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OFFICE OF INSPECTOR GENERAL
for the Millennium Challenge Corporation

**REVIEW OF THE MILLENNIUM
CHALLENGE CORPORATION'S
PROGRESS IN ACHIEVING ITS
PLANNED ORGANIZATIONAL
STRUCTURE AND BEGINNING ITS
ASSISTANCE PROGRAMS**

AUDIT REPORT NO. M-000-06-001-S
May 16, 2006

WASHINGTON, DC

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*Office of Inspector General
for the
Millennium Challenge Corporation*

May 16, 2006

MEMORANDUM

FOR: Chief Executive Officer, Millennium Challenge Corporation,
John Danilovich

FROM: Assistant Inspector General for the Millennium Challenge Corporation,
John Phee /s/

SUBJECT: Review of the Millennium Challenge Corporation's Progress in Achieving Its
Planned Organizational Structure and Beginning Its Assistance Programs
(Report No. M-000-06-001-S)

This memorandum transmits our final report on the subject review. In finalizing this report, we considered your comments on our draft report and have included those comments in their entirety as Appendix II in this report.

This report includes six procedural recommendations for corrective action. Based on your written comments to our draft report, management decisions have been reached on all six recommendations. Final action for these recommendations must be determined by MCC, and we ask that we be notified of MCC's actions.

I appreciate the cooperation and courtesy extended to my staff during the review.

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BACKGROUND

The Millennium Challenge Corporation (MCC) was established on January 23, 2004 to administer the Millennium Challenge Account (MCA). Its mission is to provide development assistance to countries that rule justly, invest in their people, and encourage economic freedom. This assistance is provided through compacts—agreements between the U.S. government and recipient countries' governments. Now in its third year of operations, MCC is steadily transforming itself from a start-up organization to a fully-fledge operating organization and structuring itself to be among the countries' largest donor.

Since its establishment, MCC has selected a total of 23 countries that are eligible to receive MCA assistance. (See Appendix III for Status of Eligible Countries by Region.). Of those 23 countries, at the time of this review, MCC had signed compacts with five: Madagascar, Honduras, Cape Verde, Nicaragua and Georgia. Additionally, MCC's Board of Directors had approved compacts—expected to be signed in the immediate future—with three additional countries: Armenia, Vanuatu and Benin.¹ MCC is actively engaging with other eligible countries to assist them in developing a successful compact.

In its commitment to work with underperforming countries, MCC also provides funding to countries that did not quite make the eligible list but are committed to implementing specific reform policies to eventually qualify for MCA assistance. At the time of our review, MCC had selected 18 countries to participate in this program, known as the threshold program. Two countries, Burkina Faso and Malawi, have threshold country plans in place and three countries—Tanzania, Albania and Paraguay—have threshold programs that have been approved by MCC. The plans for these three countries are expected to be signed in the near future.

In fiscal year 2005, MCC received an appropriation of \$1.488 billion to administer the MCA assistance and an additional \$1.75 billion for fiscal year 2006. The President is requesting an additional \$3 billion for fiscal year 2007 to administer the program. With five compacts signed and three approved, MCC has committed over \$1.5 billion for its eligible country program and nearly \$100 million for its threshold program.

REVIEW OBJECTIVES

This review was a follow up of our February 2005 review, which we reported on in Report No. M-000-05-001-S dated March 31, 2005.² As in the previous review, we directed our objectives to assess and report on the current status of the MCC in terms of achieving its planned organizational structure, developing its compact development process, and complying with the Millennium Challenge Act of 2003 and other applicable Federal laws and regulations.

Appendix I contains a discussion on the review's scope and methodology.

¹ After our fieldwork ended, MCC signed a compact agreement with these three countries.

² *Review of the Millennium Challenge Corporation's Progress in Achieving Its Planned Organizational Structure and Beginning Its Assistance Programs As of February 28, 2005*, Report No. M-000-05-001-S, dated March 31, 2005.

REVIEW FINDINGS

What progress has the Millennium Challenge Corporation made in achieving its planned organizational structure?

The Millennium Challenge Corporation (MCC) continues to make strides in achieving its planned organizational structure. Since our last review:

- A new Chief Executive Officer (CEO) was appointed to lead the organization.
- MCC restructured its departments to streamline processes and to gain better efficiency.
- MCC continued to implement internal practices by developing and revising policies and procedures that affect the organization's operations.
- MCC increased its staffing level to accommodate the anticipated increased workload of working with 23 eligible countries.

In spite of these significant changes, there are a few areas that MCC should strengthen to increase the efficiency of its operations. The recommended improvements include (a) developing an agency-specific security clearance policy to ensure that prospective employees are properly cleared for employment, (b) identifying an integrated human resource management system to maintain and track its personnel data, and (c) following internal guidelines in the procurement area. The affected areas are discussed in the Conclusions and Recommendations section on pages 13 to 20 of this report.

MCC's new CEO was confirmed by the U.S. Senate in October 2005 and assumed his duties at MCC a month later. The new CEO brings a new vision to MCC and plans to improve its services by having fewer compacts while providing greater financial assistance to the countries with which it signs a compact. Additionally, to streamline processes and gain better efficiency in the compact development process, MCC's new CEO restructured the organization by creating, dissolving, or restructuring internal departments. For example, MCC combined its former Country Programs department with particular units (such as the infrastructure, agriculture, financial and private sector units) of the Markets and Sector Assessments group and renamed it the Department of Operations. Furthermore, in anticipation of the increased workload necessary to process the additional eligible countries, MCC sought and obtained approval from the Office of Management and Budget to increase its staffing level from 200 to 300 employees. MCC's actual goal is to hire 280 employees and reserve the remaining 20 positions for future staffing needs.

As of December 2005, MCC had 160 employees, achieving 57 percent of its planned staffing level of 280 employees. In addition to MCC's 160 employees, MCC also employed 7 detailees from other federal agencies, and 24 contracted personnel. By hiring 20 employees a month, MCC plans to reach its staffing goal of 280 employees by July 2006. The table below shows MCC's staffing level by department, as of December

2005, as well as, each department's staffing target and the remaining employees it needs to recruit to reach its target.

**Table 1:
MCC's Current and Projected Staffing Levels**

MCC Departments	Staffing as of December 2005	Staffing Target by July 2006	Remaining Staff to Recruit
Accountability	27	63	36
Administration and Finance	23	41	18
Office of the CEO	5	6	1
Congressional and Public Affairs	8	12	4
General Counsel	12	17	5
Operations	76	128	52
Policy and International Relations	9	13	4
MCC's Actual Goal by July 2006	160	280	120
Reserve Positions for Future Allocation		20	
MCC's Project Full Staffing Level		300	

MCC continues to use the special hiring authority approved by the Office of Personnel Management (OPM) to reach its targeted staffing level. The hiring authority provides flexibility to MCC by granting MCC a Schedule A authority, which allows it to appoint employees to work for the agency without the competitive service requirement.³ OPM granted MCC a one-year extension to use this authority until March 2006, after which MCC is expected to develop its own competitive procedures to fill needed positions. Although MCC is in the process of developing its own competitive procedures, it still plans to request another one-year extension to facilitate meeting its staffing target of 280 by July 2006.

Additionally, MCC plans to establish an in-country presence in each compact country overseas to provide oversight, track implementation and provide guidance to the country. Each office will consist of a resident country director, a deputy resident country director and support staff. These employees will be either U.S. direct hires or local employed staff (LES).⁴ At the time of our review, MCC has hired these resident country directors for the five countries with which it has signed a compact agreement (Georgia, Cape Verde, Madagascar, Nicaragua, and Honduras) and continues to recruit for this position for the countries that are expected to sign a compact in fiscal year 2006. In addition, MCC has filled all of its overseas positions for Cape Verde and Honduras and continues to recruit for its unfilled positions in the countries of Madagascar, Georgia and Nicaragua.

³ This means that MCC has its own hiring system, which establishes the evaluation criteria it uses to fill internal vacancies. In addition, it does not require its employees to compete for the position by taking a written examination, such as the Knowledge, Skills and Ability essay.

⁴ MCC does not count LES employees in its staffing level because it does not actively recruit those employees; it contracts with the State Department to recruit local staff.

To supplement its organizational structure and assist in carrying out its mission, MCC has several formalized interagency agreements (IAAs) with other Federal government agencies. Since our last review, MCC has increased the number of federal government agencies with which it has IAAs from three to seven. For example, MCC has IAAs with the Department of Interior's National Business Center (NBC), the U.S. Department of Agriculture (USDA), and the U.S. Army Corps of Engineers to provide a variety of services to MCC. NBC currently has six IAAs with MCC and provides services such as procurement, accounting, and human resources. MCC's second largest IAA is with USDA, which provides MCC detailees with agricultural knowledge and expertise as well as other general agricultural services. In addition, MCC has three IAAs with the US Army Corps of Engineers, which provides expertise in environmental, engineering and other related services.

MCC also implemented a new employee orientation seminar, held on a monthly basis for its new employees and contractors—most of whom do not have previous Federal government experience—to introduce them to Federal government guidelines. The seminar consists of two sessions: the first session introduces employees to MCC protocols and addresses pertinent administrative issues; the second provides the employees a brief overview of the MCC policies and procedures. In addition to the course, MCC provides all new employees with a new employee handbook, which will be available online in the near future, as supplemental information.

MCC also continues to develop and update its policies and procedures for specific areas of its operations and has placed them on its intranet for easy access and distribution to its employees. At the time of our review, MCC had developed approximately 38 policies and procedures that address various issues such as administrative, contracting and compact development guidelines. Furthermore, because MCC is a government corporation, it is exempt from U.S. Code, Title 5 Chapter 43. This exemption allows MCC to develop its own performance plan without the review or approval from a performance review board or the Office of Personnel Management.⁵ In December 2005, MCC finalized and implemented its performance plan. The performance plan addresses pay and performance incentives such as the cost-of-living adjustment and performance-based salary increases, bonuses, and other incentives.

What is the status of the Millennium Challenge Corporation's compact development process?

The Millennium Challenge Corporation continues to make progress in developing compacts with its eligible countries. There are now 23 countries eligible for Millennium Challenge Account assistance and 18 countries eligible to participate in the threshold program. (See Appendix III and IV for the status of each country in the two programs.) At the time of our review, MCC had signed compact agreements with five of the eligible countries: Madagascar, Cape Verde, Honduras, Nicaragua and Georgia. In addition to these five countries, MCC's Board of Directors had approved compacts with Armenia, Vanuatu, and Benin.⁶ These compact agreements are expected to be signed in the immediate future.

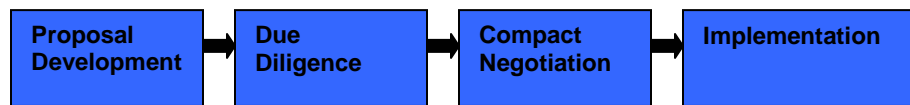
⁵ U.S.Code, Title 5-Government Organization and Employees, Chapter 43, Performance Appraisal.

⁶ After our fieldwork ended, MCC signed a compact agreement with these three countries.

In addition, MCC has approved threshold country agreements with Burkina Faso and Malawi.⁷ MCC expects to enter into more compact and threshold agreements with the remaining countries by the end of next year. At the time of our review, three of the five compact countries had received funding to begin implementing the compact's activities. However, as MCC moves forward in signing more compact agreements with eligible countries, it needs to ensure that it has developed adequate policies to cover areas such as pre-compact assistance and management of its threshold program. These areas are discussed in the Conclusions and Recommendations section on pages 13 to 20 of this report.

To ensure the successful completion of future compact agreements in a timely manner, MCC has made a number of significant changes to its compact development process. MCC's compact development process is composed of four distinct and separate phases: (1) proposal development, (2) due diligence, (3) compact negotiation and (4) implementation.

**Table 2:
Phases of MCC's Compact
Development Process**



While the phases of the compact development process have not changed, MCC has made changes, based on lessons learned, within the phases in an effort to refine the process, streamline the procedures and gain better efficiency. Those changes involve (1) providing guidelines to the eligible country during MCC's initial visit, (2) establishing target actions and dates in order to prioritize resources, (3) updating internal policies and procedures to ensure consistent application country-by-country, and (4) providing pre-compact assistance to speed up implementation.

Proposal Development

Once a country is selected as eligible for MCA assistance, MCC invites the country to submit a proposal describing the projects and activities the country wishes to implement using MCA funding. Initially, MCC posted a document to its website to assist the countries in developing proposals. However, it became apparent to MCC that the countries needed more detailed guidance than was initially provided to aid them in developing a successful proposal. Therefore, in the latter part of 2005, MCC developed a comprehensive guidebook, which includes vital information on MCC itself, the compact development process and detailed procedures for developing a proposal. The guidebook provides, among other things, information on the compact assessment and approval process, guidance on the consultative process; and describes the framework, guidelines and elements of fiscal accountability. This guidebook is provided to the country during MCC's initial visit. According to MCC officials, there are noticeable benefits from providing

⁷ After our fieldwork ended, MCC's Board of Directors had approved threshold programs for three additional countries: Tanzania, Paraguay and Albania.

countries with the guidebook and as a result expect countries to move along faster in the compact development process.

In MCC's philosophy of eliminating extreme poverty in eligible countries, country ownership is probably the most prominent principle.⁸ To ensure that the eligible country is committed to this principle and to the overall program, MCC, based on lessons learned, identified certain actions and proposed target dates that a country must achieve before MCC expends additional resources to assist the country in advancing to the next phase of the compact development process. Those actions are:

- selecting a senior point of contact to facilitate communication with MCC and to coordinate the country's overall MCC activities (*target date: 30 calendar days*),
- developing a core country team that is responsible for the development of the country proposal (*target date: 90 calendar days*), and
- submitting a proposal to MCC that meets MCC's criteria (*target date: 6 months*).⁹

Countries that meet or beat the target dates for these actions will be given higher priority by MCC as it allocates resources for items such as scheduling travel to a country for preliminary discussions and advancement to the due diligence phase of the process. For example, an eligible country that submits a sound proposal by the target date will be given first priority status and be advanced to the due diligence phase. Countries that do not meet or beat the actions and target dates will have to wait until resources are available. In other words, if a country misses the target date of 6 months for proposal submission, that country will be given a third priority status. Prior to this change, MCC had not imposed any deadlines or target dates on countries to submit proposals; as such there was no real incentive for a country to submit its proposal in a timely manner. By imposing such actions and target dates, MCC will be able to make more efficient use of its resources and identify the eligible countries that are serious about the MCC program and receiving MCA funding.¹⁰

Due Diligence

MCC has invested extensive time and resources in developing its second phase of the compact development process, due diligence—the appraisal process through which MCC determines whether the proposal meets MCC criteria for funding. The due diligence process assesses all aspects of the proposal and evaluates the country's capacity to execute the program, looking at factors such as the country's procurement systems, fiscal accountability processes, management resources, and monitoring and evaluation capacities. If the results of the due diligence process is favorable, the MCC due diligence team recommends that MCC advance to the compact negotiation phase with the country.

⁸ Country ownership refers to the country taking ownership of the entire process, from developing the proposal to implementing the compact's activities and monitoring its performance.

⁹ All target dates are from the date of MCC's initial visit to the eligible country.

¹⁰ According to MCC officials, the guidelines only apply to the countries that were selected in fiscal year 2006 and ones that will be subsequently selected. The countries selected prior to fiscal year 2006 will not be subject to these new target dates.

To ensure consistent application (although there will be slight variations), MCC revised its due diligence checklist in the latter part of 2005. The revised checklist contains standard questions that will generally apply to all proposals with respect to a given subject area. Prior to this change, each team member produced a list of questions and issues that the country needed to address depending on the team member's area of expertise as part of the due diligence process. These questions and issues were placed on a software collaboration tool and constituted the team's global "due diligence checklist." Implementing a standard checklist gives MCC some assurance that the countries' proposals and capacities will be evaluated in a consistent manner.

MCC also revised a number of other internal policies and procedures relating to its due diligence process to streamline documents and eliminate bottlenecks that have impeded the progression of the compact development process. For example, to move to the implementation phase faster, MCC revised its delegations of authority (which identifies who has authority to sign certain documents related to the compacts) and developed a policy to resolve key implementation structures and details earlier in the compact development process (prior to compact negotiations).

In addition, MCC increased its staffing level to accommodate the anticipated workload necessary for working with 23 eligible countries. It also restructured its departments directly involved in the compact development process so that significant decisions could be made in a timely manner and appropriate guidance could be provided to countries seeking assistance with the compact development process.

MCC made another significant change to its due diligence process to address its lack of available technical skills needed to effectively carry out parts of the due diligence process. Specifically, MCC increased the number of interagency agreements with other Federal agencies and is looking to establish more contracts with outside firms in an effort to build an adequate pool of resources for the critical technical skills needed in assess certain aspects of proposed projects in the eligible countries.

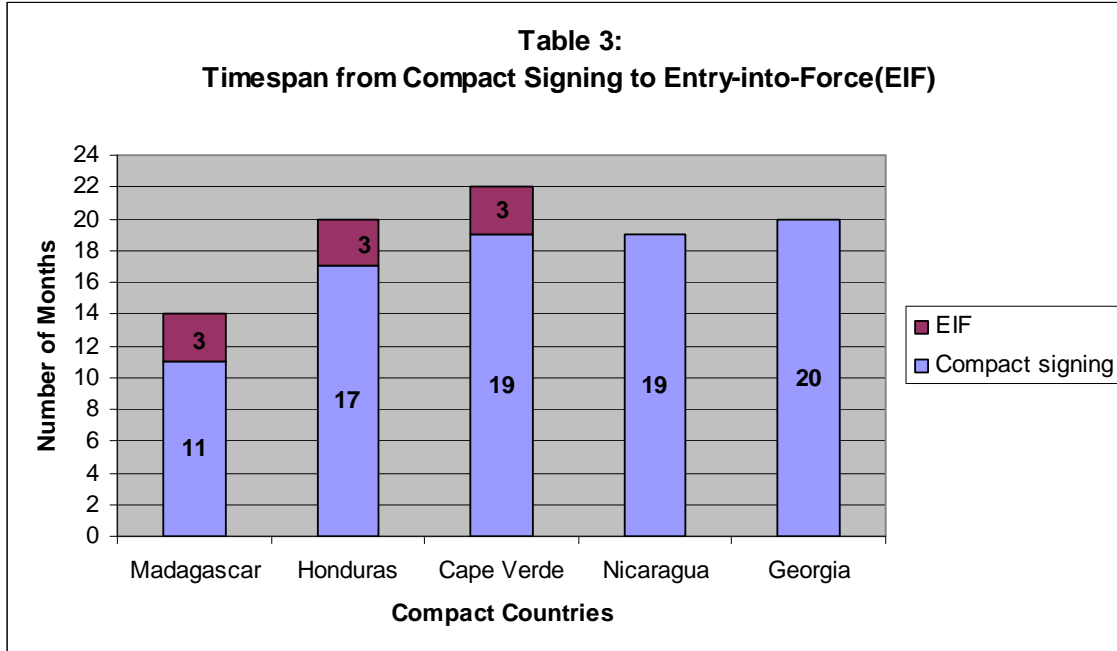
Compact Negotiation and Implementation

MCC believes that the changes it has made on the front-end of the compact development process will assist eligible countries in advancing to the compact negotiation phase faster. After the terms of the compact are negotiated and agreed to, the compact agreement is signed by MCC and the eligible country. Next comes the implementation phase, the phase in which countries receive the first disbursement of the compact award funding to begin implementing the compact's activities. At the time of our review, three countries had reached the implementation phase. Before a country can advance to this phase, there are conditions known as "conditions precedent" that must be met by MCC and the eligible country before a compact agreement goes into effect (referred to as "entry-into-force",¹¹) and before the country receives its first and subsequent disbursements. For example, before a compact reaches entry-into-force, MCC and the eligible country must first execute a disbursement agreement and a procurement agreement and certify that all domestic requirements for the compact to be fully enforceable have been met. In order for a country to receive its first disbursement, conditions precedent—such as establishing a bank agreement, entering into a fiscal

¹¹ According to MCC officials, entry-into-force is the point when a binding commitment is recognized and the compact funds are obligated.

agent agreement and developing a financial plan—must be met prior to disbursement of initial funds.

In working with the five compact countries, MCC learned that the time between compact signing and entry-into-force took much longer than anticipated due to various reasons, such as the lack of expertise and resources needed to develop such agreements and the country’s ability to pay such services. The chart below illustrates the time span between compact signing, entry-into-force, and first disbursement for the five current compact countries.



The number of months depicted in the chart begins from the date of eligibility to illustrate the number of months it took a country to sign the compact and reach entry-into-force.

As shown in the chart above, Madagascar signed a compact with MCC 11 months after being selected as an eligible country. Three months after that, the compact reached entry-into-force. Similarly, Cape Verde’s compact was signed 17 months after selection and reached entry-into-force 3 months later. These countries, along with Honduras, averaged about 3 months to advance from compact signing to entry-into-force and first disbursement. The other two countries have not reached entry-into-force or received their first disbursement for the following reasons: a ratification issue in Nicaragua and a lack of available funding to pay its core technical team in Georgia.

MCC wants to shorten the time span between compact signing, entry-into-force and first disbursement to enable the countries to start implementing the compact activities and become operational faster. One way MCC believes that this can be accomplished is by providing funding to the eligible country at compact signing. These funds will be distributed using the Section 609(g) mechanism¹² and will reduce the amount of the

¹² Section 609(g) of the MCA Act of 2003 gives the Chief Executive Officer the authority to enter into contracts or make grants for any eligible country for the purpose of facilitating the development and implementation of the Compact between the U.S. and the country.

compact awarded to the eligible country. For instance, at compact signing a percentage of funds will be provided to the eligible country to assist the country in developing supplemental agreements required for entry-into-force and first disbursement and to cover administrative expenses such as salaries, rent, and legal support payments. MCC believes that providing such funding will accelerate the time between compact signing and entry-into-force so that the compact funds could be made available to the country sooner. However, MCC needs to develop a guidance policy before it moves into full implementation of this concept. This is discussed in the Conclusions and Recommendations section on page 15 of this report.

Threshold Program

In addition to the progress MCC is making in developing and negotiating compacts with eligible countries, MCC has moved forward in establishing its threshold program. The threshold program assists selected countries that are committed to undertaking necessary reforms to improve their performance on the eligibility criteria so that they might eventually qualify for assistance as an eligible country. The U.S. Agency for International Development (USAID) manages the threshold country program with MCC's oversight. Currently, there are 18 countries eligible to participate in this program. At the time of our review, MCC has signed threshold country plans¹³ with Burkina Faso and Malawi and has approved threshold programs for three additional countries. To date, under its threshold program, MCC has committed nearly \$100 million to help countries improve their policy environment, fight corruption, improve girls' primary education and strengthen the country's rule of law. The Millennium Challenge Act provides that up to 10 percent of available funding can be used for this program.

The process that MCC and the threshold countries follow to develop a threshold plan is similar to the compact development process. First, the country has to express interest by submitting a concept paper. The concept paper can focus on any of the 16 MCA indicators.¹⁴ According to MCC officials, MCC has not restricted the concept paper to focusing only on the indicators that the country did not pass, but has left it open so that countries may focus on any of the 16 indicators to improve their overall performance. Most of the threshold countries fail on the corruption indicator and it is also the one indicator focused on by most countries. The concept paper undergoes a number of reviews by the USAID/Mission in country, USAID/Washington and MCC. USAID consolidates the comments from all parties and sends the comments and concept paper to MCC, which then holds an investment committee meeting to determine whether the concept paper has sufficient merit to justify MCC's support. If approved, MCC sends a congressional notification to the U.S. Congress, and the threshold plan is sent to MCC's board for approval. Once the board approves the plan, a grant agreement is signed with the country in order to start implementing the threshold program's activities.

¹³ A threshold plan includes a performance schedule, benchmarks to measure progress, a financial management mechanism, and a budget. The duration of a threshold plan is usually up to 2 years.

¹⁴ To determine a country's eligibility for MCA funding, MCC developed sixteen objective and quantifiable indicators to evaluate a country's demonstrated commitment to ruling justly, promoting economic freedom and investing in its people.

MCC is also working to streamline the threshold program process. First, MCC plans to provide all countries with diagnostic data for informational purposes, so that the country knows exactly where each indicator failed in meeting eligibility requirements in order to more accurately focus on needed policy reforms. In addition, as in the compact development process, MCC is imposing deadlines for the submission of the country's concept paper. For 2004 and 2005, the due date for the country's concept paper was 4 months from selection. For 2006, MCC reduced the timeframe to 3 months from selection to try to move the process along faster. However, there are some additional improvements that MCC should make to increase the efficiency of this program. These improvements are discussed in the Conclusions and Recommendations section on pages 16 and 20 of this report.

What progress has the Millennium Challenge Corporation made in complying with the Millennium Challenge Act of 2003 and other applicable Federal laws and regulations?

Since OIG's last review, MCC has continued to make progress in complying with the Millennium Challenge Act of 2003 (Act) and continues to assess the applicability of other Federal laws and regulations to its operations.

Act Authorities and Requirements

The MCA Act of 2003 has a number of authorities and requirements, as well as other provisions and requirements on reporting and coordinating with government entities, that guide the MCC on how to organize itself, identify countries that are candidates for assistance, select countries eligible to submit assistance proposals, administer assistance to the countries, and enter into agreements with the countries.

MCC has continued to comply with the several provisions of the Act. For example, pursuant to the Act, MCC has:

- Provided guidance for developing solicited proposals on the MCC website for countries to guide them in developing a proposal. However, MCC has not provided guidance for unsolicited proposals because it has not, and does not expect to receive such requests.
- Notified Congress and the public, according to the required time limits, regarding the MCC's Board's selection of eligible and candidate countries, the criteria and methodology used to select eligible countries, and the date on which MCC enters into compact negotiations with an eligible country.
- Consulted with USAID officials, especially those who are responsible for a region or country where the MCC eligible country is located.
- Notified Congress when Yemen was suspended from the threshold country program, even though this was not required by the Act. According to the Act, MCC is required to inform Congress when it suspends or terminates an eligible

country; however, MCC has made it a policy to notify Congress when a country is terminated or suspended from receiving any type of assistance—compact development and implementation or threshold program—under the MCC development funding umbrella.

The Act also requires that the MCC Board of Directors' membership include four individuals with relevant international experience. At the present time, the Board lacks two such members. According to MCC officials, the Hill has forwarded names of proposed candidates for the two open seats on the Board to the White House, which approves and appoints the board members. In MCC's opinion, the two open seats on the Board have not impeded the work of MCC. However, in order to maintain the continuity and stability of the board, it would benefit the Board as well as MCC if the two remaining seats were filled as soon as practicable. The four individuals are appointed for a term of 3 years and can be reappointed for an additional 2 years.

Other Federal Laws and Regulations

MCC continues to assess the applicability of other federal laws and regulations to its operations. Because MCC was established as a government corporation¹⁵, it is subject to any Federal statute that covers government corporations, as well, as any act that defines government corporations in its definition of agency, government instrumentality or government entity. MCC officials maintain, as a general matter, that MCC is subject to any Federal statute that covers government corporations and acts that include government corporations in its definition. However, according to MCC officials, when an act generally covers a government corporation, some provisions may not apply to MCC by virtue of overriding provisions of the Millennium Challenge Act, e.g., Section 605(a) on "notwithstanding" authority, Section 617(c) on hiring and compensation authority.

MCC identified selected Federal Laws and Regulations that it determined cover, partially cover, or do not cover MCC. For example, MCC identified the Anti-Deficiency Act, Prompt Payment Act, Federal Travel Regulations and Federal Acquisition Regulation as laws and regulations that cover MCC's operations. Conversely, MCC identified the Chief Financial Officer's Act (CFO) of 1990, the Federal Financial Management Improvement Act (FFMIA) of 1996 and the Office of Management and Budget's Form and Content of Agency Financial Statements as laws and regulations that do not cover its operations. MCC officials believe that these statutes do not apply to MCC because MCC is not a CFO Agency. Nevertheless, MCC plans to implement policies and procedures to follow certain laws and regulations, such as the CFO Act and FFMIA because it makes good business sense. Additionally, MCC identified a few laws and regulations such as the Government Management Reform Act of 1994 and the Civil Service Reform Act of 1978, that it believes partially cover MCC's operations.

In accordance with the Equal Employment Opportunity Commission's regulations, MCC is also implementing an Equal Employment Office (EEO) program. This program is intended to provide equal employment opportunities to all MCC employees and applicants. MCC plans to enter into a Memorandum of Understanding with the

¹⁵ Section 105, Title 5 of the United States Code includes government corporations in its definition of an executive agency.

Executive Office of the President to administer this program. According to MCC officials, the Executive Office will be responsible for training MCC's supervisors and staff and managing the EEO compliant system.

Since the OIG's last review, MCC has developed, in accordance with the Government Performance and Results Act, its first 5-year strategic plan, which describes its mission, strategic goals and principles. The strategic plan is intended to give MCC staff a consistent guide for its operations and establish accountability for MCC as an organization.

Conclusions and Recommendations

While MCC has advanced in its second year of operations in establishing its planned organizational structure, improving its compact development process, and complying with its authorizing legislation, there are some areas that MCC should improve upon as it continues to implement its development assistance program. Those areas are:

- implementing policies to effectively carry out its operations in the areas of security clearances, Section 609(g) bridge funding, and country selection for MCC programs,
- developing an integrated human resource system,
- disseminating contracting officer's technical representative designation letters, and
- defining the reporting requirements for proper oversight of the threshold program.

MCC Needs to Develop a Security Clearance Policy

MCC has not developed an agency-specific security clearance policy that clearly delineates and identifies the type of security clearance each MCC employee must receive to work with the organization. According to MCC officials, MCC did not have adequate resources to develop its own security-related policy due to the limited number of staff at the start of its operations. In place of its own security policy, MCC followed U.S. Department of State's Foreign Affairs Manual, Volume 12, Personnel Security (12 FAM 230) as an interim reference guide and several other Federal guidelines to make security related determinations. However, without a clearly defined written, agency-specific policy regarding security clearances, the security risks posed to the organization and the Federal Government by an employee hired by MCC will not be adequately and consistently addressed and mitigated.

According to MCC officials, MCC was established with a foreign policy/national interest mandate to quickly begin providing development assistance to foreign countries. To achieve this mandate, MCC found it necessary to promptly increase its staffing level before it developed internal security policies and to hire staff without the lengthy process of a security clearance, which would delay the start date of its employees. Additionally, the MCC included in its employment processing a waiver that allowed it to hire without a pre-employment background investigation. As a result, MCC employees can start work on a condition that clearance will be granted once the investigation is complete. However, if an employee is denied clearance, MCC will have to terminate his or her employment. MCC reported one occurrence where a decision was made that the employee would unlikely be granted a clearance. According to an MCC official, the employee was informed—after the employee began work at MCC—that based on the information provided on the security forms, it was unlikely that a security clearance would be granted. As a result, the employee then decided to resign from the corporation. Long-standing foreign affairs agencies such as the U.S. State Department

and USAID have established a security policy where they do not allow employees to start work until the agency has completed a background investigation and provided a provisional clearance for the employee.

Although MCC has not developed its own written security policy to determine the type of clearance employees should have in various positions, according to MCC officials, most of the employees who are directors, managers, and other professional staff who travel frequently receive a top secret clearance, while the administrative staff—professional, technical, and clerical—receive a secret security clearance. To make security related determinations, MCC used (1) the *Adjudicative Guidelines*, which permits the agency to determine reasons an employee should not have access to classified information, and (2) *Suitability Factors* of 5 Code of Federal Regulations 731.202, which determine if the employee's actions, such as providing false statements or criminal conduct, prevents the employee from having access to classified information.

The *Suitability Factors* also grants an agency a waiver to hire an employee for a specific timeframe, if necessary for the national interest. In addition, to determine if a specific employee should receive clearance based on the type of classified information needed, MCC uses *Executive Order 12968, Access to Classified Information*. This order also explains that the agency could grant temporary clearance to employees contingent on the completion of a full clearance. Furthermore, Executive Order 10450, also used by MCC, permits agencies to hire staff to fill sensitive positions when deemed necessary for national interest.

According to MCC officials, they are working on developing agency-specific security policies but maintain that they need to continue to postpone performing full employment investigations in order to meet MCC's staffing goals and ensure that the foreign policy/national interest directive promoted by the President is a success. However, without a documented agency-security clearance policy, MCC may grant clearance to an individual that is not deemed trustworthy for employment in a national security position. In addition, an employee working without a security clearance could be a potential threat to the organization by having access to the organization's systems and could acquire confidential information that may impede or assist a country receiving assistance from MCC. Moreover, an MCC policy on this issue would ensure that consistent application is being applied in granting clearances. As MCC continues to move forward, it needs to ensure that the appropriate clearance is given to its employees.

Recommendation 1: We recommend that the Millennium Challenge Corporation develop and implement security-related policies and procedures that (1) specifically identify the level of clearance that each job position requires and (2) require, at a minimum, a preliminary background investigation be conducted prior to any Millennium Challenge Corporation employee starting work.

MCC Needs to Modify Its Section 609(g) Policy

MCC had not modified its Section 609(g) policy to address compact support funding referred to as Section 609(g) bridge-funding. Bridge-funding, a concept developed by MCC, is intended to decrease the time between compact signing and entry-into-force in an effort to implement the compact's activities faster. MCC did not address this concept in its current 609(g) policy because the need for such funding was not previously anticipated. Although providing such funding is not prohibited by MCC's authorizing legislation (the MCA Act), MCC needs to ensure that the concept, methodology and application is fully outlined, documented and shared with eligible countries to ensure full understanding and consistent application. Without a clearly defined policy to address this concept, there is a possibility that MCC's staff may not fully understand MCC's position regarding the acceptable use of 609(g) funds which may adversely impact the implementation of the compact's program.

Section 609(g) of the Millennium Challenge Act of 2003 gives MCC the authority to provide assistance to countries to develop and implement its compact. Specifically, according to the Act, the Chief Executive Officer may enter into contracts or make grants for any eligible country to facilitate the development and implementation of the compact.

In developing the 609(g) bridge-funding concept, MCC was attempting to address a critical issue of accelerating the country's ability to move to the implementation phase more quickly once a compact is signed. The compact stipulates that certain conditions must be met before a compact is entered-into-force and the country receives its first disbursement of compact program funds.¹⁶ Based on the performance of previous countries, it became apparent to MCC that, in part, due to limited financial resources many countries were very slow in meeting those conditions. For instance, it took Madagascar approximately 3 months after its compact was signed until the compact was entered-into-force and could move to actual implementation. Similarly, Georgia, which signed its compact on September 12, 2005, had yet to reach entry-into-force 4 months later (as the end of our fieldwork). As a result, Georgia has not received its first disbursement of the \$295.3 million compact funding it was awarded. According to MCC officials, Georgia's compact has not entered-into-force because of the country's limited financial resources available to pay certain administrative expenses, such as the salaries of Georgia's technical team working on the MCC program and other operational expenses. Without such funding, Georgia is unable to meet the conditions stipulated in the compact for entry-into-force and first disbursement in a timely manner. This situation was not limited to Georgia as other countries that signed a compact with MCC faced a similar dilemma. The countries could not pay administrative and other start-up expenses due to the lack of available funding. As a result, the countries' core-teams would sometimes work months without compensation. Furthermore, at the time of this review, the first disbursement given in most countries has primarily been for administrative expenses and very little has been expended for program-related expenses. Bridge-funding is intended to assist countries in meeting disbursement conditions more quickly and to pay for certain administrative and start-up expenses prior to the flow of compact program assistance.

¹⁶ These conditions are met by implementing supplemental agreements covering disbursements, procurements, banking, governance and fiscal agent and provide assurance that the country has developed proper structures to protect and maintain the integrity of MCC funds and programs.

Because MCC did not anticipate a country would need assistance for program administrative and miscellaneous start-up expenses, this concept was not addressed in its current 609(g) policy, dated October 2005. Unlike previous 609(g) funds awarded by MCC¹⁷, bridge-funding 609(g) would be made available at compact signing and reduce the amount of the compact awarded to the eligible country. While MCC is working on updating its current policy to address this issue, it has already provided (with the CEO and Investment Committee's approval) such funding to eligible countries and is planning to continue to provide such funding in the immediate future.

While MCC has a policy on Section 609(g) funding, it needs to be modified and updated to include the bridge-funding concept. Updating the current policy will ensure that the concept, methodology and application of this type of funding is fully defined in a written policy. The policy should also be widely disseminated to eligible countries to ensure that the countries have allocated the necessary funding in their compact requests to cover such expenses. An updated policy will also ensure that the MCC staff is fully aware of MCC's management policy on the use of bridge-funding as they are negotiating future compacts.

Recommendation 2: We recommend that the Millennium Challenge Corporation update its Section 609(g) policy to include provisions to address the concept, requirements, limitations, methodology and application of Section 609(g) bridge-funding assistance to a country.

MCC Needs to Develop a Policy Addressing Selection of Countries for Participation in Both The Threshold and Eligible Programs

MCC had not developed a documented policy to address countries' participation in both the threshold and eligible country programs. This occurred because conditions did not previously exist that would have required such a policy i.e. where the same countries were participating in both programs (Threshold and Eligible country programs). However, during the last round of country selections in November of 2005, MCC's Board of Directors selected three countries currently participating in the threshold country program as being eligible to receive compact funding. Those countries had not completed their threshold programs and, for the most part, did not have an approved threshold plan in place. Although participation in the two programs is not prohibited by MCC's authorizing legislation, MCC needs to implement controls to mitigate the risk of loss or misuse of MCC provided funds by defining exactly how the two programs will be managed by the country, any perceived risks, and actions that will be taken to mitigate those risks.

MCC's Board of Directors determines if a candidate country is an eligible country based on the country's demonstrated commitment to meet 16 policy indicators in three broad categories: ruling justly, promoting economic freedom and investing in its people. Once selected, the eligible countries are invited to submit a proposal for Millennium Challenge Assistance (MCA). The threshold program is designed to assist countries that are on the "threshold," meaning they did not pass all 16 indicators, but have demonstrated a

¹⁷ Previous 609(g) funds have been given to assist the country in conducting feasibility studies, obtaining baseline data and acquiring technical assistance.

significant commitment to improve their performance as measured by these indicators. MCC's Board of Directors also selects these threshold countries to participate in this program. These countries are invited to submit a threshold country plan.

In November 2005, MCC's Board of Directors named three threshold countries as eligible countries (i.e., eligible for fiscal year 2006 MCA assistance). If successful in completing the requirements for each program, these countries will be able to participate in both the threshold and eligible countries programs. For example, Burkina Faso was selected to participate in the threshold program in fiscal year 2005. Then, the country was also selected as eligible for fiscal year 2006 MCA assistance. If Burkina Faso is successful in completing a threshold plan¹⁸ and entering into a compact agreement with MCC, it can benefit from receiving two sources of MCC's funds. According to MCC officials, both programs (threshold and eligible) will run concurrently in a country if the country is successful in completing the requirements for both programs. MCC will manage the country's eligible country program and USAID will manage the country threshold program.

Further, there is no stipulation or requirement that a threshold country must complete or graduate from its threshold program before being selected as an eligible country or receiving compact funds. However, MCC is considering taking a different approach and implementing some targets that must be achieved before a threshold country can be selected as an eligible country. One such approach is that if a threshold country is selected as an eligible country, MCC may reconsider expending resources in developing the threshold plan if the country is not far in developing the plan. At the same time, if a country's threshold plan is substantially complete, it may allow the country to continue developing the threshold plan.

MCC should also consider the difficulties that a country may encounter in meeting the requirements to participate in both programs. Although USAID is responsible for managing the threshold plan, the country is responsible for developing the threshold plan. Some countries may lack the necessary resources or capacity to manage and implement both programs. As it stands now, MCC's eligible countries are experiencing difficulty with compact development and implementation.

MCC officials stated that they are trying to ensure that there are training and capacity-building components in the threshold plan to provide a training ground for developing and implementing a compact. MCC recognizes that if a country does poorly with developing and implementing the threshold plan, the same performance is likely with the compact development and implementation. Equally, if a country performs well, its overall performance of its indicators would likely improve, and the successful implementation of a compact agreement may be more likely.

However, there is a risk that MCC may expend funds in a country to develop a threshold plan that performs poorly or does not achieve the intended results of the program. MCC would have to consider if it is reasonable to expend additional resources for that country to develop a compact. To ensure consistent application in making such determinations, MCC should develop a policy to guide itself when a threshold country has been selected as an eligible country.

¹⁸ Burkina Faso's threshold plan was signed on July 22, 2005 for \$12.9 million.

Recommendation 3: We recommend that the Millennium Challenge Corporation develop and implement a policy for making specific determinations concerning countries' participation in both the eligible and threshold country programs.

MCC Needs to Develop an Integrated Human Resource System

MCC does not have an integrated human resource management system to maintain and track its personnel data. Instead, MCC uses several different tools or applications to manage its personnel and recruitment data. The U.S. Department of Interior's National Business Center (NBC) provides human resource services to MCC. Therefore, MCC must implement a system that communicates with the system that NBC uses. Implementing an integrated system that interfaces with NBC's system would ensure the integrity of data and decrease the potential of losing data that may occur when using hard copies or different software applications that do not communicate with each other.

Currently, the Human Resources (HR) office (an office within MCC's Department of Administration and Finance) uses hard copies, internal software packages, and its contractors' software to compile and track its data, which each HR unit maintains differently. For example, the recruitment unit in HR relies on its contractor's system to track information on MCC's recruited employees, whereas HR's benefits unit relies on hard copy documents and systems used by NBC to maintain employee records. Moreover, other units of the HR office use internal software packages to track employee profiles, such as pay bands and salaries. MCC would like to implement the Oracle HR Suite to manage its personnel data internally. This suite could manage recruitment, personnel files, payroll, and procurement, but it may be difficult to implement because the system cannot interface with NBC's system. According to the HR unit, NBC officials explained that the Office of Management and Budget approves certain software that Center of Excellence agencies, such as NBC, could use, but it did not permit the use of the Oracle HR system. If MCC implements the Oracle HR system, it would prevent the transmission of certain files to NBC and cause MCC to rely on the current method of sending documents to NBC—via email or hard copy—which MCC wants to avoid.

Using an integrated system that could communicate with NBC would decrease the amount of work or the potential loss of data that may occur when using hard copies or different software applications and prove to be a more efficient use of resources.

Recommendation 4: We recommend that the Millennium Challenge Corporation document its assessment of the automated options that could integrate all units of its human resources services plus interface with the U.S. Department of Interior's National Business Center systems and develop short-range and long-range plans for implementation.

MCC Needs to Provide COTR Designation Letters

MCC's contracting officer did not adequately designate staff to manage contracts. Specifically, MCC's contracting officer did not provide Contracting Officer's Technical Representative (COTR) designation letters to staff responsible for managing contracts. This occurred because MCC did not adhere to its contracting policy that addresses the responsibilities of contracting officers. According to MCC's Contracting Procedures, MCC's contracting officer should provide each COTR with a designation letter that explains his responsibilities as they relate to the contract. Without a COTR designation letter, COTRs may not be fully aware of their responsibilities in managing the contracts and, as a result, may act outside of their authority (e.g., changing contract terms and conditions), thereby creating a financial commitment on behalf of either themselves or the U.S. Government.

MCC's contracting procedures state that the contracting officer should provide each COTR with a designation letter that explains his or her responsibilities as they relate to the contract. Similarly, a copy of the letter should be maintained in the contract file and given to the contractor. The COTR designation letter identifies the person responsible for managing the contract and outlines the COTR's responsibilities, such as maintaining reports that document the contractor's work, approving invoices, and completing contractor performance evaluation. Although copies of the COTR letters were maintained in MCC's contract files, most COTRs did not receive a copy. We surveyed approximately 10 percent of MCC's trained COTRs to determine if MCC had followed its contracting guidelines. Of the ten COTRs surveyed, only three had knowledge of the COTR letter and were in possession of it. The remaining seven COTRs—each responsible for managing between 2 to 15 contracts—had no knowledge of a COTR letter and had not received it from the contracting officer. According to the acquisition director, COTRs should receive a designation letter for each contract that they manage.

According to an MCC official, because MCC was a new agency, it needed people to manage contracts in order for it to begin operating. At that time, most of the employees were not trained as COTRs and were therefore titled as project monitors, with responsibilities similar to a COTR's, such as approving invoices. As a result, they did not receive a COTR designation letter. However, after MCC began providing COTR training in March 2005, the employees who attended and continued to manage contracts should have received COTR designation letters for their current and future contracts. Contrary to the MCC's official's comments, employees included in our survey who attended and managed contracts did not receive a COTR designation letter. For example, three of the ten COTRs surveyed who attended training in March 2005 and were designated to manage contracts after completing the training did not have a COTR letter. Furthermore, as stated above, seven of the ten COTRs that we surveyed and who managed a number of contracts had never seen a COTR designation letter.

It is important that the roles and responsibilities of the contracting officer and the COTR be clearly defined and understood by both parties. COTRs must be aware of the scope and limitations of their authority. If COTRs continue to perform their duties without being aware of their limitations, there is a greater possibility that they could act outside of their scope and legally bind either themselves or the U.S. Government to an unfavorable contract obligation.

Recommendation 5: We recommend that the Millennium Challenge Corporation provide each contracting officer's technical representative a designation letter for each contract that he or she manages.

MCC Needs to Develop A Reporting Format for USAID

MCC had not defined the type of information that the U.S. Agency for International Development should include in its progress reports on the threshold program nor the frequency of the reports. The Memorandum of Agreement between USAID and MCC requires USAID to submit quarterly reports on the financial expenditures but is silent on periodic reporting of the performance or progress of the program. According to MCC officials, quarterly reports are required from USAID, but the type of information that each report should contain has not been clearly defined because they are not at the point where the reports are due and, thus, have not worked out the details of the report. It is important that MCC be periodically informed of the progress of the threshold program in each country to maintain proper oversight. Without clearly defining the frequency and contents of progress reports, information reported to MCC may not be useful, relevant or timely.

In accordance with the Millennium Challenge Act of 2003, USAID manages the implementation of MCC's threshold country program. In October 2004, MCC and USAID formalized their understanding of managing the threshold program in a Memorandum of Agreement (MOA). The MOA outlines the terms and conditions, principles and financial reporting requirements. However, it does not specify the frequency of reporting of the program's progress that is required. MCC officials stated that quarterly reports are required, but the type of information that the report must contain has not been defined because they are not at a point where the reports are due.

Currently, there are 18 countries eligible to participate in the threshold program. Two of those countries have completed successful threshold plans, and three are expected to have threshold plans in place soon. With these two countries starting to implement the program and three other countries set to implement programs in the immediate future, it is essential that MCC define the type of information that USAID will be required to report concerning the programs' progress.

Recommendation 6: We recommend that the Millennium Challenge Corporation formally define the frequency and contents of the progress reports for the threshold program required from the U.S. Agency for International Development and communicate these requirements to that Agency.

EVALUATION OF MANAGEMENT COMMENTS

MCC provided written comments to our draft report that are included in their entirety as Appendix II. Overall, MCC management concurred with all six recommendations included in the report and is taking or planning to take actions to implement the corrective action to address them.

In response to Recommendation No. 1, MCC stated that it had developed and implemented a policy and procedures that identify the level of clearance and background investigation required for each position within MCC. The memorandum was approved on March 23, 2006. MCC also stated that it is in the process of writing a policy and procedures for conducting preliminary background investigations and will complete implementation of the policy by the end of calendar year 2006.

In response to Recommendation No. 2, MCC agreed that it should periodically update its 609(g) policy as the use of the funding evolves and stated that it has already been in the process of reviewing and revising the policy to address bridge-funding concept and other evolutions for the use of the 609(g) authority. MCC also stated while they could not commit that a revised section 609(g) policy will fully address the “concept, requirements, limitations, methodology and application” of the funding the revised policy will contain an appropriate level of detail on the use of the funding and other purposes and will continue to contain appropriate “catch all” language to provide MCC with the needed flexibility to effectively carry out its mission. MCC expects to complete the revision of this policy by May 31, 2006.

In response to Recommendation No. 3, MCC plans to review its policy on allowing countries to participate in both the eligible and threshold country programs. Once the review is completed, MCC plans to present options to the MCC Board for consideration during the next selection cycle, which is usually held in the month of November.

In response to Recommendation No. 4, MCC plans to conduct a thorough needs assessment, identify and conduct thorough evaluations of the viable options and select a system for integrating its human resource services. MCC plans to develop a timetable and project plan for completion of the tasks by June 30, 2006

In response to Recommendation No. 5, MCC plans to provide each existing contracting officer’s technical representative a copy of their designation letter by May 31, 2006.

In response to Recommendation No. 6, MCC stated that they met with USAID on March 15, 2006 and agreed on a format for reporting on the threshold program that will be used as a basis for future reporting.

Based on MCC's comments and the correction actions planned, a management decision has been reached on all six recommendations.

SCOPE AND METHODOLOGY

Scope

The Millennium Challenge Corporation's Office of Inspector General conducted this review to gain an understanding of the progress that MCC has made in establishing its organizational structure, beginning its assistance program and assessing MCC's compliance with applicable laws and regulations. Our review was not an audit and therefore was not designed to fully comply with generally accepted government auditing standards. The review was conducted at MCC headquarters located in Washington, D.C. from August 4 through September 16, 2005 and resumed again from December 2005 to January 20, 2006.

Methodology

In planning and performing this review, we interviewed MCC management officials and examined documentation relating to MCC's organization, staffing, policies and procedures, compact development process and relevant laws and regulations.

To determine the progress MCC has made in achieving its planned organizational structure, we interviewed MCC officials to determine the current status of its organizational structure in terms of where MCC is now where they expect to be when fully staffed and operational, the anticipated staffing needs of each MCC department, and its hiring plans. We also reviewed documentation such as organizational charts, staffing plans, and policies and procedures. In addition, we judgmentally selected and surveyed approximately 10 percent of its contracting officer's technical representatives to assess MCC's internal controls surrounding its procurement practices.

To determine the status of MCC's compact development process, we interviewed key MCC personnel involved with the compact development process and reviewed applicable documentation related to the process. We also interviewed key MCC and USAID personnel managing the threshold program. Furthermore, we reviewed:

- policies and procedures governing MCC's compact development process,
- guidance given to the countries to assist in the compact development process,
- compact development documents prepared by the five compact countries,
- reports indicating the status of the compact development process, and
- other file documentation pertaining to the compact development process.

To determine whether the MCC complied with the Millennium Challenge Act of 2003 (Act) and other applicable Federal laws and regulations, we met with and obtained documentation from MCC staff as well as retrieved documents from MCC's external website. We discussed with the MCC staff their interpretation of parts of the Act and whether the MCC complied with its terms. In reviewing compliance issues, we determined the minimum level of action necessary to meet the requirements of selected provisions of the Act and other Federal laws and regulations' requirements but did not attempt to fully evaluate the thoroughness, effectiveness or impact of the actions MCC has taken.

MANAGEMENT COMMENTS



Millennium Challenge Corporation

Reducing Poverty Through Growth

April 28, 2006

MEMORANDUM TO: John Phee
Assistant Inspector General for the Millennium
Challenge Corporation

FROM: Mike Casella /s/
Deputy Vice President for Administration and Finance

SUBJECT: MCC comments on the Review of the Millennium
Challenge Corporation's Progress in Achieving its
Planned Organizational Structure and Beginning its
Assistance Programs

The Millennium Challenge Corporation appreciates the opportunity to comment on this report. Attached please find our response to the six recommendations made in the report, as well as clarifying comments on the body of the report.

Clarifying comments

- Page 3 of the report refers to the MCC's request for a one-year extension of its Schedule A excepted service appointing authority. On March 29, 2006, the Office of Personnel Management (OPM) granted this request and extended the MCC's Schedule A excepted service appointing authority until March 31, 2007, to assist the MCC in reaching its approved staffing level. The MCC continues to develop and refine its own competitive hiring procedures that will be in place to fill positions after the Schedule A authority expires in March 2007.
- Page 4 correctly describes the MCC new employee orientation process as having two phases. However, phase one of the process is provided weekly for new employees and contractors on their first day of employment. During this phase, initial employee in-processing occurs and administrative policies and procedures and related Federal government guidelines are reviewed. New employees and contractors also receive hard copies of key policies and procedures and are directed to the Intranet for the full repository of MCC policies and procedures. The second phase of orientation is held monthly, as stated in the report. During this phase, the MCC mission, strategic objectives, organizational structure, departmental roles, and processes pertinent to carrying out the MCC mission, such as the selection process

for eligible and threshold countries and the compact development process, are reviewed.

- Page 4 of the report discusses the development of the MCC performance management program. It is correct that as a government corporation MCC can develop its own performance plan without the review or approval of the Office of Personnel Management. However, MCC did involve third parties in the development, review and endorsement of its performance management program. MCC consulted with a working group of the MCC Board of Directors, who provided considerable feedback throughout the entire development process. The MCC also engaged the Hay Group, an international consulting firm specializing in human resource management, for their expertise regarding best practices in performance management in both the public and private sectors. Finally, the MCC performance management program that was implemented for FY 2006 was endorsed by the MCC examiner at the Office of Management and Budget (OMB).
- Page 11 of the report discusses MCC implementation of an Equal Employment Opportunity (EEO) program. While the discussion of MCC's efforts in this area is generally correct, MCC has not made a decision to enter into a memorandum of understanding with the Executive Office of the President to administer its EEO program. An initial agreement was executed with the Equal Employment Opportunity Commission on April 27, 2006, to provide on-site training regarding the federal sector EEO process and prevention of harassment (including sexual harassment). MCC is exploring a number of options for implementing its EEO program.

Recommendation 1: We recommend that the Millennium Challenge Corporation develop and implement security-related policies and procedures that specifically identify the level of clearance that each job position requires and that it require, at a minimum, a preliminary background investigation be conducted prior to any Millennium Challenge Corporation employee starting work.

MCC concurs with the recommendation. MCC has developed and implemented a policy and procedures that identifies the level of clearance and background investigation required for each position within MCC. The memorandum, National Security Positions within MCC, was approved and March 23, 2006.

MCC is in the process of writing a policy and procedures for conducting a preliminary background investigation prior to an employee starting work and will complete implementation of this policy by the end of calendar year 2006. To accomplish this, MCC has completed recent process changes to assist with full implementation of this recommendation. A Memorandum of Agreement has been negotiated and implemented with Department of State (DOS), Bureau of Diplomatic Security. DOS is currently serving as our investigations supplier and is able to provide preliminary National Agency Check (NAC) results prior to completion of the full field investigation. A Memorandum of Agreement with the U.S. Office of Personnel Management has been negotiated and implemented to electronically submit scanned fingerprint images for applicants in completing FBI criminal history checks.

Recommendation 2: We recommend that the Millennium Challenge Corporation update its Section 609(g) policy to include provisions to address the concept,

requirements, limitations, methodology and application of Section 609(g) bridge funding assistance to a country.

MCC concurs that we should periodically update our 609(g) policy as the use of such funding evolves. MCC has been in the process of reviewing and revising its section 609(g) policy to address bridge funding and other evolutions in the use of 609(g) authority since it was originally issued, and expects to complete the revision process by May 31, 2006.

We note, however, that the provision of bridge funding is well within the scope of our current section 609(g) policy, which was in effect prior to the time we started using bridge funding. The current policy provides “catch all” authority to the effect that “MCC reserves the discretion to provide 609(g) funding even if one or more of the above conditions is not met, subject to a case-by-case analysis and, in any event, consistent with the statutory requirements on the use of such funding.” Section 609(g) is a broad authority and its use will evolve over time to meet specific challenges that we and our eligible countries encounter in developing and implementing compacts. Therefore, while the statement that “MCC did not address this concept in its current 609(g) policy *because the need for such funding was not previously anticipated*” (emphasis added) is technically correct in that MCC did not anticipate this *precise* need when the policy was drafted, we do not agree with any implication that MCC should be able to anticipate all uses of its authorities in the abstract, or that we should refrain from using such “catch all” authority where appropriate. MCC grants are a completely new approach to development assistance, and the flexibility in section 609(g) was likely provided by Congress precisely because MCC cannot anticipate all of these requirements in advance.

For this same reason, while we believe that MCC should periodically update its 609(g) policy to reflect evolutions in the use of such funding over time, MCC cannot commit at this time that a revised section 609(g) policy will fully address the “concept, requirements, limitations, methodology and application” of section 609(g) funding. We do not want a new policy that is so detailed and restrictive that we in effect have to modify it every time we provide section 609(g) bridge funding or experiment with other new approaches to the use of this authority. Our revised policy will contain an appropriate level of detail on the use of section 609(g) for bridge funding and other purposes and will continue to contain appropriate “catch all” language to provide MCC with the needed flexibility to effectively carry out its mission.

Recommendation 3: We recommend that the Millennium Challenge Corporation develop and implement a policy for making specific determinations concerning countries’ participation in both the eligible and threshold country programs.

MCC concurs with the recommendation. In November 2005, the MCC Board decided for the first time to select three countries that were already threshold countries as eligible for Compact funding under FY2006 assistance. MCC’s policy at the time allowed countries to remain eligible to participate in both programs. However, the selection of these countries to be in both programs did raise a number of issues for MCC’s consideration. These include:

- Whether a country should be allowed to participate in the threshold program and be eligible for Compact funding simultaneously.

- Whether to consider how far along a threshold program is in development prior to selecting a threshold country for eligibility status.
- Whether to require that certain benchmarks be achieved prior to allowing a threshold country to begin the Compact development process after it has been selected as eligible for Compact funding.

The Millennium Challenge Corporation agrees that it is important to address these issues and develop a policy. Therefore, we have decided to review our policy and present options to the MCC Board for their consideration during the next selection cycle. A number of options exist, ranging from an exclusivity policy (a country may only participate in one program at a time), to a conditionality policy (a country must demonstrate a certain level of achievement in its threshold program before participating in compact development), to the current policy of allowing both programs to run concurrently. All factors will be considered during our review and development of a policy.

Recommendation 4: We recommend that the Millennium Challenge Corporation document its assessment of the automated options that could integrate all units of its human resources services plus interface with the U.S. Department of Interior's National Business Center systems to develop short-range and long-range plans for implementation.

MCC concurs with the recommendation. MCC recognizes the value of implementing an integrated human resources (HR) system, as well as a human resources and payroll system that is able to interface with NBC's systems and/or the management systems of other vendors. While MCC is committed to moving forward on this effort, this is a multi-year project given the significant investment in time and money required to effectively identify and implement a solution that will best meet MCC's needs.

As noted in the report, MCC has begun to identify its needs and review its options for an integrated HR/payroll system. MCC staff members have had preliminary conversations with NBC and with the Oracle Corporation. Based on these initial conversations, we are providing clarifications on two of the statements made in the discussion in the report on this recommendation:

- The report states that the Oracle Human Resources Suite (Oracle HR) *cannot* interface with NBC's system (emphasis added). Although Oracle HR does not currently interface with NBC's system, there have been preliminary discussions between MCC and NBC regarding the possibility of building an interface between Oracle HR and NBC's Federal Personnel Payroll System (FPPS).
- The report states that the implementation of the Oracle HR system would prevent the transmission of certain files to NBC and force MCC to rely on its current methods of sending e-mail or hard-copy documents to NBC. MCC believes further review is needed before a final conclusion on this issue can be reached. MCC selected Oracle HR as a starting point for the review since MCC currently uses Oracle Financials, the financial management database used by NBC. Therefore, implementing Oracle HR would enable the MCC HR system to easily interface with NBC's Oracle financial package. It also would hopefully interface with NBC's payroll services if it is determined that MCC can not run its payroll through the Oracle

system. Therefore, the MCC believes the Oracle HR/payroll systems should continue to be a part of the ongoing assessment.

MCC's next steps are to conduct a thorough needs assessment, identify and conduct thorough evaluations of the viable options, and select a system. A timetable for the completion of these tasks has not yet been established, but we plan to develop a timetable and project plan for this process by June 30, 2006. While MCC expects the selection and implementation of an integrated HR/payroll system to be a long process, it is continuing to enhance its existing tools and identify other solutions for improving the maintenance and tracking of the MCC's personnel data in the interim. For example, MCC has begun to generate SF-52 forms, which are used to initiate personnel actions, in FPPS and transmit the data electronically to NBC, thereby eliminating the need to complete a paper form and reducing the risk of a data entry error. Also, MCC has begun to use NBC's DataMart, a software package that interfaces with FPPS, to access and report on personnel, benefit, payroll, salary, and equal employment data stored by NBC, thereby decreasing our dependence on internal databases and spreadsheets.

Recommendation 5: We recommend that the Millennium Challenge Corporation provide each contracting officer's technical representative a designation letter for each contract that he or she manages.

MCC concurs with the recommendation. MCC has placed increased emphasis on promptly forwarding the COTR designation letter to each COTR. Each existing COTR will be provided a copy of their designation letter by May 31, 2006 to ensure that all current COTRs are in receipt of a letter.






Recommendation 6: We recommend that the Millennium Challenge Corporation formally define the frequency and contents of the progress reports for the threshold program required from the U.S. Agency for International Development and communicate these requirements to that Agency.

MCC concurs with the recommendation. MCC met with representatives from the U.S. Agency for International Development (USAID) MCA Secretariat on March 15, 2006 and submitted a template defining the format and content of the progress reports for the threshold program required from USAID. We discussed the template in detail. It calls for listing the performance objectives of the threshold program, the anticipated results over the course of implementation, and the actual results as they are achieved.


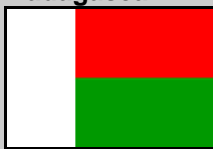




In the case of Burkina Faso, performance objectives include, among others, the building of 132 new primary schools, 1,650 girls attending school for the first time, and minimum attendance rates of 66 percent. MCC is requiring USAID to list projected targets for these objectives over the course of the two-year program, and then track those targets periodically.

The Secretariat agreed that this format is acceptable and that they will use it as a basis for future reporting.

**Table A-1:
Status of Eligible Countries by Regions**








Country	Fiscal Year(s) Eligible	Current Estimated Funding (millions)	Proposal/Compact Focus	Current Status as of February 2006
<i>LATIN AMERICA</i>				
Bolivia 	2004-2006	\$598	Micro-business	Due Diligence is pending
El Salvador 	2006	Not defined yet.	Not defined yet.	In the proposal development stage. MCC conducted initial visit to country in December 2005.
Honduras 	2004-2006	\$215	Roads project Agriculture project	Compact signed on June 13, 2005 Reached entry-into-force on September 23, 2005. First disbursement expected soon.
Nicaragua 	2004-2006	\$175	Roads Rural business Property regularization	Compact signed on July 14, 2005. Entry-into-force and first disbursement expected soon.
<i>Francophone Africa</i>				
Benin 	2004-2006	\$307	Land project Financial services project Port project	Compact approved by Board on January 30, 2006. Compact signed on February 22, 2006.

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Burkina Faso* 	2006	Not defined yet.	Not defined yet	In proposal development stage
Madagascar 	2004-2006	\$110	land tenure/financial sector reform/agricultural business investment	Compact signed on April 18, 2005. Entry-into-Force: July 27, 2005 First disbursement of \$2.5 million on July 27, 2005 Second disbursement on Dec. 31, 2005 of \$1.7 million. In implementation phase.
Mali 	2004-2006	\$309	Infrastructure Agricultural development	In due diligence phase
Morocco 	2005-2006	\$782	Preliminary: Infrastructure Rural tourism agriculture	Preliminary proposal submitted on Nov. 15, 2005.
Senegal 	2004-2006	\$255	Infrastructure	Due diligence phase underway. \$6.5 million in pre-compact assistance
Eurasia				
Armenia 	2004-2006	\$235.6	Rural Road rehabilitation project Irrigated Agriculture project	Compact approved by MCC's Board in December 2005. Compact signing expected soon.

* Burkina Faso was selected to participate in the Threshold Program in fiscal year 2006. A threshold plan was signed on July 22, 2005 for \$13 million. The two year program focuses on increasing girls' primary school enrollment and attendance.

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<p>East Timor</p> 	2006	Not defined yet	Not defined yet	MCC is scheduling its initial visit to the country in March 2006.
<p>Georgia</p> 	2004-2006	\$295.3	Regional infrastructure Energy sector rehabilitation/agriculture	Compact signed on September 12, 2005 Have not reached entry-into-force. Have not received first disbursement
<p>Mongolia</p> 	2004-2006	\$322	Housing and business training Health Transportation	Proposal submitted in September 2005. In due diligence phase.
<p>Sri Lanka</p> 	2004-2006	\$589.1	Irrigation Rural roads infrastructure	Final proposal submitted August 1, 2005. In due diligence phase.
<p>Vanuatu</p> 	2004-2006	\$65.69	Transport infrastructure (roads, wharves, airport landing strips)	Compact approved by MCC's board in January 2006. Compact signing expected soon.
Anglophone & Lusophone Africa				
<p>Cape Verde</p> 	2004 and 2006	\$110	Agriculture project Infrastructure project Private sector development	Compact signed on July 4, 2005. Entry-into-Force on Oct. 17, 2005 First disbursement of \$7.5 million received on Oct. 17, 2005 In implementation phase.
<p>Ghana</p> 	2004-2006	\$517	Agriculture/ infrastructure Financial services/extension/policy reform	Revised proposal submitted to MCC in Oct. 2005. Due diligence is being conducted.

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<p>Lesotho</p> 	<p>2004-2006</p>	<p>\$160</p>	<p>Preliminary contents:</p> <p>Water infrastructure</p> <p>Private sector development</p>	<p>Proposal development stage.</p> <p>Revised proposal expected soon.</p> <p>\$1.39 million in pre-compact assistance.</p>
<p>Mozambique</p> 	<p>2004-2006</p>	<p>\$262</p>	<p>Private sector development</p> <p>Water and sanitation</p>	<p>Revised proposal submitted on July 1, 2005</p> <p>\$6 million for pre-compact assistance</p>
<p>Namibia</p> 	<p>2006</p>	<p>Not defined yet.</p>	<p>Not defined yet.</p>	<p>MCC is planning its initial visit to the country in March 2006.</p>
<p>Tanzania</p> 	<p>2006</p>	<p>Not defined yet</p>	<p>Not defined yet.</p>	<p>MCC conducted its initial visit to the country in February 2006.</p>
<p>The Gambia</p> 	<p>2006</p>	<p>Not defined yet</p>	<p>Not define yet.</p>	<p>MCC's initial visit to the country has been postponed until further notice.</p>

**Table A-2:
Status of the MCC's Threshold Countries**

Country	Funding Level Requested	Indicator Focus	Concept Paper Submitted	Threshold Program Approved	Plan Signed (Implementation Phase)
Countries selected in FY 2004					
Albania	\$13.9	Control corruption	✓	✓	
East Timor	\$5.6	Regulatory Quality	✓		
Kenya	\$12.0	Control corruption	✓		
Sao Tome and Principe	\$4.0	Fiscal Policy	✓		
Tanzania	\$11.2	Control Corruption	✓	✓	
Uganda	\$10.0	Control corruption	✓		
Yemen	*		✓		
Countries selected in FY 2005					
Burkina Faso	\$12.9	Girls Education	✓	✓	✓
Guyana	\$11.5	Fiscal Policy	✓		
Malawi	\$20.9	Control Corruption	✓	✓	✓
Paraguay	\$34.7	Control corruption	✓	✓	
Philippines	\$20.0	Control corruption	✓		
Zambia	\$27.0	Control corruption	✓		
Countries Selected in FY 2006					
Indonesia	\$50.0	**	✓		
Jordan	\$25.0	**	✓		
Kyrgyz Republic	\$15.0	**	✓		
Moldova	\$21.5	**	✓		
Ukraine	\$49.0	**	✓		

*Yemen has been suspended from the Threshold Program due to a material decline in overall performance on the selection criteria for MCA Compact funding.

** Information not available at time of audit fieldwork.

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