OFFICE OF INSPECTOR GENERAL

AUDIT OF THE MILLENNIUM CHALLENGE CORPORATION'S FINANCIAL STATEMENTS, INTERNAL CONTROLS, AND COMPLIANCE FOR THE FISCAL YEARS ENDING SEPTEMBER 30, 2015, AND 2014

AUDIT REPORT NO. M-000-16-001-C
NOVEMBER 13, 2015

WASHINGTON, D.C.

Office of Inspector General

November 13, 2015

Ms. Dana J. Hyde
Chief Executive Officer
Millennium Challenge Corporation
875 15th Street, NW
Washington, DC 20005-2203

Subject: Audit of the Millennium Challenge Corporation's Financial Statements, Internal Controls, and Compliance for the Fiscal Years Ending September 30, 2015, and 2014 (Audit Report No. M-000-16-001-C)

Dear Ms. Hyde:

Enclosed is CliftonLarsonAllen LLP's final report on the subject audit. The Office of Inspector General (OIG) contracted with the independent certified public accounting firm to audit the financial statements of the Millennium Challenge Corporation (MCC) for the fiscal years (FYs) ending September 30, 2015, and 2014. The contract required that the audit be performed in accordance with U.S. generally accepted government auditing standards, Office of Management and Budget (OMB) Bulletin 15-02, *Audit Requirements for Federal Financial Statements*, and the Government Accountability Office/President's Council on Integrity and Efficiency *Financial Audit Manual*.

The independent auditor expressed an unmodified opinion on MCC's FY 2015 financial statements. The report states that they present fairly, in all material respects, the net position of MCC as of September 30, 2015, and 2014, and its net cost, changes in net position, and budgetary resources for the fiscal years then ended, in conformity with accounting principles generally accepted in the United States. In addition, CliftonLarsonAllen reported no instances of noncompliance with certain provisions of laws and regulations that could have a direct and material effect on the determination of the amounts in the financial statements.

In MCC's FY 2015 financial statements, the auditor identified three matters involving the internal control over financial reporting that were considered significant deficiencies. These matters are listed below and are detailed in the auditor's report.

Washington, DC 20523
http://oig.usaid.gov

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

The three significant deficiencies were:

- Uncorrected misstatements in FY 2015 financial statement because of MCC's failure to account for advances and their liquidation in a Millennium Challenge Account's (MCA's) permitted account (new finding)

- Validation controls over grant accrual estimates were weak (modified repeat finding)

- Core (general ledger) system's systemic errors (modified repeat finding)

In carrying out its oversight responsibilities, OIG reviewed the audit report and audit documentation provided by CliftonLarsonAllen. This review is different from an audit in accordance with U.S. generally accepted government auditing standards and was not intended to enable OIG to express, and we do not express, opinions on MCC's financial statements, internal control, or compliance with laws, regulations, contracts, or grant agreements. CliftonLarsonAllen is responsible for the attached auditor's report, dated November 13, 2015, and the conclusions expressed in it. However, our review disclosed no instances in which CliftonLarsonAllen did not comply, in all material respects, with applicable standards.

To address the three significant deficiencies in internal controls reported by CliftonLarsonAllen, we are listing four recommendations to MCC's management below.

> ***Recommendation 1.*** *We recommend that MCC's Department of Administration and Finance perform a more comprehensive review of advances by comparing MCA advances reported to MCC to the source data maintained by the fiscal agent.*
>
> ***Recommendation 2.*** *We recommend that MCC's Department of Administration and Finance employ substantive fluctuation and trend analyses of the advances account and promptly investigate unusual fluctuation and trends.*
>
> ***Recommendation 3.*** *We recommend that MCC enhance its Expense Accruals Financial Management Division Procedure Manual to:*
>
> a. *Define the criteria for when the assumption that MCC's maximum liability being equivalent to unused spending authority at the end of the quarter is not valid and why.*
>
> b. *Fully address the MCA confirmation process and how it is carried out and documented.*
>
> c. *Incorporate the desk procedures so that the procedures are formally reviewed and approved.*
>
> d. *Address how a grant accrual estimate provided by an MCA should be evaluated to determine if it is reasonable.*

e. Establish a procedure to ensure that MCC provides an MCA with sufficient time to address MCC's request to assess the reasonableness of the MCC calculated grant accrual for an MCA.

f. Formalize the guidance provided to an MCA on what supporting documentation should be provided to address the reasonableness of the MCC calculated grant accrual for an MCA or providing an accrual estimate for an MCA to MCC.

Recommendation 4. *We repeat the prior years' recommendation that MCC's Department of Administration and Finance continue to investigate and correct the root causes for the system limitations or problems that prevent or delay the recording, processing, and summarizing of accounting transactions.*

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

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

Sincerely,

/s/

Nathan Lokos
Assistant Inspector General for Audit
U.S. Agency for International Development
Office of Inspector General

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MILLENNIUM CHALLENGE CORPORATION

September 30, 2015

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CliftonLarsonAllen LLP
www.cliftonlarsonallen.com

INDEPENDENT AUDITORS' REPORT

To the Inspector General
U.S. 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 the Millennium Challenge Corporation (MCC), which comprise the balance sheets as of September 30, 2015 and 2014, and the related statements of net cost, changes in net position, and 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 audits. We conducted our audits in accordance with auditing standards generally accepted in the U.S.; the standards applicable to financial audits contained in the *Government Auditing Standards*, issued by the Comptroller General of the United States; and Office of Management and Budget (OMB) Bulletin No. 15-02*, Audit Requirements for Federal Financial Statements* (OMB Bulletin 15-02). Those standards and OMB Bulletin 15-02 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 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 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. 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 the Millennium Challenge Corporation as of September 30, 2015 and 2014, 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. issued by the Federal Accounting Standards Advisory Board (FASAB) require that the MCC's Management Discussion and Analysis (MD&A) on pages 7 through 32 be presented to supplement the financial statements. Such information, although not a part of the financial statements, is required by FASAB who considers it to be an essential part of financial reporting for placing the financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the MD&A in accordance with auditing standards generally accepted in the U.S., which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the financial statements, and other knowledge we obtained during our audit of the financial statements. We do not express an opinion or provide any assurance on the MD&A 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 on pages 3 and 4, Message from the Vice President, Department of Administration and Finance (DAF) and Chief Financial Officer on page 35, and other information on pages 75 to 109, are presented for purposes of additional analysis and is not a required part of the financial statements or Required Supplementary Information. 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 on Compliance Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*

Report on Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered MCC's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the 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 assertion on internal control included in the MD&A. We did not test all internal controls relevant to operating objectives as broadly defined by the Federal Managers' Financial Integrity Act of 1982 (FMFIA).

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 were not 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 certain deficiencies in internal control, described below and in Exhibit 1 that we consider to be significant deficiencies.

1. Uncorrected misstatements in FY 2015 financial statement because of MCC's failure to account for advances and their liquidation in an MCA's permitted account (new finding) - MCC DAF recorded the change in Advances in FY 2015 quarter 1 without considering the impact of the error on the FY 2015 financial statements until we requested an analysis. The accounting error resulted in FY 2015 expenses being understated by $19 million, and FY 2014 and FY 2013 expenses overstated by $0.6 million and $18.4 million, respectively. MCC included the uncorrected misstatements adjusting entries in a schedule attached to the MCC representation letter provided to the auditor. Also, the MCA incorrectly omitted $1.4 million advance liquidation in its June 30, 2015, certified data call report thereby overstating the Advances and understating the expenses. This error was corrected at September 30, 2015.

2. Validation control over grant accrual estimates were weak (modified repeat finding) - We noted certain issues that impacted the quarterly grant accrual during the year evidencing the need to continue strengthening the validation control and to enhance the grant accrual policy and procedures.

3. Core (general ledger) system's systemic errors (modified repeat finding) - The root causes of recording errors are due to system's limitations [for example: a) Purchase Order (PO) module does not interface properly with the GL module; b) Accounts Payable (AP) module does not interface properly with the GL module, c) incorrect accounting posting model, d) system module interface errors, and f) obligation/funding and/or disbursement posting errors], these systemic errors continue to exist.

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. Given these limitations, material weaknesses or significant deficiencies may exist that have not been identified.

Report on Compliance

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 and material effect on the determination of financial statements amounts.

The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported in accordance with *Government Auditing Standards* or OMB Bulletin No. 15-02.

Management's Responsibilities for Internal Control and Compliance

Management is responsible for (1) evaluating the effectiveness of internal control over financial reporting based on criteria established under 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 applicable to MCC noncompliance with which could have a direct and material effect on the determination of financial statements amounts.

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

We did not test compliance with all laws, regulations, contracts and grant agreements applicable to MCC. We limited our tests of compliance to certain provisions of laws, regulations, contracts, and grant agreements applicable to MCC noncompliance with which could have a direct and material effect on the determination of financial statements amounts. 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. 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 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 and Noncompliance Issues

We have reviewed the status of MCC's corrective actions with respect to the findings included in the prior year's Independent Auditors' Report, dated November 12, 2014. 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 and Other Matters

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

CliftonLarsonAllen LLP

CliftonLarsonAllen LLP

Arlington, Virginia
November 13, 2015

EXHIBIT 1
Significant Deficiencies

1. Uncorrected Misstatements in FY 2015 Financial Statement because of MCC's Failure to Account for Advances and their Liquidation in an MCA's Permitted Account (New Finding)

A permitted account is a bank account used by a Millennium Challenge Account (MCA) like a petty cash account primarily to pay smaller purchases or vendors in local currency. Using a permitted account for large disbursements including advances is not a typical process for the MCAs. However, one MCA was allowed by the MCC Department of Compact Operations (DCO) to use permitted account to make disbursements, including Advances, after it demonstrated that the local currency provided a better exchange rate. The MCA started using the permitted account to make Advances on its contracts beginning in 2013. Although the MCC DCO was aware of this arrangement, the MCC Department of Administration and Finance (DAF) was not aware that an MCA was using its permitted account differently from other MCAs until FY 2015.

There are two different ways disbursements made to MCA are recorded that impact Advances:

(1) The typical Advance is originally recorded as an expense when MCC makes a disbursement. At the end of each quarter, MCC DAF initiates data calls to MCAs requesting information on Advances as of a reporting date. MCC DAF then records the Advances reported by the MCAs as an asset by reducing previously recorded expenses.

(2) The untypical Advance is a disbursement made to a permitted account, which is recorded immediately as an Advance at the time of disbursement, then is liquidated based on the monthly reporting provided by the MCAs.

Due to the untypical nature of the Advances from permitted account and the lack of clarity of the data call instructions, the MCA had not reported the Advances paid out of the permitted accounts in 2013 and 2014. However, for FY 2015 quarter 1, MCC DCO, working with MCC DAF, clarified its instructions to the MCA and required the MCA to report all Advances (typical and untypical). As a result, the MCA advances went up from $79,000 at September 30, 2014, to $18.1 million at December 31, 2014.

MCC DAF recorded the change in Advances in FY 2015 quarter one without considering the impact of the error on the FY 2015 financial statements until we requested an analysis. The accounting error resulted in FY 2015 expenses being understated by $19 million, and FY 2014 and FY 2013 expenses overstated by $0.6 million and $18.4 million, respectively. Since the uncorrected misstatements in FY 2014 and 2015 were not material to the financial statements taken as a whole, MCC included the uncorrected misstatements adjusting entries in a schedule attached to the MCC management representation letter provided to the auditor.

In addition to the control deficiency described above on the MCC's failure to record Advances from the permitted account due to the deficiency in the data call process, we also noted a data call reporting error for $1.4 million in the MCA's June 30, 2015, certified data call. The MCA incorrectly omitted a $1.4 million advance liquidation thereby overstating the Advances and understating the expenses. This error was corrected at September 30, 2015.

GAO *Standards for Internal Control* in the Federal Government states internal control is not one event, but a series of actions and activities that occur throughout an entity's operations and on an ongoing basis. Some control activities include: proper execution of transactions and events and accurate and timely recording of transactions and events.

EXHIBIT 1
Significant Deficiencies

Recommendation 1. *We recommend that MCC Department of Administration and Finance perform a more comprehensive review of advances by comparing MCA advances reported to MCC to the source data maintained by the fiscal agent.*

Recommendation 2. *We recommend that MCC Department of Administration and Finance employ substantive fluctuation and trend analyses of the advances account and promptly investigate unusual fluctuation and trends*.

2. Validation Control over Grant Accrual Estimates were Weak (Modified Repeat Finding)

MCC reported approximately $621 million in compact grant related expenses and an accrued grant liability of $142 million for expenditures incurred by the MCC Compact Accountable Entities (also known as Millennium Challenge Accounts or MCAs) but not yet paid by MCC as of September 30, 2015.

In FY 2015, MCC continues to refine its accrual methodology and continues to accumulate data store to validate its methodology. However, we noted certain issues discussed below that impacted the quarterly grant accrual during the year evidencing the need to continue strengthening the validation control and to enhance the grant accrual policy and procedures.

- The grant accrual policy and procedures allows MCC staff to use accrual estimates provided by the MCAs under certain conditions, but it does not indicate what validation steps MCC staff should take to ensure that the accrual estimate is reasonable. Accordingly, certain quarterly accruals were recorded without full validation of the reasonableness of the amount. For example:

    - The first quarter 2015 total accrued estimated liability was approximately $122 million. The MCC grant accrual validation or look back analysis only accounted for $65 million, resulting in a difference of approximately $57 million. $55 million of the $57 million difference was due to one MCA, whose compact ended in September 2015. This MCA's accrued amount was $83 million (68 percent of the $122 million) and the MCC look back analysis was only $27 million. This MCA's estimated accrual reported to MCC exceeded the MCA's unused spending authority by approximately $24 million, or 42 percent. Had MCC DAF performed a trend analysis of this MCA's past history, it would show that this MCA was unlikely to exceed its unused spending authority. MCC did not take sufficient steps to ensure that the accrual estimate provided by the MCA was reasonable.

- The following deviations related to the grant accrual methodology process occurred:

    - For the first and fourth quarters, MCC accepted a grant accrual from several MCAs that were closing this fiscal year that exceeded the MCAs' unused spending authority. This is contrary to MCC's assumption that the maximum liability is the unused spending authority for the end of that quarter. In addition, a non-closing MCA also provided grant accrual estimates for the first three quarters that exceeded the MCA's unused spending authority for those quarters. MCC did not address this conflict by providing a justification under what circumstances that this assumption would not be valid and why. Inconsistency in applying the grant accrual methodology could adversely impact the grant accrual results and the reliability of the grant accrual data.

- MCC's *Expense Accruals Financial Management Division Procedure Manual*, dated June 2015, 1.3. Country Grant Accruals, states,

  In addition, MCC must take a different approach for determining the amount of the quarterly grant accrual in any of the following situations:

  - o The MCA or fiscal accountability director provides the accrual amount

  The bullet above does not identify the situation in which the MCC would accept an accrual amount from the MCA or fiscal accountability director. However, we were informed that after each quarter the Financial Management Division (FMD) issues an email to the DCO, Fiscal Accountability Officer to provide the MCAs with the calculated accrual amount, which is supposed to represent the amount of work completed before the end of the quarter. The MCAs were to review the figure and confirm that it is a reasonable estimation of work completed before the end of the quarter, but not yet billed or paid by the end of the quarter. For those compacts that were closing this fiscal year, the MCA must provide FMD with the accrual amount to enable a better estimate of work completed, but not yet paid or invoiced. MCC management indicated that starting in the fourth quarter FY 2015, the emails were sent directly to the MCAs and the DCO received a copy. This process is only addressed by a single sentence in an informal desk procedure.

  MCC did not update its grant accrual procedures to reflect this key control that involves the confirmation from the MCA on whether or not MCC's calculated grant accrual estimate is reasonable and to provide actual accrual estimates when they are in their final year of the compact. MCC is relying on informal desk procedures to document the process. If procedures are not clear regarding what is to be done, then there is a potential for errors to occur later on due to turnover in staff positions and the loss of internal MCC knowledge.

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

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

Recommendation 3. *We recommend that MCC enhance its Expense Accruals Financial Management Division Procedure Manual to:*

a. Define the criteria for when the assumption that MCC's maximum liability being equivalent to unused spending authority at the end of the quarter is not valid and why.

b. Fully address the MCA confirmation process and how it is carried out and documented.

c. Incorporate the desk procedures so that the procedures are formally reviewed and approved.

d. Address how a grant accrual estimate provided by an MCA should be evaluated to determine if it is reasonable.

e. Establish a procedure to ensure that MCC provides an MCA with sufficient time to address MCC's request to assess the reasonableness of the MCC calculated grant accrual for an MCA.

f. Formalize the guidance provided to an MCA on what supporting documentation should be provided to address the reasonableness of the MCC calculated grant accrual for an MCA or providing an accrual estimate for an MCA to MCC.

3. Core (General Ledger) System's Systemic Errors (Modified Repeat Finding)

MCC made substantial progress in implementing prior years' audit recommendation that management investigate and resolve legacy transactions and system open tickets and errors. Our audit identified many prior years' longstanding errors were finally corrected in the first half of FY 2015 and the number of system open tickets have substantially decreased. However, since the root causes of these errors are due to system's limitations, these systemic errors continue to exist. The system limitations include [for example: (1) Purchase Order (PO) module does not interface properly with the GL module; (2) Accounts Payable (AP) module does not properly with the GL module, (3) incorrect accounting posting model, (4) system module interface errors, and (5) obligation/funding and/or disbursement posting errors]. Accordingly, MCC continues to prepare journal entries – sometimes repeating same journal entries every reporting period – to adjust balances at the financial statements level until errors are finally researched and corrected in the system.

Certain financial activities entered at the onset of accounting events are still inherently prone to error and require intensive monitoring and further manual corrections and/or system fixes when errors are found. As a result, the accounting and financial reporting processes, as a whole, are inefficient, duplicative, and the risks are high that internal controls may not effective in order to timely prevent, or detect and correct errors, increasing the possibility of a material misstatement in the financial statements.

GAO *Standards for Internal Control in the Federal Government* states that internal control is not one event, but a series of actions and activities that occur throughout an entity's operations and on an ongoing basis. Control activities may be applied in a computerized information system environment or through manual processes. Information system control should be installed at an application's interfaces with other systems to ensure that all inputs are received and are valid and outputs are correct and properly distributed. Some examples of control activities include: proper execution of transactions and events, accurate and timely recording of transactions and events, and appropriate documentation of transactions and internal control.

> ***Recommendation 4.*** *We repeat the prior years' recommendation that MCC's Department of Administration and Finance continue to investigate and correct the root causes for the system limitations or problems that prevent or delay the recording, processing, and summarizing of accounting transactions.*

EXHIBIT 2
Management's Response to Findings

MILLENNIUM CHALLENGE CORPORATION
UNITED STATES OF AMERICA

November 13, 2015

Ms. Mia Leswing
Principal
CliftonLarsonAllen, LLP
4250 N. Fairfax Drive, Suite 1020
Arlington, VA 22203

Ms. Donell Ries
Deputy Assistant Inspector General for MCC
Office of Inspector General
U.S. Agency for International Development
1300 Pennsylvania Avenue, NW
Washington, DC 20005

Dear Ms. Leswing and Ms. Ries:

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

Significant Deficiency: Uncorrected Misstatements in FY 2015 Financial Statement Due to MCC's Failure to Account for Advances and their Liquidation in an MCA's Permitted Account (New)

Recommendation 1:

We recommend that MCC DAF perform a more comprehensive review of Advances by comparing MCA Advances reported to MCC to the source data maintained by the Fiscal Agent.

Recommendation 2:

We recommend that MCC DAF employ substantive fluctuation and trend analysis of the Advances account and promptly investigate unusual fluctuation and trends.

Response from MCC:

MCC concurs with recommendations 1 and 2. A comprehensive corrective action plan will be developed and implemented to address the deficiency noted.

Significant Deficiency: Validation Control over Grant Accrual Estimates Needs to be Strengthened (Modified Repeat Finding)
Recommendation 3

We recommend that MCC enhance its *Expense Accruals Financial Management Division Procedure Manual* to:

a. Define the criteria for when the assumption that MCC's maximum liability being equivalent to unused spending authority at the end of the quarter is not valid and why.
b. Fully address the MCA confirmation process and how it is carried out and documented.
c. Incorporate the desk procedures so that the procedures are formally reviewed and approved.
d. Address how a grant accrual estimate provided by the MCAs should be evaluated to determine if it is reasonable.
e. Establish a procedure to ensure that MCC provides the MCA with sufficient time to address MCC's request to assess the reasonableness of the MCC calculated grant accrual for the MCA.
f. Formalize the guidance provided to the MCA on what supporting documentation should be provided to address the reasonableness of the MCC calculated grant accrual for the MCA or providing an accrual estimate for the MCA to MCC.

Response from MCC:

MCC concurs with recommendation 3. A comprehensive corrective action plan will be developed and implemented to address the deficiency noted.

Significant Deficiency: Core (General Ledger) System's Systemic Errors (Modified Repeat Finding)

Recommendation 4:

We repeat the prior years' recommendation that MCC DAF continue to investigate and correct the root causes for the system limitations or problems that prevent or delay the recording, processing and summarizing of accounting transactions.

Response from MCC:

MCC concurs with recommendation 4. A comprehensive corrective action plan will be developed and implemented to address the deficiency noted.

Sincerely,

Matthew L. Bohn
Vice President and Chief Financial Officer
Department of Administration and Finance

EXHIBIT 3
Status of Prior Year Findings and Recommendations

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

FY 2014 Findings	FY 2014 Summary of Recommendations	FY 2015 Status
Material Weakness: Ineffective and Inefficient Integration of Data, Processes, and Controls within the Financial Management Systems (Modified Repeat Finding)	1. Perform a comprehensive review and determine whether the Shared Service Provider's (SSP) financial management system is meeting its financial management and reporting needs. As part of this review, management should continue to evaluate whether: a. a separate grants management system that focuses on program and financial administrations that interfaces with the core financial system is needed, or b. to establish alternatives to recording numerous data lines in the Oracle and AP and PO modules which is manual intensive and prone to errors.	Closed – MCC performed a comprehensive review in FY 2015 and concluded that the SSP's financial management system is meeting its financial management and reporting needs.
	2. Investigate and correct the underlying causes for the system errors and limitations that prevent or delay the recording, processing, and summarizing of accounting transactions. Key issues that remain unresolved should be escalated immediately rather than back-log the problem. MCC should ensure that errors and open tickets are resolved appropriately and timely by the SSP and that routine MCA accounting activities recorded in Oracle within the specified timeline. Moreover, manual adjusting journal entries should be used for limited transactions like unusual one-time entries or correcting entries.	Open – reported as SD# 3. Core System's Systemic Errors, modified repeat finding
	3. In collaboration with the SSP, formalize in writing the system's issues and standardize the resolution processes and policy/procedures.	Closed
	4. Further review SSP data entries relating to MCA payment processing and related adjustments (i.e. obligation/disbursement adjustments). Perform reconciliation of AP and PO on a monthly basis and proactively resolve all differences in a timely manner.	Closed
Significant Deficiency: Validation Control over Grant Accrual	5. Update its *Expense Accruals Financial Management Division Procedure Manual* to: a. Provide clear guidance regarding the accrual process as it relates to compacts that are in	a. Open – reported as SD#2, Validation

Estimates Needs to be Strengthened (Modified Repeat Finding)	their final year as to how the accrual will be determined; b. Address how contract retentions will be accounted for and included in the grant accrual estimate; and c. Provide a logical and supportable look-back analysis and validation process to assess the reasonableness of the grant accrual on a quarterly basis. The look-back analysis should provide MCC with sufficient and appropriate information to explain unusual variances between actual and estimates, or support updating the current grant accrual methodology. Such periodic assessment of the adequacy of the grant accrual methodology should be documented and supported by data analysis. The accrued liability amount is subject to the risks that actual subsequent disbursement amount may be significantly different from management's estimate. When this occurs, management should further analyze the drivers/factors to ensure the validity and reasonableness of the estimation methodology.	Control over Grant Accrual Estimates were weak, modified repeat finding b. Closed c. Closed
	6. Ensure that policies and procedures developed are current and are fully implemented by MCC staff during the grant accrual process to avoid potential calculation errors in the future.	Open – reported as SD SD#2, Validation Control over Grant Accrual Estimates were weak, modified repeat finding

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