



Office of Inspector General

October 10, 2012

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

Dear Mr. Yohannes:

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

The Reports Consolidations Act of 2000 (Public Law 106-531) requires that agency performance and accountability reports include a statement prepared by each agency's inspector general, summarizing the most serious management and performance challenges facing the agency and reporting the agency's progress in addressing those challenges. The enclosed statement will be included in MCC's fiscal year 2012 agency financial report.

We have discussed the management and performance challenges summarized in this statement with responsible MCC officials. If you have any questions or wish to discuss the statement further, please contact me or Richard Taylor, Deputy Assistant Inspector General for Audit for the Millennium Challenge Corporation.

Sincerely,

/s/

Michael Carroll
Deputy Inspector General

Enclosure

STATEMENT BY THE OFFICE OF INSPECTOR GENERAL:

MILLENNIUM CHALLENGE CORPORATION'S MOST SERIOUS MANAGEMENT AND PERFORMANCE CHALLENGES

Fiscal Year 2012

The Millennium Challenge Corporation (MCC) faces its most serious management and performance challenges in the following areas:

- Financial Management
- Information Technology Management
- Managing for Results

Financial Management

Financial management is critical to providing reliable financial information, managing results, and ensuring the effectiveness and efficiency of operations, including the use of an entity's resources. Significant MCC activities, liabilities, and expenses occur in the compact programs implemented by various Millennium Challenge Accounts (MCAs) across the globe.

MCC received an unqualified opinion on its FY 2011 financial statements; however, the audit report included two material weaknesses and two significant deficiencies in internal control.

During FY 2012, MCC continued its efforts to improve its financial management system; however, the current audit has identified issues that indicate ongoing challenges in MCC's ability to prepare complete and reliable financial statements. The challenges include the following:

Recording Compact Recipient Accruals and Advances. MCC's financial management system follows the guidance prescribed by the Federal Accounting Standards Board, whereas the independent MCAs established by recipient countries do not. MCC is in the process of addressing this challenge by adjusting its Advances and Liabilities accounts at the MCC level, in order to bring the cash basis reporting by MCAs to MCC's accrual basis. MCC has revised its accrual methodology by incorporating disbursement history, unused spending authority, and invoices received but not paid to estimate accruals. MCC will use this methodology to estimate accruals as of September 30, 2012. Advances will still be reported based on information provided by the MCAs through data calls. MCC should continue its efforts to enhance its accrual (liability) and advance (asset) estimation methodology for its compact recipients. In addition, MCC should implement policies and procedures to assess the accuracy of the estimation assumptions and methodology.

Manual Financial Processes. MCC's accounting department continues to rely on manual financial reporting processes and quality control. This is a control deficiency because manual processes are vulnerable to human error.

Information Technology Management

Since FY 2008, OIG has reported information technology (IT) management challenges affecting MCC. For FY 2013, OIG considers MCC's Privacy Program and its IT Governance Program to be serious management challenges.

Privacy Program. Last year OIG removed MCC's Privacy Program from its listing of serious management challenges because MCC had reported that final action had been taken on all 18 recommendations in OIG's July 2010 audit report¹. However, during FY 2012 the OIG followed up on MCC's implementation of selected recommendations from that report and compliance with new privacy requirements. The audit concluded that 5 recommendations had not been fully implemented and identified a number of new weaknesses. Therefore, OIG made 22 recommendations to further strengthen MCC's Privacy Program. Consequently, OIG considers MCC's Privacy Program to be a management challenge.

IT Governance. Similar to last year, OIG continues to consider IT governance as a serious management challenge. In June 2011, an OIG contractor reported that weaknesses in MCC's IT governance processes may (1) increase IT project costs, (2) lengthen deployment, and (3) deliver solutions that do not satisfy business needs. Similarly, in January 2011, OIG reported that such risks led MCC to spend more than \$6.9 million for a system that only partially met its needs. The two reports included 32 recommendations to help MCC achieve an appropriate level of IT governance and control. In response, MCC developed a 17-month plan as a roadmap to improve IT management, with the final phase to be completed by December 2012.

Managing for Results

MCC has approved 26 compact agreements totaling approximately \$9.3 billion in foreign aid to reduce poverty and increase economic growth through programs to improve the efficiency of moving people and goods and the productivity of the agriculture sector among other programs. MCC faces challenges for ensuring that these programs achieve planned results.

Compact Planning. In its FY 2012 review of 23 compacts signed from 2005 to 2011, OIG found that 6 compacts had been significantly modified with changes exceeding \$10 million per compact because of incomplete planning.² Incomplete planning occurred because critical studies, such as final feasibility studies, were not completed until after entry into force. MCC has undertaken efforts to strengthen the compact development process by revising its *Compact Development Guidance* in January 2012.

¹ Audit of the Millennium Challenge Corporation's Implementation of Key Components of a Privacy Program for its Information Technology Systems, Report No. M-000-10-003-P dated July 9, 2010.

² Incomplete planning was identified in El Salvador, Ghana, Mali, Morocco, Mozambique, and Tanzania.

Compact Implementation. OIG identified implementation challenges that resulted in significant modifications to 7 MCC compacts in its FY 2012 review of 23 compacts.³ These implementation challenges took many forms, including unfilled host-country agreements, increased costs during implementation, underperforming/nonperforming contractors, and environmental risks not identified during the project planning stage. To address these issues, MCC has taken actions including cancelling projects or portions of them, reallocating funds from other projects to cover budget shortfalls, and terminating contractors and rebidding contracts.

Sustainability. In addition, an audit found that MCC needed to improve the quality of construction and renovation of schools in Namibia: the drainage around the new schools and latrines was not always sufficient to prevent flooding caused by heavy rains and masonry workmanship was of poor quality. Improved project execution could better ensure the long-term sustainability of the schools. Finally, an audit found that unless health services were properly decentralized and functional upon health center completion in Lesotho, risk to the sustainability of the health centers existed, for example, in drug, waste, and facilities management.

³ Implementation challenges were identified in Benin, El Salvador, Ghana, Mali, Mongolia, Morocco, and Vanuatu.