



*International Board
of Auditors
for NATO*

**ANNUAL
ACTIVITIES
REPORT
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INTERNATIONAL BOARD OF AUDITORS FOR NATO

ANNUAL ACTIVITIES REPORT

FOR 2008

EXECUTIVE SUMMARY

The International Board of Auditors for NATO (Board) is an independent six-member audit body reporting to the North Atlantic Council. The Board is assisted in its work by twenty-one auditors and eight administrative support personnel who are members of the International Staff. The Board is responsible for financial and performance audits of NATO bodies and the NSIP. During 2008 the Board audited some EUR 10.4 billion, of which EUR 9.6 billion relates to NATO agencies and commands, and EUR 0.8 billion to NSIP expenditures.

On 17 July 2002, the Council adopted the accruals based IPSAS as the applicable accounting standards for all NATO entities effective for the fiscal year 2006. The Board can report that progress has continued into the second year of IPSAS implementation. Both the number of audit qualifications and the restatement of financial statements, while still elevated, have decreased compared with 2006. In 2008, the Board issued 36 financial audit reports which comprised forty-six Auditor's Opinions on the accounts of NATO bodies and associated organisations. Forty of these accounts received unqualified audit opinions, including ten accounts that were corrected and re-issued to avoid qualification. The Board issued qualified audit opinions on the financial statements of six entities of which four related to compliance with IPSAS. Starting in 2011 NATO entities will be required to recognise Property, Plant and Equipment in accordance with IPSAS 17 and urgent action is required to prepare for that important milestone.

On the NSIP side, the Board audited expenditure totalling EUR 759 million. It issued 597 COFFAs with a total value of EUR 948 million. About 580 completed projects authorised between 1979 and 1994 are still not closed. The Board is actively monitoring the application of the procedures agreed with a view to the accelerated closure of the slice programme.

The Board undertook both performance audits and ad hoc studies in 2008. It completed the performance audits on the Customer Funding at the NC3A and on the NATO Logistics for Deployed Operations and issued a special report to the Council on the implementation of IPSAS within NATO. It carried out the field work for a follow-up of the performance audit of the NATO Early Warning and control system which is now (March 2009) in the process of being cleared with the entities involved. It started a performance audit of the NSIP Management, a performance audit of the Prevention of Corruption and Fraud and a study on procurement activities at NC3A. The Board carried out ad hoc studies to provide advice and support to the NATO Committees and took action to improve its own efficiency and working methods.

The Board will follow up on the recommendations resulting from the review of the internal audit function in the various NATO entities. It formulated strong reserves against the successive attempts to weaken the financial control function in the military commands, and noted increasing audit tasks for which in future the cost will need to be recovered from audited multi-national entities. The Board intends to revisit the issue of the Council delegation of budgetary authority to a lower NATO committee on the evaluation of the arrangements in 2009.

The Board provides in this annual report detailed information on the size of the budgets and expenditure audited, the staff allocated as well as the direct cost of these audits in 2008.

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CHAPTER 1

INTRODUCTION

BACKGROUND

1.1 This report to the Council has been prepared in accordance with Article 17 of the Charter of the Board, which states:

"The Board shall prepare each year:... a detailed report on the activities of the Board during the year, and on progress made in processing its reports."

1.2 The Board is an independent audit body. It is composed of six members appointed by the Council from among candidates nominated by the member countries. According to Article 3 of the Board's Charter, its members are responsible for their work only to the Council and shall neither seek nor receive instructions from other authorities than the Council.

1.3 The primary function of the Board is to enable the Council and, through their Permanent Representatives, the Governments of member countries to satisfy themselves that the common funds have been properly used for the settlement of authorised expenditure. The Board's mandate also includes checking that the operations of NATO bodies have been carried out not only in compliance with the regulations in force but also with efficiency and effectiveness.

1.4 The Board conducts financial audits of agencies and of the NSIP expenditure and also carries out performance audits. The Board's audit scope in 2008 covered EUR 10.4 billion, of which EUR 9.6 billion related to financial statements audits and EUR 0.8 billion related to NSIP audits.

1.5 The accounts of NATO bodies may be expressed in several different currencies. To help readers, and to provide some consistency, this report uses the EURO equivalent of the currencies used.

1.6 The Board's 2005-2009 Strategic Plan identifies four major goals: strengthening financial management in NATO, improving accountability in the NATO Security Investment Programme (NSIP), encouraging effective and efficient operations in NATO and promoting the Board as a model international audit organisation. The Board pursued these goals in 2008, based upon the priorities and specific targets and measures of success set out in its 2008 annual performance plan. This annual report provides for each of the goals a brief summary of the achievements in 2008.

MAIN ISSUES IN THIS REPORT

International Public Sector Accounting Standards in NATO (IPSAS)

1.7 On 17 July 2002, the Council adopted the accruals based IPSAS as the applicable accounting standards for all NATO entities effective for the fiscal year 2006. In its 2007 Annual Activities Report, the Board reported that in 2006 the NATO entities had achieved significant progress in improving the consistency and transparency of their financial reporting, despite a large number of audit qualifications and restatements of financial statements due to non-compliance with IPSAS. Progress has continued into the second year of IPSAS implementation. Both the number of audit qualifications and the restatement of financial statements, while still elevated, have decreased in comparison with 2006. With a few notable exceptions, improvements have been noted in the application of the accruals basis of accounting to expenses. In addition, improvements have been made to the consistency of footnote disclosures through the use of more standard disclosures of accounting policies.

1.8 Several areas for further improvement include better cooperation between NATO entities that interact with each other in order to ensure that timely and accurate information is being reported between the entities, the measurement and presentation of inventories, consistency in the application of IPSAS, and more useful entity specific footnote disclosures. In addition, the expiration of the 5 year transition period for the recording of Property, Plant and Equipment is approaching (to be reported in the 2011 financial statements) and much work will be needed in this area, particularly for ACO (paras 2.1 – 2.9).

Review of the Internal Audit Function

1.9 In its Review of the Internal Audit Function the Board formulated recommendations to harmonise the mandate and the standards for the Internal Audit function in NATO and to improve their functioning, organisational status and role in their entities, relying to a great extent on governance principles approved by the Council for NPLOs. The Advisory Group of Financial Counsellors (AGFC) generally supports these recommendations and currently (April 2009) considers the implications for NATO of two crucial recommendations concerning audit committees and the application of the Council Guidelines on Corporate Governance (paras 2.10 – 2.13).

The Position of the Financial Controller in the Military Commands

1.10 Consistent with advice provided in the past on the same issue, the Board has formulated strong reserves against Initial State Peacetime Establishment proposals that would result in weakening the financial control function in the Military Commands. In line with the NFR the Financial Controller should respond directly to the Supreme Commander and have full organisational independence from other important functions in the Headquarters (paras 2.14 – 2.15).

External Audit of Multi-national Entities and Reimbursement of the Cost of the Audit

1.11 In its report to the Council, the AGFC (AGFC-D(2009)0001 (INV)) agreed that the Board carry out the external audit of multi-national entities on a full cost recovery basis and that the Civil Budget Committee is the committee that should address the Board's resource problems in this respect. The Board noted that these and other additional tasks will undoubtedly impact on its resources and on its responsibilities in the field of NSIP and performance auditing, and that it intends to examine these issues during its planning for 2010 (paras 2.16 – 2.20).

Delegation of Budgetary Authority to a Subordinate Committee

1.12 In early 2007, the Council approved the revised terms of reference for the NATO military resource committees in the context of the NATO HQ Reform. These terms of reference devolve budget approval authority from the Council to the Military Budget Committee (MBC) which is a subordinate committee of the Senior Resource Board (SRB) which responds to the Council. The Board informed the Council that the budget is a prerogative of the highest authority of an organisation which should not be delegated to a lower committee. The Board intends to examine the issue on the evaluation of the arrangements later in 2009 (paras 2.21 – 2.22).

Publication of the Board's Reports

1.13 The Board's Annual Activities Report 2005 through 2007 and the Audit Report of the NATO Security Investment Programme for 2006 and 2007 are available on the NATO web site (paras 2.23 – 2.24).

Agency Financial Audits

1.14 In 2008, the Board issued 36 financial audit reports and 46 Auditor's Opinions on the accounts of NATO bodies and associated organisations. In some cases these opinions covered several entities, several sets of financial statements or several financial years. The Board issued unqualified opinions on forty financial statements including ten accounts that were restated to avoid qualification. It issued six qualified opinions on the financial statements of Allied Command Operations (ACO) 2007, Allied Command Transformation (ACT) 2007, ACE Rapid Reaction Corps (ARRC) 2006, NATO Airborne Early Warning and Control Programme Management Organisation (NAPMO) 2007, NATO CIS Services Agency (NCSA) 2006, and Alliance Ground Surveillance Programme (AGS3) 2006. Most of the qualifications and restatements of accounts related to International Public Sector Accounting Standards (IPSAS) compliance issues, misuse of funds and lack of audit evidence (paras 3.13 - 3.24).

NATO Security Investment Programme

1.15 The Board audited the expenditure presented by the nations and agencies in 2008 which totalled EUR 759 million compared to EUR 650 million in 2007. It issued 597 COFFAs with a total value of EUR 948 million of which 348 million for UK Air Defence Ground (UK ADGE), compared to 630 COFFAs for EUR 639 million in 2007. The net credit

to NATO resulting from the audit in 2008 was EUR 14.4 million. In 2004, the IC agreed on the accelerated closure of a number of projects authorised between 1979 and 1994. In 2008 it reached agreement on an Enhanced Accelerated JFAI Procedure applicable to Slices 21 to 45. At the end of 2008, about 580 completed NSIP projects, authorised between 1979 and 1994, were either not yet technically inspected, not presented for audit, or not closed for other reasons, such as outstanding audit observations. The Board is actively monitoring the application of the accelerated closure procedures (paras 4.1 – 4.11).

Performance Audits and Ad Hoc Studies

1.16 The Board undertook both performance audits and ad hoc studies in 2008. It completed the performance audits on the Customer Funding at the NC3A and on the NATO Logistics for Deployed Operations and issued a special report to the Council on the implementation of IPSAS within NATO. It carried out the field work on a follow-up of the performance audit of the NATO Early Warning and Control System which at the time of this report was at clearance stage with the entities involved. It started a performance audit of the NSIP Management, a performance audit on the Prevention of Corruption and Fraud and a study on procurement activities at NC3A. The Board carried out ad hoc studies to provide advice and support to the NATO Committees in relation to the financial regulations, corporate governance and internal audit, and took action to improve its own efficiency and working methods. The population of the TeamMate audit management software and the preparation of a pilot audit concentrating on processes, risks and controls come under that heading (paras 5.1 – 5.9).

Matters relating to the Board

1.17 The Board had its full complement of six serving Members for the whole of 2008. Since 2006 the Board has an authorised establishment of twenty-one auditors. The auditor vacancy rate in 2008 was 1.1 staff years. At the end of 2008, five of the twenty audit staff present were women. The Board Members and Auditors came from twelve nations. The Auditors came from ten nations (paras 6.1 – 6.3).

1.18 The publication of the Board's reports is an opportunity to improve its external visibility. Internally, the Board has worked on improving staff satisfaction in the areas of training and internal communication (para 6.4).

1.19 In 2008 the Board initiated a pilot risk based audit at NAMSA, with the assistance of a consultant. The initial results look promising. The Board will evaluate the results of the pilot project in view to a potential extension of the approach to other entities (paras 6.5 – 6.6).

1.20 The Board foresees an average of two weeks' training for each auditor. In 2008 each auditor received on average 11 days of training. Common training included topics related to fraud and corruption awareness, the use of the Interactive Data Electronic Applications (IDEA) software for fraud detection, performance auditing and risk/controls based auditing, provided by external trainers. Several experience-sharing sessions covered performance auditing in the Board, sampling and auditing IPSAS compliance. Individual

auditors participated in seminars organised by their professional organisations (paras 6.7 and 6.8).

1.21 The Board provides in this annual report detailed information on the size of the budgets and expenditure audited, the staff allocated as well as on the direct cost of these audits in 2008 (paras 6.9 – 6.11).

1.22 The Competent National Audit Bodies (CNABs) met on 6th May 2008 to discuss the Board's 2007 Annual Activities Report. The Board presented that report to the Council on 2nd July 2008. The Board continued to develop its contacts with the professional audit community. The Board's representatives participate in a European Organisation of Supreme Audit Institutions (EUROSAI) conference and met with visitors from the Supreme Audit Institutions and NATO entities (paras 6.12 – 6.16).

CHAPTER 2

ISSUES OF ACCOUNTABILITY AND GOVERNANCE IMPORTANT TO THE BOARD

INTERNATIONAL PUBLIC SECTOR ACCOUNTING STANDARDS IN NATO

Introduction

2.1 On 17 July 2002, the Council adopted the accruals based IPSAS as the applicable accounting standards for all NATO entities effective for the fiscal year 2006. The Ad Hoc Working Group of Financial Controllers prepared the transition to IPSAS and acts as a forum where NATO entities can share knowledge and experience as well as working to ensure the consistent application of IPSAS. The Board participates in these meetings.

2.2 In its 2007 Annual Activities Report, the Board reported that in 2006 the NATO entities had achieved significant progress in improving the consistency and transparency of their financial reporting, despite a large number of audit qualifications and restatements of financial statements due to non-compliance with IPSAS. That progress has continued into 2007, the second year of IPSAS implementation.

2007 Results

2.3 The results of our audits of the 2007 financial statements show that both the number of audit qualifications and the restatement of financial statements, while still elevated, have decreased in comparison with 2006. The results show that 35% of the 2007 financial statements were restated (compared with 52% in 2006) as a result of our audits and that another 17% of the 2007 financial statements received negative (qualified) audit opinions due to non-compliance with the IPSAS standards (compared to 35% in 2006). Without the restatements, approximately 52% of the financial statements would have been qualified in 2007 (compared to 75% in 2006). The results, while supporting that progress has continued, also show that further progress is still necessary.

2.4 As shown above, the Board has continued with its policy in which, if certain conditions were met, the Board would issue its audit opinion based on the restated financial statements. The Board has extended such flexibility as a practical way to address the continued transition to IPSAS. In 2007, four entities took advantage of this policy, resulting in the restatement of eight¹ different financial statements (compared to nine in 2006). In all such cases where audits have been finalised as of the date of this report, the financial statements received unqualified audit opinions as a result of the restatement.

2.5 With very few notable exceptions, improvements have been noted in the application of the accruals basis of accounting for expenses. In addition, improvements have been made to the consistency of footnote disclosures through the use by most entities of more

¹ The International Staff prepared seven financial statements for 2007 (IS, New Headquarters, MSIAC, AGS3, Pension Plan, Provident Fund, and Retiree's Medical Claim Fund) that have been audited by the Board. Five of these financial statements were restated.

standard disclosures of accounting policies.

2.6 Areas needing further improvement, while not exhaustive, include:

- The cooperation between NATO entities that interact with each other in order to ensure that timely and accurate information is being reported between the entities, particularly in the areas of expenses incurred against advances received from another NATO entity and inventories managed by one entity on behalf of another NATO entity;
- Consistency of accounting treatments and presentations, such as miscellaneous and interest revenue recognition, the treatment of surplus funds and the presentation of reimbursable activities and delegated budgets;
- A lack of attention to some of the more detailed requirements of IPSAS, particularly in relation to the completion of footnote disclosures.

2.7 In addition, the expiration of the 5 year transition period for the recording of Property, Plant and Equipment is quickly approaching (to be reported in the 2011 financial statements). Much work, including the identification of assets to be reported and the valuing of such assets, will be needed in this area and the Board encourages the entities to ensure that adequate efforts are being directed towards the achievement of this goal.

Conclusion

2.8 □□ The primary objective of IPSAS implementation “was to harmonise accounting standards and reporting formalities across NATO, taking into account the Alliance’s heterogeneous structure.”² The Board recognises the continuing efforts being made by the NATO entities to improve the application of IPSAS within their entities and notes that their efforts have resulted in increased transparency, improved accountability and the availability of comprehensive and more accurate financial information to the users of the financial statements, primarily the Nations.

2.9 However, as evidenced by our 2007 audit results, much still needs to be done. The Board encourages the minority of NATO entities who have not yet achieved IPSAS compliancy to continue in their efforts to do so. For all entities, including the majority of NATO entities who have already achieved IPSAS compliancy, continual efforts will be needed to maintain, and to achieve further improvements, to the current situation.

REVIEW OF THE INTERNAL AUDIT FUNCTION

2.10 In 2005, the Board followed up on a previous review undertaken in 1996 of the Internal Audit function in NATO. The purpose of the review was to evaluate progress made in the various NATO bodies and to update the recommendations as appropriate, taking account of the changing role and environment in which the Internal Audit function operates. The Board formulated the following recommendations:

² PO(2002)109, dated 23 July 2002, Establishment of NATO Accounting Standards.

- The adoption of a common core internal audit mandate;
- Compliance with generally accepted internal auditing standards;
- Granting the possibility of direct access to senior management, also in military commands and the IS, where internal control is a financial control responsibility;
- The establishment of audit committees comprising selected nations representatives reinforced by high level executives from NATO;
- The avoidance of overlapping executive and internal audit functions; and
- The extension of the Council Guidelines of Corporate Governance for NPOs to the International Staff and the military commands.

2.11 The AGFC reviewed the report in 2008 and 2009. It voiced support for a strong internal audit function in NATO and supported most of the Board's recommendations.

2.12 At the time this annual report (April 2009) was prepared, the AGFC was still discussing the implications for NATO of two crucial recommendations related to the establishment of audit committee and the extension of the Council Guidelines of Corporate Governance to all NATO bodies.

2.13 The Board will follow up on the implementation of these recommendations in every entity.

THE POSITION OF THE FINANCIAL CONTROLLER IN THE MILITARY COMMANDS

2.14 Articles 21-25 of the NATO Financial Regulations and the related implementing measures define the responsibilities of the Financial Controller. The regulations grant him the organisational status and independence required to set up and manage a system of budgetary and financial control on behalf of the Supreme Commander and makes him personally accountable for financial anomalies.

2.15 On several occasions in the past³ the Board has formulated strong reservations against military command structure proposals that make an artificial distinction between the Financial Controller as advisor with direct access to the Supreme Commander and as head of the J8 function reporting to Deputy Chief of Staff Support/Resources (DCOS) (the so-called "dotted line" or "twin hat" arrangement). The Board's concern regarding that arrangement is that DCOS Support/Resources is an important budget holder who is subject to the Financial Controller's mandate. This means that the Financial Controller is supposed to apply control over a supervisor, a situation which creates a conflict of interest. It is clear to the Board that the Financial Controller should be placed in the organisational level that allows him to interact directly at an equal level with other senior officers responsible for the main Headquarters functions. In the Board's view, however, the proposed arrangements

³ Statement by the Chairman of the International Board of Auditors in the MBC meeting of 26 January 2005 subsequently brought under the attention of the Council as attachment to C-M(2005)0027 of 27 March 2005; Statement by the Chairman of the International Board of Auditors for NATO in the Military Committee on 19 July 2005; and letters by the Chairman of 13 December 2005 and 17 March 2009 to the Chairman Military Budget Committee, reiterating the position of the Board with regard to the alignment of the Financial Controllers in the military commands. This occurred recently again with regard to the Initial State Peacetime Establishment for HQ SACT of 22 January 2009, which seems to be representative of the approach taken for many of the posts of Financial Controller throughout the integrated military structure.

weaken the Financial Controller's position at a time when their position should be strengthened.

EXTERNAL AUDIT OF THE MULTI-NATIONAL ENTITIES AND REIMBURSEMENT OF THE COST OF THE AUDIT

2.16 At the end of 2007, the Board informed the Chairman of the Council that two new multi-nationally funded entities requested external audit by the Board. The Board's mandate does not normally cover such entities and explicit Council agreement is therefore required. Several nations in the Council raised issues for further discussion in the AGFC, namely that:

- The cost of the audit needed to be reimbursed by the multi-national entities;
- A discussion needed to be initiated about the role of IBAN and its contribution to the administrative reform of the Alliance; and
- IBAN should shoulder these additional tasks within its current staff and resources without burdening the civil budget.

2.17 The Board stated in the AGFC it was already auditing 27 multi-national entities, some of them since the early sixties and that it had no problem accepting additional entities subject to Council consent. It also stated that it had the cost information available but that charging for the audit would not directly address the resource problems as the return from the audit would flow back to the nations as miscellaneous income, and that although the impact of such audits is relatively small⁴ resource implications would ultimately need to be addressed.

2.18 The AGFC recognised that multi-nationally funded entities have an operational linkage with NATO, but also that common funds should not be used on non common-funded activities and that the Civil Budget Committee is the appropriate committee to address the resource issues for the audit.

2.19 In its report to Council, the AGFC agreed (AGFC-D(2009)0001 (INV)) that the Board should carry out the external audit of multi-national entities on a full cost recovery basis, subject to the implementation of appropriate transition measures for pre-existing arrangements and that full cost recovery would start in January 2012.

2.20 In the meantime, new multi-national entities are being established and new responsibilities are being (March 2009) designed for the Board in relation to the external audit of trust funds amounting up to USD two billion per year, an increase of the yearly audit universe by some 15%. These new tasks will undoubtedly impact on the Board's resources and affect its capability to carry out other responsibilities in the field of NSIP and performance auditing. The Board intends, in the first place, to meet these challenges through increased efficiency in the NSIP and financial audits, but it cannot exclude requests for additional resources. It will consider these issues during its planning for 2010.

⁴ An audit cost of EUR 162,648 in 2008, covering 194 staff days plus travel.

DELEGATION OF BUDGETARY AUTHORITY TO A SUBORDINATE COMMITTEE

2.21 On 14 February 2007, the Council approved C-M(2007)0010 “Revised Terms of Reference (TOR) for the Senior Resource Board, the Infrastructure Committee and the Military Budget Committee”. The revision is a result of the NATO Headquarters Reform that comprises a number of initiatives to improve NATO’s working practices and business procedures, inter-alia in the area of resource management that was previously dissipated over various committees.

2.22 Some of the provisions of these revised TOR affected the working practices and the mandate of the finance committees and still require final resolution. Other provisions delegate budget authority that previously was a Council prerogative, to the MBC, a subordinate committee of SRB. These provisions constitute a significant exception to the NATO Financial Regulations. They also violate the principles of Corporate Governance approved previously by the Council on 28 September 2005 with C-M(2005)0087. More detail on this issue is provided in the Annual Report 2006 in paras 5.6 to 5.9. As previously announced, the Board will revisit the issue on the evaluation of the arrangements, now scheduled for the second half 2009.

PUBLICATION OF THE BOARD’S REPORTS

2.23 The question of public access to the Board’s reports as a means to increase transparency and accountability has been raised several times in the past in the context of the Board’s annual report, by SAs and in the Advisory Group of Financial Counsellors (AGFC). Following a recommendation by the AGFC formulated during its review of the Board’s 2005 annual report, the Council on 21 February 2007 agreed to the publication of the annual reports beginning with the 2005 report. Similarly, on recommendation of the Infrastructure Committee, the Council agreed on 12 October 2007 that the annual reports on the audit of NSIP may be released to the public, beginning with the 2006 report.

2.24 The Board’s Annual Activities Report 2005 through 2007 and the Audit Report of the NATO Security Investment Programme for 2006 and 2007 are available on the NATO web site (<http://www.nato.int/issues/iban>).

CHAPTER 3

AGENCY FINANCIAL AUDITS

BACKGROUND

3.1 The Board audits civilian and military headquarters and other entities established pursuant to the North Atlantic Treaty. The Board also audits other activities or operations in which NATO has a particular interest such as the multi-nationally funded Commands and the NATO Parliamentary Assembly. The Board refers to all these audits as agency audits. In 2008 there were 82 such agencies that come under the Board's mandate. They include 47 military headquarters (HQ) of which 24 HQ are common funded by a NATO budget and 23 HQ are multi-nationally funded by the participating nations; 15 NATO Production and Logistics Organisations (NPLOs) plus 4 national divisions attached to these NPLOs with a budget approved by their respective finance committees or governing bodies; and 16 military, civilian and other bodies of which 4 entities have a multi-national status. The audited entities are listed in Annex C. These bodies are funded through the civil and military budgets approved by the Council, budgets approved by the governing bodies of NPLOs, or budgets approved by the nations participating in a multinational entity or activity.

Some NATO bodies also implement NSIP projects and receive funding from that programme. The Board is also mandated to audit non-appropriated funds covering morale and welfare activities for NATO staff. In 2008, the agency accounts to be audited by the Board amounted to EUR 9,613 million (see details in Annex D to this report).

3.2 NATO bodies have a varying degree of autonomy in managing their operations. All NATO bodies are subject to the NATO Financial Regulations (NFR) that are approved by the Council and that provide a high level financial and budgetary framework. These NFR also apply to most of the multinational entities via an explicit provision in their memoranda of understanding.

3.3 Although some entities group or consolidate financial information at varying levels, there is no NATO-wide financial reporting. The result is that in many cases the financial statements of the different NATO bodies are not homogeneous and difficult to compare. The implementation of IPSAS in the NATO funded entities, with effect from the 2006 financial statements, is an opportunity to harmonise and improve accounting and financial reporting.

AUDIT MANDATE

3.4 According to the Board's Charter, the primary function of the Board is, by its audit, to enable the Council and, through their Permanent Representatives, the Governments of member countries to satisfy themselves that common funds have been properly used for the settlement of authorised expenditure. The Board is responsible for checking that expenditure incurred by NATO bodies is within the physical and financial authorisations granted and that it is in compliance with applicable rules and regulations. The Board provides a similar assurance to the participating nations and the governing bodies of the multinational entities. The Board's financial audits result in an audit opinion on the financial

statements of NATO bodies issued in accordance with the NFR and international standards on auditing.

PERFORMANCE IN 2008

3.5 One of the goals of the Board's 2005-2009 Strategic Plan aims at reinforcing financial management in the NATO bodies. The Annual Performance Plan for 2008 identified two criteria to measure successful achievement: (1) timeliness of the audit reports and (2) the amount of recommendations implemented.

3.6 The target for the first objective (timeliness) was to have 100% of the high risk audits to be submitted for Board approval by the end of the calendar year. The Board approved audit reports for only five of the nine entities identified as high risk (56% of the target). The reasons are mostly external: audits planned late in the year, but also requests for extension of clearance delays, discussion on the facts and supporting evidence, and incorrect or incomplete financial statements requiring additional audit visits. In general, also audit work has been affected by the late publication of financial statements (five of the nine entities), often in connection with IPSAS related issues.

3.7 The Board came close to achieving its second target of 80% of the recommendations implemented, within a three-year period of the audit report date. Of the 82 observations formulated in 2005, 64 observations (78%) were resolved by 2008.

AUDIT METHODOLOGY AND CONDUCT OF AUDITS

3.8 The objective of the audit of financial statements is to provide assurance that these statements present fairly in all material respects, the financial position of the NATO body and the results of its operations, on a basis consistent with the previous year; and that the underlying transactions are in compliance with budgetary authorisations and relevant regulations. The Board's audit methodology distinguishes the usual phases of Planning (including mid-term strategic and annual planning), Audit Execution, Reporting and Follow-up and is compliant with the auditing standards of the International Organisation of Supreme Audit Institutions (INTOSAI), complemented, as and when required, by the International Standards on Auditing issued by the International Federation of Accountants (IFAC). The audit process is fully integrated into the TeamMate audit software.

3.9 Audits are conducted on the agency site by auditors, under the supervision of a Board Member. The more significant agencies and those with a higher risk are audited every year. A few agencies posing only a small audit risk are audited every two or three years. In that case a minimal review of the financial statements is nevertheless undertaken during the years not covered by a full audit. The Council endorsed this policy of cyclical auditing in 1990. Annex C shows the cyclical basis on which the Board plans and carries out the audits of agencies and commands. Nineteen entities were not scheduled for audit in 2007 and will be audited over the next two years. They represent about EUR 70 million in annual budget, which is less than 1% of the Board's audit scope for 2008.

ALLOCATION OF RESOURCES

3.10 The Board is responsible for the audit of some 82 different agencies and commands, some of which consolidate their accounts. Amounts audited range from less than EUR 0.5 million to over EUR 5 billion. The Board also audits the expenditure of over 30 NSIP host nations (NATO bodies and nations), with an audited scope of EUR 759 million in 2008.

3.11 Agency audits are resourced on the basis of risk and available staff. The risk assessment takes into account elements such as the entity's size in budgetary and staff terms, its organisational complexity in terms of the number of locations, programmes and budgets, the complexity of the transactions (number, variety), the time expired between two audits. It also covers the qualitative elements such as external visibility and sensitivity of the activities, and the risks for overall accountability and control. Issues that may affect the allocation of resources include a qualified or adverse audit opinion, the creation of a new NATO body, the implementation of new activities, a reorganisation or change in management, problems with the implementation of an accounting system or any other event that creates an additional risk for the agency's activities. Elements such as these explain for example why the Board uses proportionally more resources on military commands than it does on NPLOs, or why the audit effort is not necessarily proportional to the size of the entities' activities.

3.12 Throughout the process, the Board maintains a high degree of flexibility, which allows it to make optimal use of its resources. The Board considers that, through its position in NATO and the inputs from the audit teams, it has a good overview on where the risks lie and on the resources needed to cover them.

SUMMARY OF AGENCY AUDIT WORK IN 2008

3.13 In 2008, the Board issued thirty-six financial audit reports comprising forty-six Auditor's Opinions on the accounts of some 65 NATO bodies and assimilated organisations, using 10.9 staff years (52% of the authorised auditor establishment). In several cases the audit reports covered several entities, several sets of financial statements or several financial years.

3.14 Table 3.1 below summarises the amounts audited and resources used for the three types of agency audits during 2008 and 2007.

TABLE 3.1
AGENCY EXPENDITURE AND AUDIT EFFORT (2008-2007)

| | Audit Scope (EUR Million) | | Audit Effort In staff years | | Audited per Staff year (EUR Million) | |
|----------------------|------------------------------|--------------|--------------------------------|-------------|---|------------|
| | 2008 | 2007 | 2008 | 2007 | 2008 | 2007 |
| NPLOs | 7,989 | 7,586 | 5.2 | 4.6 | 1,536 | 1,649 |
| Commands | 1,019 | 836 | 3.4 | 3.6 | 300 | 232 |
| Civ. & Mil. Agencies | 606 | 459 | 2.3 | 2.3 | 263 | 200 |
| Global Average | 9,614 | 8,881 | 10,9 | 10.5 | 882 | 845 |

3.15 Resources allocated to agency financial audits increased by 4%, from 10.5 to 10.9 staff years. This increase illustrates an overall improved staff situation (a vacancy rate of 1.1 staff years compared to 1.9 in 2007), and a significant improvement in the audit effort devoted to NPLOs. The disparity between amounts audited per staff year in NPLOs and other agencies is explained by the differences in size and by different risk factors mentioned in the previous section on allocation of resources.

SIGNIFICANT AUDIT OPINIONS

3.16 In 2008 the Board issued forty-six Auditor's Opinions comprising 40 unqualified opinions, including ten accounts that were restated to avoid qualification. The Board issued six qualified opinions on the financial statements of ACO 2007, ACT 2007, ARRC 2006, NAPMO 2007, NCSA 2006, and AGS3 2006. Most of the qualifications and restatements of accounts related to International Public Sector Accounting Standards (IPSAS) compliance issues. An explanatory note on the different types of audit opinions is provided on page 3 of Annex B.

3.17 This section provides a summary of the modified opinions issued in 2008. It follows up on previous modified opinions as required.

3.18 **Qualified opinion on the ACO 2007 accounts.** The Board issued a qualified audit opinion for a limitation on the scope of the audit. This resulted from the fact that the Board has not been able to satisfy itself that inventories and expenses were accurately presented because inventory and expense data supplied by other NATO bodies were not always timely, accurate or complete (see Annex B para 1).

3.19 **Qualified opinion on the ACT 2007 accounts.** The Board issued a qualified opinion due to a scope limitation resulting from the fact that ACT did not perform an assessment to determine the adjustments, if any, that would have been necessary to properly account for IPSAS as of 1 January 2007. Therefore, the Board has not been able to provide full assurance that the 2007 expenses, and revenues, have been recorded in accordance with IPSAS (see Annex B para 2).

3.20 **Qualified opinion on the ARRC 2006 accounts.** The Board issued a qualified opinion because the command had used shared funds for a purpose that was not authorised in the budget, the used amount was not clarified and had omitted the related transactions from the financial statements. The command had used funds of the participating nations to prefinance the purchase of a commemorative painting of the British command during the HQ ARRC deployment in Afghanistan from April 2006 to February 2007 (see Annex B para 3).

3.21 **Qualified opinion on the NAPMO 2007 accounts.** The Board issued a qualified opinion because of a scope limitation relating to the fact that the Board has not been able to satisfy itself that USD 24.1 million of additions to the Large Aircraft Infra-Red Counter Measures (LAIRCM) asset in progress in 2007 represented work undertaken by the US contractor relating to the LAIRCM programme. This is because the Board does not have access to the indirect contracting process that is used by the US Government to transform

the invoices received from the US contractors into the U.S. Government billing statements that are then sent to NAPMA. As a result, the Board is not in the position to assess that this process is either reliable or results in billings that accurately represents work performed by the US contractors (see Annex B para 14).

3.22 Qualified opinion on the NCSA 2006 accounts. The Board issued a qualified opinion because NCSA had not adjusted the 2006 opening Statement of Financial Position to take account of the adoption of IPSAS as of 1 January 2006; did not report the CIS inventories held for ACO; recorded payments for NAMSA Administrative Expenses as expenses although they are in fact pre-payments, and should be reported as such until it is determined that NAMSA effectively incurred expenses against these funds; and understated expenses and revenues by EUR 4.2 million in 2006, due to the improper cut-off of expenses in accordance with accrual accounting principles at year-end (see Annex B para 17).

3.23 Qualified opinion on the AGS3 2006 accounts. The Board issued a qualified opinion for lack of compliance with IPSAS in the area of recognition of expenses. The expenses had been presented in the Statements of Financial Performance based on budgetary commitments. That approach, in material instances, did not produce accurate expenses in accordance with the accrual basis of accounting under IPSAS (see Annex B para 24).

FOLLOW-UP ON PRIOR YEARS' QUALIFIED OPINIONS

3.24 In 2007 the Board issued eleven qualified opinions on ACO 2005 and 2006, ACT 2005 and 2006, CIMIC GS 2004 and 2005, NAPMO 2006, IS 2006, MSIAC 2006, New NATO HQ 2006, NSIP 2005, RMCF 2006 and one disclaimer of opinion on NCSA 2005 accounts. In 2008, only six accounts received a qualified audit opinion. In most cases the entities had taken corrective action on the previous year's qualification issues (MSIAC 2007 and New NATO HQ 2007, RMCF 2007) but were qualified again for other IPSAS related reasons (ACO 2007 and ACT 2007, NCSA 2006). The NAPMO 2007 accounts were qualified again for a scope limitation relating to documentation insufficiently supporting the transactions. At the time this annual report was prepared (March 2009), no update information was available for the IS 2007 and CIMIC GS 2006 as the audit reports were not yet final.

CHAPTER 4

NATO SECURITY INVESTMENT PROGRAMME AUDITS

BACKGROUND

4.1 The Annual Activity Report gives a brief outline of the Board's activities and concerns in respect of the NATO Security Investment Programme (NSIP). Under Article 17 of its Charter, the Board also prepares a separate report to the Council summarising the result of the audit of NSIP expenditure. The report will be issued later in the year, after all NSIP expenditure made in 2008 has been reported by nations and NATO agencies.

4.2 NATO established the Infrastructure Programme in 1951 to build facilities to meet its military requirements. The nations share the cost of the Programme based on agreed percentages. The "Host Nation" is normally responsible for the planning and execution of the project. The Council made some major changes to the Programme in 1994 and renamed it the NATO Security Investment Programme. The Programme is overseen by the Infrastructure Committee (IC).

OBJECTIVES OF THE NSIP AUDITS

4.3 Under Articles 13, 14 and 16 of its Charter, the Board verifies that common funds have been properly used for the settlement of authorised expenditure, in particular within the physical and financial authorisation granted. It has to check whether all payments for which reimbursement is claimed have actually been invoiced and paid and to detect any item that is non-eligible for NATO funding. The audit results in a Certificate of Final Financial Acceptance (COFFA). The Board certifies for each project it has audited an amount as a charge to NATO common funds. In principle, this requires that every invoice needs to be checked.

4.4 It should be noted that this is different to the agency financial audit. There the Board's responsibility is to express an opinion as to whether the financial statements are fairly presented. The objective is to obtain reasonable assurance whether the financial statements are free of material misstatements. This allows checking the supporting documentation on a test basis.

AMOUNTS AUDITED AND CERTIFIED IN 2008

4.5 The Board audited the expenditure presented for audit by the nations and agencies in 2008. It conducted 28 audit missions in 8 nations, 4 agencies and one strategic command. These audits covered expenditure amounting to EUR 759 million, compared to EUR 650 million in 2007. The Board issued 597 COFFAs with a total value of EUR 948 million (of which EUR 348 million is for the major UK ADGE project), compared to 630 COFFAs for EUR 639 million in 2007. As a result of the audit of NSIP projects in 2008, the net credit in favour of the NSIP was EUR 14.4 million.

PERFORMANCE IN 2008

4.6 In 2008, the Board spent 2.4 staff years (11% of the authorised auditor establishment) on the audit of NSIP. The Board continued implementing its 2005-2009 Strategic Plan. One of its goals is to improve accountability in the NSIP. In its Annual Performance Plan, the Board developed measures of success and set targets for 2008. One target was to increase the percentage of the certified portion for nations by 2%. The realised figure will be commented upon in the Board's 2008 report on the audit of the NSIP. A second target of auditing at least EUR 350 million in territorial host nations was exceeded by EUR 50 million. The third target, to issue 600 Certificates of Final Financial Acceptance, was nearly met (597). These achievements illustrate the efforts of the Board to close NSIP projects.

THE BOARD'S 2007 NSIP REPORT

4.7 The Board issued its report on the 2007 audit of NSIP on 24th October 2008. The report formulated a number of comments and proposals directed towards improving the accountability and transparency of the programme. The IC is yet to discuss the document and issue its report to the Council.

ACCELERATED CLOSE-OUT OF THE SLICE PROGRAMME

4.8 In 2004, the IC agreed the proposals for an Accelerated Joint Formal Acceptance Process, aiming at the acceptance into – and the deletion from – the NATO inventory of whole groups of projects, without on-site inspection. It also agreed, in principle, that all projects qualifying under this process also automatically qualify for a lump sum conversion of the relating existing fund authorisations. This process was applicable to projects with a financial value of less than EUR 500,000.

4.9 In 2008, the IC reached agreement on an Enhanced Accelerated JFAI Procedure, applicable to Slices 21 to 45. The aim was to expedite the financial closure of projects, by means of an extension of the existing procedures to an additional group of projects, namely projects with a value from EUR 500,000 to EUR 2 million, and by new procedures for higher value projects, namely projects with a value above EUR 2 million to EUR 10 million. For these projects the JFAI reports are based on the authorised quantities, which may vary by up to 10 percent from the authorised figure within the limits of the authorised amount.

4.10 At end 2008, about 580 completed NSIP projects, authorised between 1979 and 1994, were either not yet technically inspected, not presented for audit, or not closed for other reasons, such as outstanding audit observations.

4.11 The Board is actively monitoring the application of the procedures agreed with a view to the accelerated closure of the Slice Programme.

CHAPTER 5

PERFORMANCE AUDITS AND AD HOC STUDIES

INTRODUCTION

5.1 The Board's Charter mandates it to assess efficiency and effectiveness of NATO operations. It refers to these as performance audits. The Board occasionally provides advice to NATO committees and agencies and undertakes initiatives to improve its own efficiency and working methods. These activities are referred to as ad-hoc studies.

BACKGROUND

Performance audits

5.2 The Board is committed to carry out at least one substantial performance audit per year, complemented by a number of small scale studies in which limited performance aspects are covered. To support that commitment, it has developed performance auditing guidance, requiring regular consideration by the Board of new audit topics, a systematic follow up of the progress in ongoing performance audits and the involvement of Board Members and financial auditors in the identification of potential topics in the agencies audited by them. The Board also decided to enhance its performance audit capabilities by increasing the resources dedicated to performance audits, by recruiting staff with performance audit background and providing ad-hoc performance audit training to existing staff, and investigating the possibility of involving SAI experts in certain phases of conducted performance audits. The Board has also developed a TeamMate module for performance audits that incorporates the related procedures.

5.3 In 2008 the Board spent 2.2 staff years on performance audits, corresponding to 11% of its resources (equally 2.2 staff years or 11% in 2007). It carried out performance audits on the NATO Logistics of Deployed Operations and on the system of Customer Funding at the NC3A, on which it spent respectively 0.5 and 0.4 staff years in 2008. The Board also completed the survey and started the field work for a NATO-wide performance audit on fraud prevention and detection and a performance audit of the management of the NSIP and included in its regular financial audit studies on procurement and contracting activities in NC3A and the International Staff. It completed the field work for a follow up audit on a previous performance audit on the NAEW&C Programme, for which the report was being factually cleared at the time this annual report was prepared (March 2009). A follow up audit on the ACO Financial Organisation and Management, was planned for 2008 but had to be rescheduled to 2009 due to lack of resources. The Board also issued a special report to the Council on the implementation of IPSAS within NATO.

Ad hoc studies

5.4 As in the past, the Board responded to requests for advice from NATO bodies and committees. It was involved in meetings and workshops on IPSAS. It advised NATO committees on audit, finance and governance related issues. This included issues such as

charging for the audit of multi-nationally funded entities, initiatives to enhance the internal audit function in NATO, questions relating to the position and independence of the financial controller and the internal audit function in the military commands, the application of the Council guidelines for corporate governance to the IS and military commands. Further internal study work related to the preparation of a risk and controls based pilot audit at NAMSA, with the help of a consultant (see paras 6.5 and 6.6). In 2008 the Board used 0.6 staff years (3%) on such study work and advice to NATO bodies and committees (1.3 staff years or 7% in 2007).

PERFORMANCE IN 2008

5.5 One of the goals of the Board's 2005-2009 Strategic Plan is to encourage effective and efficient operations in NATO bodies. Success is measured through (1) the proportion of reports presenting recommendations and/or options (target 100%), (2) the percentage of recommendations implemented over a three-year period (target 70%) and (3) the percentage of performance audits that are followed up two years after approval of the report (target 100%).

5.6 Both performance audit reports issued in 2008 contained recommendations and consequently met the first target. The second target of implementing 70% of the recommendations within a three-year period was only partly met as not more than half of the observations resulting from the performance audit of the NAEW&C Programme were entirely resolved. The other half of the observations was either partly or not at all resolved. The third target of following up on previous performance audits within a time frame of two years was not met. In one case the three years had elapsed before a follow up audit took place, another audit will only be followed up on four years after the approval of the report. Delays in the follow up of previous audits occurred because the Board had decided to give priority to the ongoing performance audits.

PERFORMANCE AUDITS AND STUDIES CARRIED OUT IN 2008

5.7 In its audit of the **NATO Logistics of Deployed Operations**, the Board has audited performance aspects of the NATO concept of Multinational Logistics in actual deployed operations, focussing specifically on operations in the International Security Assistance Force (ISAF) and the Kosovo Force (KFOR). The Board has formulated recommendations aiming at improving regulations, decision-making processes, funding mechanisms, training for deployed staff as well as procedures and structures to document and use lessons learnt, training and coordination of logistics support. The Board also recommended that nations, NATO Military Authorities, and NATO HQ, examine whether NATO is effectively structured to logistically support out of area operations such as ISAF (see Annex B Para 38).

5.8 In its audit of the **Customer Funding (CF) Regime at NC3A**, the Board analysed how that new mechanism of funding NC3A has affected the agency's management structure and business processes, to what extent it made NC3A services more efficient and effective, how it affected the Customers' requirement definition and performance validation, what lessons had been learnt and what the main challenges were for improving the system.

The audit confirmed that NC3A continuously adjusts its structures and processes to the new funding system. The Board recommended that the supervisory committees improve monitoring of the agency's performance. At the NSIP side, NC3A should discuss with the NOR the level of detail needed to support the requests for project service costs and it should also more closely adhere to NSIP regulations relevant to the technical validation of projects outputs. The Board recommended that ACT sign purchase orders as early as possible in the process, and try to limit the drawbacks of ACT's military staff rotation. NC3A should in its billing reports to ACT provide better information, showing the link between work invoiced and deliverables produced. The Board recommended that SHAPE improve the procedures for management of its requirements and for measurement of NC3A performance. With regard to the issue of competition with industry, the Board recommended that the related policy documents be updated: so far, NC3A customers have only made a limited use of competition and hard data on financial benefits have not yet been provided. The NC3 Board replied in its formal comments that it takes its responsibilities to measure NC3A performance very seriously, that it does not share the perception that NC3A is expensive and that it would welcome a comparative study by the IBAN auditors with similar organisations (see Annex B Para 37).

5.9 The Board's **Special Report to the Council on the Implementation of IPSAS within NATO** provides a status report on the issue after one year of IPSAS implementation. That report was approved in May 2008 but its conclusions and recommendations, because of their importance, had already been included in the 2007 Annual Report and considered by the Council in the context of that report. The concerns formulated in early 2008 remain relevant in 2009. They relate to the incorrect presentation of inventories, the lack of consistency and weak coordination between NATO bodies and the lack of attention to the detailed requirements of IPSAS. The implementation of IPSAS 17 on Property, Plant and Equipment in 2011, raising issues like definition and ownership of assets constitutes an additional challenge that needs to be properly and timely prepared (see Annex B Para 39).

CHAPTER 6

MATTERS RELATING TO THE BOARD

PERSONNEL MATTERS

6.1 The Board had its full complement of six serving members: France, Poland, Turkey, Spain, Germany and Portugal were represented on the Board for the whole of 2008.

6.2 In 2006, the Council approved two new auditor positions, augmenting the authorised establishment to 21 auditor posts, including one Principal Auditor, two Senior Auditors and 18 Auditors. One Senior Auditor left the Board in January 2008. A new auditor arrived in March 2008. At the end of 2008 there were two vacant auditor positions of which one was filled in March 2009 and another is expected to be filled in late spring 2009. Throughout 2008, the Board had an auditor vacancy of 1.1 staff years. In its recruitment, the Board strives for a proper geographical and gender balance. At the end of 2008, five of the twenty audit staff present were women. The Board Members and Auditors came from twelve nations. The Auditors came from ten nations.

6.3 The Board has 1 Administrative Officer and 7 Administrative Support Staff who perform a wide range of functions in support of the audits.

PERFORMANCE IN 2008 - THE BOARD AS A MODEL INTERNATIONAL AUDIT ORGANISATION

6.4 The fourth goal of the Board's 2005-2009 Strategic Plan aims at promoting the Board as a model international audit organisation. The publication of the Board's annual reports and annual NSIP reports on the internet are an opportunity for improving the external visibility of the Board. The Board decided not to carry out a new staff satisfaction survey in 2008 but to continue working on weak areas identified in the past, mainly training and communication. The Board also continued its monthly staff meetings and is stepping up its performance audit capacity in accordance with the 2008 Annual Performance Plan.

RISK BASED AUDIT PILOT AT NAMSA

6.5 The International Standard on Auditing (ISA) 315 and the supplementary guidance on public sector issues (ISSAI 1315) deal with the auditor's responsibility to identify and assess the risks of material misstatement of the financial statements, through understanding the entity's internal control. The standard requires the external auditor to put a greater focus on risk and controls in the audited entity through a better understanding of the entity, its processes and environment.

6.6 During 2008, the Board has laid the groundwork for a pilot risk based audit at NAMSA in compliance with that standard with the aim to improve the efficiency and effectiveness of its audits. It has organised information sessions and training for Board Members and Auditors and contracted a consultant to assist in the organisation of the audit

and the development of a methodology that could be extended to other NATO entities in the future. At the time of the preparation of this report (March 2009), the audit team had completed the first phase of the audit and anticipates completion, including evaluation of the pilot project before summer. The initial results look promising and indicate a potential for efficiency and effectiveness benefits, in addition to a better compliance with the auditing standards. The Board will evaluate the results of the pilot project in view to a possible extension of the approach to other entities.

TRAINING AND PROFESSIONAL DEVELOPMENT

6.7 In accordance with the auditing standards of INTOSAI and International Federation of Accountants (IFAC), the Board ensures that its audit and administrative staff receive adequate on-the-job training. The Board foresees an average of two weeks training for each auditor (one week shared training and one week individual training). It also draws on a detailed analysis of the individual training needs of the staff that are now updated annually as “personal development objectives” in NATO’s Performance Management system.

6.8 During 2008 the Board provided on average about 11 days of training per auditor. The annual common training covered workshops by external trainers concerning fraud awareness and audit, Performance auditing and the use of IDEA as fraud detection tool, process and controls based auditing, as well as internal training by the Board’s staff on performance auditing experiences and auditing IPSAS compliance. The Board’s staff attended user group sessions and seminars on TeamMate and IT audit, and participated in seminars and courses organised by NATO, their professional organisations or specialised training institutes.

RESOURCE ALLOCATION

6.9 Table 6.1 below shows the use of the Board's audit resources in 2008 and 2007.

**TABLE 6.1
ALLOCATION OF AUDIT RESOURCES
IN STAFF YEARS FOR 2008 and 2007**

| | Actual 2008 | Actual 2007 |
|---------------------------------------|------------------------|------------------------|
| NSIP Financial Audits | 2.4 | 2.3 |
| Agency Financial | 10.9 | 10.5 |
| Performance Audits | 2.2 | 2.2 |
| Studies | 0.6 | 1.3 |
| Training | 1.0 | 0.9 |
| Administration ⁵ | 1.5 | 0.6 |
| Board Support ⁶ | 1.3 | 1.3 |
| Sub-total | 19.9 | 19.1 |
| <i>Vacant positions</i> | 1.1 | 1.9 |
| Total authorised establishment | 21.0 | 21.0 |

DIRECT COST OF THE AUDIT

6.10 Table 6.2 below shows the allocation of the Board's audit resources and their cost in 2008.

**TABLE 6.2
DIRECT COST OF THE AUDIT IN 2008**

| Activity | Time Allocated (Staff days) | Direct Audit Cost (EUR million) |
|----------------------------------|--|--|
| Agency financial audit | 2,257 | 1.9 |
| NSIP financial audit | 491 | 0.4 |
| Performance audit | 456 | 0.3 |
| Other (Training, Board, studies) | 754 | 0.6 |
| Total | 3,958 | 3.2 |

6.11 The table at Annex D provides complete details of the audited amount, allocated resources and cost of the audit. This information on the size and the cost of the Board's audits has been compiled from different sources, including the Board's time recording system, and financial data on remuneration and travel provided by IS personnel and accounting services. It is important to note that the cost of the audit to NATO in 2008, EUR 3.3 million, is considerably less than the net return to NATO in pure monetary terms in the

⁵ The item "Administration" includes activities such as preparing travel, handling personnel matters, management reporting, performance management, sick leave and tasks that cannot be assigned to a specific audit.

⁶ The item "Board Support" covers the preparation of the Board's Activities Report, the Annual NSIP Report, and the Strategic Plan, attendance at Board Meetings and at meetings of NATO committees.

area of NSIP audits alone. Independent from the improvement in procedures and the assurance on the financial statements in the field of its agency audits, the Board's audits of NSIP projects in 2008 generated EUR 14.4 million net adjustments in favour of NATO.

ANNUAL MEETING WITH THE NATIONAL AUDIT BODIES

6.12 In accordance with the Council decision C-M(90)46, the competent national audit bodies have the opportunity to discuss the content of this annual report with the Board of Auditors. Para A.7. of the same document states that "the AGFC will take these comments into account, as appropriate, when reporting to the Council".

6.13 The 18th meeting to discuss the 2007 Annual Activity Report took place on 6th May 2008 under the chairmanship of Belgium. Representatives of twenty-two nations participated in the meeting, which was also attended by the Chairman and several national representatives of the AGFC.

6.14 On 2nd July 2007, the Board presented its 2007 annual report in the Council. The Chairman of the Board introduced the report and summarised the main achievements. The Chairman requested the Council's attention for four issues:

- The need to reconfirm the importance of IPSAS;
- Accountability in the NSIP, requiring the accelerated closure of old projects and timely inspection of currently completed projects;
- The status of Governance in NATO and the Board's intention to revisit the issue of the Council's delegation of budgetary authority; and
- The impact of increasing performance audit capacity and of audit requests by multi-nationally funded entities on the Board's resources.

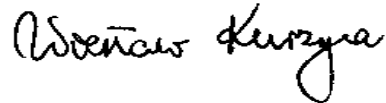
Permanent Representatives in the Council expressed strong appreciation for the Board's audit work. Coming back to the issue of delegated budget authority, the Council noted that the SRB would evaluate the arrangements in the following year.

INTERNATIONAL CO-OPERATION

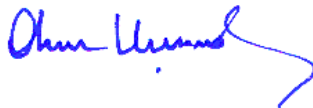
6.15 In line with Article 14 of its Charter, the Board continued to collaborate with the national audit bodies. In 2008, Board representatives met with Board Members and Staff of the Belgian Audit Court to discuss matters related to the audit of the New HQ Construction. A representative of the Board participated in the EUROSAI Congress that covered themes such as environmental audit, audit quality management and audit of education and social programs. The Board met with the President and high representatives from the Polish SAI, during its November 2008 planning meeting held in Warsaw. Board representatives also attended academic sessions commemorating the anniversaries of NPLOs.

6.16 The Board attempts through the activities such as described above to stay within the mainstream of the professional audit community. The Board believes that professional contact and interchange with other audit bodies and NATO organisations are important for maintaining a "state-of-the-art" international audit organisation, which is one of the aims of its 2005-2009 Strategic Plan.

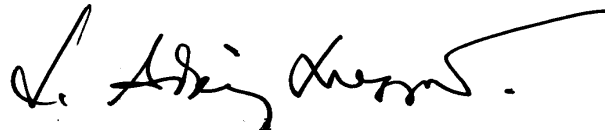
Approved by the Board on 30 April 2009



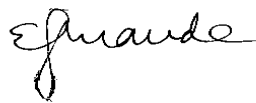
Chairman Wiesław Kurzyca (Poland)



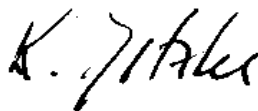
Board Member Okan Uçanok (Turkey)



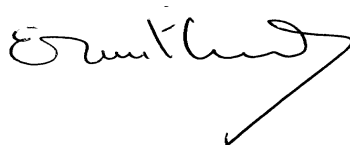
Board Member Hervé-Adrien Metzger (France)



Board Member Enrique Gómez de Aranda (Spain)



Board Member Klaus Getzke (Germany)



Board Member Ernesto da Cunha (Portugal)

**LIST OF REPORTS
RESULTING FROM AGENCY AUDITS**

| LIST OF REPORTS RESULTING FROM AGENCY AUDITS | | | |
|---|---------------------------------|--------------------|--|
| Subject | | Budget year | Reference of document and date |
| MILITARY COMMANDS | | | |
| 1. | ACO Group | 2007 | IBA-AR(2008)28, dated 12.12.2008 C-M(2009)0018 |
| 2. | ACT Group | 2007 | IBA-AR(2008)023, dated 28.11.2008 C-M(2009)0005 |
| 3. | ARRC | 2004-2006 | IBA-AR(2008)016, dated 26.09.2008 |
| 4. | CIMIC Group North (CCOE) | 2004-2006 | IBA-AR(2007)19, dated 25.04.2008 |
| 5. | NRDC ITALY | 2003-2005 | IBA-AR(2007)30, dated 29.02.2008 |
| 6. | NRDC TURKEY | 2003-2006 | IBA-AR(2007)29, dated 29.02.2008 |
| NPLOs | | | |
| 7. | BICES | 2006 | IBA-AR(2008)05, dated 29.02.2008 C-M(2008)0069 |
| 8. | CEPMA | 2006 | IBA-AR(2007)28, dated 25.04.2008 C-M(2008)0062 |
| 9. | NACMA | 2007 | IBA-AR(2008)025, dated 28.11.2008 |
| 10. | NAHEMA | 2006 | IBA-AR(2007)31, dated 29.02.2008 C-M(2008)0092 |
| 11. | NAHEMA | 2007 | IBA-AR(2008)30, dated 28.11.2008 |
| 12. | NAMEADMSA | 2007 | IBA-AR(2008)017, dated 26.09.2008 |
| 13. | NAMSA | 2007 | IBA-AR(2008)020, dated 08.09.2008 C-M(2009)0001 |
| 14. | NAPMA | 2007 | IBA-AR(2008)018, dated 30.01.2009 |
| 15. | NC3A | 2006 | IBA-AR(2008)06, dated 17.03.2008 C-M(2008)0056 |

| LIST OF REPORTS RESULTING FROM AGENCY AUDITS | | | |
|--|---|--------------------|---|
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| 19. | NHMO (HAWK) | 2006 | IBA-AR(2008)0009, dated 17.03.2008 C-M(2008)0074 |
| 20. | NHMO (HAWK) | 2007 | IBA-AR(2008)027, dated 12.12.2008 |
| 21. | RESEARCH & TECHNOLOGY ORGANISATION (RTO) | 2006 | IBA-AR(2008)004, dated 29.02.2008 C-M(2008)0048 |
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| 24. | AGS3 | 2006 | IBA-AR(2008)08, dated 30.05.2008 C-M(2009)0009 |
| 25. | IMS, NSA (INCL. PfP-MD) | 2006 | IBA-AR(2008)0002, dated 29.02.2008 C-M(2008)0035 |
| 26. | IMS, NSA (INCL. PfP-MD) | 2007 | IBA-AR(2008)022, dated 24.10.2008 C-M(2008)0115 |
| 27. | MSIAC | 2007 | IBA-AR(2008)021, dated 24.10.2008 |
| 28. | NAMFI | 2006 | IBA-AR(2007)27, dated 29.02.2008 |
| 29. | NAMFI | 2007 | IBA-AR(2008)026, dated 12.12.2008 |
| 30. | NATO DEFENCE COLLEGE (NDC) | 2006 | IBA-AR(2008)003, dated 29.02.2008 C-M(2008)020 |
| 31. | NATO PARLIAMENTARY ASSEMBLY (NPA) | 2007 | IBA-AR(2008)012, dated 25.04.2008 |
| 32. | NATO PENSION SCHEME | 2006 | IBA-AR(2008)001, dated 29.02.2008 C-M(2008)0038 |

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INTRODUCTION

After each audit, the Board issues an opinion on the financial statements. The phrase “the Board issued an "unqualified" opinion” is used whenever the Board issues an opinion that the financial statements are stated fairly and that the underlying transactions conform to the rules and regulations. A "qualified" opinion means that the Board was generally satisfied with the presentation of the financial statements but that some key elements of the statements were not fairly stated or affected by a scope limitation, or that the underlying transactions were not in conformity with budgetary authorisations and regulations. A "disclaimer" is issued when the audit scope is severely limited and the Board cannot express an opinion, or when there are material uncertainties affecting the financial statements. An "adverse" opinion is issued when the effect of an error or disagreement is so pervasive and material to the financial statements that the Board concludes that a qualification of the report is not adequate to disclose the misleading or incomplete nature of the financial statements.

In July 2002, the North Atlantic Council adopted the International Public Sector Accounting Standards (IPSAS), including the accrual and going concern assumptions, as the applicable accounting standards for NATO entities with effect from the 2006 financial statements. For the first time the Board has audited against IPSAS and accruals based accounting principles. This has in many cases lead to IPSAS related observations and restatement of financial statements as observed in the summaries below.

RESULTS OF AUDITS RELATING TO MILITARY COMMANDS

1. Allied Command Operations (ACO) – 2007

Introduction

In 2003, the NATO Command Structure was split in two at the strategic level: the Allied Command Operations (ACO) in Mons (BE), which has all operational responsibility and the Allied Command Transformation (ACT) in Norfolk (US) which has the responsibility to lead the military transformation of Alliance forces and capabilities. There are three main headquarters under ACO, Joint Force Command (JFC) Brunssum (NL), JFC Naples (IT) and Joint Command Lisbon (PO), and a number of subordinate commands and standing forces such as the NATO Airborne Early Warning Force (NAEWF). ACO presents consolidated financial statements incorporating the accounts and operations of these commands. The 2007 MBC funded budgets of ACO including credits carried forward from previous years amounted to EUR 965.6 million of which 954.4 million was committed and 768.8 million spent in 2007 (respectively EUR 950.8, 935.9 and 722.8 million in 2006). Expenditure against other sources of funding (Reimbursables, Trust Funds, NSIP, ...) amounted to an additional EUR 129 million in 2007.

Audit Highlights

The Board issued a qualified audit opinion on the 2007 financial statements for a limitation on the scope of the audit. This resulted from the fact that the Board has not been able to satisfy itself that inventories and expenses were accurately presented because inventory and expense data supplied by other NATO bodies were not always timely, accurate or complete.

The Board raised further observations and recommendations related to:

- Procurement risks and deficiencies at JFC Naples, KFOR and HQ ISAF;
- Instances of non-compliance with the NFR resulting from the “Global Funding” arrangements with NAMSA;
- Continuing weaknesses in the supervisory and internal controls and financial accounting and reporting systems of HQ ISAF;
- The need to strengthen internal controls on banking transaction at JFC Brunssum, JC Lisbon and CC AIR Izmir;
- The need to improve the follow-up of unpaid collection vouchers and the documentation of reimbursable expenditure at JFC Naples;
- Weak controls by the JFC Naples Personnel Office on the processing of Local Wage Rate payroll, entrusted to an external company;
- Overtime requirements granted and paid without prior approval at NHQ SKOPJE;
- Instances of non-compliance with the rules on write-off and disposal of assets at JFC Brunssum and NHQSa;
- Inadequate segregation of duties with the function of NAFS System Administrator at JFC Naples and KFOR;
- Issues regarding the pricing and valuation of assets at E-3A, JFC Brunssum and weaknesses in inventory management and control at HQ ISAF;
- Problems with expense recognition and accruals at E-3A and JFC Naples;
- Improvements needed to the presentation of the NSIP financial information in the ACO financial statements.

2. Allied Command Transformation (ACT) – 2007

Introduction

The Allied Command Transformation (ACT) in Norfolk (US) has the responsibility to lead the military transformation of Alliance forces and capabilities to improve the military effectiveness of the Alliance. The ACT group comprises HQ ACT in Norfolk (US), the NATO Undersea Research Centre in La Spezia (IT) (NURC), the Joint Warfare Centre in Stavanger (NO), the Joint Force Training Centre in Bydgoszcz (PL) and the Joint Analysis and Lessons Learned Centre in Lisbon (PO). The 2007 budgets of ACT, including credits brought forward from previous years, amounted to EUR 140 million of which 135 million was committed and 118 million spent in 2007 (respectively EUR 143, 141 and 115 million in 2006).

Audit Highlights

The Board issued a qualified opinion on the ACT 2007 consolidated financial statements due to a scope limitation, resulting from the fact that ACT did not perform an assessment to determine the adjustments, if any, that would have been necessary to properly account for IPSAS as of 1 January 2007. Therefore, the Board has not been able to provide full assurance that the 2007 expenses, and revenues, have been recorded in accordance with IPSAS.

The Board formulated further observations concerning:

- The need to improve and document the process for identifying and assessing contingent liabilities, and disclosure in the notes to the financial statements;
- The need to examine the necessity and usefulness of converting the Budget Execution expressed in non-EUR currencies into EUR;
- The need to more quickly identify any differences between calls for contributions and amounts received;
- The need for effective control over prepayments to staff members;
- Incomplete disclosure related to the correction of prior period errors in accordance with IPSAS 3;
- The need for continued improvement in the presentation of notes supporting the statements.

3. Allied Command Rapid Reaction Corps (ARRC) – 2004-2006

Introduction

HQ ARRC is a HRF(L) Headquarters in the NATO Force Structure. It is directly subordinated to Supreme Headquarters Allied Powers Europe (SHAPE) and is multinationally funded by fifteen nations. The Framework Nation (UK) is responsible for providing the command, communications, administration and logistical support. Expenditure in excess of these responsibilities is shared among the member nations in accordance with their share in the officer establishment. The 2004, 2005 and 2006 budgets of HQ ARRC including credits brought forward amounted to EUR 5.2, 4.7 and 2.0 million. Commitments were respectively EUR 4.7, 3.5 and 1.2 million and payments EUR 3.3, 2.7 and 0.9 million.

Audit Highlights

The Board issued unqualified opinions on the HQ ARRC's 2004 and 2005 financial statements. However, the Board issued a qualified opinion on the 2006 financial statements because the command had used shared funds for a purpose that was not authorised in the budget, the used amount was not clarified and had omitted the related transactions from the financial statements. The command had used funds of the participating nations to prefinance the purchase of a commemorative painting of the ISAF command during the HQ ARRC deployment in Afghanistan from April 2006 to February 2007.

In addition, the Board formulated observations concerning:

- Varying reporting formats and structure of the financial statements affecting their comparability over the years;
- Budget execution reporting inconsistent with the structure of the approved budget;
- Incomplete reporting of payments and receivables to and from nations and insufficient detail on credits carried forward and lapsed in the financial statements;
- Incorrect processing of lapsed credits leading to inconsistencies in the statements, and the creation of additional budget line items without proper authorisation;
- Lack of reconciliation and reporting of incorrect bank balances at year-end;
- Missing information on the refund to nations of 2003 lapsed credits and miscellaneous income and the need to pursue with nations outstanding calls for contributions;
- The need for adherence to appropriate budget control procedures and purchasing rules;
- Incompatibility between the duties of Fund Manager and Fiscal Officer in the Finance Department.

4. Civil Military Cooperation Group North Headquarters (CGN HQ) 2004-2005 and Civil-Military Cooperation Group North Centre of Excellence (CCOE) – 2006

Introduction

The Civil–Military Cooperation Group North Headquarters was established in 2003 to provide a framework for Civil-Military Cooperation (CIMIC) activities in order to support military missions, to enhance the effectiveness of military operations and to serve as an essential forum for CIMIC consultations. The headquarters was transformed into the CIMIC Centre of Excellence (CCOE) in 2006, and a new Memorandum of Understanding was signed in September 2006 by Denmark, Germany, The Netherlands and Poland. The CCOE is multi-nationally manned and funded. The 2004, 2005 and 2006 budgets of CCOE including credits brought forward amounted to EUR 1.3, 1.4 and 1.6 million. Commitments were respectively EUR 1.3, 1.3 and 1.3 million and payments EUR 1.0, 0.8 and 0.9 million.

Audit Highlights

The Board issued unqualified audit opinions on the financial statements of CGN HQ and CCOE for 2004, 2005 and 2006. The Board formulated observations on the presentation of the financial statement and on the level of cash holdings. It recommended that the Centre:

- Prepare a statement of financial position as part of its annual financial statements and revise the regulations to include this requirement;
- Duly sign and date the financial statements and check the amounts reported for consistency; consider measures to restrict treasury holdings in line with the provisions of Art. 13 of the NFR.

5. NATO Rapid Deployable Corps Italy – NRDC-IT 2003-2005

Introduction

The HQ NRDC-IT is a multi-national command responsible for establishing and maintaining a rapid deployment capability in support of the Council approved operations. It is part of the NATO Force Structure subordinate to Supreme Headquarters Allied Powers Europe (SHAPE) and is located in Solbiate Olona (IT). The NRDC-IT was established in 2002 and the related memorandum of understanding was signed by eleven NATO member nations, SHAPE and SACT. Two additional NATO nations joined in 2006-2007. The framework nation Italy bears the costs of operating and maintaining the Headquarter. Expenditure not funded by the framework nation, by individual participants or by NATO is shared by the member countries according to a pre-defined cost sharing formula based on the share of national officer establishment. The 2005 Budget including brought forward credits amounted to EUR 2.6 million; 2005 commitments were EUR 1.7 million and payments EUR 1.3 million (respectively EUR 3.3, 2.9 and 2.4 million in 2004 and EUR 2.5, 1.4 and 1.0 million in 2003).

Audit Highlights

The Board issued an unqualified opinion on the NRDC-IT financial statements for the years ended 31 December 2003, 2004 and 2005. The Board recommended that the command:

- Present complete financial statements including a formal statement of financial position and information on its cash flows;
- Update accounting procedures to clarify discrepancies between bank accounting records and bank certificates at year-end; and
- Properly document the provision of consultancy services before the start of the operational activity they were hired for.

6. NATO Rapid Deployable Corps Turkey – NRDC-T 2003-2006

Introduction

The HQ NRDC-T is a multi-national command responsible for establishing and maintaining a rapid deployment capability in support of the Council approved operations. It is part of the NATO Force Structure subordinate to Supreme Headquarters Allied Powers Europe (SHAPE) and is located in Istanbul (TU). The NRDC-T was established in 2002 and the related memorandum of understanding was signed by eleven NATO member nations, SHAPE and SACLANT. Three additional NATO nations joined in 2005. The framework nation Turkey bears the costs of operating and maintaining the Headquarter. Expenditure not funded by the framework nation, by individual participants or by NATO is shared by the member countries according to a pre-defined cost sharing formula based on the share of national officer establishment. The MOU of the HQ NRDC-T establishes that funds made available from NATO sources are requested and accounted for in accordance with the standard NATO procedures defined in the Allied Command Operations (ACO) Directives.

The administrative and financial management is carried out in accordance with the current NATO Financial Regulations and implementing procedures. The 2006 Budget including brought forward credits amounted to EUR 2.1 million; 2006 commitments were EUR 1.9 million and payments EUR 1.4 million (respectively EUR 1.9, 1.8 and 1.6 million in 2005, EUR 3.1, 1.9 and 1.8 million in 2004 and EUR 3.0, 2.3 and 1.8 million in 2003).

Audit Highlights

The Board issued an unqualified opinion on HQ NRDC-T financial statements for the years ended 31 December 2003, 2004, 2005 and 2006. It recommended that the HQ:

- Prepare a statement of financial position and a cash flow statement as part of its annual financial statements and revise the regulations to include this requirement;
- Clearly identify the final statements and submit these timely and duly signed and dated to the Senior Resource Committee and the International Board of Auditors for NATO;
- Address a number of operational weaknesses in the banking area; and
- Put in place and internal review activity in a number of important areas to ensure that basic controls are carried out adequately, as required by the NRDC-T financial regulations.

RESULTS OF AUDITS RELATING TO THE NATO PRODUCTION AND LOGISTICS ORGANISATIONS

7. NATO Battlefield Information Collection and Exploitation Systems (BICES) - 2006

Introduction

The BICES Organisation was established in 1999 with the objective of sharing and exchanging information between and among the participants, NATO and other nations and organisations, through the use of interoperable national and NATO support systems. The BICES Board of Directors is composed of representatives of each of the member nations and is responsible for the overall management of the organisation. The BICES Agency carries out the day-to-day management and NACMA provides administrative support. The BICES 2006 administrative budget including brought forward credits amounted to EUR 2.7 million, commitments were EUR 2.7 million and payments 2.6 million (respectively EUR 2.3, 2.3 and 2.2 million in 2005). Cumulative authorisations for (operational) Enhancement Projects amounted to EUR 4.6 million of which EUR 1.4 million was paid in 2006 (respectively EUR 4.1 and 1.7 million in 2005).

Audit Highlights

The Board issued an unqualified audit opinion on the BICES 2006 financial statements. The Board found that in one case, the limitation on overtime hours in the Civilian Personnel Regulations was not observed and recommended that the agency develop a policy to reduce overtime worked by individual members of the staff.

8. Central Europe Pipeline Management Organisation (CEPMO) – 2006

Introduction

CEPMO is mandated to manage the transport, storage, and delivery of petroleum products in Central Europe for military and non-military clients. For that purpose, CEPMO operates and maintains the Central Europe Pipeline System (CEPS), a system of pipelines, pump stations, input and delivery points, and depots on the territory of Belgium, France, Germany, Luxembourg and the Netherlands, the five host Nations. Canada and the United States were in 2006 the User Nations, with Canada departing from the CEPS on 31 December of that year. The CEPMO Board of Directors defines the general policy, missions, objectives and resources of the system. Tariffs, contracts and procedures to be applied are the joint responsibility of the Central Europe Pipeline Management Agency (CEPMA) and the National Organisations, within the guidelines provided by the CEPMO Board of Directors. The National Organisations are established by the Host Nations with Belgium acting on behalf of Luxembourg. The CEPMO budget for 2006 including commitments carried forward amounted to EUR 124.6 million, commitments amounted to EUR 121.2 million and payments to EUR 94.3 million (respectively EUR 117.3, 115.5 and 90.6 million in 2005).

Audit Highlights

The Board issued an unqualified opinion on the CEPMO 2006 restated financial statements of including CEPMA and the National Organisations. It raised observations related to the presentation of the financial statements, notably that:

- The CEPMA financial statements were submitted 2 months after the prescribed date of 30 September 2007;
- The agency did not adjust the 2006 opening balance of the statement of financial position for IPSAS;
- The inventory valuation methods adopted by BPO and DPO were not in line with the instructions of CEPMA that weighted average cost formulas should be used; documentary support for the stock data recorded by SNOI was lacking;
- FBG had not been able to reconcile the end international cash flow balance and the bank accounts balance because extra budgetary transactions had been processed in the bank accounts without being included in the Cash Flow Statement;
- The FBG statements contained errors that were subsequently corrected in the CEPMO financial statements;
- Lack of information made correct assessment of year-end accruals at BPO impossible.

In addition, the Board recommended that CEPMA pursue its efforts to resolve a long standing dispute with the French Authorities regarding the exemption of direct taxes on non-military operations of the pipeline system, and more recently, regarding a direct tax on the value of the CEPS buildings and installations not used exclusively for military requirements. It also recommended that BPO and the CEPMO BoD clarify the issue of contributions for military pensions charged to the CEPS budget.

9. NATO Air Command and Control System Management Organisation (NACMO) – 2007

Introduction

The Air Command and Control System Management Organisation (NACMO) has been established to plan, develop, co-ordinate and execute the programme for the implementation of the Air Command and Control System (ACCS). NACMA is the procurement and implementing agency and acts as host nation for the NATO Security Investment Programme (NSIP) projects assigned to it. NACMA reports to a Board of Directors representing the nations. It is located in Brussels and has an establishment of 113 posts. The NACMA 2007 financial statements consolidate the operations from both the administrative budget and NSIP accounts. The 2007 NSIP funded (operational) expenditures of NACMA amounted to EUR 86.6 million and the administrative budget including credits brought forward amounted to EUR 22.3 million, commitments to EUR 22.2 million and payments to EUR 19.2 million (in 2006 respectively EUR 33.4, 20.3, 20.0 and 17.7 million).

Audit Highlights

The Board issued an unqualified opinion on the NACMA 2007 financial statements. The Board noted that NACMA employs staff on successive contracts exceeding the 180 days limit set by the Civilian Personnel Regulations and recommended that NACMA obtain prior budgetary approval for such exceptions as required by the regulations.

- 10. NATO Helicopter D&D Production and Logistics Management Organisation (NAHEMO) – 2006**
- 11. NATO Helicopter D&D Production and Logistics Management Organisation (NAHEMO) – 2007**

Introduction

NAHEMO is the NATO Organisation responsible for the design, development, production and logistics support of a Tactical Transport Helicopter and a NATO Frigate Helicopter. NAHEMO consists of a Steering Committee and an agency NAHEMA, responsible for the daily management of the programme. The organisation was established by France, Germany, Italy and the Netherlands. Portugal joined the programme in 2001 and Belgium in 2007. Since 2004, NAHEMA also provides support in standardisation and interoperability to the Nordics Standard Helicopter Programme. The agency has an authorised staff of 51. In June 2000, the Participating Nations signed a Production Investment & Production Contract (PI&P) for the 1st Batch of 243 helicopters. Four aircraft manufacturers (Eurocopter, Agusta Space, Fokker Aircraft BV and Eurocopter Deutschland GmbH) act as Partner Companies for the development and production of the helicopter. NAHEMA's operational expenditure for 2006 and 2007 were EUR 439.7 and 477.9 million. The administrative budget amounted to EUR 8.5 million in 2006 and 9.2 million in 2007 and payments (respectively EUR 7.7 and 7.8 million).

Audit Highlights 2006

The Board issued an unqualified opinion on NAHEMA's 2006 restated financial statements. As a result of observations made during the audit, the agency had restated its accounts to correct two material errors. The first error occurred in the budget execution statements where commitments carried forward from previous years were merged with and disclosed as 2006 credits and in addition, commitments carried forward were based on the original 2005 financial statement figures, instead of the 2005 restated figures. A second error occurred in payables and unearned revenue because the agency, when correcting the 2005 statements had not amended all underlying accounting data and carried forward some erroneous figures into 2006. The reissued statements corrected these material issues.

The Board also noted instances where the presentation of the 2006 statements was not fully IPSAS compliant and recommended that NAHEMA when producing its 2007 financial statements address these issues.

Audit Highlights 2007

The Board issued an unqualified opinion on NAHEMA's 2007 restated financial statements. With the restatement NAHEMA corrected understated 2007 expenses resulting from overstatement errors with regard to the assessment of accruals that had remained in the system after the correction of 2005 accounts. The Board recommended that the agency take steps to ensure the availability of qualified staff to produce accurate financial statements; amend the accounting system as necessary to produce reliable accounting data, and to develop procedures to identify all 2005 partly paid invoices in order to correct future financial statements accordingly.

The Board also recommended that NAHEMA in agreement with individual nations rationalise old contribution payables and receivables so as to clear long outstanding historical positions and establish one amount owed to, or from, each nation to cover commitments in the next financial year. That position could then form the basis of future cash calls and contribute to a reduction in the excess cash held by the agency. NAHEMA should also complete its administrative budget execution statement to include the value of commitments carried forward that lapse at the end of the year.

12. NATO Medium Extended Air Defence System Design and Development, Production and Logistics Management Organisation (NAMEADSMO) – 2007

Introduction

NAMEADSMO was established in 1996 by Germany, Italy and the United States to manage the design and development of a Medium Extended Air Defence System (MEADS). MEADS is envisioned to be a tactical mobile and transportable air and missile defence system capable of countering air threats including cruise missiles and tactical ballistic missiles. The MEADS project will be designed, developed and built by private industry. The design and development phase is planned to continue through 2013. NAMEADSMO is based in Huntsville, Alabama, USA and has an authorised establishment of 110 staff. It is responsible for the day-to-day management of the programme. Authorisations for the operational budget including carried forwards in 2007 amounted to Equivalent US Dollar (EUSD) 597 (EUR 501) million, commitments were EUSD 555 (EUR 464) million and payments EUSD 391 (EUR 329) million. Authorisations for the administrative budget were EUSD 11 (EUR 9) million and commitments and payments EUSD 10 (EUR 8) million.

Audit Highlights

The Board issued an unqualified opinion on the NAMEADSMO restated 2007 financial statements. The agency restated the financial statements following an observation by the Board that the reporting on cross-border financing was not in compliance with the requirements of IPSAS. Cross-border financing is a procedure foreseen in the NAMEADSMO MOU and implies that when one nation has expended its annual financial limit, funds of another nation are budgeted to cover the remaining invoices. Such funds

provided by a particular nation will be rebalanced in the same currency. Cross borders financing was applied for the first time in 2007. The Board noted that the original financial statements did not properly report on EUR 56.5 million of cross-border financing 2007 because they improperly offset assets and liabilities, resulting in both Receivables from the receiving nation and Unearned Revenue for the providing nation being understated by that amount. The reissued statements corrected that material issue.

The Board noted several other reporting errors, though generally immaterial of disclosure in nature, and recommended that NAMEADSMA improve the preparation process and review of the financial statements. The Board also analysed a complaint regarding suspected impropriety in relation to the lease of a new vehicle and recommended that the Steering Committee perform the appropriate inquiries in order to determine the existence of any conflicts of interest surrounding that transaction. The Steering Committee has determined that the issue did not result in any conflict of interest and that no further investigation was warranted. The Board has noted that reply and took the position that, although it had not received an answer to all its questions, it has through the communication of the matter to the NAMEADSMO Steering Committee, complied with the requirements of the International Standard of Supreme Audit Institutions ISSAI 1260 Financial Audit Guideline – “Communication with those Charged with Governance” and International Auditing Standard 260, “Communication of Audit Matters with Those Charged with Governance”.

13. NATO Maintenance and Supply Organisation (NAMSO) – 2007

Introduction

The mission of the NATO Maintenance and Supply Organisation (NAMSO) and its executing agency, the NATO Maintenance and Supply Agency (NAMSA) is to provide logistic support services to NATO or to its member states individually or collectively. The objective of this mission is to maximise in peacetime and in wartime the effectiveness of logistics support to the armed forces of the NATO States and to minimise costs. In 2007, the agency's support and services extended to 19 Weapon System Partnerships, 5 Support Conferences, and several Sales Agreements and other partnership or subscription arrangements. The Agency oversaw the design and construction of a number of major infrastructure projects in Afghanistan, developed and implemented Integrated Logistic Support (ILS) solutions covering Real Life Support (RLS) and Airport of Debarcation (APOD) services. NAMSA's activities take place at three main locations: Capellen (Luxemburg) for most of the storage and maintenance works, Rueil-Malmaison (France) for the HAWK Logistics management, and Taranto (Italy) for the Southern Operational Centre. NAMSA has an establishment of about 974 staff. Budgetary expenditure in 2007 amounted to EUR 888 million. Accrual based expenses under IPSAS were EUR 970 million in 2007 (respectively EUR 776 million and 843 million in 2006).

Audit Highlights

The Board issued an unqualified opinion on NAMSA's 2007 financial statements. The Board also issued an unqualified opinion on the separate audit certificate covering NAMSA's administrative costs charged to the Military Budget Committee (MBC) funded programmes. Auditing that cost allocation is a special purpose assignment requested by the MBC. The Board formulated recommendations that NAMSA:

- Reconcile historic NADGE Stockage System (NSS) accounts to resolve discrepancies of some EUR 34 million between the NSS net equity accounts (nations' capital contributions to the programme), and the NSS inventory accounts;
- Require additional elements of proof to determine if a staff member actually "resides" in the country of service to avoid that expatriation and other allowances be unduly received;
- Work with E-3A to install an appropriate delivery reporting procedure to support accurate expense recognition in the financial statements;
- Adjust the opening balance and the comparative balances in the 2007 statements of financial position and financial performance to reflect that MBC funded inventories and PPE, were excluded from the NAMSA 2007 financial statements and included in the ACO 2007 statements;
- Apply proper segregation of duties in the process of verification and sending payments transactions files to banks;
- Include the inventory located in national depots in the financial statements since the common funded stock located in national depots is to be considered an asset to NAMSA;
- Update the NATO Logistics Stock Exchange (NLSE) system to enable customer account statement confirmation by year-end. For E-CAT1 business, payment to suppliers should be made dependent of the receipt of an invoice instead of shipping documents;
- Consistently apply depreciating an asset when it is available for use.

14. NATO Airborne Early Warning and Control Programme Management Organisation (NAPMO) – 2007

Introduction

NAPMO is responsible for the direction, co-ordination, and execution of the co-ordinated acquisition programme of the NATO Airborne Early Warning and Control (NAEW&C) system. The agency NAPMA oversees the execution of the programme for NAPMO. The US System Project Office (SPO) administers the main contract with a US contractor on behalf of NAPMA. The NAPMA agency has an authorised Peacetime Establishment of 133 personnel and is located in Brunssum (NL). The NAPMA expenditures in 2007 totalled the equivalent of USD 227 million, equalling EUR 155 million at NATO 2007 year-end rates (respectively equivalent USD 250 and EUR188 million in 2006).

Audit Highlights

The Board issued a qualified opinion on NAPMO's 2007 financial statements because of a scope limitation relating to the fact that the Board has not been able to satisfy itself that USD 24.1 million of additions to the Large Aircraft Infra-Red Counter Measures (LAIRCM) asset in progress in 2007 represented work undertaken by the US contractor relating to the LAIRCM programme. This is because the Board does not have access to the indirect contracting process that is used by the US Government to transform the invoices received from the US contractors into the U.S. Government billing statements that are then sent to NAPMA. As a result, the Board is not in the position to assess that this process is either reliable or results in billings that accurately represents work performed by the US contractors.

The Board recognises the efforts of NAPMA and the US authorities in responding to the Board's requests for additional evidence and the progress made in the current year, notably in relation to the USD 1.31 billion Mid-Term Modernisation Programme. It recommended that NAPMA and the US authorities continue their efforts to provide the Board with sufficient evidence to support the value of the work undertaken by US contractors.

The Board observed two other issues requiring management attention. These concern:

- The transfer of USD 7.2 million budget credits between parts of the programme without proper authority resulting in an overstatement of budget authorisations and an understatement of lapsed credits by that same amount. NAPMA informed the Board that it is in the process of obtaining the necessary approvals for these transfers from the nations;
- A change of accounting policy in connection with called contributions. In such cases when there is a change in accounting policy or the correction of a prior period error, IPSAS 3 requires that prior year comparative figures be restated to achieve inter-period comparability of financial information.

The report is currently (March 2009) at formal clearance stage with the NAPMO Board of Directors.

15. NATO Consultation, Command and Control Agency (NC3A) – 2006

16. NATO Consultation, Command and Control Agency (NC3A) – 2007

Introduction

The NC3A supports NATO with advice, research and development of consultation, command and control systems. As from 1 January 2000, the NC3A has been operating under a customer-funding regime. Under this regime the major NATO commands request in their budget funds for NC3A services and directly pay NC3A for those services. The Infrastructure Committee pays NC3A directly for host nation services whether for projects (100% funded) or for the administration of projects (project service costs negotiated with NC3A on a fixed price basis). External customers also pay for services on a price negotiated with NC3A and for acquisitions on a 100% refundable basis. NC3A 2007

expenditure amounted to EUR 331 million, of which 58.6% was for NSIP projects, 13.1% for acquisitions for third parties (TP) (100% reimbursable), 26.9% on customer funding i.e. the administration of projects, acquisitions and scientific work for NATO bodies and external customers, and 1.4% on the ALTBMD programme. The 2006 expenditure amounted to EUR 244 million, of which 65% was for NSIP, 15% for acquisitions for TP, 19% on customer funding and 1% on the ALTBMD programme.

Audit Highlights 2006

The Board issued an unqualified opinion on the NC3A 2006 financial statements. It recommended that the agency:

- Assess at year-end, on a project by project basis, the expenditures to be accrued, in particular for NSIP/TP acquisition projects;
- For fixed price contracts, determine revenue to be recognised in the financial year in function of the stage of completion of the project in compliance with IPSAS 11. The methods for determining the percentage of completion should be clearly documented and disclosed in the financial statements;
- Disclose all the segment financial information concerning its NSIP & TP acquisitions activities (revenue, expenses);
- Implement a system allowing foreign currency transactions to be recognized at the date of transaction in compliance with IPSAS 4 requirements;
- Keep an appropriate audit trail of the internal controls made in the area of Time Accounting System transfer of data from the project management software (EPM) to the accounting software (CFS). In addition, a system report should be developed to allow monthly reconciliation between the number of billable hours in the two systems and a list of discrepancies on a project by project basis;
- Implement the Account Receivable package within the financial system in order to have information of the balance due by each customer automatically available.

Audit Highlights 2007

The Board issued an unqualified opinion on the NC3A 2007 financial statements. It recommended that the agency:

- Ensure that short-term investments are included in its Cash Flow Statement;
- Disclose complete information in the notes to the financial statements. In the notes, NC3A stated that it had decided to establish compliance with IPSAS 17 as of 2006 for newly acquired assets and to use the transition period to bring historical records into line. The agency did not follow that approach for PPE purchased on projects funded by customers, but intended to remain NC3A property;
- Comply with the requirement of IPSAS 3 and disclose the effect of changes in accounting treatment on the comparative information;
- Ensure that the liabilities and assets are not offset. NC3A had improperly offset liabilities against receivable from sponsors and assets against advance from customers which distorted the Statement of Financial Position and limited its usefulness in providing a fair and accurate picture of the NC3A's financial position;
- Comply with the Civilian Personnel Regulations in respect of the employment of

temporary staff and, to be more transparent, obtain prior approval from the MBC, through their approval of the SPIE, when temporary staff are to be employed for periods exceeding 180 days;

- Continue to improve its system for recognition of expenditures to be accrued at year-end in the NSIP area;
- Complete the verification of its Third Parties advance from customers' accounts in order to validate the year-end balances, including appropriate confirmation with the customers.

17. NATO CIS Services Agency (NCSA) – 2006

Introduction

The re-alignment of the strategic commands required a detailed revision of tasks and responsibilities. This included adapting and re-assigning the roles of the C3 capability system and service management and the transformation of the existing NATO Communication and Information System (CIS) Operating and Support Agency (NACOSA) into the new NATO CIS Services Agency (NCSA) which aims at integrating NATO's fragmented CIS service provision into one centralised organisation. NCSA was activated in November 2004 along with the new Peacetime Establishment implementation and the transfer of staff from NACOSA to NCSA. The NCSA 2006 administrative budget including credits brought forward was EUR 56 million, commitments were EUR 56 and payments 47 million. The CIS budgets delegated to NCSA in 2006 were EUR 114 million, commitments were EUR 111 and payments EUR 68 million.

Audit Highlights

The Board issued a qualified opinion on the NCSA 2006 financial statements because NCSA:

- Had not adjusted the 2006 Opening Statement of Financial Position to take account of the adoption of IPSAS as of 1 January 2006;
- Did not report the CIS inventories held for ACO. In fact, as it was not clear at the time of the audit which organisation should present these inventories, neither NCSA nor ACO disclosed them. The Board recommended that the entities involved ensure that the accounting for inventories provides reliable balances and that they are presented in a consistent way throughout NATO and in accordance with IPSAS;
- records payments for NAMSAs Administrative Expenses as expenses although they are in fact pre-payments, and should be reported as such until it is determined that NAMSAs effectively incurred expenses against these funds. The Board recommended that NCSA obtain in a timely manner from NAMSAs a statement of the situation at year-end in order to accurately assess the level of expenses incurred in a particular year;
- NCSA expenses and revenues were understated by EUR 4.2 million in 2006 due to the improper cut-off of expenses in accordance with accrual accounting principles at year-end.

In addition to the qualification issues outlined above, the Board raised further observations as follows:

- The “Global Funding” (GF) allows the carry forward without legal liability, of credits made available to NAMSA. Such credits should be lapsed in accordance with the NATO Financial Regulations (NFR). The Board recommended to improve GF procedures in line with NFR and IPSAS and that budgetary transparency be increased in that respect;
- The Board recommended that NCSA organise an internal audit on a regular basis;
- The NCSA Unearned Revenue balance at 31 December 2006 does not include the carry forward and lapses of 2005 that were reported by ACO. The Board recommended that NCSA report the unearned revenue relating to the year 2005;
- The Board recommended that NCSA disclose the Reimbursable Budgets Execution Statements in the financial statements;
- The Board observed that the presentation only of an ending cash balance does not provide full visibility on activities carried out in the US and recommended that in addition to the end balance all revenues and expenses be reflected in the financial statements.

18. NATO Multi-Role Combat Aircraft (MRCA) Development Production and In-service Support Management Organisation (NAMMO), NATO European Fighter Aircraft Development, Production and Logistic Management Organisation (NEFMO), and NATO EF 2000 and TORNADO Development Production and Logistics Management Agency (NETMA) – 2006

Introduction

NAMMO and NEFMO are the two organisations responsible for the development, production and in-service support of the Tornado and Eurofighter 2000 aircraft programmes. They are the two largest single NATO programmes. The participating nations for the Tornado programme are Germany, Italy and the United Kingdom. Spain joins these three nations in the Eurofighter programme. They are represented in a Joint Steering Committee, which exercises supervision over both programmes, and in a Board of Directors specific to each organisation. The NETMA agency is located in Munich and supports the two programmes. It had an authorised establishment of 303 staff in 2006. Authorisations for the 2006 administrative budget including carry forward amounted to EUR 50.2 million; commitments were EUR 50.2 and payments 46.7 million (respectively EUR 47.1, 47.1 and 43.4 million in 2005). The NAMMO 2006 operational budget amounted EUR 708.4 million and payments were 609.8 million (respectively EUR 899 and 766.4 million in 2005). The NEFMO operational budget was EUR 4,679.5 million and payments were EUR 4,485.1 million (respectively EUR 5,460.8 and 5,157 million in 2005).

Audit Highlights

The Board issued unqualified audit opinions on the financial statements of NAMMO, NEFMO and NETMA for 2006. The Board raised observations on the following topics:

- NEFMO issued its final statements on 24 August 2007 after refinement work to its 2006 opening and year-end accrual balances. That additional work resulted in an amount materially consistent with the amount used to determine 2006 expenses and no restatement of the accounts was necessary. The Board recommended that NETMA continue to review and refine its methodology for estimating the value of long term contracts, including seeking written confirmation from industry of the amounts involved;
- A payment in May 2006 made under the Development Cost Plan included an amount of GBP 18.6 million which seemed not to be directly related to the international programme but to a separate agreement between one nation and the industry. The Board recommended that NETMA seek clarification from the nation MOD regarding the impact of this on the Development Cost Plan Limit of Liability, and confirmation of whether future payments will be, or have been, abated on account of this payment;
- An amount of EUR 924,466 had been recorded twice, correctly as a payable to nation and incorrectly as an account payable to vendors, with the result that NEFMO Statement of Position for Payables to Vendors is overstated. The Board recommended to correct the accounting records;
- Due to the complexity of the foreign exchange gains and losses within the financial system, the Board was unable to provide assurance on the net foreign exchange rate loss of EUR 4,879,473. The Board recommended that NETMA ensure that amounts recorded as foreign gains and losses are fully supported and justified. In addition, NETMA should develop a methodology to support audit verification in preparation for the 2007 audit, and consider booking gains and losses to the separate income and expenses GL codes within the financial system;
- The notes to the NAMMO financial statements disclose an unreconciled difference between (accruals based) expenses in the statement of financial performance and the (cash based) payments in the budgetary statement of around EUR 2.4 million. That difference is linked to the way the figures are obtained from the financial system; in the first case from a trial balance report produced from the general ledger, and in the second case from a specially designed SQL report. The Board recommended that NETMA reconcile the figures, resolve the discrepancy with corrected figures and provide a detailed explanation in the NAMMO 2007 financial statements and analyse and correct the accounting system to ensure that, in the future, all figures in the financial statements can be reconciled to each other to the general ledger. This also applies to the NEFMO and NETMA financial statements;
- The Board noted that some bank balances on the NAMMO and NEFMO statement of financial position were not converted at year-end, corporate rate resulting in overstated/understated balances and understated/overstated gains/losses on exchange by EUR 0.6 and 0.1 million. The Board recommended that the year-end corporate exchange rate be used to convert non-EUR currency cash balances, and that the gains and losses of exchange are properly identified and accounted for;
- NETMA did not properly accrue for goods and services received but not invoiced at year end. The identified immaterial discrepancy of EUR 58,899.58 resulted in a very small understatement of liabilities on the Statement of Financial Position. The Board recommended that NETMA initiate procedures to more accurately record accruals at year-end;
- The NETMA management information system does not allocate unique serial

numbers to supplier invoices and each section allocates their own invoice number manually which is a potential source of confusion and error. The Board recommended that NETMA investigate the possibility of allocating a unique serial number to each supplier invoice as they are entered into the system;

- NETMA, in the Comparison of Budget to Actual, shows Miscellaneous Income to reduce budgetary payments. However, miscellaneous income does not result in reduced budgetary payments but it only affects how those budgetary payments were funded and should be removed from future comparisons;
- The NETMA Administrative Budget is understated by EUR 1 million because a transfer from the NEFMO budget had not been formally recorded. The Board recommended that NETMA regularise the position by completing the transfer;
- There were discrepancies between basic salary amounts in the financial system payroll module, individual pay statements and the financial system general ledger for March 2006. Most of these differences were ultimately explained and corrected. The Board recommended that NETMA establish a formal monthly reconciliation procedure for payroll data.

19. NATO HAWK Production and Logistics Organisation (NHPL0) - 2006

20. NATO HAWK Production and Logistics Organisation (NHPL0) - 2007

Introduction

The NATO HAWK Production and Logistics Organisation (NHPL0) was established to provide its member countries with the HAWK weapon system. The executive body is the NATO HAWK Management Office (NHMO) which has an authorised establishment of twenty-five staff. Since 1995, only two countries, France and Italy, are members of the agency. The only operational programme active is the Logistics Programme since the completion of the Viability and AN/TSQ-73 Upgrade and Support programmes in 2005, although their financial liquidation is not yet finalised. In December 2007 the Board of Directors noted France's decision to withdraw from the Organization as from 31 December 2009. The NHPL0 Charter requires that the member states submit the request for dissolution to the Council. In May 2008 the BoD decided on the creation of a liquidation cell for the financial reconciliation activities after the closure of the Agency. The 2007 administrative budget authorisation including carry forward amounted to EUR 4 million; commitments were EUR 3.7 and payments 3.4 million (respectively EUR 4.1, 3.8 and 3.4 million in 2006, and EUR 4.1, 3.9 and 3.3 million in 2005). The 2007 operational budget authorisation amounted to EUR 13.2 million, commitments were EUR 10.8 million and payments 4.5 million (in 2006 respectively EUR 11.6, 10.5 and 3.1 million). Operational expenditure in 2005 was EUR 6.4 million.

Audit Highlights 2006

The Board issued an unqualified opinion on the NHPL0 2006 restated financial statements. The restatement corrected a number of material errors in the accounts identified during the audit. They related to:

- EUR 6 million contributions from nations that were recorded when called, rather than when the budget is expended. That method of recording revenue is not IPSAS

- compliant; and
- In relation herewith the booking of a “Payable to Suppliers” reflecting the unexpended portion of the 2006 budget, which should have been booked as a liability towards nations under “Unearned Revenue”;
- An overstatement of the Cash Flow Statement by EUR 4,4 million resulting from internal transfers and regularisations between accounts that do not represent any net changes in the Agency cash and cash equivalents situation from its operating activities.

The Board further observed bank accounts for EUR 0.7 million and transactions against these accounts to finance activities outside the normal programme and budgets that were not reflected in the financial statements. It also noted several minor errors and inconsistencies in the statements.

Audit Highlights 2007

The Board issued an unqualified opinion on the NHPLO 2007 financial statements. It recommended that the agency adjusts the accounts to achieve a clean 2008 opening balance in relation with overstated “Receivables” by EUR 170,000 due to the improper imputation of a call for funds to receivables instead of to excess funds from one nation; and EUR 0.9 million funds received in 2007 for 2008 calls incorrectly booked as “Excess Funds” instead of as “Deferred Income”. The Board also observed minor inconsistencies in the notes and the omission of the disclosure of an event after the reporting date.

21. Research and Technology Organisation (RTO) – 2006

22. Research and Technology Organisation (RTO) – 2007

Introduction

The NATO Research & Technology Organisation (RTO) is a NATO subsidiary body created within the framework of the North Atlantic Treaty. Its mission is to conduct and promote co-operative research and information exchange, to support the development of national defence research and technology, to maintain a technology lead, and to advise NATO decision-makers. The costs of RTO’s activities are mainly supported directly by the Nations. RTO’s support element RTA is funded jointly by MBC and CBC. Total 2007 authorisations including carry forward amounted to EUR 6.2 million, commitments were EUR 6.1 and payments 5.4 million (respectively EUR 6.7, 6.6 and 5.4 million in 2006 and EUR 6.8, 6.7 and 5.8 million in 2005).

Audit Highlights 2006

The Board issued an unqualified opinion on the RTO 2006 restated financial statements. The Board had raised several IPSAS related observations that were resolved with the restatement, namely that RTO had:

- Omitted to adjust its 2006 opening Statement of Financial Position for IPSAS;
- Correctly reported the unearned revenue balance relating to 2006 but omitted to include the 2005 carry forward and lapses into 2007 of EUR 0,3 million funds

- received in 2005;
- Understated revenue by EUR 0.7 million, representing expenditure in 2006 against 2004 and 2005 credits brought forward.

Audit Highlights 2007

The Board issued an unqualified opinion on the RTO 2007 financial statements. The Board raised observations concerning:

- Errors in the assessment of accruals in 2006 and 2007, resulting in expenses understated by EUR 120,000 and accounts payable understated by EUR 170,000 and carry forward overstated by EUR 130,000. The Board recommended that goods and services that have been received should be accrued in the year the goods and services are rendered, and that only amounts for which goods and services have not been received, and for which a legal liability exists, should be carried forward;
- The Board also recommended that, for a correct assessment of the accruals, the actual receipt date of goods/services be entered into the accounting system, instead of using the system default date.

RESULTS OF AUDITS RELATING TO THE CIVIL AND MILITARY AGENCIES AND OTHER ORGANISATIONS

23. AFNORTH International School – 2006-2008

Introduction

The AFNORTH International School (Brunssum, NL) provides schooling for the children of entitled staff working in the NATO community. The school comprises four independent units funded by the four founding nations of Canada, Germany, United Kingdom and the United States. Each nation supports their own education unit but many programmes and activities are common and support the cultural exchange of the children of the different nations. While each nation finances its own educational unit, some expenditure is common funded. This common funded budget is the subject of this audit. For school year 2006-2007, budget and commitments amounted to EUR 4.4 million and payments to EUR 3.8 million. In 2007-2008, budget and commitments were EUR 4.5 million and payments EUR 3.9 million. In 2008 the School population was 1,095 students.

Audit Highlights

The Board issued an unqualified audit opinion on the financial statements of the AFNORTH International School for the school years ended 31 July 2007 and 31 July 2008.

The Board recommended that the AFNORTH International School adopt written financial rules, procedures and policies to address a number of financial and budgetary issues. These issues relate to the formal consideration of the financial statements by the Board of Governors, the improvement of budgetary control at line item level, regulating the investment of funds by the School's management and the resolution of a number of malpractices such as retaining of unused budgetary credits and the performance of out-of-budget transactions.

24. Alliance Ground Surveillance Programme (AGS3) – 2006

Introduction

The objective of the Alliance Ground Surveillance (AGS) Programme is to provide the Alliance with a NATO owned and operated AGS core capability. The AGS Capability Steering Committee supported by the AGS Support Staff (AGS3) was established by the Conference of National Directors to initiate the AGS Programme. The costs of the AGS3 administrative budget are covered by successive funding arrangements between the participating Nations. Since 2002, the NATO Financial Controller of the International Staff is responsible for the financial management of the AGS3 budgets. The 2006 AGS3 administrative budget including credits brought forward from 2005 amounted to EUR 3.5 million, of which EUR 3.5 million were committed and EUR 1.9 million were expended. The difference of EUR 1.6 million was brought forward into the 2007 AGS3 budget. The respective sums for the 2005 AGS3 budget were budget credits of EUR 2.1 million and

EUR 1.4 million expenditure; the difference of EUR 0.7 million was brought forward into the 2006 administrative AGS3 budget.

Audit Highlights

The Board issued a qualified opinion on the 2006 financial statements for lack of compliance with International Public Sector Accounting Standards (IPSAS) in the area of recognition of expenses. The expenses have been presented in the Statements of Financial Performance based on budgetary commitments. That approach, in material instances, did not produce accurate expenses in accordance with the accrual basis of accounting under IPSAS. The Board also observed other instances of non-compliance with IPSAS, such as the improper classification of liabilities, offsetting of assets and liabilities, inconsistencies between various statements, inclusion of non-cash transactions in the Cash Flow Statement and the insufficient disclosure of a contingent liability. The Board also recommended that the IS and AGS3 work with the nations concerned to resolve the issue of significant outstanding contributions.

- 25. International Military Staff Budget Group, including the International Military Staff (IMS), the NATO Standardisation Agency (NSA), the IMS GroupPartnership for Peace (PfP) and the Mediterranean Dialogue (MD) – 2006**
- 26. International Military Staff Budget Group, including the International Military Staff (IMS), the NATO Standardisation Agency (NSA), the IMS GroupPartnership for Peace (PfP) and the Mediterranean Dialogue (MD) – 2007**

Introduction

The IMS supports the Military Committee. It is tasked with ensuring that the policies and decisions of the MC are implemented as directed. The IMS also prepares plans, initiates studies and recommends policies on matters of a military nature. IMS centralises PfP Activities for all the agencies funded under the IMS budget group (IMS, NSA, NATO Defence College (NDC), and the Research and Technology Organisation (RTO)) and the NATO C3 Agency. It also centralises MD activities of IMS and NDC together with the Allied Command Operations and Allied Command Transformation. NSA is a single, integrated body, composed of Military and Civilian staff headed by a Director. Its mission is to initiate, co-ordinate, support and administer standardisation activities conducted under the authority of the NATO Committee for Standardisation. The 2006 authorisation for the IMS budget group including carry forward amount to EUR 26.1 million, commitments were EUR 25.9 and payments 22.9 million. The 2007 authorisation for the IMS budget group including carry forward amount to EUR 25.8 million, commitments were EUR 25.8 and payments 21.9 million (respectively EUR 26.1, 26.0 and 21.7 million in 2005).

Audit Highlights 2006

The Board issued an unqualified opinion on the IMS Budget Group's 2006 restated financial statements including IMS, NSA, PfP and MD. The restatement addressed a

number of IPSAS related observations identified by the Board, namely that the IMS:

- Had omitted to adjust the opening balances of the Statement of Financial Position to take into account the adoption of IPSAS as of 1 January 2006;
- Had correctly included the carry forward 2006 and advance contributions 2007 in the unearned revenue as of year-end 2006, but omitted to include the 2005 carry forward and lapses into 2007 of EUR 0,5 million, funds which were received in 2005;
- Understated revenue by EUR 4.2 million, representing expenditure in 2006 against 2004 and 2005 credits brought forward.

Audit Highlights 2007

The Board issued an unqualified opinion on the financial statements of the IMS Budget Group including IMS, NSA, PfP and MD for 2007. The Board raised no observations.

27. Munitions Safety Information Analysis Centre (MSIAC) – 2007

Introduction

The Munitions Safety Information Analysis Centre (MSIAC) provides a focal point within NATO to assist national and NATO Munitions development and logistics programmes in addressing the problems associated with achieving Munitions Safety. At the end of 2007 there were 12 MSIAC member countries including three non-NATO members. The staff was composed of 8 persons. The MSIAC 2007 budget authorisations including credits brought forward were EUR 1.7 million, commitments were 1.4 million and payments 1.3 million (respectively EUR 1.7, 1.3, and 1.2 million in 2006). The International Staff Financial Controller provides the accounting services and issues the financial statements for MSIAC.

Audit Highlights

The Board issued an unqualified opinion on the MSIAC 2007 restated financial statements. MSIAC restated the accounts to correct errors in the presentation of comparative information in respect of financial year 2006 and overstatements of EUR 0.5 million in Contribution Receivables and Unearned Revenue.

The Board also observed that the Statements of Financial Position and of Budget Execution had been overstated because educational expenditure of EUR 12,350 relating to a 24 month period had been booked entirely to 2007. It recommended that expenditures be well analysed and based on the accrual principle, and be charged to the financial year in which they are incurred.

28. NATO Missile Firing Installation (NAMFI) - 2006

29. NATO Missile Firing Installation (NAMFI) - 2007

Introduction

NAMFI was established in 1964 by a number of user nations to facilitate the practice firing of missile weapon systems such as HAWK and Patriot. In 2005 there were four User Nations: Belgium, Germany, Greece and the Netherlands. They are represented in the User Nations Committee (UNAC). Greece is also host nation for NATO funded infrastructure. Other nations use the NAMFI installations on a cost reimbursable basis. NAMFI is located in Greece, on the island of Crete. Authorisations for 2007 amounted to EUR 14.2 million, commitments were EUR 12.8 and payments 9.8 million. Authorisations for 2006 amounted to EUR 13.6 million, commitments were EUR 12.1 and payments 9.9 million. Residual payments on the Dornier Target Services contract that expired in 2004 were EUR 3.4 million in 2006.

Audit Highlights 2006

The Board issued an unqualified audit opinion on the NAMFI 2006 financial statements. It formulated some recommendations to improve the financial statements, namely that NAMFI:

- Include a cash flow statement from its 2008 financial statements onwards; and
- Streamline the presentation of its financial statements from its 2008 financial statements onwards, to improve their understandability. This can be achieved by preparing a statement of budget execution, a consolidated balance sheet, the list of incomes from use of facilities and a cash flow statement. The notes would explain and cross refer to the numbers in the main statements in detail and contain all other information required by the financial regulations, as well as a narrative explaining NAMFI's accounting policies.

Audit Highlights 2007

The Board issued an unqualified audit opinion on the NAMFI 2007 financial statements. It formulated observations and recommendations about:

- A minor discrepancy on the list of incomes from use of facilities and the supporting details. That difference was explained subsequent to the audit. The Board recommended that the agency ensure that in future such discrepancies are fully reconciled;
- The detail provided on the write off of property in the financial statements that counted 29 pages in 2007 financial statements. The Board recommended that NAMFI summarise that information in its financial statement in future in order to comply with generally accepted norms for presentation in NATO.

30. NATO Defence College (NDC) – 2006

Introduction

The mission of NDC is to contribute to the effectiveness and cohesion of the Alliance through training, research and outreach programmes for officers and officials selected for important NATO appointments, and to disseminate awareness of NATO initiatives and interests. NDC is located in Rome and has an establishment of 49 NATO staff. NDC 2006 authorisations including carried forward amounted to EUR 6.4 million; commitments were EUR 6.4 and payments 6.1 million (respectively EUR 6.2, 6.2 and 5.5 million in 2005).

Audit Highlights

The Board issued an unqualified opinion on the NDC 2006 restated financial statements. The restatement addressed several IPSAS related observations, namely that the NDC:

- Had omitted to adjust the opening balances of the Statement of Financial Position to take into account the adoption of IPSAS as of 1 January 2006;
- Had correctly assessed its unearned revenue for 2006, but had omitted to adjust the unearned revenue of EUR 0.6 million against 2005 and 2004 carry forward.

The Board also observed that NDC had not disclosed a contingent liability of EUR 50,000 that was known at the time of issuing the restated financial statements.

31. NATO Parliamentary Assembly (NATO PA) – 2007

Introduction

Since 1955, the NATO PA, formerly the North Atlantic Assembly (NAA), has been a forum for legislators from member countries of the North Atlantic Alliance. The work of the NATO PA is mainly financed by contributions from member countries, based on the sharing key used for the NATO civil budget. NATO and other organisations also provide the Assembly with additional subsidies that may be designated to be spent on specific activities. The NATO PA is independent of NATO and the Board carries out the audit with the authorisation of the Council. It has a staff of some 30 employees. The NATO PA 2007 budget amounted to EUR 3.6 million and expenditure to EUR 3.5 million (EUR 3.6 and 3.5 million in 2006). The assets of the NATO PA Provident Fund as at 31 December 2007 amounted to EUR 4.6 million (EUR 4.3 million in 2006).

Audit Highlights

The Board issued unqualified opinions on the financial statements of the NATO PA and the NATO PA Provident Fund for 2007. It had no observations.

32. NATO Pension Scheme – 2006

Introduction

The NATO Pension Scheme applies to all staff recruited between 1st July 1974 and 30th June 2005. The members of staff recruited prior to July 1974 are members of the Provident Fund. The staff members recruited after 1st July 2005 are members of the Defined Contribution Pension Scheme. The NATO Pension Scheme is a 'defined benefit plan'. It defines rights to either a leaving allowance or a pension and includes provisions for invalidity, survivor's, orphan's and dependant's pensions. The Scheme is unfunded. Benefits are paid from annual budgets financed by the nations and by a contribution from staff which in 2006 was 8.9% of their salary. On a long term actuarial basis, staff contributions are intended to finance one-third of the costs of the Pension Scheme. In 2006, the Pension Scheme supported 2,459 pensioners, and over 4,300 staff paid into the scheme. Total payments made under the Scheme for 2006 amounted to EUR 90 million (EUR 84.6 million in 2005).

Audit Highlights

The Board issued an unqualified opinion on the financial statements of the Pension Scheme for the year ended 31 December 2006. The Board recommended that the Pension Scheme management improve the presentation of the financial statements in line with International Accounting Standards 26, awaiting the issuance of an IPSAS specific standard on employee benefits. It also recommended that the date of actuarial valuation be disclosed in the financial statements and that management complies with the requirements of IPSAS concerning accruals and the disclosure of provisions.

33. NATO Provident Fund – 2006

Introduction

The NATO Provident Fund provides retirement benefits to civilian staff who joined NATO before 1 July 1974, and who are not members of the NATO Pension Scheme. The Fund invests the retirement contributions (7% of the basic salary from members and 14% from NATO) using the services of an investment banker. The International Staff carries out the day to day accounting of the Fund since 2005 when it took over from ACO Treasury. The value of the Fund's assets at 31 December 2006 was EUR 81 million (EUR 98.6 million in 2004). As at 31 December 2006, there were 216 members contributing to the Fund (263 members in 2005).

Audit Highlights

The Board issued an unqualified opinion on the Provident Fund's 2006 financial statements. It raised observations as follows:

- The interest allocated to participants exceeded actual investment gains and losses for the year by EUR 0.6 million. The Board recommended that the IS investigate whether excess payments have been made to participants as a result of this;
- The Fund's financial statements do not present financial information in a clear and efficient manner. The Board recommended that the Fund improve the presentation of the financial statements in line with International Accounting Standard 26, awaiting the issuance of an IPSAS specific standard on employee benefits;
- The Board recommended that the Fund in line with IAS 26 record retirement plan investments at fair value in the statement of net assets available for benefits and account for any resulting unrealised gains and losses in the statement of changes in net assets available for benefits;
- The accounting system which manages the fund and produces the financial statements consists only of a series of spreadsheet tables, which have very few built-in controls. The Board recommended that a formal accounting package be used to record the activities of the fund;
- Interest to be received on the purchase of bonds should be booked as an asset "Interest Receivable", not as an expense converted into income on receipt of the interest amount.

34. New NATO Headquarters – 2007

Introduction

At the Washington Summit, in April 1999, the Heads of State and Governments of NATO countries formally decided to build a new Headquarters in Brussels to meet the Alliance's needs in the twenty-first century. The North Atlantic Council, upon recommendation of the Civil Budget Committee, approves the budget for the new NATO Headquarters which is funded from national contributions based on a specific cost-share agreement among the 26 NATO nations. Belgium is responsible for the management of the project and acts as host nation under the principles of the NATO Security Investment Programme. The estimated date for completion of the project is 2014 with an overall cost of EUR 1,177 million. The budget for 2007 including brought forward credits was EUR 45.6 million; commitments in 2006 were EUR 45.6 million and payments EUR 20 million (respectively EUR 21.8, 21.6 and 16.7 million in 2006).

Audit Highlights

The Board issued an unqualified opinion on the restated financial statements of the New NATO Headquarters for the year ended 31 December 2007. The restatement corrected several material IPSAS related errors observed by the Board, notably:

- An understatement of the value of "PPE - Fixed assets in progress" by EUR 1.3 million, due to the non-capitalisation of costs from 2007, paid or to be paid in 2008;
- An overstatement of the item "Prepayments" and the related liability by EUR 7.5 million as it includes costs which relate to the 2007 accounting period and that should not have been treated as "Prepayments";

- An understatement of the item “Interests” by 0.4 million because 2007 interests received in 2008 were not properly accrued.

The Board observed in addition that EUR 0.2 million were incorrectly recorded as “Unearned Revenues – Credits carried forward” since they correspond to payments in 2008 for services performed in 2007 and should have been booked as “Payables” in 2007 and observed several inconsistencies between the notes and the figures in the tables of the financial statements.

35. Representation Allowances – 2007

Introduction

The Board audits the Representation Allowance expenditures of senior NATO officials in accordance with the provisions set out by the Permanent Representatives in 1980 and further guidance established in 1998. The Board’s report is submitted to the Secretary General for onward transmission to the Permanent Representatives. The total 2007 allowances amounted to EUR 0.2 million.

Audit Highlights

The Board found that for 2007, most of the recipients of the allowance complied with the accountability requirements. In a few cases, recipients spent less than the allowance received. Such under spends are to be reimbursed in accordance with the Secretary General’s instructions. The Board further found instances of minor deviations from the applicable rules with regard to documentation/justification and eligible costs, and recommended that the administration remind the recipients of the related provisions.

36. SHAPE International School (SIS) – 2007

Introduction

The SHAPE International School provides schooling for dependants of the SHAPE community, from Kindergarten through to the secondary levels. The school comprises nine national curricula, 6 curricula languages and students from 41 nations. Nations determine the curricula of their national units, pay their own teachers, and provide supplies. That expenditure is accounted for and audited nationally. The school’s General Services Unit is funded internationally by contributions of member countries. These contributions mainly depend on the number of Nationals attending the school. The Board only audits the General Services unit. The General Services budget in 2007 amounted to EUR 5.1 million; commitments were EUR 5.0 million and payments EUR 4.4 million (respectively EUR 5, 5 and 3.8 million in 2006). The School has about 2,500 students.

Audit Highlights

The Board issued an unqualified audit opinion on the 2007 financial statements of the SHAPE International School and raised no new observations.

PERFORMANCE AUDITS AND SPECIAL STUDIES

37. The Customer Funding Regime at the NATO C3 Agency (NC3A)

Introduction

The NATO C3 Agency (NC3A) was created in 1995 and started operating on 1 July 1996. As of 1 January 2000 the agency has been operating under a new funding mechanism, known as a “Customer Funding (CF) Regime”. Under CF, customers define their priorities, obtain funding for them, and negotiate contracts for their implementation by the agency. CF was introduced with the intention to better align the focus of NC3A’s products and services to its customers’ priorities, to enhance transparency and efficiency, and to secure better value for money for NATO. From the outset, the Senior Resource Board recognised the need for regular monitoring of the Customer Funding Regime.

The Board carried out a performance audit of the CF Regime at NC3A, to find out how this mechanism affected the agency’s management structure and business processes, to what extent it made NC3A services more efficient and effective, how it affected the Customers’ requirement definition and performance validation, what lessons had been learnt and what the main challenges were for improving the system. To achieve the audit objectives, the audit team conducted interviews with and collected documents from programme officials at NC3A, HQ SACT, SHAPE, JFC HQ North, the NATO HQ C3 Staff, and the NATO Office of Resources of the International Staff. The field work included a review of the implementation of a sample of projects and NSIP capability packages.

Audit Highlights

The Board found that:

- The NC3A has significantly adjusted its management structure and business processes to the new funding, and continues to do so. The NC3 Board which is the entity that oversees the agency and provides policy guidance and directives has not yet fully exercised its chartered authority with regard to the monitoring of the NC3 Agency performance;
- With regard to Agency efficiency, NC3A performance indicators point to a number of positive developments, but they also show that some areas still demonstrate a clear potential for improvement;
- Since the start of the CF, the NC3A revenue has more than doubled in size. The steady growth of the operational income and expenditure reflects the increased demand for NC3A services. The customer base diversified considerably. The growing share of non-common funded customers indicates that NC3A has also managed to attract new customers;
- The CF objective, to ensure that work at NC3A was directed by its customers and aligned to their priorities, concerned mainly the Strategic Commands. At ACT, the project preparation, screening and prioritisation process was refined continuously. At ACO, improvements are required in the procedures for identification, consolidation

and harmonisation of the requirements;

- The issue of competition has been the subject of differing views since the inception of CF. NC3A, largely supported by the NC3 Board and the NC3 Representatives, is of the opinion that the agency should not compete with industry. So far, NC3A customers have only made a very limited use of competition. Hard data on any financial benefits resulting from competition have not yet been provided.

The Board formulated recommendations that:

- The NC3 Board, in conjunction with the MBC, examine how it could more formally discharge its role in the monitoring of the NC3A performance;
- With regard to Project Service Costs (PSC) claimed for the implementation of NSIP projects, the NC3A and the NATO Office of Resources discuss whether such requests for PSC should be more detailed to allow more thorough screening. In order to allow timely technical validation of NSIP project outputs, NC3A should more closely adhere to the relevant NSIP regulations;
- Regarding the agreements with ACT, the relevant purchase orders should be signed as early as possible, and that options be investigated to limit the drawbacks of ACT's military staff rotation. On the other hand, NC3A's billing reports should provide better information on the link between work invoiced and deliverables produced;
- SHAPE improve its procedures for the identification, consolidation and harmonisation of its requirements, and for the measurement of NC3A performance;
- On the issue of competition, the related policy documents be updated. In particular, the obligation on customers to test the market before selecting suppliers for C3 services should be reconsidered.

The NC3 Board responded that it takes its Charter responsibilities to measure NC3A performance very seriously and that it actively holds the NC3A General Manager to account it. The NC3 Board also stated that it does not share the perception that NC3A is expensive and that it would welcome a comparative study by the IBAN auditors with similar organisations.

38. NATO Logistics Support to Deployed Operations

Introduction

Since the end of the Cold War in 1990, NATO has increasingly engaged in operations such as crisis response operations (CRO) and disaster relief, requiring the deployment of NATO member states' forces. The majority of the NATO costs related to these operations are funded from varying NATO sources (MBC, NSIP) and are under the command and control of different NATO military authorities. Other NATO organisations such as NC3A and NAMSA provide support to NATO deployed operations. NATO has six on-going operations/missions, and NATO CRO budgets were almost 200 million Euro in 2007. The Board audited specific performance aspects of NATO logistics support to deployed operations, dealing with such questions as:

- How effectively has NATO implemented its concept of Multinational Logistics in actual deployed operations? Has it clearly delineated its responsibilities versus those

of the member nations? Has it been able to effectively implement the concept of “lead-nation” role in multinational logistics?

- To what extent do NATO’s decision-making processes and funding mechanisms, regulations and policies ensure that logistical support for deployed operations is effective and efficient?
- To what extent has NATO learned and applied lessons from challenges and obstacles encountered in providing logistics support to past and on-going deployed operations?

The audit encompassed operations and NATO financial expenditures related to the years 2003-2007. The audit focussed on NATO logistical support to the following operations: International Security Assistance Force (ISAF) and the Kosovo Force (KFOR).

Audit Highlights

The Board found that:

- KFOR command is generally aware of the different bi or multi-lateral logistics arrangements among national forces. In ISAF this is not the case and the command does not have a truly accurate and comprehensive view of the logistics capabilities, assets, or resources that are in the theatre. This limits the ability of the commander to effectively establish the logistic requirements and coordinate logistic planning and support within the area of responsibility;
- Nations are reluctant to rely on multinational logistics solutions where the nation would have to cede national control or authority to another nation or NATO. As a result, duplication of logistics efforts is not minimised. With fewer nations willing to assume “lead nation” roles, NATO may have to undertake more such responsibilities in the future;
- The creation of true Multinational Integrated Logistic Units (MILU) in KFOR and ISAF has not yet happened because of obstacles to successful implementation of the concept;
- In general, the Board did not find significant problems related to the provision of logistic support to KFOR. In ISAF the current procedures related to NATO’s decision-making processes and funding mechanisms pose a greater problem because the operational environment is dynamic and constantly changing. Obstacles in ISAF include decisions taken to put interim solutions in place based upon the Minimum Military Requirement (MMR) principle;
- The frequent rotation of in-theatre staff and the lack of continuity of information and knowledge of NATO funding rules and procedures poses an obstacle to the successful implementation of the Project Submission Requirements process;
- KFOR and ISAF logistics staff were unaware of the extent of lessons learned documentation available and documentation specifically related to logistics is limited. Because of frequent staff rotation, institutional knowledge about previous challenges and solutions are not always kept. It does not appear that any entity in NATO is actively disseminating lessons learned and monitoring other NATO bodies to determine if these lessons learned are implemented. Although the exploitation of lessons learned could be done at a national level, there seems to be no organised process to put them in common at the coalition level or even more in the NATO

community.

The Board recommended that:

- ACO develop procedures to ensure that the KFOR and ISAF commanders have the authority to coordinate logistic support within their area of responsibility;
- The Council review the concept of “cost lie where they fall” to determine if revised common-funding or eligibility rules could encourage more nations to take on “lead-nation” roles in order to minimise duplication of logistic functions;
- The Council task ACO to review the apparent contradiction in MC-319/2 relating to collective responsibility and national responsibility which limits the effectiveness of the concept of multinational logistics;
- The Council task ACO to review the concept of MILU’s to determine if emphasis should be placed on the development of more bi- and multi-lateral cooperative logistics solutions;
- A dialogue be established between all parties in determining the definition of the MMR in regards to specific projects;
- SHAPE/JFCs should provide KFOR/ISAF with more in-theatre support in terms of working visits to instruct KFOR/ISAF staff on NATO procedures;
- KFOR/ISAF should better train staff on the existence and use of the JALLC lessons learned database. In addition, a logistics related body should be tasked to ensure that logistics lessons learned are implemented and applied to other NATO operations;
- KFOR/ISAF should develop additional training and more specific and detailed handover procedures for new logistics staff;
- A larger debate needs to occur between the nations, NATO Military Authorities, and NATO HQ, to determine if NATO is effectively structured to logistically support out of area operations such as ISAF.

39. SPECIAL REPORT TO THE COUNCIL ON THE IMPLEMENTATION OF THE INTERNATIONAL PUBLIC SECTOR ACCOUNTING STANDARDS (IPSAS) WITHIN NATO

Introduction

On 17 July 2002, the Council adopted IPSAS, including the accrual and going concern assumptions, as the applicable accounting standards for all NATO entities effective for the fiscal year 2006. Expected benefits were harmonisation and consistency of accounting and financial reporting NATO-wide, improved accountability as well as comprehensive and more accurate financial information for the users of the financial statements. The Board has compiled in this report the main conclusions relevant to the implementation of IPSAS NATO wide from its audit of the 2006 financial statements.

Highlights

The audit confirmed that the NATO entities have achieved significant progress in improving consistency and transparency of financial reporting. In a number of cases, however, IPSAS compliance was achieved only after correction and restatement of the financial statements,

which in some instances delayed the preparation and audit of the final versions. Other NATO entities had chosen not to restate their 2006 accounts but to concentrate on issuing accurate 2007 financial statements. The 2006 audit revealed recurring problems relating to the improper application of accruals principles to expenditure and revenue; the incorrect presentation of inventories; a lack of consistency and weak co-ordination between NATO entities; and a lack of attention to the detailed requirements of IPSAS. Additional challenges are arising with the expiration of the transitional period of the standard on Property, Plant and Equipment in 2010. This will entail issues about the definition of assets, ownership of the assets and about what entity will account for them and how. These and similar issues should be dealt with before the transitional period expires.

Conclusion

The Board acknowledges the efforts made by the NATO entities to implement IPSAS and it notes that, as a result, the consistency and transparency of financial reporting within NATO is improving. That momentum should be maintained. The Board therefore would welcome that the Council reconfirm the importance of IPSAS as NATO accounting standards in support of the efforts of the NATO Financial Controllers for a consistent application of IPSAS NATO-wide.

* * * *

The North Atlantic Council considered the subject report on the implementation of IPSAS in the context of the discussion of the Board's Annual Activities report for 2007 on 2 July 2008 and recalled the importance of maintaining the momentum of IPSAS implementation (Section III of C-DS(2008)0044 dated 11 July 2008).

AUDITED ENTITIES AND ACTIVITIES
AND AUDIT CYCLE

The Board audits 82 entities, of which 46 are audited on an annual basis, and 36 are audited on a cyclical basis, every two to three years.

MILITARY COMMANDS AND OPERATIONS

Annual

- ACO Consolidated¹
 - ACO Treasury
 - SHAPE
 - Joint HQ Lisbon
 - JFC HQ Brunssum
 - JFC HQ Naples
 - CC-Air HQ Ramstein
 - CC-Land HQ Heidelberg
 - CC-Air HQ Izmir
 - CC-Land HQ Madrid
 - CC HQ Northwood (incl. MEWSG)
 - CRO (incl. JFC, KFOR, NHQSa, ISAF, NTMI, AMIS/Trust Funds)
 - E-3A Component
 - NAEW FC
 - NPC Glons
- (+ associated budgets not linked to a specific location)

- ACT Consolidated
 - SACT HQ
 - JFTC Bydgoszcz
 - NURC La Spezia
 - JALLC Monsanto
 - JWC Stavanger
- (+ associated programme budgets)

Cyclical

- ARRC²
- CAOCS (10 commands)²
- CIMIC Group North²
- CIMIC Group South²
- COE-DAT²
- HQ RRC-FR²
- IFC²
- JAPCC²
- JCBRN Defence COE²
- NRDC (5 commands)²

¹ The Board audits the most important commands every year. Smaller commands are audited on a bi- or tri-annual basis. The audit of these commands also includes a number of programmes that are budgeted and reported separately from the command's budgets.

² Multi-nationally funded command(s).

NATO PRODUCTION AND LOGISTICS ORGANISATIONS

Annual

ALTBMDPMO
BICES
CEPMO
- CEPMA
- Belgian Division
- French Divisions
- German Divisions
- Netherlands Division
NACMO
NAGSMO
NAHEMO
NAMEADSMO
NAMSO
NC3A
NETMA
- NAMMO
- NEFMO
NAPMO
NHMO
NCSA (incl. NCISS)
NSA
RTO

MILITARY, CIVILIAN AND OTHER BODIES

Annual

AFNORTH International School³
AGS3
Defined Contribution Pension Scheme
IMS, PfP and MD
IS
MSIAC
NATO HQ Adaptation
NAMFI³
NDC
NPA³
Provident Fund
Pension Scheme
Retirees Medical Claims Fund
Representation Allowances
SHAPE International School³

Cyclical

FORACS

³ Multi-nationally funded entity.

FINANCIAL AUDIT COVERAGE FOR AUDITED ENTITIES

| | | Last Audit | | Next Audit | |
|--------------------------|--------------------------|--------------|------------------|--------------------|------------------|
| | | Done in year | Covering year(s) | To be done in year | Covering year(s) |
| MILITARY COMMANDS | | | | | |
| 1. | ACO Group | 2008 | 2007 | 2009 | 2008 |
| 2. | ACT Group | 2008 | 2007 | 2009 | 2008 |
| 3. | ARRC | 2008 | 2004/05/06/07 | 2009 | various |
| 4. | JAPCC | 2009 | 2006/07/08 | 2009 | various |
| 5. | CAOCs (10 sites) | 2008 | 2005/06/07 | 2009 | various |
| 6. | Cimic (1 site out of 2) | 2008 | 2005/06/07 | 2009 | various |
| 7. | NRDC | 2008 | 2005/06/07 | 2009 | various |
| NPLOs | | | | | |
| 1. | NAMSO | 2008 | 2007 | 2009 | 2008 |
| 2. | NETMA | 2008 | 2007 | 2009 | 2008 |
| 3. | NAPMO | 2008 | 2007 | 2009 | 2008 |
| 4. | NHMO | 2008 | 2007 | 2009 | 2008 |
| 5. | CEPS | 2008 | 2007 | 2009 | 2008 |
| 6. | NC3A | 2008 | 2007 | 2009 | 2008 |
| 7. | NACMO | 2008 | 2007 | 2009 | 2008 |
| 8. | NAHEMO | 2008 | 2007 | 2009 | 2008 |
| 9. | NAMEADSMO | 2008 | 2007 | 2009 | 2008 |
| 10. | BICES | 2008 | 2007 | 2009 | 2008 |
| 11. | RTO | 2008 | 2007 | 2009 | 2008 |
| 12. | NSA ⁴ | 2008 | 2007 | 2009 | 2008 |
| 13. | NCSA | 2008 | 2007 | 2009 | 2008 |
| 14. | NAGSMO (to be activated) | - | - | - | - |
| 15. | ALTBMDPMO ⁵ | 2008 | 2007 | 2009 | 2008 |

⁴ The audit is combined with the audit of the IMS which prepared the consolidated IMS-NSA financial statements.

⁵ Incorporated into the NC3A Financial Statements.

FINANCIAL AUDIT COVERAGE FOR AUDITED ENTITIES

| | | Last Audit | | Next Audit | |
|--|-------------------------------------|--------------|------------------|--------------------|------------------|
| | | Done in year | Covering year(s) | To be done in year | Covering year(s) |
| MILITARY, CIVILIAN AND OTHER BODIES | | | | | |
| 1. | IS | 2008 | 2007 | 2009 | 2008 |
| 2. | NATO HQ Adaptation | 2008 | 2007 | 2009 | 2008 |
| 3. | IMS | 2008 | 2007 | 2009 | 2008 |
| 4. | NAMFI | 2008 | 2007 | 2009 | 2008 |
| 5. | Provident Fund | 2008 | 2007 | 2009 | 2008 |
| 6. | Pension Scheme Group | 2008 | 2007 | 2009 | 2008 |
| 7. | Defined Contribution Pension Scheme | 2008 | 2007 | 2009 | 2008 |
| 8. | Retirees Med. Claims Fund | 2008 | 2007 | 2009 | 2008 |
| 9. | Representation Allowance | 2008 | 2007 | 2009 | 2008 |
| 10. | NDC | 2008 | 2007 | 2009 | 2008 |
| 11. | FORACS | 2007 | 2000/01/02/03/04 | 2009 | 2005/06/07/08 |
| 12. | MSIAC | 2008 | 2007 | 2009 | 2008 |
| 13. | AFNORTH School | 2008 | 2007/08 | 2009 | 2009 |
| 14. | SHAPE School | 2008 | 2007 | 2010 | 2008/09 |
| 15. | AGS3 | 2008 | 2007 | 2009 | 2008 |
| 16. | NPA | 2008 | 2007 | 2008 | 2008 |

**AUDIT UNIVERSE AND DIRECT COST OF THE AUDIT
IN 2008**

AUDIT UNIVERSE AND DIRECT COST OF THE AUDIT IN 2008

| BODIES | Audit Universe in 2008 Million EUR (1) | Auditor Time (days) (2) | Salary + Travel Cost 2008 EUR (3) |
|---|---|----------------------------------|--|
| AGENCY FINANCIAL | | | |
| Commands | | | |
| ACO Group ⁽¹⁾ | 889.5 | 432.0 | 364,991 |
| ACT Group | 112.0 | 164.3 | 148,173 |
| ARRC | 1.1 | 43.3 | 36,228 |
| JAPCC | 1.2 | - | - |
| CAOCs - 10 commands | 5.8 | 64.9 | 53,377 |
| CIMICs - 2 commands | 1.3 | - | - |
| NRDCs - 4 commands | 7.7 | - | - |
| NPLOs | | | |
| ALTBMDPO | 5.5 | - | - |
| BICES | 5.0 | 32.0 | 24,123 |
| CEPMO | 107.4 | 122.1 | 109,500 |
| NACMO ⁽²⁾ | 20.0 | 55.8 | 42,075 |
| NAHEMO | 487.1 | 59.9 | 51,413 |
| NAMEADSMO | 365.4 | 35.8 | 36,983 |
| NAMMO-NEFMO-NETMA | 5,454.1 | 152.8 | 145,426 |
| NAMSO | 888.0 | 190.4 | 164,478 |
| NAPMO | 155.0 | 96.8 | 79,514 |
| NC3A | 333.6 | 135.3 | 106,526 |
| NCSA | 152.2 | 94.4 | 74,648 |
| NHMO | 9.5 | 80.0 | 69,606 |
| RTO | 5.8 | 17.8 | 17,052 |
| Civilian & Military & Agencies | | | |
| AFNORTH SCHOOL | 4.4 | 24.4 | 20,373 |
| AGS3 | 3.1 | 13.7 | 10,338 |
| DCPS ⁽³⁾ | 24.0 | - | - |
| FORACS | 0.8 | 5.3 | 4,007 |
| IMS (Incl. NSA, PfP, MD) | 22.7 | 23.8 | 17,952 |
| IS | 172.0 | 165.5 | 124,861 |
| IS New HQ | 40.7 | 42.5 | 32,057 |
| MSIAC | 1.6 | 14.6 | 10,979 |
| NAMFI | 11.9 | 32.2 | 29,686 |
| NDC | 6.0 | 19.9 | 19,432 |
| NPA ⁽⁴⁾ | 8.2 | 15.6 | 12,125 |
| PENSION SCHEME | 92.8 | 55.0 | 41,514 |
| PROVIDENT FUND ⁽⁵⁾ | 67.2 | 24.0 | 18,112 |
| REP. ALLOWANCE | 0.2 | 9.5 | 7,133 |
| RMCF ⁽⁶⁾ | 146.2 | 20.1 | 15,147 |
| SHAPE SCHOOL | 3.9 | 13.8 | 10,859 |
| Subtotal | 9,612.9 | 2,257.4 | 1,898,687 |

AUDIT UNIVERSE AND DIRECT COST OF THE AUDIT IN 2008

| | Audit Universe in 2008 Million EUR (1) | Auditor Time (days) (2) | Salary + Travel Cost 2008 EUR (3) |
|---------------------------|---|----------------------------------|--|
| NSIP FINANCIAL | | | |
| Annual File Review | | 135.1 | 101,921 |
| NSIP Financial Statements | | 3.7 | 2,762 |
| ACO | 17.0 | 32.2 | 29,057 |
| BELGIUM | - | - | - |
| CEPMO | 3.9 | 7.3 | 6,523 |
| DENMARK | 0.2 | - | - |
| FRANCE | 2.0 | - | - |
| GERMANY | 67.3 | 68.5 | 59,455 |
| GREECE | 30.2 | 22.2 | 21,439 |
| HUNGARY | 15.5 | 7.7 | 10,109 |
| ITALY | 25.2 | 25.2 | 24,026 |
| LITHUANIA | 14.9 | 6.3 | 5,673 |
| NACMO | 39.5 | 18.9 | 14,288 |
| NAMSO | 92.0 | 15.0 | 12,958 |
| NC3A | 205.4 | 33.8 | 25,528 |
| The NETHERLANDS | 0.7 | - | - |
| NORWAY | 2.0 | - | - |
| TURKEY | 61.2 | 38.9 | 33,065 |
| UNITED KINGDOM | 161.4 | 52.8 | 46,818 |
| UNITED STATES | 20.2 | 23.6 | 25,104 |
| | Subtotal | 491.3 | 418,725 |
| PERFORMANCE AUDITS | | | |
| Internal Audit | | 1.7 | 1,282 |
| Logistics of Deployed Ops | | 102.0 | 77,457 |
| NAEW&C Follow-up | | 21.2 | 16,707 |
| NC3A Customer Funding | | 75.3 | 57,509 |
| NC3A Procurement | | 27.4 | 20,675 |
| NSIP Management | | 161.1 | 122,784 |
| Fraud & Corruption | | 67.5 | 52,745 |
| | Subtotal | 456.2 | 349,159 |
| STUDIES | | | |
| IT reviews | | 3.1 | 2,324 |
| IPSAS | | 5.3 | 9,317 |
| TeamMate-IDEA | | 72.4 | 54,663 |
| Various | | 37.6 | 30,935 |
| | Subtotal | 118.4 | 97,239 |
| BOARD | | 270.0 | 217,894 |
| ADMINISTRATION | | 150.3 | 113,408 |
| TRAINING | | 215.1 | 166,169 |
| GENERAL TOTAL | 10,371.5 | 3,958.8 | 3,261,281 |

Column (1)

Represents the budget authorised in 2007 audited in 2008 in the case of Agencies, or the NSIP amounts presented for audit during 2008.

Column (2)

Represents the time spent by the audit staff during 2008.

Column (3)

Represents the cost of the audit to the NATO Civil Budget, including remuneration and a notional pension/leaving allowance amount of auditors and travel cost of auditors and Board Members.

It does not contain the cost of support staff amounting to EUR 572,795 and the salaries and allowances of Board Members that are a national charge

Footnotes

- (1) Not including EUR 18.2 million NSIP project expenditure.
- (2) Not including EUR 86.8 million NSIP project expenditure.
- (3) EUR 24 million net assets available for employee benefits.
- (4) Including 4.6 million assets of the 30 members of the NPA Provident Fund.
- (5) EUR 67.2 million assets spread over 167 individual members' accounts.
- (6) Including EUR 104 million assets of the RMCF investment fund.

LIST OF ABBREVIATIONS

| | |
|-----------------|--|
| ACO | Allied Command Operations |
| ACT | Allied Command Transformation |
| AFNORTH | Allied Forces, Northern Europe |
| AGFC | Advisory Group of Financial Counsellors |
| AGS3 | Alliance Ground Surveillance Support Staff |
| ALTBMDPMO | Active Layered Theatre Ballistic Missile Defence Programme Management Organisation |
| AMIS | African Union Mission in Sudan |
| ARRC | Allied Rapid Reaction Corps |
| BICES | Battlefield Information Collection and Exploitation System |
| Board | International Board of Auditors for NATO |
| BoD | Board of Directors |
| BPO | Belgian Pipeline Organisation |
| CAOCs | Combined Air Operation Centres |
| CCOE | Civil-Military Cooperation Centre of Excellence |
| CEPMA | Central Europe Pipeline Management Agency |
| CEPMO | Central Europe Pipeline Management Organisation |
| CEPS | Central Europe Pipeline System |
| CF | Customer Funding |
| CIMIC GN/CGN HQ | Civil and Military Cooperation Group North |
| CIMIC GS | Civil and Military Cooperation Group South |
| CNABs | Competent National Audit Bodies |
| COE-DAT | Centre of Excellence-Defence against Terrorism |
| COFFA | Certificate of Final Financial Acceptance |
| Council | North Atlantic Council |
| CRO | Crisis Response Operations |
| DCOS | Deputy Chief of Staff Support/Resources |
| DCPS | Defined Contribution Pension Scheme |
| DPO | Defensie Pijpleiding Organisatie |
| EUR | Euro |
| EUROSAI | European Organisation of Supreme Audit Institutions |
| FBG | Fernleitungs-Betriebsgesellschaft |
| FORACS | NATO Naval Forces Sensor and Weapons Accuracy Check Sites |
| GF | Global Funding |
| HQ | Headquarters |
| HQ RRC | Headquarters Rapid Reaction Corps |
| IBAN | International Board of Auditors for NATO |
| IC | Infrastructure Committee |
| IDEA | Interactive Data Extraction and Analysis |
| IFAC | International Federation of Accountants |
| IFC | Intelligence Fusion Centre |
| IMS | International Military Staff |
| INTOSAI | International Organisation of Supreme Audit Institutions |
| IPSAS | International Public Sector Accounting Standards |
| IS | International Staff |
| ISA | International Standard on Auditing |
| ISAF | International Security Assistance Force [Afghanistan] |
| ISSAI | International Standard of Supreme Audit Institutions |
| IT | Information Technology |

ANNEX E
IBA-M(2009)1

| | |
|-----------|--|
| JALLC | Joint Analysis and Lessons Learned Centre |
| JAPCC | Joint Airpower Competence Centre |
| JC | Joint Command |
| JCBRN | Joint Chemical Biological Radiological and Nuclear Defence Centre of Excellence |
| JFAI | Joint Final Acceptance Inspection |
| JFC | Joint Force Command |
| JFTC | Joint Force Training Centre |
| JWC | Joint Warfare Centre |
| KFOR | KOSOVO Forces |
| MBC | Military Budget Committee |
| MD | Mediterranean Dialogue |
| MEADS | Medium Extended Air Defence System |
| MEWSG | Multiservice Electronic Warfare Support Group |
| MILU | Multi-national Integrated Logistics Unit |
| MMR | Minimum Military Requirement |
| MOU | Memorandum of Understanding |
| MSIAC | Munitions Safety Information Analysis Centre |
| NAFS | NATO Automated Financial System |
| NACMA | NATO ACCS Management Agency |
| NACMO | NATO ACCS Management Organisation |
| NACOSA | NATO Communication and Information System (CIS) Operating and Support Agency |
| NAEW&C | NATO Airborne Early Warning and Control |
| NAEWF | NATO Airborne Early Warning Force |
| NAGSMO | NATO Alliance Ground Surveillance Management Organisation |
| NAHEMO | NATO Helicopter Design and Development Production and Logistics Management Organisation |
| NAMEADSMA | NATO Medium Extended Air Defence System Design and Development, Production and Logistics Management Agency |
| NAMEADSMO | NATO Medium Extended Air Defence System Design and Development, Production and Logistics Management Organisation |
| NAMFI | NATO Missile Firing Installation |
| NAMMO | NATO Multi-Role Combat Aircraft Development and In-Service Support Management Organisation |
| NAMSA | NATO Maintenance and Supply Agency |
| NAMSO | NATO Maintenance and Supply Organisation |
| NAPMA | NATO AEW&C Programme Management Agency |
| NAPMO | NATO AEW&C Programme Management Organisation |
| NC3A | NATO Consultation, Command and Control Agency |
| NCISS | NATO Communications and Information Systems School |
| NCSA | NATO CIS Services Agency |
| NDC | NATO Defence College |
| NEFMO | NATO European Fighter Aircraft Development, Production and Logistics Management Organisation |
| NETMA | NATO Euro Fighter 2000 and Tornado Development Production and Logistics Management Agency |
| NFR | NATO Financial Regulations |
| NHMO | NATO HAWK Management Office |
| NHPLO | NATO HAWK Production and Logistics Organisation |
| NHQSa | NATO HQ Sarajevo |

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| NATO PA | NATO Parliamentary Assembly |
| NOR | NATO Office of Resources |
| NPA | NATO Parliamentary Assembly |
| NPC | NATO Programming Centre |
| NPLO | NATO Production and Logistics Organization |
| NRDC | NATO Rapid Deployable Corps |
| NRFA | Northern Region Financial Administration |
| NSA | NATO Standardization Agency |
| NSIP | NATO Security Investment Programme |
| NTM-I | NATO Training Mission Iraq |
| NURC | NATO Undersea Research Centre |
| PfP | Partnership for Peace |
| PPE | Property, Plant and Equipment |
| PSC | Project Service Costs |
| PSO | Peace Support Operations |
| RFAS | Reaction Force Air Staff |
| RMCF | Retirees Medical Claims Fund |
| RTA | Research and Technology Agency |
| RTO | Research and Technology Organisation |
| SACLANT | Supreme Allied Commander Atlantic |
| SACT | Supreme Allied Command Transformation |
| SAIs | Supreme Audit Institutions |
| SHAPE | Supreme Headquarters Allied Powers Europe |
| SNOI | Service National des Oléoducs Interalliés |
| SPIE | Statement of Planned Income and Expenditure |
| SPO | System Project Office |
| SRB | Senior Resource Board |
| TOR | Terms of Reference |
| TP | Third parties |
| UK ADGE | UK Air Defence Ground |
| UNAC | User Nations Committee |
| USD | United States Dollar |