Millennium Challenge Corporation

Performance Accountability Report

Fiscal Year 2007

Reducing Poverty Through Growth

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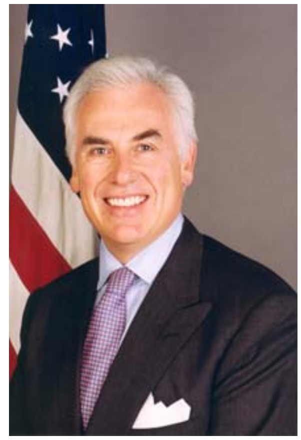
Message from the Chief Executive Officer



In submitting the *2007 Performance and Accountability Report* for the Millennium Challenge Corporation, we mark the maturing of the program and a new emphasis on implementation moving forward. Our efforts in 2007 reflect well on the resources that Congress has provided us. By the end of fiscal year 2007, we signed 14 Compacts and have approved 17 Threshold programs. We opened fiscal year 2008 with the signing of our 15th Compact with Mongolia, and look forward to signing our Compact with Tanzania. Well over a majority of MCC eligible and threshold countries are either in implementation or initiating the last steps necessary to begin implementation of their programs.

As this report reflects, MCC is now fully engaged in every area of the developing world and in wide spectrum of development projects. In Asia, we are supporting programs to reduce corruption in the Philippines and Indonesia. In Central America, we are engaging in infrastructure projects, land reform, and agricultural development. In Africa, where we have signed compacts with eight countries, we have launched land reform, initiated port projects and enhanced new opportunities for agriculture development. Finally, we are well along the way with critical infrastructure projects in Armenia and Georgia. All these projects benefit the very poorest of citizens and target key constraints to economic development.

More, of course, needs to be done. Our efforts looking forward are increasingly focused on shifting from compact development to compact implementation. This is a significant turning point for MCC. Though we continue to believe that our partner countries are best able to identify barriers to their economic development, propose programs, and implement them, MCC's role in supporting country implementation is paramount. In supporting our partner countries, we work to leave behind a sustainable contribution that enhances each country's inherent capacity to develop on its own. Indeed, enhancing country capacity is a distinctive element of the MCC model. Consequently, we will continue to empower our partners to implement their programs and support them at key junctures with resources and lessons learned from other programs to ensure successful outcomes. These outcomes will become more and more apparent in fiscal year 2008 when several programs will be far enough along to begin assessing and reporting on performance.

MESSAGE FROM THE CHIEF EXECUTIVE OFFICER

This approach has already yielded results. In 2007, MCC continued to build significant in-country capacity by bringing key individuals from partner countries to Washington for training in procurement, fiscal accountability, monitoring and evaluation, and environmental and social assessments. Moreover, we have reduced the complexity of our compact documents and have transferred more responsibility to our Resident Country Directors to give those in the field the latitude to make decisions that will deliver results quickly. Further, the lag time between compact signing and program implementation has been significantly reduced.

Because another distinctive feature of MCC is to promote policy reform, I would be remiss if I did not mention the "MCC effect." By providing assistance to countries that practice good policies, MCC continues to be a catalyst for reform. Countries, in turn, are initiating reforms, not just to qualify for MCC's assistance but also because it is the right thing to do. For example, we are proud of the resolution that Congress passed recognizing Lesotho's enactment of *the Law to Improve Women's Rights* and acknowledging MCC's role in that reform. Other countries, that are not yet eligible for our assistance, continue to use the prospect of an MCC compact as an incentive to push further reforms.

I am pleased to report that MCC has been a good steward of resources and has received an unqualified opinion on its financial records from an independent auditor. Moreover, I can certify with reasonable assurance that MCC's systems of accounting and internal controls are in compliance with the provisions of Section 2 (internal and administrative controls) and Section 4 (financial systems) of the *Federal Managers' Financial Integrity Act*. I have also concluded that the systems of accounting and internal controls provide reasonable assurance of MCC compliance with the internal control objectives stipulated by the Office of Management and Budget in Circular A-123, *Management's Responsibility for Internal Control*. Finally, I have determined that MCC is currently in substantial compliance with pertinent requirements of the *Federal Financial Management Improvement Act*.

We look forward to the challenges of the year ahead and to reporting more results in a number of our programs next year.

John J. Danilovich
Chief Executive Officer

MESSAGE FROM THE CHIEF FINANCIAL OFFICER

The 2007 Performance and Accountability Report of the Millennium Challenge Corporation (MCC) reflects our commitment to the highest standards of federal management as embodied in the President's Management Agenda. Since inception, the MCC has received an unqualified or "clean" audit opinion from the Office of the Inspector General (OIG) on its financial statements.

The current year has been one of growth and maturity in all areas of the MCC, and the Department of Administration and Finance is no exception. Building upon the solid groundwork laid in the prior year, we have accomplished a number of significant goals in the current year:

- We developed an Enterprise Architecture model that provides a framework to align MCC's future business vision with technology planning and procurement efforts.

- We are committed to the implementation of a fully integrated financial system compliant with the requirements of the Federal Financial Management Improvement Act (FFMIA). In 2007 we completed an assessment of our financial systems environment and developed options for moving to a fully integrated system within the next two years.

- To address cash management concerns raised by the OIG and improve timeliness of reporting from our partner countries, we piloted a Common Payment System (CPS) in Mali. The CPS centralizes the payment of compact expenses with MCC's financial services provider and eliminates the need to "advance" funds to partner countries. The CPS will be deployed in all new and existing compact countries over the next twelve to eighteen months.

- We are developing a Business Intelligence and Data Storage (BIDS) tool that will automate reporting from our partner countries, provide a workflow component for the efficient approval and storage of documents, and merge performance and financial data to support managerial cost accounting, budget/performance integration, and reporting to internal and external stakeholders.

MESSAGE FROM THE CHIEF FINANCIAL OFFICER

- Recognizing that the future success of MCC is dependent on maintaining a small highly skilled work force, we have significantly improved our diversity profile, conducted an employee engagement survey, and installed a new system to manage MCC's staffing and personnel management needs. The Office of Personnel Management in conjunction with a study conducted by the American University recognized MCC as one of the best small agencies to work in the Federal government.

We have worked aggressively to resolve outstanding OIG issues from our FY 2005 financial audit, and I am pleased to report that the number of audit findings decreased from nine in FY 2006 to four in the current year. We have accepted responsibility to resolve these findings and plans are already underway to address them in the upcoming year. We have also worked to resolve other audit issues dealing with management accountability. For example, a recent follow-up audit by the OIG of our Contracts and Grants Management Division resulted in no new findings, and an acknowledgement that previous recommendations had been resolved. This is a significant achievement in an area vital to the success of the MCC model.

As the MCC focuses its efforts on compact implementation, it is our goal to continue to provide the financial, contracting, personnel, and technology support to ensure our future success. This focus will provide the necessary tools to demonstrate accountability, results, and effective utilization of our resources.

Michael W.S. Ryan
Vice President
Administration and Finance

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1. MANAGEMENT DISCUSSION AND ANALYSIS

OUR MISSION AND HISTORY

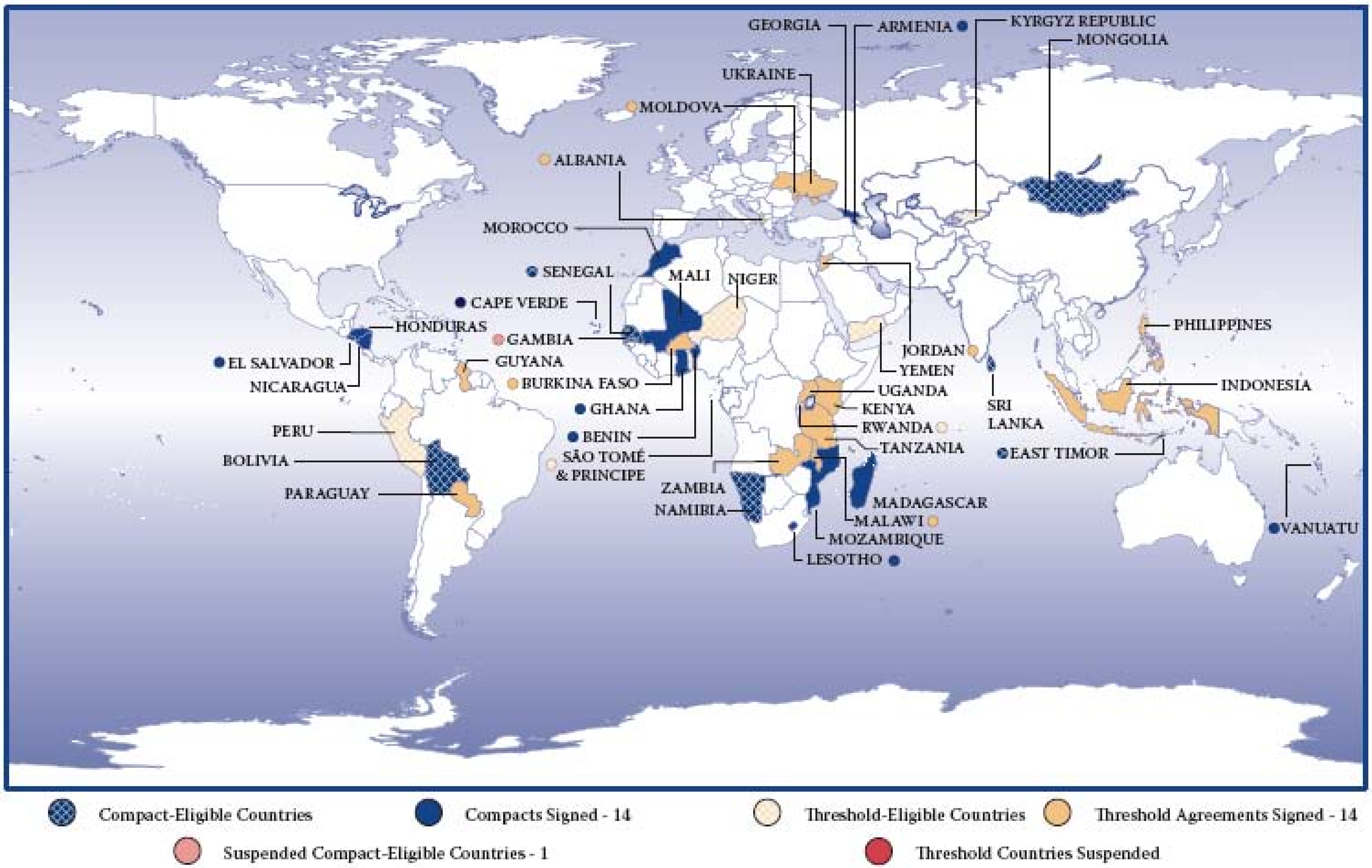
The Millennium Challenge Corporation's (MCC) mission is to reduce poverty by supporting sustainable, transformative economic growth in developing countries that create and maintain sound policy environments.

MCC is a United States Government corporation designed to work with some of the poorest countries in the world. Established in January 2004, MCC is based on the principle that aid is most effective when it reinforces good governance, economic freedom, and investments in people. MCC's mission is to reduce global poverty through the promotion of sustainable economic growth. Led by a Chief Executive Officer (CEO) and overseen by a Board of Directors, MCC is responsible for the stewardship of the Millennium Challenge Account (MCA), which receives funds each year appropriated by Congress.

MCC selects countries that are eligible for a compact, a multi-year agreement between MCC and an eligible country to fund specific programs targeted at reducing poverty and stimulating economic growth. To become eligible to receive a compact, MCC evaluates a country's performance on 17 independent and transparent policy indicators in three categories: ruling justly, investing in people, and economic freedom. Countries that have demonstrated significant improvement in policy indicators but do not yet qualify for a compact grant may be eligible for Threshold program assistance. Threshold programs are smaller grants designed to help improve performance on specific indicators.

MCC has signed compacts with 14 countries. In addition, 14 countries receive Threshold program assistance. The countries currently receiving MCC assistance and those that are eligible for assistance are detailed in Exhibit 1-1.

Exhibit 1-1: Compact and Threshold Countries



MCC's Fundamental Principles

MCC awards grants—not loans—to partner countries through an innovative and competitive process built upon three fundamental principles that are essential for the effective and efficient use of development assistance—good policy performance, country ownership, and tangible results.

1. **Good Policy Performance: Selection Process.** MCC works with countries that rule justly, invest in their people, and promote economic freedom. MCC assesses a government's performance in these three areas by using objective, transparent, and third-party indicators taken from non-U.S. Government sources. MCC uses these indicators to create a scorecard measuring a country's policy performance among its own peer group in the same per capita income range. MCC's Board of Directors then uses these scorecards to determine and select annually which countries are eligible to receive aid based on policy performance.
2. **Country Ownership: Compact Development Process.** Once countries qualify and are selected for MCC assistance on the basis of their policy performance, they are invited to develop a proposal for funding—what MCC calls a compact. Eligible countries must first identify their main constraints to poverty reduction and economic growth. Eligible countries are expected to design and submit their proposals for funding that address their own priorities and constraints. Countries develop their proposals in consultation with their own society, building country ownership that increases the likelihood of success and sustainability. MCC evaluates and conducts due diligence on each proposal to determine whether it will lead to poverty reduction and growth. If a country's proposal is approved for funding, MCC and the country sign a compact. This mutual agreement outlines responsibilities for both MCC and the partner country and stipulates performance benchmarks to ensure accountability and outcomes.
3. **Tangible Results: Implementation Process.** Once MCC's Board approves a compact proposal, MCC holds its partner countries responsible for the aid they receive. That is why MCC's assistance goes to those countries that develop programs with clear objectives, benchmarks to measure progress, procedures to ensure sound financial management, and a plan to monitor outcomes and evaluate impacts. Ultimately, MCC expects its assistance to generate tangible results in the lives of the poor. To ensure transparency and accountability, MCC's assistance is disbursed only as performance benchmarks are achieved.

MILLENNIUM CHALLENGE CORPORATION'S ORGANIZATION

Structure and Staffing

MCC's model for providing development assistance to partner countries puts the responsibility for program development and implementation on the partner country. MCC maintains a very small staff in its Washington, D.C. headquarters when compared with other international development institutions. MCC's staff is composed of regional and sector experts that assist partner countries through the compact development and implementation process. During the intense period of compact development and implementation start-up, MCC contracts with additional outside experts for limited engagements. MCC also uses contractors for oversight, supervision, monitoring, and evaluation assistance.

In FY 2007, MCC concluded an aggressive hiring process to fill remaining slots under the authorized level of 300 full-time employees at the Washington, D.C. headquarters. This process was completed in mid-2007. MCC has been successful in attracting top candidates from the public and private sectors and has maintained an organizational structure with a high percentage of senior staff and a low percentage of administrative support personnel. This is consistent with MCC's original design and vision.

In keeping with its model of high standards of accountability, but also requiring countries to take ownership of their own development, MCC's practice is to have a small staff, usually three to five people, in each compact country. MCC set up new offices in six countries in FY 2007 for a total of 14 overseas offices, one in each country with which MCC has a compact. These offices will play a pivotal role in MCC's increased emphasis on implementation oversight because of their proximity to the MCA entities responsible for implementation.

Governance

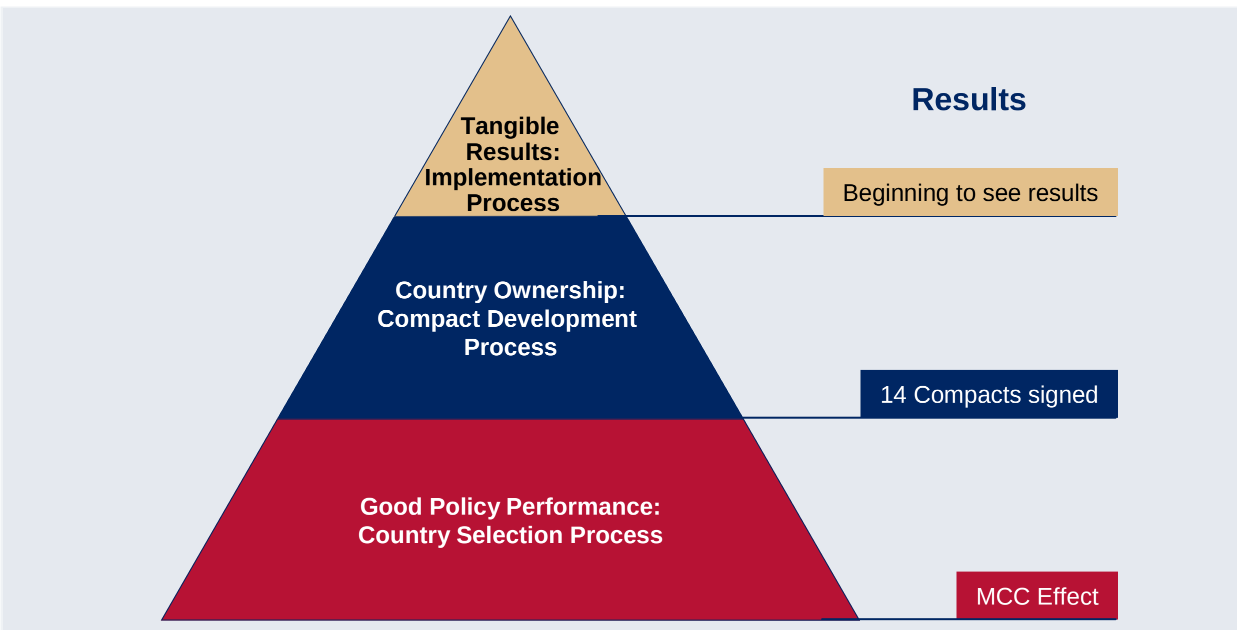
MCC is governed by a Board of Directors composed of the Secretary of State, Secretary of the Treasury, U.S. Trade Representative, Administrator of the United States Agency for International Development (USAID), and MCC's CEO. In addition, the Board has four public members appointed by the President with the advice and consent of the U.S. Senate. The Secretary of State is the Chair of the Board and the Secretary of the Treasury is the Vice Chair. A CEO, appointed by the President and confirmed by the Senate, manages MCC.

While MCC is not a Chief Financial Officers (CFO) Act agency, it has decided to adhere to the requirements and principles applicable to such agencies by preparing an annual Performance Accountability Report (PAR) in accordance with Office of Management and Budget (OMB) requirements and guidance.

FISCAL YEAR 2007 HIGHLIGHTS—
OCTOBER 1, 2006 TO SEPTEMBER 30, 2007

In Fiscal Year (FY) 2007, MCC achieved results in each of the three core principles that MCC's model is built upon: (1) policy performance, (2) country ownership, and (3) tangible results. Exhibit 1-2 illustrates how these three elements are related.

Exhibit 1-2: MCC Principles



The foundation of MCC's engagement with partner countries is the principle that policies matter. History has demonstrated that countries with strong policies in the areas of ruling justly, investing in people, and economic freedom have lower rates of poverty and higher rates of economic growth. In FY 2007, MCC continued to see countries improving their policy environment to become eligible or remain eligible for MCC funding. This positive incentive that is created by the prospect of MCC funding is referred to as the "MCC effect."

Building on the foundation of a sound policy environment, MCC is seeing real results in country ownership as countries take ownership of their own development and play the lead role in the process of developing and implementing their compacts. This ownership is crucial to ensuring that development results are sustainable and truly transformational.

By the end of FY 2007, MCC had selected 25 countries as eligible for assistance because of their policy performance. MCC successfully signed compacts with 14 of these countries, and MCC expects to sign compacts with up to four additional countries in FY 2008. As a result, MCC is beginning to see the impact of the third principle, tangible results—an area that will be a key focus for FY 2008 and beyond.

Principle 1—Good Policy Performance: Key Results from FY 2007

While delivering country-specific results through compacts and Threshold programs, MCC's approach offers positive incentives for creating the conditions that make development sustainable and transformative. This is core to MCC's early successes and demonstrates how MCC is changing the conversation about how development takes place.

Changing Lives Through Policy Reforms

MCC motivates reforms.

By insisting on sound political, economic, and social policies, MCC motivates the hard work of policy changes in countries that want to either maintain their eligibility with MCC or qualify for it. As a result, countries are making improvements in governance, increasing investments in health and education, and creating pro-business conditions. Even before a dollar of MCC assistance is invested, countries are investing in their own development to qualify for MCC funding, a phenomenon we call the "MCC effect." For example:

- According to the World Bank's Doing Business project, 24 countries specifically cited MCC as the primary motivation for their efforts to improve their business climate.
- Inter-ministerial committees and presidential commissions have been set up in at least a dozen countries to devise reform strategies that address MCC's selection criteria.
- Guatemala is interested in becoming eligible and has taken significant steps to improve its policy performance on MCC's indicators. Tough anti-corruption reform measures include prosecuting high-ranking officials on charges of corruption, creating a financial crimes unit, hiring a foreign accounting firm to audit spending by the legislature, initiating online disclosure of government procurements, and implementing a performance-based budgeting process.
- Liberian President Ellen Johnson-Sirleaf has expressed great interest in adopting the reforms necessary to be selected to participate in MCC. Her administration is addressing corruption in the Finance Ministry, requiring senior government appointees to declare their financial assets, canceling all timber export contracts, and reviewing port handling concessions.

These countries are representative of many others that, although not yet eligible for MCC assistance, are undertaking policy reforms and improving their practices and procedures with the expectation of qualifying for MCC assistance.

Transforming Lives by Rejecting Corruption

MCC promotes a culture of transparency.

- MCC is the only donor that currently ties eligibility for assistance to performance on a transparent and public Control of Corruption indicator. Passing this corruption indicator is the only hard hurdle to qualify for MCC funding. This creates a powerful incentive for countries to adopt tough anti-corruption laws, strengthen oversight institutions, open up the public policymaking process to greater scrutiny, and increase corruption-related investigations and prosecutions.
- Georgia—as just one example—adopted dramatic anti-corruption reforms leading to a significant improvement in its control of corruption indicator from the 36th percentile in 2004 to the 78th in 2005. The percentage of firms in Georgia reporting that bribes are necessary to get things done plummeted from 37 percent to 7 percent. Georgia has arrested scores of public officials, made legislative changes that facilitate the prosecution of corruption cases, fired 15,000 members of the police force, and increased the salaries of 10,000 public servants to counter the lure of petty corruption. The World Bank's 2006 and 2007 Doing Business reports identified Georgia as one of the world's most aggressive reformers.

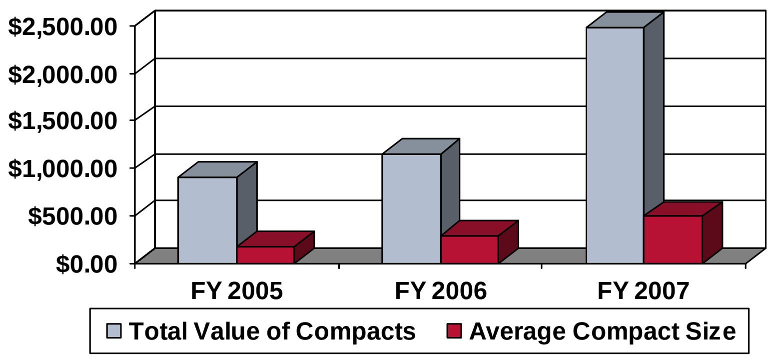
Principle 2—Country Ownership/Compact Development: Key Results from FY 2007

Building on the first principle that policies matter and the key results that are taking place in the area of policy reform, MCC is demonstrating results in the second principle, country ownership. Eligible countries are designing and submitting their proposals for funding that address their own priorities and constraints. Countries develop their proposals in consultation with their own society, building country ownership that increases the likelihood of success and sustainability.

As of the end of FY 2007, MCC signed 14 compacts, totaling nearly $4.55 billion. Five of these, representing more than $2.5 billion, were signed in FY 2007. The compacts signed in FY 2007 were consistent with the President's stated request that compacts be larger in size and transformative (see Exhibit 1-3). During FY 2007, MCC worked with a number of other countries to help them develop their compacts, and MCC expects to sign compacts with up to four additional countries in FY 2008. MCC has also signed Threshold agreements with 14 countries, totaling approximately $316 million. Seven of MCC's 14 Threshold agreements were signed in FY 2007.

Exhibit 1-3: Number of Compacts, Total Value of Compacts, and Average Compact Size by Fiscal Year (all figures in $ millions)

	Year of Compact Signing		
	FY 2005	FY 2006	FY 2007
Number of Compacts Signed	5	4	5
Total Value of Compacts	$905.2	$1,155.6	$2,482.8
Average Compact Size	$181.0	$288.9	$496.6



A compact is a multi-year agreement between MCC and an eligible country to fund specific programs aimed at reducing poverty and stimulating economic growth. It is a mutual promise between the U.S. Government and a partner country, each with specific responsibilities to fulfill. The compact enters into force after initial set-up and when project implementation begins. Exhibit 1-4 lists the dates that compacts were signed and entered into force.

Exhibit 1-4: Compacts in Signing Order

Compact With	Award (in millions)	Signed On	Entry Into Force On
Madagascar	$109.8	April 18, 2005	July 27, 2005
Honduras	$215.0	June 13, 2005	September 29, 2005
Cape Verde	$110.0	July 4, 2005	October 17, 2005
Nicaragua	$175.0	July 14, 2005	May 26, 2006
Georgia	$295.3	September 12, 2005	April 7, 2006
Benin	$307.3	February 22, 2006	October 6, 2006
Vanuatu	$65.7	March 2, 2006	April 28, 2006
Armenia	$235.7	March 27, 2006	September 29, 2006
Ghana	$547.0	August 1, 2006	February 16, 2007
Mali	$460.8	November 13, 2006	September 17, 2007
El Salvador	$461.0	November 29, 2006	September 20, 2007
Mozambique	$506.9	July 13, 2007	Pending
Lesotho	$362.6	July 23, 2007	Pending
Morocco	$697.5	August 31, 2007	Pending
Total	**$4,549.6**		

A Threshold program is designed to assist countries that are on the threshold of eligibility, meaning they have not yet qualified for compact funding but demonstrate significant commitment to improving their performance on the eligibility criteria for full compact funding. MCC's authorizing legislation allows using up to 10 percent of MCC funding for the Threshold program. Exhibit 1-5 lists Threshold programs that are currently underway as of the end of FY 2007.

Exhibit 1-5: Threshold Programs in Signing Order

Threshold Program With	Award (in millions)	Signed On
Burkina Faso	$12.9	July 22, 2005
Malawi	$20.9	September 23, 2005
Albania	$13.9	April 3, 2006
Tanzania	$11.2	May 3, 2006
Paraguay	$34.6	May 8, 2006
Zambia	$22.7	May 22, 2006
The Philippines	$20.7	July 26, 2006
Jordan	$25.0	October 17, 2006
Indonesia	$55.0	November 17, 2006
Ukraine	$45.0	December 4, 2006
Moldova	$24.7	December 15, 2006
Kenya	$12.7	March 23, 2007
Uganda	$10.4	March 29, 2007
Guyana	$6.7	August 23, 2007
Total	**$316.4**	

Transforming Lives Through Capacity Building

MCC helps countries build institutional capacity.

- By insisting that partner countries design and implement their own development plans, MCC is strengthening institutions and encouraging critical thinking about what policies are necessary to ensure sustainability. Country ownership reinforces the good policies MCC demands.
- In **Ghana**, one of the major obstacles to successful development has been the lack of adequately trained procurement specialists. The ability to procure goods and services in a transparent and competitive manner ensures the best use of public funds. MCC is funding a procurement capacity-building initiative within the Ghanaian government designed to strengthen the effectiveness of various procurement entities to help Ghana help itself overcome this barrier to its own development. Ghana also has said that it will use the consultative and rigorous MCC process that led to its compact to evaluate non-MCC funded

activities within the country. Moreover, to share experiences and lessons learned in developing and implementing compacts, Ghana hosted fellow African country MCA officials at a conference.

- **Mozambique** is applying the skills and expertise of the core team that worked on drafting its compact to other government processes unrelated to MCC.
- In **Georgia**, extensive collaborative efforts are strengthening the Georgia Department of Statistics to ensure that MCA-Georgia, which is responsible for compact implementation, monitoring, and evaluation, has the best possible data to evaluate its program and to generate stronger impact evaluation and data gathering capacity within the Georgian government overall. Asking countries, such as Georgia, to develop their own compacts, including the monitoring and evaluation plans, enhances their abilities and skills to evaluate other programs, including those of their own governments. MCC partner countries are responsible for establishing baselines and demonstrating and measuring results to focus on outcomes and impacts rather than projects.

Country ownership encourages civil participation and accountability.

- In **Nicaragua**, extensive public participation in designing and implementing the MCA program has generated unwavering support from local officials, civil society groups, and program beneficiaries. This support serves to sustain the program during elections and political transitions, allowing it to progress uninterrupted.
- **Benin** held a nationwide consultative workshop to select communes to participate in the Rural Landholding Plans activity. The list of selected communes was made public on MCA-Benin's website.
- In **Honduras**, 200 municipalities attended workshops to identify roads to be improved under the Farm-to-Market Roads activity, resulting in applications for improvements to 6,645 kilometers of road. Civil engineers are now using publicly available criteria to conduct field assessments of the applications to make selections.
- In **Armenia**, the MCA Stakeholders' Committee, representing the water users' associations, farmers, non-governmental organizations (NGOs), and the beneficiary community, has taken an active role in organizing public outreach events and in engaging with MCA-Armenia.

Country ownership helps sustain high environmental and social impact standards.

- **Cape Verde's** compact supports the protection of the environment and citizens' rights. MCA has carried out environment-related public awareness sessions, environmental impact assessments, an environmental and social monitoring plan, community-based watershed management plans, and resettlement action plans.

- The **Georgia** compact raised the bar on environmental protection by applying unprecedented environmental standards to gas pipeline repairs. Georgian corporations supervised project construction in accordance with international environmental standards for the first time.

Principle 3—Tangible Results/Implementation: Key Results from FY 2007

The purpose of MCC's emphasis on the policy environment and country ownership, Principles 1 and 2, is ultimately to pave the way for success in achieving Principle 3, to yield tangible results in the lives of poor people. MCC holds its partner countries responsible for the aid they receive. All MCC compacts include specific monitoring and evaluation plans that lay out benchmarks that evaluate whether the program is on track to reach the outcomes for which it was intended.

FY 2007 represented a year of transition for MCC as the Corporation moved from a focus on incentivizing policy reforms and working with countries to design and complete compact programs, to helping partner countries in the implementation of those programs.

Initial performance results reported by countries in compact implementation demonstrate that MCC is making substantial progress, particularly in the agriculture and land sectors. Key results as of September 1, 2007, include:

- In **Madagascar**, a total of more than 876,000 documents have been inventoried to enable better land use. Six Agricultural Business Centers are now operational in five zones, with more than 3,950 visitors to date and 45 field agents providing services to small and medium-size enterprises. The agricultural project is providing technical training and small business skills to more than 6,400 farmer beneficiaries in five zones.
- In **Armenia**, 2,453 participants have been trained in on-farm water management to ultimately increase agricultural production, of which 571—almost 23 percent—are female farmers.
- In **Georgia**, the Agribusiness Development Project has awarded grants worth $1.1 million to 34 new or expanding agribusinesses. These grants will support agribusiness development projects by improving technologies and facilitating market access. They will employ about 400 people and do business with 22,000 customers and suppliers. Phase I repairs of the North-South Gas Pipeline have been completed.
- In **Nicaragua**, out of 43,000 property titles to be delivered, 26 beneficiaries have received titles and 500 more beneficiaries are in the process of receiving titles.

Exhibit 1-6 describes each compact program and current implementation results. The results indicate that MCC is reaching key process milestones on these projects such that longer term objectives can be achieved.

Exhibit 1-6: Compact Programs and Tangible Results

Country	Program Description	Implementation Results
Africa		
Benin	Compact is for 5 years and $307 million, and intends to: ▫ Increase investment and private sector activity. ▫ Increase access to land through more secure and useful land tenure. ▫ Expand access to financial services through grants given to micro, small, and medium-size enterprises. ▫ Provide access to justice by bringing courts closer to rural populations. ▫ Improve access to markets by eliminating physical and procedural constraints currently hindering the flow of goods through the Port of Cotonou.	▫ Rural land titling program is expected to formalize land registries in the form of “Plans Fonciers Ruraux” in 300 villages across Benin. ▫ An engineering solution to the sedimentation of the entrance channel to the Port of Cotonou has been identified; it provides an opportunity for collaboration with a coastal erosion protection program to be funded by others. ▫ Studies of the demand for financial services and of technological alternatives for the provision of financial services have been completed and form the basis for a competitive grant facility to begin in 2008.
Cape Verde	Compact is for 5 years and $110 million, and intends to: ▫ Help achieve the national development goal of converting the economy from aid dependency to sustainable, private sector-led growth. ▫ Increase rural incomes of the poor by increasing agricultural productivity, integrating internal markets, reducing transportation costs, and developing the private sector through greater private sector investment and financial sector reform.	▫ Construction has begun on the first of five roads and four bridges on the islands of Santiago and Santo Antao. ▫ Compact supports the protection of the environment and citizens’ rights. ▫ MCA has carried out environment-related public awareness sessions, environmental impact assessments, an environmental and social monitoring plan, community-based watershed management plans, and resettlement action plans.
Ghana	Compact is for 5 years and $547 million, and intends to: ▫ Reduce poverty by raising farmer incomes through private sector-led agribusiness development. ▫ Increase the production and productivity of high-value cash and food staple crops in some of Ghana’s poorest regions. ▫ Enhance competitiveness of Ghana’s agricultural products in regional and international markets.	▫ Compact entered into force on February 16, 2007, and MCC made an initial disbursement on March 7, 2007. ▫ MCC has disbursed more than $11 million toward program administration and activities as of September 1, 2007. ▫ The Millennium Development Authority (MiDA), the entity responsible for the compact’s implementation, has signed Implementing Entity Agreements with the Bank of Ghana; the Public Procurement Authority; the Ministry of Food and Agriculture; and the Institute of Statistical, Social, and Economic Research.

Country	Program Description	Implementation Results
Lesotho	Compact is for 5 years and $363 million, and intends to: ▫ Have a positive economic impact on Lesotho's entire population. ▫ Increase water supplies for industrial and domestic use. ▫ Strengthen the country's health care infrastructure. ▫ Remove barriers to foreign and local private sector investment.	▫ Lesotho's compact was signed on July 23, 2007, and has not yet entered into force.[1]
Madagascar	Compact is for 4 years and $110 million, and intends to: ▫ Help the island nation move from subsistence to a market-driven economy, particularly in agricultural production. ▫ Raise incomes in rural areas by enabling better land use, expansion of the financial sector, and increased investment in farms and other rural businesses.	▫ Nineteen local land offices are in operation and have issued approximately 729 land certificates. ▫ All existing land documents in 29 land-administration services—a total of more than 876,000 documents—have been inventoried. ▫ Sites for two of six branches of the National Savings Bank to improve access to finance in rural areas have been identified, and building designs are being completed. ▫ Institutional support fund for microfinance institutions is operational and has received seven proposals for a total of $1 million. ▫ Six Agricultural Business Centers are operational in five zones, with more than 3,950 visitors and 45 field agents providing services to small and medium-sized enterprises. ▫ The agricultural project is providing technical training and small business skills to more than 6,400 farmer beneficiaries in five zones. More than 340 business plans have been developed by newly established cooperatives, associations, and small enterprises. ▫ Land certificate acquisitions have resulted in the mobilization of $485,000 in credit from microfinance institutions to 2,200 MCA-Madagascar clients.

[1] After a compact is signed the compact enters into force and compact implementation begins.

Country	Program Description	Implementation Results
Mali	Compact is for 5 years and $461 million, and intends to: ▫ Increase the productivity of the agriculture sector and regional enterprises. ▫ Serve as a catalyst for sustainable economic growth and poverty reduction through key infrastructure investments that capitalize on two of Mali's major assets, the Bamako-Sénou International Airport and the Niger River for irrigated agriculture.	▫ Fiscal and procurement agents have mobilized; the bank agreement has been executed; the compact has been ratified; and feasibility and design work has begun for major infrastructure, all before entry-into-force on September 17, 2007. ▫ The MCA-Mali unit has been transferred from the Prime Minister's office to the Presidency. This reflects the close integration of the MCC program with the President's 5-year socio-economic development plan. ▫ The recruitment process for nine key MCA-Mali positions is in the contract negotiations phase.
Morocco	Compact is for 5 years and $698 million, and intends to: ▫ Increase productivity and improve employment in high-potential sectors, including investments in fruit tree productivity, small-scale fisheries, and artisan crafts. ▫ Support small business creation and growth through investments in financial services and support.	▫ Compact was signed on August 31, 2007, and has not yet entered into force.
Mozambique	Compact is for 5 years and $507 million, and intends to: ▫ Increase the productive capacity of the population in selected districts with the intended impact of reducing the poverty rate, increasing household income and employment, and reducing chronic malnutrition. ▫ Improve water systems, sanitation, access to markets, land tenure services, and agriculture in the targeted districts.	▫ Compact ratified on August 7, 2007, by the Council of Ministers, which also approved the creation of MCA-Mozambique to manage implementation. ▫ The Ministry of Public Works, Ministry of Agriculture, and Ministry of Finance continue to prepare and plan for the implementation of their respective projects and activities. ▫ The Council of Ministers approved the Water Sector Policy, which is essential to the compact's success.

Country	Program Description	Implementation Results
Eurasia		
Armenia	Compact is for 5 years and $236 million, and intends to: ▫ Increase economic performance in the agricultural sector. ▫ Upgrade 943 kilometers of roads. ▫ Increase the productivity of 250,000 farmer households through improved water supply, higher yields, higher value crops, and a more competitive agricultural sector.	▫ Armenia exercised a groundbreaking approach to evaluating the impact of on-farm water management training that various villages and communities are to receive. ▫ 2,453 participants have been trained in on-farm water management to ultimately increase agricultural production, of which 571—almost 23 percent—are female farmers. ▫ The design phase for initial rural road and irrigation infrastructure is nearing completion, and construction is anticipated to begin by the end of 2007.
Georgia	Compact is for 5 years and $295 million, and intends to: ▫ Help Georgians reduce poverty by renovating key regional infrastructure and improving the development of regional enterprises. ▫ Improve rural transportation, providing agricultural suppliers with the opportunity to connect more easily with consumers, and to increase regional trade. ▫ Enhance productivity in farms, agribusinesses, and other enterprises that will increase jobs and rural income.	▫ The Agribusiness Development Project has awarded grants worth $1.1 million to 34 new or expanding agribusinesses. These grants will support agribusiness development projects by improving technologies and facilitating market access. They will employ about 400 people and do business with 22,000 customers and suppliers. ▫ Phase I repairs on the North-South Gas Pipeline have been completed. These repairs protect the pipeline from corrosion, landslide, and floodwaters. ▫ The Georgia Regional Development Fund made its first investment totaling $1.7 million.
Vanuatu	Compact is for 5 years and $66 million, and intends to: ▫ Improve the country's poor transportation infrastructure. ▫ Support 11 infrastructure projects including roads, wharfs, an airstrip, and warehouses. ▫ Reduce transportation costs and improve the reliability of access to transportation services in order to benefit poor, rural agricultural producers and providers of tourist-related goods and services.	▫ The National Budget contains a substantial increase of $4.5 million for the Public Works Department's budget for road maintenance. The funds are being used for community maintenance contracts and small civil works. ▫ The invitation to bid on the design and construction of the compact's transport infrastructure projects has been issued and construction should commence in the first quarter of 2008.

Country	Program Description	Implementation Results
Latin America		
El Salvador	Compact is for 5 years and $461 million, and intends to: ▫ Improve the lives of Salvadorans through strategic investments in education, public services, agricultural production, rural business development, and transportation infrastructure. ▫ Physically unify El Salvador's Northern Zone with the rest of the country, thereby enabling new economic opportunities for rural households, and decreasing transportation costs and travel times to markets for more than 850,000 beneficiaries.	▫ FOMILENIO, the entity implementing the compact, has become fully staffed and is operating at full capacity. ▫ The Board of Directors has been confirmed and met nearly a dozen times. ▫ Program implementation plans are well advanced, including key feasibility studies and environmental/social impact studies, which will speed program execution. ▫ FOMILENIO signed banking agreements to manage program funds, signed a $2.5 million service contract to support the productive development program, and published a number of requests for proposals for program activities.
Honduras	Compact is for 5 years and $215 million, and intends to: ▫ Reduce poverty by (a) increasing the productivity and business skills of farmers and their employees who operate small and medium-sized farms and (b) reducing transportation costs between targeted production centers and national, regional, and global markets.	▫ More than 800 program farmers are receiving technical assistance for crop production and product commercialization. A total of 8,225 are on track to be trained by the end of the program. ▫ A total of 325 program farmers have developed business plans following their participation in a business-planning workshop. ▫ More than 1,200 kilometers of rural roads have been traveled in the process of evaluating their overall condition, location, and compliance with defined qualifying criteria in addition to collecting information required to estimate the economic rate of return. ▫ 18 proposals for funding under the Agriculture Public Goods Grant Facility were received and are in the process of being evaluated. ▫ MCA-Honduras contracted with a local firm to develop and implement resettlement action plans for those people affected by road improvements. Firm has completed surveys for approximately 850 people and will begin the process of clearing the right of way and acquiring land in October 2007. ▫ Designs for the northern half of the CA-5 Highway improvement have been finalized and the selection of construction firms has begun. Construction is expected to begin in March 2008.

Country	Program Description	Implementation Results
Nicaragua	Compact is for 5 years and $175 million, and intends to: ▫ Support those living in the Leon and Chinandega region by significantly increasing incomes of rural farmers and entrepreneurs. ▫ Reduce transportation costs, improve access to markets, strengthen property rights, increase investment, and raise incomes for farms and rural businesses.	▫ Early titling efforts are underway, and 26 beneficiaries have received titles and 500 more beneficiaries are in the process of receiving titles out of 43,000 to be delivered. ▫ Approximately 1,070 bean, cassava, and sesame producers have received technical assistance to market their products. ▫ 374 rural and urban small and medium-sized enterprises benefited from business development services. ▫ Some 476 business plans for forestry producers are being implemented. ▫ In total, 4,568 men and women have benefited from the rural business development project. ▫ 425 new jobs have been created through new businesses attracted through investment promotion activities. ▫ MCA-Nicaragua is cooperating with local communities on two management plans for environmentally sensitive areas. ▫ MCA-Nicaragua has assisted local municipal governments in elaborating environmental policies and regulation through technical assistance. ▫ MCA-Nicaragua has developed and implemented a gender policy that secures equal access for women to the program's benefits. ▫ MCA-Nicaragua has developed technical capacity that has resulted in signing 299 contracts worth $21.7 million through an open and transparent procurement process.

MCC PERFORMANCE RESULTS FOR FY 2007

How MCC Measures Performance

In November 2005, the MCC Board approved MCC's Strategic Plan covering FY 2006 to FY 2011. The Strategic Plan has four goals:

1. Achieve sustainable, transformative development.
2. Support development of a sound policy environment for economic growth and poverty reduction in the developing world.
3. Advance international development assistance practice by continually improving MCC's operational effectiveness.
4. Build MCC's capabilities to achieve its primary strategic goals.

Each strategic goal has specific performance objectives that are laid out in MCC's FY 2007 Annual Performance Plan. In setting performance targets, MCC considers three issues: (1) which indicators should include targets, (2) how numerical values should be set, and (3) how frequently performance against targets should be assessed. It is MCC's policy that the performance indicators selected for targeting are important, measurable, and to the extent possible subject to MCC's control. Compact-specific target values are established according to what would be required to achieve the economic returns or benefits envisaged at the time the project was presented for approval by the MCC Board of Directors. Therefore, the target values are closely linked to the original justification of the projects.

MCC has also identified a number of goals that, although not directly attributable to MCC interventions, do provide important information on the progress of partner countries that are relevant to MCC's programs. MCC considers these to be "supplemental indicators." These indicators are tracked by MCC but not treated as formal indicators.

Most of the performance data reported in the PAR comes from external sources, including other donor agencies, or from independent evaluations contracted for by the candidate countries during the compact implementation process. Where data is not available for select indicators, MCC often conducts surveys by an independent third party to assess its performance. For performance results that are based on data that MCC collects from MCAs, MCC takes steps to ensure that information is accurate.

A summary of MCC's performance in FY 2007 toward achieving these strategic goals is presented in the tables below. As shown, MCC has met five out of seven performance objectives for which data is currently available, excluding supplemental indicators. The following section includes a summary of results, a discussion of the strategies and resources MCC used to achieve performance goals, and steps MCC has taken to ensure the reliability of performance data. For detailed information on indicators, targets, and current and historical performance results, please see Section 2.

Strategic Goal #1: Achieve Sustainable, Transformative Development		
Performance Objective	**Indicator**	**Target Rating**
Generate economic growth and reduce poverty in compact regions	Compact-specific economic growth and poverty reduction	Data available at the end of each compact (first results will be in 2009)
Achieve sustainable projects in compact countries	Sustainability	NA[2]
Countries improve their capacity to meet basic human needs	United Nations (UN) Human Development Index (HDI)	Supplemental indicator
Improve GDP growth	GDP per capita growth rate	Supplemental indicator
Decrease the percentage of the population living on less than $1 or $2 per day	Percentage of population living below $1 and $2 per day	Supplemental indicator
Compact-eligible and threshold countries receive higher average country credit rating	Institutional investor country credit rating	Supplemental indicator
Improve annual percentage of compact targets met on time	Compact-specific annual performance targets	Final data available in December 2007
Increase the Conditions Precedent[3] met on time	Compact-specific Conditions Precedent	Target met

Strategic Goal #1 Results

The first strategic goal encompasses MCC's core mission. MCC has one objective that is not a supplemental indicator and for which data is currently available, increase conditions precedents met on time. As shown above, MCC has met that performance objective. Successful performance on this goal demonstrates that compact countries are taking necessary actions to ensure proper implementation of their compacts. Additional results will be reported as data becomes available.

Strategic Goal #1 Strategies and Resources

The key change in MCC's approach for FY 2007 was an increased focus on compact implementation. Specific efforts for increasing efficiency in compact development and implementation included:

[2] This indicator is still in the process of being defined and therefore baseline and performance result data is not available to report. This is consistent with MCC's description of this objective in the FY 2007 Annual Performance Plan.

[3] Conditions Precedent are actions that a compact country needs to take before MCC will release a disbursement of funds.

- Restructuring several parts of the organization to streamline the proposal evaluation and compact development process
- Working with the Federal Executive Institute to improve the efficacy and productivity of teams working on compacts
- Providing clear guidance to countries immediately after their eligibility selection to enable them to move swiftly toward the development of their compact proposals
- Offering "MCC University" to representatives from newly selected and currently compact-eligible countries to address questions about how to develop and implement a successful compact proposal
- Reducing the time between compact signing, entry into force, and first disbursement through "bridge" funding (609(g)) that allowed partner countries to begin working on implementation requirements
- Putting into place fiscal and procurement agents earlier in the process to reduce delays in initial compact disbursement
- Shifting responsibility, decision-making, and authority for implementation from MCC headquarters to resident country directors in compact countries
- Installing a common payment system designed to create efficiencies and minimize idle cash balances in countries entering implementation

Strategic Goal #2 (a): Support Development of a Sound Policy Environment for Economic Growth and Poverty Reduction in the Developing World	
Performance Objective	**Supplemental Indicator**
Improve policy performance in ruling justly	Political Rights
	Civil Liberties
	Control of Corruption
	Government Effectiveness
	Rule of Law
	Voice and Accountability
Improve policy performance in investing in people	Health Expenditure
	Immunization Rates
	Girls' Primary Education Completion Rate
Improve policy performance in economic freedom	Fiscal Policy
	Cost of Starting a Business
	Time of Starting a Business
	Regulatory Quality

Strategic Goal #2 (b): Threshold Program			
Summary Results			
Total Indicators		**Performance Summary**	
Number of Objectives	88	Number of Targets Met	42
Number of Indicators	88	Number of Targets Not Met	12
		Number with Data Lags	34

Strategic Goal #2 Results

While the performance objectives for Strategic Goal #2 are considered supplemental and do not have formal targets or a performance rating, MCC expects the performance on these indicators to improve more significantly for threshold and compact eligible countries than for the remaining candidate countries.

Results for the Threshold program, which supports Strategic Goal #2, are detailed in the Performance Section of the PAR. Each country established a separate set of performance objectives based on its program. The Threshold program met 42 out of 54 performance targets for which data was available.

Strategic Goal #2 Strategies and Resources

MCC facilitated policy reform by two primary means: the “MCC effect” and the Threshold program. The “MCC effect” uses the possibility of large-scale assistance to encourage countries to adopt the reforms needed to become eligible for an MCC compact. The Threshold program assists countries in becoming eligible for compact assistance by improving their performance in the three policy areas. Countries are selected by the MCC Board to participate in the Threshold program based on their demonstrated commitment to improving policy performance on MCA selection criteria areas.

In FY 2007, MCC signed seven Threshold agreements, with Jordan, Indonesia, Ukraine, Moldova, Kenya, Uganda, and Guyana. Beginning with Threshold programs approved in FY 2007, MCC has incorporated more vigorous monitoring and evaluation activities and all FY 2007 programs include independent program evaluations. Whether country specific, activity specific, or multi-faceted, these evaluations will provide MCC—and the development community more generally—lessons learned and information on the impact of Threshold program activities.

Threshold Program/USAID Results for FY 2007

MCC’s Threshold program supports Strategic Goal #2, Support Development of a Sound Policy Environment for Economic Growth and Poverty Reduction in the Developing World. USAID administers all of the existing Threshold programs on behalf of MCC, providing the benefit of USAID’s technical expertise, development experience, field presence, and administrative infrastructure.

MCC's approach to the Threshold program necessarily varies from that used with compacts. Activities include technical assistance, strategic planning, legislative development, and control of corruption. MCC's strategy is to:

- **Use a short timeframe.** Unlike many other policy reform programs, the Threshold program lasts only for a short timeframe (generally 2 years). This has been shown to be a motivation for the countries to act quickly and smartly, taking advantage of MCC resources to accelerate their reforms.
- **Create a pipeline for compacts.** The Threshold program provides a critical pipeline of countries for MCC's compact program, establishing the countries' relationship with MCC and enhancing MCC's understanding of the specific countries and their challenges. Five threshold countries have already been selected for compact eligibility, giving MCC and the countries an opportunity to work in partnership on policy reforms and establishing an institutional relationship prior to engaging on much larger compact programs.

As a result of the Threshold program's focus, it has a separate set of performance measures in addition to the objectives set under Strategic Goal #2 in MCC's FY 2007–2008 Performance Plan. Each country has a different set of objectives based on its particular program. Details of these performance goals and results can be found in Section 2 of this report.

Strategic Goal #3: Advance International Development Assistance Practice by Continually Improving MCC's Operational Effectiveness		
Performance Objective	**Indicator**	**Target Rating**
Enhance MCA Model recognition and support within the International Development Community	Leadership in Development Practice	Baseline to be set in 2008
Enhance MCC Country Partnership	Assessment of MCC Country Partnership	Data available in December 2007

Strategic Goal #3 Results

Results for performance objectives under Strategic Goal #3 will be reported as data becomes available. Baseline data for the Assessment of MCC Country Partnership measure will be based on a survey conducted during FY 2007. Results of this survey will be available in early December 2007. MCC plans to conduct a survey for the Leadership in Development Practice measure during FY 2008 to establish the baseline for that indicator.

Strategic Goal #3 Strategies and Resources

MCC's outreach efforts garnered constructive feedback and support from domestic and international constituencies for MCC's approach and support for adequate resources for MCC to achieve its goals.

- MCC continuously refines its operating model: Beginning in FY 2007, MCC set out to complete larger, more transformative compacts. MCC has been successful in this effort.
- MCC communicates its lessons learned: MCC employs a variety of tools and techniques in our outreach activities, including public speaking engagements, outreach events, the MCC website, and working relationships in donor and recipient countries. MCC also collaborates with other development practitioners to share lessons learned and to determine which practices are most effective. MCC maintains transparency in its operations and disseminates information on its practices and operations in order to facilitate feedback that will strengthen its model.

Strategic Goal #4: Build MCC's Capabilities to Achieve Its Primary Strategic Goals		
Performance Objective	**Indicator**	**Target Rating**
Minimize the administrative cost of developing and implementing MCC compacts compared to the total value of compacts	Efficiency and Resource Productivity Measure 1	Target met
	Efficiency and Resource Productivity Measure 2	Below target
Address and close Inspector General recommendations within agreed-upon timeframes	Compliance	Below target
Achieve high level of staff effectiveness and satisfaction	Staffing Survey	Baseline set in 2007

Strategic Goal #4 Results

The indicators under Strategic Goal #4 help MCC measure its efficiency and effectiveness. Efficiency is defined as the ratio of an effective outcome or output to the total input resources; effectiveness is having an intended or expected effect and can be combined with cost information to show cost-effectiveness. MCC has two indicators that measure efficiency—one expresses efficiency as a function of compact funds committed and the other as a function of compact funds disbursed. MCC met one of the two efficiency goals during FY 2007.

MCC is committed to making the most effective and efficient use of its resources to achieve its primary goal of poverty reduction through economic growth. Now that MCC has moved out of its start-up phase and its programs on the ground are beginning to achieve results, MCC's efficiency will improve as additional compact funds are disbursed.

Strategic Goal #4 Strategies and Resources

In FY 2007, MCC undertook a multi-pronged approach to improve its capacity to implement its key programs while simultaneously improving the internal control environment so that MCC fully complies with federal rules and regulations. Highlights of MCC's FY 2007 efforts include:

- **Development of a highly effective and diverse workforce.** Three hundred direct hire employees can support a program of the size and complexity of MCC only if they have the highest qualifications and skills, and MCC continues its efforts to recruit a highly qualified and diverse workforce while developing a new and comprehensive training program.
- **Pay for performance.** MCC fully implemented its delegated personnel authority in March 2007. It continues to implement its pay-for-performance system.
- **Competitive sourcing of integrated support services.** MCC took maximum advantage of the President's initiative to competitively source administrative support services.
- **Compliance with federal requirements.** MCC is committed to full compliance with all U.S. Government requirements and has continued efforts to achieve unqualified audits and meet other key financial management and internal control requirements, such as those contained in OMB Circular A-123, Management's Responsibility for Internal Control.

Plans to Improve Performance

Under the Threshold program, which supports Strategic Goal #2, 42 of 54 performance targets for which data was available were met. In FY 2007, MCC instituted a new performance measurement and monitoring method with USAID for the implementation of the Threshold program. This effort is still relatively new, and MCC is continuing to work with USAID to standardize performance objectives, monitoring, and reporting. MCC expects that the improved goal setting process and monitoring of progress will be reflected in improved performance in future years.

MCC performed below target in one of the two efficiency indicators under Strategic Goal #4. MCC is committed to minimizing administrative costs, and its first objective under Strategic Goal #4 is to minimize the administrative cost of developing and implementing MCC compacts compared to the total value of compacts. The second efficiency measure, which compares administrative costs to funds distributed to MCAs, reflects a slower rate of disbursements than originally planned. MCC has a fiduciary responsibility to American taxpayers to make disbursements only when partner countries are ready to use the investments to deliver results in the lives of the poor, but MCC is addressing the need for faster disbursements by shifting MCC's focus to compact implementation. The strategies noted under Strategic Goal #1 are expected to help MCC increase disbursements and, as a result, improve performance on the second efficiency objective in coming years. In addition, MCC produced significant guidance documents in several areas, such as interim financial accountability plans, best practices in resettlement, codification of monitoring and impact evaluation practices, and multiple procurement topics, that will help prepare MCAs to receive disbursements.

In FY 2007, MCC started to apply management cost accounting principles to its country-specific compacts and Threshold programs on a pilot basis. It will be implemented comprehensively in FY 2008. This will allow MCC to report on a consistent and objective basis on the efficiency and effectiveness of its programs. The cost accounting initiative will enable MCC in FY 2008 to link the strategic goals and performance objectives to specific cost categories and thereby measure the efficiency and effectiveness of programs.

Another indicator under Goal 4 for which MCC performed below target was the compliance indicator for MCC's objective to address and close USAID Office of Inspector General (OIG) recommendations within agreed-upon timeframes. MCC has already taken action to ensure performance on the compliance indicator. MCC completed several OIG recommendations on time but failed to formally notify the OIG, resulting in recommendations remaining open. Had MCC provided the formal notification, the recommendations would have closed before their due dates and MCC would have achieved its performance target of 75 percent. MCC has dedicated a resource to track OIG recommendations and due dates.

Use of Non-Parties

MCC's FY 2007 PAR has been developed by the Department of Administration and Finance (A&F) with MCC-wide input and the coordination assistance of a consulting company.

FINANCIAL PERFORMANCE AND ANALYSIS

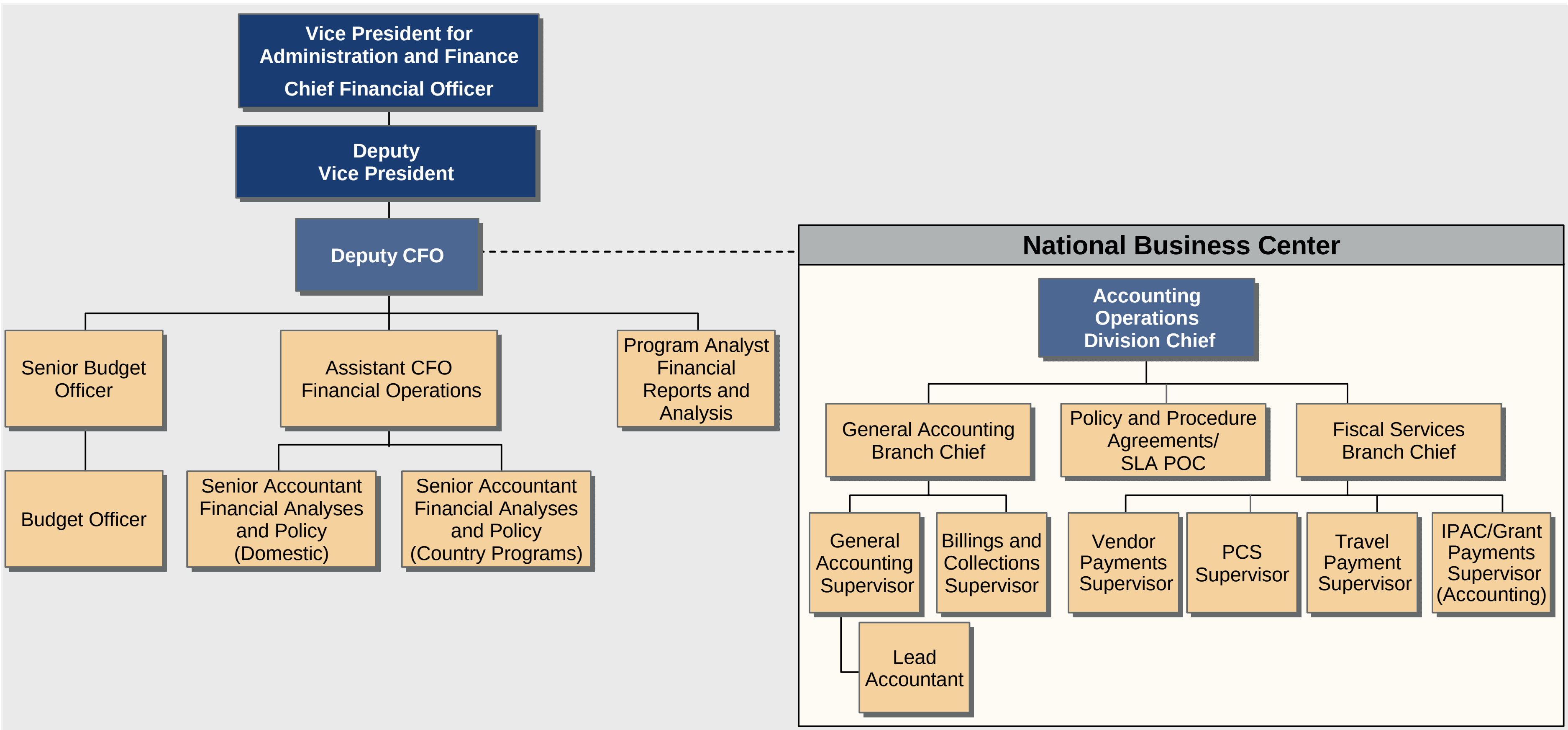
MCC's financial management operations are managed and controlled by the Division of Finance, within A&F and under the leadership of MCC's Vice President of Administration and Finance. The Division is responsible for implementing financial management policies, controls, and systems and for providing comprehensive financial management for MCC. In addition, the Division is responsible for managing MCC's internal control implementation and assessment efforts. At the beginning of FY 2007, the Division included eight full-time equivalents (FTEs) and was composed of three functional teams: (1) Accounting and Financial Operations, (2) Budget Formulation and Execution, and (3) Travel Management and Logistics. In FY 2007, the Travel Management and Logistics branch was moved to the Division of Administrative Services, within A&F, and a new branch, Financial Reports and Analysis, was created. The new Financial Reports and Analysis branch was created to respond to increased requests for financial reporting by external constituencies including OMB, the Congress, auditors, think-tanks, and other constituencies, as well as to create reports for internal management purposes to inform business decisions, improve corporate performance, and optimize and streamline resource allocation. In keeping with MCC's results-focused operational model, this branch and function will play a central role in MCC's future efforts to focus on compact implementation oversight.

The majority of MCC's financial management services and all its financial management systems, including the core financial system and program feeder systems, are provided by the Department of Interior's National Business Center (NBC), one of the Federal Government's financial management "Centers of Excellence" under OMB's financial management line of business. Exhibit 1-7 illustrates the Division of Finance and NBC's organizational structure.

In FY 2007, the Division of Finance completed its staffing plan, and it has the resources in place to ensure sound financial management for core operations as well as the ability to focus on strategic initiatives to improve MCC's financial operations. The Division of Finance undertook several initiatives to enhance financial management and internal controls during the year that will yield long-term benefits for MCC including the following:

- Undertook a focused effort, with the assistance of a reputable international professional services firm, to develop and implement a comprehensive financial management policies and procedures manual for the use and guidance of all MCC employees. The inaugural edition of the manual was completed in March 2007 and revised in August 2007.
- Continued to improve compliance with OMB Circular A-123 by (1) developing and adopting a methodology for selecting and testing internal controls in MCA countries and (2) conducting a comprehensive review of NBC internal control documentation and agreeing to participate in NBC conducted internal controls testing on MCC transactions in the forthcoming fiscal year.
- Completed its first Program Assessment Rating Tool (PART) assessment. PART is used by the OMB to analyze the effectiveness and efficiencies of agencies across government. MCC was rated "Adequate," having just begun showing concrete results and improved efficiencies and comparing favorably to other programs with similar purposes and goals.
- Improved control of cash balances residing in off-shore permitted bank accounts by minimizing exposure risk through the successful development of a pilot payment initiative referred to as the Common Payment System (CPS). The CPS leverages two existing U.S. Department of the Treasury payment systems—the International Treasury Service and the Secure Payment System—to facilitate foreign and domestic payments on behalf of the accountable entities in our partner countries. In addition to limiting exposure risk, the CPS allows for the simplification of local bank agreements and enhances management reporting. MCC will begin implementation of the CPS in new MCC compact countries and will develop a timeline for implementation in existing compact countries.

Exhibit 1-7: Division of Finance and National Business Center



- Developed managerial cost accounting functional requirements to be used in implementing a system acquisition strategy focused on acquiring an integrated system capable of generating budget, performance, and other data-driven management information tools for management decision-making. The initiative also led to the development of MCC's cost accounting methodology for (1) accumulating and reporting cost information, (2) establishing responsibility segments to match costs with outputs, (3) determining the full costs of good and services, (4) recognizing inter-entity costs, and (5) using appropriate costing methodologies to accumulate and assign costs to outputs.

During FY 2007, MCC's financial operations continued to intensify with the signing of five compacts with eligible countries.[4] MCC's cumulative level of compact commitments increased significantly during the year and will continue to trend upward as MCC formally enters into additional compacts with eligible countries in future years. The following sections present the overall perspectives and highlights of MCC's financial performance through the end of FY 2007.

Financial Statements Highlights

For FY 2007, MCC received an unqualified ("clean") opinion from its independent auditors on its annual financial statements. While the MCC's auditors rendered an unqualified opinion on the financial statements, they also reported two material weaknesses and two material non-compliance findings necessitating resolution (see the auditor's report at the end of this document). While MCC is not a CFO Act agency, MCC adheres to the requirements and principles imposed upon such agencies by the CFO Act, the Government Management Reform Act of 1994, and other pertinent laws and regulations. As such, MCC prepares annual financial statements for audit and presentation to OMB and other stakeholders. MCC's comparative financial statements present MCC's financial position and its changes during the reporting period, its cost of operations, and its budgetary resources and their status for the fiscal years ending September 30, 2007 and September 30, 2006.

Balance Sheets

The balance sheets present amounts of future economic benefits owned or managed by MCC (assets), amounts owed by MCC (liabilities), and amounts that constitute the difference (net position).

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4 MCC entered into compacts with the following countries during FY 2007: Mali, El Salvador, Mozambique, Lesotho, and Morocco.

Assets and Unexpended Appropriations

As of September 30, 2007, MCC reported total assets of almost $5.6 billion, an increase of $1.5 billion from September 30, 2007. This increase is primarily the result of funds appropriated by Congress that had not been expended as of the end of the year. At fiscal year-end, MCC held $5.5 billion in unexpended appropriations, $0.7 billion of which represent the balance of unobligated funds not available.

MCC's Fund Balance with Treasury constitutes the vast majority (99.3 percent) of total assets. Because MCC neither owns any of its facilities or other real property nor has any capital leases for office space or its information technology (IT) equipment, MCC has very few capital assets in relation to total assets. The increased capitalization thresholds are $200,000 for IT equipment and $50,000 for other fixed assets. As of September 30, 2007, MCC reported fixed assets of $7.1 million, composed solely of leasehold improvements. The leasehold improvements are for enhancements made to leased office space.

Liabilities and Net Position

As of September 30, 2007, MCC had approximately $44.6 million in liabilities, which were amounts owed to its vendors, contractors, trading partners, and employees. MCC's ratio of assets to liabilities as of September 30, 2007, was 124 to 1.

MCC's overall net position as of September 30, 2007, was $5.54 billion. During FY 2007, MCC's net position increased by $1.46 billion, or 26 percent from September 30, 2006. During this period, MCC received $1.752 billion in appropriated funds and expended approximately $279 million. The available appropriations that are reflected in MCC's positive net position represent the resources necessary to fund future compacts and are indicative of a lag between appropriation, commitment, and expenditure of compact funds. As of the end of FY 2007, MCC signed compacts with 14 countries and was working with 11 other countries to complete compacts.

Statements of Net Cost

The Statements of Net Cost (SNC) are designed to show separately the components of the net cost of MCC's operations for the period.

Program Costs

During FY 2007, MCC incurred $287.6 million in net program costs. As of the end of FY 2007, MCC had cumulatively disbursed $32 million in advances to MCA-accountable entities and other Federal Government agencies.

Statements of Changes in Net Position

The Statements of Changes in Net Position (SCNP) report the change in net position during the reporting period. Net position is affected by changes to its two components: Cumulative Results of Operations and Unexpended Appropriations. Cumulative Results of Operations amounted to $4.7 million as of September 30, 2006, and $7.4 million as of September 30, 2007. This balance is the cumulative difference, for all previous fiscal years through 2007, between funds available to MCC from all financing sources and the net costs of MCC.

Statements of Budgetary Resources

The Statements of Budgetary Resources (SBR) and related disclosures provide information about how budgetary resources were made available and their status at the end of the period. The Resources section of the statements present the total budgetary resources available to MCC. The Status of Resources section of the statements displays information about the status of budgetary resources at the end of the period. The total amount displayed for the status of budgetary resources equals the total budgetary resources available to MCC as of the reporting date. For FY 2007, MCC had total budgetary resources of $4.4 billion, including $3.8 billion carried forward at the beginning of FY 2007 from prior years. MCC incurred obligations of $2.2 billion for the year, an almost 100 percent increase from the $1.1 billion of obligations incurred during 2006.

The following section provides additional details pertaining to MCC's use of the funds appropriated to it by Congress.

Status and Use of Funds

MCC's programs and activities are funded by Congress through annual no-year appropriations. Since its establishment, MCC has received total funding of almost $6 billion, including $1.752 billion in FY 2007 (see Exhibit 1-8).

Exhibit 1-8: Annual Funding by Fiscal Year (in thousands)

Fiscal Year	Annual Funding (in thousands)
2004	$ 994,000
2005	1,488,100
2006	1,752,300
2007	1,752,300
Total	**$5,986,700**

As of September 30, 2007, $1.5 billion of MCC's realized resources represented the balance of apportioned funds available for obligation. While MCC receives no-year funding, OMB apportions, per congressional limits, the amount of funds that MCC may obligate for administrative purposes. Administrative costs include personnel salaries and benefits, leases, rentals, travel, and other miscellaneous expenses. For FY 2007, OMB apportioned $86.2 million for MCC to use for administrative purposes. OMB authorized MCC to use $11.2 million from FY 2005 and FY 2006 appropriations. During FY 2007, MCC obligated approximately $81 million in administrative funds, or 94 percent of the total amount apportioned by OMB.

As noted in Exhibit 1-9, administrative funds represent a small proportion of the total funds provided by Congress, while in FY 2007 about 96 percent of MCC's obligations were for program operations. Should MCC not obligate the total amount of administrative funds apportioned by OMB during the budget year, the excess (unobligated) amount is no longer available for administrative purposes but "rolls over" and is subsequently available for program purposes.

Exhibit 1-9: Obligations by Fund Category (in thousands)

Funds Category	FY 2007 Obligations (in thousands)	Lifetime Obligations (in thousands)
Administrative	$ 81,448	$ 197,099
Compacts (including CIF/Grants)	1,850,021	3,055,331
609(g)	14,544	49,160
Due Diligence	43,321	84,765
Threshold	182,160	234,953
Audit	2,549	7,026
Total	**$ 2,174,045**	**$ 3,628,334**

MCC classifies appropriations in six fund categories:

- **Administrative.** Funds appropriated by Congress and apportioned by OMB for the purpose of operating expenses.
- **Compact.** Funds approved by Congress, apportioned by OMB, and obligated by MCC to cover compacts between MCC and partner countries.
  - **Compact Implementation Fund (CIF).** Funds approved by Congress and apportioned by OMB. CIF funds represent a portion of the funds agreed to in a compact and are made available at the time of compact signing for the purposes of speeding implementation between compact signing and entry into force. MCC uses authority provided in Section 609(g) of its authorizing legislation to provide these funds to a partner country.[5]
  - **Grants.** Funds apportioned by OMB for grants and cooperative agreements.
- **609(g).** Funds approved by Congress and apportioned by OMB to fund contracts or grants for the purpose of facilitating the development and/or implementation of a compact between the MCC and a partner country.

[5] Section 609(g) of the Millennium Challenge Act of 2003 provides that the MCC CEO may 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.

- **Due Diligence.** Funds apportioned by OMB and used by MCC to cover costs associated with assessing compact proposals developed by eligible countries and providing compact implementation oversight.
- **Threshold.** Funds appropriated by Congress, apportioned by OMB, and used by MCC to assist countries in meeting selection criteria for MCA eligibility. (Such countries are considered "on the threshold" of qualifying for eligibility for an MCC compact.)
- **Audit.** Funds appropriated by Congress and apportioned by OMB for audits of MCC operations and programs. (The USAID OIG is responsible for MCC audits.)

During FY 2007, MCC incurred total obligations of approximately $2.2 billion for all program fund categories. Total lifetime obligations incurred by MCC since inception are approximately $3.6 billion. Exhibit 1-9 presents total FY 2007 and lifetime obligations by fund category.

Exhibit 1-10 shows funds obligated for compacts by country as of the end of FY 2007.

In addition to the program obligations in FY 2007, MCC recorded an estimated $1.47 billion in commitments (anticipated obligations) for signed compacts with Morocco ($665 million), Lesotho ($349 million), and Mozambique ($456 million) that had not entered into force during FY 2007.

Exhibit 1-10: Compact Obligations (in thousands)

MCA/ Country	Total Compact Obligations (in thousands)
Armenia	$ 235,650
Benin	307,298
Cape Verde	110,079
Georgia	294,693
Ghana	547,009
Honduras	215,000
Lesotho	15,669
Kenya	100
Morocco	32,400
Madagascar	109,773
Mali	460,684
Mozambique	25,346
Nicaragua	175,000
El Salvador	460,940
Vanuatu	65,690
Total	**$ 3,055,331**

Note: Compact obligations listed are inclusive of CIF and grant funds per Section 609(g) of the Millennium Challenge Act of 2003.

Financial Management Systems, Internal Controls, and Compliance with Laws and Regulations

MCC uses NBC as a financial management shared services provider for financial and payroll systems. MCC is responsible for overseeing NBC and ensuring that financial systems and internal controls are in place to fulfill legislated and regulatory financial management requirements. The following sections present information regarding MCC's financial systems, controls, and compliance with key laws and regulations.

Management Assurances

Federal Financial Management Improvement Act of 1996

The Federal Financial Management Improvement Act (FFMIA) requires federal agencies to implement and maintain financial management systems that are in substantial compliance with (1) federal financial management systems requirements, (2) federal accounting standards, and (3) the United States Standard General Ledger at the transaction level. Because MCC uses NBC for financial management and reporting services, MCC relies upon NBC's evaluations of its financial management systems and its determinations of compliance with FFMIA. NBC issued a letter dated October 1, 2007, stating that its auditor, KPMG, found no weaknesses or significant deficiencies in evaluating NBC's financial systems during the Statement of Auditing Standards No. 70 (SAS 70) review.

Federal Managers' Financial Integrity Act of 1982

The Federal Managers' Financial Integrity Act (FMFIA) of 1982 and the related revised OMB Circular No. A-123 requires agencies to issue an annual statement of assurance to the President and Congress on their internal controls. Internal controls are the organization, policies, and procedures used to reasonably ensure that (1) programs achieve their intended results; (2) resources are used consistent with agency mission; (3) programs and resources are protected from waste, fraud, and mismanagement; (4) laws and regulations are followed; and (5) reliable and timely information is obtained, maintained, reported, and used for decision-making. MCC's management is responsible for ensuring that proper internal controls over financial reporting and systems are in place and are functioning effectively.

In FY 2007, MCC assessed MCC's internal controls to verify that MCC could provide a reasonable assurance that internal controls are in compliance with objectives established by OMB Circular A-123 and FMFIA. The components involved in the assessment and development of MCC's internal control review include:

- Scope and Materiality Report
- Entity Level Control Report
- A review of transaction-related controls at MCC's service provider, NBC
- Report on Internal Controls

These components constitute a comprehensive internal control review. Overall, the assessment found that MCC made significant progress on improving internal controls. Specifically, MCC has considerably strengthened its internal controls environment across the organization, in particular within A&F, by developing formal financial management policies and procedures. Moreover, the assessment found that MCC is currently working to establish a greater degree of oversight over its entity level controls. These activities include resolving information technology (IT) system issues, developing a plan to meet Federal Information Security Management Act (FISMA) compliance requirements, establishing an MCC-wide employee training program, and decentralizing budgets to MCC departments.

Internal Controls over Financial Reporting

In December 2004, OMB revised Circular A-123 to improve federal managers' accountability and the effectiveness of federal programs by establishing, assessing, correcting, and reporting on internal control. Circular A-123, Appendix A, provides requirements and a methodology for agency management to assess, document, and report on internal control over financial reporting. The revised circular was effective for FY 2006 (and thereafter).

MCC's FY 2007 A-123 assessment documented MCC's business processes and key controls for the following 11 key business processes:

- Contracts and Grants Management
- Compact Management
- Travel Management
- Funds Management
- Financial Reporting
- Budget
- Human Capital Management
- Information and Technology
- Personnel, Salary, and Benefits
- Interagency Agreements
- Property, Plant, and Equipment

The assessment confirmed that MCC had made significant progress in addressing internal control weaknesses during FY 2007. In accordance with recommendations from the Audit of the Millennium Challenge Corporation's Financial Statements, Internal Controls, and Compliance for the Period Ending September 30, 2006 and 2005, MCC developed and implemented a Financial Management Policies and Procedures Manual. MCC also made significant progress in developing asset records by taking an initial inventory and approving an asset management policy. The Division of Finance increased its involvement in reviewing financial reports from MCA and has ensured that disbursements are made monthly rather than quarterly.

According to the Implementation Guide for OMB Circular A-123, agencies should confirm that their financial service providers implement adequate internal controls and can determine whether additional testing at the service provider is necessary. As part of conducting its FY 2007 OMB A-123 review, MCC, in collaboration with a contractor, traveled to NBC's Accounting Operations Branch in Lakewood, Colorado. While at NBC, the contractor reviewed the business process documentation and key control test results for the processes NBC performs on behalf of MCC.

In July 2007, NBC issued its SAS 70 reports for the Federal Personnel and Payroll System and the Oracle Federal Financial System and its assurance letter. The two reports and the assurance letter did not disclose any findings for the period of June 16, 2006 through June 15, 2007. The letter states that the results of the testing conducted between October 1, 2006 and May 31, 2007 indicated that no material weaknesses or significant deficiencies were uncovered and that processes and controls in place during that time period were adequate and effective to safeguard data from waste, fraud, abuse, and destruction. NBC sent an update to this letter in October 2007 for the remaining period, June 15, 2007 to September 30, 2007. NBC reported that controls had not changed during that period and the assessment in the previous letter still applies.

Controls over financial reporting for the MCA countries (countries for which formal compacts between MCC and the countries had been signed during FY 2006 and which had entered into force) were not included in the assessment because all the countries were in the early stages of compact implementation. However, MCC, with contractor assistance, reviewed all current compact countries for available policies, audit documentation, and relevant agreements. The review also explored the approach to overseas A-123 internal controls testing of key business processes, including determining how to decide which countries to assess in the future.

On the basis of MCC's assessment of its internal controls, NBC's assurance statements, and other relevant information (such as the Government Accountability Office [GAO] and OIG audit reports), the CEO concluded with reasonable assurance that MCC's internal controls are in compliance with the provisions of FMFIA, Section 2, and that MCC is in compliance with the internal control objectives stipulated by OMB in Circular A-123.

Compliance with Laws and Regulations

In addition to complying with FMFIA and OMB Circular A-123 requirements, MCC's management is also responsible for ensuring MCC's compliance with other relevant financial management laws and regulations. Principal among these are:

- Prompt Payment Act
- Debt Collection Improvement Act of 1996 (DCIA)
- Improper Payments Information Act of 2002
- Federal Information Security Management Act (FISMA)

Prompt Payment Act

The Prompt Payment Act (Public Law 100-496), as amended, requires federal agencies to pay vendors transacting business with them in a timely manner. With certain exceptions, the Act requires agencies to make payments within 30 days of the later of (1) receipt of properly prepared invoices or (2) the receipt of goods or services. For amounts owed and not paid within the specified payment period, agencies are required to pay interest on the amount owed at a rate established by the Department of the Treasury.

An agency's performance under the Act for any given period is most often measured by the percentage of payments made within the specified timeframes out of all payments subject to the Act's provisions. In FY 2007, MCC's "prompt payment" performance improved to 97.5 percent, a 1.9 percent increase over FY 2006's 95.6 percent. During the year, MCC paid $6,960 in late interest to vendors, a 33 percent decrease from FY 2006's $10,490.

Also, during the year, NBC made 98.9 percent of MCC's vendor payments via electronic transfer, a 2.5 percent increase over FY 2006's 96.4 percent.

Debt Collection Improvement Act of 1996

In 1996, Congress passed the DCIA in response to steady increases in the amount of delinquent debt owed to the Government. Under the Act, all federal agencies must refer past due, legally enforceable, non-tax debts that are more than 180 days delinquent to the Department of the Treasury's Financial Management Service (FMS) for collection through the Treasury Offset Program. A debt is considered delinquent if it is 180 days past due and is legally enforceable. A debt is legally enforceable if there has been a final agency decision that the debt, in the amount stated, is due and there are no legal bars to collection action.

During FY 2007, MCC referred no debts to FMS for collection.

Improper Payments Information Act of 2002

An improper payment is any payment that should not have been made or was made in an incorrect amount. The President has made the development of management controls to detect and prevent improper payments a major focus of his Management Agenda. Congress, following the President's lead, passed the Improper Payments Information Act of 2002 (Public Law 107-300). The Act requires agencies to review annually all programs and activities to identify those that are susceptible to improper payments, estimate the annual improper payments in susceptible programs and activities, and report the result of their improper payment reduction plans and activities. OMB Memorandum 03-13 defines a program as susceptible to improper payments if it has improper payments that exceed 2.5 percent and $10 million of program spending. MCC can report excellent payment performance that was significantly below the OMB ceiling.

Federal Information Security Management Act

The OIG audit of FY 2007 indicates that MCC has made improvements in complying with FISMA. In FY 2006, the OIG recommended that MCC complete the Certification and Accreditation process on MCCnet, provide quarterly FISMA filings to OMB, conduct risk assessments and security audits, document policies and procedures, provide security training for staff, and establish a comprehensive Continuity of Operations Plan (COOP).

To address these recommendations, MCC formed a dedicated FISMA team. During FY 2007, MCC completed one-third of the Certification and Accreditation. MCC also conducted a risk assessment and security awareness training. In addition, MCC brought all servers into compliance with requisite security patches and updates. MCC also introduced and tested a new COOP.

Although MCC is making progress, weaknesses still remain. For example, MCC needs to prepare additional policies and procedures for its information security program; reconsider the low-impact categorization assigned its general support system, MCCnet; and strengthen its process for mitigating security vulnerabilities on its network. In addition, it needs to address two FISMA audit recommendations that pertain to weaknesses in MCC's COOP and the Certification and Accreditation of its general support system.

MCC's system now stores sensitive data and should be categorized as a medium impact system, thus requiring greater protection. Using the guidelines in Federal Information Processing Standard (FIPS) 199, MCC's Information Technology Department and the FISMA Internal Audit Team are taking the necessary steps to secure MCCnet as a moderate impact system.

MCC's internal FISMA team began conducting MCCnet scans in July 2007 and correcting vulnerabilities that were found. MCC's internal FISMA team also will make the corrections to the findings contained in the 2007 OIG audit. The expected completion date for all additional FISMA-related improvements is March 2008.

Summary of Material Weaknesses, Non-Compliance, and Corrective Actions

MCC received two material weakness findings related to internal control over financial reporting and two instances of non-compliance with federal regulations. MCC reviewed and commented on current status and corrective actions for the future. The section below summarizes the audit findings and MCC's corrective action plans.

MCC Did Not Sufficiently Execute Its Monitoring Functions Related to Advances (material weakness)

MCC agreed to work with its financial services provider, the NBC, to ensure all prior and future advances are liquidated on a first in, first out (FIFO) basis and to update the Financial Management Policy and Procedures to affect this change.

MCC implemented the CPS in Mali in May 2007. All countries signing compacts after that date will use CPS. The CPS provides for payment of MCA expenses through the U.S. Treasury based upon presentation of a valid approved invoice. CPS supports sound cash management by eliminating the current practice of cash advances to MCA compact countries. MCC will establish a timeline for converting to CPS countries that entered into compacts prior to May 2007. In the interim, MCC intends to follow sound cash management practices and will disburse funds consistent with the GAO policy and based on the best information available and grant requirements in any given quarter. MCC will continue to release the funds in monthly tranches.

MCC Lacks Written Policies and Procedures Related to Financial Reporting Accountability and Document Control (material weakness)

In conjunction with the reorganization of the Operations Department, MCC will be reviewing existing polices and procedures related to compact implementation. This will include documenting the roles and responsibilities for ensuring receipt of required reports from partner countries.

MCC has submitted a comprehensive Records Disposition (retention) schedule to the National Archives and Records Association for review and approval within the next 6 to 9 months. The issue of version control and a centralized repository is being addressed as part of development of the Enterprise Architecture and the implementation of the Business Intelligence and Data Storage (BIDS). A key component of BIDS will be the Administrative Data Store (ADS). The ADS is a data warehouse that will include MCA compact data; MCA progress reports; and records of MCC reviews, approvals, and decisions captured through an automated workflow process. The expected implementation date for this BIDS component is June 2008. In the interim, MCC will establish procedures to address the version control issue using existing tools.

MCC Does Not Fully Comply With the Federal Financial Management Improvement Act (material non-compliance)

During FY 2007, A&F made substantial progress on reviewing its current financial systems environment and developing alternatives for a fully integrated system to meet FFMIA requirements. A&F established system requirements, performed a gap analysis based on its current environment, and developed cost alternatives to close the existing gaps. A&F also will work with OMB to find the best resolution for this condition, whether with the NBC or some other federal or private center of excellence.

A&F will continue to work with the NBC on the interface between E-travel and Oracle to resolve the issues noted during initial testing phases. Also, MCC will be changing to a new government credit card provider in FY 2008 for travel and purchase card transactions to address the need for an integrated financial management system. MCC is currently considering banks that have a fully tested and integrated interface with the Oracle Federal Financial System (OFFS). Regarding the payroll integration, the NBC has indicated its business plan does not include the integration of payroll with OFFS apart from the labor interface already provided.

MCC Does Not Fully Comply With the Federal Information Security Management Act (material non-compliance)

During FY 2007, MCC management created a new Chief Information Systems Security Officer (CISSO) position, hired two full-time FISMA staff, and completed three milestones in the initial phases of FISMA compliance. Also during the year, MCC approved three additional FISMA team members to review policies and procedures, document controls, and ensure the necessary steps toward full FISMA compliance.

Other Management Information, Initiatives, and Issues

While MCC has received unqualified opinions on its annual financial statements, improvements and refinements are warranted in the financial management operations area to further enhance efficiencies and effectively resolve identified deficiencies. The following are brief summaries of a number of goals, initiatives, and issues that the Division of Finance will address in future fiscal periods:

- **Implementation of Enterprise Architecture.** Contribute financial management, budget, and performance expertise in MCC’s efforts to implement a comprehensive Enterprise Architecture, which will include a fully integrated financial management application, a collaborative environment application (i.e., SharePoint), a business intelligence application and data store, and a management information system.
- **Consistent and comparable performance metrics for compacts.** Further develop MCC’s reporting capacity and routinely disseminate to MCC’s managers viable and pertinent information on funds status to assist in the development of performance metrics to be used for decision-making and monitoring of corporate performance.
- **Improve financial management operations and internal controls.** Continue to devise, enhance, implement, and maintain strong financial management policies, procedures, and internal controls, stressing continuous improvement in all aspects of MCC’s financial management operations. Desired outcomes include improved timeliness, accuracy, and consistency in the financial data and reports provided to internal and external customers.

Limitations of Financial Statements

The principal financial statements have been prepared to report the financial position and results of MCC's operations pursuant to the requirements of 31 U.S.C. 3515(b). While the statements have been prepared from the books and records of MCC in accordance with Generally Accepted Accounting Principles (GAAP) for federal entities and the formats promulgated by OMB and prescribed by the Federal Accounting Standards Advisory Board, the statements are in addition to the financial reports used to monitor and control budgetary resources that are prepared from the same books and records.

The statements should be read with the understanding that they have been prepared for a component of the U.S. Government, a sovereign entity.

2. PERFORMANCE REPORT

In accordance with the Government Performance Results Act of 1993, MCC's Board of Directors approved its Strategic Plan on November 8, 2005, covering FY 2006 to FY 2011. The Strategic Plan defines MCC's mission as follows:

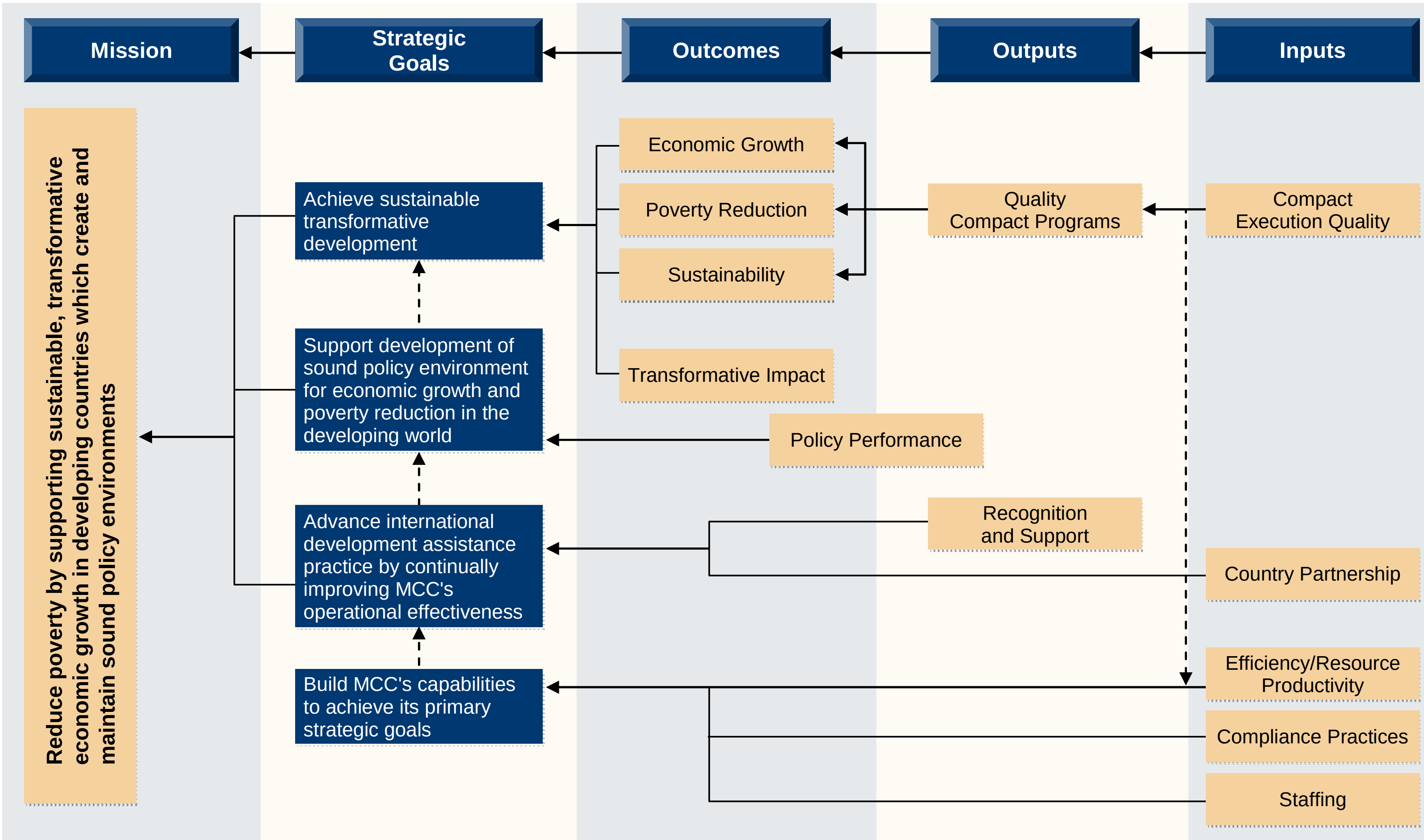
MCC's mission is to reduce poverty by supporting sustainable, transformative economic growth in developing countries which create and maintain sound policy environments.

The Strategic Plan defines four strategic goals for MCC:

- **Strategic Goal #1.** Achieve sustainable, transformative development.
- **Strategic Goal #2.** Support development of a sound policy environment for economic growth and poverty reduction in the developing world.
- **Strategic Goal #3.** Advance international development assistance practice by continually improving MCC's operational effectiveness.
- **Strategic Goal #4.** Build MCC's capabilities to achieve its primary strategic goals.

MCC developed and submitted a FY 2007 Performance Plan to OMB in February 2007. The Performance Plan includes input, output, and outcome measures that tie to the four strategic goals outlined in the 5-year Strategic Plan. Exhibit 2-1 maps the annual performance goals from the FY 2007 MCC Performance Plan to MCC's strategic goals. The following section details MCC's FY 2007 annual performance objectives, methods for verifying data, and approach to setting targets and measuring progress. The remaining portion of the performance section is dedicated to reporting the results for each of MCC's annual performance objectives for 2007, including data from previous years as available.

Exhibit 2-1: MCC's Corporate Performance Plan



PERFORMANCE INDICATOR FRAMEWORK

MCC is designed to support innovative strategies and to ensure accountability with measurable results. MCC integrates monitoring and evaluating into each compact so that progress can be measured against targets agreed to at the start of the program. However, due to the nature of international development work, the difficulty of obtaining current data, and the impact of external factors, performance is not always quantifiable or immediately measurable. Setting baseline data has been difficult due to the lack of current data. Many of MCC's partner countries also have limited capacity to measure outcome or output results. In addition, compacts are normally implemented over a 5-year period, making outcome data available only well into the implementation period.

As a result, MCC did not set targets for all indicators for FY 2007/2008. Please see MCC's policy on performance targets below for details on MCC's approach. In the coming years, MCC will consider further refinements to these measures, including the possibility of measuring criteria relative to trends, addressing the problem of infrequently measured data, and considering alternative data sources. MCC has already incorporated significant enhancements to its corporate performance management by establishing a Performance Management Working Group, bringing together MCC resources across all its departments. The working group met weekly over a period of 5 months to assess and screen the quality of numerous data sources for the corporate performance indicators. The working group only selected data that is SMART (Specific, Measurable, Achievable/Attributable, Realistic/Relevant, and Timely/Trackable). Accordingly, most data comes from reliable external sources, including other donor agencies or independent evaluations contracted for by the candidate countries during the compact implementation process. Where data is not available for select indicators, MCC is developing and conducting surveys by independent third parties to assess its performance.

Data Verification and Validation

MCC has developed improved tools and increased transparency for economic analysis, including joint efforts with newly eligible countries to do a growth constraint analysis as a framework for consultation on program development, enhanced beneficiary analysis, and improved sensitivity analysis of expected returns. For performance results that are based on data that MCC collects, MCC has taken steps to ensure that information from MCA reports is accurate. MCAs are required to submit comprehensive quarterly reports that form the basis for annual performance evaluations on compact-specific indicators. MCC reviews these reports for accuracy to ensure that the final performance results reported in the PAR are accurate.

Beginning with threshold programs approved in FY 2007, MCC has incorporated more vigorous monitoring and evaluation activities, and all FY 2007 programs include independent program evaluations. MCC has devised Results Reporting Tables (RRT) to measure quarterly progress on a series of program indicators. MCC initiated this process and has coordinated efforts closely with USAID, which submits the RRTs along with its quarterly narrative reports. The RRT indicators typically originate either from the Threshold Country Plan or from a list of performance benchmarks that MCC, USAID, and the Threshold country government work together to develop.

MCC Policy on Performance Targets

MCC's policy on setting performance targets addresses three related issues: which indicators should include targets, how numerical values should be set, and how frequently performance against targets should be assessed. It is MCC's policy that the performance indicators selected for targeting be important, measurable, and to the extent possible subject to MCC's control. Compact-specific target values are established according to what would be required to achieve the economic returns or benefits envisaged at the time the project was presented for approval by the MCC Board of Directors. Therefore, the target values are closely linked to the original justification of the projects.

The frequency of performance assessment against output targets is established on a case-by-case basis, dictated by the nature of the program. For example, infrastructure projects that do not start construction for a year do not have targets for the first year. Agricultural projects involving crops that will mature in year three will have targets on yields starting in year three. Assessment against compact-specific outcome targets will not normally take place until later in the life cycle of each compact because their targets assume the completion of most compact activities.

Supplemental Measures

Because MCC's mission is to be transformative, a number of supplemental measures of economic growth, poverty reduction, and policy reform are included in this performance plan. However, these measures do not strictly meet the "A" in the SMART criteria, because they are not directly attributable to MCC interventions. For example, while MCC can point to specific examples where the "MCC effect" has led to policy reform measures, MCC cannot claim credit for country performance on the 13 policy indicator measures in this plan. Similarly, while MCC and partner countries have jointly set targeted economic growth and poverty reduction targets in each MCC compact, MCC will not be solely responsible for nation-wide improvements in per capita income growth, poverty rate reduction, the Human Development Index, or the Institutional Investor credit rating.

At the same time, dropping these indicators altogether would deprive MCC of important information on the overall progress of partner countries that is directly relevant to MCC's programs. Therefore, while MCC will measure trends in these 17 supplemental indicators, it will not set specific targets for these indicators or otherwise treat them as formal outcome indicators.

External Factors Affecting Performance

Various external factors affected MCC's ability to reach its performance goals for FY 2007–2008. These factors, consistent with those identified in MCC's FY 2007 Performance Plan, included:

- **Economic and political environment.** Stable economic and political environments in partner countries are necessary for these countries to pursue MCC programs.
- **Policy reform.** MCC compact, threshold, and candidate[6]countries must undertake significant policy reforms that may face significant domestic opposition. Compact-eligible countries at a minimum must avoid backsliding on key policy issues.
- **Compact-eligible country capacity.** Compact-eligible countries must adequately engage in all aspects of compact development and implementation with sufficient resources and human and political capital. Inadequacies in administrative capability, technical expertise, fiscal and procurement capacity, and other areas can impact a country's performance.
- **Congress.** Congress authorized MCC in 2004, and as an entirely grant-making institution MCC, depends on congressional appropriations to fund its compacts and Threshold programs.
- **Partner U.S. Government agencies.** MCC must maintain the support of agencies that serve on the MCC Board, as well as OMB and the National Security Council, on key policy and operational issues. MCC also depends on assistance from a number of agencies in the implementation of MCC programs.
- **Non-Governmental Organizations.** The support of key U.S. NGOs is essential to MCC because NGOs provide (a) an independent source of information about the countries with which MCC works, and (b) can provide independent evaluation and validation of specific MCC programs.

[6] Candidate countries are those countries that meet per capita income levels set by MCC.

MCC PERFORMANCE IN FY 2007

STRATEGIC GOAL #1

Achieve Sustainable, Transformative Development

The following are the objectives that constitute Strategic Goal #1:

1.1 Generate economic growth and reduce poverty in compact regions
1.2 Achieve sustainability of successful projects in compact countries
1.3 Improve compact countries' capacity to meet basic human needs
1.4 Improve compact countries' GDP growth
1.5 Decrease percentage of population living on less than $1 and $2 per day
1.6 Improve compact-eligible and threshold countries' average country credit ratings
1.7 Improve annual percentage of compact targets met on time
1.8 Increase the number of Conditions Precedents (CPs) met on time

The MCC Strategic Plan defines the expected outcome for this strategic goal to be a significant reduction in poverty through sustainable, material economic growth for a significant number of people. MCC has defined a number of outcome, output, and input measures to assess progress toward this strategic goal. Over the last year, MCC has refined these measures further, including measuring criteria relative to trend, managing the problem of infrequently measured data, and considering alternative data sources. MCC has also added several indicators this year to measure economic growth and poverty reduction effectively at a level tailored more specifically to MCC programs.

Example of Significant Achievement

MCC Helps Malagasy Families Increase Rural Incomes

Ampasimazava is a village situated on the east coast of Madagascar where because of poor soil quality and poor agricultural infrastructure, few options existed for revenue generation. In the past, the principal economic activities of the villagers consisted of collecting firewood and producing charcoal. The average weekly revenue for a charcoal producer was less than $5.

In October 2006, MCA-Madagascar's Agricultural Business Investment Project began working with an association of 18 villagers from Ampasimazava in producing essential oil from niaouli leaves, commonly used in cosmetic and skin care products. MCA-Madagascar assisted the association in developing a business plan, acquiring financing of $3,000 from a local micro-finance institution to set up a distilling plant, and linking the association to buyers in the capital.

As a result of the villagers' dynamism and MCA-Madagascar's assistance, the association and its members have become successful almost overnight.

The association has generated more than $1,000 of profit within the first 2 months of operations from member fees, which the members plan to use to make improvements to the village, including building wells to supply drinking water. They have begun to pay off their loan with the micro-finance institution, and they have begun to create a tree nursery to begin production of eucalyptus essential oil.

Exhibits 2-2 and 2.3 detail MCC's performance against its objectives for Strategic Goal #1. Exhibit 2-2 summarizes the number of objectives MCC met in FY 2007. Exhibit 2-3 details the specific objective, indicator, and performance, including for prior years. Four supplemental indicators are included under Strategic Goal #1 due to the fact that progress in these areas is largely outside of MCC's control.

Exhibit 2-2: Strategic Goal #1 Results Summary

Strategic Goal #1: Achieve Sustainable, Transformative Development			
Summary Results			
Total Indicators		**Performance Summary**	
Number of Objectives	8	Number of Targets Met	1
Number of Indicators	8	Number of Targets Not Met	0
		Number with Data Lags or Not Yet Defined	3
		Supplemental Indicators (no target)	4

Exhibit 2-3: Strategic Goal #1 Detailed Results

Objective 1.1: Generate Economic Growth and Reduce Poverty in Compact Countries			
Outcome Indicator: Compact-Specific Economic Growth and Poverty Reduction			
Compact Country	**Income Indicator (varies by country)**	**Baseline**	
		Year	**Value**[7]
Armenia	Change in real income from agriculture in rural areas (Index)	2005	100%
Benin	Average household income in land and finance areas	2006	Baseline data is not yet available
Cape Verde	Increase in annual income (US$ millions)	2005	$0
El Salvador	Annual per capita income of program beneficiaries in the Northern Zone (treatment group)	2004	$720
	Annual per capita income of program beneficiaries in the Northern Zone (control group)	2004	$720
Georgia	Incremental increase in household incomes from compact interventions	2007	$0
Ghana	Crop income (Northern Zone) (US$ per household)	2006	$700
	Crop income (Afram Basin Zone – East) (US$ per household)	2006	$820
	Crop income (Afram Basin Zone – West) (US$ per household)	2006	$540
	Crop income (Southern Zone) (US$ per household)	2006	$1,860

[7] The baseline value for compact-specific GDP will be in national currency units. The baseline value for the poverty headcount ratio will be in percent.

Objective 1.1: Generate Economic Growth and Reduce Poverty in Compact Countries			
Outcome Indicator: Compact-Specific Economic Growth and Poverty Reduction			
Compact Country	**Income Indicator (varies by country)**	**Baseline**	
		Year	**Value[7]**
Honduras	Increase in income of beneficiaries (annual US$ millions)	2005	$0
Madagascar	Increase in household income in zones	2005	$698
Mali	Total revenue of firms servicing the airport (US$ millions)	2007	$8
	Total receipts of hotels and restaurants in Bamako (US$ millions)	2007	$133
	Gross value-added of firms in the Industrial Park (US$ millions)	2007	$0
	Real income from irrigated agricultural production (US$ per capita)	2007	$0
Nicaragua	Total expected income gains (US$ millions)	2007	Data not yet available
Vanuatu	Average cash income per capita of residents living within the catchment area of infrastructure sub-projects	2005	$1,206
Rating	Data not yet available. Will measure once compact completed.		
Justification	Creating compacts that increase economic growth and reduce poverty is MCC's most important goal. Successful projects in compact countries will produce economic growth and reduce poverty for the populations affected by the compact. Baseline years for this measure vary country by country and are determined by the implementation schedule of the compact. The first round of results for these indicators are not expected until 2009 as was stated in the FY 2007 Annual Performance Plan.		

Objective 1.2: Achieve Sustainable Projects in Compact Countries	
Outcome Indicator: Sustainability	
Comments	
MCC is in the process of defining an indicator to accurately measure the sustainability of projects. MCC intends for this indicator to measure the extent to which the impact of successful programs or compact activities has continued after a compact has been completed and all funding has been disbursed. Baselines, targets, and a reporting framework for this indicator will be completed when a precise indicator is identified.	
Rating	Indicator not yet defined

Objective 1.3: Countries Improve Their Capacity to Meet Basic Human Needs		
Supplemental Indicator: United Nations Human Development Index (HDI)		
Date	**Actual**	**Comments**
2006	0.545 for non-eligible countries; 0.555 for threshold countries; 0.601 for compact countries	Baseline data is from the 2006 Human Development Report, which uses 2004 country data. The baseline covers countries that were compact-eligible or Threshold-eligible candidates in FY 2004 and FY 2005.
2007	Will be provided in November 2007 when the 2007 Human Development Report is released.	The 2007 Human Development Report will use 2005 country data. Data is expected to be available on November 27, 2007.
Rating	Not applicable.	
Justification	The HDI measures a country's achievements in three dimensions of human development—life expectancy at birth; adult literacy rate and the combined primary, secondary, and tertiary gross school enrollment ratio; and GDP per capita. The average HDI score of countries that are eligible for MCC assistance (either compact or threshold) gives a broad indication of their level of development. MCC will monitor the average HDI score of countries eligible for compact or threshold assistance to see whether the level of human development is increasing following MCC selection and delivery of assistance. Relative changes in average HDI schores of the three country groups (candidate, threshold, and eligible) will be monitored.	

Objective 1.4: Improve GDP Growth		
Supplemental Indicator: GDP Per Capita Growth Rate		
Date	**Actual**	**Comments**
2004	Non-eligible countries: 4.277% Threshold countries: 1.99% Compact countries: 3.581%	These are the baseline figures (per capita growth rates in 2004).
2005	Non-eligible countries: 4.165% Threshold countries: 2.183% Compact countries: 3.730%	Non-eligible countries had a decrease of 0.112% in GDP per capita annual growth rate from 2004 to 2005. Threshold countries had an increase of 0.184% in GDP per capita annual growth rate from 2004 to 2005. Compact countries had an increase of 0.149% in GDP per capita annual growth rate from 2004 to 2005.
2006	Non-eligible countries: 4.047% Threshold countries: 3.022% Compact countries: 4.155%	Non-eligible countries had a decrease of 0.229% in GDP per capita annual growth rate from 2004 to 2006. Threshold countries had an increase of 1.023% in GDP per capita annual growth rate from 2004 to 2006. Compact countries had an increase of 0.574% in GDP per capita annual growth rate from 2004 to 2006.
2007	Data available November 2007	MCC is using the International Monetary Fund (IMF) World Economic Outlook (WEO) database instead of the World Bank Development Indicators (WDI) database, which had been used in the prior year. This decision was based on a few key factors. First, the IMF produces its database through biannual exercises of data collection, resulting in the production of timely, accurate national income data twice a year. Conversely, the WDI produces its statistics once a year (April) and does not always have the most recent data to publish. Further, national income data from the WEO database is used in other indicator analysis in this report (e.g., fiscal policy). To ensure data integrity of the entire report, it is best to use the WEO going forward.
Rating	Not applicable.	
Justification	The average GDP growth per capita of countries that are eligible for MCC assistance (either compact or threshold) gives a broad indication of whether their economic performance is improving and creating conditions for sustainable poverty reduction. MCC will monitor year-on-year changes in the average GDP growth per capita of countries eligible for compact or threshold assistance to see how their economies are performing following MCC selection and delivery of assistance.	

Objective 1.5: Decrease Percent Living on Less Than $1 and $2 Per Day			
Supplemental Indicator: Percent of Population Living below $1 and $2 per Day			
Date	**Country**	**$1 per day (actual)**	**$2 per day (actual)**
2007	Armenia	2% (2003)	31.07% (2003)
	Benin	30.9% (2003)	73.74% (2003)
	Bolivia	23.2% (2002)	42.18% (2002)
	Burkina Faso	27.19% (2003)	71.77% (2003)
	Cape Verde	NA	NA
	El Salvador	19.04% (2002)	40.55% (2002)
	Georgia	6.514% (2003)	25.29% (2003)
	Ghana	45.05% (1999)	75.01% (1999)
	Honduras	14.9% (2003)	35.71% (2003)
	Jordan	2% (2003)	6.95% (2003)
	Lesotho	36.4% (1995)	56.03% (1995)
	Madagascar	61.03% (2001)	85.1% (2001)
	Mali	36.13% (2001)	72.07% (2001)
	Moldova	2% (2003)	20.75% (2003)
	Mongolia	10.82% (2002)	44.58% (2002)
	Morocco	2% (1999)	14.33% (1999)
	Mozambique	36.18% (2002)	74.14% (2002)
	Namibia	34.93% (1993)	55.78% (1993)
	Nicaragua	45.12% (2001)	79.93% (2001)
	Senegal	17.01% (2001)	56.17% (2001)
	Sri Lanka	5.55% (2002)	41.59% (2002)
	Tanzania	57.82% (2000)	89.93% (2000)
	Timor-Leste	NA	NA
	Ukraine	2% (2003)	4.94% (2003)
	Vanuatu	NA	NA
Rating	Not applicable.		
Justification	Data reported in 2007 sets the baseline for this indicator. MCC will monitor progress on this indicator on an annual basis. Changes in this indicator are a measure of poverty reduction. Compact-specific indicators outlined in Objective 1.1 are specific to those households directly impacted by MCC projects. This metric provides supplementary data for MCC to assess trends in poverty reduction at a national level. Because MCC programs do not have a national scope, targets will not be set.		

Objective 1.6: Compact Eligible and Threshold Countries Receive Higher Average Country Credit Ratings	
Supplemental Indicator: Institutional Investor Country Credit Rating[8]	
Period (Year)	**Actual–Compact Eligible**
2004 (Baseline)	26.2
2006	28.0
2007	32.1
Period (Year)	**Actual–Threshold**
2004 (Baseline)	23.1
2006	26.7
2007	31.1
Period (Year)	**Actual–Other Candidate**
2004 (Baseline)	22.0
2006	28.3
2007	31.2
Rating	Not applicable.
Justification	This indicator was added in the 2007 Annual Performance Plan because it demonstrates the extent to which a country is making progress in attracting private investment. Moving countries toward "graduation" from donor funding to private sector funding of development is one of the key goals of the MCC model of assistance. It is expected that performance on this indicator will improve more significantly for threshold- and compact-eligible countries than for the remaining MCA candidate countries.

[8] The Country Credit Rating indicator measures on a scale of 0 to 100, with 0 representing the highest risk and 100 representing the lowest risk.

Objective 1.7: Improve Annual Percentage of Compact Targets Met on Time			
Output Indicator: Quality of Compacts in Implementation			
Date	**Target**	**Actual**	**Comments**
2006	NA	67%	Actual percent targets met include: ▫ Madagascar completed two out of three targets
2007	80%	33%*	▫ As of June 2007, a total of six compact countries—Cape Verde, Georgia, Honduras, Madagascar, Nicaragua, and Vanuatu—have an obligation to report on targets. ▫ Thirty-five of a total of 51 targets were reported, representing a 69% response rate. ▫ Seventeen of the 35 reported targets achieved or exceeded the targets established in MCC approved Monitoring and Evaluation Plans, representing an overall 33% achievement of all established target values. *This percent achievement (33%) is lower than the target because: ▫ The data reflected for FY 2007 includes only the first two quarters. Final data should be received by the end of December 2007. At that time, MCC's performance is anticipated to be much closer to the 80% target. ▫ MCC has given no margin for "targets completed," i.e., they were either fully completed quantitatively and counted or not fully completed and not counted. MCC Monitoring and Evaluation group is currently in discussions about how to put margins around these targets. ▫ It is also worth noting that some targets identified as "completed" or "met" have in fact been exceeded by a wide margin, i.e., over-achieved. This is not reflected here because the indicator is nominal in scale—either you met the target or you did not.
Rating	Complete data is expected to be available in December 2007.		
Justification	This indicator is a composite measure of quality of MCA implementation of all MCC compacts. As such it is an appropriate measure of MCC performance in implementing its compacts. It treats all compacts to be of equal importance and all targets of equal weight. The scaling of the scorecard is arbitrary but consistent across all compacts. The level of indicator achievement should increase from one year to the next as shown in the targets below.		
Program Improvement	MCC anticipates reaching 80% compact targets met when all final information is reported in December 2007.		

Objective 1.8: Increase the Conditions Precedents (CPs) Met on Time			
Input Indicator: Compact Execution Quality			
Date	**Target**	**Actual**	**Comments**
2006 (Baseline)	NA	73% met on time	For 13 disbursements made during FY 2006, 250 CPs were met on time and 92 CPs were deferred. None were waived.
2007	Meet 75% on time	77% met on time	For FY 2007, 1,201 CPs were scheduled to be reported during this period and 77% (915) were met on time.
Rating	Target met		
Justification	This metric measures the percentage of CPs that were met on time. CPs are actions that a compact country needs to take before MCC will release a disbursement of funds. CPs can include such actions as appointing key personnel, completing feasibility studies or environmental impact assessments, or reaching specific implementation milestones. The low percentage of CPs deferred or waived demonstrates that MCA countries are taking necessary actions to ensure proper implementation of their compacts.		

The percent of CPs met on time for each compact country during FY 2007 is outlined in Exhibit 2-4.

Exhibit 2-4: Conditions Precedents Met

Compact Country	CPs Reported for FY 2007	CPs Met	% of CPs Met
Armenia	163	144	88%
Benin	249	169	68%
Cape Verde	124	95	76%
Georgia	276	199	72%
Ghana	24	20	83%
Honduras	59	54	92%
Madagascar	152	120	77%
Nicaragua	115	89	77%
Vanuatu	39	25	64%
Total	**1,201**	**915**	**77%**

STRATEGIC GOAL #2

Support Development of a Sound Policy Environment for Economic Growth and Poverty Reduction in the Developing World

The following are the objectives that constitute Strategic Goal #2:

2.1 Improve policy performance in ruling justly
2.2 Improve policy performance in investing in people
2.3 Improve policy performance in economic freedom

The MCC Strategic Plan defines the expected outcome for this strategic goal to be the creation of incentives for developing countries to adopt sound policies by making available substantial benefits to countries that rule justly, invest in their people, and encourage economic freedom.

Due to the policy-reform nature of the objectives under this strategic goal and the fact that progress in these areas is largely outside of MCC's control, all the indicators identified under this strategic goal are supplemental indicators. They do not strictly meet the "A" in the SMART criteria in that they are not directly attributable to MCC interventions, as discussed in more detail in the previous section. Although MCC cannot claim credit for country performance along these indicators, they are included because they are reflective of overall progress in partner countries and therefore directly relevant to MCC's programs. Therefore, while MCC will measure trends in these supplemental indicators, MCC will not set specific targets for these indicators or otherwise treat them as formal outcome measures.

Tied closely to Strategic Goal #2 is the Threshold program, for which MCC has identified several formal outcome measures. The Threshold program assists countries in becoming eligible for compact assistance by helping countries improve their performance on the policy indicators under Goal #2. Therefore, results for this program are also reported in this section.

Example of Significant Achievement—Sound Policy Environment for Economic Growth

Burkina Faso and MCC Foster Learning Through Girl-Friendly Schools

Safoura is among the lucky children with a new opportunity for learning in Koutoula Yarce, one of the 132 communities receiving elementary school funding from MCC in Burkina Faso. As a 9-year-old, Safoura should already be in third grade. However, when she was 7, the age of enrollment in Burkina Faso, her village had no school, and her parents were reluctant to allow her to walk several kilometers to the nearest school.

Although she started school late, Safoura is still among a fortunate minority in Burkina Faso, where fewer than half of all girls attend school. Long walking distances from schools, early and forced marriages, time-consuming household chores, and lack of interest in educating girls are some of the barriers that keep thousands of girls like Safoura from going to school.

The 2-year MCC project, called BRIGHT, provides incentives to remove these barriers and encourages increased enrollment and regular attendance of children, particularly girls. The program is simple, but grand in its scope: to build, equip, and support 132 schools in 10 of the 45 provinces. Three-classroom schools, boreholes for drinking water, separate latrines for girls and boys, and teacher housing are being constructed in remote communities that have no education infrastructure. Each school will be provided with sufficient desks to allow children to sit comfortably, free textbooks and school supplies, and a mid-day lunch. An incentive will be provided to girls who have at least a 90 percent attendance rate in the form of a take-home food ration worth $4 per month. An awareness raising campaign will be organized with students' parents and community leaders during the 2-year project period to help overcome the various obstacles that keep girls from attending school.

Example of Significant Achievement—Threshold Program

*In **Paraguay**, the government resolved as part of its Threshold program to make the business registration process faster and more efficient. This year, it cut the cost of business registration by more than $600 and reduced the number of days it takes to register a business from 74 to 35. It now plans to lower the average wait to fewer than 10 days—beyond its original objective.*

***Kenya**, one of the top 10 reformers of 2007, eliminated 10 days worth of red tape at the company registry by simply streamlining administrative processes. It also introduced competition among land valuers, which reduced the time it takes to register property by 9 days.*

*In **Albania**, the government, which already has reduced the cost of starting a business by 30 percent in 2 years, plans to use its Threshold program to lower costs by an additional 40 percent. To implement its 2007 law on business registration, the first National Registration Center opened in September 2007, initiating "one stop" business registration.*

How MCC Measures Policy Reform

Calculating Rates of Change for Policy Performance Variables

To calculate rates of change for different indicators and comparison groups, MCC has made a number of important assumptions. MCC chose to calculate proportional changes in the median performance of individual peer groups for each income level classification. The Low Income Countries (LIC) are divided into compact-eligible countries, threshold countries, and the remaining candidate countries.[9]

MCC first measured absolute changes in median performance on 13 indicators.[10] This calculation uses 2002 as the base year (in most cases) and the most recent year for which data is available as the end year.[11] MCC then divided the absolute change in a particular peer group's median performance by the "data range" in the base year. MCC defines the data range as the difference between the 90th percentile and the 10th percentile for all countries classified as LIC or Low Middle Income Countries (LMIC) in 2003.

There are a number of important caveats regarding these calculations. MCC divides these caveats into five categories: sample sizes, time lags, inferences based on median changes, categorical classifications, and rate of reform comparisons.

General Caveats

- **Sample Sizes.** For some of the indicators, data is missing for a non-trivial number of countries. This can significantly reduce the sample of countries for which comparisons can be made across any specific time period.[12] It is possible that these reduced sample sizes may introduce bias into the calculations, because rapidly improving countries may be more likely or less likely to have more complete data series, and therefore may be more likely or less likely to be included in our calculations.

[9] The Remaining Candidate Countries category includes all countries that satisfy the income criteria for MCA candidacy, including those that are statutorily prohibited from receiving U.S. assistance. We chose to include the statutorily prohibited countries because they are currently included in the median calculations used to determine eligibility for MCA assistance. The basis for determining whether countries satisfy the income criteria comes from the most recently available data on Gross National Income (GNI) per capita for 2003.

[10] The MCC currently uses 17 indicators in its selection process, however only 13 are discussed in this exercise. The indicators omitted include: land rights and access, which are used for the first time in the FY 2008 selection process; natural resource management, which are used for the first time in the FY 2008 selection process; trade policy, for which the underlying tariff rate data come from varying years and which may not reflect changes made in the time period of interest; and inflation, for which many changes will be driven by exogenous factors.

[11] 2002 is used as the base year due to the fact that the MCA selection criteria were first announced in 2002 and since much of the data used in the initial selection rounds (FY 2004 and FY 2005) was from 2002.

[12] The sample size is further constrained by a rule that requires a country to have data for *both* the base year and the end year in order to remain in the sample considered for the calculation. This rule was created to eliminate the kind of bias that would emerge if, for example, one country that was a lower performer, had data only in the base year and another country that was a higher performer had data only in the end year. The change in median would therefore be skewed not by country performance but by the difference in composition of the base year and end year groups.

In addition, when countries are separated into different categories, e.g., threshold, compact, and other, the sample of countries for which the necessary data points are available may be quite small. Across indicators, the composition of the sample for these different categories may vary for any given time period. While there is no reason to assume that this will introduce any systematic bias, it may introduce noise into the measure that will limit MCC's ability to draw inferences from observed changes.

Within the small samples for which median performance is being calculated there are also very large outliers present for some indicators. The use of the median rather than the average attempts to mitigate the impact of outliers, but outliers can still tend to make the rate of change very noisy from year to year. For this reason, great caution should be used in drawing inferences about the performance of categories of countries (e.g., threshold, compact, or other candidate countries) from year to year.

For the purposes of this exercise, data points are considered missing either because no data has been reported for a given year or because third-party providers have reported data that has not been updated, e.g., they have reported the same value for a given indicator in consecutive years without updating the information.[13]

- **Time Lags.** In most cases, there is a significant lag between changes in policy performance and changes in indicator performance. Reporting periods also vary by indicator, rendering rate-of-reform comparisons across indicators and "categorical rates of reform" highly problematic. The data available in a given year for a given indicator may also reflect a range of reporting periods. For example, some sub-indicators, which jointly constitute the indicators used in the selection process, report on a calendar year; others report on 12-month periods that vary from the calendar year; and others cover 2- or 3-year periods.
- **Inferences Based on Changes in the Median.** The measure of reform reflects changes in the medians for individual indicators. This measure necessarily gives a limited picture of how the full distribution of values changes over time. The median only provides information about where the two countries in the middle of each distribution fall. It does not provide any information about the mean or the rest of the distribution, which might be compressing, expanding, or skewing in either direction. Medians are also highly sensitive to the composition of the group being evaluated. The presence or absence of just one country can potentially have dramatic effects on the median score; this potential is greater in smaller sample sizes. Any inferences regarding the change in performance over time for any given indicator should keep the nature of MCC's chosen summary statistic well in mind.

[13] There are some cases in which data values from different years have been pooled to construct values for a given year. Where this is applicable, this has been noted in the text.

- **Categorical Classifications.** For the purposes of this exercise, countries were divided into different categories according to their status (e.g., compact eligible, threshold, and other) as established by the FY 2005 selection process for LICs and the FY 2006 selection process for LMICs.

Differences from the FY07 Measures

To report on FY 2007 performance, MCC revised how it calculated results on the policy measures. As a result, MCC revised historical data that was previously reported in MCC's FY 2007–2008 Performance Plan. Changes regarding the calculation of results are explained below:

- **Changing the Basis for Status Categorization for Low Income Countries.** Eligibility status in FY 2005 was used to classify LICs in this exercise. In FY 2007, FY 2004, and FY 2005, status was used to create categories. This year only FY 2005 status is used, and FY 2006 figures have been updated to reflect this new classification rule in order to provide comparability across years.
- **Fiscal Policy Indicator.** This year MCC is using the figure used for the selection process, i.e., the average ratio of fiscal deficit to GDP for 3 years (e.g., "2005" data actually reflects performance in 2003, 2004, and 2005). Last year MCC used annual data on fiscal balances. The reason for the change is that a round of debt relief caused unusual volatility in the fiscal deficit figures for the most recent fiscal year.

Exhibit 2-5 details MCC's performance against its objectives for Strategic Goal #2 and summarizes the number of objectives MCC met in FY 2007. Exhibit 2-6 details the specific objective, indicator, and performance, including for prior years.

Exhibit 2-5: Strategic Goal #2 Results Summary

Strategic Goal #2 (a): Support Development of a Sound Policy Environment for Economic Growth and Poverty Reduction in the Developing World			
Summary Results			
Total Indicators		**Performance Summary**	
Number of Objectives	3	Number of Targets Met	0
Number of Indicators	13	Number of Targets Not Met	0
		Number with Data Lags	0
		Supplemental Indicators (no target)	13
Strategic Goal #2 (b): Threshold Program			
Summary Results			
Total Indicators		**Performance Summary**	
Number of Objectives	88	Number of Targets Met	42
Number of Indicators	88	Number of Targets Not Met	12
		Number with Data Lags	34

Exhibit 2-6: Strategic Goal #2 (a) Detailed Results

Objective 2.1: Improve Policy Performance in Ruling Justly		
Supplemental Indicator: Political Rights[14]		
Date	**Actual–Compact Eligible**	**Comments**
2003	27	Actual data is from 2002.
2006	27	Actual data is from 2005 (1-year time lag). The political rights indicator rate of change for 2003-2006 is 0%.
2007	28	Actual data from 2006 (1-year lag). The political rights indicator rate of change for 2003–2007 is 3.39%.
Date	**Actual–Threshold**	**Comments**
2003	21	Actual data is from 2002.
2006	24	Actual data is from 2005. The political rights indicator rate of change for 2003–2006 is 10.17%.
2007	25	Actual data is from 2006. The political rights indicator rate of change for 2003–2007 is 13.56%.
Period (Year)	**Actual Value–Other Candidate**	**Notes**
2003	9.5	Actual data is from 2002.
2006	10.5	Actual data is from 2005. The political rights indicator rate of change for 2003–2006 is 3.39%.
2007	11	Actual data is from 2006. The political rights indicator rate of change for 2003–2007 is 5.08%.
Rating	Not Applicable.	
Justification	The indicators were selected as a proxy for quality of policy environment. An improvement in these indicators is consistent with improvement in the policy environment in this area. It is expected that performance on these indicators will improve more for threshold- and compact-eligible countries.	
Supplemental Indicator: Civil Liberties[15]		
Period (Year)	**Actual Value–Compact Eligible**	**Notes**
2003	41	Actual data is from 2002.
2006	41.5	Actual data is from 2005. The civil liberties indicator rate of change for 2003–2006 is 1.43%.
2007	41	Actual data is from 2006. The civil liberties indicator rate of change for 2003–2007 is 0%.

[14] The Political Rights indicator evaluates countries on a 40-point scale, with 40 representing "most free" and 0 representing "least free."

[15] The Civil Liberties indicator evaluates countries on a 60-point scale, with 60 representing "most free" and 0 representing "least free."

Objective 2.1: Improve Policy Performance in Ruling Justly		
Period (Year)	**Actual Value–Threshold**	**Notes**
2003	35	Actual data is from 2002.
2006	37	Actual data is from 2005. The civil liberties indicator rate of change for 2003–2006 is 5.71%.
2007	36	Actual data from 2006. The civil liberties indicator rate of change for 2003–2007 is 2.86%.
Period (Year)	**Actual Value–Other Candidate**	**Notes**
2003	20	Actual data is from 2002.
2006	21	Actual data is from 2005. The civil liberties indicator rate of change for 2003–2006 is 2.86%.
2007	22	Actual data is from 2006. The civil liberties indicator rate of change for 2003-07 is 5.71%.
Rating	Not applicable.	
Justification	The indicators were selected as a proxy for quality of policy environment. An improvement in these indicators is consistent with improvement in the policy environment in this area. It is expected that performance on these indicators will improve more for threshold- and compact-eligible countries.	
Supplemental Indicator: Control of Corruption[16]		
Period (Year)	**Actual Value–Compact Eligible**	**Notes**
2003	-0.411	Actual data is from 2002.
2006	-0.466	Actual data is from 2005. The control of corruption indicator rate of change for 2003–2006 is -4.32%.
2007	-0.479	Actual data is from 2006. The control of corruption indicator rate of change for 2003–2007 is -5.38%.
Period (Year)	**Actual Value–Threshold**	**Notes**
2003	-0.821	Actual data is from 2002.
2006	-0.803	Actual data is from 2005. The control of corruption indicator rate of change for 2003–2006 is 1.46%.
2007	-0.702	Actual data is from 2006. The control of corruption indicator rate of change for 2003–2007 is 9.38%.

[16] The Control of Corruption indicator measures rate of change on a scale that ranges from 3 to -3. A higher score indicates a higher level of performance.

Objective 2.1: Improve Policy Performance in Ruling Justly		
Period (Year)	**Actual Value–Other Candidate**	**Notes**
2003	-0.918	Actual data is from 2002.
2006	-1.034	Actual data is from 2005. The control of corruption indicator rate of change for 2003–2006 is -9.18%.
2007	-0.980	Actual data is from 2006. The control of corruption indicator rate of change for 2003–2007 is -4.88%.
Rating	Not applicable.	
Justification	The indicators were selected as a proxy for quality of policy environment. An improvement in these indicators is consistent with improvement in the policy environment in this area. It is expected that performance on these indicators will improve more for threshold- and compact-eligible countries.	
Supplemental Indicators: Government Effectiveness[17]		
Period (Year)	**Actual Value–Compact Eligible**	**Notes**
2003	-0.303	Actual data is from 2002.
2006	-0.348	Actual data is from 2005. The government effectiveness indicator rate of change for 2003–2006 is -3.24%.
2007	-0.330	Actual data is from 2006. The government effectiveness indicator rate of change for 2003–2007 is -1.95%.
Period (Year)	**Actual Value–Threshold**	**Notes**
2003	-0.735	Actual data is from 2002.
2006	-0.775	Actual data is from 2005. The government effectiveness indicator rate of change for 2003–2006 is -2.83%.
2007	-0.727	Actual data is from 2006. The government effectiveness indicator rate of change for 2003–2007 is 0.57%.
Period (Year)	**Actual Value–Other Candidate**	**Notes**
2003	-0.906	Actual data is from 2002.
2006	-0.996	Actual data is from 2005. The government effectiveness indicator rate of change for 2003–2006 is -6.36%.
2007	-1.009	Actual data is from 2006. The government effectiveness indicator rate of change for 2003–2007 is -7.29%.

[17] The Government Effectiveness indicator measures rate of change on a scale that ranges from 3 to -3. A higher score indicates a higher level of performance.

Objective 2.1: Improve Policy Performance in Ruling Justly		
Rating	Not applicable.	
Justification	The indicators were selected as a proxy for quality of policy environment. An improvement in these indicators is consistent with improvement in the policy environment in this area. It is expected that performance on these indicators will improve more for threshold- and compact-eligible countries.	
Supplemental Indicators: Rule of Law[18]		
Period (Year)	**Actual Value–Compact Eligible**	**Notes**
2003	-0.297	Actual data is from 2002.
2006	-0.210	Actual data is from 2005. The rule of law indicator rate of change for 2003–2006 is 5.71%.
2007	-0.323	Actual data is from 2006. The rule of law indicator rate of change for 2003–2007 is -1.68%.
Period (Year)	**Actual Value–Threshold**	**Notes**
2003	-0.589	Actual data is from 2002.
2006	-0.601	Actual data is from 2005. The rule of law indicator rate of change for 2003–2006 is -0.79%.
2007	-0.559	Actual data is from 2006. The rule of law indicator rate of change for 2003–2007 is 1.97%.
Period (Year)	**Actual Value–Other Candidate**	**Notes**
2003	-1.031	Actual data is from 2002.
2006	-1.051	Actual data is from 2005. The rule of law indicator rate of change for 2003–2006 is -1.29%.
2007	-0.979	Actual data is from 2006. The rule of law indicator rate of change for 2003–2007 is 3.46%.
Rating	Not applicable.	
Justification	The indicators were selected as a proxy for quality of policy environment. An improvement in these indicators is consistent with improvement in the policy environment in this area. It is expected that performance on these indicators will improve more for threshold- and compact-eligible countries.	

[18] The Rule of Law indicator measures rate of change on a scale that ranges from 3 to -3. A higher score indicates a higher level of performance.

Objective 2.1: Improve Policy Performance in Ruling Justly		
Supplemental Indicator: Voice and Accountability[19]		
Period (Year)	**Actual Value–Compact Eligible**	**Notes**
2003	-0.100	Actual data is from 2002.
2006	-0.080	Actual data is from 2005. The voice and accountability indicator rate of change for 2003–2006 is 0.96%.
2007	-0.053	Actual data is from 2006. The voice and accountability indicator rate of change for 2003–2007 is 2.24%.
Period (Year)	**Actual Value–Threshold**	**Notes**
2003	-0.402	Actual data is from 2002.
2006	-0.352	Actual data is from 2005. The voice and accountability indicator rate of change for 2003–2006 is 2.39%.
2007	-0.311	Actual data is from 2006. The voice and accountability indicator rate of change for 2003–2007 is 4.32%.
Period (Year)	**Actual Value–Other Candidate**	**Notes**
2003	-1.220	Actual data is from 2002.
2006	-1.153	Actual data is from 2005. The voice and accountability indicator rate of change for 2003–2006 is 3.19%.
2007	-1.105	Actual data is from 2006. The voice and accountability indicator rate of change for 2003–2007 is 5.45%.
Rating	Not applicable.	
Justification	The indicators were selected as a proxy for quality of policy environment. An improvement in these indicators is consistent with improvement in the policy environment in this area. It is expected that performance on these indicators will improve more for threshold- and compact-eligible countries.	

[19] The Voice and Accountability indicator measures rate of change on a scale that ranges from 3 to -3. A higher score indicates a higher level of performance.

Objective 2.2: Improve Policy Performance in Investing in People		
Supplemental Indicator: Health Expenditure[20]		
Period (Year)	**Actual Value–Compact Eligible**	**Notes**
2004	2.64	Actual data is from 2002.
2006	2.79	Actual data is from 2004. The health expenditure indicator rate of change for 2003–2006 is 3.55%.
2007	2.88	Actual data is from 2005. The health expenditure indicator rate of change for 2003–2007 is 5.51%.
Period (Year)	**Actual Value–Threshold**	**Notes**
2004	2.56	Actual data is from 2002.
2006	2.96	Actual data is from 2004. The health expenditure indicator rate of change for 2003–2006 is 9.18%.
2007	2.79	Actual data is from 2005. The health expenditure indicator rate of change for 2003–2007 is 5.39%.
Period (Year)	**Actual Value–Other Candidate**	**Notes**
2004	1.95	Actual data is from 2002.
2006	1.76	Actual data is from 2004. The health expenditure indicator rate of change for 2003–2006 is -4.36%.
2007	1.69	Actual data is from 2005. The health expenditure indicator rate of change for 2003–2007 is -5.97%.
Rating	Not applicable.	
Justification	The indicator was selected as a proxy for quality of policy environment. An improvement in these indicators is consistent with improvement in the policy environment in this area. It is expected that performance on these indicators will improve more for threshold- and compact-eligible countries.	
Supplemental Indicator: Immunization Rates[21]		
Period (Year)	**Actual Value–Compact Eligible**	**Notes**
2004	86.5	Actual data is from 2002.
2006	90	Actual data is from 2004. The immunization indicator rate of change for 2003–2006 is 7.14%.
2007	91	Actual data is from 2006. The immunization indicator rate of change for 2003–2007 is 9.18%.

[20] The actual value reported under the Health Expenditure indicator is government health expenditure as a percentage of GDP. Figures are originally estimated in million national currency units (million NCU) and in current prices.

[21] The Immunization Rate indicator measures the percentage of population that has received immunizations.

Objective 2.2: Improve Policy Performance in Investing in People		
Period (Year)	**Actual Value–Threshold**	**Notes**
2004	74.5	Actual data is from 2002.
2006	87.5	Actual data is from 2004. The immunization indicator rate of change for 2003–2006 is 26.53%.
2007	90	Actual data is from 2006. The immunization indicator rate of change for 2003–2007 is 31.63%.
Period (Year)	**Actual Value–Other Candidate**	**Notes**
2004	69	Actual data is from 2002.
2006	74.5	Actual data is from 2004. The immunization indicator rate of change for 2003–2006 is 11.22%.
2007	77	Actual data is from 2006. The immunization indicator rate of change for 2003–2007 is 16.33%.
Rating	Not applicable.	
Justification	The indicator was selected as a proxy for quality of policy environment. An improvement in these indicators is consistent with improvement in the policy environment in this area. It is expected that performance on these indicators will improve more for threshold- and compact-eligible countries.	
Supplemental Indicator: Girls Primary Education Completion Rate[22]		
Period (Year)	**Actual Value–Compact Eligible**	**Notes**
2004	57.57	Actual data is the most recent of 2001 or 2002.
2006	68.75	Actual data is the most recent of 2003 or 2004. The girls' primary education completion indicator rate of change for 2003–2006 is 15.65%.
2007	70.58	Actual data is the most recent of 2005 or 2006. The girls' primary education completion indicator rate of change for 2003–2007 is 18.21%.
Period (Year)	**Actual Value–Threshold**	**Notes**
2004	62.63	Actual data is the most recent of 2001 or 2002.
2006	62.43	Actual data is the most recent of 2003 or 2004. The girls' primary education completion indicator rate of change for 2003–2006 is -0.28%.
2007	71.64	Actual data is the most recent of 2005 or 2006. The girls' primary education completion indicator rate of change for 2003–2007 is 12.61%.

[22] The Girls' Primary Education Completion Rate measures gross intake ratio of female students into their last year of primary school.

Objective 2.2: Improve Policy Performance in Investing in People		
Period (Year)	**Actual Value–Other Candidate**	**Notes**
2004	56.10	Actual data is the most recent of 2001 or 2002.
2006	65.41	Actual data is the most recent of 2003 or 2004. The girls' primary education completion indicator rate of change for 2003–2006 is 13.03%.
2007	64.46	Actual data is the most recent of 2005 or 2006. The girls' primary education completion indicator rate of change for 2003–2007 is 11.70%.
Rating	Not applicable.	
Justification	The indicator was selected as a proxy for quality of policy environment. An improvement in these indicators is consistent with improvement in the policy environment in this area. It is expected that performance on these indicators will improve more for threshold- and compact-eligible countries.	

Objective 2.3: Improve Policy Performance in Economic Freedom		
Supplemental Indicator: Fiscal Policy[23]		
Period (Year)	**Actual Value–Compact Eligible**	**Notes**
2002	-0.048	Actual data is from 2002.
2006	-0.024	Actual data is from 2005. The fiscal policy indicator rate of change for 2003–2006 is 29.43%.
2007	-0.017	Actual data is from 2006. The fiscal policy indicator rate of change for 2003–2007 is 38.85%.
Period (Year)	**Actual Value–Threshold**	**Notes**
2002	-0.043	Actual data is from 2002.
2006	-0.026	Actual data is from 2005. The fiscal policy indicator rate of change for 2003–2006 is 20.39%.
2007	-0.010	Actual data is from 2005. The fiscal policy indicator rate of change for 2003–2007 is 40.41%.
Period (Year)	**Actual Value–Other Candidate**	**Notes**
2002	-0.031	Actual data is from 2002.
2006	-0.024	Actual data is from 2005. The fiscal policy indicator rate of change for 2003–2006 is 8.10%.
2007	-0.014	Actual data is from 2006. The fiscal policy indicator rate of change for 2003–2007 is 21.17%.

[23] The Fiscal Policy indicator measures the percent rate of change based on the percentage change of the budget deficit divided by GDP as a three year average.

Objective 2.3: Improve Policy Performance in Economic Freedom		
Rating	Not applicable.	
Justification	The indicator was selected as a proxy for quality of policy environment. An improvement in these indicators is consistent with improvement in the policy environment in this area. It is expected that performance on these indicators will improve more for threshold- and compact-eligible countries.	
Supplemental Indicator: Cost of Starting a Business[24]		
Period (Year)	**Actual Value–Compact Eligible**	**Notes**
2003	77	Actual data is from 2003.
2006	49.6	Actual data is from 2006. The cost of starting a business indicator rate of change for 2003–2006 is -11.27%.
2007	37.4	Actual data is from 2007. The cost of starting a business indicator rate of change for 2003–2007 for is -16.29%.
Period (Year)	**Actual Value–Threshold**	**Notes**
2003	123.2	Actual data is from 2003.
2006	96.0	Actual data is from 2006. The cost of starting a business indicator rate of change for 2003–2006 is -11.19%.
2007	77.6	Actual data is from 2007. The cost of starting a business indicator rate of change for 2003–2007 is -18.75%.
Period (Year)	**Actual Value–Other Candidate**	**Notes**
2003	139.5	Actual data is from 2003.
2006	78.5	Actual data is from 2006. The cost of starting a business indicator rate of change for 2003–2006 is -25.09%.
2007	73.9	Actual data is from 2007. The cost of starting a business indicator rate of change for 2003–2007 is -26.98%.
Rating	Not applicable	
Justification	The indicator was selected as a proxy for quality of policy environment. An improvement in these indicators is consistent with improvement in the policy environment in this area. It is expected that performance on these indicators will improve more for threshold- and compact-eligible countries.	

[24] The Cost of Starting a Business measures the cost incurred in all stages of starting a new business. Cost is expressed as a percentage of the country's Gross National Income per capita.

Objective 2.3: Improve Policy Performance in Economic Freedom		
Supplemental Indicator: Time of Starting a Business[25]		
Period (Year)	**Actual Value–Compact Eligible**	**Notes**
2003	58	Actual data is from 2003.
2006	42	Actual data is from 2006. The days to start a business indicator rate of change for 2003–06 is -20.20%.
2007	29	Actual data is from 2007. The days to start a business indicator rate of change for 2003–2007 is -36.62%.
Period (Year)	**Actual Value–Threshold**	**Notes**
2003	43	Actual data is from 2003.
2006	37	Actual data is from 2006. The days to start a business indicator rate of change for 2003–2006 is -7.58%.
2007	35	Actual data is from 2007. The days to start a business indicator rate of change for 2003–2007 is -10.04%.
Period (Year)	**Actual Value–Other Candidate**	**Notes**
2003	44	Actual data is from 2003.
2006	43	Actual data is from 2006. The days to start a business indicator rate of change for 2003–2006 is -7.58%.
2007	37	Actual data is from 2007. The days to start a business indicator rate of change is -8.84%.
Rating	Not applicable	
Justification	The indicator was selected as a proxy for quality of policy environment. An improvement in these indicators is consistent with improvement in the policy environment in this area. It is expected that performance on these indicators will improve more for threshold- and compact-eligible countries.	
Supplemental Indicator: Regulatory Quality[26]		
Period (Year)	**Actual Value–Compact Eligible**	**Notes**
2003	-0.327	Actual data is from 2002.
2006	-0.329	Actual data is from 2005. The regulatory quality indicator rate of change for 2003–2006 is -0.16%.
2007	-0.299	Actual data is from 2006. The regulatory quality indicator rate of change for 2003–2007 is 1.68%.

[25] The Time of Starting a Business measures the number of days necessary to start a new business.

[26] The Regulatory Quality indicator measures on a scale that ranges from 3 to -3. A higher score indicates a higher level of performance.

Objective 2.3: Improve Policy Performance in Economic Freedom		
Period (Year)	**Actual Value–Threshold**	**Notes**
2003	-0.503	Actual data is from 2002.
2006	-0.508	Actual data is from 2005. The regulatory quality indicator rate of change for 2003–2006 is -0.33%.
2007	-0.520	Actual data is from 2006. The regulatory quality indicator rate of change for 2003–2007 is -1.03%.
Period (Year)	**Actual Value–Other Candidate**	**Notes**
2003	-0.963	Actual data is from 2002.
2006	-1.001	Actual data is from 2005. The regulatory quality indicator rate of change for 2003–2006 is -2.31%.
2007	-0.992	Actual data is from 2006. The regulatory quality indicator rate of change for 2003–2007 is -1.79%.
Rating	Not applicable	
Justification	The indicator was selected as a proxy for regulatory quality of policy environment. An improvement in these indicators is consistent with improvement in the policy environment in this area. It is expected that performance on these indicators will improve more for threshold- and compact-eligible countries.	

Threshold Program Performance Results

The Threshold program is closely related to Strategic Goal #2 because the program assists countries in becoming eligible for compact assistance by helping them improve their performance on the policy indicators that fall under Strategic Goal #2. For this reason, Threshold program results are reported in this section. Each Threshold program has performance objectives based on the specifications of the program, so each country has unique objectives and targets.

Exhibit 2-7 summarizes the performance results for Tanzania, Ukraine, the Philippines, Paraguay, Malawi, Indonesia, Burkina Faso, and Albania and provides a breakdown for each country. These countries have begun program implementation. The remaining Threshold countries are in the early stages of program development and did not report on indicator progress in FY 2007.

Exhibit 2-7: Strategic Goal #2 (b) Threshold Program Detailed Results

Threshold Program				
Summary Results				
Country	**Number of Objectives**	**Performance Summary**		
		Targets Met	**Targets Not Met**	**Data Lag/NA**
Tanzania	6	3	2	1
Ukraine	21	5	1	15
Philippines	9	6	1	2
Paraguay	10	2	2	6
Malawi	8	5	3	-
Indonesia	9	-	-	9
Burkina Faso	8	5	2	1
Albania	17	16	1	-
Total	**88**	**42**	**12**	**34**

Tanzania						
Performance Objective	**Expected Output**	**Baseline as of May 2006**	**Target**		**Actual**	
			2006	**2007**	**2006**	**2007**
Districts using public expenditure tracking	60	12	18	34	15	31
Anti-corruption investigations brought to court	28	20	21	24	37	144
Media stories exposing corruption	1,300		144	576	60	816
Media stories of anti-corruption cases brought to court	300	50	--	124	0	109
Financial Intelligence Unit cases opened	30	0	--	--	0	0
Procurement audits conducted on Media Development Associations and Local Government Authorities	40	0	--	12	0	20
Rating	Target Met (3), Not Met (2), NA (1)					
Justification	The indicator was selected as a proxy for quality of policy environment. An improvement in the indicator is consistent with improvement in the policy environment in this area.					

Ukraine				
Performance Objective	Target	Baseline as of January 2007	Target 2007 Q3	Actual 2007 Q3
Increased public knowledge of corruption reforms and issues	4.5 million	0	1.5 million	1.4 million
Advocacy campaigns lead to anti-corruption reforms	24	0	0	0
More consistent application of law	TBD	TBD	--	0
More transparent case assignment	100	0	--	0
More transparent and substantive selection of judges	600	0	0	0
More transparent and objective discipline practice	32	0	--	0
Improved transparency in enforcement procedures	100%	40	42	42
Improved enforcement of judgments	28%	22	22	22
Well-trained administrative judges	500		-	
Opportunity for corrupt licensing practice reduced	100%	0	NA	
Improved monitoring of professional standards	40	0	NA	
Improved customs regulatory system	19	0	1	
Improved transport regulatory system	TBD	0	NA	
Trained personnel on New Computerized Transit System	30	0	5	
Regulations governing construction permits improved	9	0	0	0
Streamlined regulatory processes	25	0	0	0
Procedures of land parcels connectivity to utilities improved and simplified	9	0	0	
Student body prepared for standardized testing techniques	100%	10	10	10
Question bank adequately populated	100%	0	NA	0
Tests securely administered	1.5 million	82,000	240	247
Rating	Target Met (5), Not Met (1), NA (15)			
Justification	The indicator was selected as a proxy for quality of policy environment. An improvement in the indicator is consistent with improvement in the policy environment in this area.			

Philippines							
Performance Objective	Target	Baseline as of December 2005	Target		Actual	
			2006	2007	2006	2007
Conviction rate of Office of Ombudsman	40	33%	33	33	25	35
Cases mediated in the Office of Ombudsman	300/year	0	0	25	0	10
Revenue integrity protection service cases filed	50/year	18	13	15	27	16
Number of officials charged by RIPS–Suspended by the Ombudsman	35	6	7	7	12	12
Percentage increase in income tax returns filed	+10%	487,594 tax returns	5.0	7.0	8.3	NA
Percentage increase in corporate tax returns filed	+10%	134,151 tax returns	5.0	7.0	6.6	NA
Number of tax evasion cases filed	116	44	44	50	77	87
Number of cases filed by RATS at the Department of Justice	24/yr	11	9	7	17	16
RATS cases filed before the Court of Tax Appeals	15/yr	1	2	3	4	4
Rating	Target Met (6), Not Met (1), NA (2)					
Justification	The indicator was selected as a proxy for quality of policy environment. An improvement in the indicator is consistent with improvement in the policy environment in this area.					

Paraguay				
Performance Objective	Target	Baseline as of January 2007	Target	Actual
			2007 Q3	2007 Q3
The number of cases being investigated by newly trained personnel using new forensic laboratory and new criminal investigative techniques	20	0	Results are not expected until a later date.	NA
Increase in number of disciplinary measures, cases, and accusations submitted to the Public Ministry and the Jury for the Prosecution of Judges		Baseline not defined	NA	NA
Number of audits yielding punishable offenses or administrative misconduct that are then followed by the Public Ministry and Congress	12	0	This indicator is under review for possible substitution.	NA
Percentage of information accessed (Motor Vehicles Registry, Judiciary Court Registry, and Identifications Registry database)	100%	0	20%	This indicator is under review for possible modification.
Number of public agencies subject to budget execution legislative oversight system	20	0	NA	NA
Reduced Value Added Tax (VAT) Breach	35%	53%	46%	Data not available

Paraguay				
Performance Objective	Target	Baseline as of January 2007	Target	Actual
			2007 Q3	2007 Q3
Customs collections from seized merchandise	$6.5 million	0	$1.3 million	$1.07 million
Internal corruption cases from Finance Ministry submitted correctly to the Public Ministry	13	0	1	36
Number of days to start a business	36	74	36	25
Number of *maquilas* (businesses with low cost structures) installed	15	0	4	0[27]
Rating	Target Met (2), Not Met (2), NA (6)			
Justification	The indicator was selected as a proxy for quality of policy environment. An improvement in the indicator is consistent with improvement in the policy environment in this area.			

Malawi						
Performance Objective	Target	Baseline as of July 2006	Target		Actual	
			2006	2007	2006	2007
Adequate reports for ministries and the National Assembly	Reports implemented	Reports distributed 2 years after fiscal year	Computer procurement process initiated	IFMIS training for capacity to deliver quarterly reports	Yes	No
Financial Intelligence Unit (FIU) established in accordance with the anti-money laundering/combating financing of terrorism law	Establishment and operation of an effective FIU	No FIU	AML/CFT law passed	Procurement initiated	Yes	No
National Assembly has more control over own budget	National Assembly oversight function strengthened	MOF did not fully and regularly fund National Assembly	MOF allocates full budget allowance	MOF allocates full budget allowance	Yes	Yes
Media Council (MC) established	MC established by 2007	No MC in operation	Identification of key stakeholders	MC develops transparent by-laws	Yes	Yes
Number of civil society groups testifying before the National Assembly triples	Civil society integrated into anti-corruption campaign	0	4	9	4	4
AML/CFT passed by November 2006	Key pieces of reform legislation promulgated	No AML/CFT law	AML/CFT legislation passed by National Assembly	AML/CFT legislation passed by National Assembly	Yes	Yes

27 Five *maquilas* are in the process of installation. This indicator is in the process of modification.

Malawi						
Performance Objective	Target	Baseline as of July 2006	Target		Actual	
			2006	2007	2006	2007
More than 500 people trained across all program components	Government of Malawi's capacity to combat corruption enhanced	0	85	340	47	718
Sovereign credit rating moves from CCC+ to B- (positive outlook)	Sovereign credit rating improved	2006: CCC+	Hire Fitch and prepare for GOM/Fitch meeting	Develop plan to disseminate and explain results of Fitch report	Yes	Yes
Rating	Target Met (5), Not Met (3)					
Justification	The indicator was selected as a proxy for quality of policy environment. An improvement in the indicator is consistent with improvement in the policy environment in this area.					

Indonesia				
Performance Objective	Target	Baseline as of May 2007	Target	Actual
			2007 Q4	2007 Q3
Number of judges trained on judicial code of ethics	200	0	72	NA
Number of court personnel trained on budget procedures	1,600	0	0	NA
Number of trials monitored in Jakarta	180 p.a.	160	43	NA
Percentage of Suspicious Transaction Reports filed by non-bank financial institutions as percent of total filings	10%	3.20%	3.2%	NA
Total number of children less than 1 year of age immunized with DPT and measles in seven Threshold provinces	Cumulative Target: 4,754,265	2005 Baseline: 2,283,094 adjusted for over-reporting	611,998	NA
Percentage of Puskesmas using local area monitoring (LAM) mapping tools for immunization coverage	100% Puskesmas in Threshold Districts	Available September 2007	10%	NA
Number of project priority districts/municipalities annual EPI action plans launched and monitored by local government	Cumulative Target: 75	0	10	NA
Percent of presence districts that faced no vaccine (DPT or measles) stock outs greater than 1 week during the reporting quarter	0%	Available September 2007	50%	NA

Indonesia				
Performance Objective	Target	Baseline as of May 2007	Target	Actual
			2007 Q4	2007 Q3
Number of individuals trained in immunization, supportive supervision, and vaccine management	Cumulative Target: 2,543	0	271	NA
Rating	Target Met (), Not Met (), NA (9)			
Justification	The indicator was selected as a proxy for quality of policy environment. An improvement in the indicator is consistent with improvement in the policy environment in this area.			

Burkina Faso								
Performance Objective	Target	Baseline as of April 2006	Target			Actual		
			2006 Q3	2006 Q4	2007	2006 Q3	2006 Q4	2007
Total number of girls recruited (cumulative Year 1 plus Year 2)	3,300	0	1,650	-	3,300	2417	-	6,338
Temporary classrooms in operation	132	0			120			132
Girl-friendly educational complexes: –Completed –Construction in progress	132	0		0	132		26	101 21
Take-home rations provided for each girl	3,300	0			3,300			NA
Total number of social mobilization campaigns conducted on the benefits of girls' schooling	132 Comm unities	0	33	33	33	33	33	33
Literacy and training provided to mother mentors	7,920	0	0	0	7,920	0	0	7,840
Teachers and outreach staff trained in gender pedagogy	238	0	0	0	238	0	0	246
Government employees trained in monitoring and evaluation	30		0	0	30	0	0	30
Rating	Target Met (5), Not Met (2), NA (1)							
Justification	The indicator was selected as a proxy for quality of policy environment. An improvement in the indicator is consistent with improvement in the policy environment in this area.							

Albania				
Performance Objective	Project End Target	Baseline	Target 2007 Q3	Actual 2007 Q3
Number of tax laws, pieces of secondary legislation, and regulations reviewed, drafted, revised, and/or amended	17	0	15	19
Tax revenues collected from the large taxpayers as a percentage of total tax	50%	30%	30%	50.75%
Number of procurement regulations developed, reviewed, and/or revised	5	0	0	6
Training modules complete	1	0	0	1
Number of trainers trained	35	0	20	20
Percentage of Public Procurement Bulletins electronically published	100%	0	37.5%	25.0%
Percentage of Public Procurement Agency staff trained in new procurement policies	100%	0	92%	92%
Percentage of PPA staff trained in IT integration using e-procurement software	35%	0	40%	48%
Number of procurement officers and public officials trained	2,000	0	400	411
Number of economic operators trained in new public procurement law and regulations	1,400	0	0	97
Number of commercial registry-related laws reviewed	20	0	0	18
Number of commercial registry- related laws drafted, revised, and/or amended	9	0	0	11
Preparation of secondary legislation for the establishment of National Registration Center (NRC)	16	0	0	16
New commercial registry law establishing the NRC enacted by Council of Ministers	1	0	0	1
New commercial registry law establishing the NRC enacted by parliament	1	0	0	1
Amendments for the new commercial registry laws enacted by parliament	9	0	0	9
NRC secondary legislation enacted by Council of Ministers	16	0	0	16
Rating	Target Met (1), Not Met (16), NA ()			
Justification	The indicator was selected as a proxy for quality of policy environment. An improvement in the indicator is consistent with improvement in the policy environment in this area.			

STRATEGIC GOAL #3

Advance International Development Assistance Practice by Continually Improving MCC's Operational Effectiveness

The following are the objectives that constitute Strategic Goal #3:

3.1 Enhance MCA model recognition and support within the international community

3.2 Enhance MCC country partnership

MCC's Strategic Plan defines the expected outcome for Strategic Goal #3 to be that MCC will be at the forefront of the development assistance field and viewed as a model of effectiveness by other development practitioners. MCC identifies best practices, internally and externally, and adopts them to improve its operations.

The first objective, "Enhance MCA model recognition and support within the international community," assesses whether there is recognition of MCC's approach, or a good understanding of the MCA model and whether MCC is recognized for innovative and best practice approaches. The second indicator, "Enhance MCC country partnership," assesses how good a development partner MCC is relative to other donors and to itself over time.

Exhibit 2-8 details MCC's performance against its objectives for Strategic Goal #3 and summarizes the number of objectives MCC met in FY 2007. Exhibit 2-9 details the specific objective, indicator, and performance, including for prior years.

Exhibit 2-8: Strategic Goal #3 Results Summary

Strategic Goal #3: Advance International Development Assistance Practice by Continually Improving MCC's Operational Effectiveness			
Summary Results			
Total Indicators		**Performance Summary**	
Number of Objectives	2	Number of Targets Met	0
Number of Indicators	2	Number of Targets Not Met	0
		Number with Data Lags or NA	2

Exhibit 2-9: Strategic Goal #3 Detailed Results

Objective 3.1: Enhance MCA Model Recognition and Support Within the International Community			
Output Indicator: Leadership in Development Practice			
Date	**Target**	**Actual**	**Comments**
2007	NA	NA	Survey to be conducted every other year beginning in FY 2008.
Rating	NA		
Justification	Data is not available until the end of FY 2008.To assess whether MCC is receiving recognition and support for the MCA approach, it will be necessary to determine first whether stakeholders in the international development community know about and understand the model and whether MCC is impacting other development actors' behavior. This indicator expects that as MCC demonstrates the effectiveness of the operational approach and, as a result, the recognition of the MCA model increases, MCC will have an increasing impact on others' behavior.		

Objective 3.2: Enhance MCC Country Partnership			
Input Indicator: Assessment of MCC Country Partnership			
Date	**Target**	**Actual**	**Comments**
Baseline year (2007)	NA	Baseline	Will set performance trend once baseline data is collected.
Rating	NA		
Justification	Data will be available November 2008.The measure will evaluate MCC's performance relative to other donors and to MCC itself and will aid in assessing effectiveness and informing efforts to improve performance. The trend, therefore, should be continually improving.		

STRATEGIC GOAL #4

Build MCC's Capabilities to Achieve Its Primary Strategic Goals

The following are the objectives that constitute Strategic Goal #4:

4.1 Minimize the administrative cost of developing and implementing MCC compacts compared to the total value of compacts

4.2 Address and close Inspector General recommendations within agreed-upon timeframes

4.3 Achieve high level of staff effectiveness and satisfaction

MCC's Strategic Plan defines the expected outcome for Strategic Goal #4 to be the efficient and effective operation of MCC. To enable MCC to achieve its mission, MCC will develop its human resources and financial and administrative capacities; articulate clear processes, policies, and quality standards; and build strong support systems.

Example of Significant Achievement

MCC Receives Award for Being a Best Place to Work in the Federal Government

The MCC placed fifth out of 31 small agencies in the Federal Government in the 2007 Best Places to Work ranking. The Best Places to Work award drew on responses from more than 221,000 civil servants to produce detailed rankings of employee engagement across 283 federal agencies and subcomponents. In addition to the employee engagement rating, agencies and subcomponents are also scored in 10 workplace environment categories such as effective leadership, employee skills/mission match, and work/life balance.

Exhibit 2-10 details MCC's performance against its objectives for Strategic Goal #4 and summarizes the number of objectives MCC met in FY 2007. Exhibit 2-11 details the specific objective, indicator, and performance, including for prior years.

Exhibit 2-10: Strategic Goal #4 Results Summary

Strategic Goal #4: Build MCC's Capabilities to Achieve Its Primary Strategic Goals			
Summary Results			
Total Indicators		**Performance Summary**	
Number of Objectives	3	Number of Targets Met	1
Number of Indicators	4	Number of Targets Not Met	2
		Number with Data Lags	1

Exhibit 2-11: Strategic Goal #4 Detailed Results

Objective 4.1: Minimize the Administrative Cost of Developing and Implementing MCC Compacts Compared to the Total Value of Compacts			
Input Indicator: Efficiency and Resource Productivity 1			
Period (Year)	**Target**	**Actual**	**Notes**
2005 (Baseline)	NA	3.4%	The numerator is the annual total administrative and due diligence obligations and the denominator is the total amount committed under compacts and threshold agreements in the fiscal year.
2006	NA	4.7%	
2007	2.7%	2.6%	MCC outperformed its target.
Rating	Target met		
Justification	As MCC signs and begins to implement compacts, the workload for MCC staff is shifting from compact development to compact implementation. This indicator measures efficiency increases as MCC's administrative and due diligence expenses are focused on project implementation and results. A lower percentage indicates improvement in efficiency.		
Input Indicator: Efficiency and Resource Productivity 2			
Period (Year)	**Target**	**Actual**	**Notes**
2005 (Baseline)	NA	1,289.8%	The numerator is the annual total administrative and due diligence disbursements and the denominator is the annual total amount disbursed for compacts, threshold agreements, and 609(g) activities.
2006	NA	151.2%	
2007	40.0%	61.5%	
Rating	Target not met		
Justification	As MCC signs and begins to implement compacts, the workload for MCC staff is shifting from organizational start-up to on-the-ground implementation of compacts and threshold agreements. This indicator measures efficiency increases as MCC's administrative and due diligence expenditures shift from fixed start-up costs to marginal costs of implementation. A lower percentage indicates improvement in efficiency.		
Performance Improvement	MCC is taking several steps to improve the compact implementation process, therefore increasing the amount of funds disbursed. For example, MCC has reduced the amount of time between compact signing, entry into force, and the first disbursement. In addition, MCC is putting fiscal and procurement agents in place earlier in the process to reduce delays in initial compact disbursement. Strategies noted under Strategic Goal #1 in the MD&A are expected to bolster MCC's results on this objective in coming years.		

Objective 4.2: Address and Close Inspector General Recommendations Within Agreed-Upon Timeframes			
Input Indicator: Compliance			
Date	**Target**	**Actual**	**Comments**
2006 (Baseline)	NA	44%	
2007	75%	67%	There were a total of 36 recommendations that were closed, 24 of which (67%) were closed on time. MCC had several OIG recommendations that had been completed on time but MCC failed to formally notify the OIG and so they remained open. Had MCC provided the formal notification, the recommendations would have closed before their due dates and MCC would have achieved its performance target of 75%.
Rating	Target not met.		
Justification	The MCC IG assesses MCC internal controls and practices through the annual financial audit and other audit reports and program reviews. While MCC may disagree with the IG in very isolated instances, MCC's responsiveness on the vast majority of recommendations on which it makes a "management decision" to accept is the best single measure of MCC's compliance with U.S. Government laws and regulations and implementation of financial management best practices.		
Performance Improvement	MCC has since dedicated a resource to track OIG recommendations and due dates.		

Objective 4.3: Achieve High Level of Staff Effectiveness and Satisfaction			
Input Indicator: Staffing Survey			
Date	**Target**	**Actual**	**Comments**
2007	NA	3.64 Grand Mean	For FY 2007, 300 MCC employees were sent invitations to complete the 2007 Employee Engagement Survey (Gallup's Q12 questions plus the Federal Human Capital Survey questions); 250 employees participated. The Gallup median response rate for their survey is 85%; MCC's response rate of 83% is considered to be good. MCC's Grand Mean for 2007 is 3.64, which puts the organization at the 31st percentile in the Gallup 2007 Overall Q12 database of public and private sector clients and at the 39th percentile in the Gallup 2007 Public Sector Q12 database and 44th percentile for first year clients.
Rating	NA – FY 2007 sets the baseline for this indicator.		
Justification	This indicator was selected to measure MCC's ability to recruit, motivate and provide professional development for, and retain a workforce of high-performing staff and reward exceptional results. Indicator changes may signal a need for modifications to MCC's procedures, compensation, and benefits package.		

3. FINANCIAL SECTION

In accordance with the OMB Circular A-136, Financial Reporting Requirements, MCC is presenting its financial statements in the appropriate form and content for FY 2007. The tables below outline the following financial statements:

- Balance Sheets
- Statements of Budgetary Resources
- Statements of Net Cost
- Statements of Changes in Net Position

Further details are provided in the Notes to Financial Statements section that follows.

BALANCE SHEETS

	FY 2007	FY 2006
Assets		
Intra-Governmental		
Fund Balance with Treasury *(Note 2)*	**$5,549,289,597**	**$4,078,656,972**
Accounts Receivable *(Note 3)*	67,798	62,202
Total Intra-Governmental	5,549,357,395	4,078,719,174
General Property, Plant, and Equipment *(Notes 4 and 5)*	7,115,606	4,632,785
Advances *(Note 1F, P)*	32,243,157	18,881,386
Total Assets	**$5,588,716,158**	**$4,102,233,345**
Liabilities		
Intra-Governmental		
Other	$1,457,862	$2,516,786
Total Intra-Governmental	**1,457,862**	**2,516,786**
Accounts Payable *(Note 1G)*	39,176,698	10,134,698
Other	3,971,886	2,698,070
Total Liabilities	**$44,606,446**	**$15,349,554**
Net Position		
Unexpended Appropriations – Other Funds	$5,536,714,361	$4,082,189,638
Cumulative Results of Operations – Other Funds	7,395,351	4,694,153
Total Net Position	**$5,544,109,712**	**$4,086,883,791**
Total Liabilities and Net Position	**$5,588,716,158**	**$4,102,233,345**

The notes are an integral part of these financial statements.

STATEMENTS OF BUDGETARY RESOURCES

	FY 2007	FY 2006
Budgetary Resources		
Unobligated Balance – Beginning of Period	$2,671,372,416	$2,053,722,184
Recoveries of Prior Years Obligations	15,930,609	-
Budget Authority:		
Appropriations	1,752,300,000	1,770,000,000
Nonexpenditure Transfers, Net, Anticipated and Actual	(9,415,980)	0
Permanently Not Available *(Note 7)*		(17,700,000)
Total Budgetary Resources	**$4,430,187,045**	**$3,806,022,184**
Status of Budgetary Resources		
Obligations Incurred		
Direct	$2,174,044,542	$1,109,535,594
Unobligated Balance Available	1,516,900,216	877,383,424
Unobligated Balance Not Available	$739,242,287	$1,819,103,166
Total Status of Budgetary Resources	**$4,430,187,045**	**$3,806,022,184**
Change in Obligated Balance		
Obligated Balance, Net – as of October 1, 2005		
Unpaid Obligations, Brought Forward, October 1	$1,408,398,635	$272,636,873
Obligations Incurred	2,174,044,542	1,109,535,594
Gross Outlays	(278,605,423)	(109,119,072)
Recoveries of Prior Year Unpaid Obligations, Actual	(15,930,609)	-
Obligated Balance, Net – End of Period		
Unpaid obligations	$3,287,907,145	$1,273,053,395
Net Outlays		
Gross Outlays	$278,605,423	$109,119,072

The notes are an integral part of these financial statements.

STATEMENTS OF NET COSTS

Program	2007 Total	2006 Total
Program Costs		
Compact		
Gross Costs *(Note 6)*	$81,079,458	$16,747,194
Less: Earned Revenue	-	-
Net Program Costs	81,079,458	16,747,194
609 (g) Programs		
Gross Costs	17,172,113	5,895,167
Less: Earned Revenue	-	-
Net Program Costs	17,172,113	5,895,167
Threshold Programs		
Gross Costs	75,766,215	15,235,063
Less: Earned Revenue	-	-
Net Program Costs	75,766,215	15,235,063
Due Diligence Programs		
Gross Costs	32,789,662	15,137,340
Less: Earned Revenue	-	-
Net Program Costs	32,789,662	15,137,340
Audit		
Gross Costs	2,865,820	619,714
Less: Earned Revenue	-	-
Net Program Costs	2,865,820	619,714
Administrative		
Gross Costs	77,922,457	54,785,827
Less: Earned Revenue	-	-
Net Program Costs	77,922,457	54,785,827
Program Costs – Net of All Programs	**$287,595,725**	**$108,420,305**
Net Costs of Operations	**$287,595,725**	**$108,420,305**

The notes are an integral part of these financial statements.

STATEMENTS OF CHANGES IN NET POSITION

	FY 2007	FY 2006
Cumulative Results of Operations		
Beginning Balances	$4,694,987	$4,276,833
Adjustments	-	-
Beginning Balance, as Adjusted	$4,694,987	$4,276,833
Budgetary Financing Sources		
Appropriations Used	$288,359,297	$107,689,343
Other Financing Sources		
Donations and Forfeitures of Property	$123,750	$ -
Imputed Financing	1,813,042	1,148,282
Total Financing Sources	290,296,089	108,837,625
Net Cost of Operations	(287,595,725)	(108,420,305)
Net Change	2,700,364	417,320
Cumulative Results of Operations	**$7,395,351**	**$4,694,153**
Unexpended Appropriations		
Beginning Balance	$4,082,189,638	$2,437,546,656
Changes in Accounting Principles	-	-
Beginning Balance, as Adjusted	$4,082,189,638	$2,437,546,656
Budgetary Financing Sources		
Appropriations Received	$1,752,300,000	$1,770,000,000
Appropriations Transferred In/Out	(9,415,980)	-
Other adjustments *(Note 7)*		(17,700,000)
Appropriations Used	(288,359,297)	(107,657,018)
Total Budgetary Financing Sources	1,454,524,723	1,644,642,982
Total Unexpended Appropriations	5,536,714,361	4,082,189,638
Net Position	**$5,544,109,712**	**$4,086,883,791**

The notes are an integral part of these financial statements.

NOTES TO FINANCIAL STATEMENTS (AS OF SEPTEMBER 30, 2007)

Note 1—Summary of Significant Accounting Policies

A. Basis of Presentation

The accompanying principal financial statements have been prepared to report the financial position, results of operations, and budgetary resources for MCC, as required by Section 613 of the Millennium Challenge Act of 2003. They have been prepared using MCC's books and records in accordance with MCC accounting policies, the most significant of which are summarized in this note. The statements are presented in accordance with the guidance and requirements of the recently issued OMB Circular A-136, which incorporates and updates Bulletin 01-09, Form and Content of Agency Financial Statements, and the Government Management Reform Act of 1994. FY 2006 statements, previously prepared in accordance with the Government Corporation Control Act (31 U.S.C. §9106), have been reformatted and republished for Circular A-136 comparative purposes. FY 2006 financial statements also have been restated for comparative purposes to include Threshold program balances that were not reflected in a timely manner prior to final publication.

MCC accounting policies follow generally accepted accounting principles for the Federal Government, as recommended by the Federal Accounting Standards Advisory Board (FASAB). The FASAB has been recognized by the American Institute of Certified Public Accountants (AICPA) as the official accounting standard set for the Federal Government. These standards have been agreed to and published by the Director of OMB, Secretary of the Treasury, and Comptroller General.

MCC's principal financial statements are:

- Balance Sheets
- Statements of Budgetary Resources
- Statements of Net Cost
- Statements of Changes in Net Position

These notes are considered an integral part of the financial statements.

B. Reporting Entity

MCC was formed in January 2004 pursuant to the Millennium Challenge Act of 2003 (Public Law 108-199). MCC's mission is to reduce poverty by supporting sustainable, transformative economic growth in developing countries that create and maintain sound policy environments. The assistance is intended to provide economic growth and the elimination of extreme poverty, strengthen good governance, encourage economic freedom, and promote investments in people.

C. Budgets and Budgetary Accounting

MCC's programs and activities are funded through no-year appropriations. Such funds are available for obligation without fiscal year limitation and remain available until expended. MCC was provided total appropriations of almost $1.752 billion and $1.770 billion in FY 2007 and FY 2006, respectively. OMB apportions MCC administrative funds on an annual basis pursuant to statutory limitations in MCC's annual congressional appropriations. In addition, MCC receives from OMB a separate apportionment for due diligence funds, which MCC uses for compact evaluations and support, compact programs, 609(g) funds, the Threshold program, and audit funds. Because of the no-year status of MCC appropriations, unobligated administrative, audit, and due diligence funds (apportioned annually) are not returned to the Treasury; however, unobligated balances as of September 30 for these three categories of funds are transferred to the compact fund category at the beginning of the subsequent fiscal year for future use.

D. Basis of Accounting

Financial transactions are recorded on accrual and budgetary bases in accordance with pertinent federal accounting and financial reporting requirements. Under the accrual method of accounting, financing sources are recognized when used and expenses are recognized when incurred, without regard to receipt or payment of cash. Budgetary accounting facilitates MCC's compliance with legal constraints and controls over the use of federal funds.

The accompanying Balance Sheets, Statements of Net Cost, and Statements of Changes in Net Position have been prepared on the accrual basis. The Statements of Budgetary Resources have been prepared in accordance with budgetary accounting rules.

E. Fund Balance with Treasury

MCC does not maintain cash in commercial bank accounts. Rather, MCC's funds are maintained in Treasury accounts. The Department of the Treasury processes all cash receipts and disbursements for MCC. The Fund Balances with Treasury represent no-year funds, which are maintained in appropriated funds that are available to pay current and future commitments.

F. Advances to Others

MCC advances funds to eligible compact and pre-compact countries in order to implement compact projects in an MCA country or for Federal Government inter-agency agreements. Funds advanced to compact and pre-compact countries are used to pay legitimate costs and expenses incurred by MCC and partner countries. Advances at the end of FY 2007 and FY 2006 were $32.2 million and $18.9 million, respectively. Of the 21 MCC outstanding advances, four are greater than 180 days.

G. Accounts Payable

MCC records as liabilities all amounts due to others as a direct result of transactions or events that have occurred. Accounts payable represent amounts due to federal and non-federal entities for goods and services received by MCC, but not paid at the end of the accounting period. Accounts payable reported at the end of FY 2007 and 2006 were $39.2 million and $10.1 million, respectively. The increase in the Accounts Payable is attributable to an increase from $7.6 million in FY 2006 to $28.6 million in FY 2007 for USAID Threshold programs.

H. Actuarial FECA Liability

The Federal Employees' Compensation Act (FECA) provides income and medical cost protection to covered federal civilian employees injured on the job, employees who have incurred a work-related occupational disease, and beneficiaries of employees whose deaths are attributable to a job-related injury or occupational disease.

Claims incurred for benefits for MCC employees under FECA are administered by the Department of Labor (DOL) and later billed to MCC. MCC's actuarial liability for workers' compensation includes any costs incurred but unbilled as of year-end, as calculated by DOL, and not funded by current appropriations.

MCC incurred no FECA liabilities during FY 2007 and FY 2006.

I. Accrued Annual Leave

The value of employees' unused annual leave at the end of each fiscal quarter is accrued as a liability. At the end of each fiscal quarter, the balance in the accrued annual leave account is adjusted to reflect current pay rates and leave balances. Annual leave is funded from current appropriations. Sick leave and other types of non-vested leave are expensed when used, and in accordance with federal requirements no accruals are recorded for unused leave.

J. Net Position

Net position is composed of unexpended appropriations and cumulative results of operations. Unexpended appropriations are funds appropriated by Congress to MCC that are still available for expenditure at the end of the fiscal year. Cumulative results of operations represent the net differences between financing sources and expenses from MCC's inception.

K. Financing Sources

In accordance with Note 1.C, MCC funds its program and operating expenses through no-year appropriations. Appropriations are recognized as an accrual-based financing source at the time they are used to pay program or administrative expenses, except for expenses to be funded by future appropriations.

L. Retirement Benefits

MCC's employees participate in either the Civil Service Retirement System (CSRS) or the Federal Employees Retirement System (FERS). FERS was established by Public Law 99-335. Pursuant to this law, most U.S. Government employees hired after December 31, 1983, are covered by FERS and Social Security. Federal employees hired prior to January 1, 1984, were allowed to elect whether they desired to participate in FERS (with Social Security coverage) or remain in CSRS. For employees covered by CSRS, MCC contributes 7 percent of their gross pay toward their retirement benefits. For those employees covered by FERS, MCC contributes 11 percent of their gross pay toward retirement. Employees are also allowed to participate in the federal Thrift Savings Plan (TSP). For employees under FERS, MCC contributes an automatic 1 percent of basic pay to TSP and matches employee contributions up to an additional 4 percent of pay, for a maximum MCC contribution amounting to 5 percent of pay. Employees under CSRS may participate in the TSP, but will not receive either MCC's automatic or matching contributions.

For FY 2007, MCC has made contributions of $142,000 to CSRS, $2.4 million to FERS, and $849,000 to TSP. During FY 2006, MCC made retirement contributions of $761,000 to CSRS, $1.977 million to FERS, and $620,700 to TSP.

M. Use of Estimates

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of financing sources and expenses during the reporting period. Actual results could differ from such estimates.

N. Contingencies

MCC can be a party to various routine administrative proceedings, legal actions, and claims brought by or against it, including threatened or pending litigation involving labor relations claims, some of which may ultimately result in settlements or decisions against MCC. In the opinion of MCC's management and legal counsel, there are no proceedings, actions, or claims outstanding or threatened that would materially impact MCC's financial statements.

O. Judgment Fund

Certain legal matters to which MCC can be named as a party may be administered and, in some instances, litigated and paid by other federal agencies. In general, amounts paid in excess of $2,500 for Federal Tort Claims Act settlements or awards pertaining to these litigations are funded from a special appropriation administered by the Department of the Treasury called the Judgment Fund. Although the ultimate disposition of any potential Judgment Fund proceedings cannot be determined, management expects that any liability or expense that might ensue would not be material to MCC's financial statements.

P. Custodial Receivables and Liabilities

Under current policy and procedures, MCC funds all compacts and pre-compacts with countries by advancing funds on a monthly basis to cover projected needs. Such funds provided to the countries are required to be deposited in interest-bearing accounts, if legally feasible, until disbursed. The interest earned on these accounts is remitted to MCC and deposited into an account at the U.S. Treasury. Such interest may not be retained or used by MCC, but periodically is returned to the Treasury's general funds. MCC had outstanding advances related to compact and pre-compact financing of approximately $30.8 million and $18.8 million on September 30, 2007, and September 30, 2006, respectively. MCC received and deposited $1.65 million and $304,000 in interest remittances on September 30, 2007, and September 30, 2006, respectively.

Q. Donated Services

MCC may on occasion use donated services from other federal agencies and private firms in the course of business operations. The approximate fair market value of these donated services for September 30, 2007, was $123,750 and was $0 in FY 2006.

R. Transfers to Other Federal Agencies

MCC is a party to allocation transfers to other federal agencies as a transferring entity. Allocations are legal delegations by one agency of its authority to obligate budget authority and outlay funds to another agency. A separate fund account (child account) is created in the U.S. Treasury as a subset of the parent fund account for tracking and reporting purposes. All allocation transfers of budget authority are credited to this account, and subsequent obligations and outlays incurred by the child entity are charged to this allocation account as they execute the delegated activity on behalf of the parent entity.

All financial activity related to these allocations and transfers (e.g., budget authority, obligations, and outlays) is reported in the financial statements of the parent entity, from which the underlying legislative authority, appropriations, and budget appointments are derived. MCC allocates funds, as a parent agency, to USAID to administer designated MCC programs. In FY 2007 and FY 2006, MCC transferred budgetary authority of $161 million and $155 million, respectively, to USAID for Threshold programs.

Note 2—Fund Balance with Treasury

The U.S. Treasury accounts for all U.S. Government cash on an overall consolidated basis. The Fund Balance with Treasury (FBWT) line items on the Balance Sheets for September 30, 2007, and September 30, 2006, consisted of amounts presented in Exhibit 3-1. MCC funds its program and operating expenses through no-year appropriations; therefore, all unobligated balances as of September 30 are transferred to the compact fund category at the beginning of the subsequent fiscal year and are available for use in future years until fully expended.

Exhibit 3-1: Fund Balance with Treasury as of September 30 (in thousands)

	September 30, 2007	September 30, 2006
Appropriated Funds		
Unobligated	$2,261,383	$2,805,604
Obligated	3,287,907	1,273,053
Total	**$ 5,549,290**	**$ 4,078,657**

Note 3—Accounts Receivable, Net

Accounts receivable reflect overpayments of payroll, travel, and other MCC current/former employee expenses. MCC does not record an allowance for doubtful accounts because these expenses are deemed wholly collectible. Total receivables were $68,000 and $62,000 as of September 30, 2007, and September 30, 2006, respectively.

Note 4—General Property, Plant, and Equipment, Net

In March 2007, MCC revised its property capitalization threshold from an original cost of $25,000 or more and an estimated useful life of 2 or more years to an original cost of $50,000 or more and an estimated useful life of 5 or more years, except for its software capitalization (which was changed to an original cost of $200,000 or more and an estimated useful life of 5 or more years) and its information technology infrastructure capitalization (which was changed to an original cost of $200,000 or more and an estimated useful life of 3 or more years). These revisions reduce MCC's administrative costs associated with accounting for General Property, Plant, and Equipment (PP&E) and results in increased operational efficiency.

MCC changed its depreciation convention, converting from a half-year convention to a quarter-year convention. Assets are depreciated (or amortized) quarterly over their estimated useful lives using the straight-line depreciation method. This change resulted in additional depreciation expense of $181,638. As required by FASAB 21, the net effect of this change has been included in the FY 2007 cumulative results of operations and net position.

MCC's actual depreciation expense for FY 2007 is $860,061.

Note 5—Leases

MCC leases office space in two adjacent locations in Washington, D.C. These leases are on 10-year (Bowen Building) and 8-year (City Center) lease terms that terminate on May 25 and May 26, 2015, respectively (see Exhibit 3-2). MCC made significant leasehold improvements to the office space and amortizes the improvement based on the in-service (invoice) date of the improvement. Amortization is calculated on a quarterly basis. These leasehold improvements will be reflected as a Fixed Asset on MCC's Balance Sheets net of amortization.

Exhibit 3-2: Operating Leases (in dollars)

Future Payments Due			
Fiscal Year	**Bowen**	**City Center**	**Totals**
FY 2008	$5,394,621	$1,889,524	$7,284,145
FY 2009	5,394,621	1,889,524	7,284,145
FY 2010	6,352,911	1,889,524	8,242,435
FY 2011	6,352,911	1,942,376	8,295,287
FY 2012	6,352,911	1,942,376	8,295,287
After 5 Years	19,058,733	5,932,834	24,991,567
Total Future Lease Payments	**$48,906,708**	**$15,486,158**	**$64,392,866**

Note 6—Intra-Governmental Costs and Exchange Revenue

The Statements of Net Cost reports MCC's gross cost less earned revenues to arrive at net cost of operations. Costs have been illustrated by MCC specific programs (see Exhibit 3-3). The format of the Statements of Net Cost is also now consistent with OMB Circular A-136 guidance. Exhibit 3-3 shows the value of exchange transactions between MCC and other federal entities as well as non-federal entities. Intra-Governmental Costs relate to transactions between MCC and other federal entities. Public costs, on the other hand, relate to transactions between MCC and non-federal entities. MCC does not have any exchange revenues.

Exhibit 3-3: Intra-Governmental Costs and Exchange Revenue (in thousands)

	Compact	609(g)	Threshold	Due Diligence	Audit	Admin	September 30, 2007	September 30, 2006
Intra-Governmental	-	59	-	3,567	2,789	7,741	14,156	9,428
Public	81,079	17,113	75,766	29,223	77	70,181	273,439	98,992
Total–Program	81,079	17,172	75,766	32,790	2,866	77,922	287,595	108,420

Note 7—Adjustments to Beginning Balance of Budgetary Resources

In FY 2006, $17.7 million of amounts appropriated under the FY 2006 Foreign Operations, Export Financing, and Related Programs Appropriations Acts (Public Law 109-148) were rescinded. The rescission was part of the Across-the-Board Rescission enacted for FY 2006.

There were no adjustments to the FY 2007 beginning balances of Budgetary Resources.

Note 8—Explanation of Differences between the SBR and the Budget of the U.S. Government

MCC ensures that the information reported on its books is reflected within the Budget of the U.S. Government. Because MCC's financial statements are published before the President's Budget, this reconciliation is based on the Statements of Budgetary Resources for FY 2006 and the 2006 actual data reported in the President's 2008 budget submission. FY 2007 actual data will be published in February 2008 within the 2009 Budget of the United States. Material differences reported in the Budgetary Resources column ($2.053 billion) represent unobligated balances reported on MCC's SBR and SF 133, but not in the Budget of the U.S. Government. Material differences reported in the Total Outlays column represent SF 133 outlays reported by USAID in FY 2006 that were not reported timely to MCC to present in its FY 2006 financial statements (See Exhibit 3-4).

Exhibit 3-4: Material Differences Between the SBR and the President's Budget (in millions)

	Budgetary Resources	Obligations Incurred	Distributed Offsetting Receipts	Net Outlays
Statements of Budgetary Resources	3,806	1,109		109
Unobligated Balance Carry Forward from FY 2005	(2,053)			
Unreported Outlays				2
Budget of the U.S. Government	1,753		1	111

Note 9—Undelivered Orders at the End of the Period

The reported net position consists of unexpended appropriations and cumulative results of operations, which reflects the difference between financing sources and expenses since MCC's inception. Exhibit 3-5 represents undelivered orders—unpaid for compact and 609(g) funds as of September 30, 2007 and September 30, 2006.

Exhibit 3-5: Undelivered Orders—Compact and 609(g) Funds (in dollars)

Undelivered Orders	2007	Compacts	609(g) Funding	2006
Armenia	$227,716,911	$227,716,911	$-	$235,646,174
Benin	293,870,370	293,870,370	-	1,062,985
Cape Verde	96,151,990	96,147,871	4,119	106,077,520
El Salvador	458,715,779	458,715,779	-	-
Georgia	265,875,250	264,656,190	1,219,060	296,178,084
Ghana	538,097,271	537,668,659	428,612	13,584,891
Honduras	204,027,319	204,027,319	-	213,166,147
Kenya	25,000	25,000	-	-
Lesotho	16,078,147	15,668,416	409,731	902,934
Madagascar	87,042,735	87,042,735	-	103,290,130
Mali	462,993,330	458,630,248	4,363,082	4,421,534
Morocco	32,400,000	32,400,000	-	-
Mozambique	31,254,763	25,346,200	5,908,563	12,956,078
Nicaragua	165,314,884	165,314,884	-	173,583,320
Senegal	1,930,524	-	1,930,524	4,882,237
Tanzania	9,800,000	-	9,800,000	-
Vanuatu	63,683,392	63,683,392	-	65,214,603
Total–Undelivered Orders	**$2,954,977,665**	**$2,930,913,974**	**$24,063,691**	**$1,230,966,637**

Note 10—Reconciliation of Net Cost of Operations to Budget

Exhibit 3-6 reconciles the FY 2007 resources available to MCC to finance operations with the net cost of operating MCC's programs. Some operating costs, such as depreciation, do not require direct financing sources. This exhibit illustrates the reconciliation of Net Cost of Operations to Budget.

Exhibit 3-6: Reconciliation of Net Cost of Operations to Budget (in dollars)

Resources Used to Finance Activities		Program Costs	
Budgetary Resources Obligated			
Net obligations	$2,189,975,151	**Gross Costs**	$287,595,725
Net other resources used to finance activities	1,936,792		
Total resources used to finance activities	2,191,911,943		
Total resources used to finance items not part of the net cost of operations	(1,905,176,279)	**Less: Earned Revenue**	-
Total resources used to finance the net cost of operations	286,735,664		
Total components of net cost of operations that will not require or generate resources	860,061		
Net Cost of Operations	**$ 287,595,725**	**Net Cost of Operations**	**$287,595,725**

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4. AUDIT OF THE MILLENNIUM CHALLENGE CORPORATION'S FINANCIAL STATEMENTS, INTERNAL CONTROLS, AND COMPLIANCE FOR THE PERIOD ENDING SEPTEMBER 30, 2007 AND 2006 REPORT NO. M-000-08-001-C

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Office of Inspector General
for the
Millennium Challenge Corporation

November 9, 2007

The Honorable John J. Danilovich
Chief Executive Officer
Millennium Challenge Corporation
875 15th Street, NW
Washington, DC 20005-2203

Subject: Audit of the Millennium Challenge Corporation's Financial Statements, Internal Controls, and Compliance for the Period Ending September 30, 2007 and 2006
Report No. M-000-08-001-C

Dear Mr. Ambassador:

Enclosed is the final report on the subject audit. The Office of Inspector General (OIG) contracted with the independent certified public accounting firm of Williams Adley & Company, LLP to audit the financial statements of the Millennium Challenge Corporation (MCC) for the period ending September 30, 2007. The contract required that the audit be performed in accordance with United States Generally Accepted Government Auditing Standards, Office of Management and Budget (OMB) Bulletin 07-04, *Audit Requirements for Federal Financial Statements,* and the GAO/PCIE *Financial Audit Manual.*

In its audit of the MCC's financial statements for the period ending September 30, 2007 the auditors found:

- The financial statements were fairly presented in conformity with U.S. Generally Accepted Accounting Principals.

- MCC's internal controls over financial reporting and its operation contained two significant deficiencies. These significant deficiencies are material weaknesses.

- MCC had two instances of material noncompliance with laws and regulations.

The material weaknesses identified in MCC's internal controls process increases MCC's need to develop written policies and procedures to streamline its financial operations. Under current operating procedures, the material weaknesses increase the risk of improper recording, unauthorized transactions, omissions, potential funds control violations and noncompliance with laws, regulations, contracts and grant agreements. Williams Adley & Company, LLP reported the following internal control weaknesses:

1. MCC did not sufficiently execute its monitoring functions related to advances.

2. MCC lacks written policies and procedures related to financial reporting accountability and document control.

Williams Adley & Company, LLP also reported instances of noncompliance with laws, regulations, contracts, and grant agreements, inclusive of those referred to in the Federal Financial Management Improvement Act of 1996 (FFMIA) and disclosed instances of noncompliance or other matters that are required to be reported under Government Auditing Standards, issued by the Comptroller General of the United States, and OMB Bulletin 07-04, *Audit Requirements for Federal Financial Statements.* The instances of noncompliance are:

1. MCC did not fully comply with FFMIA (material noncompliance).

2. MCC did not fully comply with the Federal Information Security Management Act (FISMA) (material noncompliance).

In carrying out its oversight responsibilities, the OIG reviewed Williams Adley & Company, LLP's report and related audit documentation. This review, as differentiated from an audit in accordance with U.S. Generally Accepted Government Auditing Standards, was not intended to enable the OIG to express, and we do not express, opinions on MCC's financial statements, or internal control; on whether MCC's financial management systems substantially complied with FFMIA; or on MCC's compliance with other laws and regulations. Williams Adley & Company, LLP is responsible for the attached auditor's report, dated October 23, 2007, and the conclusions expressed in the report. However, our review disclosed no instances that Williams Adley & Company, LLP did not comply, in all material respects, with applicable standards.

To address the internal control weaknesses and the noncompliance findings reported by Williams Adley & Company, LLP, we are making the following recommendations to MCC's management:

Recommendation No. 1: We recommend that the Millennium Challenge Corporation's management:

1.1. Implement a policy that reduces outstanding advances based on the First-in, First-out (FIFO) method.

1.2. Implement the common payment system for all MCAs on a more aggressive timeline.

1.3. Make payments in accordance with the monthly schedule, and if a payment is held, consider the need for it to be disbursed at all.

1.4. Ensure that there is a more rigorous review of advance requests including an assessment of outstanding advances.

Recommendation No. 2: We recommend that the Millennium Challenge Corporation management:

2.1. Formally document the MCC accountability for ensuring MCA compliance with the reporting provisions.

2.2. Implement document retention policies that include standards for version control and a central repository for documents that are used by multiple MCC units.

2.3. Continue with the planned implementation of the BIDS project and ensure that information is validated prior to inclusion in the new system.

Recommendation No. 3: We recommend that management continue to assess the automated options available to handle the Millennium Challenge Corporation 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 processing of financial transactions, and decrease the risk of errors.

In finalizing the report, we received and considered MCC's response to the draft report and the recommendations included therein. In its comments, MCC was generally responsive; however, the corporation did not provide estimated implementation dates for corrective action on recommendations 1 and 3.

Please provide revised management decisions for recommendations 1 and 3, and inform us when you have taken final action on recommendation number 2.

The OIG appreciates the cooperation and courtesies extended to our staff and to the staff of Williams Adley & Company, LLP during the audit. Please contact me or Richard J. Taylor, Director, Financial Audits Division, at (202) 216-6963, if you have any questions concerning this report.

Sincerely,

/s/
John M. Phee
Assistant Inspector General
Millennium Challenge Corporation

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Williams, Adley & Company, LLP
Certified Public Accountants/Financial Management Consultants

Independent Auditors' Report

Inspector General
United States Agency for International Development

Board of Directors
Millennium Challenge Corporation

We have audited the accompanying Balance Sheets of the Millennium Challenge Corporation (MCC or Corporation) as of September 30, 2007 and 2006 and the related Statements of Net Costs, Changes in Net Position, and Budgetary Resources for the year ended September 30, 2007 and 2006. These financial statements are the responsibility of Corporation management. Our responsibility is to express an opinion on these financial statements based on our audit.

In the prior fiscal year MCC prepared their financial statements in accordance with the requirements of the Government Corporation Control Act and the OMB Circular A-136 requirement for 45 day reporting. In fiscal year 2007 MCC decided to early adopt all requirements of OMB Circular A-136, as permitted by the Circular. The requirements resulted in a change in the financial statements presented by the Corporation. The fiscal year 2006 information has been formatted in accordance with the new presentation.

In connection with our audit, we also considered the MCC's internal control over financial reporting and tested the MCC's compliance with certain provisions of applicable laws, regulations, contracts and grant agreements that could have a direct and material effect on the financial statements.

SUMMARY

As stated in our opinion, we concluded that the MCC's financial statements as of and for the year ended September 30, 2007 and 2006 are presented fairly, in all material respects, in conformity with accounting principles generally accepted in the United States of America.

Our consideration of internal control over financial reporting and its operation resulted in two matters that we consider to be significant deficiencies. We believe that these significant deficiencies are material weaknesses.

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1. ***MCC Did Not Sufficiently Execute Its Monitoring Functions Related to Advances***

2. ***MCC Lacks Written Policies and Procedures Related to Financial Reporting Accountability and Document Control***

The results of our tests of compliance with certain provisions of laws, regulations, contracts, and grant agreements, inclusive of those referred to in the *Federal Financial Management Improvement Act of 1996* (FFMIA), disclosed two instances of noncompliance or other matters that are required to be reported herein under *Government Auditing Standards*, issued by the Comptroller General of the United States, and Office of Management and Budget (OMB) Bulletin No. 07-04, *Audit Requirements for Federal Financial Statements*:

3. ***MCC did not fully comply with FFMIA (material noncompliance)***

4. ***MCC did not fully comply with Federal Information Security Management Act (material noncompliance)***

The following sections discuss our opinion on the MCC's financial statements, our consideration of the MCC's internal control over financial reporting, our tests of the MCC's compliance with certain provisions of applicable laws, regulations, contracts, and grant agreements, and the distribution of our report. The status of prior year findings is included as Appendix A. Management's response to the findings and our evaluation of said response is included as Appendix C and Appendix B, respectively. We noted other matters that were communicated to management in a separate letter.

OPINION ON THE FINANCIAL STATEMENTS

We have audited the accompanying Balance Sheets of the Corporation as of September 30, 2007 and 2006, and the related Statements of Net Costs, Changes in Net Position, and Budgetary Resources for the year ended September 30, 2007 and 2006. These financial statements are the responsibility of Corporation management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and standards applicable to financial statement audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, and the Office of Management and Budget (OMB) Bulletin No. 07-04, *Audit Requirements for Federal Financial Statements.* Those standards require that we plan and perform the audit to obtain reasonable assurance that the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In the prior fiscal year MCC prepared their financial statements in accordance with the requirements of the Government Corporation Control Act and the OMB Circular A-136 requirement for 45 day reporting. In fiscal year 2007 MCC decided to early adopt all requirements of OMB Circular A-136, as permitted by the Circular. The requirements resulted in a change in the financial statements presented by the Corporation. The fiscal year 2006 information has been formatted in accordance with the new presentation.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial positions of the Corporation as of September 30, 2007 and 2006, and changes in net position, net costs, and budgetary resources for the years ended September 30, 2007 and 2006, in conformity with accounting principles generally accepted in the United States of America.

Our audit was made for the purpose of forming an opinion on the basic financial statements of the Corporation taken as a whole. The information contained in the Management's Discussion and Analysis and Performance Section is not a required part of the financial statements, but is supplementary information required by the Federal Accounting Standards Advisory Board guidance. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the information. However, we did not audit the information and do not express an opinion thereon.

INTERNAL CONTROL OVER FINANCIAL REPORTING

In planning and performing our fiscal year 2007 audit, we considered MCC's internal control over financial reporting by obtaining an understanding of MCC's internal control, determined whether internal controls had been placed into operation, assessed control risk, and performed tests of controls in order to determine our auditing procedures for the purpose of expressing an opinion on the financial statements. We limited our internal control testing to those controls necessary to achieve the objectives described in OMB Bulletin No. 07-04 and *Government Auditing Standards*. We did not test all internal controls relevant to operating objectives as broadly defined by the *Federal Managers' Financial Integrity Act of 1982* (FMFIA), such as those controls relevant to ensuring efficient operations. The objective of our audit was not to provide assurance on internal control; accordingly, we do not provide an opinion on internal control.

Our consideration of internal control over financial reporting would not necessarily disclose all matters that might be reportable conditions. Under standards issued by the American Institute of Certified Public Accountants, significant deficiencies are matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect MCC's ability to record, process, summarize, and report financial data consistent with the assertions by management in the financial statements.

Material weaknesses are significant deficiencies in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements, in amounts that would be material in relation to the financial statements being audited, may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Because of inherent limitations in internal controls, misstatements, losses or noncompliance may occur and not be detected.

We noted two matters involving the internal control over financial reporting and its operation that we consider to be significant deficiencies. We believe that these significant deficiencies are material weaknesses. We noted other matters that were communicated to management in a separate letter.

MATERIAL WEAKNESSES

MCC Did Not Sufficiently Execute Its Monitoring Functions Related to Advances

Condition:

MCC entered into various compacts and provided several advances during fiscal year 2007. MCC personnel indicated that monthly disbursements were made based upon the quarterly disbursement requests. Current policies and procedures require that the disbursement requests are reviewed by several organizations within MCC for reasonableness, accuracy and need. Also, MCC personnel indicated that advances are generally liquidated within approximately 180 days using the quarterly financial reports provided by the Millennium Challenge Accounts (MCAs). The current policy requires that outstanding advances are liquidated within the Oracle Federal Financial System on the First-in First-out (FIFO) basis. However, we noted the following:

1. Several advances were not liquidated within 180 days (see chart below).

2. Advances were not always liquidated on the FIFO basis. For example, we noted that although Georgia had an advance for $255,713 outstanding for 541 days, re-disbursements equaling $6,477,332 were posted against an advance that was 348 days outstanding instead. Additionally, we noted that Ghana had advances totaling $3,065,233 outstanding for 290 days or greater, however, re-disbursements totaling $685,738 were posted against an advance outstanding for 207 days.

3. MCAs were granted additional funds in spite of open advances that were outstanding for 180 days or greater. We noted that Madagascar had outstanding advances totaling $13,790,783 as of June 30, 2007, with re-disbursements posted of $2,467,082, and received additional advances of $1,110,762 for August and $3,663,616 for September.

4. We noted that monthly tranches were not always issued properly. Three MCAs received two months of advances within one month. We noted that El Salvador received $1,361,939 and $364,347 on August 1, 2007 for the months of July and

August; and Georgia received $3,655,620 and $3,500,000 on June 29, 2007 for the months of March and June.

5. The fourth quarter financial reports indicated that four MCAs had cash on hand of greater than 30 days cash needs as evidenced by no disbursement requested until the second month of the quarter or in one instance no disbursement was requested for the entire quarter.

Country	Date of Disbursement	Amount of Disbursement	Amount Remaining as of 9/30/07	Days Outstanding
Benin	8/31/2007	$1,531,951	$556,849	264
Georgia	2/26/2007	$10,913,824	$5,966,180	348
Ghana	6/14/2007	$863,315	$299,414	294
	3/7/2007	$55,620	$55,620	207

Also, in our review of the outstanding advances we noted that interagency advances to the Department of Treasury of $1,611,899 and U.S. Agency for International Development (USAID) of $120,000 were over 365 days outstanding.

The Department of the Treasury's Financial Management Service publications did not envision the inclusion of sovereign governments; however, in the analysis of cash management, we used the Treasury Financial Manual (TFM) as a valuable source of sound business practices. The TFM is the Department of the Treasury's official publication for financial accounting and reporting of all receipts and disbursements of the Federal Government. The purpose of the TFM is to provide policies, procedures, and instructions for Federal departments and agencies to follow in carrying out their fiscal responsibilities.

Also, through various OMB Circulars, OMB has attempted to address the need for advances to cover immediate cash needs or timely disbursements of an entity for direct program costs for carrying out the purpose of the approved program or project. Thus, funds paid to a grantee are not to be held, but are to be promptly applied to the grant purpose. Although the timeframe for immediate cash needs has not been clearly defined by OMB, the general rules employed by various Federal agencies are 30 days for non-governmental entities as outlined in the TFM. Based upon this definition, MCC has provided Federal funds in excess of immediate cash needs.

Criteria:

Per the Appropriations Law Volume II, advances under an assistance program are intended to accomplish the program purposes and not to profit the recipient other than in the manner and extent specified in the program. Section 2025 of The Treasury Financial Manual –Volume 1, Part 6-Chapter 2000, states that advances to a recipient organization will be limited to the minimum amounts necessary for immediate disbursement needs and will be timed to be in accord only with the actual immediate cash requirements of the recipient organization in carrying out the purpose of an approved program or project. The timing and amount of cash advances will be as close as is administratively feasible to actual disbursements by the recipient organization.

Best business practice defines immediate cash needs as money used for the purpose of carrying out the Compact's approved programs within a thirty day period. Also, when funds are drawn from Treasury before it is needed, or in excess of current needs, the government loses the use of the funds.

Cause:

Although, MCC's management has changed the advance issuance and monitoring policies and procedures, several aspects of advance monitoring have not been effectively implemented. The review of the advance requests related to immediate cash needs and outstanding advances currently performed is inadequate.

Effect:

The lack of effective advance monitoring has lead to excess cash on hand and increasing amounts of interest remitted from FY 2006 ($304,000) to FY 2007 ($1,624,762). Not using the FIFO method to liquidate the advances distorts the aging of outstanding advances and provides inaccuracies in the data.

Recommendation # 07-01:

We recommend that MCC management:

(1) Implement a policy that truly reduces outstanding advances based on the FIFO method;
(2) Implement the common payment system for all MCAs of a more aggressive timeline;
(3) Make payments in accordance with the monthly schedule and if a payment is held consider the need for it to be disbursed at all; and
(4) Management should ensure that there is a more rigorous review of advance requests including an assessment of outstanding advances.

MCC Lacks Written Policies and Procedures Related to Financial Reporting Accountability and Document Control

Condition:

In performing our analysis of compact expenses and advances, we requested supporting documentation of approved disbursement requests and final quarterly financial reports (QFR) by country for FY 2007. MCC's Department of Administration and Finance was hampered in addressing our request in a timely manner because of the lack of a centralized data/document repository. Also, MCC does not have adequate version control over the documents to ensure that the final documents are maintained in a manner that is accessible to all MCC employees requiring information.

During FY 2007, MCC disbursed over $82 million to compact countries who in turn reported approximately $72 million in expenses on their quarterly reports. The disbursement requests and quarterly reports are essential to ensuring that expenses and advances are accurately reported in the proper period. MCC has policies and procedures for processing and clearing the disbursement requests and quarterly financial reports that are received from the MCAs. The MCA is required to submit the QFR by the 10^{th} day of the third month of the quarter. The remaining 20 days of the month are used by MCC to process and clear the reports through various MCC departments including the country teams, legal, Fiscal Accountability, and Department of Administration and Finance. However, MCC does not have written policies and procedures related to the non-receipt of the QFR and identification of the accountable person(s) for ensuring compliance and notification.

MCC has decided to invest in an enterprise information system that will serve as a central repository for the documentation related to the various countries supported by the MCC. The projected implementation of the system is the third quarter of FY 2008.

Criteria:

The GAO *Standards for Internal Control in the Federal Government* states that internal control and all transactions and other significant events need to be clearly documented and the documentation should be readily available for examination. Also, information should be recorded and communicated to management and others within the entity who need it and in a form and within a timeframe that enables them to carry out their internal control and other responsibilities.

OMB Circular A-127 "*Policies and Standards for Financial Management Systems*" states that financial management in the Federal government requires accountability of financial and program managers for financial results of actions taken, control over the Federal government's financial resources and protection of Federal assets. To enable these requirements to be met, financial management systems must be in place to process and record financial events effectively and efficiently, and to provide complete, timely, reliable and consistent information for decision makers and the public.

Additionally, management and employees should establish and maintain an environment throughout the organization that sets a positive and supportive attitude toward internal control and conscientious management. A positive control environment is the foundation for all other standards. It provides discipline and structure as well as the climate which influences the quality of internal controls.

Cause:

The country teams and specifically, the program officer, are responsible for ensuring that quarterly financial reports are received from each country in accordance with the timeline established. However, the written roles and responsibilities of the position and operational area do not include the accountability for these reports and provision for a centralized repository. Also, MCC has not established document retention standards that include document versioning controls. Additionally, MCC believes that because the agreements require the submission of the reports and funds cannot be disbursed to the MCA without current reports on file, the possibility of nonsubmission is nonexistent. However, if the MCA has sufficient funds on hand and thus does not require a disbursement, the incentive to provide timely reporting decreases.

Effect:

If compact expenses are not recorded timely and accurately based upon approved documentation, the MCC financial reporting and financial statements will be inaccurate and MCC management's ability to rely on the financial statements to make informed decisions will be impaired. As the number of compact countries and amounts of funds disbursed increases, the ability to maintain documentation and report accurately and timely becomes increasingly more important to the effective and efficient running of MCC operations.

Also, operating efficiency is reduced because the lack of centralized records causes people to keep their own set of records because they can not rely on information being available when needed. Specifically, it has required the Department of Administration and Finance to expend additional efforts to track down the required reports for recording in the accounting system and providing to the auditors. The lack of version control and central repository also affects other reports and documentation required from the various countries including performance reports, monitoring and evaluations plans, etc. Currently, the 9 compacts that are in force require 4 QFRs, at least 4 disbursement requests, and 2 performance reports on an annual basis. Also, countries receiving Compact Implementation Funds (CIF) and 609g funds required to submit quarterly QFRs. Additionally, there are untold draft versions of these same reports. If you multiply these reports by the additional countries that will be reporting in the future, the proper controls over documentation become increasingly critical to effective data management.

Recommendation # 07-02:

We recommend that MCC management:

(1) Formally document the MCC accountability for ensuring MCA compliance with the reporting provisions;
(2) Implement document retention policies that include standards for version control and a central repository for documents that are used by multiple MCC units; and

(3) Continue with the planned implementation of the Business Intelligence and Data Storage (BIDS) and ensure that information is validated prior to inclusion in the new system.

The status of prior year's findings is provided in Appendix A. Management's response in its entirety is included in Appendix C.

As required by OMB Bulletin No. 07-04, with respect to internal controls related to performance measures determined by management to be key and reported in the Management's Discussion and Analysis, we obtained an understanding of the design of significant internal controls relating to the existence and completeness assertions. Our procedures were not designed to provide assurance on internal control over performance measures and, accordingly, we do not provide an opinion thereon.

COMPLIANCE WITH LAWS AND REGULATIONS

MCC's management is responsible for complying with laws and regulations applicable to MCC. As part of obtaining reasonable assurance that MCC's balance sheet is free of material misstatements, we performed tests of its compliance with certain provisions of laws and regulations, noncompliance with which could have a direct and material effect on the determination of financial statement amounts, and certain other laws and regulations specified in OMB Bulletin No. 07-04, including the requirements referred to in the FFMIA. We limited our tests of compliance to these provisions and we did not test compliance with all laws, regulations, contracts, and agreements applicable to MCC. Providing an opinion on compliance with laws, regulations, contracts, and grant agreements was not an objective of our audit and, accordingly, we do not express such an opinion.

Under OMB Bulletin No. 06-03 and FFMIA, we are required to report whether MCC's financial management systems substantially comply with: (1) Federal financial management systems requirements, (2) applicable Federal accounting standards, and (3) the United States Government Standard General Ledger at the transaction level. To meet this requirement, we relied on the results of a SAS 70 review of the Department of Interior's Oracle Federal Financial System performed by an Independent Audit Firm. The results of that review have been presented to MCC in a separate report. Providing an opinion on compliance with those provisions was not, however, an objective of our audit and, accordingly, we do not express such an opinion.

The results of our tests disclosed that the Corporation did not fully comply with the FFMIA, which is required to be reported under *Government Auditing Standards* or OMB Bulletin No. 06-03.

Under FFMIA, we are required to report whether the Corporation's financial management systems substantially comply with the Federal financial management systems requirements, applicable Federal accounting standards, and the United States Government Standard

General Ledger at the transaction level. To meet this requirement, we performed tests of compliance with FFMIA section 803(a) requirements.

The results of our tests disclosed two instances of noncompliance with laws and regulations.

MATERIAL NONCOMPLIANCE

MCC Does Not Fully Comply With The Federal Financial Management Improvement Act

Condition:

Millennium Challenge Corporation (MCC) systems do not comply with the Federal Financial Management Improvement Act (FFMIA). The FFMIA requires an integrated financial management system. MCC does not have an integrated financial management system. MCC has multiple incompatible systems that cannot exchange data electronically, i.e. E-Travel and Federal Personnel/Payroll System (FPPS). The entry of the travel expenses and disbursements must be done manually. The entry of obligations and commitments requires a process of manual entry into Oracle Federal Financial (OFF). The payroll expenses and disbursements must be uploaded into OFF from FPPS.

During FY 2007, the Department of Accounting and Finance (A&F) traveled to NBC's Headquarters to perform testing of the interface between E-travel and OFF. A&F tested the interface based on 17 different employee travel scenarios, and noted that only five standard scenarios processed through both E-travel and OFF successfully.

Criteria:

The FFMIA requires MCC to implement and maintain a financial management system that complies substantially with Federal requirements for an integrated financial management system.

Cause:

The MCC does not have its own financial system. The Corporation has contracted with NBC to provide accounting and IT services including usage of its OFF application. The MCC is required by government regulations to use Federal Centers of Excellence of which NBC is one. According to MCC officials the Corporation has been directed to use the systems available through NBC. MCC believes that in fiscal year 2007 it used the only options available. NBC is working with MCC to provide enhancement to the system to accommodate MCC needs within the context of the OMB requirements for Centers of Excellence.

Effect:

The financial systems may not provide users with complete, accurate, timely financial information needed for decision-making purposes because of the inefficiencies caused by the manual processes.

Recommendation # 07-03:

We recommend that management continue to 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 processing of financial transactions; and decrease the risk of errors.

MCC Does Not Fully Comply With The Federal Information Security Management Act (FISMA)

An OIG audit identified significant non-compliance with FISMA requirements. Also, MCC engaged an outside expert to perform an independent security audit. MCC acknowledged that it had not met the majority of the FISMA requirements and proposed a timetable for compliance.

We are reporting this deficiency as required by the guidance issued by the Office of Management and Budget. However, because this deficiency was addressed in a prior OIG audit report, we are not making any recommendations in this report.

DISTRIBUTION

This audit was performed pursuant to the Government Corporation Control Act, OMB Circular A-136, and is intended solely for the information and use of the United States Congress, the President, the Director of the Office of Management and Budget, Comptroller General of the United States, the Corporation and its Inspector General, and is not intended to be, and should not be, used by anyone other than these specific parties.

Williams, Adley & Company, LLP /s/
October 23, 2007
Washington, D.C.

STATUS OF PRIOR YEAR FINDINGS

MCC Does Not Fully Comply with The Federal Information Security Management Act (FISMA)

In a report issued June 2005, an OIG audit identified significant non-compliance with FISMA requirements. Subsequently, MCC completed its FISMA report to OMB as of September 30, 2005, where it acknowledged that it had not met the majority of the FISMA requirements and proposed a timetable for compliance.

We are reporting this deficiency, as required by the guidance issued by the Office of Management and Budget. However, because this deficiency was addressed in a prior OIG audit report, we are not making any recommendation in this report.

The OIG continues to report significant noncompliances with FISMA requirements in fiscal year 2006 and 2007.

MCC's Policies and Procedures Were Not Always Complete and Consistent (material weakness)

During fiscal year (FY) 2006, the Millennium Challenge Corporation (MCC) used various processes to address the financial aspects of its operations. These processes evolved during the year as the organization grew in both number of personnel and span of operations. However, during this growth, the development and implementation of final written policies and procedures to guide MCC's streamlined operational structure was not adequately addressed. During the fiscal year, MCC lacked final written policies and procedures. Written policies and procedures must be in place to ensure operational efficiencies, risk reduction, and consistent application. Several policies and procedures, i.e. advances, budget, and accruals, remained in draft form, throughout the year. Additionally, several procedures do not address the responsible positions at the various control levels for the processing of data/data entry functions, or submission and approval levels and procedures in the areas of fixed assets and the open obligations review required revision.

While the current Department of Administration and Finance (A&F) management team has emphasized the preparation and issuance of a comprehensive financial management policies and procedures (FMPP) manual, as of the end of the FY, such a manual was being drafted. MCC has hired contractors to assist in the production of the FMPP manual by December 31, 2006.

Recommendation #06-01:

We recommend that Millennium Challenge Corporation's Department of Administration and Finance complete the Financial Management Policies and Procedures (FMPP) manual and implement the written policies and procedures for all areas that result in a financial event.

Status:

The Department of Administration and Finance completed the FMPP manual in March 2007. It was implemented and also updated in August 2007.

MCC Policies for Disbursing Advances to Grantees Do Not Accommodate Effective Cash Management (material weakness and noncompliance)

Condition:

MCC entered into various compacts and provided several advances during fiscal year 2006. MCC personnel indicated that monthly disbursements were made based upon the quarterly request. However, we noted that for most Millennium Challenge Authorities (MCAs), MCC disbursed funds on a quarterly basis based upon the disbursement request, rather than monthly. We noted that several disbursements were not used within 30 days nor the quarter.

Country	Date of Disbursement	Amount of Disbursement	Projected Cash Balance at September 30, 2006	Date when disbursement was completely expended
Madagascar	July 28, 2005	$ 2,500,924	-	March 30, 2006
	December 13, 2005	$ 1,755,506	-	June 30, 2006
	May 31, 2006	$ 5,391,665	$2,311,342	Not expected to be expended by September 30, 2006
Georgia	May 2, 2006	$ 3,603,404	$221,594	Not expected to be expended by September 30, 2006
	September 15, 2006	$6,509,706	6,509,706	
Honduras	February 28, 2006	$ 1,646,545	$138,840	Not expected to be expended by September 30, 2006
	September 29, 2006	$1,369,849	$1,369,849	
Cape Verde	February 1, 2006	$ 7,526,864	$3,913,663	Not expected to be expended by September 30, 2006
Vanuatu	June 30, 2006	$ 1,127,055	$1,023,658	Not expected to be expended by September 30, 2006
	August 9, 2006	$ 219,504	$219,504	
	September 6, 2006	$ 111,688	$111,688	
	September 18, 2006	$ 116,377	$116,377	
Nicaragua	June 30, 2006	$ 1,483,399	433,889	Not expected to be expended by
	August 28, 2006	$ 378,550	378,550	

Country	Date of Disbursement	Amount of Disbursement	Projected Cash Balance at September 30, 2006	Date when disbursement was completely expended
	August 31, 2006	$ 289,110	289,110	September 30, 2006

The Department of the Treasury's Financial Management Service publications did not envision the inclusion of sovereign governments; however, in the analysis of cash management, we used the Treasury Financial Manual (TFM) as a valuable source of sound business practices. The TFM is the Department of the Treasury's official publication for financial accounting and reporting of all receipts and disbursements of the Federal Government. The purpose of the TFM is to provide policies, procedures, and instructions for Federal departments and agencies to follow in carrying out their fiscal responsibilities.

Also, through various OMB Circulars, OMB has attempted to address the need for advances to cover immediate cash needs or timely disbursements of an entity for direct program costs for carrying out the purpose of the approved program or project. Thus, funds paid to a grantee are not to be held, but are to be promptly applied to the grant purpose. Although the timeframe for immediate cash needs has not been clearly defined by OMB, the general rules employed by various Federal agencies are 30 days for non-governmental entities as outlined in the TFM. Based upon this definition, MCC has provided Federal funds in excess of immediate cash needs.

Recommendation # 06-02:

We recommend that Millennium Challenge Corporation:

1) Develop and implement policies and procedures to ensure that the payment schedules and other agreements entered into with grantees are reflective of the U.S. Treasury requirements concerning advances and immediate cash needs.
2) Develop and implement policies and procedures to ensure that all disbursement requests from the accountable entity of the recipient countries follow the official format that documents the cash requirements for each month of the quarterly period.
3) Make and document all payments to the recipient countries on a monthly basis instead of a quarterly basis.
4) Establish and implement 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.

Status:

The Millennium Challenge Corporation developed and implemented policies and procedures reflective of the GAO policy based on an evaluation of what was needed to meet grant purposes in any given quarter, through the funds will be released in tranches on a monthly schedule. The MCAs submit quarterly financial reports that include disbursement requests. The disbursement requests provide a monthly schedule of cash needs that NBC and the

Division of Finance follow to issue the disbursements. DF and The National Business Center (NBC) have implemented controls and review procedures to ensure quarterly disbursement requests and subsequent monthly disbursements comply with policies and procedures per the FMPP. Disbursements are recorded when issued and expenses are recorded on a quarterly basis based upon the financial reports received from the MCA. The interest receipts are recorded in the general ledger by NBC.

MCC Does Not Have a Property Management System (material weakness)

We noted that MCC reported $5,656,567 in property as of June 30, 2006; however, they were unable to provide detailed records to support the amount reported. The MCC does not have a property management system that provides detail information on original cost, date of purchase, location, useful life, depreciation, and accumulated depreciation.

For the year end financial statements, sufficient analysis was performed to ensure consistent application of the capitalization policy and to determine an appropriate measure of depreciation expense to ensure that fixed assets would be fairly stated.

Recommendation #06-03:

We recommend that Millennium Challenge Corporation develop and maintain appropriate fixed asset records to ensure accurate reporting and physical control.

Status:

MCC implemented new property policies and procedures in FY 2007. MCC with the assistance of a contractor conducted an inventory and reconciled it to the general ledger. Also, MCC established fixed asset records and computed and recorded depreciation expenses during the year.

MCC Did Not Properly Record Compact Expenses During the Fiscal Year (material weakness)

As a result of our review of the third quarter financial statements, we noted that MCC did not report any compact program costs. Although MCC had received disbursement requests that can be used to post the expenses incurred, nothing was recorded. According to the compact and disbursement agreement, each MCA is required to submit quarterly disbursement requests that include the expenses incurred to date. These requests are due regardless of the need for funding. The requests should provide the following:

- Previous quarter advances;
- Previous quarter disbursements;
- Estimated expenses; and
- Next quarter's advance request.

For the year end financial statements, MCC recorded compact expenses of $8,493,394. Additional analysis was performed utilizing the disbursement requests to increase expenses recorded and to ensure that advances and compact expenses were fairly stated.

Recommendation #06-04:

We recommend that Millennium Challenge Corporation's management:

(1) Require that the final quarterly request received from the accountable entity of the recipient countries be made available to the Department of Administration and Finance and the Fiscal Accountability Office.

(2) Develop and implement policies and procedures that ensure compact expenses are properly and accurately recorded and reported on a quarterly basis

(3) Implement written procedures requiring that appropriate and timely follow-up measures are performed and are recorded for historical reference on incomplete, outstanding, or late disbursement requests.

(4) Develop and implement policies and procedures that require the Department of Administration and Finance to perform a thorough review of the financial statements to ensure that costs are not omitted.

Status:

The Department of Administration and Finance in conjunction with the Fiscal Accountability Office developed and implemented revisions to the quarterly financial reports to streamline the process for recording compact expenses and related accruals. The current process requires that quarterly reports and disbursement requests are cleared by the Department of Administration and Finance and the Fiscal Accountability Office thereby ensuring that they are received. MCC issued policies and procedures for tracking and follow-up on outstanding quarterly disbursement requests and financial reports. Also, procedures for the review of quarterly and annual financial statements were developed and implemented by the Division of Finance.

MCC's Chief Financial Officer Was Not an Integral Part of the Compact/Grant Processes (material weakness)

Based on interviews and observations, we noted that MCC's Division of Finance was not integrally involved in the compact/grant processes to ensure that the financial aspects are addressed, recorded and reported in their proper sequence and appropriate timing. The Chief Financial Officer or his designees should be integrally involved in all MCC operations that result in a financial transaction. The CFO should be integrally involved in the:

(1) establishment of the compact amount to ensure that there is sufficient appropriations available,
(2) development of grant policies and procedures to ensure that they are in compliance with Federal government laws and regulations and to ensure that sufficient financial information is provided to MCC to accomplish its responsibilities,
(3) review of compacts in order to initiate accounting transactions in the system and budget transactions with OMB, and
(4) establishment of the reporting structure to ensure that financial information is provided timely and in the format necessary for required financial reporting.

Recommendation #06-05:

We recommend that Millennium Challenge Corporation's management revise their policies and procedures to invest the Office of the Chief Financial Officer with the level of responsibility, role, and all levels of authority established by the Chief Financial Officer Act.

Status:

The Chief Executive Officer sent a memorandum to MCC's executive team iterating CFO's responsibilities for the full spectrum of the Corporation's financial management activities. The FMPP manual reiterates the full spectrum of the CFO's responsibilities also.

MCC's Travel Disbursement Controls and Procedures Do Not Permit the Effective and Efficient Management of Travel (reportable condition)

MCC follows the Federal Travel Regulations and has an overall policy related to travel. However, prior to February 2006, MCC was using blanket travel authorizations (TA) to serve as an approval for employee travel. Once MCC approved the blanket TA, it was submitted to National Business Center (NBC) to post an obligation within Oracle. After February, MCC modified the travel policy that instituted the individual TA's that outlined the specific purpose of the employee's travel. NBC no longer posts travel obligations in advance in Oracle but obligates and pays the travel vouchers, simultaneously.

Similar to FY 2005, MCC requires all employees to post their travel expenses online in E-Travel. Although the travel voucher process is electronic, E-Travel does not interface with Oracle Federal Financials. Therefore, an NBC accounting technician must manually enter each voucher. During our travel testing, we noted twenty-six instances totaling $97,802 for which employees' receipts were not available. We also noted the following:

1. Eleven of 115 (10%) travel vouchers totaling $869 exceeded per diem rates;
2. Six of 115 (5%) vouchers equaling $557 consisted of expenses in excess of $75 and were not supported; and
3. Four of 115 (3%) vouchers totaling $35,663 were not approved by the travel manager within E-Travel.

MCC enhanced its travel policy in August 2006. MCC management changed the Corporation's supporting documentation requirements to require travelers to scan into the E-travel system and electronically attach to the pertinent travel vouchers receipts for claimed expenses of $75 or more. Division of Finance personnel are responsible for reviewing submitted vouchers to ascertain that required receipts are electronically attached to travelers' vouchers. Travelers who do not scan and attach their required receipts to vouchers are contacted by Division of Finance staff to obtain "missing" receipts.

Recommendation #06-06:

We recommend that Millennium Challenge Corporation's management develop and implement controls to reject travel expense reimbursement requests that exceed the allowable country per diem unless additional electronic authorization is provided.

Status:

The Deputy CFO instructed the DF's travel management staff to not approve any claimed travel expenses that exceed established limitations as defined by the Federal Travel Regulations (FTR) and to reject travelers' claims that exceed per diem limits. The travelers were provided feedback on travel voucher errors and a traveler's responsible manager/supervisor was apprised of claimed expenses that are not in compliance with per diem (actual costs) requirements. The manager/supervisor explicitly approved such expenses.

DF travel management staff underwent refresher FTR training and provided training on using the E-Travel system to MCC employees to better orient and guide them in properly preparing travel authorizations and vouchers.

MCC Did Not Fully Comply with FFMIA and GPRA

Millennium Challenge Corporation has not fully complied with the following laws and regulations:

- Government Performance and Results Act (GPRA)
- Federal Financial Management Improvement Act (FFMIA)

We noted that the agency performance plans provided to us did not fully comply with GPRA requirements, for example: human, capital and other resources needed to achieve performance goals were not quantified as required. Also, agency performance goals were not written in a manner that could be quantified in several instances and milestones were not included. Therefore, we could not directly link measurement of agency performance goals with the overall strategic plan. In addition, baseline data to be used as performance indicator measurement thresholds were not provided for some indicators.

The FFMIA requires an integrated financial management system. MCC does not have an integrated financial management system. When MCC decided to outsource its accounting operations, MCC selected NBC from the available Federal Centers of Excellence as the best choice to meet its needs. In order to address the needs of MCC, multiple systems, i.e. E-Travel, procurement, and Federal Personnel and Payroll System (FPPS), are used, but these systems cannot exchange data electronically. The entry of the travel expenses and disbursements must be done manually. The entry of obligations and commitments requires a process of emails, scanning and manual entry into Oracle Federal Financial (OFF) System application. The payroll expenses and disbursements must be uploaded into OFF from FPPS.

Additionally, we obtained and reviewed the Financial Management Controls and Assertion letter and noted the following assertion, "During FY 2006, NBC's sytems were not in substantial compliance with FFMIA requirements. In its assurance statement as of June 30, 2006, NBC asserted that 'were in substantial non-compliance with FFMIA requirements'." Subsequently, NBC instituted several corrective actions to address the issues raised and were in substantial compliance by September 30, 2006, per their representation.

Recommendation #06-07:

We recommend that MCC management:

(1) Develop performance goal templates and follow-up training to ensure that Government Performance and Results Act (GPRA) requirements are adequately addressed and consistent. We also recommend that baseline data be finalized or performance indicators reviewed and amended such that they can be measured against obtainable data.

(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 processing of financial transactions; and decrease the risk of errors.

Status:

The Department of Administration and Finance managed a performance working group, representing all departments to revise the MCC corporate performance plan for FY 2007, and acquired the services of a contractor to assist in drafting the plan, setting baselines and targets, and developing procedures to ensure that departmental and individual performance plans are aligned with the corporate plan. MCC was able to complete the performance plan which expanded the Framework, made key decisions on the baseline, performance measures, reliable data sources, and the vetting process to be employed by each department. The departmental plans are expected to be completed in October and the individual employee plans in December 2007.

In FY 2007 MCC has assessed various automated options related to the integration of its various systems and discussed options with their service provider. They have determined system requirements and performed a gap analysis. However, integration of the various systems requires additional analysis, planning and assessment.

Management Comments and Our Evaluation

We received and evaluated MCC's management comments to the recommendations made in this report. We considered their comments to be generally responsive except for specific exceptions detailed below. Management comments have been included in their entirety in Appendix C.

In its response, MCC's management stated that it recognizes the importance of accountability, effective stewardship, and public disclosure related to the resources entrusted to it, and that their goal is to achieve and maintain excellence in financial management, financial reporting and internal control systems. Further, MCC's management commented that it will implement the recommendations as soon as possible to strengthen their systems of internal controls and lend further credibility to their financial statements and overall financial operations. MCC's management went on to address each recommendation. MCC's management also recognized and thanked the OIG and Williams, Adley & Company, LLP for working closely with them during the audit process.

Based on MCC's comments, we consider that a management decision has been reached on recommendation 2 provided in this report but not on recommendations 1 and 3. These recommendations do not provide defined timelines for the corrective action implementation. Also, the corrective action for recommendation 1.4 requires additional details to ensure that the recommendations are appropriately addressed. MCC should report to the OIG when management decision has been reached on the four recommendations and when final action has been taken on the recommendations. The following is a brief summary of MCC's management comments on the three recommendations included in this report and our evaluation of those comments.

Recommendation No. 1

MCC accepts the recommendation. With regard to Recommendation # 1, MCC's current Financial Management Polices and Procedures do not contain any requirement to liquidate advances on a First-in, First-out (FIFO) basis; however we agree that FIFO would provide for improved reporting of outstanding advances. MCC will work with the National Business Center (NBC), its financial services provider, to ensure that all prior and future advances are liquidated on a FIFO basis.

MCC implemented the Common Payment System (CPS) in Mali in May 2007. All countries signing compacts after that date will utilize CPS. The CPS provides for payment of MCA expenses through the U.S. Treasury based upon presentation of a valid approved invoice. CPS supports sound cash management by eliminating the current practice of cash advances to MCA compact countries

MCC will establish a timeline for converting to CPS countries that entered into Compacts prior to May 2007. In the interim, MCC intends to follow sound cash management practices, and will disburse funds consistent with the GAO policy and based on the best information available and grant requirements in any given quarter. MCC will continue to release the funds in tranches following a monthly schedule.

Auditor Evaluation: We conclude that management has not adequately addressed this issue because the response does not address recommendation 1.4; and does not provide an implementation date.

Recommendation No. 2

MCC accepts the recommendation. In conjunction with the reorganization of the Operations Department, MCC will be reviewing existing polices and procedures related to compact implementation. This will include documenting the roles and responsibilities for ensuring receipt of required reports from partner countries.

MCC has submitted a comprehensive Records Disposition (retention) schedule to the National Archives and Records Association for review and approval within the next six to nine months. The issue of version control and a centralized repository is being addressed as part of development of the Enterprise Architecture and the implementation of the Business Intelligence and Data Storage (BIDS). A key component of BIDS will be the Administrative Data Store (ADS). The ADS is a data warehouse that will include MCA Compact data, MCA Progress Reports, and records of MCC reviews, approvals and decisions captured through an automated workflow process. The expected implementation date for this component of the BIDS is June 2008. In the interim, MCC will establish procedures to address the version control issue using existing tools.

Auditor Evaluation: We conclude that management has adequately addressed this issue.

Recommendation No. 3

MCC accepts the recommendation. The Department of Administration and Finance (A&F) will continue to work to the National Business Center (NBC) on the interface between Etravel and Oracle to resolve the issues noted during initial testing. MCC will be changing to a new government credit card provider in FY 2008 for both travel and purchase card transactions. MCC is currently considering either JP Morgan Chase or Citibank, both of which have a fully tested and integrated interface with the Oracle Federal Financial System (OFFS). Regarding the payroll integration, the NBC has indicated its business plan does not include the integration of FPPS with OFFS, outside of the labor interface already provided.

During FY 2007, A&F made substantial progress on reviewing its current financial systems environment and developing alternatives for a fully integrated system to meet the requirements of the FFMIA. A&F has established system requirements, performed a gap analysis based on its current environment, and developed cost alternatives to close the exiting gaps. A&F will also work with the Office of Management and Budget (OMB) to find the best resolution for this condition whether with the NBC, or with some other federal or private center of excellence.

Auditor Evaluation: We conclude that management has not adequately addressed this issue because no defined timetable has been stated for the corrective action.

MILLENNIUM CHALLENGE CORPORATION
REDUCING POVERTY THROUGH GROWTH

November 2, 2007

TO: John Phee
Assistant Inspector General

FROM: Michael Ryan /s/
Vice President, Administration and Finance

SUBJECT: Management Response to Draft Independent Auditor's Report on MCC's Financial Statements for Fiscal Years Ended September 30, 2007 and 2006, Respectively

We have received the subject draft report and are pleased to note that the independent auditors, Williams, Adley and Company, LLP, are issuing an unqualified opinion on our principal financial statements, namely the:

Balance Sheets;
Statements of Net Costs;
Statements of Changes in Financial Position; and
Statements of Budgetary Resources.

The auditor's unqualified opinion is being issued despite material internal control weaknesses and noncompliance with selected laws and regulation that have been identified.

The Millennium Challenge Corporation's (MCC) management recognizes the importance of accountability, effective stewardship and public disclosure related to the resources entrusted to it. Our goal is to achieve and maintain excellence in our financial management, financial reporting and internal control systems. Accordingly, we will implement the recommendations as soon as possible to strengthen our systems of internal control and lend further credibility to our financial statements and overall financial operations.

We wish to recognize and thank you, your team, and Williams, Adley and Company for working closely with us during the audit process. Any questions may be addressed to Mr. Dennis Nolan, Deputy Chief Financial Officer, or to me.

Following are our management decisions and responses to Williams Adley's audit recommendations.

***Material Weakness 1*:** MCC did not sufficiently execute its monitoring functions related to advances.

Recommendations: Williams, Adley and Company recommend that the Millennium Challenge Corporation's management:

1.1. Implement a policy that reduces outstanding advances based on the FIFO method.

1.2. Implement the common payment system for all MCAs on a more aggressive timeline.

1.3. Make payments in accordance with the monthly schedule and if a payment is held consider the need for it to be disbursed at all.

1.4. Ensure that there is a more rigorous review of advance requests including an assessment of outstanding advances.

Management Decision: MCC accepts the recommendation. With regard to Recommendation # 1, MCC's current Financial Management Polices and Procedures do not contain any requirement to liquidate advances on a First-in, First-out (FIFO) basis; however we agree that FIFO would provide for improved reporting of outstanding advances. MCC will work with the National Business Center (NBC), its financial services provider, to ensure that all prior and future advances are liquidated on a FIFO basis.

MCC implemented the Common Payment System (CPS) in Mali in May 2007. All countries signing compacts after that date will utilize CPS. The CPS provides for payment of MCA expenses through the U.S. Treasury based upon presentation of a valid approved invoice. CPS supports sound cash management by eliminating the current practice of cash advances to MCA compact countries

MCC will establish a timeline for converting to CPS countries that entered into Compacts prior to May 2007. In the interim, MCC intends to follow sound cash management practices, and will disburse funds consistent with the GAO policy and based on the best information available and grant requirements in any given quarter. MCC will continue to release the funds in tranches following a monthly schedule.

Material Weakness 2: MCC lacks written policies and procedures related to financial reporting accountability and document control.

Recommendations: Williams, Adley and Company recommends that the Millennium Challenge Corporation management:

2.1. Formally document the MCC accountability for ensuring MCA compliance with the reporting provisions.

2.2. Implement document retention policies that include standards for version control and a central repository for documents that are used by multiple MCC units.

2.3. Continue with the planned implementation of the BIDS project and ensure that information is validated prior to inclusion in the new system.

Management Decision: MCC accepts the recommendation. In conjunction with the reorganization of the Operations Department, MCC will be reviewing existing polices and procedures related to compact implementation. This will include documenting the roles and responsibilities for ensuring receipt of required reports from partner countries.

MCC has submitted a comprehensive Records Disposition (retention) schedule to the National Archives and Records Association for review and approval within the next six to nine months. The issue of version control and a centralized repository is being addressed as part of development of the Enterprise Architecture and the implementation of the Business Intelligence and Data Storage (BIDS). A key component of BIDS will be the Administrative Data Store (ADS). The ADS is a data warehouse that will include MCA Compact data, MCA Progress Reports, and records of MCC reviews, approvals and decisions captured through an automated workflow process. The expected implementation date for this component of the BIDS is June 2008. In the interim, MCC will establish procedures to address the version control issue using existing tools.

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Material Noncompliance 1: MCC does not fully comply with the Federal Financial Management Improvement Act (FFMIA).

Recommendation: Williams, Adley and Company recommend that management continue to assess the automated options available to handle the Millennium Challenge Corporation 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 processing of financial transactions; and decrease the risk of errors.

Management Decision: MCC accepts the recommendation. The Department of Administration and Finance (A&F) will continue to work to the National Business Center (NBC) on the interface between Etravel and Oracle to resolve the issues noted during initial testing. MCC will be changing to a new government credit card provider in FY 2008 for both travel and purchase card transactions. MCC is currently considering either JP Morgan Chase or Citibank, both of which have a fully tested and integrated interface with the Oracle Federal Financial System (OFFS). Regarding the payroll integration, the NBC has indicated its business plan does not include the integration of FPPS with OFFS, outside of the labor interface already provided.

During FY 2007, A&F made substantial progress on reviewing its current financial systems environment and developing alternatives for a fully integrated system to meet the requirements of the FFMIA. A&F has established system requirements, performed a gap analysis based on its current environment, and developed cost alternatives to close the exiting gaps. A&F will also work with the Office of Management and Budget (OMB) to find the best resolution for this condition whether with the NBC, or with some other federal or private center of excellence.

Material Noncompliance 2: MCC does not comply with the Federal Information Security Management Act (FISMA). Williams, Adley and Company makes no recommendation(s) relative to this material noncompliance. This deficiency was identified by the Office of Inspector General in a prior audit. During FY 2007, MCC management:

- Hired two fulltime FISMA staff;
- Completed an MCC Self Assessment;
- Completed an MCC's Information System Security Plan (ISSP);
- Completed Quartile scans on MCCnet;
- Approved three additional FISMA team members-Subject Matter Expert, Technological Writer and Network Engineer; and
- Created a new CISSO position with an additional slot, and hired a full-time employee who will start in November.

BALANCE SHEETS

In dollars	FY 2007	FY 2006
Assets		
Intra-Governmental		
Fund Balance with Treasury *(Note 2)*	**$5,549,289,597**	**$4,078,656,972**
Accounts Receivable *(Note 3)*	67,798	62,202
Total Intra-Governmental	5,549,357,395	4,078,719,174
General Property, Plant, and Equipment*(Note 4, Note 5)*	7,115,606	4,632,785
Advances *(Note 1F,P)*	32,243,157	18,881,386
Total Assets	**$5,588,716,158**	**$4,102,233,345**
Liabilities		
Intra-Governmental		
Other	$ 1,457,862	$ 2,516,786
Total Intra-Governmental	**1,457,862**	**2,516,786**
Accounts Payable *(Note 1G)*	39,176,698	10,134,698
Other	3,971,886	2,698,070
Total Liabilities	**$ 44,606,446**	**$ 15,349,554**
Net Position		
Unexpended Appropriations – Other Funds	$5,536,714,361	$4,082,189,638
Cumulative Results of Operations – Other Funds	7,395,351	4,694,153
Total Net Position	**$5,544,109,712**	**$4,086,883,791**
Total Liabilities and Net Position	**$5,588,716,158**	**$4,102,233,345**

The notes are an integral part of the financial statements

STATEMENTS OF BUDGETARY RESOURCES

In dollars	FY 2007	FY2006
Budgetary Resources		
Unobligated Balance – Beginning of Period	$2,671,372,416	$2,053,722,184
Recoveries of Prior Years Obligations	15,930,609	-
Budget Authority:		
Appropriations	1,752,300,000	1,770,000,000
Nonexpenditure Transfers, Net, Anticipated and Actual	(9,415,980)	-
Permanently Not Available *(Note 7)*	-	(17,700,000)
Total Budgetary Resources	**$4,430,187,045**	**$3,806,022,184**
Status of Budgetary Resources		
Obligations Incurred		
Direct	$2,174,044,542	$1,109,535,594
Unobligated Balance Available		
Apportioned	1,516,900,216	877,383,424
Unobligated Balance Not Available	$ 739,242,287	$1,819,103,166
Total Status of Budgetary Resources	**$4,430,187,045**	**$3,806,022,184**
Change in Obligated Balance		
Obligated Balance, Net – as of October 1, 2005		
Unpaid Obligations, Brought Forward, October 1	$1,408,398,635	$ 272,636,873
Obligations Incurred	2,174,044,542	1,109,535,594
Gross Outlays	(278,605,423)	(109,119,072)
Recoveries of Prior Year Unpaid Obligations, Actual	(15,930,609)	-
Obligated Balance, Net – End of Period		
Unpaid obligations	$3,287,907,145	$1,273,053,395
Net Outlays		
Gross Outlays	$ 278,605,423	$ 109,119,072

The notes are an integral part of the financial statements

STATEMENTS OF NET COSTS

Program	2007 Total	2006 Total
Program Costs (In dollars)		
Compact		
Gross Costs (Note 6)	$ 81,079,458	$ 16,747,194
Less: Earned Revenue	-	-
Net Program Costs	81,079,458	16,747,194
609 (g) Programs		
Gross Costs	17,172,113	5,895,167
Less: Earned Revenue	-	-
Net Program Costs	17,172,113	5,895,167
Threshold Programs		
Gross Costs	75,766,215	15,235,063
Less: Earned Revenue	-	-
Net Program Costs	75,766,215	15,235,063
Due Diligence Programs		
Gross Costs	32,789,662	15,137,340
Less: Earned Revenue	-	-
Net Program Costs	32,789,662	15,137,340
Audit		
Gross Costs	2,865,820	619,714
Less: Earned Revenue	-	-
Net Program Costs	2,865,820	619,714
Administrative		
Gross Costs	77,922,457	54,785,827
Less: Earned Revenue	-	-
Net Program Costs	77,922,457	54,785,827
Program Costs – Net of All Programs	**$287,595,725**	**$108,420,305**
Net Costs of Operations	**$287,595,725**	**$108,420,305**
The notes are an integral part of the financial statements		

STATEMENTS OF CHANGES IN NET POSITION

In dollars	FY 2007	FY 2006
Cumulative Results of Operations		
Beginning Balances	$ 4,694,987	$ 4,276,833
Adjustments	-	-
Beginning Balance, as Adjusted	$ 4,694,987	$ 4,276,833
Budgetary Financing Sources		
Appropriations Used	$ 288,359,297	$ 107,689,343
Other Financing Sources		
Donations and Forfeitures of Property	$ 123,750	$ -
Imputed Financing	1,813,042	1,148,282
Total Financing Sources	290,296,089	108,837,625
Net Cost of Operations	(287,595,725)	(108,420,305)
Net Change	2,700,364	417,320
Cumulative Results of Operations	**$ 7,395,351**	**$ 4,694,153**
Unexpended Appropriations		
Beginning Balance	$4,082,189,638	$2,437,546,656
Changes in Accounting Principles	-	-
Beginning Balance, as Adjusted	$4,082,189,638	$2,437,546,656
Budgetary Financing Sources		
Appropriations Received	$1,752,300,000	$1,770,000,000
Appropriations Transferred In/Out	(9,415,980)	-
Other adjustments *(Note 7)*	-	(17,700,000)
Appropriations Used	(288,359,297)	(107,657,018)
Total Budgetary Financing Sources	1,454,524,723	1,644,642,982
Total Unexpended Appropriations	5,536,714,361	4,082,189,638
Net Position	**$5,544,109,712**	**$4,086,883,791**

The notes are an integral part of the financial statements

Note 1—Summary of Significant Accounting Policies

A. Basis of Presentation

The accompanying principal financial statements have been prepared to report the financial position, results of operations and budgetary resources for MCC, as required by Section 613 of the Millennium Challenge Act of 2003. They have been prepared using MCC's books and records in accordance with MCC accounting policies, the most significant of which are summarized in this note. The statements are presented in accordance with the guidance and requirements of the recently issued OMB Circular A-136, which incorporates and updates Bulletin 01-09, Form and Content of Agency Financial Statements, and the Government Management Reform Act of 1994. Fiscal Year 2006 statements, previously prepared in accordance with the Government Corporation Control Act (31 U.S.C. §9106), have been reformatted and republished for Circular A-136 comparative purposes. Fiscal year 2006 financial statements have also been restated for comparative purposes to include Threshold program balances that were not reflected timely prior to final publication.

MCC accounting policies follow generally accepted accounting principles for the Federal government, as recommended by the Federal Accounting Standards Advisory Board (FASAB). The FASAB has been recognized by the American Institute of Certified Public Accountants (AICPA) as the official accounting standard set for the Federal government. These standards have been agreed to, and published by the Director of OMB, the Secretary of the Treasury, and the Comptroller General.

MCC's principal financial statements are:

- Balance Sheet
- Statement of Budgetary Resources
- Statement of Net Cost
- Statement of Changes in Net Position

These notes are considered an integral part of the financial statements.

B. Reporting Entity

MCC was formed in January 2004 pursuant to the Millennium Challenge Act of 2003 (Public Law 108-199). MCC's mission is to reduce poverty by supporting sustainable, transformative economic growth in developing countries that create and maintain sound policy environments. The assistance is intended to provide economic growth and the elimination of extreme poverty, strengthen good governance, encourage economic freedom, and promote investments in people.

C. Budgets and Budgetary Accounting

MCC's programs and activities are funded through no-year appropriations. Such funds are available for obligation without fiscal year limitation and remain available until expended. MCC was provided total appropriations of almost $1.752 billion and $1.770 billion in FY 2007 and FY 2006, respectively. OMB apportions MCC administrative funds on an annual basis pursuant to statutory limitations in MCC's annual congressional appropriations. In addition, MCC receives from OMB a separate apportionment for due diligence funds, which MCC uses for compact evaluations and support, compact programs, 609(g) funds, the Threshold program, and audit funds. Because of the no-year status of MCC appropriations, unobligated administrative, audit, and due diligence funds (apportioned annually) are not returned to the Treasury; however, unobligated balances as of September 30 for these three categories of funds are transferred to the compact fund category at the beginning of the subsequent fiscal year for future use.

D. Basis of Accounting

Financial transactions are recorded on accrual and budgetary bases in accordance with pertinent federal accounting and financial reporting requirements. Under the accrual method of accounting, financing sources are recognized when used and expenses are recognized when incurred, without regard to receipt or payment of cash. Budgetary accounting facilitates MCC's compliance with legal constraints and controls over the use of federal funds.

The accompanying Balance Sheet, Statement of Net Cost, and Statement of Changes in Net Position have been prepared on the accrual basis. The Statement of Budgetary Resources has been prepared in accordance with budgetary accounting rules.

E. Fund Balance with Treasury

MCC does not maintain cash in commercial bank accounts. Rather, MCC's funds are maintained in Treasury accounts. The Department of the Treasury processes all cash receipts and disbursements for MCC. The Fund Balances with Treasury represent no-year funds, which are maintained in appropriated funds that are available to pay current and future commitments.

F. Advances to Others

MCC advances funds to eligible compact and pre-compact countries in order to implement compact projects in an MCA country or for federal government inter-agency agreements. Funds advanced to compact and pre-compact countries are used to pay legitimate costs and expenses incurred by MCC and partner countries. Advances at the end of FY 2007 and FY 2006 were $32.2 million and $18.9 million, respectively. Of the twenty-one (21) MCC outstanding advances, four (4) are greater than 180 days.

G. Accounts Payable

MCC records as liabilities all amounts due to others as a direct result of transactions or events that have occurred. Accounts payable represent amounts due to federal and non-federal entities for goods and services received by MCC, but not paid at the end of the accounting period. Accounts payable reported at the end of FY 2007 and 2006 were $39.2 and $10.1 million, respectively. The increase in the Accounts Payable is attributable to an increase from $7.6 million in FY 2006 to $28.6 million in FY 2007 for USAID Threshold programs**.**

H. Actuarial FECA Liability

The Federal Employees' Compensation Act (FECA) provides income and medical cost protection to covered federal civilian employees injured on the job, employees who have incurred a work-related occupational disease, and beneficiaries of employees whose deaths are attributable to a job-related injury or occupational disease.

Claims incurred for benefits for MCC employees under FECA are administered by the Department of Labor (DOL) and later billed to MCC. MCC's actuarial liability for workers' compensation includes any costs incurred but unbilled as of year-end, as calculated by DOL, and not funded by current appropriations.

MCC incurred no FECA liabilities during FY 2007 and FY 2006.

I. Accrued Annual Leave

The value of employees' unused annual leave at the end of each fiscal quarter is accrued as a liability. At the end of each fiscal quarter, the balance in the accrued annual leave account is adjusted to reflect current pay rates and leave balances. Annual leave is funded from current appropriations. Sick leave and other types of non-vested leave are expensed when used, and in accordance with federal requirements no accruals are recorded for unused leave.

J. Net Position

Net position is composed of unexpended appropriations and cumulative results of operations. Unexpended appropriations are funds appropriated by Congress to MCC that are still available for expenditure at the end of the fiscal year. Cumulative results of operations represent the net differences between financing sources and expenses from MCC's inception.

K. Financing Sources

In accordance with Note 1.C, MCC funds its program and operating expenses through no-year appropriations. Appropriations are recognized as an accrual-based financing source at the time they are used to pay program or administrative expenses, except for expenses to be funded by future appropriations.

L. Retirement Benefits

MCC's employees participate in either the Civil Service Retirement System (CSRS) or the Federal Employees Retirement System (FERS). FERS was established by Public Law 99-335. Pursuant to this law, most U.S. Government employees hired after December 31, 1983, are covered by FERS and Social Security. Federal employees hired prior to January 1, 1984, were allowed to elect whether they desired to participate in FERS (with Social Security coverage) or remain in CSRS. For employees covered by CSRS, MCC contributes 7 percent of their gross pay toward their retirement benefits. For those employees covered by FERS, MCC contributes 11 percent of their gross pay toward retirement. Employees are also allowed to participate in the federal Thrift Savings Plan (TSP). For employees under FERS, MCC contributes an automatic 1 percent of basic pay to TSP and matches employee contributions up to an additional 4 percent of pay, for a maximum MCC contribution amounting to 5 percent of pay. Employees under CSRS may participate in the TSP, but will not receive either MCC's automatic or matching contributions.

For FY 2007, MCC has made contributions of $142,000 to CSRS, $2.4 million to FERS, and $849,000 to TSP. During FY 2006, MCC made retirement contributions of $761,000 to CSRS, $1.977 million to FERS, and $620,700 to TSP.

M. Use of Estimates

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of financing sources and expenses during the reporting period. Actual results could differ from such estimates.

N. Contingencies

MCC can be a party to various routine administrative proceedings, legal actions, and claims brought by or against it, including threatened or pending litigation involving labor relations claims, some of which may ultimately result in settlements or decisions against MCC. In the opinion of MCC's management and legal counsel, there are no proceedings, actions, or claims outstanding or threatened that would materially impact MCC's financial statements.

O. Judgment Fund

Certain legal matters to which MCC can be named as a party may be administered and, in some instances, litigated and paid by other federal agencies. In general, amounts paid in excess of $2,500 for Federal Tort Claims Act settlements or awards pertaining to these litigations are funded from a special appropriation administered by the Department of the Treasury called the Judgment Fund. Although the ultimate disposition of any potential Judgment Fund proceedings cannot be determined, management expects that any liability or expense that might ensue would not be material to MCC's financial statements.

P. Custodial Receivables and Liabilities

Under current policy and procedures, MCC funds all compacts and pre-compacts with other countries by advancing funds on a monthly basis to cover projected needs. Such funds provided to the countries are required to be deposited in interest-bearing accounts, if legally feasible, until disbursed. The interest earned on these accounts is remitted to MCC and deposited into an account at the U.S. Treasury. Such interest may not be retained or used by MCC, but periodically is returned to the Treasury's general funds. MCC had outstanding advances related to compact and pre-compact financing of approximately $30.8 million and $18.8 million on September 30, 2007, and September 30, 2006, respectively. MCC received and deposited $1.65 million and $304,000 in interest remittances on September 30, 2007, and September 30, 2006, respectively (see Note 2).

Q. Donated Services

MCC may on occasion use donated services from other federal agencies and private firms in the course of business operations. The approximate fair market value of these donated services for September 30, 2007, is $123,750 and was $0 in FY 2006.

R. Transfers with Other Federal Agencies

MCC is a party to allocation transfers with another federal agency as a transferring entity. Allocations are legal delegations by one agency of its authority to obligate budget authority and outlay funds to another agency. A separate fund account (child account) is created in the U.S. Treasury as a subset of the parent fund account for tracking and reporting purposes. All allocation transfers of budget authority are credited to this account, and subsequent obligations and outlays incurred by the child entity are charged to this allocation account as they execute the delegated activity on behalf of the parent entity.

All financial activity related to these allocations and transfers (e.g., budget authority, obligations, and outlays) is reported in the financial statements of the parent entity, from which the underlying legislative authority, appropriations, and budget appointments are derived. MCC allocated funds, as the parent, to USAID. In FY 2007 and FY 2006, MCC transferred budgetary authority of $161 million and $155 million, respectively, to USAID for Threshold programs.

Note 2—Fund Balance with Treasury

The U.S. Treasury accounts for all U.S. Government cash on an overall consolidated basis. The Fund Balance with Treasury (FBWT) line items on the Balance Sheet for September 30, 2007, and September 30, 2006, consisted of amounts presented in Exhibit 3-1. MCC funds its program and operating expenses through no-year appropriations; therefore, all unobligated balances as of September 30 are transferred to the compact fund category at the beginning of the subsequent fiscal year and are available for use in future years until fully expended.

Exhibit 3-1: Fund Balance with Treasury as of September 30 (in thousands)

	September 30, 2007	September 30, 2006
Appropriated Funds		
Unobligated	$2,261,383	$2,805,604
Obligated	3,287,907	1,273,053
Total	**$ 5,549,290**	**$ 4,078,657**

Note 3—Accounts Receivable, Net

Accounts receivable reflect overpayments of payroll, travel, and other MCC current/former employee expenses. MCC does not record an allowance for doubtful accounts because these expenses are deemed wholly collectible. Total receivables were $68,000 and $62,000 as of September 30, 2007, and September 30, 2006, respectively.

Note 4—General Property, Plant, and Equipment, Net

In March 2007, MCC revised its property capitalization threshold from an original cost of $25,000 or more and an estimated useful life of 2 or more years to an original cost of $50,000 or more and an estimated useful life of 5 or more years, except for its software capitalization which was changed to an original cost of $200,000 or more and an estimated useful life of 5 or more years and its information technology infrastructure capitalization to an original cost of $200,000 or more and an estimated useful life of 3 or more years. These revisions reduce MCC's administrative costs associated with accounting for General Property, Plant, and Equipment (PP&E) and results in increased operational efficiency.

MCC changed its depreciation convention, converting from a half-year convention to a quarter-year convention. Assets are depreciated (or amortized) quarterly over their estimated useful lives using the straightline depreciation method. This change resulted in additional depreciation expense of $181,638. As required by FASAB 21, the net effect of this change has been included in the FY 2007 cumulative results of operations and net position.

MCC's actual depreciation expense for FY2007 is $860,061.

Note 5—Leases

MCC leases office space in two adjacent locations in Washington, D.C. These leases are on 10-year (Bowen Building) and 8-year (City Center) lease terms that terminate on May 25 and May 26, 2015, respectively (see Exhibit 3-2). MCC made significant leasehold improvements to the office space and amortizes the improvement based on the in-service (invoice) date of the improvement. Amortization is calculated on a quarterly basis. These leasehold improvements will be reflected as a Fixed Asset on MCC's Balance Sheet net of amortization.

Exhibit 3-2: Operating Leases Funds (in dollars)

Future Payments Due			
Fiscal Year	**Bowen**	**City Center**	**Totals**
FY 2008	$5,394,621	$1,889,524	$7,284,145
FY 2009	5,394,621	1,889,524	7,284,145
FY 2010	6,352,911	1,889,524	8,242,435
FY 2011	6,352,911	1,942,376	8,295,287
FY 2012	6,352,911	1,942,376	8,295,287
After 5 Years	19,058,733	5,932,834	24,991,567
Total Future Lease Payments	**$48,906,708**	**$15,486,158**	**$64,392,866**

Note 6—Intra-Governmental Costs and Exchange Revenue

The Statement of Net Cost reports MCC's gross cost less earned revenues to arrive at net cost of operations. Costs have been illustrated by MCC specific programs (see Exhibit 3-3). The format of the Statement of Net Cost is also now consistent with OMB Circular A-136 guidance. Exhibit 3-3 shows the value of exchange transactions between MCC and other federal entities as well as non-federal entities. Intra-Governmental Costs relate to transactions between MCC and other federal entities. Public costs on the other hand relate to transactions between MCC and non-federal entities. MCC does not have any exchange revenues.

Exhibit 3-3: Intra-Governmental Costs and Exchange Revenue (in thousands)

	Compact	609(g)	Threshold	Due Diligence	Audit	Admin	September 30, 2007	September 30, 2006
Intra-Governmental	-	59	-	3,567	2,789	7,741	14,156	9,428
Public	81,079	17,113	75,766	29,223	77	70,181	273,439	98,992
Total – Program	81,079	17,172	75,766	32,790	2,866	77,922	287,595	108,420

Note 7— Adjustments to Beginning Balance of Budgetary Resources

In FY 2006, $17.7 million of amounts appropriated under the FY 2006 Foreign Operations, Export Financing and Related Programs Appropriations Acts (Public Law 109-148) were rescinded. The rescission was part of the Across-the-Board Rescission enacted for FY 2006.

There were no adjustments to the FY 2007 beginning balances of Budgetary Resources.

Note 8—Explanation of Differences Between the SBR and the Budget of the U.S. Government

MCC ensures that the information reported on its books is reflected within the Budget of the U.S. Government. Because MCC's financial statements are published before the President's Budget, this reconciliation is based on the Statement of Budgetary Resources for FY 2006 and the 2006 actual data reported in the President's 2008 budget submission. FY 2007 actual data will be published in February 2008 within the 2009 Budget of the United States.

Material differences reported in the Budgetary resources column ($2.053 billion) represent unobligated balances reported on MCC's SBR and SF 133, but not in the Budget of the U.S. Government. Material differences reported in the Total Outlays column represent SF 133 outlays reported by USAID in FY 2006 that were not reported timely to MCC to present in its FY 2006 financial statements. (See Exhibit 3-4.)

Exhibit 3-4: Material Differences Between the SBR and the President's Budget (in millions)

	Budgetary Resources	Obligations Incurred	Distributed Offsetting Receipts	Net Outlays
Statement of Budgetary Resources	3,806	1,109		109
Unobligated Balance Carry Forward from FY 2005	(2,053)			
Unreported Outlays				2
Budget of the U.S. Government	1,753		1	111

Note 9—Undelivered Orders at the End of the Period

The reported net position consists of unexpended appropriations and cumulative results of operations, which reflects the difference between financing sources and expenses since MCC's inception. Exhibit 3-5 represents Undelivered orders—unpaid for compact and 609(g) funds as of September 30, 2007 and September 30, 2006.

Exhibit 3-5: Undelivered Orders—Compact and 609(g) Funds (in dollars)

Undelivered Orders	2007	Compacts	609(g) Funding	2006
Armenia	$ 227,716,911	$ 227,716,911	$ -	$ 235,646,174
Benin	293,870,370	293,870,370	-	1,062,985
Cape Verde	96,151,990	96,147,871	4,119	106,077,520
El Salvador	458,715,779	458,715,779	-	-
Georgia	265,875,250	264,656,190	1,219,060	296,178,084
Ghana	538,097,271	537,668,659	428,612	13,584,891
Honduras	204,027,319	204,027,319	-	213,166,147
Kenya	25,000	25,000	-	-
Lesotho	16,078,147	15,668,416	409,731	902,934
Madagascar	87,042,735	87,042,735	-	103,290,130
Mali	462,993,330	458,630,248	4,363,082	4,421,534
Morocco	32,400,000	32,400,000	-	-
Mozambique	31,254,763	25,346,200	5,908,563	12,956,078
Nicaragua	165,314,884	165,314,884	-	173,583,320
Senegal	1,930,524	-	1,930,524	4,882,237
Tanzania	9,800,000	-	9,800,000	-
Vanuatu	63,683,392	63,683,392	-	65,214,603
Total–Undelivered Orders	**$2,954,977,665**	**$2,930,913,974**	**$24,063,691**	**$1,230,966,637**

Note 10—Reconciliation of Net Cost of Operations to Budget

Exhibit 3-6 reconciles the FY 2007 resources available to MCC to finance operations with the net cost of operating MCC's programs. Some operating costs, such as depreciation, do not require direct financing sources. This exhibit illustrates the reconciliation of Net Cost of Operations to Budget.

Exhibit 3-6: Reconciliation of Net Cost of Operations to Budget (in dollars)

Resources Used to Finance Activities		Program Costs	
Budgetary Resources Obligated			
Net obligations	$2,189,975,151	**Gross Costs**	$287,595,725
Net other resources used to finance activities	1,936,792		
Total resources used to finance activities	2,191,911,943		
Total resources used to finance items not part of the net cost of operations	(1,905,176,279)	**Less: Earned Revenue**	-
Total resources used to finance the net cost of operations	286,735,664		
Total components of net cost of operations that will not require or generate resources	860,061		
Net Cost of Operations	**$ 287,595,725**	**Net Cost of Operations**	**$287,595,725**