



USAID
FROM THE AMERICAN PEOPLE

**UNITED STATES AGENCY FOR INTERNATIONAL DEVELOPMENT
OFFICE OF INSPECTOR GENERAL
FOR THE
MILLENNIUM CHALLENGE CORPORATION**

**SEMIANNUAL REPORT
TO THE CONGRESS**

April 1, 2006 - September 30, 2006

Mission

The mission of the Office of Inspector General (OIG) is to contribute to and support integrity, efficiency, and effectiveness in all activities of the organizations for which it has oversight responsibilities.

Values

In accomplishing our mission, OIG is committed to the following:

- Integrity
- Excellence
- Teamwork

Strategic Goals

- Promote sound accounting and reporting on financial activities and information security.
- Promote economy, efficiency, and effectiveness, and assess program results.
- Preserve and protect program and employee integrity.

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MESSAGE FROM THE INSPECTOR GENERAL

This Semiannual Report to the Congress presents information regarding the United States Agency for International Development, Office of Inspector General's (OIG) work and results achieved during the six-month period ending September 30, 2006. It is issued in accordance with the requirements of the Inspector General Act of 1978, as amended, and specifically addresses our responsibilities for the Millennium Challenge Corporation (MCC).

The work reported was planned and executed in support of OIG/MCC's three strategic goals:

- Promote sound accounting and reporting on financial activities and information security;
- Promote economy, efficiency, and effectiveness, and assess program results; and
- Preserve and protect program and employee integrity.

Significant OIG activity and achievements in support of these goals are described in this report, and comprehensive statistics and data regarding our efforts are also included.

OIG continues to take a results-oriented approach in support of the integrity, efficiency, and effectiveness of MCC during this critical phase of program and operations development.

Donald A. Gambatesa
Inspector General



EXECUTIVE SUMMARY

OIG's collaborative working relationship with MCC continues to demonstrate positive results. During this reporting period, management decision was reached on 23 recommendations. Final action was recorded on five recommendations. Work continued and was initiated in support of three strategic goals, and progress was realized under each of the goals as follows:

Strategic Goal 1: Promote sound accounting and reporting on financial activities and information security

OIG's role in support of in-country auditing arrangements resulted in the identification and qualification of audit firms in six countries to conduct audits of U.S. Government programs. Approval of firms in three additional countries is pending receipt of additional records and documentation. Additionally, OIG reviewed statements of work for audits in four countries to be conducted by local audit firms. Emphasis continues on building relationships with other organizations with experience or interest in

international auditing of development projects.

Three reports were issued: an audit of the financial system to be used to account for funds under an agreement with El Salvador;¹ a risk assessment of Millennium Challenge Account (MCA)/Cape Verde's financial operations;² and an audit of MCC's compliance with the provisions of the Federal Information Security Act of 2002.³ Vulnerabilities were identified that might lead directly to fraud, erroneous payment, or misappropriation of funds. The need for improvements to MCC's information security program was identified, though OIG noted that MCC had made some improvements in addressing such weaknesses.

Strategic Goal 2: Promote economy, efficiency, and effectiveness, and assess program results

An audit addressed MCC's procedures for ensuring that Section 609(g)⁴ assistance funds, grants made to facilitate Compact implementation, are used for intended purposes.⁵ The report

noted MCC's compliance with its current policy and initiatives to track and monitor funds, but identified several areas needing further improvement. Another audit report was issued addressing MCC's progress in developing its organizational structure and managing programs.⁶ The audit found that progress had been made but identified areas needing further attention.

Strategic Goal 3: Preserve and protect program and employee integrity

Fraud awareness briefings were conducted in five countries and MCC headquarters. These briefings highlighted potential contracting irregularities and educated those with responsibility for administering U.S. Government assistance programs to potential vulnerabilities.

1. Information Sensitive But Unclassified.

2. "Risk Assessment of Millennium Challenge Account Cape Verde's Financial Operations," September 26, 2006 (Audit Report No. M-000-06-004-F).

3. Information Sensitive But Unclassified.

4. Millennium Challenge Act of 2003, Section 609(g) – Assistance for Development Compact authorizes the Chief Executive Officer 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 United States and the country.

5. "Audit of the Millennium Challenge Corporation's Management of Section 609(g) Funds," September 28, 2006 (Audit Report No. M-000-06-002-P).

6. "Review of the Millennium Challenge Corporation's Progress in Achieving its Planned Organizational Structure and Beginning its Assistance Programs," May 16, 2006 (Audit Report No. M-000-06-001-S).

SUMMARY OF RESULTS

Strategic Goal #1: Promote sound accounting and reporting on financial activities and information security.

OIG continues to address MCC's challenge to develop effective financial management systems and related internal controls by testing MCC's systems to ensure they provide reliable and secure data.

OIG also provides expertise to MCC's in-country auditing arrangements. Prior to qualification, OIG assesses local firms for eligibility to perform audits, reviews documents to facilitate the in-country audit process; and audit products are evaluated for quality concerns. In the last six months, audit firms have been qualified in Benin, Cape Verde, Georgia, Ghana, Nicaragua, and Vanuatu. Approval of local audit firms to perform MCC work in El Salvador, Nicaragua, and Vanuatu is pending submission of additional information. Also, during this reporting period, OIG reviewed statements of work for audits planned by implementing agencies in Cape Verde, Georgia, Honduras and Madagascar.

OIG works to build relationships with other organizations that are active in the financial auditing of development projects. This is particularly useful where USAID does not have a presence. During this reporting period, OIG met with representatives of The World Bank's Europe and Central Asian Regions in Washington, DC to gain a better understanding of The World Bank's performance reviews, financial management and procurement practices.

AUDIT AND ASSESSMENT WORK

Audit of the General and Application Controls of the Government of El Salvador's Integrated Financial Administration System

The Integrated Financial Administration System is maintained by the Ministry of Hacienda and is the system expected to be used

to account for MCC funds under an agreement with El Salvador. OIG tested it to determine if it meets current information technology control standards for confidentiality, integrity, and availability. Six control weaknesses that could lead directly to erroneous or fraudulent payments and 77 additional weaknesses with potential to compromise the confidentiality, integrity, or availability of the data or information systems were identified.

OIG's audit report⁷ recommended that the six control weaknesses that could lead directly to erroneous or fraudulent payments be corrected or mitigated through compensating controls before MCC program funds are disbursed, and that MCC obtain an action plan for correcting the other 77 weaknesses before providing program funds to the Government of El Salvador. Management decision was reached on the report's recommendations. Final action is pending.

Risk Assessment of MCA/Cape Verde's Financial Operations

OIG conducted a risk assessment of MCA/Cape Verde,⁸ a \$110 million Compact program, during the implementation phase to detect vulnerabilities that could prevent the establishment of effective financial operations. Procurement

7. Information Sensitive But Unclassified.

8. "Risk Assessment of MCA/Cape Verde's Financial Operations," September 26, 2006 (Audit Report No. M-000-06-004-F).

policies have been implemented in compliance with guidelines established by MCA and MCC. However, MCA/Cape Verde's cash management process was identified as being at medium to high risk for misappropriation of funds and in need of improvement to its process for estimating immediate cash needs. Improvements are also needed in MCA/Cape Verde's review and approval process for disbursement requests and in its provision of guidance and oversight related to contractors' advances.

Audit of the Millennium Challenge Corporation's Compliance with the Provisions of the Federal Information Security Management Act of 2002 for Fiscal Year 2006

An audit was conducted to determine if MCC's information security program met the requirements of the Federal Information Security Management Act of 2002 (FISMA) for an agency-wide information security program that protects MCC's information and assets.⁹

MCC made improvements to its information security program but did not meet all of the requirements of FISMA. Several important challenges remain: certification and accreditation of its general support system; a process to manage remedial actions to strengthen information security; and oversight and evaluation of the contractor operated system.

9. Information Sensitive But Unclassified.

Strategic Goal #2: Promote economy, efficiency, and effectiveness, and assess program results.

OIG directs its efforts to evaluating MCC's response to management challenges and provides management with recommendations to address vulnerabilities. The challenges relate to human capital; the application of laws and regulations; and development of effective management oversight methodologies and programs.

AUDIT AND ASSESSMENT WORK

Audit of the Millennium Challenge Corporation's Management of Section 609(g) Funds

OIG reviewed compliance with policy and procedures to ensure funds issued under grants to facilitate Compact implementation, called Section 609(g) assistance funds, are used for intended purposes.¹⁰

MCC has developed initiatives to track and monitor Section 609(g) funds to ensure such funds were used for the purposes intended under the Millennium Challenge Act

of 2003. Section 609(g) assistance funds awarded after policy was implemented in June 2005, were found to be in accordance with policy. However, Section 609(g) funds were awarded to MCC's initial five recipient countries before the policy was implemented.

OIG identified several areas needing further improvement to the Section 609(g) program and made specific recommendations to address the lack of Section 609(g) bridge-funding policies and procedures; inadequate monitoring and tracking of Section 609(g) funds, specifically in the areas of financial controls and country capacity procurement assessment guidelines; and inadequate oversight of overseas procurement activities.

Review of the Millennium Challenge Corporation's Progress in Achieving Its Planned Organizational Structure and Beginning Its Assistance Programs

OIG reviewed MCC's progress in organizational and program management.¹¹ MCC made strides

in implementing its organizational plan; entering into Compacts with eligible countries; complying with the Millennium Challenge Act of 2003; and assessing the applicability of other federal laws and regulations to its operations.

Further attention is needed to policy development in the following areas: security clearance requirements; Section 609(g) pre-Compact funds; and countries' participation in both the threshold and eligible country programs. Short- and long-range plans are needed for an integrated human resource management system that will maintain and track personnel data and interface with external systems. Procedures to designate Contracting Officer's Technical Representatives (COTR) and to define the type and frequency of information that USAID should include in its progress reports on the threshold program.

Six recommendations were made, and management decision was reached on all. Final action was taken on one recommendation.

10. "Audit of the Millennium Challenge Corporation's Management of Section 609(g) Funds," September 28, 2006 (Audit Report No. M-000-06-002-P).

11. "Review of the Millennium Challenge Corporation's Progress in Achieving Its Planned Organizational Structure and Beginning Its Assistance Programs," May 16, 2006 (Audit Report No. M-000-06-001-S).

Strategic Goal #3: Preserve and protect program and employee integrity.

OIG's Fraud Awareness program focuses on prevention and protection of resources and consists of briefings and a manual that highlights potential contracting irregularities. Semi-annual briefings are conducted at MCC Headquarters for MCC, MCA entities of host countries, and other interested parties. During this reporting period, OIG also conducted Fraud Awareness briefings in Cape Verde, Georgia, Benin, Ghana, and Vanuatu for local government, implementing agencies, and audit firm staff, foreign government officials, and Supreme Audit Institute members.



REPORTING REQUIREMENTS

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DESCRIPTION OF RECOMMENDATIONS FOR CORRECTIVE ACTION MADE DURING THE REPORTING PERIOD WITH RESPECT TO SIGNIFICANT PROBLEMS, ABUSES OR DEFICIENCIES IDENTIFIED

**As of September 30, 2006
IG Act, Section 5(a)(2)**

Report	Recommendations for Corrective Action
M-000-06-001-S	<ol style="list-style-type: none"> 1. Personnel Security Procedures: Need for security-related policies and procedures that (1) identify clearance level for each employee and (2) require a preliminary background investigation at a minimum. 2. Program Policy improvements: Need to update Section 609 (g) policy regarding concept, requirements, limitations, methodology and application. 3. Program Policy improvements: Need for policy guidance on whether a country should be in both the “Eligible” and “Threshold” country programs. 4. Information Technology: Assessment recommended for automated options to integrate human resource functions and interface with Department of Interior’s National Business Center. 5. Procurement - Contracting Officer’s Technical Representative: MCC should provide each Contracting Officer’s Technical Representative with a designation letter for each contract they manage. 6. Program Development - Progress Reports: MCC should formally define the frequency and contents of progress reports for the Threshold Program and communicate these requirements to USAID.
M-519-06-002-P	<ol style="list-style-type: none"> 1. Information Technology: Deficiencies in information technology system for the Financial Accounting System should be corrected prior to awarding MCC program funds. 2. Information Technology - Timeline for Improvements Require an action plan with timeframes to correct information technology deficiencies prior to awarding MCC program funds.

Report	Recommendations for Corrective Action
M-000-06-004-F	<ol style="list-style-type: none"> 1. Financial Management - Cash Management Establish policies and procedures to evaluate disbursement requests from recipient countries and require excess cash to be refunded to MCC. 2. Financial Statements - Accounting for MCC Funds by the Recipient Country Require financial statements covering MCC funds managed by the recipient country to be on the accrual basis of accounting or provide data to inform MCC of accrual expenditures. 3. Financial Management - Cash Management Establish policies and procedures to guide the recipient country in disbursements to secondary recipients.
M-000-06-002-P	<ol style="list-style-type: none"> 1. Financial Management – Procurement Establish procedures to ensure validity of the invoice and improve voucher approval and payment. 2. Financial Management - Procurement Establish a policy for the process of approving deviations to the Procurement Agreement. 3. Financial Management – Procurement Issue guidance for assessing procurement capacity by a government or others. 4. Financial Management – Procurement Define MCC responsibility for monitoring and reviewing the recipient country’s procurement.
M-000-06-003-P	<ol style="list-style-type: none"> 1. Information Technology – FISMA Compliance Complete certification and accreditation of the general support system for MCC 2. Information Technology – FISMA Compliance Develop a process to ensure compliance with FISMA 3. Information Technology - FISMA Compliance Develop a process to improve FISMA compliance and submit a Plan of Action and Milestone Report to the Office of Management and Budget quarterly. 4. Reopened:- from M-000-05-003-P (Recommendation 2) Information Technology – Security Conduct periodic risk assessments. 5. Reopened – from M-000-05-003-P (Recommendation 3) Information Technology – Security Establish policies and procedures to address risks identified in assessments 6. Reopened – from M-000-05-003-P (Recommendation 4) Information Technology - Security Document a process to periodically evaluate the effectiveness of information security 7. Reopened – from M-000-05-003-P (Recommendation 5) Information Technology – Security Delegate the Chief Information Officer authority to ensure compliance with Information systems policy and designate a Information Security Officer

**SIGNIFICANT AUDIT RECOMMENDATIONS DESCRIBED IN A
PREVIOUS SEMIANNUAL REPORT ON WHICH CORRECTIVE
ACTION (FINAL ACTION) HAS NOT BEEN COMPLETED
IG Act, Section 5 (a) (3)**

As of September 30, 2006

Report Number	Issue Date	Recommendation Number	Recommendation
M-000-05-003-P	June 20, 2005	8	Establish and document plans to ensure continuity of operations for information systems
M-000-06-001-C	December 6, 2005	1	Revise and reissue written policies and procedures that provide additional specificity including the Fund Balance with Treasury, financial reporting, payroll processing, accrual generation and reporting, interagency reporting, fixed assets, travel, monitoring and internal grant processes.
		3.1	Develop policies and procedures to ensure that the payment schedules and other agreements entered into with the grantees reflect U.S. Treasury requirements concerning advances and immediate cash needs.
		3.2	Establish policies and procedures to ensure that any custodial liabilities, e.g. interest owed to the U.S. government resulting from the grantee advances, are properly recorded.
		5.2	Assess the automated options available to handle MCC operations and develop short range and long range plans for the implementation of the most appropriate information technology structure to address electronic integration of at least the payroll, procurement and travel functions and systems to increase the efficiencies and effectiveness of the process of financial transactions, and decrease the risk of errors.
M-000-06-003-F		1	Establish and provide a set of detailed accounting policies and procedures to recipient countries prior to the initial cash disbursement, which can be used during their implementation phase.
		2	Establish and distribute a set of policies and procedures for managing assets purchased with MCC funds.

REPORTING REQUIREMENTS FOR WHICH THERE IS NOTHING TO REPORT

As of September 30, 2006

Reporting Requirement	IG Act Reference
Summary of matters referred to prosecutive authorities and the prosecutions and convictions that have resulted	Section 5 (a) (4)
Summary of instances in which information or assistance was refused: The Inspector General Act of 1978 (Public Law 95-452), as amended, requires the identification of any reports made to the head of an agency describing where information or assistance was refused or not provided. During this reporting period, there were no reports to the Millennium Challenge Corporation describing instances where information or assistance was unreasonably refused or not provided.	Section 5(a) and 6(b)(2)
Audit reports issued by subject matter with questioned costs, unsupported costs and the dollar value of recommendations that funds be put to better use.	Section 5(a)(6)
Number of audit reports issued, with questioned costs, and unsupported costs	Section 5(a)(8)
Number of audit reports, with the dollar value of recommendations that funds be put to better use.	Section 5(a)(9)
Summary of each audit report issued before the start of the reporting period for which no management decision has been made by the end of this reporting period	Section 5(a)(10)
Decisions and reasons for significant revised management decisions	Section 5 (a) (11)
Information concerning significant management decision with which the IG is in disagreement	Section 5(a)(12)
Information under the Federal Financial Management Improvement Act of 1996 (Section 05B) – Remediation Plan Information	Section 5(a)(13)
OIG review of legislation and regulation	Section 4 (a) (2)
Particularly serious or flagrant problems, abuses or deficiencies relating to the administration of programs and operations	Section 5 (d)





USAID
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Inspector General **HOTLINE**

OIG's Hotline makes it easy to report allegations of fraud, waste, abuse, mismanagement or misconduct in programs and operations of the USAID, IAF, ADF, and MCC. Employees, contractors, program participants and the general public may report allegations directly by e-mail, telephone, or mail to:

Phone 1-202-712-1023
1-800-230-6539

E-mail ig.hotline@usaid.gov

Mail USAID OIG HOTLINE
P.O. Box 657
Washington, DC 20044-0657



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www.usaid.gov/oig/public/semiann/mcc1.htm