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THE MILLENNIUM CHALLENGE CORPORATION'S GLOBAL IMPACT

HEARING

BEFORE THE

COMMITTEE ON FOREIGN RELATIONS UNITED STATES SENATE

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THE MILLENNIUM CHALLENGE CORPORATION'S GLOBAL IMPACT

TUESDAY, APRIL 26, 2005

U.S. SENATE,
FOREIGN RELATIONS COMMITTEE,
Washington, DC.

The committee met, pursuant to notice, at 9:30 a.m., in room SD–419, Dirksen Senate Office Building, Hon. Richard G. Lugar, chairman of the committee, presiding.

Present: Senators Lugar, Coleman, Martinez, Sarbanes, Nelson, Obama.

OPENING STATEMENT OF HON. RICHARD G. LUGAR, U.S. SENATOR FROM INDIANA

The CHAIRMAN. This hearing of the Senate Foreign Relations Committee is called to order.

Today the Foreign Relations Committee meets to review the progress of the Millennium Challenge Corporation. We are pleased to welcome Mr. Paul Applegarth, the CEO of the Millennium Challenge Corporation, to present firsthand evidence of the MCC's experience around the globe over the last 13 months.

We also welcome David Gootnick, Director of International Affairs and Trade at the U.S. Government Accountability Office, to present the results of a year-long review of the activities of the MCC.

Our committee has enthusiastically endorsed the concept of the Millennium Challenge Corporation, which will provide assistance to developing countries that invest in their people, uphold political freedoms, fight corruption, maintain the rule of law, and pursue sound economic policies. We want to ensure that the MCC becomes an efficient and valuable tool of U.S. foreign policy. We want it to be a bold weapon in the battle against poverty, disease, corruption, disorder, and terrorism. We want the MCC to help lift deserving nations and provide incentives for meaningful reform in countries around the world.

More than 6 months ago, at our last hearing on the MCC, I said, "My hope is that the MCC will perform so well during the next year that Members of Congress of both parties will embrace it enthusiastically as an inspired idea and an essential program. But for this to happen, the execution of the MCC concept must be extraordinary. Compacts must be concluded, and money must be spent quickly, while ensuring that those dollars are distributed fairly, effectively, and without corruption."

Last week, at a ceremony at the State Department, the United States and the Republic of Madagascar signed the first MCC compact. I am encouraged by this action, and salute the efforts of the Government of Madagascar to meet MCC eligibility requirements. I look forward to hearing more about the steps taken to reach this compact and its potential impact on other nations.

It is imperative that the MCC moves forward to expand its portfolio of compacts with eligible countries. As new compacts are being concluded, we must ensure that U.S. taxpayer funds are closely monitored and the process for selecting countries and evaluating proposals is carried out in a transparent process. We are eager to know the timetable for completing additional compacts, and whether the process can be accelerated, while maintaining requisite standards of operation.

In July, the leaders of the G–8 will meet in Gleneagles, Scotland, to tackle the ambitious agenda of poverty reduction in Africa. Tony Blair, the host of this year's summit, has presented Great Britain's plan through the Commission on Africa. The MCC will play an important role in the U.S. contribution to this effort. We must demonstrate to the rest of the world that we are committed to the MCC's success.

President Bush requested $3 billion for the Millennium Challenge Corporation in this fiscal year. The Foreign Relations Committee endorsed that amount in the Foreign Affairs Authorization bill that we reported to the Senate.

Some have argued that the President should have requested $5 billion—the amount he originally had conceived for the Corporation's third year of funding. Others have argued that $3 billion is too much for a new venture that is just getting off the ground, and that some of this money should be shifted to other priorities. My own view is that $3 billion is a reasonable amount, given the scope of the program and its potential for spurring democratic reforms overseas. The credibility of the program, which foreign nations are observing closely, would be strengthened by congressional support for the President's funding request. Today, we will be seeking additional assurances that the program is on target to productively and efficiently use the funds that Congress and the President have devoted to it.

The MCC holds great promise for both participating countries and the United States. It gives us a chance to invigorate our relationships with the developing world and help set them on a course of progress. We hope that the MCC, working closely with Congress, can realize the original vision of President Bush to dramatically expand our ability to spur economic development throughout the world.

Again, we welcome our witnesses to the committee, and look forward to their testimony.

I'm advised that Mr. Applegarth is not in the committee room at this point, and therefore we will proceed with Mr. David Gootnick as our first witness, and then proceed to Mr. Applegarth later.

Mr. Gootnick, we are delighted you are here, and let me say that your prepared statement will be made part of the record in full. You may proceed as you wish, perhaps with a summary of major points, and then we will have questions for you.

STATEMENT OF DAVID B. GOOTNICK, DIRECTOR, INTERNATIONAL AFFAIRS AND TRADE, U.S. GENERAL ACCOUNTABILITY OFFICE, WASHINGTON, DC

Mr. GOOTNICK. Thank you, Mr. Chairman. Thank you for the opportunity to be here to discuss GAO's observations on the Millennium Challenge Corporation. Overall, MCC has made progress in its first 15 months of operations, at the same time it faces key challenges looking forward. Today I will discuss four aspects of MCC's activities to date.

First, its eligibility determinations; second, its progress in developing compacts; third, coordination issues; and fourth establishment of its corporatewide management and accountability structures. This work is based on our ongoing analysis for your committee, and our field work in Honduras in January of this year.

First, regarding country eligibility determinations. In its first year, MCC developed a methodology based on quantitative indicators for making eligibility determinations. The Corporation's Board deemed 17 countries eligible for compact assistance in 2004 and 2005, including three countries that did not meet the quantitative indicator criteria. The Board also selected 13 countries to participate in the Corporation's threshold program.

MCC's public reports on the Board's eligibility determinations were brief, and did provide limited information. The reports did not explain the Board's rationale for not selecting 13 countries that met the indicator criteria. Almost by definition, an indicator-based methodology has some inherent limitations, such as measurement uncertainty and missing data. These limitations made some indicators less useful in distinguishing among candidate countries. For seven of the indicators, primary source data was not readily accessible to the public. MCC has clearly stated that it will continue to refine its methodology in response to these and other limitations.

Next, Mr. Chairman, regarding MCC's progress in developing compacts. Thus far, the Corporation has received proposals from 16 eligible countries. These proposals focused, among other things, on agri-business, large-scale infrastructures such as roads and ports and policy reforms, including public sector capacity building.

The Corporation expects eligible countries to set priorities, consult broadly with civil society, and build on existing national development strategies. In Honduras, we found that the proposal was drawn largely from its Poverty Reduction Strategy paper. We also observed an engaged civil society with an active, ongoing debate regarding the selection of projects proposed to MCC.

MCC reports that it evaluates proposals' objectives, costs, and projected economic benefits. It also examines plans for fiscal management, procurement, monitoring and evaluation, and audit functions. Prior GAO work suggests that identifying host country-based institutions that have the capacity to execute these functions will be a key challenge for MCC. MCC's compact with Madagascar is funded at $110 million over 4 years, making MCC Madagascar's fifth largest donor.

Regarding coordination with key stakeholders—in an effort to leverage its small staff, the Corporation has sought advice, resources, and assistance from several Federal agencies. USAID will implement the threshold program. Treasury, Agriculture, and the Army

Corp of Engineers will provide technical assistance to evaluate compact proposals. MCC has also begun a dialog with other donors and NGOs.

Finally, regarding MCC's corporatewide management and accountability structures—the Corporation has developed key aspects of its administrative structures necessary to support its operations. In its first year, for example, MCC has expanded from 7 to well over 100 employees, and intends to reach a goal of 200 employees by the end of 2005. The Corporation has made some progress on structures needed to establish accountability and manage risk. For example, MCC established its Investment Committee to support the compact development process. It also established an audit capability through its IG, and the Board adopted bylaws to govern its activities. However, a range of key governance, internal control, and human capital structures remain to be implemented.

For example, the Corporation has not completed a strategic plan or an annual performance plan, and the Board has not yet fully defined roles and responsibilities in formulating and executing MCC's corporate strategy. We are recommending that the Corporation complete these overarching accountability structures.

In conclusion, Mr. Chairman, MCC has made considerable operational progress, and has signed its first compact. Of note, the Corporation's 2006 budget justification estimates that it will finalize two to four compacts each quarter through the end of that fiscal year. Given these ambitious goals, we view MCC's completion of corporatewide accountability structures as necessary to establish a viable and sustainable enterprise that effectively manages its institutional risk. Our recommendations are detailed in our written statement, and MCC has agreed to take these recommendations under consideration. We will continue to monitor the Corporation's progress in this regard.

Mr. Chairman, this completes my statement, our written statement has been submitted for the record and is publicly available at the GAO Web site. I'm happy to answer the committee's questions.

[NOTE.—Due to the length of the documents submitted, Mr. Gootnick's prepared statement and GAO Report will not be printed. They will be retained in the premanent record and can also be accessed at www.gao.gov/cgi-bin/getrpt?GAO-05-455T.]

The CHAIRMAN. Well, thank you very much, Mr. Gootnick. We thank you and your associates for a very detailed written statement, for your written recommendations, and for your very concise oral summary of those this morning.

The Chair would like to call now upon the Honorable Paul Applegarth, the CEO of the MCC, and a good friend of this committee. He has been a companion of mine as we've traveled on recent foreign missions. We have witnessed the work of some remarkable MCC personnel in the state of Georgia as they are working in the field on some of the things we are talking about today.

Mr. Applegarth, thank you for coming. Let me say your entire written statement will be made part of the record in full. Perhaps you would summarize orally and then we'll proceed to questions of both of our witnesses.

STATEMENT OF HON. PAUL V. APPLEGARTH, CHIEF EXECUTIVE OFFICER, THE MILLENNIUM CHALLENGE CORPORATION, ARLINGTON, VA

Mr. APPLEGARTH. Thank you, Mr. Chairman. Maintaining bipartisan support is part of my job description. I also want to thank the previous speaker for his efforts and those of his team. As we build our own internal structure and team, we've relied a lot on him and his team to help identify issues, spot potential areas of concern for us early, and help us to address them early on, and I find—even though they're an external reviewer—their efforts to be quite collaborative and very helpful to us.

The MCC is built on a commonsense idea. Foreign aid yields better results when invested where it will be used well, in countries that have put in place policies to support poverty reduction and economic growth. Policies such as good governance, investment in health and education, and creating an enabling environment for entrepreneurs.

The President has requested $3 billion in fiscal year 2006 funding for the MCC to help to reduce poverty and to preserve the strong incentive for positive policy reforms. That $3 billion appropriation ensures that MCC can credibly tell our partner countries that we can fully fund compacts to reduce poverty and spur economic growth. It is critical for MCC eligible countries to recognize the United States will live up to its Monterey commitment, and the $3 billion request helps us make such assurances.

My presentation today will focus on three areas. A discussion of the need for the $3 billion; the progress we were making on existing country proposals; and the strength of our current pipeline, and the steps we were taking to accelerate progress. Thus far we've received country proposals totaling more than $4.5 billion. Through due diligence, elimination of items that do not show a strong link to poverty reduction and growth, items that are not yet ready for consideration, or they do not appear to arise from an adequate consultative process—that $4.5 billion has been reduced to around $3 billion. However, that does not include the likely proposal from Morocco, which is expected to be fairly large.

Our current estimate is that the amounts required to fund the proposals from existing eligible countries are expected to exceed resources currently available from fiscal year 2004 and fiscal year 2005 appropriations by about a billion dollars. To approach the problem from another perspective, the Government Accountability Office found that the funding from existing appropriations will only allow MCC to fund between 4 and 13 compacts. In contrast to this minimum of 4 countries, and maximum of 13 countries, the MCC now has 17 eligible countries. Appropriations below $3 billion for fiscal year 2006 will most likely require reductions in the number or scope of MCC compacts, and force the MCC to forgo funding good proposals. Such reductions will undercut MCC's effectiveness, both in its direct impact on poverty reduction, and the incentive it provides for policy reform.

Let me now turn to the state of our current pipeline. I am both pleased and proud to report that MCC has made substantial progress since I testified before you last October. Our most recent notable event was the signing, last week, of our first compact, with

Madagascar for just under $110 million. The Madagascar compact marks an important step forward for MCC, but it is only a beginning. There are many more countries working hard for the opportunity to sign a compact. There are hundreds of millions of lives that we are in a position to improve provided we have adequate means.

In addition to Madagascar, MCC has already notified Congress of our intention to negotiate compacts with Honduras, Georgia, Nicaragua, and Cape Verde. Subject to successful negotiations, positive due diligence results and Board approval, we hope to sign compacts with all of them this summer. Honduras is up next with its proposal to be considered by MCC's Board on May 20.

We also have a robust pipeline of countries in various stages of compact development. This chart shows our most recent update, including the time required for due diligence, compact negotiation, Board approval and congressional consultation for each country. I realize it's difficult to see the details from where you are, but I think you get a sense of the momentum behind the current pipeline. The country names have been redacted, as these are ongoing negotiations with foreign governments, and represent our internal management assessment for where we are with each. The top five countries on the chart are those in active compact negotiations with MCC, plus Madagascar, which is already signed. The rest of the countries are in various stages in the proposal preparation or the due diligence process.

While this is a fluid document, and as an internal management tool is revised frequently, it gives you a sense of how we are managing the compact pipeline. My staff and I can also brief you and your staff in a more confidential setting about how we are progressing with each of the countries underlying this chart, some of the specific concerns we are addressing, when we hope to sign the compact, et cetera.

In terms of sectors, the country proposals reflect recurring themes. Rural development, agriculture and irrigation, land tenure, financial sector reform, private sector development and infrastructure. We're confident that the completed compacts with our eligible countries will yield positive results, results that are real and measurable. In fact, the MCC has already obtained results, even before spending money. Governments have consulted their citizens, some for the first time. Since the announcement of MCC indicators, in February 2003, the medium number of days to start a business has dropped from 61 to 46 in MCC candidate countries.

Many countries have targeted corruption, which is a primary MCC indicator. For example, Bangladesh's Finance Minister, when proposing a tough program targeting corruption, cited his country's exclusion from the MCC as an example of the heavy price it was paying for being branded a corrupt country. One official from an eligible country said, "Even if we receive less than requested, the intangible gains from taking control of our own development destiny are the most important part of the process."

Finally, I want to take this opportunity to address some of the concerns we've heard regarding the MCC timeline. The MCC's mission differs from many other assistance efforts. In disaster relief, and many humanitarian assistance programs, the diagnosis of the

problem, and the determination of the solution, are relatively straightforward to identify and execute; i.e., rescue the people in danger, feed and house them. MCC's task is fundamentally different. The problems more intractable, and the solutions less obvious. Identifying the real reasons for grinding poverty and finding answers that will lead to poverty reduction and long-term growth require serious consideration and thoughtful effort.

In addition, our partner countries are leading this process for the first time. They don't want quick fixes, they want help making structural, long-term changes in their countries that will reduce poverty. We do help, and together with them, we identify the objectives, determine what results the countries want and how they will be measured, develop detailed implementation plans and incorporate transparent procurement procedures, fiscal accountability, and donor coordination. And we're already seeing the value of this rigorous process.

A nonpartisan observer recently described our Madagascar program as a rare example of a development agency doing virtually everything right. While I prefer to describe it as an example of one of our partner countries doing virtually everything right, the point is clear: Identifying obstacles to growth, consulting broadly, focusing on measurable results and doing detailed planning in advance takes time, but leads to a better result. Our mission will be hurt if we cut corners to meet artificial deadlines, or rush money out the door.

I want to emphasize that preserving country ownership does not mean that countries are left without assistance during compact development. We don't sit passively by waiting for countries to act. During compact development, we do many things to speed up the completion of country plans. We want to do things right, but we also want to do things right, fast.

For example, our teams make frequent trips to eligible countries to work with our partners. In several recent weeks, we've had teams in five different countries each week. We engage various experts, both private sector and from other U.S. Government agencies to help. Even before a compact is signed, MCC is using funding under section 609(g) of its legislation to implement projects that will speed up compact implementation after signing. For example, to gather baseline data in Madagascar and Nicaragua, and to fund environmental impact studies and preliminary engineering design in other countries.

The MCC has the potential to accomplish a great deal in the struggle to reduce poverty. Mr. Chairman, you saw first-hand—during our visit to Georgia for Prime Minister Zhvania's funeral—the involvement and commitment of our partner countries' most senior leadership in MCC's efforts. We are strengthening the hands of reformers to accomplish important changes.

MCC impacts the poorest people in the world—people who live on less than $2 a day. We have an opportunity to reduce poverty in some of the poorest countries of the world, and we have a responsibility to the American people to invest their money wisely, with achievable, positive results. We do take these responsibilities seriously.

MCC and international development assistance are not only about bringing the best of America to our relationship to the world, but are a key component of U.S. national security. As the 9/11 Commission Report recommends, "a comprehensive U.S. strategy to counterterrorism should include economic policies that encourage development, more open societies, and opportunities for people to improve the lives of their families, and to enhance prospects for their children's future." That is, of course, the mission of the MCC. By lifting countries out of poverty, and providing people of the world's poorest nations a stake in their future, these countries will less likely be havens for terrorists.

The most recent country selection means that MCC has relationships with 30 countries, totaling 400 million people. By focusing our efforts on countries that rule justly, invest in people, and promote economic freedom, we can help the world, one country at a time.

Thank you again, Mr. Chairman, and your colleagues for your bipartisan support, and I will now be pleased to take your questions. Thank you very much.

[The prepared statement of Mr. Applegarth follows:]

PREPARED STATEMENT OF PAUL V. APPLEGARTH, CHIEF EXECUTIVE OFFICER, MILLENNIUM CHALLENGE CORPORATION (MCC), ARLINGTON, VA

Mr. Chairman, members of the committee, thank you for this opportunity to appear before you again as the CEO of the Millennium Challenge Corporation (MCC). I am grateful for the bipartisan support of the Members of Congress in creating and backing the MCC, and I hope to strengthen that bipartisan coalition. I am pleased to have much to report since we met in October 2004.

Today, I want to focus on topics that I believe concern this committee and describe our activities since we last met.

The President has requested $3.0 billion in fiscal year 2006 funding for the MCC to help reduce poverty through measurable results and preserve the strong incentive for positive policy reforms throughout the world. A $3 billion appropriation ensures that MCC can credibly tell our partner countries that we are ready, and able, to fully fund compacts that show a real commitment to reducing poverty and spurring economic growth. It is critical for Millennium Challenge Account (MCA) eligible countries to recognize that the United States is committed to funding good proposals, and the $3 billion request helps us make such assurances.

The amounts in the original concept papers and compact proposals totaled roughly $4.5 billion. Through due diligence, elimination of items that did not contribute sufficiently to poverty reduction and growth, components that did not appear to arise from an adequate consultative process, and phasing of items that might unduly delay an initial compact, that total has been reduced to around $3 billion. However, that amount does not include Morocco's proposal, which, given the size of the country, is expected to be fairly large. In short, proposals from eligible countries already are expected to exceed resources currently available by about $1 billion. In addition, MCC estimates that the addition of new fiscal year 2006 candidate countries, along with amendments to existing compacts, will increase the total requests from MCA-eligible countries by as much as $3 to $5 billion in fiscal year 2006.

As you are aware, on January 23, 2004, the MCC was established to administer the MCA, an innovative new foreign assistance program designed to more effectively focus U.S. development assistance on poverty reduction.

MCC is built on the commonsense idea that foreign aid yields better results when invested where countries have put in place policies that support poverty reduction and economic growth—policies such as good governance, investment in health and education, and an enabling environment for entrepreneurs. Indeed, MCC is about helping these countries help themselves.

In addition, MCC and international development assistance are not only about bringing the best of America to our relationship with the world, but as a key component of U.S. national security, as the 9/11 Commission Report recommends: "A comprehensive U.S. strategy to counterterrorism should include economic policies that

encourage development, more open societies, and opportunities for people to improve the lives of their families and to enhance prospects for their children's future."

When I met with you in October 2004, MCC had been in existence for less than 1 year, yet had significant milestones to report. Candidate countries had been identified, and the Board had already selected the first 16 eligible countries to submit proposals for funding.

By mid-2004, less than 8 weeks after MCC's Board had selected them, MCC teams had visited all 16 of our eligible countries. We are continuing to spend time on the ground in virtually every country and I can assure you that considerable progress is being made.

We count among our recent accomplishments, the MCC Board of Directors approval of our first compact with the country of Madagascar for just under $110 million. The MCC compact signing ceremony with the Republic of Madagascar was scheduled for April 7, but due to the attendance of Secretary Rice and Malagasy President Ravalomanana at the funeral of Pope John Paul II, we had to reschedule it for April 18.

The Madagascar compact marks an important step forward for the MCC. But it is only a beginning. There are many more countries working hard for the opportunity to sign a compact. There are hundreds of millions of lives that we are in a position to improve, provided we have adequate means.

We have already notified Congress of our intention to negotiate compacts with Honduras, Georgia, Nicaragua, and Cape Verde, and—subject to successful negotiations, favorable due diligence results and Board approval—we hope to be in a position to sign compacts with each of them by this summer. In short, while it is difficult to be precise about our schedule, we anticipate that compact approvals will proceed at a rapid pace.

To that end, we are also working hard on the compact proposals from the rest of the eligible countries that have submitted proposals. We are asking: What is the link to poverty reduction and growth? Who are the beneficiaries? How do you rank your priorities? How does this relate to what other donors are doing? These 11 countries are still working to be in a position where the United States can confidently make an investment, and we are helping them get there.

We are generally pleased with the quality and content of many of the compact proposals we have received. Several countries moved quickly into effective program development with MCC. Other MCA-eligible countries, however, were initially unfamiliar with the new approach and have taken longer to develop effective programs which MCC can support. MCC has adhered to the principles of country ownership, while neither pushing money out the door, nor meeting artificial deadlines for signing compacts. However, country ownership and responsibility does not mean that MCC abandons countries to work on their own. Rather, MCC has been proactively helping eligible countries to design workable programs with detailed plans for monitoring and evaluating performance, fair and transparent procurement procedures, fiscal accountability, and donor coordination.

While the concept of preparing their own development proposals was not entirely new to some of these countries, many eligible countries are accustomed to having donors set priorities, design programs, handle implementation, procure goods and services, and manage most other aspects of these activities. Not surprisingly, these countries initially looked to MCC to do the same. Other countries produced "laundry lists" of projects which had been left on the shelf from earlier donor programs.

In certain instances, eligible countries were informed that the initial proposals required greater involvement from other stakeholders in the countries' development process, such as civil society, academia, and the private sector. In other cases the proposals needed more work in defining the planned poverty reduction impact.

Specific problems have also surfaced in developing key components in the proposals, sometimes reflecting a shortage of institutional capacity to put a comprehensive proposal together. In such cases, MCC has worked with the countries to develop that capacity locally. It is a process that has taken patience and diligence on both sides to ensure that the proposal is the final product of the eligible country's decisionmaking, while MCC supports each country to move the process along as rapidly as possible. MCC continues to explore ways to facilitate faster, better compact development by MCA-eligible countries consistent with the principle of country ownership, such as more extensive use of compact development assistance under section 609(g) of the Millennium Challenge Act.

The result is that MCC has a robust pipeline of countries in varying stages of compact development, many of which will be finalized during the remainder of 2005. In our review of these proposals we have identified several recurring themes: Rural development, agriculture and irrigation, land reform and tenure, financial sector reform, and private sector development.

As discussed above, the current total of the 16 compact proposals we have received from fiscal year 2004 eligible countries (we are still waiting for a proposal from one 2005 eligible country, Morocco) is currently around $3 billion. In order to fulfill these valid requests we need more funds to do it. If the MCC is going to be able to fund our currently eligible countries, select additional eligible countries, select from the new category of lower middle-income countries eligible for the first time in fiscal year 2006 as provided in our legislation, as well as fund our threshold countries, there is a strong need for fully funding the President's request.

The concepts behind the MCC are bold and, as a package, unique. More importantly, they make sense for U.S. development assistance and for the countries we are helping. In 2004, the U.S. Government created MCC as an alternative to what has previously been done in the field of foreign assistance. The Millennium Challenge Corporation has the potential to accomplish a great deal in our steadfast struggle to reduce poverty. MCC impacts the poorest people in the world, people who live on less than $2 a day, those without access to clean water, without access to basic health care, those who suffer through disease and drought, and have no way to sustain themselves. The MCC was created to help to these people.

Through the years, the United States and others have devoted considerable funding to alleviating the effects of global poverty. Regrettably, however, there is far too little to be seen in terms of poverty reduction in relation to dollars spent. The MCC offers a new development assistance approach that requires measurable results for aid investment. We have learned that simply giving large sums of money away without quantifiable targets is not the most productive means of providing foreign assistance.

We know, now, that money is best spent on those countries that rule justly, invest in their people, and encourage economic freedom. This is the environment that can use the goodwill of the United States and translate it into sustainable economic growth. The MCC was established to make this happen in the poorest countries in the world.

Investing is always a risk when a measurable and positive outcome is desired. Bill Gates said that "giving money away is a far greater challenge than earning it." The MCC has eagerly accepted this challenge. We have taken on the responsibility of helping fortify the desired results and of assisting in the measurement of them—we expect the United States will be proud of the results we achieve.

In fact, the success of the MCC has already begun, as our role in the foreign assistance arena has yielded results even before spending money. Early indications tell us that our process is working. Morocco and Vanuatu have consulted NGOs and the business sector for the first time. The MCA incentive has also prompted reform; anecdotal evidence points to a strong MCA role. One country, for example, passed four pieces of anticorruption legislation and began enforcement, in the hope of receiving MCC assistance. Since the announcement of MCA indicators in February 2003, the median number of "days to start a business" dropped from 61 to 46 in MCA candidate countries. Many countries have targeted corruption—a primary MCC indicator—and are making strides to reduce corruption within their governments. Bangladesh's Finance Minister, Saifur Rahman, while proposing a tough program targeting corruption, cited his country's exclusion from MCA eligibility specifically as an example of the heavy price his country was paying for being branded a corrupt country. One official from an eligible country said, "even if we receive less than requested, the intangibles gained from taking control of our own development destiny are the most important part of the process."

MCC believes in country ownership. We believe that countries, no matter how poor, should have the opportunity to create a real program of economic growth for the benefit of their country—reflecting their priorities which address the needs of the people of their country—not just their government's or ours. Countries maintain their autonomy while working with the MCC and, through mutual effort, a compact takes shape.

Yet the MCC does more than provide assistance; it disseminates and encourages democratic ideals. The monetary incentive of the MCA is incredibly powerful. When a respectable but weak country is provided the means to grow and develop, the national security interests of the United States are better protected.

The MCC has great responsibility. We have a responsibility to reduce poverty in some of the poorest countries of the world and we have a responsibility to the American people to invest their money wisely with achievable positive results. We take these responsibilities seriously and we thank you for supporting us thus far.

While exactly how much we will obligate is driven by country priorities and pace of development and is contingent upon the MCC review process, provided our due diligence supports requests made in the compact proposals and our Board approves,

we expect to commit most of our current funding by the end of this calendar year or early in 2006.

The requests that we have on hand exceed the $2.5 billion appropriated thus far. From those resources the MCC also needs funds for threshold countries, expenditures for due diligence on the proposals themselves, a small portion for administrative expenses, and for compact development.

MCC also has the authority under provision 609(g) of its legislation to make disbursements to eligible countries to facilitate development and implementation of the compact.

Our compacts are implemented over 3 to 5 years, but, as directed by Congress, we obligate all our money up front and disburse as needed based on quantifiable benchmarks. This is part of the strength of the MCA and what will make us especially effective. Upfront monetary commitment helps motivate and support policy reform, assures all countries involved that substantial development progress can be made, that programs can be administered effectively, and that poverty will be reduced.

I would like to update you on the status of our Threshold Country Program. As you are aware, the Threshold Program is designed to support those countries that do not qualify for MCA assistance, but are close and have demonstrated a commitment to undertake the policy reforms necessary to improving their growth conditions and their prospects for qualifying for the MCA. In cooperation with USAID, we are currently working with 13 threshold countries. Seven threshold countries were chosen in September 2004 and were given a January 31 deadline to submit concept papers. Six more were chosen in November and were given a March 15 deadline. All 13 met the deadline and submitted concept papers.

Eight of the proposals are in excellent shape and we have suggested to these countries that they work on their detailed implementation plans and determine the results—quantifiable results—they will generate out of the programs. That work has started.

Five of the threshold countries' proposals do not yet meet MCC standards. We have given these countries an additional 60 days to improve their proposals. We and USAID are working very hard with these countries to give them as good an opportunity as possible.

I also want to take this opportunity, formally, to address and respond to comments I have heard regarding the MCC timeline—specifically the notion that MCC has been off to a slow start.

The Millennium Challenge compact development process (Appendix 1*) is thorough and it has never been done. As a point of reference, in the private sector, when an investment proposal is received, the parties have been through the process before, the objectives are known (e.g., financial return or credit-worthiness) and the management organization and implementation plan are known.

In contrast, the MCC and our countries are going through this process for the first time. Together we must identify our objectives, how we will measure results, and work to develop detailed implementation plans. We do not want the efficacy of the mission to be reduced because we are rushing to meet artificial deadlines or rushing money out the door. We want to do things right and we want to do them right the first time. But we also want to do the right thing fast.

My experience has taught me that you are doing well in the private sector if it takes only 4 to 5 months from the time a sound and well-supported proposal is received until an investment is made—and I am sure many of you can attest to this. I am told the World Bank takes an average of 18 months to make a lending decision. We received the first draft of Madagascar's compact proposal in October 2004. In only 6 months, Madagascar and the MCC have succeeded in creating a workable compact that will reduce poverty through economic growth. Certainly, this is a good accomplishment by any standard.

Preparing a proposal is a new approach for our partners. Part of the novelty of MCC's approach is that if governments create a prodevelopment policy environment, they are given a significant amount of responsibility in establishing projects and goals, focusing on outcomes, and ensuring community responsibility. And we are actively working with them to develop the best possible proposals as fast as possible. This takes time, but we encourage our countries to take the time to create an excellent proposal, then work with them to develop a program as quickly as possible.

For example, we are using the 609(g) authority in connection with the Madagascar compact to provide some initial funds to do baseline data collection to facilitate compact implementation. The lack of available data and local capacity to collect statistics in rural areas poses significant timing challenges for measurement of the program. This use of 609(g) funds will substantially accelerate the implementation of program activities and the establishment of measurable outcome targets.

Also, MCC teams make frequent trips to eligible countries to work with our partner's teams there. In several recent weeks, we have had teams in five different countries each week.

MCC engages engineers and consultants to help refine country plans following proposal submission; in addition to providing our own funding and resources, we have arranged with UNDP to set up a capability to fund some items, if requested by countries.

MCC has identified "Lessons Learned" from Madagascar and other countries that are more advanced in compact development, and is holding meetings and seminars with other countries, including:

A Washington seminar for all Ambassadors to the United States from eligible countries.

Outreach with a similar message to U.S. Ambassadors and USAID mission chiefs during country visits.

In addition to formal seminars, we meet regularly with government officials from MCC countries visiting Washington, to focus on solutions to current obstacles in the process, and on next steps.

MCC's Web site is regularly updated with compact guidelines (in seven different languages) and other useful information, and the Madagascar compact will be posted as an example as soon as it is signed.

The Millennium Challenge Corporation is not a quick-fix to poverty. We put substantial time into compact development and review to ensure that the U.S. investment will make a definitive and positive impact on the poorest countries in the world. We are fiduciaries of the money Congress has appropriated. We remain committed to making sure the American taxpayers' investment is used wisely.

Because Madagascar was the first eligible country to sign a compact, I would like to briefly expand on it.

Years of instability have left it one of the poorest countries in the world. Out of a population of almost 17 million, over 80 percent live on less than $2 a day. When the United Nations ranked countries on the Human Development Index—or better "Human Misery Index"—Madagascar ranked at the 85th percentile as one of the very poorest countries. However, in the last 2 years Madagascar has demonstrated a strong commitment to good governance and social investment. The government is implementing wide-ranging, anticorruption, financial management, and judicial reform policies.

Poverty in Madagascar is overwhelmingly rural. Its agriculture productivity is among the lowest in the world; 73 percent of Madagascar's population live in rural areas; 80 percent of those who live under the poverty line are rural inhabitants. In this situation, the most effective vehicle to reduce poverty is for the rural poor to invest in their land, to plant new crops, to learn how to increase productivity, to improve farming methods, to get credit to implement these new methods and, finally, sell to new markets.

Consequently, the Government of Madagascar asked MCC to support a major effort to attack two of the root causes of poverty: First, a weak land-titling system that fails to provide the incentive or collateral for investments in poor rural areas, and second, a dysfunctional financial system that fails to serve the rural poor.

The Malagasy people believe that reforming the broken-down land-titling system will give them clear rights to their property and the ability to borrow against it; the best asset they have to improve their lives and those of their children. Improved property rights will also help reduce the incentive to engage in environmentally destructive practices, such as slash-and-burn land clearance.

In developing these concepts, the Government of Madagascar engaged in consultation focused on developing commitment around a sound program for consideration by MCC. A national workshop was organized in September 2004 to discuss the obstacles to growth and poverty reduction consisting of more than 350 participants, including President Ravolomanana, to describe the MCA and discuss obstacles to economic growth and poverty reduction.

The Government of Madagascar then organized six regional consultative workshops, each consisting of 50 to 150 representatives of the business community, nongovernmental organizations, civil society, and donors in all the provincial capitals. The government also ran radio and TV broadcasts about the MCC, and published newspaper ads that announced meetings and called for submissions of ideas from all segments.

The Land Tenure Project of the compact will formalize the titling and surveying systems, modernize the national land registry, and decentralize services to rural citizens. The Financial Project will make financial services available to rural areas, improves credit services, and create a streamlined national payments system. The

Agricultural Business Investment Project will help farmers and enterprises identify new markets and improve production technologies and marketing practices to sell to new markets.

To the credit of the Malagasy, they have proven to be excellent partners in designing systems and procedures that provide the proper controls and safeguards over the use of MCC funding.

Accordingly, the Malagasy will engage a professional firm to control funds, manage cash, and oversee accounting and procurement services. The Madagascar Steering Committee will select this firm as a result of a competitive process that is already underway. Our agreement with Madagascar also requires regular independent audits, and we will conduct our own onsite reviews over the course of the compact.

The MCC project development, due diligence, and implementation supervision process requires indepth design, expertise, resources, and time. After the MCC received legislative approval in January 2004, we started with a staff of seven detailed employees. We now have between 110 and 120 people, plus detailees and PSCs, and we're on plan to reach to our target number of 200 staff by the end of 2005. Talented staff have come from within the government, the private sector, universities, nongovernmental organizations, and international institutions. That has taken a fair amount of our time, particularly because we need highly skilled people with specific qualifications.

As we move forward with our other compact negotiations, we are seeking input on a Natural Resources Management indicator from a broad range of natural resource experts from academia, think tanks, and NGOs. Furthermore, we have an ongoing and active dialog with these groups and institutions about MCC operations and policy matters of mutual interest. We are grateful to them for their support and their constructive feedback on issues such as the consultative process. In fact, with regard to that issue, these groups have even mobilized their partner groups in countries to engage in the consultative process and to provide us feedback, which we greatly appreciate.

I would like to conclude my remarks today by putting the President's request for $3 billion in context.

The Government Accountability Office found that, using data on MCA-eligible countries, MCC would need to have total resources of roughly $3.4 billion to be one of the top three donors in 8 to 14 countries. In other words, to have the impact of one of the top three donors in eligible countries, MCA programs would need to be on the order of $250 million per country on average, based on 3-year compact programs; 5-year programs would require proportionately greater funds. This analysis, combined with our experience to date, forms the basis for our projections. (Appendix 2*)

MCC must focus its available resources to fulfill its mission of supporting transformative development programs. MCA is intended to provide a significant policy incentive to candidate countries by commanding the attention needed to galvanize the political will essential for successful economic growth and sustainable poverty reduction, and needs substantial resources to have that incentive effect.

Appropriations below $3 billion for fiscal year 2006 will most likely require reductions in the number or scope of MCC compacts, and/or force the MCC to forego funding good proposals. Such reductions would undercut MCC's effectiveness in having a significant impact on poverty reduction and economic growth.

Moreover, for fiscal year 2006 and beyond, up to 25 percent of the funds appropriated for fiscal year 2006 can go to lower middle-income countries as specified by our legislation. Therefore, there will be two competitions: One for lower income countries and one for lower middle-income countries. This will further increase the demand on limited MCC funding.

We are deeply appreciative of your support thus far and are grateful to have had the opportunity to begin our mission. There is much more work to be done, however. To make significant progress in reducing poverty we need to uphold the commitment made by the United States. Now is an opportunity to reaffirm that the United States is serious about reducing poverty on a global level.

The most recent country selections means that the MCC is in a position to have potential relationships with as many as 30 countries—some of the poorest in the world—totaling 400 million people. By focusing our efforts on countries that rule justly, invest in their people, and promote economic freedom, we can help the world, one country at a time. This will be beneficial for those countries, for the impoverished people living in them and for the United States.

I want to end by thanking the committee, which under the leadership of Chairman Lugar and Ranking Member Biden has given the MCC true bipartisan support,

which has been vital to our accomplishments so far, and which will be even more vital for our future success.

I welcome any questions you might have.

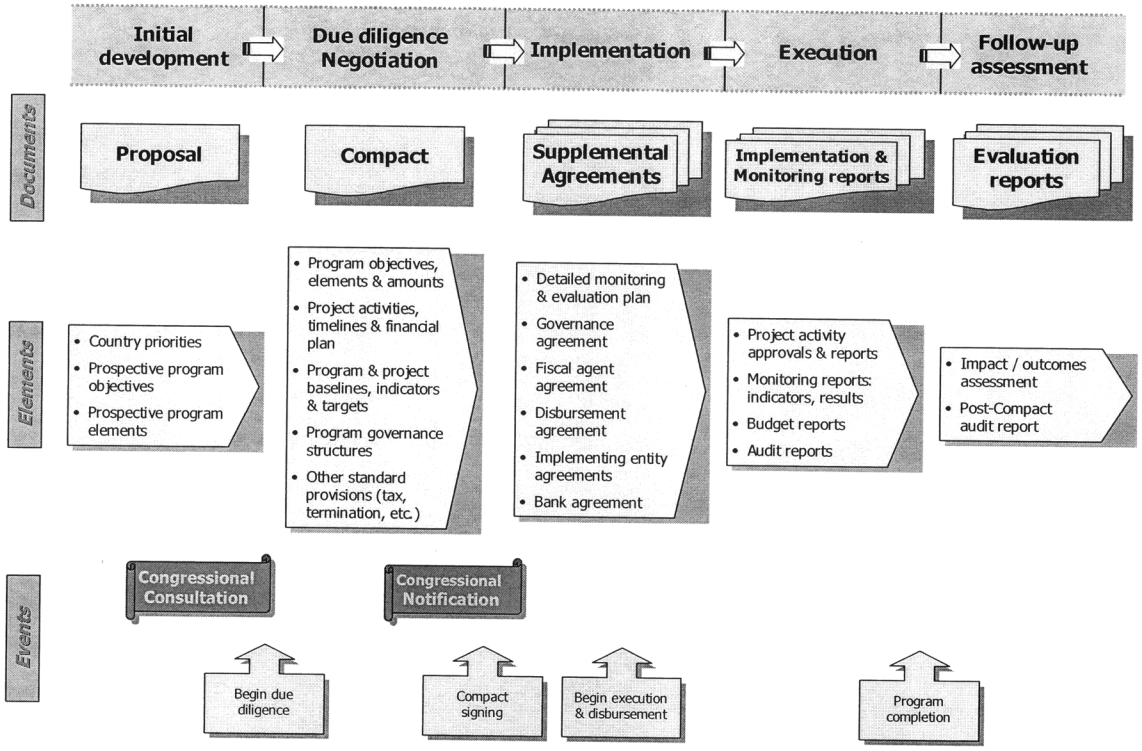
*Note.—Appendix 1 and 2 referred to are in the GAO statement submitted by David B. Gootnick which has not been printed in this hearing but has been retained in the permanent record of the hearing.

CONGRESSIONAL BUDGET JUSTIFICATION SUMMARY

[In millions of dollars]

	Funding FY 2004/FY 2005			Funding FY 2006		
	No. of trans-actions	Average amount	Totals	No. of trans-actions	Average amount	Totals
Low-income countries	12		2,278	6	291	1,745
Amendments to earlier compacts	—		—	3	100	300
Low middle-income countries	—		—	4	170	680
Total compacts and amendments	12		2,278	13		2,725
Threshold programs			130			140
Total assistance			2,408			2,865
Administrative expenses			55			85
Due diligence/monitoring & evaluation			17			48
Audit expenses (Inspector General-USAID)			2			2
Rescissions—FY 2004 and FY 2005			18			—
Total administrative, due diligence, M&E			92			136
Total obligations			2,500			3,000

MCC Process Overview



The CHAIRMAN. Well, thank you very much, Mr. Applegarth, for your statement and for your leadership. We'll proceed with questions from those who have gathered here today. The Chair will suggest a 10-minute limit. We'll have one round, and maybe two, and maybe three, if required, so that we have an opportunity to explore this.

Let me commence, Mr. Applegarth, by pointing out the obvious. In each of our hearings, we've discussed our own unusual budgetary structure in this country in which, in this particular case in this year, we've tried to set aside $3 billion for a program which we now know something about. You've described in previous hearings the data that you seek, how nominees come to the fore, and likewise the parameters of what kind of assistance might be available, within the $3 billion framework for the entire group, whether this involves a minimum of 4 countries, as you say, or a maximum of the 17 that are now potentially in the zone, with others still trying to sign up.

As you pointed out, the effects of this program have been extraordinary with regard to countries that are not yet eligible and may not be. For example, in a mission during which I had to look for Weapons of Mass Destruction in Albania last August, I found that the MCC was of extraordinary interest to the Albanian Government. It was off the charts of much of our consideration. We explored how they might shape up for the Millennium Challenge. The corruption issue, in particular, was foremost. And as you've quoted a development official in another country, even if countries don't finally qualify for the money, the internal changes in governance are healthy for their people, healthy—really—for the world. So, an influence from this program that often is not overtly cited, can nonetheless be clearly observed in countries around the world.

Now, the dilemma that we have posed for you in each hearing is that if there are not results to show for the authorization and the appropriation, very rapidly, then rival means of doing good and spending the funds and so forth, will not only be found, but suggested and forwarded, at the expense of the MCC while it is still working its way through. So, we always couple these hearings with the thought, "Please, make decisions and spend money," but then on the other hand, we point out, "Don't spend your funds irresponsibly. Make sure all the controls are there, and involve the government in that process."

On the face of this, this is contradictory. We are trying to root out corruption in a culture doesn't happen in a 2- or 3-month period to fit our authorization or appropriations cycle—and we are attempting, likewise, to bring about extraordinary changes which are profoundly important in the life of those countries. This process takes time, and yet for all of us there isn't much time. There are results that need to be achieved. This is why we call you today, and we call Mr. Gootnick as an auditor of the whole endeavor, looking at measurements from the outside, saying, "How are we doing?"

Now, having said all of that, the fact is you have got a compact with Madagascar, and there are a list of other countries you have suggested that are close. And, maybe Madagascar will expend its funds and be able to report—through the local press, through international audits—results. Meanwhile, we are conducting hearings

about multinational development banks, which is another way the countries have been receiving funds. For a long while, and in a multinational sense, we have been finding that in some cases, those funds have gone to governments that displayed quite a bit of corruption. The citizens of the countries lost twice. First of all, the project didn't happen very well, if at all, and second, the citizens still had a debt hanging over them. And then the world community holds conferences on how much of the debt should be relieved. So we know that all the money is going out, and the expenditures are documented. You could make a case for humanitarian efforts. Sometimes the results on the ground are de minimis. The results, with regard to the world financial picture, are disastrous. So, you're curing that, but it's tedious. And I keep going through this because I'm not sure how to resolve it.

We had, in this committee during the markup—and you were here in the audience, witnessing—the authorization in which a serious amendment came forward to tailor the $3 billion back to a smaller figure. And the arguments offered were good ones, namely, there are agencies now doing good things, and perhaps MCC is not quite up to it yet, maybe we just are not getting along, and therefore maybe $2 billion or $2 billion-plus would do all of that.

And we'll have that argument almost every year until there is a track record that indicates that the flow moves, that there is progress, that decisions are being made, despite our testimony about corruption in the development banks. There will be conferences, you'll take part in these on Africa, even this year. And rightly so. There is tremendous interest in the pervasive poverty of a majority of African countries—in addition to problems of starvation. We hear testimony from the World Food Program officials, as well as testimony about HIV/AIDS and tuberculosis—there are horrendous complications and mortality.

So, the pressures will be on this country and the rest of the world. What are we going to do about it? We've been talking about a program to alleviate world poverty. But here, how starkly can you make it? In the midst of this, the criticism will come—where does the Millennium Challenge fit? How many African countries? How many are likely to be involved? And you can say, well, some of the governments are not really up to speed on the corruption level, on the planning level.

As a result, American taxpayer funds under our charter really can't go to this, but others are going to be arguing funds are going there, they're going with regards to AIDS, and tuberculosis, the World Food Program—and you could argue back—but with sometimes mixed results. Misappropriation, dictators who starve other people in the same country while we're trying to feed people. This is the way the world works. And I parse it all in this way to ask you, once again, for the best rationalization of why this program is different, why it's better, why we should be patient, why the $3 billion is the right figure for this? What can we anticipate your request will be next year? In other words, give a prognosis, if you can, for the future of this program.

Mr. APPLEGARTH. Thank you, Mr. Chairman.

First, I take your points quite seriously, and there are, of course, other competing needs for funds that are valid. I would also think,

it would be fair to say, if you took a survey of MCC staff it would be unanimous that no one is more impatient than I am, in terms of getting results, in terms of getting compacts done.

We are having an impact already, in terms of policies, we are having an impact now in terms of results. At the end of the day, the best evidence that the MCC model works will be good compacts done, having an impact on the ground, I think all of us believe that.

Madagascar, frankly, did an amazing job from the time they gave us a proposal in early October, which was simply a couple ideas. We took those ideas, determined what they wanted, determined how the implementations and plans were going to work, determined how results would be measured, and they had it ready for us to recommend to the Board in under 5 months. From the time we received the initial idea, to signing, was about 6 months. Even against private sector standards, that's a very good track record, where typically it would take 4 to 5 months from the time you get a fully developed proposal from an existing management team, with the results known, to the time you were able to sign. They did a very good job. I'm told the IFIs, International Financial Institutions, take on an average of about 18 months.

Nonetheless, we're trying to keep our process to 5 or 6 months. Most countries won't meet that standard, but if you're going to do it right, with detailed plans, get the things in place, you have to take time to make sure that the money's going out well, the money's going to get from us to the right place. But we take the charge very seriously. The need is there, we believe this is a model that will work to lead to long-term poverty reduction and growth, and we are as impatient as you all are to be able to show results.

The CHAIRMAN. Thank you very much.

Senator Nelson? All right, Senator Obama.

Senator OBAMA. Well, thank you very much, Mr. Chairman. Thank you Mr. Applegarth, Mr. Gootnick.

I want to focus my questions on a couple of fronts. I'm somebody who's supportive of the notion that we do no good for the people of countries by funneling money to governments that aren't effective. And I think the basic goals of the MCC are ones that I'm approving of, and supportive of, and I wish the utmost success for the Millennium Challenge Corporation.

There are two areas that I'm trying to figure out, and you may not have all the answers, but maybe you can give me some understanding of how you're thinking about them.

The first has to do with funneling our aid through a variety of different mechanisms. In a 1996 article in Foreign Affairs, former Secretary of State Lawrence Eagleburger wrote, "The current structure of U.S. foreign policy bureaucracy invites foreign countries, both allies and adversaries, to play agencies or issues against each other. A consolidated structure would buy the United States more effective diplomacy for the buck."

Currently, you have USAID, you have MCC, and you have the State Department making determinations on allocations of foreign assistance resources. This is setting aside special projects like Iraq or Afghanistan, I don't know where Pakistan falls in that category, but I recognize these are unique areas where there are strategic

objectives that the administration is trying to pursue. Setting aside special objectives I'm wondering whether we are losing some coherency in terms of how all these programs fit together.

So let me pose some specific questions.

In a country where AID is already functioning, and that is also an applicant for a Millennium Challenge grant, does the AID operation suspend itself during the operation of MCC, or is it running on parallel tracks while in this particular country? What is the relationship going to be between MCC and existing foreign aid programs? Will the MCC supplant and take over all our foreign aid efforts in a particular country that's received the grant, or will the AID program continue? And if so, then how do you make sure that they're not working at cross purposes?

Mr. APPLEGARTH. Thank you for your question, Senator.

I think you should first start with recognizing there are different types of foreign assistance, with different purposes. AID, I think, has an unparalleled track record in, for example, disaster relief. They stepped up in the tsunami, and in other areas to really do a tremendous job similarly, in humanitarian assistance. I think the State Department programs are targeted toward democracy, political affairs, ESF funding. OPIC, another agency which you didn't mention, targets the development of the private sector, EXIM bank—each has a particular mandate or function.

MCC's function is to try something different that is truly focused on results, on selectivity among the countries, where countries have to compete for it, with the idea that you are really incentivizing, and recognizing, governments that are demonstrating, not promising, but actually demonstrating—a commitment to poverty reduction by putting good policies in place. And you take our model of countries competing, countries putting good policies in place in advance, before we even consider them for funding, and then we work with them to really focus on poverty reduction, and not poverty alleviation; we focus on results. Then, I think, that is the context. We do cooperate closely, and coordinate particularly with AID quite closely, and I'll be glad to elaborate, but I don't want to interrupt you.

Senator OBAMA. I appreciate what MCC is trying to do, again, I'm just trying to figure out what is the relationship in a country, let's say, like Madagascar that's receiving $35 million in AID funds. Are those $35 million still flowing? Will they be spent by AID or channeled through MCC? Are there AID workers still on the ground in Madagascar that are working with the same government officials that MCC is? Are there some requirements incorporated into the MCC plan that indicates how existing aid should be coordinated? I'm trying to get some specifics on that.

Mr. APPLEGARTH. I think you see the levels of cooperation—and let's talk specifically about AID—in a variety of ways. You see it first, here in Washington, Administrator Natsios is a member of the MCC Board, I see him regularly, we both attend the Secretary of State's morning meetings, so I see him at all of those. We also meet regularly, at least once a month, to go through specific operational issues. In addition, AID is administering the Threshold Program, together with us.

In the field, the AID mission is in place in Madagascar, will continue to function and operate; they are doing some things in rural development, doing a variety of other things, and those programs will be continuing. We have certainly discussed at the local level there, our efforts, and not only in Madagascar, elsewhere the AID mission directors. We seek their advice in both evaluating programs, and reviewing them, and we want to make sure that our programs are fully coordinated.

Senator OBAMA. So, Mr. Applegarth, am I to understand that these other programs are going to still be operating even as MCC is taking place? They're not supplanted, is that correct?

Mr. APPLEGARTH. That's correct, I think individual accounts may go up and down, and I don't believe AID has set its final programs for fiscal year 2006, I think they're still waiting for the final appropriation this year. But, I personally believe that MCC is intended to be additional, if we're going to have a proper impact. I think if you look at the administration requests overall for foreign assistance in the 150 account, they've gone up substantially over the last several years, even not counting MCC, and of course, MCC will represent a significant increase as it goes forward.

Senator OBAMA. Let me shift topics, because I've got a limited amount of time here. I want to discuss the strategic value of MCC. I want to play Devil's advocate here. Madagascar is a beautiful country with wonderful people, and we want to make sure that they are receiving rewards for doing the right thing. But when I look at the universe of potential MCC compacts—Honduras or Nicaragua, or Cape Verde or Madagascar—it's not clear to me how grants there impact the strategic interests of the United States. This seems especially true in the context of other countries with enormous poverty, enormous corruption, and seismic influence, in terms of how countries and regions are operating. What if we said, we're going to take all this money and we're going to give it to Nigeria, Indonesia, and Mexico, where there's rampant corruption, but also enormous populations, enormous strategic considerations? Why would we not take into account some of our larger strategic objectives in terms of reshaping the climate in these areas? Presumably, if Nigeria underwent significant government reforms and economic reforms, that could have spillover effects into the entire western portion of Africa, for example. Has there been any discussion about how we think about that? Or is it very much just going to be whichever country, no matter how small, meets the MCC criteria and comes up with the best proposal?

Mr. APPLEGARTH. I wouldn't underestimate our scale, Senator, with existing eligible countries, and threshold countries, we have relationships, as I mentioned in my remarks, with 30 countries, 400 million people. If you exclude the populations of India and China, that represents a fairly significant portion of the population of the developing world.

Moreover, the low middle-income countries, which we could not legally consider before, will be considered out of this coming appropriation, in addition to the list of threshold and eligible countries. And, I think you'll see some fairly large countries potentially competing this year.

In addition, the incentive effect is there. We would like, very much, to work and to have influence on some of these countries. By chance, the Finance Minister of Nigeria is coming by this afternoon, we're sitting down and talking about MCC criteria and how they measure, and how we measure up, so that we can have a greater influence there. Similarly, President Yushchenko, when he was here, from the Ukraine, was already talking about MCC and how they want to qualify, so I wouldn't diminish the value of our impact in looking at the countries where we're currently operating. The fact that we chose eight countries in sub-Saharan Africa, I think, surprised everybody out of our first group. To me, it was a clear statement that there are good leaders in sub-Saharan Africa, and good governments that are helping their people, and they do serve as examples to their neighbors.

Senator OBAMA. Thank you, Mr. Chairman.

The CHAIRMAN. Thank you, Senator Obama.

Senator Coleman.

Senator COLEMAN. Senator, I'll yield at this time to Senator Martinez.

The CHAIRMAN. Very well. Senator Martinez.

Senator MARTINEZ. Thank you, sir. Thank you, Mr. Chairman. Thank you, Senator Coleman.

Sir, I wanted to pursue this sub-Saharan subject with you. I know that over the 1980 to 2003 timeframe I think we could count up about $32 billion in assistance over that time, while at the same time, apparently a per capita GDP in the sub-Saharan area has fallen from $660 to $585. There have been other sources that have provided bilateral and multilateral assistance with billions of dollars as well, so apparently assistance has not been the key ingredient that has not afforded them a path to greater development and greater prosperity. And I am pleased to see that 8 of the 17 countries eligible are in sub-Saharan Africa, and I commend you for the relationships you've developed there, and I'm intrigued with where you are with Cape Verde, which I understand has submitted, you've submitted a letter to the chairman for the 15-day period of consultation, prior to starting the compact negotiations, so I wondered if you could update us on the status of Cape Verde and their application and where we are with them.

Mr. APPLEGARTH. Thank you, Senator. I think anyone who looks at the performance in sub-Saharan Africa over the last number of years recognizes that simply disbursing funds isn't a solution to the problem, and that you have to learn lessons from what's worked and not worked. Those lessons are the lessons on which MCC is built. If aid is going to work, country ownership is important, policies are important, focusing on results, outcomes—what are you going to get for this money that you're investing? Even though it's grant money, we view this as an investment, we look for a growth return.

These are the models upon which MCC is built, and which we're trying to implement. We very much want to have an impact in sub-Saharan Africa, and I think we already are having it, and will continue to have it. But it has to be done in a way that is focused on results, unless you're doing simple humanitarian assistance. Humanitarian assistance is important, but it does not get you out of

poverty reduction, it does not help countries reduce their dependency on foreign aid.

With particular reference to Cape Verde, I think progress has moved along quite well. We are in the final stages of due diligence, my current estimate is that it will not be ready for a consideration of the Board in May. Assuming we have a June Board meeting, I think it's quite likely that, based on the latest information I have, that it would be ready for consideration by the Board by, in June, for signing sometime in July.

Senator MARTINEZ. I also noted that, in Latin America there were not as many countries in which you are engaged. Can you tell us a little something about that region, and what obstacles you encountered to being able to develop in those countries?

Mr. APPLEGARTH. The principle reason there are so few Latin American countries that are eligible right now is really the income threshold. By design, in our first 2 years MCC is only focused on the poorest countries in the world. We have an income ceiling and, I think six or seven Latin American countries are even on the list to compete. Obviously Cuba does not have a government that promotes good governance, full freedom, or the kinds of things we measure. We do not believe the kinds of policies they put in place lead to poverty reduction and lead to growth, therefore they're not eligible to receive funds, but the point is, although they're under the income ceiling, they don't qualify. Haiti is in a similar situation; the balance of the countries, Honduras and Nicaragua, they're both eligible, Bolivia is eligible, Paraguay and Guiana have been named as threshold countries. I would expect to see a significant increase of the number of countries on the candidate list in November when, for the first time, we can include lower middle-income countries on the list.

Senator MARTINEZ. So, that will be an ongoing process in which the threshold will rise as time goes on?

Mr. APPLEGARTH. Under our legislation there are two ceiling caps. One is for lower income countries, that's roughly $1,450 per capita; in addition, under the legislation, Congress gave us the authority, starting in our third year, which is fiscal year 2006, to begin considering lower middle-income countries and up to 25 percent of the program funds can go to them.

Senator MARTINEZ. You know, I have some experience with domestic programs that assist with trying to eliminate poverty and improve economic development conditions and so forth, and one of the things we've found is that oftentimes, those in most desperate need—communities and cities that had the most need—were the least capable of managing those funds which were sent in their direction, or to prepare the applications for competitive grants. What are you doing about capacity building within those nations that are in need of funds, in need of assistance, in need of participation with the Millennium Challenge Account, but yet, may not have the wherewithal to properly cross t's and dot i's and be able to qualify and be competitors?

Mr. APPLEGARTH. I think even the best of our countries need help. They're being asked to do this for the first time, in terms of really taking ownership. That's what we're really trying to do, actively now. We don't interfere in the priority-setting process, be-

cause we're afraid that if we start advising or saying what the priorities should be, they become our priorities, not the country's. But once that priority-setting process is underway, we provide engineering help, we provide help in program development, whether it's 609(g) funds, visits by our people. We had seminars, during the recent World Bank IMF meetings, on lessons learned from our most advanced compacts. We had a workshop for senior ministers from eligible countries, what's worked, what hasn't worked. Leaving up to them how they want to approach it.

But it's clear that things like dedicating a full-time host country MCC coordinator is important. Involvement of the senior leadership of the country is important. Dedicating a certain amount of resources to it. These are the kind of things, very practical nuts and bolts things, but we're trying to assist the process to move it on really quickly.

Senator MARTINEZ. One of the things that frustrates me, I think, as I look to this process, is that sometimes countries who have tremendous need also have an equally dysfunctional government, or a corrupt government, and I wonder how we break through that cycle so that we can get help to people that desperately need it and move them out of poverty into better lives, while at the same time, having to work in an environment where the governmental structures are not sufficiently stable or transparent enough for us to be able to work with them.

Mr. APPLEGARTH. Senator, that problem concerns us, too. Right now, we're trying to set a model of working with the best, poorest countries in the world, with the idea that if they can set an example, and we create an incentive for other governments to put policies in place that will lead to poverty reduction and growth, so that people can see their neighbors doing a good job.

I think realistically, there are certainly a lot of very poor people in countries we're not working with. How you best address them is something we're trying to think about. Other parts of the administration are trying to think about it, too, because it's pretty clear that working in an MCC model with those governments as they currently function is not a solution. You may have to do as AID does; go in targeting directly the populations, go around the government, try to do some other things, and maybe try to focus primarily on poverty alleviation, rather than the long-term poverty reduction, until you have a true part of government that's committed to doing things.

It is a real dilemma; we understand it. Hopefully by what we're doing with the better of the countries, we can be an example to help the countries that don't measure up at this point.

The CHAIRMAN. Thank you very much, Senator Martinez. Let me just mention that the questions, by and large, have been directed to Mr. Applegarth. Some may be directed to you, Mr. Gootnick, but if you have a comment, and it's appropriate, even if a question's been directed at Mr. Applegarth, please make your comment, and if you don't, don't feel compelled to. But at the same time, we really want to have the insights of both of our distinguished witnesses, and we appreciate that.

Senator Nelson.

Senator NELSON. Thank you, Mr. Chairman. Tell me about the programs that you're negotiating in Honduras and Nicaragua.

Mr. APPLEGARTH. I believe both the compact proposals are public, but I will describe them in general terms. Both are targeted toward rural development. Increases in agricultural productivity, increasing rural incomes. In the case of Honduras, which is somewhat more advanced at this stage, they are targeting a region to the western part of the country, focused really on a broad-based integrated rural development effort. Increasing crop yields through drip irrigation, through agricultural extension, through microcredit, through rural roads. It then is linked to getting those crops to market. So from the rural roads, you go into the secondary roads, you go into a major highway stretch that we're funding—if the Board approves—we will fund. The stretch is the final length between a road that is being funded by the World Bank, and another road that is funded by the Inter-American Development Bank, where we are the final link to complete a corridor that will not only allow the crops in the rural program areas to get to market, but will also provide a major corridor that links many Central American countries together.

Senator NELSON. How is that different from the USAID program?

Mr. APPLEGARTH. I would perhaps like someone who's somewhat more expert on the AID program to comment in more detail, but actually parts of this program are built on AID efforts, including some of their agricultural extension efforts in Honduras, which I think are quite impressive in terms of what they've achieved in crop diversification. I think you would see it being different in its integrated focus, its scale, its focus on overall country competitiveness, and the involvement of the country leadership in trying to assure that the program will succeed against measurable benchmarks and outcomes.

Senator NELSON. So, if I talk to the President of Honduras, for example, he will be able to tell me the difference between this program and USAID because he is committing to achieve certain goals. Is that what you're suggesting?

Mr. APPLEGARTH. I would suggest that if you talk to President Maduro, he would be able to describe to you, intimately, the details of the MCC program; how and why it is important for Honduras; why it is a strategic priority for them; how it addresses poverty reduction and growth. I don't know whether he knows all of the programs that AID is doing.

Senator NELSON. And if I ask him, "Well, what's the difference between that and the USAID program?" What would he say there?

Mr. APPLEGARTH. I would hate to speculate, but I think he would say one difference is that through a consultative process here, this is our program. These are the areas we think are most important, this will lead to long-term poverty reduction here, and lead to long-term growth here.

I can tell you what the senior leadership of Madagascar said, because they were quoted in the papers, and we took great pleasure in it. They did not talk about the MCC program. They talked about Madagascar's program, and how they were going to use the MCC funding. They talked about their goal: How they wanted to improve

rural incomes, that they were focused on the 80 percent of their population that was poor, that lived outside the urban areas, with 70 percent of them living on 41 cents a day or less. And that their primary focus was to increase the incomes of these people. But it is their program, they designed it, and we're working with them to help implement it. It's a very different dialog, it's a very different way of describing what they are trying to do.

Senator NELSON. I notice that Paraguay is in the second group of countries with which you're expected to negotiate. It's well-known in Latin America sometimes, even as a standing joke, about the level of corruption within the Government of Paraguay. And they're trying to do something about it. Now, tell me, as you negotiate with a country, or you think about putting a country on your list, how do you think the MCC program can help a country with so much corruption?

Mr. APPLEGARTH. Yes, sir. First of all, to clarify; Paraguay is a threshold country, it's not an eligible country, and that means that the Board is not recognizing them as being fully eligible to submit a proposal for poverty reduction through growth.

Where we would assist Paraguay, if they come to us and say "This is our program, we want to improve performance under your MCC indicators so that we have a better chance of being selected to be eligible for MCC funding, will you help us?" That's what the threshold program is about. In the case of Paraguay, we've received their initial proposal. As you can imagine, it is targeted on corruption. They recognize that they need help. The inheritance, whether it's in the genes or the product of the regime for years and years, I don't know. But the point is, you do see signs of serious effort and commitment by the government to begin to root out this problem. And, we'll see what the program looks like, and finally, whether it measures up. If the commitment is there, and the program looks like it's going to work, we'll provide them some funding, but we're still in the early days of the project.

Senator NELSON. Mr. Gootnick, why does the program need more money, since they haven't spent what's been appropriated thus far?

Mr. GOOTNICK. Well, Senator, Congress has provided the Millennium Challenge Corporation considerable flexibility in the use of its funds so that, unlike AID, these funds are not earmarked, these are no-year funds, and the appropriations language stipulates that the compacts be funded up front from day one. That means that, while it's a tremendously ambitious goal, MCC may indeed have a shot at obligating the funds that you are considering, that the appropriations process is considering putting forward.

That said, MCC has established a very ambitious set of goals carrying forward, looking at signing two to four compacts per quarter, through at least the middle of fiscal year 2006. And their assumptions are based on the premise that these compacts will be, on average, considerably larger than the Madagascar compact. So, all of that is to say that they have a good shot at obligating the funds that you are considering putting forward.

The only other thing I would say to that is that obligating the funds is a different matter than spending the funds, and that's a different concern that faces MCC going forward.

Senator NELSON. Well, let me ask you: How much has the MCC spent on development assistance, compared with administrative expenses?

Mr. GOOTNICK. Madagascar was the first compact that they've signed, and funds have not yet begun to flow, per se, to the Madagascar compact. If you look at what is in the compact itself, what you will find that, as a product of their due diligence efforts, considerably more information about the project areas that are proposed under the compact. There is reference to a range of in-country structures that MCC/Madagascar will build that will allow the funds to flow. So the oversight entity, the fiscal entity, the monitoring and evaluation, the audit function, the procurement function, those are articulated in principle, but are to be determined in terms of actually building those structures to MCC specifications, which will allow the funds to flow. And that will take place at some point in the future.

The CHAIRMAN. Thank you very much, Senator Nelson.

Senator Coleman.

Senator COLEMAN. Thank you very much, Mr. Chairman. First, a comment about the MCC. I think this is a tremendous idea. As I've listened to some of the conversation and some of the discussion we've had, not just in this hearing, but in others, there have been some concerns raised about whether MCC is taking money away from other programs. I would hope that we're not engaged in a situation that since the President's proposed this, that all of a sudden it becomes politicized, that if it comes out of the White House, somehow there's got to be something wrong with it.

This is the way I think aid should be done. You work with the country, you identify objective indicators as to the type of things we'd like to see in place: Ruling justly, investing in people, fostering enterprise and entrepreneurship—and then it's not our program, but it's their program. You give folks ownership to tell us the ways in which we can reduce poverty, increase quality of life. So I think in concept, it is a magnificent concept, and I just hope that it is not getting caught up in some of the politicization that we see around here.

I am concerned about some of the funding issues. The last 2 years, Congress has failed to fully fund MCC accounts, and that causes me concern. So, just a general statement, I think the Millennium Challenge Account, MCA, and the work that the MCC is doing is critical, and I hope we get it out of the realm of politics.

I would note, my friend and colleague from Florida, I'm sure his comment on Paraguay was reflecting on the past. I do want to say, as chairman of the Western Hemisphere Subcommittee, that I have been impressed by the efforts of President Duarte Frutos, that Paraguay is making great strides, and the President's shown great courage. Endemic corruption is difficult to challenge, when folks do that, I do think that they deserve our support and appreciation.

I want to ask a question about Nicaragua. There you have a President who's taken great personal risk to tackle corruption, he may be paying a price politically.

And I'd ask the question, both to Director Gootnick, and Mr. Applegarth. This is the other side of the coin. On one side you have corruption and how do you deal with it. But how do you factor in

political courage in deciding to support a country, move forward with an MCA relationship? Can you factor it in? Is that something, as you looked at the qualification standards, is that something that is there, or that should be there? In other words, we have leadership taking risks to fight corruption, how does that factor into the analysis? Mr. Applegarth, I'd appreciate your comments.

Mr. APPLEGARTH. Would you like me to go first, Senator?

Senator COLEMAN. That's fine.

Mr. APPLEGARTH. I think you see it in a lot of ways, and I wouldn't limit courage to either simply Paraguay and Nicaragua. We are, no question, helping reformers in these countries make some very tough changes, and some of them are doing it under very difficult circumstances. Certainly President Bolaños is in a quite difficult situation. We believe that a successful Nicaraguan compact should strengthen him.

I think you see political courage first reflected in the indicators themselves, and performance under the indicators, it's not short-term courage, but it's courage over a period of time that begins to show up in the indicators. I think you see it also, and certainly the Board takes it into account, in the countries that are substantially below on some indicators, but we're looking at the commitment of the leadership and commitment of the countries themselves to take steps to address the areas that are substantially below in the indicators. The last area is where the data is clearly outdated, as it was in the case of Georgia where the indicator measured the Shevardnadze regime versus the Saakashvili regime, where you had true leadership, clearly reinforcing the principles of the Millennium Challenge, to fight corruption, to clean up the government, to put effective procedures in place. So I think you see it throughout our decisionmaking process in the selection of countries, both eligible and threshold, and then when you start to look at the kind of programs these leaders are presenting to us.

Senator COLEMAN. Mr. Gootnick, could you respond, can you assess whether the indicators adequately measure political courage?

Mr. GOOTNICK. Right. I would say that the indicator methodology, the eligibility determinations, there's a clear recognition that there will be objective and quantifiable indicators, and that there will be discretion. And a great deal of work went in, both prior to the organic authorization of the Millennium Challenge Corporation, and subsequent to it, on building this methodology that relies both on objective indicators and discretion. The results demonstrate that MCC exercised some discretion in the eligibility determinations.

I would only add to that, that to the maximum extent possible, to the extent that MCC could make public its determinations, the use of its discretion, and make those results transparent, recognizing that there are some limitations there, that there is confidential information, there is classified information, there may be diplomatic issues, but in order to both justify, explain and, when necessary, defend those eligibility determinations to potential recipients, to stakeholders and others, and to Congress, that to the maximum extent possible, documenting those decisions would be of benefit to the Corporation.

Senator COLEMAN. Mr. Gootnick's comments actually kind of lead into my next question, that's to you, Mr. Applegarth. I wasn't here

earlier, and I apologize for that, but I'm interested in your reaction to two of the areas of the GAO report, they've talked about internal controls and oversight, and then apparently transparency here, can you react to that?

Mr. APPLEGARTH. We believe in, and try to demonstrate our commitment to transparency. We have open Board meetings to the extent we can, we post everything we do on the Web, our criteria are there, how countries rank individually there, who does the ranking—since we don't do them—their methodology is all there. As much data as we can, underlying the data, we try to put there. We frequently hold public outreach meetings, I think on average once every 6 weeks or so, since the time virtually, that I came on board, as well as a number of meetings—frequently—with NGOs, members of the business community, both in the United States and in the countries that we're operating. Our compacts will be public documents, they are going to be on the Web, I think the Madagascar compact's up already.

We believe this is important so that the potential beneficiaries of the compact can see what the compact's supposed to accomplish, and if they're not getting the benefits then they can complain about it. We see this as an implicit part of monitoring and evaluation, so we consciously try, throughout our activities, to be as transparent as we can, and we welcome suggestions as to how to be more so.

Senator COLEMAN. Thank you, Mr. Applegarth. I do want to repeat that I think that the work that's being done by the Millennium Challenge Corporation in bringing to life the principles behind MCA is really important. This is, I think the future of aid and development.

One other quick question; I'm going to Armenia at the end of this month. What message should I bring to the Armenians? They're one of those eligible countries where we don't have a compact yet. Where are we at with Armenia? What are some of the challenges that are faced, and what message can I articulate to facilitate that process?

Mr. APPLEGARTH. I think we should perhaps have a considered response to that at a later date. We just received a revised proposal from Armenia, and I think you would see—not only there, but in many of our other countries—significant improvements in the focus of the proposal. They've clearly benefited and learned from a consultative process when I think instinctually they may not have opted for that initially, but I think they would now publicly acknowledge it's been beneficial, and I think they're clearly on the right track. We would like it to go faster, I think they would like it to go faster. This is an example of the learning curve, when you're asking countries to undertake a new process for the first time and try to do it and try to do it right. I think they're making quite significant progress now and I'd be basically encouraging to them.

Senator COLEMAN. I look forward to having that conversation before my trip. Thank you, Mr. Chairman.

The CHAIRMAN. Thank you very much, Senator Coleman.

Senator Sarbanes.

Senator SARBANES. Thank you very much, Mr. Chairman.

I say to the witnesses, if I ask a question that's been previously covered, please indicate as such. Unfortunately we have to cover a number of hearings in the course of a morning, and I regret I haven't been able to be with you until now.

Mr. Applegarth, the Millennium Challenge Corporation has been appropriated $2.5 billion to date; is that right?

Mr. APPLEGARTH. Close. Subject to slight rescission, that's correct, Senator.

Senator SARBANES. And there's a request for an addition $3 billion in this year's budget from the President?

Mr. APPLEGARTH. That's correct.

Senator SARBANES. So, if the Congress were to appropriate what the President asks for, you'd have $5.5 billion?

Mr. APPLEGARTH. We would have had a total of $5.5 billion appropriated, some of that has already been obligated, and you did miss the presentation on the pipeline.

Senator SARBANES. Well, how much has been expended, to date, of the $2.5 billion?

Mr. APPLEGARTH. Of actual disbursements, there's a certain amount for administrative expenses, I think it's on the order of $25 million. We've obligated now $110 million for Madagascar, we have a Honduras compact up for consideration by the Board on May 20. The chart on my immediate right demonstrates our current planning for commitments for the balance of the year, and early next year.

Senator SARBANES. So, how much do you plan to commit by the balance of which year?

Mr. APPLEGARTH. By calendar year 2006, I believe we will be close to exhausting, under this current timetable, and this moves around, but we will have virtually obligated all of the money that we currently have appropriated, plus or minus $100 million or so, I think is the current estimate.

Senator SARBANES. By when?

Mr. APPLEGARTH. By the end of the calendar year.

Senator SARBANES. Which calendar year?

Mr. APPLEGARTH. 2005.

Senator SARBANES. Fiscal or calendar year?

Mr. APPLEGARTH. Calendar.

Senator SARBANES. So by the end of this year, you will have obligated the $2.5 billion?

Mr. APPLEGARTH. Close to it, plus or minus $100 million or so, under the current planning. I did testify to this earlier, but we've taken the initial proposals we received from countries, reduced them from over $4.5 billion to approximately $3 billion. The $3 billion does not include Morocco, which we expect to be a fairly sizable program. Our current estimate is simply to fund the good proposals that have already, after initial vetting from the fiscal year 2004 and 2005 eligible countries, we need, at least, an additional billion dollars to fund those proposals. In addition, we have the new lower middle-income countries coming in November. We expect to have more lower income countries, and we will have additional threshold countries.

Senator SARBANES. How much will be expended by the end of the calendar year?

Mr. APPLEGARTH. By expended I presume you mean disbursed? Or obligated, Senator?

Senator SARBANES. You just told me virtually all would be obligated.

Mr. APPLEGARTH. Obligated, correct.

Senator SARBANES. The question I'm obviously asking is disbursed. I think, because I think you already told me the other.

Mr. APPLEGARTH. Correct, I just wanted to make sure we were on the same page. My guesstimate, and I would have to give you more precise numbers looking at the programs, because we obligate over a 3- to 5-year period, say, on average, 4 years—if you take the total amount obligated, divided by roughly four, that would give you the amount that would be disbursed over 12 months, the first 12 months from the time the compact is signed. I think the final disbursements this year will depend very much on the particular compacts that are signed, and the size of them.

Senator SARBANES. So, the first year of the disbursement would extend beyond the end of the calendar year, in every instance, actually.

Mr. APPLEGARTH. The first 12 months from every compact will extend beyond this calendar year; yes. We have started, expect to start disbursements on the Madagascar compact reasonably soon, I have already approved disbursements for what's called 609(g) funding, to accelerate the compact development in three different countries.

Senator SARBANES. Now, during the committee's last oversight hearing on the MCC in March 2003, Under Secretary of State Alan Larson said repeatedly that the MCA "must complement, not replace, other assistance"; "The MCA will not come at the expense of USAID." Despite this assurance, we see in the administration's fiscal 2006 budget proposal, that the MCA is slated for large increases, in fact a doubling from last year's level of $1.5 billion to a request of $3 billion this year.

But at the same time, the President has proposed significant cuts in core USAID accounts, such as development assistance and child survival and health, as well as international organizations such as UNICEF. What's the explanation for this failure to carry through on the assurances the Under Secretary gave to the Congress?

Mr. APPLEGARTH. Senator, I don't think I would characterize the comments as a failure to carry through. First, I agree with Under Secretary Larson, our programs should be complementary, not to replace other programs. And we also, as I testified to this earlier, believe we should be additional.

And I think if you look at the track record of the administration, there have been significant increases in development assistance of the last 4 years, and I think there's a significant increase in the request this year, even before you look at the MCC increase.

In terms of specifics, I would refer you to, perhaps, those program administrators——

Senator SARBANES. Are you asserting there's been an increase in development assistance, and child survival and health in this year's budget submission?

Mr. APPLEGARTH. I was testifying in terms of the aggregate. I believe there's a significant increase in the total even before you con-

sider MCC. Regarding specific accounts, others are more expert on that.

I've been told that the administration has asked for more for child survival and health this year than they did last year. I could be wrong on that, I'd have to check.

Senator SARBANES. And UNICEF as well?

Mr. APPLEGARTH. I don't have any information on that, I would certainly be happy to get that for you, Senator.

[The submitted written answer to the requested information follows:]

MCC believes that State Department is better positioned to explain U.S. funding levels for UNICEF and we would direct your question to them. That said, we are unclear why there is a suspected linkage between MCC and UNICEF funding. The President's FY 2006 Budget requests a significant increase in funding for the United Nations and U.N.-affiliated agencies. We hope the Congress fully funds the President's request. Moreover, the President's FY 2006 Budget requests an increase in contributions to all International Organizations compared to 2005 levels and represents a 30-percent increase from what the Congress appropriated to all International Organizations in 2004.

Senator SARBANES. But you adhere to the view that you're not supposed to be cutting other programs in order to fund the MCA, is that correct?

Mr. APPLEGARTH. I believe the MCC should be additional, that's how we have the incentive effect. I don't think the establishment of the MCC is a guarantee that every program is immune from rationalization or being plus or minus'd, depending on the effectiveness of the program, I don't think Congress would want to enter into that kind of a guarantee to the program either, but I think if you look at overall, in aggregate, there have been significant increase in funding over the last 5 years from the administration, and I think it reflects the recognition that there's a genuine need, recognition that development assistance is not only a projection of American values, but important for the national security of the United States, and it is fundamentally the kind of thing Americans want to do.

Senator SARBANES. What "scrub-down" process do you follow with respect to proposals that you receive?

Mr. APPLEGARTH. I think the due diligence process is quite rigorous. As evidence of it, as I mentioned earlier, the proposals we received initially from countries total an excess of $4.5 billion, that total is now reduced to $3 billion. That is significant evidence of scrubbing.

Senator SARBANES. Well, what's the process for reducing it?

Mr. APPLEGARTH. We look at several things. First, will the program lead to poverty reduction? That's our first test. And by that, we want to see, what are the outcomes, what are going to be the measures of success, how do we know 5 years from now this program was successful or not? And we don't want just a bunch of words, we want some demonstrated measures. We also want detailed plans of how we're going to get from here to there, we want some assurance that the money's going to get from us to the intended beneficiaries, and then we also want to know that the program came from a consultative process, that it was broadly defined, within the country, as being a true obstacle to growth, an obstacle

to poverty reduction and reflects some national sense that this is important for the country.

Senator SARBANES. Now you said the MCC conducts due diligence to ensure that countries consult fully with civil society groups when they develop their proposals. I'm interested in what this due diligence consists of. What steps do you take to ensure that women, poor people, and local civil society groups are meaningfully consulted in the process of developing compact proposals?

Mr. APPLEGARTH. I see my red light's on, Senator, but I'll try to answer you quickly.

Senator SARBANES. The way it usually works is if we get the question in by the time the red light goes off, then you get an answer.

Mr. APPLEGARTH. I'll ask the chairman not to hit me with the gavel or his electric prod here.

A consultative process, Senator, is going to vary from country to country, there's no cookie-cutter approach, it's going to reflect the country's own history, culture, and customs. And we've actually worked with a number of NGOs to try to develop guidance for a consultative process—broad principles—and examples from which countries that are moving more quickly have done. We held a seminar for visiting ministers at IMF meetings that focused on this, and we just recently published further guidance on the consultative process.

But I think if you look at the principles, first, it needs to be timely, it has to be early in the process, and continue throughout. Second, it's got to be participatory, which means not only the business community and NGOs but women, farmers, others should be participating in the process. And during the due diligence we talk to them, we don't simply rely on the word of the government, we go out and talk to them as to their assessment of the process. And it has to be meaningful, so it's not just a hollow exercise. You can hopefully see some impact of the consultation on the proposal design and implementation. I think we are seeing that.

My personal standard for a good consultation was in one of our countries; I was meeting with the leader of the opposition. We came out of his office and there was a couple of members of the press there, and one of the questions was directed toward the consultative processes, and the leader of the opposition said, "You know, I don't agree with everything that's in the government's proposal, but I will agree that they ran a fair, consultative process." Are we going to achieve that standard in every country? Probably not, but the point is, if you can actually get the leader of the opposition giving credit to the government for the adequacy of the consultative process, I think that's a pretty good test.

Senator SARBANES. Can I ask one followup question?

If I'm a country that's interested in submitting a compact, wouldn't it behoove me to ask for a lot of money on the assumption that you're going to bring it down, regardless of the request? Can I assume that if I inflate my figure, my chances of getting a good figure at the end of the process will be enhanced?

Mr. APPLEGARTH. I guess my initial reaction is probably not, Senator, where we've seen what we would have considered very large proposals, the impact has been to delay the process, not to speed

it up. If you believe achieving a compact in a reasonable and expedited time is important, that wouldn't be an appropriate thing to do.

I think the MCC disciplines remain the same. Will this lead to poverty reduction? Is there an economic return on this investment of U.S. taxpayer dollars; are the outcomes measurable? Are there benchmarks along the way, is there detailed planning, and did it arise from a consultative process? I also know that in, at least, a couple of the compacts, the amounts have actually gone up as a result of this review, when you look at the detailed plans, and you don't believe that the funding is adequate to accomplish the objective, so you've actually seen some increases in some of the compacts. I think, and I'll have to double check this, I believe Madagascar's an example of that. I can think of a couple of others off the top of my head where the amount has gone up as a result of the due diligence process, when you see what resources are needed to do the job right.

[The submitted written answer to the requested information follows:]

MCC does not have a formula for allocating funds across countries but, reviews individual country proposals in terms of viability, likely impact, contribution to poverty reduction, and economic rates of return for the program.

In several cases the amount committed or planned to be committed under compacts either exceeds or is less than the original amount requested. This variation can be due to several reasons, including the deletion or modification of components because they did not have an adequate economic benefit or did not arise from a consultative process, or because due diligence revealed that a larger investment would be needed for the compact program to be successful.

In the specific case of Madagascar, the amount did increase from just under $90 million to $110 as we got a better understanding of the costs of the project.

Senator SARBANES. Are there some guidelines, linked to a country's size and population or extent of poverty, that give them a range, in terms of the size of the proposal to make? I mean, I'm a country getting ready to apply, and I have enormous needs, let's assume. How do I know what is a realistic proposal to come forward with?

Mr. APPLEGARTH. Currently we don't have such guidelines, Senator, and it's a topic we debate constantly, for some of the reasons you're implying, and we'd welcome your advice.

Right now we've said focus on what are important obstacles to growth in your country and show us what's needed to really eliminate those obstacles and lead to poverty reduction and growth. That's the standard we're applying, so you don't see a rigid formula of *x* country with a small population gets a small amount of dollars, and a larger country with a bigger population gets more. We're really trying to assess the quality of the proposals. It's not always easy, I understand that. Sometimes countries ask for guidance, we try to keep coming back to—tell us why this is important to you, what are the real obstacles to poverty reduction, and we'll try to work with you.

Senator SARBANES. Well, that's helpful. Are any of these countries hiring lobbyists here to try to help them frame their proposals in advancing and moving through the process in Washington?

Mr. APPLEGARTH. We've seen some countries hire lobbyists to try to influence the selection process for eligibility or threshold. I don't

have a universal survey, but I would think that that has been detrimental to their prospects, not helpful. There certainly is no positive correlation, I believe the Board has been quite seriously focused on the criteria, and government performance, and immune to advice from lobbyists, and I think it's come as a surprise to the countries who hired them. I would think the countries would spend better time investing in proposal development, and putting a good proposal before us is more likely to have results.

We do see countries engaging assistance in the consultative process. The Asia Foundation is assisting a couple of countries in that area, we certainly are providing help in proposal development, in terms of engineering, environmental impact, early stage data gathering through 609(g), and we see the UNDP trying to assist countries in some other parts, so you see a variety of help as the countries take ownership of this process, but lobbyists is not a way that would be productive.

Senator SARBANES. That might be something we might want to keep an eye on, Mr. Chairman.

Mr. APPLEGARTH. My hunch is that you will see them before we do, Senator. I suspect you will be closer to that than we will.

The CHAIRMAN. We can share our information. Thank you, Senator Sarbanes.

Let me ask you, Mr. Gootnick, a question about the trip that you and your staff took to Honduras. This is a hands-on attempt to gather information on the Millennium Challenge Corporation in the field. I'm curious whether your research findings were different from information you had received from the MCC headquarters, and what your impressions were of the way in which MCC personnel were working with USAID in the field. Can you give us some recollection of those impressions?

Mr. GOOTNICK. Certainly, thank you.

A number of observations from the field work in Honduras that are responsive to both your question and perhaps some of the broader dialog that we've had here this morning.

I would say, first observation is that in the case of Honduras the Inter-American Development Bank did provide some funding to assist the Government of Honduras in developing its proposal, and I think that was instrumental in them being really one of the early eligible countries that had proceeded through the process.

The other observation I would make is that the proposal that came forward from Honduras was very clearly based in its national development strategy, in Honduras' case the Poverty Reduction Strategy paper. And the Honduran officials were quite clear and indeed, proud, of the fact that their proposal could be culled, or pulled, largely from the PRSP. From that perspective, consider that the proposals will have some of the strengths, and perhaps some of the inherent limitations that a national development strategy, for example, a PRSP will have. To wit, the level of civil society and broader input to a national development strategy, as has been alluded to in this discussion, can be very difficult to measure. One has to distinguish between consultation and consensus around proposed MCC projects. In fact, in Honduras we observed a fair degree of consultation, I would say, with respect to consensus there was

a lively debate and certainly some disagreement as to what projects should be funded, and whose needs were most being considered.

And then finally I would speak to the partnership with AID. I think AID, from what we saw in Honduras, was acting as a tremendously good faith partner, providing some of their staff, certainly providing entire to MCC, to a broad range of actors in the country, governmental and nongovernmental officials, and beginning to articulate its role in an environment where MCC would be active in both Honduras and Nicaragua.

For example, the regional strategy that AID has put forward in Central America really adopts and has begun to bring in some core MCC principles into its core strategy.

The CHAIRMAN. Well, those insights are helpful in giving a sophisticated view of how the process works. For example, you've stated Honduras, as a country, had done quite a bit of work in thinking about this. It's not that all countries have not given some thought, but I suspect if you went systematically from country to country you would find the planning efforts in some vastly superior to the almost minimal efforts in others.

So, one could conceive a situation in which a country within its own political structure has been thinking about development and, as you suggest, having debate—maybe not consensus, but a good bit of consultation—and this is occurring transparently so that the ruling party, or whoever happens to be in power at the time, has responsibility for applying, but the opposition is clearly aware of the debate that has preceded this plan that's being shared, and then—interestingly enough as you said—a factor, perhaps, of some funds from the Inter-American Development Bank, sort of a crosshatch, in a way, of the multinational development banks.

There's nothing wrong with that, but obviously, maybe an ingenious aide comes along, and the Honduran Government says "Help us," and we use some of these funds to develop our plan, to interact with the MCC officials who have criteria, some of which we have met, or some we're trying to meet and so forth. And that, I thought, was an interesting thought. I'm not certain—we'll have to go through each of the applications to see who may have offered some assistance—if not a bank, whether there were other consultants, whether others came into the process, to alter and refine a final product which may be better than the kind of application Honduras was making to the Inter-American Development Bank, or the problems we have been observing in some of the loans from that Bank, not necessarily to Honduras, but to others.

All the strategies and the criteria and the indices that you were examining were not necessarily part of their pictures, but might be. So in a way, we're describing, perhaps, the evolution of the process of effective foreign assistance. Bit by bit we all learn more of the state of the art as to what is effective in the use of scarce resources, credibility, honesty about the whole process, transparency, building of democracy that comes from all of the above, as opposed to broad humanitarian efforts to get the money out there, to show our sense of compassion. But in the process, the degree of necessary sloppiness, arbitrariness may have disillusioned some people—including American taxpayers. We've not intruded into the conversation today about this program, but I would guess one rea-

son that the President suggested the program was that there has been an uphill fight for foreign assistance in this country.

There are a lot of very generous Americans, and I don't want to overplay that argument. But given the needs in the world, one would say, why isn't the United States more forthcoming? Well, one reason is that people like ourselves, members who represent constituents, visit at town meetings with people who say, "Why in the world are our dollars being expended in Honduras? As opposed to Kokomo, Indiana, we've got some problems here, you folks ought to recognize that," and we say, "Well, this is a big world, and there are important issues," and they say, "We understand that," but nevertheless, rationalize.

And what about the waste? What about the fraud? What about the dictators? Before long, you're off to the races again in an argument that you're not going to do well on in any particular meeting unless you have a very congenial group that sort of started with the thought that we're oriented this way.

Now, here you come along, both of you, with a program in which we're saying, "There are criteria." There's advancement of anticorruption, of democracy, of the best use of dollars to help very poor people. And these countries are very poor, and your indices show that. You're buttressing this, Mr. Gootnick, as the honest auditor, so that their enthusiasm doesn't get us carried away. You're taking a look at the country as you did, and that's why I draw on your meeting with Hondurans and your staff, which I hope will continue. In that vein, what other trips do you have planned or, how will you, in the future, attempt to do the kind of intensity of work that you did with your associates in Honduras?

Mr. GOOTNICK. One small technical correction to my prior remarks before I go too far, I believe it's the Central American Bank for Economic Integration.

The CHAIRMAN. Very well, we'll correct the record for all of us.

Mr. GOOTNICK. With respect to your question about how do we carry forward from here, my intention would be to consult both internally at GAO, and then to get with your staff to look at how we can best support this committee's efforts of oversight, carrying forward, and we'll be establishing that plan in the very near future.

The CHAIRMAN. We would welcome that. I think GAO is obviously very appropriate, and we would appreciate your inclusion of our bipartisan interest in this. As you've both witnessed today, we've had good participation of, at least, three Senators on both sides of the aisle and their staffs. We're appreciative of that, given all the conflicts that Senators may have.

Now, let me ask, Mr. Applegarth, have you noted, talking about the development of the state of the art in all of this, any changes in other donor policies of other international agencies, or even agencies in our own Government, whose outlook toward giving assistance, humanitarian care, might have been influenced at all by the new approach of your corporation?

Mr. APPLEGARTH. Senator, I'm always reluctant to claim causality.

The CHAIRMAN. I understand, that's why I'm asking so that you have an opportunity.

Mr. APPLEGARTH. I think you clearly see an increasing focus by other institutions on some of the same principles that we're talking about, government effectiveness, country ownership, outcomes, results, there's no question that our ranking system—as imperfect as it is, and I don't think anybody claims that it represents perfection, is receiving a lot of attention. We are open to comments and suggestions on how to improve it, and we get them, and we try to incorporate them. But our rating sheets, which are up there on the Web for everybody to see, are looked at by other development ministers, and are looked at by the senior leaders of the countries we've selected. We're seeing it in a variety of ways, as I mentioned, President Yushchenko, even the Palestinian authority who wanted to understand, not so much that they have any prospect of qualifying for MCA assistance any time soon, but what are the policies that are demonstrated to lead to poverty reduction, and to lead to growth, there are committed leaders around, there are committed donors around, we're all trying to do, ultimately the same thing, which is to help people who are living in abject poverty to do better.

On that, I would like to add that I know Congress is going to have some tough decisions with MCA and the big funding request and some other decisions. This is not a black and white or zero sum thing. The beneficiaries of the Millennium Challenge are the same beneficiaries of some of the other programs, and the real question is, What's the most effective way to deliver assistance to them? They're still the rural poor, it is still farmers, it is still people looking for an opportunity for a job, what's the best way to do it? MCC's built on the lessons of development—what's worked in the past, what works best? And that's what we're trying to do and that's the basis upon which the countries are responding, they're putting policies in place that will lead to poverty reduction and growth and we believe we need to deliver on the promise for those governments that are taking the steps they committed to.

The CHAIRMAN. Well, it's obvious, I think, to you, having been through our hearings, that the majority of the members of this committee applaud that thought. It's not a question of diminishing our interest in other countries, but rather augmenting it through programs in which there is the confidence of the Congress and the public. Therefore we are more likely to have momentum to do more as we try to take part in these international conferences.

Let me just ask both of you this question. A comment was made earlier on—as a country is approached—for example, Georgia was mentioned specifically—the indicators and the data might very well have been from the Shevardnadze government of the past. But suddenly here are the young Georgians, they had a revolution, they had an election, they are struggling with enormous poverty and they approach you. When examining the track record of the country, to what extent do you have to make a political speculation, a prediction on the basis of trial results? This would be even more problematic, I would guess, in the other international situation I mentioned in Albania.

I come back to that because this is such an extraordinary, new experience for me. I had not visited Albania before, and I would not have visited Albania on this occasion, but there were strong reports

that there was a lot of nerve gas up in the mountains, and it might not be guarded. I take these things seriously. We move out with the Cooperative Threat Reduction people and put a fence and guards around it, with the cooperation of the host country, but this is out of the blue.

Now, while we're there, they also identify 79 missiles in the shed. We got a pledge to destroy those during the next month. Then we come down the hill and we talk to a Defense Minister. So we have a new relationship now, and we're going to make, as a requirement for our new military academy, that our graduates have proficiency in the English language. Well, that's a rather extraordinary situation. Maybe 3 weeks before, there wasn't such a requirement. Quite apart from the missiles discovered and destroyed, or the nerve gas.

But then we have a further request that we send an ambassador to the country. I understood our problem. We had sent our Ambassador to Iraq, and that was an urgent situation, but nevertheless, they felt in this new spirit that we needed an ambassador on the ground here. So our committee worked with the State Department. We were in the last 60 days of a highly partisan campaign, all sorts of people stacked up waiting for confirmation, but to make a long story short, because of the national urgency, a very distinguished lady in our State Department was identified and confirmed as an ambassador, and got there.

Now, on top of all of that, then, they said, "Oh, by the way, we're interested in the Millennium Challenge business, and we've got some problems—pervasive corruption," and that understates it. Huge problems, just in terms of title of land, any land, any enterprise. There are all sorts of things going on with almost no legal basis. That's why Albania didn't regress to, at least, the list under consideration. It's because suddenly there was a dramatic turn in the life of a country that has had a horrendous dictatorship, so obnoxious the Soviet Union did not find it very compatible. They searched from the Chinese or from others for much of their history, and suddenly they want to change, to become a democracy, to become affiliated with us, and to deal with us on weapons of mass destruction and terrorism and so forth. But this is really tough if you are an evaluator. The kind of data we're talking about today, this is not like looking at an American corporation coming in for a large loan, and trying to find a track record. It's a given with all of our legal system and banking data.

Now this is what leads me to ask both of you: How do we deal with these situations? How do we deal with the young Georgians who had a slight track record? They certainly did root out a whole lot of corruption, firing the entire police department of the country and rehiring a few because all of them were corrupt, the whole lot. That's pretty demonstrable that you take corruption seriously. It hadn't happened with all the neighbors around, but it is instructive as to what catches our attention. How much of this do we take into consideration? How much can we, in fairness to the other applicants, and likewise in making your case, which you must make to the Congress for funds, and for credibility? Will you try that one on, first of all Mr. Applegarth, and then Mr. Gootnick, will you give your observations?

Mr. APPLEGARTH. There have to be considered judgments, I wouldn't say speculation, I would say considered judgments, and I think that's why you have a Board, the quality of the Board we have, and the kind of people we have.

The CHAIRMAN. Now, how is the Board selected, where do they come from? And you've mentioned the quality and their dialog, but that's an important consideration? Who are they?

Mr. APPLEGARTH. The Chair of the Board is the Secretary of State, Dr. Rice. it used to be Secretary Powell. Vice Chair is the Secretary of the Treasury; the U.S. Trade Representative is on the Board; Administrator Natsios, the head of AID is on the Board; I am on the Board, in addition we have spaces for four members selected from lists provided by Congress. The first two of those have been named, Kenneth Hackett, who is the head of Catholic Relief Services globally, a large NGO with operations in many of the countries where we operate, and Christine Todd-Whitman, former head of the Environmental Protection Agency.

The CHAIRMAN. Are there other nominees before the Congress, or are there still two—

Mr. APPLEGARTH. There are two nominees still in the process. They have not been formally proposed at this point. But I think the quality of the Board, and this is not an ex-officio board, these Board members come to meetings and they work, and I think that reflects the fact that they think this is an important mission and it also reflects the judgments they bring to bear based on considerable experience.

I also think the transparency of our decisionmaking, the criteria being out there, and anybody who looks and sees how the rankings of the country says, "Yes, MCC stuck to what it said it was going to do." Considered judgments applied to the criteria, it wasn't a formula but fundamentally these are the right kind of countries being selected and the Board is paying attention to the criteria. It seems to me that helps as a check and balance on the judgments being brought to bear. Now, is there some element of judgment? Absolutely. Is there some risk taking? Yes, but it is perhaps risk taking in the context of Board credibility. We have demonstrated considered judgment and prudent risk-taking, in the case of Georgia already, at the time we picked them in May. We knew it was going to be many months before they actually would get funding, so we could continue to see that track record, and certainly there's no guarantee that any country named eligible is going to get funding. So you've got a chance to see how the country runs the consultative process, how they select the priorities, and the quality of the proposal.

I think in the case of Albania it's a different situation because it is a threshold country. Many of the threshold countries are having to deal with the same thing which is corruption and rule of law. These are very difficult problems to get rid of. Ultimately we're seeing the evidence of the countries making steps in the right direction and committed to trying to do something about it. The question is, Can they give us a good program that looks like it's going to work that really fundamentally addresses these kinds of things? If they do, we'll give them funding, it won't be large amounts, there's much smaller amounts of money at risk, and it will be tar-

geted very specifically. But if the country does a good job and increases our confidence that it will use the money as a full compact eligible country, the rest of the money will go. So it's a modulated approach, it's certainly based on consideration and judgment but it's also transparent and it is targeted.

The CHAIRMAN. Mr. Gootnick.

Mr. GOOTNICK. Mr. Applegarth has spoken to the use of objective indicators versus discretion quite thoroughly. Beyond that, I'd say with respect to your comments on Albania, Georgia, or any of a number of other, either eligible or threshold countries, your observations go very much to the heart of our recommendation, which is that MCC as an evolving institution needs to identify, manage, minimize on an ongoing basis, assess its major institutional risks, and in this environment, those major institutional risks pertaining to the large flows of funds through the corporation to in-country structures that the corporation expects to establish to execute its projects. In that regard, one could look on page 23, figure 6 of our document, where we've articulated the key institutional structures that MCC expects to establish to execute its programs. Oversight entity, fiscal entity, procurement entity, audit entity, monitoring and evaluation entity, and that those entities performing up to MCC specifications represents a key issue and a major institutional risk for the Corporation going forward, and may be the subject of a debate and discussion a year from now, as compact funds have begun to flow.

The CHAIRMAN. I suspect it will be, and I thank you for drawing our attention specifically to those six criteria which you identify in your report. That's important, it gives some credibility to your evaluation to the American public that's looking over your shoulder to see what you're doing and how you're doing it.

Let me just ask—these compacts have a time limit to them. They're for a certain period of time. What is the probability that if things go well in a country, there may be an additional plan, additional submissions, additional years? Now, that speculates that the President of the United States and the Congress will continue to find this to be the constructive avenue we believe that it is, and that it's going to be. It may be expanding for all we know, if we were to have this hearing 10 years from now. But as a country looks at this, is there some thought or some hope on the part of some of the leaders, that if things go well, if really remarkable results are produced, that we will not simply indicate "Congratulations! You've graduated," and head on to another country? In some cases we have taken that view with regard to foreign assistance for a good reason. Countries that were desperately difficult in terms of their economies, their politics or whatever, got better, and as a matter of fact, began to show a lot of growth from their internal qualities. All our efforts were a spur to get things moving, not as a permanent donor. What is the expectation of these countries that you're dealing with, by the very definition of the group income-wise, and prospects that you've talked about to begin with?

Mr. APPLEGARTH. Of course, Mr. Chairman, our ultimate objective is to have these countries graduate from the need for assistance. That's what we're trying to do, build the capacity, reduce poverty and create the model for sustainable growth, and then ulti-

mately reduce their dependency on foreign aid. Of course, we are targeted at some of the poorest countries in the world.

The CHAIRMAN. They're not on the threshold of graduation to begin with by the very——

Mr. APPLEGARTH. No, even the most successful is going to take some time. These are not easy problems that we're going to address. We would like to see progress. What we're about is to try to help them make the progress. To do it so that ultimately, maybe you get the success of the Asian tigers and some of the other countries that are no longer dependent on foreign assistance. But that's not going to happen in the short term. Our expectation is that when additional program components are ready, countries can come back, and we could amend a compact to fund it, at least in some of the countries. Madagascar certainly said, "Let's focus on the key fundamentals first, phase one, hopefully at some point we can talk to you about a phase two." If and when they're ready, we'll be glad to talk to them.

There are two legislative limitations on our ability to do that, one is right now we can only have one compact at a time with a country, so we can't enter into a new compact, you can only amend an existing compact for an additional element. In addition, there is a 5-year maximum term for any compact. So anything we do by way of an amendment, at least under our current understanding, would have to be accomplished within 5 years as well.

The CHAIRMAN. With Madagascar, this data is in your submissions, but off the top of the head, do you recall what is the per capita income of a citizen of Madagascar presently?

Mr. APPLEGARTH. I probably have it handy. The latest data that I have is for 2003, is $290 per person.

The CHAIRMAN. $290.

Mr. APPLEGARTH. Per year, that's right.

The CHAIRMAN. Talking about graduation, this does illustrate how far—if, in fact, there were a doubling of the income of the country in a short period of time, or even a tripling of the income, the average citizen would still have less than $1,000 per capita income a year.

Mr. APPLEGARTH. You're correct, Mr. Chairman, I think in my opening remarks I talked about countries living under $2 a day per capita, this is less than $1 a day. If you triple this, you're still probably under $2 a day.

The CHAIRMAN. This illustrates the awesome problem. I probably don't do justice to the Financial Times chart that was published recently, but I thought it was remarkable the other day in discussing the extraordinary growth of China and its economy, which is truly dynamic. It is often stated as 9 percent growth or more per year, and that has been the case now for several years, so it is compounded annually. That's extraordinary given the size of the country, the number of people, but I think the Financial Times indicated that maybe 5 years ago or 10 years ago, sometime in the intermediate time range, the per capita productivity of a person in China was 5 percent of the productivity of a person in the United States. Now, over the course of this 5- to 10-year period, that 5 percent has changed to 16. That is a major feat. In essence, a tripling of the five, if you do the math. But you come out, even then at a

point that at this point the equivalence of that production, granted, times a billion or more people, adds up to a big figure. The United States has maybe 300 million times whatever figure we have, so the multiple of the Chinese people at some point may get to a GNP that begins to come into the United States range. But it indicates that even with those situations that we look at with some degree of awe in terms of how all that occurs, the yawning gap, and standards of living, now moving down to Madagascar, that's a very different situation altogether. I would just say that's why this whole process would be tremendously interesting, not only to this committee and to you, but to the American people. How much headway can we make against pervasive, awesome poverty? Even in a fairly small country, as we become more ambitious and take on larger countries, more complex societies that have these cross-hatches of AIDS and tuberculosis and chronic malnutrition on top of all this, that is the quest. How do you get governance of these countries into shape so that it can be sustained by the people, their own democratic dialog, and their own consensus?

Mr. Gootnick, do you have a final thought before we conclude the hearing about this process?

Mr. GOOTNICK. Mr. Chairman, I'd simply reiterate the key challenge, I think the Corporation faces going forward, is the ability to expend these funds accountably with the in-country structures that they intend to build at each of the recipient nations. The other key challenge I think I would highlight, is the evaluation of compact proposals. While there's been and there is a due diligence in that process, the technical rigor required to determine that a given project is the right project for the right country at the right time is a key challenge.

The CHAIRMAN. You'll try to achieve that obviously through your interviews with the MCC, but likewise in some in-country examination by you and your own personnel, and by these indicators, some of which you've said are classified, confidential. At the same time we have to have confidence that you are handling that material discretely and that's being funneled into your overall evaluation, and then hopefully over the course of time there will be a free press in the countries that will highlight what's occurring, argue about it, in an open society, with the benefit of debate. Whether it's the legislature or the political campaigns or so forth, these often tell a lot about a country, and the views of its own citizens. That may be informative to us as to what our objectives and criteria ought to be.

All of that, you have encompassed, I think, in your report. I have simply, for sake of emphasis, mentioned this as we try to conclude this hearing. We've tried to have an oversight hearing today at another mid-point to see how we're doing.

I congratulate you, Mr. Applegarth, and your associates, and you, Mr. Gootnick, and your associates for the roles that you are playing and that I think you're playing well. I think the comments from my fellow committee members indicated that.

We thank you for appearing, and the hearing is adjourned.

(Whereupon, at 11:35 a.m., the hearing was adjourned.)

ADDITIONAL QUESTIONS AND ANSWERS SUBMITTED FOR THE RECORD

RESPONSES OF PAUL APPLEGARTH, CHIEF EXECUTIVE OFFICER, MILLENNIUM CHALLENGE CORPORATION, TO QUESTIONS SUBMITTED FOR THE RECORD BY SENATOR BIDEN

Question. What capacity does the Millennium Challenge Corporation (MCC) have to assess the different impacts a country's proposal might have on women and men in terms of potential benefits? How are you encouraging different country teams to focus on this important issue as they work with countries during the proposal process?

Answer. Each compact includes a plan for monitoring various results of the program through the life of the compact, as well as a plan for evaluating the impact of the program on poverty reduction and economic growth. Data collection for this evaluation will be conducted during the compact term. The analysis of this data may continue, in some cases, after the end of the term. In general, all ex-post evaluations will assess the extent to which the program or project increased the incomes of the targeted beneficiaries.

We are in the process of recruiting staff with gender expertise to analyze the compacts generally, as we think this is an important responsibility. Additionally, we also have within our staff technical experts who incorporate gender analysis into their work on agriculture, infrastructure, environmental/social impact issues, land tenure, financial sector, and in the monitoring and evaluation frameworks. Additionally, our country teams include individuals with development experience that have done this type of analysis, are sensitive to gender issues, and take them into account when evaluating program design.

As part of our proposal analysis, MCC staff consults with women and women's groups to form a judgment about whether the proposed programs will reach women. For example, with regard to agricultural programs in Africa, where a significant share of agricultural work is performed by women, MCC's agricultural specialists work with stakeholders in each country proposing to work on agriculture to identify the particular status and role of women and how design interventions can improve their situation. Understanding a woman's role in agriculture can help to illuminate how to improve technologies to make women's work easier and more productive, whether it involves packaging inputs in volumes that can be handled more easily by women, assisting with water supply, energy for cooking, transportation to markets, etc. Supporting productivity enhancements in the crops important to women, whether for household consumption or marketing, is an important part of program design that MCC considers.

Question. Through what mechanism does the MCC evaluate how countries have taken into account the degree of input local women and/or women's organizations have had during the consultation process in which a government is to engage in order to develop its proposal?

Answer. Our approach starts with the consultative process and continues through to monitoring and evaluation. In our discussions with countries and in our written guidance, MCC stresses the importance of consultations with women and women's groups to understand their challenges. We specifically examine the extent to which women participate in consultations, including during program and project design. We also ask our staff to evaluate the extent to which their input of women is taken into account and shapes the program design.

On the program itself, MCC staff consults with women and women's groups to form a judgment about whether the programs will reach women. For example, with regard to agricultural programs in Africa, where a significant share of agricultural work is performed by women, MCC's agricultural specialists work with stakeholders in each country proposing to work on agriculture to identify the particular status and role of women and how design interventions can improve their situation. Understanding a women's role in agriculture can help to illuminate how to improve technologies to make women's work less onerous and more productive, whether it involves packaging inputs in volumes that can be handled more easily by women, assisting with water supply, energy for cooking, transportation to markets, etc. Supporting productivity enhancements in crops is important to women, whether for household consumption or marketing, and is an important part of program design that MCC explores with the partner country.

Our monitoring and evaluation indicators are, to the extent practicable, disaggregated by gender, age, and income level, so that we can see whether impacts are reaching the intended beneficiaries and are the impacts different across these groups.

Question. How will the MCC monitor and evaluate the different impact that MCA funded programs have—in both the short and long term—on women and men?

Answer. Because development interventions can have different impacts on men and women, data on performance indicators should be disaggregated by gender whenever feasible. MCC's Monitoring & Evaluation unit has adopted as policy that program evaluations include a description of which indicators can be disaggregated in this manner. For example, rural roads in Honduras will be evaluated on the extent to which they reduced travel time and cost to markets and public services for both men and women. In Madagascar, land tenure indicators will disaggregate title and land certificate holders by gender.

The due diligence process includes an assessment of the capacity of host country institutions to measure results. Where there are weaknesses in capacity during implementation, funding for monitoring and evaluation as part of the compact budget could be used to address specific areas of weakness. If weaknesses were identified prior to finalizing compact negotiations, MCC may use its 609(g) authority to help put in place the means to measure results based on gender. We expect, however, that weaknesses in collecting gender-disaggregated data ordinarily would not become apparent until a program is in the implementation phase, which is one reason that M&E plans include a description of data quality assessments to be conducted over the life of the program. This is in addition to making regular performance reporting publicly available which, in turn, allows interested groups outside of the country and MCC to review results. Based on these data quality assessments, we may structure necessary capacity building measures for collecting and analyzing gender-disaggregated results.

Question. Explain the MCC's role in helping a country finalize a compact proposal. How does the MCC balance an emphasis on country ownership with the need to ensure that proposals are sound? In the cases of Madagascar and Cape Verde, how closely do the final compacts reflect the initial proposals?

Answer. The MCC has engaged countries from the outset after they were identified as eligible to clarify our goal (reducing poverty through economic growth) and guidelines for proposal development. This has involved visits to the country as well as meetings with government counterparts in Washington and elsewhere. The MCC has suggested to governments that they put together a team to carry out a consultative process to develop a proposal for MCC funding and name a point of contact so that there is a clearly identified interface in the country. Once the MCC receives a proposal, our technical staff review that proposal in terms of the way the proposal was developed, ensuring that there was indeed a consultative process and that the program reflects national priorities, as well as identified program impacts and economic returns and policy changes that would result from the program's implementation. The MCC has defined what makes a good compact and this information is shared with host country counterparts. The criteria that the MCC considers in reviewing a proposal include:

- *Poverty reduction:* Positive impact on poverty reduction, via constructive distributive effects (as measured, for example, by the percentage of identified beneficiaries from poor households or the creation of new economic opportunities accessible to the poor).
- *Economic rate of return:* MCC economists work with our MCC partners to analyze the economic growth impact, including positive assessment of economic logic and ability to measure the expected results of how this project will contribute to growth.
- *It's measurable:* The project should have measurable targets and interim milestones for key indicators, with linkage to disbursements to the extent this is possible.
- *Country support:* Proposals should be designed with broad public support, developed through a consultative process. If the proposed projects are important to the country, and not included as the result of political compromise, MCC will consider give them careful consideration.
- *Policy reform:* For some proposed projects to be successful, it is necessary that the government implement policy reforms. MCC will consider the government's willingness to make the necessary policy reforms to make the project a success.
- *Environmental sustainability:* This is measured principally by adherence to MCC's environmental guidelines.

In the context of these criteria, the MCC team works with the country to clarify the proposal so that there can be a full understanding of what exactly the country anticipates that the MCC would fund and the links between the program proposal and the projected results. To carry out initial phases of this interchange, the MCC sends a team to the country to develop an "opportunity memo" that identifies the

context, the program, the consultative process used by the country, the opportunity for investment, likely results, sustainability and potential for policy reform. In discussions with host country counterparts, the MCC asks for rigorous justification of programs in terms of the consultative process, the feasibility of implementation, and the economic rate of return. If the program falls short on any of these, a more detailed program justification is requested to address shortcomings; in some cases, based on these discussions, the host country decides to eliminate or modify program elements.

Countries are responsible for defining their priorities in their initial proposals. However, MCC works with the country to take a development priority and help develop it into a concrete proposal. In addition, the MCC makes every effort to respect country ownership by using consistent standards to make recommendations to the host country as to whether projects will be included in the compact.

The attached table shows the components that were in the original Madagascar proposal and those components that are in the final compact. As for Cape Verde, there is not yet a final compact and negotiations are still underway. However, there have been some changes since the initial proposal.

SUMMARY COMPARISON OF MCA PROGRAM ACTIVITIES—ORIGINAL PROPOSAL VERSUS COMPACT SIGNED APRIL 18

LAND TENURE REFORM PROJECT

Original proposal (Oct. 2004) $20 M	MCC compact draft (Feb. 2005) $37.8 M
• Launch a national information campaign to educate the public. • Simplify the land code and facilitate the acquisition of land by poor rural people.	**Activity A: Support the Development of the Malagasy National Land Policy Framework ($1.1 M)** • Carry out information, education and communication campaigns designed to explain the specific land tenure reforms contemplated in the initial PNF to potential beneficiaries of such reforms, the staff of the National Land Service Administration and other interested parties. • Consolidate and refine the PNF, during and after completion of the campaigns outlined above, which may result in additional white papers, additional land law proposals and suggested donor interventions. • Conduct public outreach and dissemination of the final PNF after completion of the consolidation and refinement outlined above.
• Modernize and reform property and topographic services by installing an improved service structure and interdependency of land tenure with other sectors (tourism, agriculture, industrial investments, etc.). • Create a system for land and topographic information. • Create aerial maps. • Secure land management information electronically (rehabilitate, save and catalog all property and topographic documents in a database) and train staff.	**Activity B: Improve the Ability of the National Land Service Administration to Provide Land Services ($19.8 M)** • Index and restore documents. ○ Ask all current landholders of land titles and other formal ownership documents to bring these documents to existing land offices to compre the information currently on record with the physical documents being produced. ○ Take inventory of the existing 800,000 land documents (land titles and surveys) currently stored at the existing land management offices and produce a plan for (i) restoring the damaged land documents and (ii) scanning and digitizing all of the existing documents, including those produced by current holders above. ○ Restore a portion of the damaged land titles and surveys in and around Antananarivo and in the Zones (approximately 300,000). ○ Resolve disputes and address irregularities encountered in the indexing and restoration process.

LAND TENURE REFORM PROJECT—Continued

Original proposal (Oct. 2004) $20 M	MCC compact draft (Feb. 2005) $37.8 M
	• Modernize and computerize system. ○ Install an automated land parcel information system containing property rights information relating to each parcel (e.g., date of transfer, identification of occupant, legal property description, physical boundaries and restrictions). ○ Scan and digitize a portion of the existing land titles and surveys in and around Antananarivo and in the Zones (approximately 400,000), including those produced by current holders. ○ Procure satellite imagery for use in generating parcel maps. ○ Train staff of National Land Service Administration (central and regional offices). ○ Introduce mobile service units of the National Land Service Administration.
• Strengthen and decentralize services related to land tenure.	**Activity C: Decentralization of Land Services ($7.7 M)** • Build and equip new local land management offices (10 per Zone). ○ Finance an initial 2-year period of the operating costs of such new land management offices. ○ Provide on-the-job training to local land management office staff. ○ Establish procedures and practices for communications and coordination between the National Land Service Administration and local land management offices. ○ Develop capacity for on-going management of records in the local land management offices.
• Develop a system for registration of rural land by removing legal barriers, dedicate rights to undisputed parcels and issue land titles whenever possible.	**Activity D: Land Tenure Regularization in the Zones ($7.9 M)** • Formalize tenure in selected municipalities (communes) using one of three registration methods endorsed by the National Land Service Administration. • Implement a fast-track titling and/or property registration process within selected areas within the Zones.

LAND TENURE REFORM PROJECT—Continued

Original proposal (Oct. 2004) $20 M	MCC compact draft (Feb. 2005) $37.8 M
	Activity E: Information Gathering, Analysis and Dissemination ($1.3 M) • Finance the cost of a resident long-term land tenure expert with international experience to provide ongoing advice and technical assistance regarding policy matters (e.g., to eliminate market distortions) to MCA-Madagascar and policy-level government institutions, offices or agencies. • Finance occasional short-term national and international experts to provide more operational ongoing technical assistance and training to the staffs of the National Land Service Administration and local land management offices. • Organize and conduct workshops, seminars and other outreach activities with intended beneficiaries and other stakeholders in order to obtain their feedback and comments to improve procedures relating to property transactions and other related services. • Organize formal training and study tours outside of Madagascar for the staffs of the National Land Service Administration and local land management offices. • Complete needs assessments for future reform relating to (i) land conflict resolution methods, (ii) policy development and (iii) legal framework, based on lessons learned from the activities carried out under the Land Tenure Project.

FINANCIAL SECTOR REFORM PROJECT

Original proposal (Oct. 2004) $63 M	MCC compact draft (Feb. 2005) $35.9 M
• Improve the legal, regulatory, and policy environment for business. • Support the emergence of new trades, notably in the fields of brokerage and ancillary services.	**Activity A: Promote Legal and Regulatory Reform ($1.1 M)** • Finance the development of new banking laws and laws regulating financial instruments and markets, including enabling legislation for expanded intermediation and new credit and investment instruments. • Train government officials, judges and potential beneficiaries on the contents and application of these new laws. • Promote public awareness of these new laws through an educational and public awareness campaign.
• Develop the financial market—expand existing market for short-term treasury bonds, allow distribution of securities by microfinance institutions (MFIs), allow distribution of securities by businesses at a regional level, establish regulatory and monitoring mechanisms that guarantee the roll-out and transparency of transactions.	**Activity B: Reform Sovereign Debt Management and Issuance ($1.0 M)** • Automate all sovereign debt issuance operations. • Create new forms of sovereign debt that will appeal to a broader set of investors, including new denominations of Treasury bills. • Create a fiscal policy unit within the Ministry of Finance that will advise the Minister of Finance on sovereign debt portfolio management and issuance alternatives.
• Implement a financial system that is better adapted and more accessible for SMEs. • Promote the establishment of new financial institutions that can supply appropriate financial services through a public account.	**Activity C: Strengthen the National Savings Bank ($1.9 M)** • Increase the operational efficiency of the NSB through modernization and computerization, in particular by automating branch operations and agency issuance for sovereign debt instruments. • Increase the quality of service through staff training and the establishment of new NSB branches in the Zones. • Increase mobilization of domestic savings. • Strengthen capacity to manage liquidity facilities for MFIs.

FINANCIAL SECTOR REFORM PROJECT—Continued

Original proposal (Oct. 2004) $63 M	MCC compact draft (Feb. 2005) $35.9 M
• Implement new financial instruments (factoring, risk management, etc.).	**Activity D: Provide New Instruments for Agribusiness Credit ($8.4 M)** • Create a revolving fund for refinance of MFI assets. • Extend warehouse receipts and leasing as a means of extending credit to rural and agricultural producers. • Conduct a major study on constraints and alternatives for providing access to market-based credit to agribusiness all along the value chain.
• Improve the payments system through the installation of telecommunication and security systems in the provinces and priority zones.	**Activity E: Modernize National Interbank Payments System ($21.0 M)** • Conduct a design and cost study for a new national interbank payments system that will reduce check clearing from the current 45 days to D+3. • Provide information technology and telecommunications equipment and installation services, if the above study demonstrates feasibility and the results are acceptable to MCC (including within the expected budget or if additional financing is secured).
• Strengthen and improve accounting practices. • Establish a central credit reporting agency. • Improve communication and education in the finance sector.	**Activity F: Improve Credit Skills Training, Increase Credit Information and Analysis ($2.5 M)** • Increase awareness of new accounting standards and provide sustainable training of finance and accounting professionals through Madagascar including accountants, business managers, and microfinance loan officers. • Create a central database accessible by all providers of credit that contains credit data and payment and repayment history.

Question. Given that 70 percent of the population of Madagascar lives on less than $0.40 a day, as the MCC points out in its fact sheet, and less than 2 percent of the population holds formal bank accounts, I am surprised that almost a fifth of the total compact would go toward a check-clearing improvement system. Could you explain the rationale and public support for such a high priority on this intervention?

Answer. The focus of this component is not the 2 percent who have accounts but the 98 percent who do not. Kofi Annan announced 2005 as the International Year of Microcredit (2005) on December 29, 2003, with the following words:

> The stark reality is that most poor people in the world still lack access to sustainable financial services, whether it is savings, credit or insurance. The great challenge before us is to address the constraints that exclude people from full participation in the financial sector . . . Together, we can and must build inclusive financial sectors that help people improve their lives.

Current research shows that making the financial sector more inclusive, disproportionately benefits the poor (vis-a-vis the wealthy) and therefore reduces poverty. Two recent examples from the World Bank summarize the theoretical basis for focus on the financial sector as a poverty reduction tool:

- Finance for Growth: Policy Choices a Volatile World. World Bank and Oxford University Press; 2001, Washington.
  - "The World Bank Group has long recognized that poverty reduction and growth depend on effective national financial systems." Page ix.
  - "There is now a solid body of research strongly suggesting that improvements in financial arrangements precede and contribute to economic performance. In other words, the widespread desire to see an effectively functioning financial system is warranted by its clear causal link to growth, macroeconomic stability, and poverty reduction." Page 5.
- World Bank Policy Research Working Paper 3338, June 2004. "Finance, Inequality and Poverty: Cross-Country Evidence." Thorsten Beck, Asti Demirguc-Kunt, and Ross Levine.

- While substantial research finds that financial development boosts overall economic growth, we study whether financial development is pro-poor: Does financial development disproportionately raise the income of the poor? Using a broad cross-country sample, we find that the answer is yes: Financial intermediary development reduces income inequality by disproportionately boosting the income of the poor and therefore reduces poverty.

Madagascar's payment system is outdated and dysfunctional. It can take up to 45 days for a check to clear. We are told that the average period for a check to clear is around 25 days. Compare this to 1 or 2 days in the United States. The failure of the financial sector to achieve greater penetration must be due, at least in part, to its failure to provide one of the fundamental services—handling everyday payments. By any measure, Madagascar's financial sector fails to meet standards of performance. The country's population is approximately 17 million. Only about 200,000 bank accounts exist, implying about 1 percent of the population is participating in the formal financial sector. Another measure of the lack of penetration of the financial sector is the credit/GDP ratio, approximately 10 percent, and characterized by the IMF as among the lowest in sub-Saharan Africa, which has the lowest intermediation rate of any region in the world.

Poverty reduction and economic growth will only be permanent in Madagascar when conditions permit greater mobilization of domestic capital. A constraint is the archaic operations of the financial sector, as measured by the excessive check-clearing time. The goal of the payments system project is to reduce check-clearing times from a maximum of 45 days to a maximum of 3 days after the date of deposit ("D+3" in banker's language). We believe that this will eliminate a major barrier to the growth of the financial sector in Madagascar. This development, in turn, will permit the financial sector to make its contribution to poverty reduction and economic growth—a contribution that, by any measure is now severely constrained.

As the above analysis indicates, the beneficiaries of the project will be all the poor of Madagascar. Access to safe, remunerated savings vehicles and to the credit that will allow them to enter into the real economy will benefit anyone who avails himself or herself of the opportunity. We take other steps in the compact to assure that credit will, in fact, flow to the poor. A critical step to any of those steps, however, is an efficiently functioning traditional financial sector, including the payments system.

Question. Access to information and transparent processes are required for citizens to be able to engage in the MCA process and ultimately hold their own governments accountable for good use of MCA development funds. What steps are being taken to ensure that MCA country citizens have the information and resources, if necessary, to hold their governments accountable for MCA program objectives?

Answer. The MCC insists on transparency as a fundamental principle for program design and implementation in all programs that it funds. At the outset, the MCC advises country counterparts of the importance the MCC places on the consultative process and the fact that the way this process is carried out will be a significant consideration in program approval. The MCC encourages countries to make their proposals to the MCC public—in terms of establishing a Web site to provide continuous information not only about the proposal, but about the interactions taking place as the original proposal evolves, as well as encouraging interaction with civil society, business groups, and other relevant groups in all parts of the country and with a variety of interests. The MCC asks that the country document this process so that there can be an objective discussion of exactly what type of consultative process is taking place in relation to the MCC program.

In terms of program implementation, the MCC has encouraged countries to include nongovernmental advisors for the "accountable entity" that will oversee operations; in some countries, the proposal has included a public-private oversight board where nongovernmental members have voting rights. The MCC also encourages countries to make public all aspects of program implementation, including procurement and budgetary data, so that there will be public scrutiny of program implementation and consistency of implementation with the original design. Programs in some countries are building on the concept of social audit of implementation and include capacity building for local civil society to have the necessary information and training to carry out this oversight role.

Question. The Government Accountability Office (GAO) has made several recommendations for the MCC in the areas of transparency and governance. What are you going to do to correct the fact that not all source data used to generate country scores on the indicators were publicly available?

Answer. MCC is striving for complete transparency in the country selection process. MCC staff have considered GAO's recommendations, as well as other public

comments received about the indicators and the transparency of data. We believe that improvements in the Web site, including additional links to supplementary data sources can address the issues cited.

Question. What about what the GAO termed the "inherent limitations" in some of the indicators—how do you plant to address those limitations?

Answer. MCC evaluates the indicators used to measure government policies on an ongoing basis to ensure that we are using the best available indicators. If we find that there is a better measure of a government's policy that meets our criteria for selecting an indicator, we will propose a change to the Board of Directors. For the last selection process, the Board adopted two changes to the indicators based on our recommendation—substitution of Girls' Primary Education Completion Rates and lowered the inflation ceiling from 20 percent to 15 percent.

Additionally, to address the weaknesses in the indicators where no change is recommended, MCC can provide the Board with supplemental information to address weaknesses such as lags, gaps, and trends not reflected in the data.

Question. When do you anticipate that the MCC Board will address the corporate governance issues that GAO raised in terms of defining its role in the areas of developing corporate strategies, audit and assurance processes and developing risk management and communicating and coordinating with corporate stakeholders?

Answer. This is an ongoing process. The Board holds regular meetings in which the Board members have an opportunity to provide input and guidance to the CEO on program development matters and other strategic issues. In addition to regular meetings, there are a variety of ways in which the Board carries out its responsibilities. MCC's CEO and staff regularly apprise the Board of MCC activities through oral briefings of members and their staffs, background papers and other documents, affording the Board the opportunity to provide input to management, either directly or through agency staff.

MCC has established an interagency working group of Board agency staff that meets regularly so that all Board agencies are aware of pending issues and have the opportunity to provide an agency perspective. In its role of overseeing audit and assurance processes, the Board recently invited the inspector general to brief the Board on its planned audit activities and to provide individual Board members an opportunity to ask questions and provide input. Consideration has been given to the establishment of an audit committee to assist the Board in its risk management responsibilities, although any decision on that will likely be made after the full Board is in place. In another example, the Chair recently designated three Board members to sit on a committee to engage the CEO on compensation matters.

To more formally institutionalize these and other Board responsibilities, MCC is in the process of developing a more comprehensive "Governance Policy" for Board consideration that will address both statutory and nonstatutory Board roles in the overall oversight of the corporation, including, for example, compact development, public outreach, risk management, coordination with other donors, and policy development. Board members will be given the opportunity to consider the proposed governance policy and provide input prior to adoption of the policy by the Board.

Question. Does the board plan to establish an audit committee?

Answer. The Board will most likely make a decision as soon as the full complement of directors is appointed (two Board positions remain open at this time).

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