Requirements.*

MCC will also prepare an Annual Performance Report (APR) for FY 2017 that will also be included in MCC's FY 2019 Congressional Budget Justification (CBJ). The APR will be posted on MCC's website in February 2018. Together, the AFR and APR provide a comprehensive presentation and disclosure of important financial and programmatic information related to MCC's operations and results, including a fair assessment of MCC's leadership and stewardship of the resources entrusted to the agency. MCC provides further information related to its activities in an Annual Report to its Board of Directors, Congress, stakeholders, and the public on its website.

Organization of This Report

The FY 2017 AFR includes a message from the Chief Executive Officer (CEO), followed by three sections and one appendix:

- **Section I: Management's Discussion and Analysis** integrates performance and financial information with key performance results, financial statements, systems and controls, compliance with laws and regulations, and actions taken or planned to address problems.
- **Section II: Financial Section** contains a message from the Acting Vice President, Department of Administration and Finance and Chief Financial Officer (CFO), the financial statements and accompanying notes, and the independent auditor's report.
- **Section III: Other Information** includes the Office of Inspector General's (OIG's) top management challenges, MCC Management's response to the top management challenges, Summary of Financial Statement Audit and Management Assurances, MCC's Payment Integrity, Fraud Reduction Report, and Grants Oversight & New Efficiency (GONE) Act Requirements.
- **Appendix A** includes a list of acronyms used in this report.

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

Message from the Millennium Challenge Corporation's Acting Chief Executive Officer

November 15, 2017

I am pleased to submit the Millennium Challenge Corporation's (MCC) fiscal year (FY) 2017 Agency Financial Report (AFR). MCC's core business is leveraging evidence and evaluation to drive poverty reduction through economic growth. MCC works only in partner countries that have demonstrated a commitment to ruling justly, investing in their people and supporting economic freedoms. The agency's approach is selective and business-like. Decisions are based on hard data and rigorous analysis. Results are evaluated, monitored and publicly shared. This process ensures that MCC's resources are allocated efficiently and effectively.

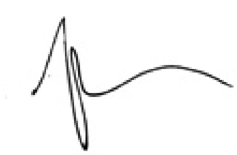
MCC had a busy and productive FY 2017. MCC signed new programs with Nepal and Kosovo. The agency also began the 5-year implementation clock with Benin and Morocco, closed out an important and impactful compact with Jordan, and selected Tunisia, Burkina Faso, and Timor Leste as eligible to begin developing programs with MCC. MCC continued to advance programs in development and implementation that will address the most binding constraints to economic growth in some of the world's poorest communities. Most recently, MCC was rated first among eight federal agencies in Results for America's "2017 Federal Invest in What Works Index," reaffirming MCC's commitment to accountability.

As MCC looks to the future, the agency is focused not only on delivering and expanding the impact of its effective, data-driven programs, but also maximizing the efficiency and performance of its lean, dedicated workforce. Programmatically, the agency seeks to increase the impact of its investments by exploring regional partnerships, as bi-partisan legislation advances in both the House and the Senate to give MCC this important new authority. Moreover, in line with the Administration's priorities, MCC leadership team is making strategic investments to strengthen its organizational health and effectiveness, as well as enhancing operational efficiencies.

MCC's singular focus on economic growth is one of the most effective ways to achieve widespread and lasting reductions in poverty in the developing world. By holding itself and its partner countries accountable for results and continued good governance, MCC advances American security, values, and prosperity. And with cost-effective projects, a lean staff, and an evidence-based approach, MCC is a good investment for the American people.

The financial and performance information presented in this AFR reflect the core principles on which MCC was founded 13 years ago. I am grateful to all the supporters and stakeholders who help hold MCC accountable, and I — along MCC's leadership team and staff — welcome your feedback.

Sincerely,



Jonathan G. Nash
Acting Chief Executive Officer
Millennium Challenge Corporation

Management's Discussion and Analysis

Mission, Values and Organizational Structure

Mission

The Millennium Challenge Act of 2003, 22 United States Code (U.S.C.) 7701-7718, established MCC as a wholly-owned Government corporation, as defined by the Government Corporation Control Act of 1945. MCC's mission is to reduce poverty by supporting sustainable economic growth in select developing countries that demonstrate a commitment to sound policies in the areas of democratic governance, economic freedom, and investment in their people. Good governance includes democratic rights and the rule of law, respect for human and civil rights, protection of private property rights, transparency and accountability in governance, and a commitment to fight against corruption. Economic freedom requires policies that enable citizens and firms to participate in global product and capital markets, promote private sector growth, and limit direct government interference in the economy. Investment in people encompasses investments in education and health care for a country's own citizens, with a particular emphasis on women and children.

MCC achieves this mission by investing in grant programs that unlock economic growth in our partner countries and help people lift themselves out of poverty. MCC's approach employs development best practices on selection, country ownership, and accountability; stimulates policy reform with analysis and data-driven decision-making; and leverages partnerships with donors and the private sector.

Specifically, MCC provides assistance through two types of grants to eligible countries:

- A ***compact*** provides for a five-year grant to a country that meets MCC's eligibility criteria and is selected for assistance by MCC's Board of Directors. The compact establishes a multi-year plan of partnership between the country and MCC to achieve shared development objectives. The compact establishes an investment program designed to reduce poverty through sustainable economic growth, and is built on the principles of country ownership, transparency and accountability, with input from the private sector, partner governments, other development partners, and civil society organizations. The compact agreement defines each party's responsibilities and includes benchmarks, timetables, and performance goals.
- A ***threshold program*** grant 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.

MCC's grant programs are focused on various sectors, including agricultural development, education, enterprise and private sector development, governance, health, water and sanitation, irrigation, transportation, electricity, and trade and investment capacity-building. MCC's governing statute requires MCC to provide assistance in a manner that promotes economic growth and reduces poverty.

MCC is just one member of the U.S. Government (USG) international development community. MCC works closely with the Department of State, the United States Agency for International Development (USAID), and other agencies to ensure that MCC programs complement related USG efforts and therefore maximize both MCC's and the USG's impact around the world. 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, a result that promotes America's national security interests.

Values

MCC's values define how we operate on a daily basis, both as individuals and as an institution, in pursuit of MCC's mission. Our values identify who we are and what is important to us. They guide how we make decisions, set priorities, address challenges, manage trade-offs, recruit and develop staff, and work together with our partner countries and stakeholders.

MCC's values are CLEAR:

Embrace Collaboration — 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 the best solutions.

Always Learn — 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 learning opportunity, and we apply and share those lessons broadly.

Practice Excellence — 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 one another to advance the fight against global poverty.

Be Accountable — 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 and foster strong working relationships with our colleagues at MCC, in our partner countries, and throughout the development community.

Organizational Structure

Board of Directors

MCC is overseen by a nine-member Board of Directors that is chaired by the Secretary of State. The Board of Directors also includes the Secretary of the Treasury, who acts as the Vice Chair, the U.S. Trade Representative, the USAID Administrator, MCC's CEO, and four private sector representatives appointed by the President of the United States with the advice and consent of the U.S. Senate. The Board of Directors generally meets four times each year. Among other responsibilities, the Board provides policy guidance to MCC, makes annual eligibility and selection determinations, and approves compact and threshold programs.

Executive Offices

MCC accomplishes its mission through the following executive offices:

Office of the Chief Executive Officer is led by the Senate-confirmed CEO and provides executive leadership and strategic direction for the agency; coordinates activities and communications across departments; manages the agency's Investment Management Committee; and oversees overall agency performance and day-to-day operations.

Department of Congressional and Public Affairs manages MCC's relationship with Congress, USG agencies, the media, universities, nongovernmental organizations, think tanks, the private sector, and other key groups interested in MCC's mission. The department also handles all media inquiries and interview requests, manages the MCC Speakers Bureau, coordinates all public events, serves as a liaison to the staff of MCC's Board of Directors, maintains MCC's public website, and disseminates information to the public via statements, press releases, and speeches, among other means.

Department of Compact Operations manages the operational relationships with MCC compact partner countries; leads MCC's work in developing and implementing high-impact, sustainable economic development projects around the world; provides technical and regional expertise and rigorous oversight of USG resources to address constraints to economic growth and reduce poverty; and works with other international development agencies and the private sector to coordinate efforts within MCC partner countries. The department divides the management of the MCC compact portfolio into two regional divisions, (1) Africa and (2) Europe, Asia, the Pacific and Latin America, and two technical divisions, (1) Sector Operations and (2) Infrastructure, Environment and the Private Sector. Department staff have a wide array of expertise, including education, fiscal accountability, infrastructure, agriculture, land policy, procurement, environmental and social performance, gender integration, private sector engagement, and human and community development.

Department of Policy and Evaluation manages MCC's annual country eligibility and selection processes and the development and implementation of threshold programs. The department also promotes effective policy improvement and reform; performs economic analysis; oversees monitoring and evaluation of MCC programs, including MCC's rigorous independent evaluations; and provides institutional leadership on interagency engagement.

Office of the General Counsel advises MCC's Board of Directors and staff on all legal issues affecting MCC, its programs, policies, and procedures; provides counsel on all legal aspects of country eligibility and selection, threshold programs, and other policy initiatives; addresses and resolves legal issues associated with compact and threshold programs; conducts and evaluates due diligence on country proposals; leads compact negotiations; provides advice on all issues affecting the internal operations of MCC; advises on matters of statutory interpretation, interagency agreements (IAAs) and communications, and other public initiatives; leads MCC's Anti-Fraud and Corruption Program; serves as Corporate Secretary to the MCC Board of Directors; and manages MCC's ethics program, providing related training and guidance to staff.

Department of Administration and Finance plans and directs all activities related to financial management and budgeting; manages MCC's human resources; oversees information technology (IT) infrastructure and services; enters into and manages all MCC contracts, acquisitions, grants and cooperative agreements; ensures personnel and physical security; coordinates and manages MCC's facilities; provides administrative services; oversees and administers MCC's Enterprise Risk Management (ERM) program; maintains official corporate records; coordinates audit interactions with the OIG and the Government Accountability Office (GAO); and coordinates and ensures timely and relevant reporting

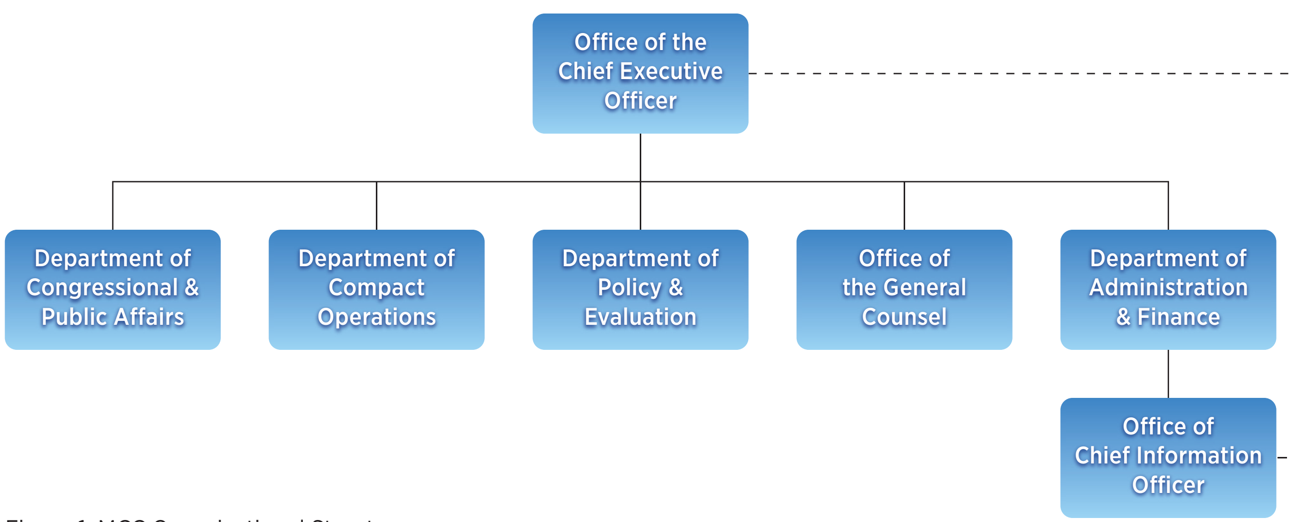


Figure 1. MCC Organizational Structure

of performance data on compact programs. There is a dotted reporting line between the Office of the CEO and the Office of the Chief Information Officer (CIO). The Office of the CIO oversees corporate IT investments on behalf of the agency.

Staffing

MCC is a small government agency headquartered in Washington, DC. Table 1 shows Federal employee staffing levels from FY 2015 through FY 2017.

Table 1. MCC Staffing Full Time Equivalent (FTE)*

	FY 2017	FY 2016	FY 2015
Headquarters	286	266	254
Overseas	26	24	22
Total	**312**	**290**	**276**

**Staffing report based on Standard Form (SF)-113A reporting of FTE calculations based on the fourth quarter of each FY.*

Performance Goals, Objectives, and Results

MCC utilizes an innovative and tested approach to fight global poverty. MCC's mission is to reduce poverty by supporting sustainable economic growth in select developing countries that demonstrate a commitment to sound policies in the areas of democratic governance, economic freedom, and investment in people. MCC achieves this mission by investing in grant programs that will unlock economic growth in our partner countries and help people lift themselves out of poverty. MCC's approach employs development best practices on selection, country ownership, and accountability; drives policy reform with analysis and data-driven decision-making; and leverages partnerships with donors and the private sector. MCC programs invest in a wide variety of sectors — including power, agriculture, education, clean water, and roads — in each case based on an analysis of which sectors or issues are holding back economic growth in our partner countries. As part of its FY 2019 CBJ, MCC will provide an APR, which will be available in February 2018. A high-level summary of MCC's strategic direction and performance during FY 2017 follows.

Strategic Direction

In February 2016, MCC launched a five-year strategic plan called *NEXT.* Based on a comprehensive review of MCC's experiences and lessons learned over its first 10 years of operations, *NEXT* seeks to expand MCC's impact through new strategic directions, while doubling down on the core strengths of the MCC model. The plan sets forth five strategic goals to frame and guide the agency's work moving forward:

- **GOAL 1:** Help countries choose evidence-based priorities in growth and poverty reduction strategies that reflect new learning and new **opportunities.**
- **GOAL 2:** Strengthen reform **incentives** and accountability.
- **GOAL 3:** Capitalize on public and private partnerships for more impact and **leverage.**
- **GOAL 4:** Lead data and results **measurement,** learning, transparency, and development effectiveness.
- **GOAL 5:** Maximize internal efficiency and productivity. Maintain and motivate a **world class,** high-functioning staff.

More information about *NEXT* is on MCC's website (www.mcc.gov/resources/pub/next).

Building on *NEXT,* MCC established the following corporate priorities for FY 2017 to guide agency activities:

- Advance and deliver high-quality compacts in a timely manner.
- Effectively oversee compacts in implementation.
- Advance and deliver high-quality threshold programs in a timely manner and effectively oversee programs in implementation.
- Develop a strong and dynamic knowledge management system, set of business practices, and tools to systematically share and deploy learning and results internally and externally.
- Develop and deploy corporate risk and portfolio management tools to inform resource allocation and strategic decisions.
- Enable transparent and efficient decision-making and integrate MCC CLEAR values and norms into daily operations to facilitate program success and strengthen organizational health.
- Strengthen and motivate agency workforce through data-driven workforce planning, consistent performance expectations, and improved performance management systems and feedback.

These FY 2017 corporate goals are reflected in the work and activities discussed in this AFR.

Snapshot of MCC Portfolio and Programming

As of September 30, 2017, MCC is currently engaged in partnerships with 26 countries (including compacts and threshold programs). Table 2 displays the number of countries in the development and implementation phases of compacts and threshold programs.

Table 2. MCC Portfolio as of Sept. 30, 2017
8 Countries in Compact Development
12 Countries in Compact Implementation
2 Countries in Threshold Program Development
4 Countries in Threshold Program Implementation

Table 3 displays grant totals, net of deobligated amounts, for every MCC compact signed since the agency's inception in 2004 through September 30, 2017.

Table 3. Value of Compact Grants as of September 30, 2017 (in thousands)

TOTAL	**$ 11,708,252**	*(100.0%)*
Tanzania	$ 694,546	*(5.9%)*
Morocco	$ 650,053	*(5.6%)*
Indonesia	$ 600,000	*(5.1%)*
Ghana	$ 536,289	*(4.6%)*
Nepal	$ 500,000	*(4.3%)*
Ghana II	$ 498,200	*(4.3%)*
Burkina Faso	$ 474,744	*(4.1%)*
Morocco II	$ 450,000	*(3.8%)*
El Salvador	$ 449,567	*(3.8%)*
Mozambique	$ 447,905	*(3.8%)*
Niger	$ 437,024	*(3.7%)*
Mali	$ 434,287	*(3.7%)*
Senegal	$ 433,318	*(3.7%)*
Georgia	$ 387,179	*(3.3%)*
Philippines	$ 385,072	*(3.3%)*
Benin II	$ 375,000	*(3.2%)*
Lesotho	$ 358,046	*(3.1%)*
Zambia	$ 354,758	*(3.0%)*
Malawi	$ 350,700	*(3.0%)*
Benin	$ 301,810	*(2.6%)*
Namibia	$ 295,719	*(2.5%)*
El Salvador II	$ 277,000	*(2.4%)*
Jordan	$ 272,935	*(2.3%)*
Mongolia	$ 268,994	*(2.3%)*
Moldova	$ 259,372	*(2.2%)*
Liberia	$ 256,726	*(2.2%)*
Honduras	$ 204,015	*(1.7%)*
Armenia	$ 176,550	*(1.5%)*
Georgia II	$ 140,000	*(1.2%)*
Nicaragua	$ 112,703	*(1.0%)*
Cabo Verde	$ 108,512	*(0.9%)*
Madagascar	$ 85,594	*(0.7%)*
Cabo Verde II	$ 66,230	*(0.6%)*
Vanuatu	$ 65,404	*(0.6%)*

In total, 28 countries have received funding through 34 compacts (Benin, Cabo Verde, El Salvador, Georgia, Ghana, and Morocco have signed two compacts each), and 25 countries have received funding through 27 threshold programs (Albania and Paraguay each signed two). Burkina Faso, Honduras, Indonesia, Jordan, Liberia, Malawi, Moldova, Niger, Philippines, Tanzania, and Zambia have signed both compacts and threshold program agreements.

In FY 2017, MCC signed one new compact (Nepal) and closed one compact (Jordan). MCC also signed one new threshold program (Kosovo).

MCC's Approach to Results and Performance Measurement

Overview

MCC is committed to achieving and measuring results; holding itself accountable for those results; transparently reporting results, data, and evaluations; and learning from the evidence to improve future programs. To fulfill this commitment, data-driven decision-making and monitoring and evaluation (M&E) are integrated into the entire program lifecycle, from country selection, to program conceptualization, to implementation and beyond. First, MCC chooses partners based on 20 publicly available indicators that measure democracy, good governance, and sound economic and social policies.

During program development, proposed investments, focused on alleviating binding constraints to growth, are identified through a rigorous, data-driven methodology. In addition, a clear program logic, indicators, baselines, milestones, targets, and benchmarks are typically identified to measure progress over the life of the program. After a compact or threshold program grant is signed, the partner country's accountable entity (typically also referred to as Millennium Challenge Account [MCA]) and MCC finalize an M&E plan for the program that provides the framework for monitoring and evaluating program activities. (Note: this structure may differ for threshold programs.)

The monitoring component of the M&E plan lays out the methodology and process for assessing progress toward the program goal. It identifies indicators, establishes performance milestones and targets, and provides details on the plan for data collection and reporting that will allow the MCA and MCC to track progress against targets on a regular basis.

The evaluation component identifies and describes the evaluations that will be conducted, the key evaluation questions and methodologies, and the data collection strategies that will be employed. M&E plans are revised as needed during the life of the program to adjust to changes in the program's design and to incorporate lessons learned for improved performance monitoring and measurement.

Figure 2 illustrates how results for the various phases are tracked and become part of a feedback loop to improve performance during a compact and to apply lessons learned to future compacts.

Monitoring Program Performance

MCC monitors progress by using performance indicators that measure progress at all levels. Lower-level process and output-level indicators are typically drawn from project and activity work plans, whereas higher-level targets are often linked directly to the economic rate of return analysis. MCC conducts this analysis to estimate the impacts of the investment, drawing from benefit streams. MCC reviews data quarterly to assess whether results are being achieved and subsequently integrates this information into project management decisions. Data for performance monitoring and reporting comes from baseline and follow-up surveys, project implementers, and other entities.

MCC strongly supports comprehensive, quality data collection conducted by local resources and frequently uses M&E program funds to invest in surveys fielded by both private firms and national statistical agencies or other government entities. All collected data, whether from surveys or implementers, undergo regular quality checks monitored by MCC to ensure integrity and accuracy.

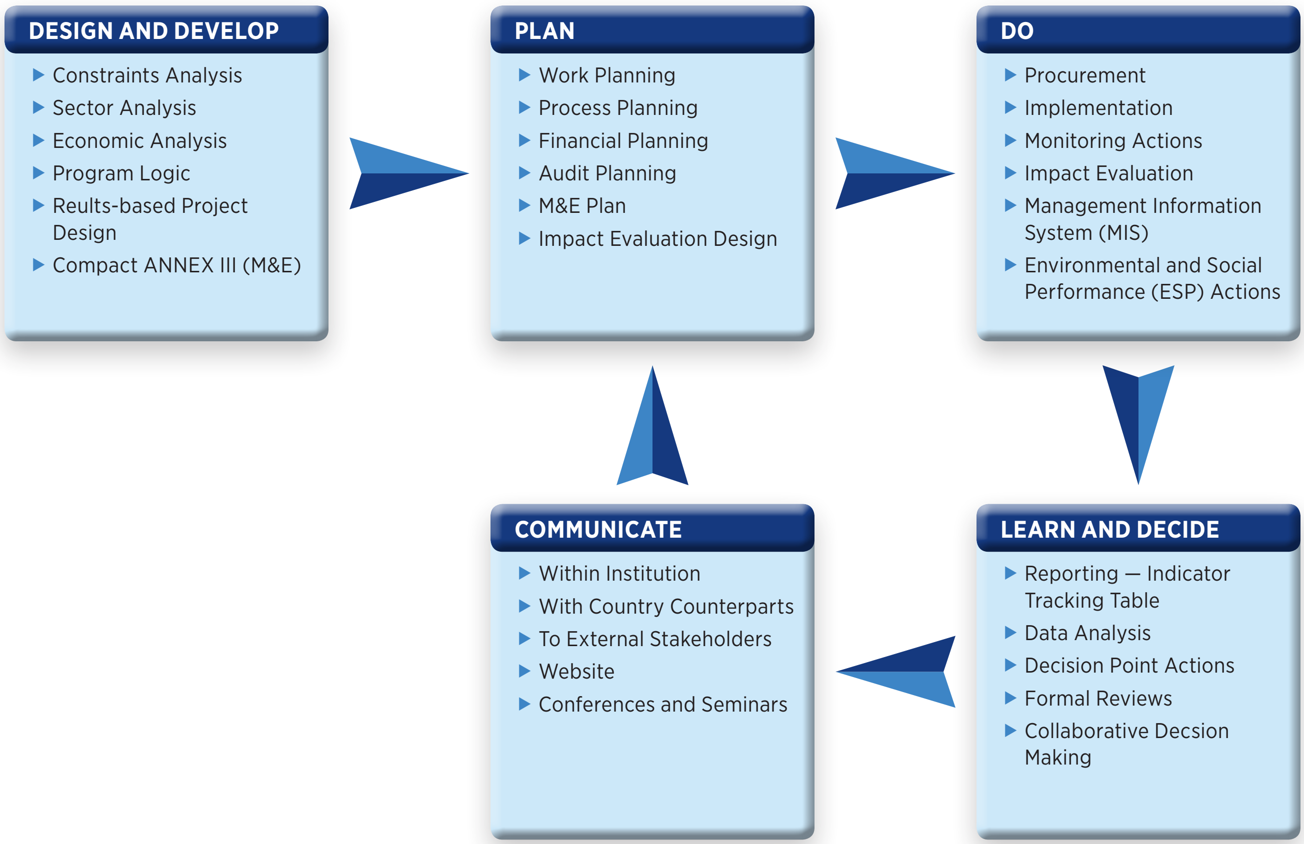


Figure 2. Integrating M&E in Compact Operations

Evaluating Program Performance and Results

MCC's development initiatives have helped reduce poverty, while spurring entrepreneurship and economic growth and helping build more stable, accountable, and inclusive societies. With a data-driven, evidence-based approach to decision-making, MCC invests heavily in tracking the impact and outcomes of these investments. 100 percent of MCC's projects are evaluated, with nearly 40 percent undergoing rigorous impact evaluations led by third party entities. In terms of beneficiaries, MCC's investments in areas like water and sanitation, agriculture, education, and energy are expected to benefit more than 174 million people around the world. MCC is also committed to assessing the cost-effectiveness of its investments to ensure that taxpayer dollars earn a social rate of return. A recent internal review of 122 closed projects found that, based on final costs and expected benefits, these projects had an average estimated economic rate of return of 15 percent.

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

MCC works with the development community to reassess its indicators periodically. MCC may complete early process-level indicators, such as contract dollars disbursed, more quickly than other indicators. The actual construction of a road, for example, will take more time and will be a more relevant indicator as time passes.

Table 4 presents MCC's program results across a representative set of select output indicators as of June 30, 2017, 2016, and 2015. The table aggregates

Table 4. Program Results by Sector on Select Output Indicators for FYs 2017, 2016, and 2015

	Cumulative Target Through FY 2017	Actual			Performance on Targets[1]		
		June 30, 2017	June 30, 2016	June 30, 2015	June 30, 2017	June 30, 2016	June 30, 2015
Sector — Roads							
Indicator: Value of signed contracts for road work *(dollars in millions)*	$ 2,242	$ 2,345	$ 2,345	$ 2,367	105%	105%	116%
Indicator: Kilometers of roads under works contracts	3,904	3,918	3,918	3,918	100%	100%	100%
Indicator: Kilometers of roads completed	3,551	3,055	2,876	2,876	85%	81%	86%
Countries Tracked: Armenia, Burkina Faso, Cabo Verde, El Salvador I, El Salvador II, Georgia, Ghana, Honduras, Mali, Moldova, Mongolia, Mozambique, Nicaragua, Philippines, Senegal, Tanzania, Vanuatu							
Sector — Agriculture and Irrigation							
Indicator: Hectares under new or improved irrigation	292,362	203,963	121,795	120,063	70%	42%	54%
Indicator: Value of agricultural and rural loans *(dollars in millions)*	$ 87	$ 87	$ 85[2]	$ 87	100%	97%	102%
Indicator: Farmers trained	282,785	321,708	274,442	120,063	114%	116%	105%
Indicator: Enterprises assisted	3,564	4,223	4,203	4,137	118%	118%	114%
Countries Tracked: Armenia, Burkina Faso, Cabo Verde, El Salvador, Georgia, Ghana, Honduras, Indonesia, Madagascar, Mali, Moldova, Morocco, Mozambique, Namibia, Nicaragua, Senegal							
Sector — Water and Sanitation							
Indicator: Value of signed contracts for water and sanitation works *(dollars in millions)*	$ 777	$ 795	$ 590	$ 574	102%	116%	112%
Countries Tracked: Cabo Verde, El Salvador, Georgia, Ghana, Jordan, Lesotho, Mozambique, Tanzania, Zambia							
Sector — Education							
Indicator: Students participating	266,094	215,398	215,243	215,160	81%	81%	80%
Indicator: Facilities completed	811	776	746	746	96%	92%	82%
Indicator: Value of signed contracts for construction and/or equipping of educational facilities *(dollars in millions)*	$ 201	$ 207	$ 187	$ 180	103%	100%	82%
Countries Tracked: Burkina Faso, El Salvador I, El Salvador II, Georgia II, Ghana, Mongolia, Morocco I, Morocco II, Namibia							
Sector — Land							
Indicator: Stakeholders trained	30,020	75,986	73,211[2]	99,059	253%	270%	105%
Indicator: Land administration offices established	280	384	393	249	137%	158%	NA
Countries Tracked: Benin, Burkina Faso, Cabo Verde II, Ghana, Lesotho, Madagascar, Mali, Mongolia, Mozambique, Namibia, Nicaragua, Senegal							

[1] Based on the cumulative target for that year.

[2] Data declined due to corrections of misreported data in closed compacts.

country-specific output 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 the 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.

MCC posts additional data on these five sectors on the results pages on its website (www.mcc.gov).

Post-Program Evaluations

As noted above, MCC also commissions independent **performance** and **impact** evaluations to help evaluate the long-term results of its investments.

- **Performance evaluations** estimate the contribution of MCC investments to changes in trends on outcomes, including household income. Performance evaluations serve an accountability purpose by comparing changes between the situation both before and after the MCC investment.
- **Impact evaluations** are the most rigorous form of evaluations because they estimate the causal impact of the MCC investment on key outcome indicators. They make it possible to know whether the observed impacts were caused specifically by an MCC investment or were the result of external factors. Impact evaluations compare what happened with the investment to what would have happened without it through use of a counterfactual.

Country Selection Process

The MCC Board of Directors selects eligible countries for MCC assistance and also selects the eligible countries with which MCC will seek to enter into a compact. Transparency regarding both the process and the criteria that govern and inform the selection of eligible country partners is a hallmark of the MCC model. For a country to be selected for an MCC assistance program, it must demonstrate commitment to just and democratic governance, investment in its people, and economic freedom as measured by a variety of policy indicators. MCC's Board of Directors examines this commitment primarily by consulting annual country "scorecards" of policy performance, as well as relevant supplemental information. It then considers the overall opportunity to reduce poverty and generate economic growth in a country, as well as the funding available.

MCC's selection process relies heavily on these public, data-driven country scorecards, which allow stakeholders, policy makers, Congress, taxpayers, and beneficiaries to hold the agency accountable for its decisions. Table 5 lists the selection indicators included in MCC's annual country scorecards.

MCC Effect

MCC's approach to selecting partners encourages countries — and not just MCC partner countries — to improve their economic and social policies before MCC invests a single dollar. This is sometimes called the "MCC Effect." MCC sees this when government and civil society groups contact MCC or indicator institutions to learn about and improve their scorecard performance.

A number of countries set up inter-ministerial committees to improve their scorecard performance and policy data. An independent global survey of development stakeholders found that they repeatedly identified MCC eligibility criteria as among the most influential external assessments of government performance. Many countries also regard their MCC scorecard performance as a stamp of approval that tells their citizens and the private sector that the country is well-governed.

Compact Development, Implementation, and Closure

Countries seeking to sign a compact with MCC must first be selected to develop a compact by MCC's

Table 5: Selection Indicators		
Indicator	**Category**	**Source**
Access to Credit Indicator	Economic Freedom	▶ International Finance Corporation
Business Start-Up Indicator	Economic Freedom	▶ International Finance Corporation
Child Health Indicator	Investing in People	▶ Columbia/Yale
Civil Liberties Indicator	Ruling Justly	▶ Freedom House
Control of Corruption Indicator	Ruling Justly	▶ World Bank/Brookings Institution
Fiscal Policy Indicator	Economic Freedom	▶ International Monetary Fund
Freedom of Information Indicator	Ruling Justly	▶ Freedom House ▶ Centre for Law and Democracy ▶ Freedom House
Gender in the Economy Indicator	Economic Freedom	▶ World Bank
Girls' Primary Education Completion Rate Indicator	Investing in People	▶ United Nations Educational, Scientific and Cultural Organization (UNESCO)
Girls' Secondary Education Enrollment Ratio Indicator	Investing in People	▶ UNESCO
Government Effectiveness Indicator	Ruling Justly	▶ World Bank/Brookings Institution
Health Expenditures Indicator	Investing in People	▶ World Health Organization (WHO)
Immunization Rates Indicator	Investing in People	▶ WHO/United Nations International Children's Emergency Fund (UNICEF)
Inflation Indicator	Economic Freedom	▶ International Monetary Fund
Land Rights and Access Indicator	Economic Freedom	▶ International Fund for Agricultural Development ▶ International Finance Corporation
Natural Resource Protection	Investing in People	▶ Columbia/Yale
Political Rights Indicator	Ruling Justly	▶ Freedom House
Primary Education Expenditures Indicator	Investing in People	▶ UNESCO
Regulatory Quality Indicator	Economic Freedom	▶ World Bank/Brookings Institution
Rule of Law Indicator	Ruling Justly	▶ World Bank/Brookings Institution
Trade Policy Indicator	Economic Freedom	▶ The Heritage Foundation

Board of Directors based on the process described above and the indicator criteria identified in Table 5. Several principles are key to ensuring countries develop successful compact proposals. Eligible countries should demonstrate **country ownership and commitment** by providing leadership, mobilizing resources, and engaging broad groups of stakeholders and potential beneficiaries throughout the compact development process. Countries should directly address constraints to poverty-reducing **economic growth,** even when doing so may involve difficult public policy decisions. Compact programs should be based upon **strong program logic** that clearly ties proposed projects to measurable results and **high economic returns,** as demonstrated by increased incomes for beneficiaries. Well-developed compact programs also have **manageable technical, financial, environmental, and social risks** and allow for **timely implementation** within a fixed, five-year term, given each country's own oversight and management capacities.

To develop a compact program, countries typically follow a process that includes five phases. During Phase One, the country works closely with MCC on a preliminary analysis of the constraints to its economic growth and poverty reduction. During Phase Two, the country identifies the root causes behind the most binding constraints, establishes clear program objectives, and begins to develop program logic. In Phase Three, the country proposes specific investment projects to address one or more of the binding constraints and achieve program objectives. The most promising projects are further developed and appraised during Phase Four. MCC and the country agree on the terms of the proposed program, sign the compact, and prepare for the compact to enter into force. Once a compact enters into force, the five-year implementation period (Phase Five) begins.

Compact implementation is governed by the terms and conditions of each compact and the related program implementation agreement, as well as MCC policies and guidelines. The compact and program implementation agreement generally include a description of the program, including all projects, activities, and their associated objectives; the overall grant amount, project allocations, and a multi-year financial plan for the program; the obligations and responsibilities of the partner country, including any conditions precedent to the disbursement of compact funding; implementation and oversight structure and responsibilities, including designation of the partner country's accountable entity as responsible for program administration and oversight; a description of the M&E approach, including a summary of indicators and related targets; and required MCC approvals and associated fiscal and procurement controls.

MCC also maintains guidance to ensure the orderly and efficient closure of compacts at the end of their five-year term. The closure process starts with the development of a concise program closure plan by the partner country's accountable entity, which describes the closure strategy for each project and activity, the wind-up or continuation of the accountable entity, and other important aspects required to close out program activities. While the content of such closure plans varies by country, project, and activity, all plans must include the components outlined in MCC's *Program Closure Guidelines,* and must be approved by MCC. All compact programs formally close within 120 days following the final day of the compact's five-year term.

Looking Forward

New Compacts and Threshold Programs

In FY 2017, MCC signed two new programs and the MCC Board of Directors approved two new compacts. In addition, two compacts entered into force, a key milestone that starts the five-year implementation timeline. Each of these programs will initiate new activities and remain a focus in FY 2018.

First, MCC and the Government of Nepal signed a $500 million compact in September 2017. The Government of Nepal is contributing an additional $130 million, which represents the largest upfront commitment by any MCC partner country. The five-year compact with Nepal is designed to increase the availability of electricity and lower the cost of transportation, and combines infrastructure investments with technical assistance to improve the capacity of sector institutions. Specifically, the investment will add critical electricity transmission capacity and strengthen Nepal's road maintenance regime. The Nepal program also represents the culmination of MCC's efforts to forge a strategic partnership with India, as directed by MCC's

Board of Directors when Nepal was first selected in December 2014. Planned compact investments are designed to help realize a long-imagined regional energy market — benefiting both Nepal and India through infrastructure to enable electricity trading. These investments are expected to benefit approximately 23 million people throughout Nepal.

In addition, in September 2017 MCC and the Government of Kosovo signed a $49 million threshold program. MCC's investment in Kosovo will be composed of two projects: the Reliable Energy Landscape Project and the Transparent and Accountable Governance Project. The Reliable Energy Landscape Project will support Kosovo to implement policies to incentivize household adoption of energy efficiency measures and encourage independent power producers to enter the market. The Transparent and Accountable Governance Project will make data and information available to the public, allowing for thoughtful and productive interaction with that information, and encourage data-driven decision making by the government.

At MCC's quarterly Board meeting in September 2017, MCC's Board of Directors approved a $524 million compact for Cote d'Ivoire. MCC's investment will be supplemented by an additional $22 million contribution from the Government of Cote d'Ivoire. The five-year compact is designed to reduce poverty and diversify Cote d'Ivoire's economy to achieve long-term inclusive growth. The compact is composed of a project that will increase the supply of skilled workers to meet private sector demand as well as a project to improve the mobility of goods and people in Cote d'Ivoire's economic hub, Abidjan. The projects are underpinned by key institutional and policy reforms in the education and transportation sectors, and structured to leverage private and donor investment. The compact is expected to benefit nearly 11 million people over 20 years.

In addition to these three new programs, two new compacts entered into force in FY 2017. Specifically, MCC's $450 million Morocco Employability and Land Compact entered into force on June 30, 2017. This five-year compact addresses two binding constraints to economic growth and investment in Morocco: education quality and land policy and implementation. The compact is expected to benefit over 825,000 people over a 20 year period.

Also, on June 22, 2017, the Benin Power Compact entered into force. Signed in September 2015, the $375 million compact seeks to unlock private investment by supporting policy reform and investing in electricity generation, distribution, and off-grid electrification. To achieve this milestone, the Government of Benin adopted several critical reforms, including an electricity sector master plan and steps to ensure professional staffing and sustainable financing for the sector. These measures were conditions precedent to entry into force and will contribute to the financial health, operational independence, and governance of the national electricity utility — critical for compact sustainability.

Looking forward, MCC expects to bring three compacts (Mongolia, Senegal and Sri Lanka) and two threshold programs (Togo and Timor-Leste) to the Board of Directors for approval during FY 2018.

Concurrent Compacts/Regional Investments

MCC continues to seek authorization to enter into concurrent compacts in order to maximize the economic impact of its work through cross-border, regional investments. After more than 13 years of successfully delivering large, complex infrastructure projects coupled with supporting difficult policy reforms in partner countries, MCC is well-positioned to increase the impact of its investments by focusing regionally.

On April 25, 2017, Senator Cardin (D-MD), Senator Coons (D-DE) and Senator Isakson (R-GA), introduced the African Growth and Opportunity Act (AGOA) and Millennium Challenge Act Modernization Act (S.832). This bill gives MCC increased flexibility to promote regional trade, collaboration, and economic growth by authorizing MCC to enter into two concurrent compacts with an eligible country. The bill would also allow MCC to extend the term of any private sector Board member for one additional year beyond his or her appointment or reappointment, until a replacement has been confirmed by the U.S. Senate. On July 27, 2017, House Foreign Affairs Committee Chairman Ed Royce (R-CA), Ranking Member Eliot Engel (D-NY) and Representatives Chris Smith (R-NJ) and Karen Bass (D-CA), introduced an identical version of the bill in the House of Representatives (H.R. 3445). Since introduction in both chambers, the AGOA and Millennium Challenge Act Modernization Act has passed the Senate Foreign Relations Committee and the House Foreign Affairs Committee. MCC now awaits a final floor vote in both the full House and full Senate of the 115th Congress.

Upon passage of the AGOA and Millennium Challenge Act Modernization Act, MCC will be able to simultaneously research and work with multiple eligible countries in a region to identify, negotiate, and eventually fund investments that would have a positive economic impact for each country involved as well as the region. By making coordinated investments across multiple countries to expand infrastructure, MCC will be able to help partners work together to build and grow regional markets, facilitate trade, and foster greater impact through economies of scale. This, in turn, will help generate new business and market opportunities for U.S. and other companies by making it cheaper, easier, and faster for businesses to get their products to new, emerging regional markets.

The authority MCC is seeking would allow the agency to maintain its focused, data-driven model for country and project selection. Projects would still be required to undergo a rigorous economic analysis and have an economic rate of return that ensures the program logic is geared toward a measurable impact on poverty. Regional investments will employ MCC's local implementation and accountability, allowing for multiple bilateral compacts to be knitted together into a regional project. Concurrent compact authority will allow MCC to develop regional projects while still adhering to the agency's important country-owned processes that demand accountability and the core elements of MCC's operational model to produce high returns on investments.

Operational Efficiency and Effectiveness

In FY 2017, MCC undertook a deliberate planning process to develop an agency reform plan, consistent with Executive Order 13781, *Comprehensive Plan for Reorganizing the Executive Branch,* and subsequent OMB guidance, including Memorandum M-17-22. The agency reform plan includes specific measures to improve the efficiency, effectiveness, and accountability of MCC in achieving its mission of reducing poverty through economic growth.

In FY 2018, MCC will begin implementation of several components in the agency reform plan aimed at increasing operational efficiency and effectiveness, resulting in direct cost savings, greater productivity of MCC staff, and improved outcomes from MCC investments. These components include, but are not limited to:

- Introduction of the Star Report business process, which will decrease internal reporting burdens and ensure that MCC systematically collects, validates, and memorializes critical information for every compact and threshold program at key decision points in program development and at each quarter of implementation.
- Implementation of a contract lifecycle management system to improve workflow and reduce risks. MCC's 10-year savings from this new system is approximately $1.7 million and the system is estimated to save approximately two to three days in processing time for a typical action.
- Implementation of selected, staff-generated proposals designed to identify efficiencies in the compact and threshold program development processes in order to shorten the development timeline without reducing quality and consistent with MCC's investment criteria.
- Implementation of a knowledge management action plan, including staff-driven, near-term priorities, IT infrastructure, and critical behavioral changes based on organizational needs and feedback received.

- Continued implementation of a new budget framework to improve internal oversight of MCC's limited resources while improving transparency and accountability throughout the agency. Implementation activities for the Integrated Planning, Budgeting, and Execution (IPBE) system began in FY 2017. This framework will position MCC to capitalize on the best use of limited funding through the integration of budget formulation and execution exercises, focusing on analysis and availability of funds as strategy and funding decisions are made, as well as support MCC's external budget requests.

Engaging U.S. Businesses

From its creation, MCC has promoted participation by U.S. firms in MCC-funded procurements overseas. As a result of this outreach and the open, competitive process outlined in the *Program Procurement Guidelines,* U.S. firms win 67 percent of procurements when participating. Building on this base, since late 2016, MCC has further ramped up its outreach to prospective U.S. bidders through enhanced collaboration with the Department of Commerce, U.S. Trade and Development Agency (USTDA), World Bank, U.S. Chamber of Commerce, U.S. Department of State, and others. In addition, MCC has continued holding one-on-one meetings and seminars with U.S. firms that are doing business in MCC partner countries or are interested in exploring these opportunities. MCC utilizes these forums to provide clarification on the procurement procedures as well as help U.S. firms connect with potential local partners. During this period, MCC has also strengthened its procurement procedures to include "best value procurements" and "total cost of ownership" in the evaluation criteria. These improved procedures will support selection of U.S. firms that bring a higher value to partner countries.

MCC has developed and is currently implementing a detailed market outreach plan to inform, attract, and further encourage U.S. firms to work with MCC overseas. The market outreach plan includes the promotion of MCC country counterpart procurements, as well as showcasing opportunities for U.S. business to invest following MCC compacts, and partner with MCC through co-investment, joint research, knowledge sharing, and program co-design. This plan includes a new "Work With Us" page on MCC's website; providing a 12-month forecast of upcoming procurement and grant opportunities; identifying specific procurement and partnership opportunities particularly suitable for U.S. firms and targeting outreach efforts to these firms; soliciting feedback from U.S. firms on barriers to participation, and addressing these obstacles; active promotion to prospective bidders and partners on the advantages of working on MCC-funded projects, such as the full commitment of funding upfront and direct payment from the U.S. Treasury; facilitating joint-ventures between U.S. and local firms through partnership platforms; and incorporating webinars for pre-bid meetings and electronic submissions to reduce the cost of doing business with MCC.

MCC is actively working with the U.S. Department of Commerce's Advocacy Centers to reach their network of U.S. firms. Multiple presentations and meetings have been undertaken and planned, including engagements between the senior managers of MCC with those of the U.S. Department of Commerce and the U.S. Department of State. MCC also continues to actively engage the MCC Advisory Council, which was established under the Federal Advisory Committee Act and launched in 2016. The council is comprised of 25 individuals from across the private sector with diverse technical expertise in infrastructure, information and communications technology, manufacturing, finance, and sustainable development. The council is charged with providing MCC operational advice and insight on innovations in infrastructure, technology, and sustainability; perceived risks and opportunities in MCC partner countries; and new financing mechanisms.

Analysis of MCC's Financial Statements

Financial Discussion and Analysis

At the end of FY 2017, MCC prepared four basic financial statements with accompanying notes and presented them to the USAID 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 (SBR).

Balance Sheet

The Balance Sheet is a representation of MCC's financial condition at the end of the FY. It shows the resources available to meet its statutory requirements (assets); the amounts it owes that will require payment from available resources (liabilities); and the difference between assets and liabilities (MCC's net position).

Assets

As of September 30, 2017, MCC held total assets of $5.1 billion compared to $4.9 billion reported in FY 2016. The majority of MCC's assets (98 percent) are held in its Fund Balance with Treasury (FBWT), which increased by $188 million due to differences in Appropriations Received and Gross Outlays.

Other assets, which reflect only 2 percent of MCC's total assets, include Advances, Property, Plant and Equipment (PP&E), and Accounts Receivable. Advances (Intragovernmental) decreased by $3 million due primarily to intragovernmental advances with the Department of Transportation for the countries of Liberia, Nepal, Cote d'Ivoire, and Guatemala; the Department of Treasury (Office of Technical Assistance) for the countries of Guatemala and Honduras; and USAID for the country of Morocco. 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 capitalize its leases. Further, MCC has set capitalization thresholds at $200 thousand for IT equipment, $500 thousand for internal use software, and $50 thousand for other fixed assets. In FY 2017, MCC capitalized development costs of $10.3 million associated with the development of internal software. In FY 2016, MCC relocated its headquarters to Franklin Court, and as of September 30, 2016, had capitalized $11 million in General PP&E related to Leasehold Improvements such as build-out, engineering, construction, and furniture costs.

Liabilities

As of September 30, 2017, MCC had $108 million in liabilities, which represents amounts owed to grantees, vendors, contractors, trading partners, and employees. Grant liabilities comprise $86 million, or nearly 80 percent of MCC's total liabilities. Grant liabilities and retentions increased by $2 million and $25 million, respectively, primarily due to increases in retentions for compacts in Malawi and Indonesia.

Net Position

MCC's overall net position as of September 30, 2017, was $5.0 billion, an increase of $164 million, over 3 percent, from FY 2016. The available appropriations reported in MCC's positive net position represent the resources necessary to fund future compacts.

Statement of Net Cost

This statement shows MCC's net cost of operations by major program or appropriation fund categories. Table 6 describes each program.

During FY 2017, MCC incurred $747 million in net program costs, allocated among MCC's six active programs. Table 7 shows the percentage of FY 2017 net costs by program. Net program costs increased by $144 million, or 24 percent, from FY 2016 due to a net increase in compact program costs.

Statement of Changes in Net Position

This statement shows the change in net position during the reporting period. MCC's net position on September 30, 2017, was $5.0 billion, an increase of $164 million from September 30, 2016. Net position is affected by changes to its two components: Cumulative Results of Operations and Unexpended Appropriations. As of September 30, 2017, Cumulative Results of Operations amounted to $9.6 million, an increase of $7.1 million from September 30, 2016. This balance is the cumulative difference, for all previous FYs, between funds available to MCC from all financing sources and the net costs incurred. The second component of net position, Total Unexpended Appropriations, amounted to $4.9 billion, an increase of $157 million, or 3 percent, from FY 2016.

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 the entity's budgetary general ledger in accordance with Federal accounting rules. The SBR 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, 2017.

For FY 2017, MCC reported total budgetary resources of $3.3 billion compared to $3.3 billion in FY 2016. Budgetary resources of $905 million were provided through FY 2017 appropriations and $2.3 billion were carried forward from appropriations in FY 2016 and prior years.

Table 6. MCC Fund Categories

Fund	Source and Purpose
Compact	Funds appropriated 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 (CIF) when it signs a compact to speed compact implementation by the partner country.
609(g)	Funds appropriated 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)	Funds appropriated 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 MCC 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 Program	Funds appropriated by Congress, apportioned by OMB, and used by MCC to help countries become eligible for MCC compact assistance.
Due Diligence	Funds appropriated by Congress, apportioned by OMB, and used by MCC to cover costs associated with assessing compact proposal 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.

Table 7. MCC Net Program Costs (Dollars in Thousands)

Program	FY 2017	FY 2016	% Change	Reason for Change
Compact	$ 554,320	$ 428,348	29%	The $126 million increase was primarily the result of an increase in expenditures for the Indonesia, Malawi, and Zambia compacts as they entered into years four and five of their compact lifecycles.
609(g)	17,537	11,214	56%	The $6.3 million increase was primarily the result of increased expenditures for the Nepal and Ghana II 609(g) programs as they entered into the compact stage.
Threshold	7,594	3,776	101%	The $3.8 million increase was primarily the result of increases in expenses for the countries of Honduras and Guatemala.
Due Diligence	56,627	47,278	20%	The $9.3 million increase was primarily due to an increase in program costs associated with infrastructure projects in Cote d'Ivoire, Indonesia, the Philippines, and Nepal.
Audit	4,210	3,369	25%	The $0.8 million increase was due primarily to an increase in external contract expenses incurred by the USAID OIG.
Administrative	106,313	108,714	–2%	The $2.4 million decrease was due to a reduction in external contract expenses and capitalization costs related to the development of internal use software offset by an increase personnel costs.
TOTAL	$ 746,601	$ 602,699		

Analysis of MCC's Systems, Controls, and Legal Compliance

Systems

MCC's financial management systems strategy employs the use of a shared service provider (SSP) to achieve its financial and budget management goals. MCC has benefited from the economies of scale provided by the SSP strategy since its inception in 2004 and plans to continue utilizing the SSP for the foreseeable future. If MCC elected to change this strategy, system changes and implementation require approval from MCC IT Investment Review Board (IT-IRB). The IT-IRB provides executive decision-making on, and oversight of, MCC IT investment planning and management to ensure compliance with statutory and regulatory direction from Congress, OMB, and other applicable Federal oversight entities. Currently, the Interior Business Center (IBC), operated by the Department of the Interior, is MCC's SSP for financial and payroll management systems. IBC maintains and operates the following systems on MCC's behalf:

- **Oracle Federal Financials (OFF)** — the system of record for MCC's Financial Statements and Notes. The system processes financial and budgetary transactions. OFF is also the main system of record for USAspending.gov reporting compliant with the Digital Accountability and Transparency Act of 2014 (DATA Act) and OMB Memorandum M-15-12, Increasing Transparency of Federal Spending by Making Federal Spending Data Accessible, Searchable, and Reliable.
- **Federal Personnel Payroll System (FPPS)** — Provides support for the full lifecycle of personnel and payroll transactions. FPPS is integrated with OFF to account for payroll transactions.

MCC is responsible for overseeing IBC to ensure that the SSP complies with pertinent federal financial management system and internal control requirements applicable to those systems used for MCC's financial transaction processing and reporting.

MCC management is responsible for complying with federal requirements for its financial management operations, systems, controls and reporting. The American Institute of Certified Public Accountants (AICPA) Statements on Standards for Attestation Engagements (SSAE) No. 18 prescribes requirements for assessing SSPs. MCC obtains the SSAE 18 Report for both IBC administered systems, and reviews it for observations and risks which may require risk mitigation and compensating controls. Additionally, MCC verifies that complementary end user controls are in place and operating effectively based on the reports. MCC believes its financial management systems strategy achieves compliance with OMB Circular A-123, Appendix D, *Compliance with the Federal Financial Management Improvement Act of 1996.*

Controls

On an annual basis, MCC assesses the vulnerability of its programs and systems in alignment with the Federal Managers' Financial Integrity Act of 1982 (FMFIA) and its implementing guidance, OMB Circular No. A-123, *Management's Responsibility for Enterprise Risk Management and Internal Control,* as well as the associated guidelines issued by the CFO Council. OMB Circular No. A-123, Appendix A, *Internal Control over 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 reporting. OMB Circular A-123 Appendix A allows for modified implementation to fit the circumstances, conditions, and structure of each entity. During FY 2017, MCC continued its efforts to reassess, improve, and enhance its financial, systems, program, and performance information.

Management Assurances

CEO Assurance Statement

Millennium
Challenge Corporation
United States of America

November 13, 2017

FY 2017 Assurance Statement from the CEO

The Millennium Challenge Corporation's (MCC) 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 risk and internal control, and compliance with applicable laws and regulations in accordance with Office of Management and Budget (OMB) Circular Number A-123, *Management's Responsibility for Enterprise Risk Management (ERM) and Internal Control.*

Reporting Pursuant to FMFIA Section 2

- **Overall Statement of Assurance**
  Based on the results of its assessment, MCC can provide unmodified reasonable assurance that internal controls over operations, reporting, and compliance were operating effectively as of September 30, 2017.
- **OMB Circular A-123, Appendix A: Internal Control over Reporting**
  In accordance with Appendix A of OMB Circular A-123, MCC conducted its assessment of the effectiveness of internal control over reporting, which included the safeguarding of assets and compliance with applicable laws and regulations. Based on the results of this assessment, we can provide unmodified reasonable assurance that MCC's internal control over reporting was designed and operating effectively as of September 30, 2017. Accordingly, the assessment did not identify any material weaknesses in the design or operation of the controls.

Reporting Pursuant to FMFIA Section 4

The Federal Financial Management Improvement Act of 1996 (FFMIA) was designed to advance federal financial management by ensuring that federal financial management systems provide accurate, reliable, and timely financial management information to the government's managers. Compliance with the FFMIA provides the basis for the continuing use of reliable financial management information by program managers, as well as by the President, Congress, and public. The FFMIA requires agencies to have financial management systems that comply substantially with federal financial management system requirements, applicable federal accounting standards, and the application of the U.S. Government Standard General Ledger (USSGL) at the transaction level.

The vulnerability of MCC programs and systems was assessed in accordance with FMFIA and OMB guidance. Based on the results of the OMB Circular A-123 assessment, MCC has determined that our financial management systems comply with financial management system requirements and are in substantial conformance with the Section 4 (Financial Systems) requirements of FMFIA as of September 30, 2017.

Sincerely,

Jonathan G. Nash
Acting Chief Executive Officer, Millennium Challenge Corporation

Statement of Assurance from Service Provider

United States Department of the Interior
INTERIOR BUSINESS CENTER
Washington, DC 20240

October 3, 2017

Dear IBC Oracle Customer:

The purpose of this letter is to provide assurance that the Oracle Federal financial application controls remained unchanged for the period August 1, 2017, through September 30, 2017.

You were previously notified that KPMG LLP examined the description of the Oracle financial application controls at the Department of the Interior (Department), Interior Business Center (IBC). The results of their review and analysis were provided in a Service Organization Control Report (SSAE18) covering the period July 1, 2016, through July 31, 2017. A softcopy version of the report provided to at the beginning of September, 2017.

The SSAE 18 review was conducted for the purpose of expressing an opinion as to whether (1) IBC's description of the Oracle Federal 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 July 31, 2017. 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 Federal financial application controls at the IBC for the period August 1, 2017, through September 30, 2017. This time period was not covered by the SSAE 18 examination report previously provided. To the best of my 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 July 31, 2017, did not change for the period of August 1, 2017, through September 30, 2017. The description of controls in the FY 2017 SSAE 18 examination report presents fairly the aspects of IBC controls that were in place as of September 30, 2017.

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, 2017. 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, 2017. As a result, the IBC continues to assert substantial compliance with financial accounting and reporting controls in place from July 1, 2017, through September 30, 2017.

If you have any questions on this assurance statement, please contact Margaret Treadway, Chief Enterprise Support Office, Margaret_Treadway@ibc.doi.gov or 202-256-3079.

Sincerely,

Donna L. Edsall, CPA Associate Director
Financial Management Directorate Interior Business Center

Legal Compliance

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

Prompt Payment Act

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 latter 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 for all payments subject to the Prompt Payment Final Rule. In FY 2017, MCC's prompt payment performance was 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 Bureau of the Fiscal Service past due, legally enforceable, non-tax debts that are more than 180 days delinquent. During FY 2017, MCC referred no debt to the Department of the Treasury.

Federal Information Security Modernization Act (FISMA) of 2014

In FY 2017, MCC continued to make progress towards compliance with Homeland Security Presidential Directive 12 (HSPD-12), by using Personal Identity Verification (PIV) cards for logical identification and authentication to the MCC Network. In addition, MCC contractors are transitioning to PIV compliant badges, which will enable full compliance to HSPD-12. MCC expects full compliance in FY 2018. In addition, MCC has instituted advanced security enhancements that prevent unauthorized software applications from executing on the network. This security control is above the recommendation for moderate-impact systems issued by the National Institute of Standards and Technology (NIST) in Special Publication (SP) 800-53, Revision 4, *Security and Privacy Controls for Federal Information Systems and Organizations.*

Digital Accountability and Transparency Act of 2014

Congress enacted the DATA Act to further transparency in USG spending. The DATA Act builds on the Federal Funding Accountability and Transparency Act of 2006 (FFATA) as amended by the Government Funding Transparency Act of 2008. It requires agencies to disclose direct Federal agency expenditures and link Federal contract, loan, and grant spending information to agency programs. Additionally, it establishes government-wide data definition standards to make spending data consistent and reliable throughout the USG, and improve the data reported by Federal agencies under FFATA. The law aligns with OMB Memorandum M-10-06, issued on December 8, 2009, to increase transparency and create a more data-driven Federal Government. The USAID OIG audited MCC's DATA Act initiative and reported no recommendations in its report titled, "MCC Took Initial Steps to Implement the Digital Accountability and Transparency Act of 2014." MCC strives to comply with all facets of the DATA Act and will continue to make improvements based on recommendations and new requirements.

Limitations of the Financial Statements

The principal financial statements have been prepared to report the financial position and results of operations of MCC, 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 Circular A-136, 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 financial statements should be read with the understanding that they are for a component of the USG, a sovereign entity.

Financial Section

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

November 15, 2017

On behalf of the Millennium Challenge Corporation (MCC), I am pleased to present the results of operations for the fiscal year (FY) ended September 30, 2017. The agency had an exciting year with entry into force of the Benin Power Compact, the Morocco Employability and Land Compact, and the Kosovo Threshold Program. MCC also signed a $500 million compact with the Federal Democratic Republic of Nepal to increase the availability of electricity and lower the cost of transportation. In FY 2017 MCC obligated $1.002 billion, increasing cumulative investments worldwide to more than $11 billion across 34 compacts and 27 threshold programs since inception. We also disbursed $717 million this fiscal year through investments in 12 active compacts and four active threshold programs.

In line with MCC's strategic focus to increase agency-wide efficiency, we introduced a new budget framework called the Integrated Planning, Budgeting, and Execution (IPBE) system. The IPBE system aims to improve budget policies, processes, and procedures in alignment with the federal budget process. The new system will improve MCC's fiscal stewardship by providing senior leaders and staff with relevant data, processes, and systems to manage more strategically the agency's resources, as well as improving the accuracy and efficiency of MCC's budget formulation and execution.

In FY 2018, the agency has signed a compact with Côte d'Ivoire and will oversee implementation of that compact and 12 others, three of which — those with Cabo Verde, Indonesia, and Malawi — will close out during the fiscal year. MCC is developing compact programs with Burkina Faso, Lesotho, Mongolia, Philippines, Senegal, Sri Lanka, and Tunisia. MCC is also developing threshold programs with Timor-Leste and Togo. MCC will continue implementation oversight of four threshold programs. In addition, MCC will launch program development with any new compact and threshold partner countries selected by the MCC Board in December 2017.

MCC's transparent decision-making and evaluation processes are often cited as an example for both domestic and international development agencies. For the second year in a row, MCC was recognized as the leader for data-driven, transparent investments in the "Federal Invest in What Works Index," published by Results for America. MCC is focused on strategic oversight, operating with a light footprint in country to reduce the expense of large country missions. This country-led process has the added benefits of building the capacity of our partner countries, as well as ensuring greater relevancy and accountability for our projects.

We are pleased to report that MCC received an unmodified opinion on the FY 2017 financial statements. The auditor's "Report on Internal Controls over Financial Reporting" identified two significant deficiencies and eight recommendations. We have resolved four of the auditor's eight recommendations issued in FY 2016 and plan to resolve the remaining during FY 2018. At MCC, we will continue to prioritize financial management as a mission-critical support activity to ensure the agency can continue to stimulate economic growth and reduce poverty worldwide.

Mahmoud Bah
Acting Vice President and Chief Financial Officer
Department of Administration and Finance

Financial Statements

The principal financial statements have been prepared to report the financial position and the results of operations of MCC. The financial statements have been prepared from MCC's books and records in accordance with formats prescribed in OMB Circular No. A-136, *Financial Reporting Requirements* (revised on August 15, 2017). The financial statements should be read with the understanding that they are for a component of the USG, a sovereign entity. Comparative data for September 30, 2017 and September 30, 2016 has been included. MCC is presenting the following financial statements and notes to the financial statements:

- Balance Sheet
- Statement of Net Cost
- Statement of Changes in Net Position
- Statement of Budgetary Resources
- Notes to the Financial Statements

Note that totals may vary slightly due to rounding.

Balance Sheet

As of September 30, 2017 and September 30, 2016 (in thousands)		
Assets	**FY 2017**	**FY 2016**
Intragovernmental:		
Fund Balance with Treasury *(Note 2)*	$ 4,973,783	$ 4,785,540
Advances *(Note 3)*	6,461	9,651
Total Intragovernmental	**4,980,244**	**4,795,191**
Accounts Receivable, Net *(Note 4)*	378	470
General Property, Plant, and Equipment, Net *(Note 5)*	20,580	11,147
Advances *(Note 3)*	61,025	62,026
Total Assets	**$ 5,062,227**	**$ 4,868,834**
Liabilities		
Intragovernmental:		
Accounts Payable	$ 398	$ 617
Other Liabilities	537	455
Total Intragovernmental	**935**	**1,072**
Accounts Payable	7,465	7,979
Accrual — Grant Liabilities *(Note 7)*	85,956	58,614
Other Liabilities *(Note 8)*	13,512	10,884
Total Liabilities *(Note 10)*	**$ 107,868**	**$ 78,549**
Commitments and contingencies *(Note 9)*		
Net Position		
Unexpended Appropriations — All Other Funds	$ 4,944,802	$ 4,787,823
Cumulative Results of Operations — All Other Funds	9,557	2,462
Total Net Position	**$ 4,954,359**	**$ 4,790,285**
Total Liabilities and Net Position	**$ 5,062,227**	**$ 4,868,834**

The accompanying notes are an integral part of these statements.

Statement of Net Cost

For the Years Ended September 30, 2017 and September 30, 2016 (in thousands)		
Program Costs *(Note 12)*	**FY 2017**	**FY 2016**
Compact Program Costs	$ 554,320	$ 428,348
609 (g) Program Costs	17,537	11,214
Threshold Program Costs	7,594	3,776
Due Diligence Program Costs	56,627	47,278
Audit Costs	4,210	3,369
Administrative Costs	106,313	108,714
Net Cost of Operations	**$ 746,601**	**$ 602,699**

The accompanying notes are an integral part of these statements.

Statement of Changes in Net Position

For the Years Ended September 30, 2017 and September 30, 2016 (in thousands)	FY 2017	FY 2016
Cumulative Results of Operations:		
Beginning Balances	$ 2,462	$ (3,976)
Corrections of Errors	3,902	—
Beginning Balances, as adjusted	6,364	(3,976)
Budgetary Financing Sources:		
Appropriations Used	748,021	606,968
Other Financing Sources:		
Donations and Forfeitures of Property *(Note 10)*	292	348
Imputed Financing	1,481	1,821
Total Financing Sources	**749,794**	**609,137**
Net Cost of Operations	**(746,601)**	**(602,699)**
Net Change	**3,193**	**6,438**
Cumulative Results of Operations	**9,557**	**2,462**
Unexpended Appropriations:		
Beginning Balance	4,787,823	4,493,791
Budgetary Financing Sources:		
Appropriations Received	905,000	901,000
Appropriations Used	(748,021)	(606,968)
Total Budgetary Financing Sources	**156,979**	**294,032**
Total Unexpended Appropriations	**4,944,802**	**4,787,823**
Net Position	**$ 4,954,359**	**$ 4,790,285**

The accompanying notes are an integral part of these statements.

Combined Statement of Budgetary Resources

For the Years Ended September 30, 2017 and September 30, 2016 (in thousands)	FY 2017	FY 2016
Budgetary Resources:		
Unobligated Balance Brought Forward, October 1	$ 2,258,582	$ 2,311,459
Recoveries of Unpaid Prior Year Obligations	93,350	85,915
Other Changes in Unobligated Balance	127	—
Unobligated Balance from Prior Year Budget Authority, Net	2,352,059	2,397,374
Appropriations (discretionary and mandatory)	905,000	901,000
Total Budgetary Resources	**$ 3,257,059**	**$ 3,298,374**
Status of Budgetary Resources:		
New Obligations and Upward Adjustments (Total)	$ 1,095,124	$ 1,039,792
Unobligated Balance, End of Year:		
Apportioned, unexpired accounts	2,152,203	2,225,327
Unapportioned, unexpired accounts	9,732	33,255
Unexpired unobligated balance, end of year	2,161,925	2,258,582
Unobligated Balance, End of Year (Total)	2,161,935	2,258,582
Total Budgetary Resources	**$ 3,257,059**	**$ 3,298,374**
Change in Obligated Balance:		
Unpaid obligations:		
Unpaid obligations, brought forward, October 1	$ 2,526,949	$ 2,288,851
New obligations and upward adjustments	1,095,124	1,039,792
Outlays (gross)	(716,917)	(715,779)
Recoveries of prior year unpaid obligations	(93,350)	(85,915)
Unpaid obligations, end of year	**$ 2,811,806**	**$ 2,526,949**
Memorandum entries:		
Obligated Balance, Start of Year	**$ 2,526,949**	**$ 2,288,851**
Obligated Balance, End of Year	**$ 2,811,806**	**$ 2,526,949**
Budget Authority and Outlays, Net:		
Budget Authority, Gross (discretionary and mandatory)	$ 905,000	$ 901,000
Actual Offsetting Collections (discretionary and mandatory)	(127)	—
Recoveries of Prior Year Paid Obligations (discretionary and mandatory)	127	—
Budget Authority, Net (Total) (discretionary and mandatory)	**$ 905,000**	**$ 901,000**
Outlays, Gross (discretionary and mandatory)	$ 716,917	$ 715,779
Actual Offsetting Collections (discretionary and mandatory)	(127)	—
Outlays, Net (Total) (discretionary and mandatory)	**$ 716,790**	**$ 715,779**

The accompanying notes are an integral part of these statements.

Notes to the Financial Statements

Note 1 — Summary of Significant Accounting Policies

A. Reporting Entity

The Millennium Challenge Act of 2003, 22 U.S.C. 7701-7718, established MCC as a wholly-owned Government corporation, as defined by the Government Corporation Control Act of 1945. 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, five-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 U.S. 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 USAID 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 GAAP in the U.S. and accounting standards issued by the Federal Accounting Standards Advisory Board (FASAB) in the format prescribed by OMB Circular No. A-136, *Financial Reporting Requirements,* as amended. FASAB is recognized by the AICPA as the official accounting standards-setting body for USG 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 CFO Act of 1990, the Government Management Reform Act of 1994, and the Government Corporation Control Act (31 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 SBR is prepared in accordance with budgetary accounting rules.

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.

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 assets and 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. The assumptions made and estimates used by MCC management to prepare the financial statements are based upon the facts that exist when the statements are prepared, and on various other assumptions that are believed to be reasonable under the circumstances. Changes in estimates are reflected in the period in which they become known. Actual results may differ from those estimates. The Notes to the Financial Statements include information to assist the reader in understanding the effect of changes in assumptions on the related information.

The most significant estimates are a result of the accrued expenses recorded by MCC for grant liability incurred by MCAs. The majority of those liabilities are related to large infrastructure project and quantity estimates made on works performed but not yet invoiced as of the end of the FY. Due to the nature of the infrastructure contracts, the variability in quantities estimated or projected may differ from actual quantities billed through interim or final invoicing.

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 FY 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.

F. Accrual — Grant Liabilities

Grant accrual liabilities represent the carrying value of obligations assumed by MCC for works, goods, and services performed/rendered/delivered but not yet invoiced through the Balance Sheet date. MCC's partner countries, through their respective accountable entities, are allocated a spending authority each quarter or as appropriate. A spending authority for a given period is the portion of the compact or threshold that MCC authorized, approved, and made available to MCAs for current and past works, goods, and services incurred/delivered/received and for which MCAs can request disbursement in a given quarter. Unused spending authority is the difference between the authorized and approved spending authority and the actual disbursements in a given period.

MCC's grant accrual methodology assumes that "unused spending authority" in a given period represents the upper limit of the accrual calculation and that invoices on hand at the end of a given period (MCA in-house invoices) represents the lower limit of the accrual calculation. In arriving at a reasonable estimate of the MCAs' accrued liabilities using information available at the time of the calculation, MCC discounts the unused spending authority by using a rolling average of actual disbursements to calculate the grant accrual liabilities. When better information is available from MCAs on accrued liabilities, MCC relies on such information in arriving at the best estimate.

MCA large infrastructure projects are structured to include retentions on invoices. The contract retentions represent a percentage of invoice amounts retained by the MCAs as a guarantee for completion of works contractually agreed upon. The contract retentions are for works completed and, as such, are owed to the contractor contingent upon the fulfillment of specific requirements stipulated in the relevant contracts. MCAs do not release the retentions or request MCC payment for the retentions until the MCAs have verified the contractor has met all the requirements and obligations under the contract. MCC recognizes MCA contract retentions as part of the grant accrual liabilities.

G. Fund Balance with Treasury

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

H. Advances

MCC makes funding available to Federal agencies, MCAs, and local vendors. Federal agencies are funded through IAAs. MCAs are funded either directly through a local bank account called the permitted account, or indirectly through vendor advance payments in accordance with the compact agreement. The provision of such funding is mainly to address cash flow flexibility for operating and administrative costs, to leverage better foreign exchange translation for the MCAs, or to meet contractual requirements of MCAs such as mobilization of equipment on large infrastructure projects. MCC records advances as assets. The advances are liquidated or amortized as follows: the funding made available to MCAs through the local permitted account is tracked and liquidated on a monthly basis via the *Monthly Commitments and Disbursements Report* provided by the MCAs to MCC. The funding advanced to contractors or vendors (mobilization advances) is amortized via contractually agreed upon schedules.

I. Accounts Receivable, Net

Accounts receivable reflect overpayments of payroll, travel, and other MCC current and former employee expenses. Accounts receivable also reflect disallowed and sustained 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 PP&E consists of capitalized general equipment costs. MCC's capitalization threshold is $50,000 for all assets, except for 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.

MCC controls, values, and reports purchased or developed software as tangible property assets, in accordance with FASAB Statement of Federal Financial Accounting Standards (SFFAS) No. 10, *Accounting for Internal Use Software.* MCC identifies software investments as capital property for items that, in aggregate, cost $500,000 or more to purchase, develop, enhance or modify a new or existing system. Software projects that are not completed at year end and are expected to exceed the capitalization threshold are recorded as software in development. All internal use software meeting the capitalization threshold is amortized over a five-year period using the straight line half-year convention.

Leasehold improvements and furniture are depreciated using the straight-line method of depreciation over the estimated useful lives of the improvements (10 years). All other general PP&E is depreciated using the straight-line method over an estimated useful life of five 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.

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, 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, 2017 and 2016, respectively. 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 (PL) 99-335. Pursuant to this law, most USG 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 five 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 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. Liabilities Not Covered by Budgetary Resources

As of September 30, 2017 and September 30, 2016, budgetary resources have not yet been made available to fund certain liabilities reported on the Balance Sheet. Liabilities not covered by budgetary resources represent amounts for which Congressional appropriation is required and funding is generally made available in the year payments are due or anticipated. Liabilities not covered by budgetary resources include the Judgment Fund, unfunded leave, Federal Employees Compensation Act (FECA), unemployment compensation, and unamortized rent abatement liability.

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 the Department of the 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.

Unfunded 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.

Unfunded Federal Employees Compensation Act

FECA (established by PL 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 liability for workers' compensation includes any costs incurred but unbilled as of quarter end, as calculated by DOL, and not funded by current appropriations.

Unfunded Unemployment

DOL's unemployment programs provide unemployment benefits to eligible workers who become unemployed through no fault of their own, and meet certain other eligibility requirements. The Unemployment Compensation for Federal Employees program provides benefits for eligible, unemployed, former civilian Federal employees. MCC's liability for unemployment includes any costs incurred but unbilled as of quarter end, as calculated by DOL, and not funded by current appropriations.

Unamortized Rent Abatement Liability

The rent abatement represents MCC's period of free rent awarded by the lessor of the Franklin Court building. MCC maintains a 10-year operating lease for office space at Franklin Court, on which lease payments commenced in FY 2017. Per the terms of the contract, MCC was awarded approximately 15 months of rent abatement beginning on December 1, 2015. As a result of this 15 month rent abatement, and in accordance with the Financial Accounting Standards Board Accounting Standards Codification No. 842, *Leases,* MCC recorded a liability which will be amortized on a monthly basis utilizing a straight-line approach over the 10 year lease period.

O. 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.

P. Parent/Child Relationships with Other Federal Agencies

MCC is a party to allocation transfers with other Federal agencies as both a transferring (parent) entity and receiving (child) entity. Allocation transfers are legal delegations by one department of its ability to obligate budget authority and outlay funds to another department. A separate fund account (allocation account) is created in the U.S. 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 incurred by the child entity are also charged to this allocation account as they execute the delegated activity on behalf of the parent entity. Generally, 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 budget apportionments are derived. Per OMB guidance, child transfer activities are to be included and parent transfer activities are to be excluded in trial balances.

As the parent entity, MCC allocated funds to USAID. As a result, there are amounts reported in MCC's Balance Sheet, Statement of Net Cost, Statement of Changes in Net Position, and SBR for which the activity is performed by USAID acting as the child in this financial relationship. As the child entity, MCC was allocated funds from the U.S. President's Emergency Plan for AIDS Relief, Office of the U.S. Global AIDS Coordinator.

Q. 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 prepare consolidated financial statements which eliminate intragovernmental transactions.

R. Foreign currency transactions

The functional currency of the agency is United States Dollars (USD) and these financial statements are presented in that currency. Each MCC compact's budget amount is fixed and denominated in USD. The financial execution of our compacts cannot exceed the total budgeted amount. Disbursements occurring in other currencies are translated into USD and recorded in USD. The MCAs bear all currency translation risk and, as such, MCC does not record any foreign translation gain or loss in its financial statements.

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, 2017 and September 30, 2016 (in thousands)

Fund Balances	2017	2016
General Funds	$ 4,973,783	$ 4,785,540
Total	**$ 4,973,783**	**$ 4,785,540**

The Status of FBWT 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 FYs
- **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 FBWT** — 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, 2017 and September 30, 2016 (in thousands)

Status of Fund Balance with Treasury	2017	2016
Unobligated Balance		
Available	$ 2,152,203	$ 2,225,327
Unavailable	9,732	33,255
Obligated Balance not yet Disbursed	2,811,806	2,526,949
Non-Budgetary FBWT	42	9
Total	**$ 4,973,783**	**$ 4,785,540**

Note 3 — Advances

As of September 30, 2017, MCC reported intragovernmental advances totaling $6,461 thousand, and public advances totaling $61,025 thousand. As of September 30, 2016, the amounts reported were $9,651 thousand and $62,026 thousand, respectively. The decrease of $1,001 thousand in public advances is driven primarily by the closure of the Philippines Compact. The $3,190 thousand decrease in intragovernmental advances is driven primarily by IAA advance liquidations with the Department of Transportation and the Department of the Treasury, Office of Technical Assistance.

Note 4 — Accounts Receivable, Net

Total receivables at September 30, 2017 and 2016 were $378 thousand (net of allowance for doubtful accounts of $5 thousand) and $470 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. For FY 2016, the majority of the accounts receivable balance is due to employee payroll receivable transactions for overpayments of post allowance and post differential to MCC overseas employees, which occurred between FY 2013 and FY 2015. 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, 2017 (in thousands)	Estimated Useful Life	Cost	Accumulated Depreciation	Book Value
General PP&E				
Leasehold Improvements	10 years	$ 8,392	$ (1,421)	$ 6,971
Furniture	10 years	3,788	(673)	3,115
Internal Use Software	5 years	10,253	—	10,253
Vehicles	5 years	369	(128)	241
Total		**$ 22,802**	**$ (2,222)**	**$ 20,580**

Status of General Property, Plant, and Equipment, Net as of September 30, 2016 (in thousands)	Estimated Useful Life	Cost	Accumulated Depreciation	Book Value
General PP&E				
Leasehold Improvements	10 years	$ 8,292	$ (566)	$ 7,726
Furniture	10 years	3,597	(291)	3,306
Vehicles	5 years	177	(62)	115
Total		**$ 12,066**	**$ (919)**	**$ 11,147**

Note 6 — Leases

MCC leases office space at the Franklin Court building in Washington, DC. The lease is an operating lease with a 10-year lease term with an effective date of December 1, 2015, and a termination date of November 30, 2025. The total Franklin Court lease is valued at $53,718 thousand with a termination liability in the amount of $19,848 thousand.

Future Lease Payments Due — Buildings, Franklin Court (in thousands)	Totals
FY 2018	$ 6,145
FY 2019	6,260
FY 2020	6,378
FY 2021	6,499
FY 2022	6,622
After FY 2022	21,814
Total Future Lease Payments	**$ 53,718**

MCC also has short-term leases for one corporate vehicle (through September 13, 2020) and 20 copier machines (through December 31, 2017). The future lease payments due for the buildings and copier machines are depicted below.

Future Lease Payments Due — Equipment (in thousands)	Asset Category		
	Vehicle	Copier	Totals
FY 2018	$ 8	$ 16	$ 24
FY 2019	6	—	6
FY 2020	6	—	6
Total Future Lease Payments	**$ 20**	**$ 16**	**$ 36**

Note 7 — Accrual – Grant Liabilities

In September 30, 2017 and 2016, MCC had grant liabilities of $85,956 thousand and $58,614 thousand, respectively. The $27,342 thousand increase in grant liabilities was the result of changes in the compact portfolio in FY 2017.

Note 8 — Other Liabilities

MCC's total other liabilities as of September 30, 2017 (in thousands), is as follows:

	Non-Current Liabilities	Current Liabilities	Total
With the Public			
Employer Contributions & Payroll Taxes Payable	$ —	$ 89	$ 89
Accrued Funded Payroll Benefits	—	2,117	2,117
Accrued Unfunded Annual Leave	—	4,438	4,438
Rent Abatement Liability	6,460	408	6,868
Total Liabilities with the Public	6,460	7,052	13,512
Total Other Labilities	**$ 6,460**	**$ 7,052**	**$ 13,512**

MCC's total other liabilities as of September 30, 2016 (in thousands), is as follows:

	Non-Current Liabilities	Current Liabilities	Total
With the Public			
Employer Contributions & Payroll Taxes Payable	$ —	$ 66	$ 66
Accrued Funded Payroll Benefits	—	1,754	1,754
Accrued Unfunded Annual Leave	—	4,112	4,112
Rent Abatement Liability	4,768	184	4,952
Total Liabilities with the Public	4,768	6,116	10,884
Total Other Labilities	**$ 4,768**	**$ 6,116**	**$ 10,884**

Note 9 — Commitments and Contingencies

MCC's program execution results in commitments of future obligations with country-specific accountable entities. MCC and the accountable entity agree on the terms of the proposed program (compact/threshold), sign an agreement, and prepare for the agreement to enter into force. Once a compact/threshold enters into force, the obligation is recorded by MCC; until such time, MCC recognizes commitments for these accountable entities. As of September 30, 2017, MCC had commitments for the compacts of Nepal and Niger totaling $869,350 thousand. Similarly, as of September 30, 2016, MCC had commitments for the compacts of Benin II, Morocco II, and Niger totaling $1,195,498 thousand.

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. 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.

Note 10 — Liabilities Not Covered by Budgetary Resources

Liabilities Not Covered by Budgetary Resources at the end of the period totaled $11,401 thousand and $9,154 thousand as of September 30, 2017 and September 30, 2016, respectively.

Liabilities Not Covered by Budgetary Resources (in thousands)	2017	2016
Intragovernmental		
FECA	$ 73	$ 82
Unemployment	23	9
Total Intragovernmental	96	91
Annual Leave Liability	4,437	4,112
Franklin Court Unamortized Rent Abatement	6,868	4,951
Total Liabilities Not Covered by Budgetary Resources	11,401	9,154
Total Liabilities Covered by Budgetary Resources	96,467	69,395
Total Liabilities	**$ 107,868**	**$ 78,549**

Note 11 — 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 $292 thousand for FY 2017 and $348 thousand for FY 2016.

Note 12 — Intragovernmental Costs

The table below illustrates the value of exchange transactions between MCC and other Federal (intragovernmental) entities, as well as Non-Federal (public) entities.

Intragovernmental Costs (in thousands)	2017	2016
Compact Programs		
Intragovernmental	$ 936	$ 37
Public	553,384	428,311
Total Compact Costs	**554,320**	**428,348**
609(g) Programs		
Intragovernmental	2,403	2,333
Public	15,134	8,881
Total 609(g) Costs	**17,537**	**11,214**
Threshold Programs		
Intragovernmental	1,268	1,130
Public	6,326	2,646
Total Threshold Costs	**7,594**	**3,776**
Due Diligence Programs		
Intragovernmental	4,829	5,179
Public	51,798	42,099
Total Due Diligence Costs	**56,627**	**47,278**
Audit Programs		
Intragovernmental	4,065	3,231
Public	145	138
Total Audit Costs	**4,210**	**3,369**
Administrative Programs		
Intragovernmental	26,796	25,165
Public	79,517	83,549
Total Administrative Costs	**106,313**	**108,714**
Total Program Costs	**$ 746,601**	**$ 602,699**

Note 13 — Undelivered Orders at the End of the Period

Undelivered Orders represent the amount of goods and/or services ordered to perform MCC's program activities, which have not been received. Undelivered orders at the end of the period totaled $2,782,851 thousand and $2,529,225 thousand as of September 30, 2017 and, 2016, respectively.

Undelivered Orders at September 30, 2017 and September 30, 2016 (in thousands)

Programs	2017	2016
Compact	$ 2,311,905	$ 2,098,656
CIF	99,785	91,757
609(g)	60,479	53,735
Threshold	121,894	86,439
Due Diligence	115,137	115,810
Audit	3,024	3,752
Administrative	70,627	79,076
Total	**$ 2,782,851**	**$ 2,529,225**

Note 14 — Explanation of Differences Between the Combined Statement of Budgetary Resources and the Budget of the U.S. Government

The table below documents the differences between the FY 2016 SBR and the actual amounts reported for FY 2016 in the Budget of the U.S. Government released on May 23, 2017. Since the FY 2017 financial statements will be reported prior to the release of the Budget of the U.S. Government, MCC is reporting for FY 2016 only. Typically, the Budget of the U.S. Government with the current year actual data is published in February of the subsequent year. Once published, the FY 2017 actual data will be available on www.whitehouse.gov/omb.

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

	Budgetary Resources	Obligations Incurred	Net Outlays
Statement of Budgetary Resources	$ 3,298	$ 1,040	$ 717
Deductions	—	—	(1)
Budget of the U.S. Government	**$ 3,298**	**$ 1,040**	**$ 716**

Note 15 — Reconciliation of Net Cost of Operations to Budget

SFFAS No.7, *Accounting for Revenues and Other Financing Sources and 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 SBR. The table below reconciles the net obligations derived from the SBR 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 as of September 30, 2017 and 2016, respectively. Total Resources Used to Finance Items Not Part of the Net Cost of Operations at the end of the period totaled negative $253,626 thousand and negative $347,028 thousand as of September 30, 2017 and 2016, respectively, and is comprised of current year Unpaid Obligations, Advances, and Recoveries of Prior Year Obligations.

Reconciliation of Net Cost of Operations to Budget for the Year Ending September 30, 2017 (in thousands)

Resources Used to Finance Activities		FY 2017 Reported Program Costs	
Budgetary Resources Obligated		Gross Costs	
New Obligations and Upward Adjustments	$ 1,095,124	Net Program Costs	$ 746,601
Less: Recoveries of Prior Year Unpaid Obligations and Offsetting Collections	(93,477)		
Other Financing Sources	1,773		
Total Resources Used to Finance Activities	1,003,420		
Total Resources Used to Finance Items Not Part of the Net Cost of Operations	(253,626)	Less: Earned Revenue	
Total Components of Net Cost of Operations that will Not Require or Generate Resources	(3,193)	Net Program Revenue	—
Net Cost of Operations per the Budget	**$ 746,601**	**Net Cost of Operations per the Statement of Net Cost**	**$ 746,601**

Reconciliation of Net Cost of Operations to Budget for the Year Ending September 30, 2016 (in thousands)

Resources Used to Finance Activities		FY 2016 Reported Program Costs	
Budgetary Resources Obligated		Gross Costs	
New Obligations and Upward Adjustments	$ 1,039,792	Net Program Costs	$ 602,699
Less: Recoveries of Prior Year Unpaid Obligations and Offsetting Collections	(85,915)		
Other Financing Sources	2,169		
Total Resources Used to Finance Activities	956,046		
Total Resources Used to Finance Items Not Part of the Net Cost of Operations	(347,028)	Less: Earned Revenue	
Total Components of Net Cost of Operations that will Not Require or Generate Resources	(6,319)	Net Program Revenue	—
Net Cost of Operations per the Budget	**$ 602,699**	**Net Cost of Operations per the Statement of Net Cost**	**$ 602,699**

Note 16 — Correction of an Error

Incidental to the release of Federal Financial Accounting Technical Release 16 — *Implementation Guidance for Internal Use Software,* MCC recorded the correction of an error in the FY 2017 Financial Statements. Between 2014 and 2016, the costs associated with software developed for internal use was expensed instead of being capitalized in accordance with the SSFAS No 10, *Accounting for Internal Use Software.*

If MCC had accounted for the capitalization of development costs of internal use software in FY 2016 the impact on the FY 2016 Financial Statements would have been as follows:

Related Effect on Previously Issued Financial Statements (in thousands)

	2016 As Previously Reported	Adjustments Increase (Decrease)	2016 As Corrected
Balance Sheet			
General Property, Plant and Equipment *(Note 5)*	$ 11,147	$ 3,902	$ 15,049
Total Assets	$ 4,868,834	$ 3,902	$ 4,872,736
Cumulative Results of Operations — All Other Funds	$ 2,462	$ 3,902	$ 6,364
Total Net Position	$ 4,790,285	$ 3,902	$ 4,794,187
Total Net Position and Liabilities	$ 4,868,834	$ 3,902	$ 4,872,736
Statement of Net Costs			
Due Diligence Program Costs	$ 47,278	$ (1,321)	$ 45,957
Administrative Costs	$ 108,714	$ (1,341)	$ 107,373
Net Cost of Operations	$ 602,699	$ (2,662)	$ 600,037
Statement of Changes in Net Position			
Cumulative Results of Operations:			
Beginning Balances	$ (3,976)	$ 1,240	$ (2,736)
Net Cost of Operation	$ (602,699)	$ 2,662	$ (600,037)
Net Change	$ 6,438	$ 2,662	$ 9,100
Cumulative Results of Operations	$ 2,462	$ 3,901	$ 6,363
Net Position	$ 4,790,285	$ 3,902	$ 4,794,187

Independent Auditors' Report

OFFICE OF INSPECTOR GENERAL
U.S. Agency for International Development

Audit of MCC's Fiscal Years 2017 and 2016 Financial Statements

AUDIT REPORT M-000-18-002-C
NOVEMBER 15, 2017

1300 Pennsylvania Avenue NW • Washington, DC 20523
oig.usaid.gov • 202-712-1150

Office of Inspector General, U.S. Agency for International Development

The Office of Inspector General provides independent oversight that promotes the efficiency, effectiveness, and integrity of foreign assistance provided through the entities under OIG's jurisdiction: the U.S. Agency for International Development, U.S. African Development Foundation, Inter-American Foundation, Millennium Challenge Corporation, and Overseas Private Investment Corporation.

Report waste, fraud, and abuse

Millennium Challenge Corporation Hotline
Email: mcchotline@usaid.gov
Phone: 202-712-1023 or 800-230-6539
Mail: USAID OIG Hotline, Attn: MCC Hotline, P.O. Box 657, Washington, DC 20044-0657

Office of Inspector General, U.S. Agency for International Development

MEMORANDUM

DATE: November 15, 2017

TO: MCC, Acting Chief Executive Officer, Jonathan Nash

FROM: Deputy Assistant Inspector General for Audit, Donell Ries /s/

SUBJECT: Audit of MCC's Fiscal Years 2017 and 2016 Financial Statements (M-000-18-002 C)

Enclosed is the final audit report on Millennium Challenge Corporation's (MCC) financial statements as of September 30, 2017, and 2016. The Office of Inspector General (OIG) contracted with the independent certified public accounting firm CliftonLarsonAllen LLP (Clifton) to conduct the audit. The contract required Clifton to perform the audit in accordance with generally accepted government auditing standards and Office of Management and Budget Bulletin No. 17-03, "Audit Requirements for Federal Financial Statements."

In carrying out its oversight responsibilities, OIG reviewed Clifton's report and related audit documentation and inquired of its representatives. Our review, which was different from an audit performed in accordance with generally accepted government auditing standards, was not intended to enable us to express, and we do not express, an opinion on MCC's financial statements. Clifton is responsible for the enclosed auditor's report and the conclusions expressed in it. We found no instances in which Clifton did not comply, in all material respects, with applicable standards.

The audit objectives were to (1) express an opinion on whether MCC's financial statements as of September 30, 2017, and 2016, were presented fairly, in all material respects; (2) obtain sufficient understanding of internal control over financial reporting to plan the audit; and (3) test compliance with certain provisions of applicable laws, regulations, contracts, and grant agreements. The purpose was not to provide an opinion on the effectiveness of the entity's internal control or compliance with provisions of applicable laws, regulations, contracts, and grant agreements.

The audit firm concluded that MCC's financial statements as of fiscal years ending September 30, 2017, and 2016, are presented fairly, in all material respects, in accordance with U.S. generally accepted accounting principles. The

Office of Inspector General, Millennium Challenge Corporation
Washington, DC
oig.usaid.gov

audit firm also found no instances of noncompliance with certain provisions of laws, regulations, contracts, and grant agreements.

The auditors reported two significant deficiencies in internal control related to:

- Grant accrual estimates and validation (Modified repeat finding)
- Millennium Challenge Accounts' financial reporting and compliance (New finding)

To address the significant deficiencies identified in the report, Clifton made, and OIG agrees with, the following recommendations to MCC's management. We recommend that MCC's management:

Recommendation 1. Evaluate whether its grant accrual methodology assumptions and calculations are effective. This evaluation should include an assessment of root causes for variances in estimated and actual accruals and take into consideration experiences from at least the last 5 years.

Recommendation 2. Update the "Expense Accruals Financial Management Division Procedure Manual" to:

- Require supporting documentation, including rationale, for deviating from MCC's accrual policy and procedures. This documentation should also include MCC's management approval for any deviations.
- Indicate in the guidance how reinstated, unused spending authority and applicable subsequent disbursements are to be addressed in the grant accrual calculation.

Recommendation 3. Correct the accrual data for quarters three and four to reflect the actual spending authority and disbursements.

Recommendation 4. Update the "Compact Grant Accrual Validation Data Call Desktop Manual" to include timeframes for validating Millennium Challenge Accounts' grant accrual estimates and MCC's follow-up on significant differences so errors are promptly identified and addressed.

Recommendation 5. Provide Millennium Challenge Accounts with additional written instructions and training on evaluating the reasonableness of MCC's grant accrual estimates, and require each Millennium Challenge Account to submit documentation showing why it agrees with MCC's estimate.

Recommendation 6. Implement procedures for tracking and monitoring Millennium Challenge Accounts' compliance with grant management policies and procedures, including Millennium Challenge Accounts' grant oversight, procurement eligibility verification, and grant award processes.

Recommendation 7. Enforce the requirement for the Millennium Challenge Accounts to submit quarterly financial reports and financial information by the due dates.

Recommendation 8. Establish procedures to ensure that Millennium Challenge Accounts are providing accurate, complete, supportable, and valid financial information for data calls for contract retentions.

MCC concurred with all eight recommendations.

We ask that you provide us written notification of actions planned or taken to reach management decisions on recommendations 1 through 8.

We appreciate the assistance extended to our staff and the audit firm's employees during the engagement.

MILLENNIUM CHALLENGE CORPORATION

Independent Auditors' Report of MCC's Financial Statements for the Period Ending September 30, 2017

Table of Contents

CliftonLarsonAllen LLP
901 North Glebe Road, Suite 200
Arlington, VA 22203
571-227-9500 | fax 571-227-9552
CLAconnect.com

INDEPENDENT AUDITORS' REPORT

To the Inspector General
United States Agency for International Development

To the Board of Directors
Millennium Challenge Corporation

Report on the Financial Statements

We have audited the accompanying financial statements of Millennium Challenge Corporation (MCC), which comprise the balance sheets as of September 30, 2017, and 2016, and the related statements of net cost, changes in net position, the combined statements of budgetary resources for the years then ended, and the related notes to the financial statements (financial statements).

Management's Responsibility for the Financial Statements

MCC management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America (U.S.); this includes the 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.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the U.S.; the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States; and Office of Management and Budget Bulletin No. 17-03, Audit Requirements for Federal Financial Statements (OMB Bulletin 17-03). Those standards and OMB Bulletin 17-03 require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit 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 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 MCC'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 MCC's internal control. Accordingly, we express no such opinion. An audit 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.

A member of Nexia International

INDEPENDENT AUDITORS' REPORT (Continued)

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 Millennium Challenge Corporation as of September 30, 2017, and 2016, 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 the information in MCC's Management Discussion and Analysis (MD&A), and Required Supplementary Information (RSI) sections 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, 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 required supplementary information 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 audits of the financial statements. We do not express an opinion or provide any assurance on this information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information
Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The Message from the Chief Executive Officer, Message from the Vice President, Department of Administration and Finance and Chief Financial Officer, and other information, are presented for purposes of additional analysis and is not a required part of the financial statements or RSI. In addition, management has included references to information on websites or other data outside of the Agency Financial Report. This 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 Report on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*

Internal Control over Financial Reporting

In planning and performing our audits 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 statement of assurance 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 statement of assurance on internal control included in the MD&A.

INDEPENDENT AUDITORS' REPORT (Continued)

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. 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.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section 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 have not been identified. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, we did identify deficiencies in internal control, summarized below and detailed in Exhibit I that we considered as significant deficiencies.

1. Controls over grant accrual estimates and validation need to be strengthened (Modified Repeat Finding)
2. Controls over the Millennium Challenge Accounts' (MCAs) financial reporting and compliance need to be strengthened (New Finding)

Compliance with Laws, Regulations, Contracts, and Grant Agreements

As part of obtaining reasonable assurance about whether MCC's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements noncompliance with which could have a direct effect on the determination of material financial statement amounts and disclosures. 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 that are required to be reported in accordance with Government Auditing Standards or OMB Bulletin 17-03.

Management's Responsibility for Internal Control and Compliance

Management is responsible for (1) evaluating the effectiveness of internal control over financial reporting based on criteria established under Federal Managers Financial Integrity Act (FMFIA), (2) providing a statement of assurance on the overall effectiveness on internal control over financial reporting, and (3) complying 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, and (2) testing compliance with certain provisions of laws, regulations, contracts, and grant agreements.

We did not evaluate all internal controls relevant to operating objectives as broadly established by 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

3

INDEPENDENT AUDITORS' REPORT (Continued)

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, regulations, contracts and grant agreements applicable to MCC. We limited our tests to certain provisions of laws, regulations, contracts and grant agreements noncompliance with which could have a direct effect on the determination of material financial statement amounts and disclosures. However, providing an opinion on compliance with those provisions was not an objective of our audits, and accordingly, we do not express such an opinion. We caution that noncompliance 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 the findings identified in our report is presented in Exhibit 2. We did not audit MCC's response and, accordingly, we express no opinion on it.

Status of Prior Year's Control Deficiencies

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 11, 2016. The status of prior year findings is presented in Exhibit 3.

Purpose of the Report on Internal Control over Financial Reporting and the Report on Compliance

The purpose of the Report on Internal Control over Financial Reporting and the Report on Compliance 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
November 13, 2017

EXHIBIT I
Significant Deficiencies

I. Controls over grant accrual estimates and validation need to be strengthened (Modified Repeat Finding)

For every quarter, MCC calculates the grant accrual liability estimate for each MCA. The MCA is responsible for confirming that the grant accrual estimate is accurate, or provide support for the MCA's calculated estimate. The MCAs are also responsible for assisting MCC in validating the estimated liability. MCC reported approximately $554 million in compact grant related expenses and an accrued grant liability of $86 million comprising retentions payable and expenses incurred but not yet reported by the MCC Compact Accountable Entities (also known as Millennium Challenge Accounts or MCAs) as of September 30, 2017. The compact grant activities are the core of MCC's financial and program operations.

We audited the grant accruals and validation for reasonableness and compliance with MCC's *Expense Accruals Financial Management Division Procedure Manual* (Manual). During Fiscal Year (FY) 2017, MCC continued to refine its accrual methodology and collect supporting information in its data store to help validate the methodology. However, we found the following conditions during our testing that impacted the quarterly grant accrual estimates. These issues increase the potential for the grant accrual estimate to be misstated and incorrectly reported in MCC's financial statements and we consider these to be significant deficiencies.

Issues with Grant Accrual Estimate — In our review of the quarterly grant accrual, we noted issues that raise concerns about MCC's ability to ensure that its grant accrual methodology is valid and reliable. The actual costs incurred when compared to the estimates were materially not close to actual. For example, the first quarter 2017 accrual vs. actual showed that the accrual was more than the actual payments by approximately $15.8 million. However, the third quarter accrual versus actual showed that the accrual was less than the actual payments by approximately $13.5 million. Based on the accrual validation that MCC performed in accordance with their policies and procedures, the third quarter accrual versus actual showed that the accrual was less than the actual payments by only $4.8 million. However, an additional $8.7 million related to cost incurred for that same period was not included. MCC explained that their procedures do not capture such costs.

For the first quarter accruals, we noted that one MCA experienced a slower rate of project execution than expected. Another MCA relied on its system records to identify works completed but not yet paid instead of reaching out to respective MCA directors/engineers to confirm that its system records were accurate to support its acceptance of the MCC calculated accrual. The causes for the differences are not fully known, and MCC is investigating the differences noted in the third quarter accruals.

Weak Validation Controls — MCC, as part of its internal control process, performs a validation of its accrual estimates as a key control to assess the reasonableness of the estimated amount recorded in the prior quarter. This validation process should provide MCC an indication of whether the estimation methodology continues to be sound. During our testing we found that MCC did not follow-up on the significant accrual differences in a timely manner. MCC's Compact Grant Accrual Validation Data Call Desktop Manual does not provide deadlines for completing the validation or for MCC to complete its investigation. For example, for the first quarter ending December 31, 2016, the validation was not completed until July 2017. In addition, MCC did not complete its

[1] A data store is a repository for storing and managing collections of data which include not just repositories like databases, but also simpler store types such as simple files, email, etc.

EXHIBIT I
Significant Deficiencies

follow-up on significant differences until late September 2017. Upon further analysis, MCC found one MCA provided an incomplete validation which required an updated validation submission an additional $1.1 million of incurred cost applicable to the first quarter. Inability to identify these errors in a timely manner might affect MCC's management decision making process.

Insufficient documentation of deviations from the Grant Accrual Process — MCC deviated from its grant accrual process by not accounting for the total amount of approved spending authority and the total disbursements for the third and fourth quarters in FY 2017. In addition, MCC excluded the disbursements related to the portion of the spending authority that was not accounted for. MCC's approved spending authority for the third and fourth quarters, did not fully reflect what the MCA spent for those quarters. Although the deviation did not change the outcome of the MCA estimated grant accrual, it captured incorrect data that caused errors in calculating MCC's grant accrual estimate and will impact the calculations for future quarters. MCC did not document its justification for deviating from its grant accrual methodology.

GAO *Standards for Internal Control in the Federal Government,* Section OV3.05 states that when evaluating implementation, management determines if the control exists and if the entity has placed the control into operation. A deficiency in implementation exists when a properly designed control is not implemented correctly in the internal control system. 3.09 states that management develops and maintains documentation of its internal control system. 3.10 states that effective documentation assists in management's design of internal control by establishing and communicating who, what, when, where, and why of internal control execution to personnel. 12.03 states that management documents in policies for each unit its responsibility for an operational process's objectives and related risk, and control activity design, implementation, and operating effectiveness.

Federal Financial Accounting and Auditing Technical Release 12, *Accrual Estimates for Grant Programs, Federal Financial Accounting* (August 4, 2010), Paragraph 31, *Training and Monitoring of Grantees* states, "Since preparation of accrual estimates is dependent upon relevant and reliable data, accurate and timely reporting by grant recipients serves as the basis for historical data used in preparing future estimates and provides reliable actual data to which accrual estimates can be compared. Agencies should consider whether grant recipients need training on completing required financial reports." Also, Paragraph 12, *Preparing Accrual Estimates for Grant Programs* states, "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 also facilitate the auditor's testing of the estimates. Documentation should be complete and stand on its own, i.e., a knowledgeable independent person could perform the same steps and replicate the same results. If the documentation were from a source that would normally be destroyed, then copies should be maintained in the file for the purpose of reconstructing the estimates.

We recommend that MCC's Department of Administration and Finance and the Chief Financial Officer:

Recommendation 1: Evaluate whether its grant accrual methodology assumptions and calculations are effective. This evaluation should include an assessment of root causes for variances in estimated and actual accruals and take into consideration, experiences from at least the last 5 years.

Recommendation 2: Update the "Expense Accruals Financial Management Division Procedure Manual" to:

EXHIBIT I
Significant Deficiencies

a) Require supporting documentation, including rationale for deviating from MCC's accrual policy and procedures. This documentation should also include MCC's management approval for any deviations.

b) Indicate in the guidance how reinstated unused spending authority and applicable subsequent disbursements are to be addressed in the grant accrual calculation.

Recommendation 3: Correct the accrual data for quarters three and four to reflect the actual spending authority and disbursements.

Recommendation 4: Update the "Compact Grant Accrual Validation Data Call Desktop Manual" to include timeframes for validating Millennium Challenge Accounts' grant accrual estimates and MCC's follow-up on significant differences so errors are promptly identified and addressed.

Recommendation 5: Provide Millennium Challenge Accounts with additional written instructions and training on evaluating the reasonableness of MCC's grant accrual estimates, and require each Millennium Challenge Account to submit documentation showing why it agrees with MCC's estimate.

2. Controls over MCAs' financial reporting and compliance need to be strengthened (New Finding)

The Department of Compact Operations, through collaboration with the Department of Administration and Finance, establishes operational oversight and financial reporting controls and procedures to govern the conduct and administration of the MCC Compact/Threshold portfolio by the MCA entities. The MCAs' financial operations are an essential component to MCC's financial statements as their financial activities are material and significant. During our MCA visits, we evaluated the MCAs' design and effectiveness of internal controls. As a result of procedures performed, we identified the following control deficiencies that collectively we considered a significant deficiency in controls over financial reporting and compliance.

Grant program oversight — MCA-Indonesia's Green Prosperity (GP) Project accounts for approximately $332.50 million of its $600 million compact funding. MCA-Indonesia formed an MCA Grant Management Team (GMT) to provide oversight over the GP grants administration. The GMT conducts desk reviews and field observation visits of GP grantees as part of its oversight function. Documented guidelines and field observations are key oversight and monitoring controls of the MCA-Indonesia grantees. An important element of the GMT mission is to detect questionable costs incurred by GP grantees. We found that the GP Project Financial Management Guideline (FMG) did not adequately document GMT's grants administration and oversight procedures. For example, the sampling methodology for the desk reviews and field observation visits were not documented and the basis for the sample size for the desk reviews that GMT performed were not adequately documented. In addition, as of August 2017 MCA-Indonesia had not conduct 36 of the 76 field observations required by December 31, 2017.

Contract retentions reporting errors and improper payment — Every quarter MCC requests the MCAs updated contract retentions data to record retentions payable in MCC's financial statements. In December 2016, the Project Implementation Unit (PIU), which has oversight responsibility over a portion of MCA-Liberia's compact funding, understated one contract by $433,679 and overstated one contract by $200. In addition, MCC compact funds were improperly used to pay for $1,047,145 in contract retentions withheld from invoices that were paid by a pre-existing donor. The improper payment amount was subsequently returned to MCA-Liberia.

I-3

EXHIBIT I
Significant Deficiencies

MCA's Quarterly Financial Reports (QFR) were submitted late — The QFR provides an overview of the financial developments since the last disbursement period and explains and justifies any proposed cash requests for the next period. The QFR is prepared by the MCA with input from the MCA's Fiscal Agent (FA) for financial reporting. The report is also used to determine MCA's funds control, reallocation of funds in the Multi-year Financial Plan, and spending limits. The QFR contains: (1) the Multi-Year Financial Plan Adjustment Request Form; (2) Summary of Multi-year Financial Plan Adjustments to Date; (3) Actual Expenditure & Commitment Report (current period); (4) Commitment Forecast Report (next period); (5) Forecasted Program Cash Requirements (next period); and (6) Cash Reconciliation and Interest Summary. QFRs must be completed for all 609g, CIF, threshold, and compact funding.

During our testing we noted following late submissions of QFRs:

MCA	Days Late	Quarter 2017	Type of Funding
Honduras	39 days	First quarter	Threshold
Honduras	59 days	Third Quarter	Threshold
Benin II	5 days	Second Quarter	Compact
Liberia	66 days	Second Quarter	Compact
Cabo Verde II	1 day	Second Quarter	Compact

The MCC Compact Financial Management Division Procedure (April 2016), Section1.2.4.2 Spending Authority Request Package [QFR] states that "…The quarterly Disbursement Request (DR) packages are due to MCC no later than the 10th day of the third month of the quarter."

Late submission of QFRs delayed MCC's approval of MCAs' spending authority. With the exception of working capital amounts and exceptional situations detailed in the Common Payment System (CPS) Financial Management Division (FMD) Procedure, no funds will be disbursed against the MCA in a given quarter until spending authority has been established.

Procurement eligibility verification not completed — During our review of the MCA-Honduras procurements, we noted that MCA-Honduras' Procurement Unit did not properly verify the eligibility of a vendor. Only five of seven U.S. Government databases—required to determine eligibility—were verified. MCA-Honduras subsequently conducted a full eligibility review after we brought this issue to their attention. Eligibility verification checks are in place to ensure that ineligible vendors are not allowed to participate in the compact program.

Grant award process not followed — MCA-Honduras' Threshold Manual Operating Fund of Grants for Social Liability requires MCC's approval of the Committee of Donation's members and documentation of potential projects for grant awards. We noted that one of the Committee's appointed members was replaced without proper authorization. Further, the Committee did not document their approval and rejection of the project proposals. An MCA official stated that MCA will not be issuing any more grants.

I-4

EXHIBIT I
Significant Deficiencies

We recommend that MCC's Department of Administration and Finance and the Chief Financial Officer:

Recommendation 6: Implement procedures for tracking and monitoring Millennium Challenge Accounts' compliance with grant management policies and procedures, including Millennium Challenge Accounts' grant oversight, procurement eligibility verification, and grant award processes.

Recommendation 7: Enforce the requirement for the Millennium Challenge Accounts to submit quarterly financial reports and financial information by the due dates.

Recommendation 8: Establish procedures to ensure that Millennium Challenge Accounts' are providing accurate, complete, supportable, and valid financial information for data calls for contract retentions.

EXHIBIT 2
Management's Response to Audit Findings

MILLENNIUM
CHALLENGE CORPORATION
UNITED STATES OF AMERICA

November 13, 2017

Ms. Mia Leswing
Principal
CliftonLarsonAllen, LLP
450 N. Fairfax Drive, Suite 1020
Arlington, VA 22203

Thomas E. Yatsco
Assistant Inspector General for Audit
Office of Inspector General
United States Agency for International Development
1300 Pennsylvania Avenue, NW
Washington, DC 20005

Dear Ms. Leswing and Mr. Yatsco,

In response to the audit findings and recommendations cited in the *"Audit of MCC's Financial Statements, Internal Controls, and Compliance for the Fiscal Years Ending September 30, 2017, and 2016"* report, MCC provides the following comments:

Significant Deficiencies: Controls over grant accrual estimates and validation need to be strengthened (Modified Repeat Finding)

Recommendation 1: Evaluate whether its grant accrual methodology assumptions and calculations are effective. This evaluation should include an assessment of root causes for variances in estimated and actual accruals and take into consideration, experiences from at least the last five years.

Recommendation 2: Update the "Expense Accruals Financial Management Division Procedure Manual" to:

a) Require supporting documentation, including rationale for deviating from MCC's accrual policy and procedures. This documentation should also include MCC's management approval for any deviations.

b) Indicate in the guidance how reinstated unused spending authority and applicable subsequent disbursements are to be addressed in the grant accrual calculation.

1099 14th Street, NW, Suite 700 | Washington, DC | 20005-3550 | p: (202) 521.3600 | f: (202) 521.3947 | www.mcc.gov

2-1

Recommendation 3: Correct the accrual data for quarters three and four to reflect the actual spending authority and disbursements.

Recommendation 4: Update the "Compact Grant Accrual Validation Data Call Desktop Manual" to include timeframes for validating Millennium Challenge Accounts' grant accrual estimates and MCC's follow-up on significant differences so errors are promptly identified and addressed.

Recommendation 5: Provide Millennium Challenge Accounts with additional written instructions and training on evaluating the reasonableness of MCC's grant accrual estimates, and require each Millennium Challenge Account to submit documentation showing why it agrees with its estimate.

> **MCC Response:** MCC concurs with recommendations 1, 2, 3, 4 and 5. A comprehensive corrective action plan will be developed to address the deficiency noted.

Significant Deficiencies: Controls over MCAs' financial reporting and compliance need to be strengthened (New Finding)

Recommendation 6: Implement procedures for tracking and monitoring Millennium Challenge Accounts' compliance with grant management policies and procedures, including Millennium Challenge Accounts' grant oversight, procurement eligibility verification, and grant award processes.

Recommendation 7: Enforce Millennium Challenge Accounts' submissions of quarterly financial reports and financial information by the required due dates.

Recommendation 8: Establish procedures to ensure that Millennium Challenge Accounts' are providing accurate, complete, supportable, and valid financial information for data calls for contract retentions.

> **MCC Response:** MCC concurs with recommendations 6, 7 and 8. A comprehensive corrective action plan will be developed to address the deficiency noted.

Sincerely,

Mahmoud Bah
Acting Vice President and Chief Financial Officer
Department of Administration and Finance

2-2

EXHIBIT 3
Status of Prior Year Recommendations

Our assessment of the current status of the recommendations related to findings identified in the prior year audit is presented below:

FY 2016 Recommendations	***Type***	***Fiscal Year 2017 Status***
1. Enhance MCC's Expense Accruals Financial Management Division Procedure Manual.	Significant Deficiency (SD)	Open — Reported as Modified SD — Repeat Finding
2. Conduct a comprehensive review and formalize the Grant Accrual Validation Whitepaper as an official policy and procedures	SD	Closed
3. Establish internal control procedures to properly review the accounting and reporting of funds returned.	SD	Closed
4. Establish internal control process to ensure financial statements are prepared in accordance with current version of OMB A-136.	SD	Closed
5. Conduct quarterly reconciliation between the status of budgetary resources and the OMB SF-132.	SD	Closed
6. Implement management control to properly review and approve unapportioned funds at the fund level before entries are made.	SD	Closed
7. Implement management control to review the impact of funds unapportioned at the fund level before apportionment and recoveries adjustments are recorded.	SD	Closed
8. Continue requiring all compact obligating documents be accompanied by an Enter-Into-Force memo prior to recognizing obligation.	SD	Closed

Other Information

Fiscal Year 2018 Top Management Challenges Identified by the Inspector General

Ann Calvaresi Barr
Inspector General

Message From the Inspector General

USAID provides humanitarian assistance to people in areas besieged by natural disaster, health crisis, or armed conflict, while supporting the U.S. commitment to help countries confront chronic conditions such as hunger, child and maternal mortality, illiteracy, and gender inequality. The work of the Millennium Challenge Corporation (MCC) complements USAID's mission by investing in countries committed to poverty reduction through policies for sound economic growth. USAID and MCC—together with the U.S. African Development Foundation (USADF), the Inter-American Foundation (IAF), and the Overseas Private Investment Corporation (OPIC)—managed over $30 billion in budgetary resources in fiscal year 2016 to advance economic growth and democracy around the world, which promotes U.S. national security interests.

To help ensure the U.S. Government achieves maximum return on these investments, OIG provides independent oversight of USAID, MCC, USADF, IAF, and OPIC.[1] As part of this oversight, the Reports Consolidation Act of 2000 (Public Law 106–531) requires applicable Federal agencies to include in their performance and accountability reports a statement by their Inspector General summarizing the agencies' most daunting challenges and the progress made in managing them.

From our recent audits and investigations, we identified four top management challenges for fiscal year 2018:[2]

- **Improving program planning and monitoring.** USAID policy calls for rigorous planning, design, monitoring, and evaluation to better ensure that foreign assistance programs have the resources needed to achieve objectives and to identify and address fraud and other risks. However, effectively putting these policies into effect continues to be a challenge, particularly in overseas contingency operations and the nonpermissive environments USAID frequently works in.[3]
- **Reconciling interagency priorities and functions to more efficiently and effectively advance international development.** Providing foreign assistance through multiple U.S. Government agencies has presented significant challenges for USAID in achieving its core development mission. Coordinating with the State Department, which leads multiagency responses to political and security crises, has complicated

[1] *OIG also provides oversight of overseas contingency operations as part of lead inspector general initiatives (described in section 8L of the Inspector General Act, as amended).*

[2] *Our recent work identified a challenge for MCC related to strengthening local capacity and increasing sustainability in the activities it funds, discussed on pages 13 and 14. No serious challenges were identified for USADF or IAF.*

[3] *Work in nonpermissive and contingency environments includes overseas contingency operations, which integrate the efforts of the Departments of Defense and State, USAID, and other partners to respond to conflicts and emergencies.*

USAID's project planning and execution. Despite broad interagency guidance on State's role in these environments, key USAID staff remain unclear as to how to manage and respond to additional layers of review, changing priorities, and competing short- and long-term priorities.

- **Strengthening country ownership and local capacity to promote sustainability of U.S.-funded development.** To sustain development after U.S. involvement ends, USAID calls for investing in communities that have a stake in continuing activities and services, building the skills of local stakeholders, and ensuring public- or private-sector participation and financial backing. While USAID policies require assessments of country capacity and the risks in providing direct assistance to a sovereign state, the policies lack the clarity needed to ensure rigorous assessments.
- **Meeting Governmentwide financial and information management and security requirements.** The Federal Government established strict financial and information management requirements to promote effective stewardship of Government resources. Despite noteworthy actions to better ensure compliance, USAID is still unable to meet all of these requirements.

In addition to meeting the requirements of the Reports Consolidation Act, this document will help inform our work and frame our dialogues with Congress, the new administration, and other stakeholders about their priorities for effective stewardship of U.S. funds dedicated to foreign aid and development.

OIG remains committed to conducting thorough and timely audits and investigations of USAID programs and management—as well as those of MCC, USADF, IAF, and OPIC—and when appropriate, recommending actions to help address the challenges we identify.

If you would like to discuss or have any questions about USAID's top management challenges for fiscal year 2018, please contact me at 202-712-1150.

USAID OFFICE OF INSPECTOR GENERAL

MEMORANDUM

DATE: October 16, 2017

TO: Acting Chief Executive Officer, Millennium Challenge Corporation, Jonathan Nash

FROM: Deputy Assistant Inspector General for the Millennium Challenge Corporation, Donell Ries /s/

SUBJECT: Fiscal Year 2018 Management Challenge for MCC

The USAID Office of Inspector General (OIG), which provides independent oversight of MCC to help ensure maximum return on its investments in compact countries, annually identifies the agency's top management challenges and the progress it has made in managing them. In keeping with the Reports Consolidation Act of 2000 (Public Law 106-531), we submit this summary for inclusion in MCC's performance and accountability report. The summary captures the examples in OIG's Top Management Challenges report for fiscal year 2018 [Top Management Challenges].

Although our full report did not include a separate chapter for MCC, we highlighted a challenge related to strengthening local capacity and increasing sustainability in the activities it funds. For example, the capacity of some accountable entities to manage compact activities is limited. This was the case with a $19.3 million, MCC-funded construction project in Morocco. An OIG investigation uncovered a product substitution and false billing scheme facilitated by the supervisory engineering firm that Morocco's accountable entity hired to oversee construction. A survey of the project sites also revealed construction defects and safety hazards due to poor workmanship and materials—defects that neither the supervisory engineer nor Morocco's accountable entity reported. MCC asked the Government of Morocco to remediate the quality and safety issues, which will require an estimated $4.1 million.

We also noted risks to sustainability in MCC's projects. Our audit of the Philippines Revenue Administration Reform Project found that two information systems critical to modernizing tax collection were implemented without clear goals, schedules, or sustainability measures, making it difficult for the Philippine Government to manage and sustain the systems. In response to our recommendations, MCC finalized new policy and guidelines to assess sustainability in project design and require reporting on sustainability during project implementation.

We will continue to monitor how these changes in policy are implemented in future compacts. We also have an ongoing audit to determine if MCC has sufficient policies, procedures, and guidance to meet sustainability goals for road infrastructure projects and whether MCC tracks and assesses activities to improve their sustainability.

In determining our oversight priorities, we consider such risks. Our 2017–2018 plan includes audits of infrastructure project planning, monitoring, and sustainability, while our investigative efforts will continue to focus on detecting, deterring, and neutralizing fraud and corruption in infrastructure projects.

Office of Inspector General, Millennium Challenge Corporation
Washington, DC
oig.usaid.gov

MCC Management's Response to the Inspector General

November 10, 2017

Ms. Ann Calvaresi Barr
Inspector General
U.S. Agency for International Development
1300 Pennsylvania Avenue, NW
Washington, DC 20523

Dear Ms. Barr:

I am writing in response to the U.S. Agency for International Development (USAID) Office of Inspector General's (OIG's) *Fiscal Year (FY) 2018 Top Management Challenges,* which identified a Millennium Challenge Corporation (MCC) management challenge related to *Strengthening Country Ownership and Local Capacity To Promote Sustainability of U.S.-Funded Development.*

Attached, you will find MCC's response to the USAID OIG FY 2018 MCC Top Management Challenges.

MCC staff and leadership look forward to our continued constructive engagement with the USAID OIG as we work together to enhance our ability to perform MCC's mission effectively.

Sincerely,

Jonathan G. Nash
Acting Chief Executive Officer
Millennium Challenge Corporation

MCC's Response to OIG FY 2018 Top Management Challenges Letter

The Millennium Challenge Corporation's (MCC) response to the U.S. Agency for International Development (USAID) Office of Inspector General's (OIG) Fiscal Year 2018 Top Management Challenges (the "OIG 2018 Statement") is presented below. The OIG 2018 Statement identified the following management challenge for MCC: Strengthening Country Ownership and Local Capacity to Promote Sustainability of U.S. Funded Development.

MCC is committed to enhancing the effectiveness of our operations both domestically and abroad and is committed to collaborating with the OIG to address the challenge identified in the OIG 2018 Statement, as well as other issues or recommendations raised by the OIG. MCC's response below includes not only relevant updates on the issues identified in the OIG 2018 Statement, but also, where necessary, clarifications to ensure that the assertions set forth in the OIG 2018 Statement provide a fair representation of the situation on the ground (i.e., execution of the Morocco Compact in country) and are factually complete.

Strengthening Country Ownership and Local Capacity to Promote Sustainability of U.S. Funded Development

In March 2017, MCC notified the Government of Morocco of an investigation carried out by USAID OIG which revealed construction defects and false contractor billing on works related to the construction of olive oil processing units funded under the first MCC Morocco Compact. The Government of Morocco formally responded to MCC in April 2017, noting that they shared MCC's concerns and were committed to remediation. Since May 2017, the Ministry of Agriculture has been working with the United Nations Office for Project Services (UNOPS) to further assess potential construction defects and address them effectively. On November 2, 2017, MCC met with the Moroccan Ministry of Finance and the Moroccan Ministry of Agriculture to review the Government of Morocco's progress on meeting its commitment to address construction defects. The Ministry of Agriculture has approved a $1.8 million budget for remediation and has prioritized sites in order to immediately address health and safety concerns. Remediation work has also begun in two regions, with the estimated completion for all remediation work now forecasted for late January 2018.

The OIG 2018 Statement also included risks associated with the MCC Philippines Compact. We appreciate that the OIG recognized our progress in implementing recommendations from the Philippines Sustainability Audit Report. With respect to the Philippines Compact, by compact end the first stage of electronic Tax Information System (eTIS) had been implemented in 13 Bureau of Internal Revenue (BIR) offices, covering 73 percent of taxpayer revenue. The BIR has committed to extending coverage to reach a total of 95 percent of taxpayers, as well as to developing and implementing five additional modules of eTIS. The Government of the Philippines is also preparing to launch the Philippine Tax Academy in January 2018 to develop the capabilities of tax collectors and administrators, improving their tax collection efficiency and further enhancing the sustainably of MCC's investments. The Secretary of Finance has acknowledged the impact of the MCC Revenue Administration Reform Project (RARP) in improving BIR's skills in analyzing data, thereby leading to improved tax collection. While MCC has acknowledged that the Philippines will face challenges in building upon the systems and procedures initiated under RARP, the Government of the Philippines continues to show good faith in honoring its commitments and allocating the necessary resources to manage and sustain the systems.

Summaries of Financial Statement Audit and Management Assurances

Table 8. Summary of Financial Statement Audit

Audit Opinion	Unmodified Opinion					
Restatement	No					
Material Weaknesses		Beginning Balance	New	Resolved	Consolidated	Ending Balance
None		0		0		0
	Total Material Weaknesses	0		0		0

Table 9. Summary of Management Assurances

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

Statement of Assurance	Unmodified					
Material Weaknesses	Beginning Balance	New	Resolved	Consolidated	Reassessed	Ending Balance
None	0					0
Total Material Weaknesses	0					0

Effectiveness of Internal Control over Operations (FMFIA §2)

Statement of Assurance	Unmodified					
Material Weaknesses	Beginning Balance	New	Resolved	Consolidated	Reassessed	Ending Balance
None	0					0
Total Material Weaknesses	0					0

Conformance with Federal Financial Management System Requirements (FMFIA §4)

Statement of Assurance	System conforms					
Non-Conformances	Beginning Balance	New	Resolved	Consolidated	Reassessed	Ending Balance
None	0					0
Total Non-Conformances	0					0

Compliance with Section 803(a) of the Federal Financial Management Improvement Act (FFMIA)

	Agency	Auditor
1. System Requirements	No lack of compliance noted	No lack of compliance noted
2. Accounting Standards	No lack of compliance noted	No lack of compliance noted
3. USSGL at Transaction Level	No lack of compliance noted	No lack of compliance noted

Payment Integrity

MCC is dedicated to reducing fraud, waste, and abuse by adequately reviewing and reporting programs susceptible to improper payments in accordance with OMB Circular A-123, *Management's Responsibility for Enterprise Risk Management and Internal Control,* Appendix C, *Requirements for Effective Estimation and Remediation of Improper Payments.* To improve the integrity of the USG's payments and the efficiency of its programs and activities, Congress enacted the Improper Payment Information Act of 2002 (PL 107-300). The IPIA contains requirements in the areas of improper payment identification and reporting. It requires agency heads to annually review all programs and activities, identify those that may be susceptible to significant improper payments, estimate annual improper payments in susceptible programs and activities, and report the results of their improper payment activities.

OMB Memorandum M-15-02 requires that agencies do the following:

- Review all funds to identify those susceptible to significant improper payments. OMB defines significant improper payments as gross annual improper payments (i.e., the total amount of overpayments plus underpayments) in the program exceeding (1) both 1.5 percent of program outlays and $10,000,000 of all program or activity payments made during the FY reported or (2) $100,000,000 (regardless of the improper payment percentage of total program outlays).
- Obtain a statistically valid estimate of the annual amount of improper payments in programs and activities for those programs that are identified as susceptible to significant improper payments.
- Implement a plan to reduce improper payments.
- Report estimates of the annual amount of improper payments in programs and activities and progress in reducing them.

In order to identify improper payments and assess MCC's compliance with OMB Circular No. A-123, Appendix C, MCC conducted a quantitative and qualitative risk assessment of all MCC funds with payment activity. Payment activity is defined as disbursements, excluding intragovernmental transactions, during the assessment period beginning July 1, 2016 through June 30, 2017. As part of the quantitative risk assessment, MCC developed a payment inventory which included a self-identified improper payment total grouped by fund to assess whether any fund will reach the OMB threshold of susceptibility to significant improper payments. Additionally, the risk assessment methodology also consisted of a qualitative approach which measured and scored each applicable MCC fund by risk factors in order to estimate the probability and impact of risk resulting in an overall rating of low, medium, or high. As a result of the risk assessment process, MCC assessed no funds as susceptible to significant improper payments because none exceeded the OMB susceptibility thresholds based on the quantitative risk assessment approach. Table 10 summarizes the results.

Table 10. MCC Risk Assessment

Fund[1]	Susceptible to Significant Improper Payments
609g	No
Administrative	No
Audit	No
CIF	No
Compact	No
Due Diligence	No
Threshold	No

[1] *The 614(g) fund did not have payment activity and was not included in the risk assessment process. MCC conducted the last risk assessment over the 614(g) fund in 2016. Based on the risk assessment, the fund was assessed as low risk and not susceptible to significant improper payments. MCC completed a risk assessment on all other funds in 2017.*

During the qualitative risk assessment process, MCC identified the compact fund as a potential high risk of susceptibility to significant improper payments based on the risk scoring. As a result, MCC elected to perform testing on the compact fund to validate its risk assessment results.

Sampling and Estimation

MCC conducted statistical sampling of the compact fund and tested the selected sample. The scope of the sampling and testing efforts covered the period from July 1, 2016 to June 30, 2017. The objective of the sampling was to:

- Select a statistically valid random sample of sufficient size to support an estimate with a 90 percent confidence interval of plus or minus 2.5 percent around the estimate of the percentage of improper payments.
- Select a sample from all compact disbursement transactions, excluding intragovernmental payments, and compose the population so that each item had an opportunity for selection.
- Select a representative sample 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 underpayments [i .e ., not the net of over and under payments]).

MCC utilized a stratified random sample design. The population data was divided into groups, or strata, and each stratum was sampled separately, with different sampling rates to increase the efficiency of the design. During estimation, the sample is appropriately weighted to reflect the sampling rates for the different strata. The design variable was an individual invoice's amount. The final sample design is shown below.

Each sample was tested to validate that all payments were made in the correct amount under statutory, contractual, administrative, or other legally applicable requirements. A review of supporting documentation, including but not limited to vendor submitted invoices, approval forms, and systems reports, was conducted to verify the validity of each payment. OMB Circular No. A-123, Appendix C, 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 that are 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).

Stratum Number	Stratum Definition	Population Size	Population Amount	Sample Size	Sample Amount
1	$0 to $39,570	2,679	$ 19,097,556	9	$ 68,554
2	$39,571 to $127,923	791	58,750,920	9	599,451
3	$127,924 to $289,579	356	64,801,319	9	1,574,533
4	$289,580 to $531,374	182	72,549,845	9	3,501,918
5	$531,735 to $865,843	113	75,718,487	9	6,242,974
6	$865,844 to $1,685,705	64	71,726,253	9	11,501,502
7	$1,685,706 to $4,199,999	24	62,529,154	9	23,791,814
8	$4,200,000 and above	10	75,926,330	10	75,926,330
Total		**4,219**	**$ 501,099,864**	**73**	**$ 123,207,076**

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 as a result of insufficient or lack of documentation, this payment must also be considered an improper payment. MCC did not identify any improper payments based on its testing. As a result, MCC validated its risk assessment approach and conclusions.

Readers can find more detailed information on improper payments, including information previously reported in Performance and Accountability Reports (PAR) and AFRs related to Federal government agencies that are not included in current year disclosures at https://paymentaccuracy.gov/.

Recapture of Improper Payment Reporting

OMB Circular No. A-123, Appendix C, requires agencies to have a cost-effective program of internal control to prevent, detect, and recover overpayments. For agencies that have programs and activities that expend more than $1 million in a fiscal year, a payment recapture audit program is a required element of their internal controls over payments if conducting such audits is cost-effective. MCC conducted an analysis and determined that the recapture audits would not be cost-effective. During assessment periods prior to 2017, MCC did not identify any funds susceptible to significant improper payments based on the risk assessment methodology. Additionally, MCC voluntarily conducted statistical testing and identified no improper payments during the previous five assessment periods. However, the 2017 qualitative risk assessment identified one fund, the MCC compact fund, which was assessed as susceptible to significant improper payments. MCC elevated this fund from a moderate level in previous assessments to a high level in 2017 due to a reassessment of inherent risk during the Risk Assessment Process. Although MCC self-identified improper payments during the period of July 1, 2016 through June 30, 2017, the improper payments did not exceed the OMB thresholds and were mainly isolated incidents based on historical results. These improper payments have been recovered or will be recovered during the upcoming FY. Additionally, no improper payments were identified during current year OMB Circular No. A-123, Appendix C, testing on the compact fund as discussed in the previous section. The remaining MCC funds were not assessed as susceptible to significant improper payments. MCC also self-identified improper payments related to these funds, but a significant portion was related to a SSP Duplicate Payment Schedule previously disclosed in the FY 2016 AFR. The remaining portion consisted of OIG audit reports and prompt payment interest.

Based on previous testing history and the isolated nature of significant self-identified improper payments, MCC concluded that a payment recapture audit would not be cost effective and would not add benefit to the MCC internal control structure for all MCC funds. As a result, OMB concurred with this analysis in September 2017. MCC plans to reevaluate in future FYs as part of its OMB Circular No. A-123 Assessment Program.

Although MCC identified no improper payments during compact fund testing and received OMB approval related to the completion of recapture audits, MCC occasionally identifies improper payments through internal control processes and other reviews, including OIG reporting. In these instances, MCC pursues recapture of overpayments appropriately. MCC expects full recovery of all outstanding improper payments. Table 11 provides a summary and outcome of self-identified improper payments and recovery efforts:

Table 11. Overpayments Recaptured Outside of Payment Recapture Audits			
Fund	Amount Identified for Recapture[2]	Amount Recaptured	Recapture Rate
Administrative[3]	$ 459,774.52	$ 340,504.49	74%
Compact	1,462,017.87	1,212,381.72	83%
Due Diligence[4]	55,589.95	55,389.95	100%
Threshold	30,000.00	30,000.00	100%
Total	**$ 2,007,182.34**	**$ 1,638,276.16**	**82%**

[2] The "Amount Identified for Recapture" column includes overpayments which are eligible to be recaptured.

[3] The Administrative Fund includes the amounts related to an overseas payroll issue totaling $402,401.38 previously identified and disclosed in the FY 2016 AFR. MCC recaptured $283,507.70 as of September 30, 2017. Both amounts are included in the Administrative Fund Line Item in the table. MCC continues to actively pursue collection and expects full recovery.

[4] The amount identified is related to an improper payment originally identified and disclosed in the FY 2016 AFR. However, MCC originally disclosed that the amount was fully recovered in FY 2016, but actual recovery occurred in early October 2016. Therefore, MCC is disclosing it in FY 2017 for informational purposes.

Agency Improvement of Payment Accuracy with the Do Not Pay Initiative

Processing payments accurately and timely is a top priority for MCC. The Contracts and Grants Management Division strictly adheres to the Federal Acquisition Regulations (FAR) and ensures potential MCC vendors are registered in the System Acquisition Management (SAM), are not on the excluded party listing, and are not prohibited from competing for Federal Government acquisitions. MCC's financial service provider, IBC, checks and verifies vendors' information before entering MCC vendor data into the core financial management system (Oracle) and before issuing payments. IBC issued a total of 6,602 payments to MCC local and foreign vendors during FY 2017. IBC has developed a custom process to house the results of the Do Not Pay (DNP) Continuous Monitoring data. MCC participates in that process and uses Oracle Discoverer to retrieve the results of these monitoring activities. Prior to submitting an Oracle Vendor request form to IBC, the MCC Contracts and Grants Management Division ensures that the vendor is not listed on the DNP listing.

MCC works diligently with its SSP to maintain oversight of payments. MCC adjudicated those payments monthly on the DNP portal and researched all matches or flags for any probable or possible improper payments. During FY 2017, MCC issued no stop payment orders and the Treasury DNP system did not report any payments with matches either through the Death Master File (DMF) or the SAM. In cases where DNP were to provide a listing of unmatched payments, which were payments that Treasury could not match to the DMF or SAM, MCC would investigate through the DNP Discoverer application within Oracle to verify the payments before adjudicating the monthly report on the DNP Portal.

Fraud Reduction Report

In accordance with the Fraud Reduction and Data Analytics Act of 2015, MCC is required to report on its fraud reduction efforts and progress in regard to the following topics:

- Establishment of strategies to curb fraud.
- Identification of fraud risks and vulnerabilities.
- Execution of the fraud risk principle in the GAO's *Standards for Internal Control in the Federal Government.*
- Application of OMB Circular No. A-123, *Management's Responsibility for Enterprise Risk Management and Internal Control,* with respect to leading practices for managing fraud risk.
- Implementation of financial and administrative controls.

MCC utilized the GAO's *Standards for Internal Control in the Federal Government* and OMB Circular No. A-123, *Management's Responsibility for Enterprise Risk Management and Internal Control,* to ensure compliance with the Act, along with GAO's *A Framework for Managing Fraud Risks in Federal Programs* as a best practice.

MCC's anti-fraud and corruption program is led by the Anti-Fraud and Corruption Team (AFC Team), within the Office of the General Counsel. The AFC Team provides direction and oversight for the agency in regards to preventing and detecting fraud in MCC-funded operations under its compact and threshold programs carried out by MCC and its Accountable Entities (the local units, sometimes also referred to as MCAs, which implement each country's MCC Compact Program or Threshold Program). The AFC Team developed a Five Pillar Strategy to prevent, detect, and remediate fraud and corruption:

- **AFC Policy** — The document covers the roles, responsibilities, and principles that govern activities of MCC and entities funded by the MCC with respect to preventing, detecting, and remediating risks of fraud and corruption in MCC compact and threshold programs.
- **Mandatory Training** — In-depth Fraud Awareness Training is required for all MCC staff in operations related to an MCC compact or threshold program, and encouraged for all non-operational staff. The AFC Team conducts in-country trainings with MCA staff early during the compact or threshold implementation. All AFC training includes real-world examples from, among other sources, allegations of fraud and corruption from past and current MCC-funded operations, as well as historical trends and lessons learned from AFC allegations and findings.
- **Mitigants** — MCC relies on existing policies, procedures, and internal controls throughout the budgeting, procurement, and disbursement process to mitigate the risks of fraud and corruption.
- **Assessments and Action Plans** — MCC and the MCA jointly prepare compact-specific AFC Risk Assessments early during the compact process, after the MCA staff have participated in their in-country AFC trainings. The Risk Assessment process includes a field study to gain perspectives, broaden discussion, and complete the risk matrix and corresponding action plans. Risks assessed at a high level are incorporated into a publicly released AFC Action Plan to implement additional safeguards. The MCA is responsible for publicly reporting on the implementation of the AFC Action Plan on an annual basis.
- **AFC Team** — MCC has staff who are designated to receive, screen, and manage allegations in consultation with the USAID Office of Inspector General Investigation Team (OIG/I). In order to report allegations, all MCC and MCA staff are aware of the OIG hotline to report allegations of potential fraud.

In addition, MCC began to implement its ERM Program during FY 2016. MCC hired a Chief Risk Officer to provide oversight of the process and assist in the development of the ERM Program. MCC also established a Risk Committee during FY 2017 under the leadership of its Chief Risk Officer. The Risk Committee is a multi-disciplinary group with membership drawn from all six MCC departments. The Risk Committee meets on a periodic basis and focuses on program risk and ERM topics, including formalization of MCC's ERM Program and development of an agency-wide Risk Profile following guidance contained in the revised OMB Circular A-123. MCC utilized a consulting firm to assist in the development of its initial Risk Profile. The consulting firm conducted interviews with MCC Senior Management to identify the most prevalent risks affecting the agency. Afterwards, it consolidated the risks into a list (a "risk register") and identified risk drivers, potential consequences, and current management actions based on the senior management interviews. As part of the Risk Profile development process, MCC created an internal work group which analyzed the consolidated risk listing, discussed the risk drivers, potential consequences, and current management actions in an open forum, and voted to identify the most important risks facing the agency. Utilizing the voting, MCC developed a Risk Profile, along with risk ratings pertaining to inherent risk (the level of risk present if no controls existed to mitigate the risk event), the likelihood that a risk event may occur, the impact if the risk occurred, and an overall residual risk rating considering current management actions and control activities. The Risk Committee reviewed the document and approved the risk ratings. Fraud risk was identified during the ERM process as one of the key risks affecting the agency.

As part of the OMB A-123 Assessment Program, MCC also considers fraud risk affecting all cycles in conjunction with its Three Year Assessment Plan. These cycles include accounts payable and disbursement management, human resources and payroll management, grants management (i.e., MCC-managed grants, compacts, and thresholds), and procurement management. The fraud risk category is based on Principle 8, Assess Fraud Risk, in GAO's *Standards for Internal Control in the Federal Government.* MCC reassesses fraud risk affecting all cycles on an annual basis during the OMB A-123 planning phase and documents the results in the Three Year Assessment Plan.

Based on MCC's fraud strategy, the agency has a heavy focus on preventive controls. However, MCC also has detective controls in place to identify potential fraud. The table below provides a brief summary of preventive and detective controls related to MCC's anti-fraud and corruption activities. These controls can be categorized as financial and administrative, but MCC identified the controls as preventive and detective to better illustrate the control environment mitigating fraud risk at the agency.

MCC has made progress in implementing and developing its fraud risk program, and will continue to strengthen it in subsequent years as the program matures.

Preventive Controls	Detective Controls
▶ MCC implemented an AFC team to oversee the prevention and detection of potential fraud at MCC and its MCAs. ▶ The AFC team implemented a policy to direct and govern activities with the agency, MCAs, and OIG/I. ▶ MCC operational staff and MCA employees are required to attend AFC trainings. ▶ MCC employees are required to attend an Ethics Training on an annual basis. ▶ The OIG/I holds Fraud Awareness Briefings for MCC and MCA staff. ▶ Compacts and threshold programs have implemented policies and procedures related to procurements and disbursements. ▶ The AFC Team and OIG/I have open communication regarding fraud referrals and investigations. All potential fraud is referred to the OIG/I immediately. ▶ MCC and MCA employees are aware of the USAID OIG Fraud Hotline to report potential fraud and corruption. ▶ Administrative interventions and sanctions are available as forms of remediation based on potential fraud and corruption cases and investigations.	▶ The annual MCA and threshold audit program contain steps to address and report fraud. ▶ Independent auditors review policies and procedures as part of required annual audits, and test the overall design and operating effectiveness of internal controls. The auditors are required to report to the OIG if testing identifies potentially fraudulent transactions. ▶ The OMB A-123 engagement performs process and transaction-level testing to verify controls are designed and operating effectively. ▶ MCC conducts statistical testing related to OMB A-123, Appendix C, *Requirements for Effective Estimation and Remediation of Improper Payments.* The testing identifies potential improper payments. ▶ MCC and MCA officials conduct random site visits to operating field locations. ▶ MCC requires independent oversight of programs including monitoring and evaluation.

Grants Oversight and New Efficiency Act Requirements

The Grants Oversight and New Efficiency Act of 2016 (GONE) prescribes reporting requirements to ensure agencies are performing timely close-out activities for expired grants. Table 12 illustrates the number of MCC grants and cooperative agreements for which closeout has not yet occurred as of September 30, 2017, but for which the period of performance has elapsed by more than two years.

MCC is currently working towards closing out all of these agreements and anticipates that these will be closed by December 31, 2018. MCC anticipates recovering most, if not all, of the undisbursed amount and is in the process of preparing the closeout documentation.

Table 12. Grant and Cooperative Agreement Closeout Monitoring

Category	2–3 Years	> 3–5 Years	> 5 Years
Number of Grants/Cooperative Agreements with Zero Dollar Balances	0	2	3
Number of Grants/Cooperative Agreements with Undisbursed Balances	0	0	2
Total Amount of Undisbursed Balances (in thousands)	**$0**	**$0**	**$300**

Appendix

Appendix A: Acronyms

Acronym	Definition
AFC	Anti-Fraud and Corruption
AFR	Agency Financial Report
AGOA	African Growth and Opportunity Act
AICPA	American Institute of Certified Public Accountants
APR	Annual Performance Report
CBJ	Congressional Budget Justification
CEO	Chief Executive Officer
CFO	Chief Financial Officer
CIF	Compact Implementation Fund
CIO	Chief Information Officer
CSRS	Civil Service Retirement System
DATA Act	Digital Accountability and Transparency Act of 2014
DMF	Death Master File
DNP	Do Not Pay
DOL	Department of Labor
ERM	Enterprise Risk Management
FAR	Federal Acquisition Regulation
FASAB	Federal Accounting Standards Advisory Board
FBWT	Fund Balance with Treasury
FECA	Federal Employees Compensation Act
FERS	Federal Employees Retirement System
FFATA	Federal Funding Accountability and Transparency Act of 2006
FFMIA	Federal Financial Management Improvement Act
FISMA	Federal Information Security Modernization Act of 2014
FMFIA	Federal Managers Financial Integrity Act
FPPS	Federal Personnel Payroll System
FTE	Full-time Equivalent
FY	Fiscal Year
GAAP	Generally Accepted Accounting Principles
GAO	Government Accountability Office
GONE	Grants Oversight and New Efficiency Act of 2016
HSPD-12	Homeland Security Presidential Directive 12
IAA	Interagency Agreement
IAF	Inter-American Foundation
IBC	Interior Business Center
IG	Inspector General
IPBE	Integrated Planning, Budgeting, and Execution
IPIA	Improper Payments Information Act

Acronym	Definition
IT	Information Technology
IT-IRB	Information Technology Investment Review Board
M&E	Monitoring and Evaluation
MCA	Millennium Challenge Account
MCC	Millennium Challenge Corporation
MD&A	Management's Discussion and Analysis
NIST	National Institute of Standards and Technology
OFF	Oracle Federal Financial System
OIG	Office of Inspector General
OIG/I	Office of Inspector General Investigative Team
OMB	Office of Management and Budget
OPIC	Overseas Private Investment Corporation
OPM	Office of Personnel Management
PII	Personally Identifiable Information
PIV	Personal Identity Verification
PL	Public Law
PP&E	Property, Plant, and Equipment
SAM	System for Award Management
SBR	Statement of Budgetary Resources
SF	Standard Form
SFFAS	Statement of Federal Financial Accounting Standards
SP	Special Publication
SSAE	Statement on Standards for Attestation Engagements
SSP	Shared Service Provider
TSP	Thrift Savings Plan
UNESCO	United Nations Educational, Scientific and Cultural Organization
UNICEF	United Nations Children's Fund
USADF	United States African Development Foundation
USAID	United States Agency for International Development
U.S.	United States
U.S.C	United States Code
USD	United States Dollars
USG	United States Government
USSGL	United States Standard General Ledger
USTDA	United States Trade and Development Agency
WHO	World Health Organization

MCC Welcomes Your Comments

MCC welcomes comments and suggestions regarding this report.

Please contact MCC at:

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

or write to:

1099 14th Street, NW
Suite 700
Washington, DC 20005-3550
(202) 521-3600

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

Reducing Poverty Through Growth

MILLENNIUM
CHALLENGE CORPORATION
UNITED STATES OF AMERICA

1099 14th Street, NW • Suite 700
Washington, DC 20005-3550
www.mcc.gov

2017-001-2013