



Supreme Audit Office

KON.410.002.01.2019

P/19/037/01

Auditor's Report
on the Financial Statements of
the Headquarters Multinational Corps
Northeast
for the year ended 31 December 2017
Framework Nations Budget

December 2019

I. Audit identification data

Audit number and title	P/19/037/01– Execution of the Framework Nations Budget 2017 by the Headquarters Multinational Corps Northeast
Auditing entity	Supreme Audit Office of Poland Department of National Defence
Auditors	1. Małgorzata Romanowicz, Senior Public Audit Expert; 2. Mariusz Tupaj, Senior Public Audit Expert; 3. Adam Gęstwicki, Senior Public Audit Expert.
Audited entity	Headquarters Multinational Corps Northeast (hereinafter “Corps” or “HQ MNC NE”), Łukasińskiego 33, Szczecin 71-215.
Head of the audited entity	Lieutenant General Manfred Hofmann (until 11 September 2018), Lieutenant General Sławomir Wojciechowski (since 12 September 2018).

II. Introduction

Legal basis	The audit was conducted pursuant to of Article 10 item 4 of the Corps Convention ¹ of 5 September 1998 and the Agreement concluded by SAI Poland, SAI Denmark and SAI Germany ² , as well as Article 2 item 3 point 4 in conjunction with Article 12a item 1 and 2 of the Supreme Audit Act of 23 December 1994 ³ .
Mission, activity and elements of HQ MNC NE	Tasks and missions of the Corps were defined in Article 3 of the Corps Convention. The elements of the Corps which are to be funded equally by the Framework Nations, were defined in Article 10 item (2) of the Corps Convention. Details concerning the organisation and activity of the Corps were defined in the Agreement between the Ministry of Defence of the Kingdom of Denmark, the Federal Ministry of Defence of the Federal Republic of Germany and the Ministry of National Defence of the Republic of Poland ⁴ .
General information on contributions and budget execution of HQ MNC NE	In 2017 HQ MNC NE received contributions made by the Framework Nations in the total amount of PLN 26.710.455. The 2017 budget, amounting to PLN 33.643.524 was used in the amount of PLN 25.797.123, i.e. in 76,7% (without carry forwards 2015-2016).

¹ Convention between the Government of the Federal Republic of Germany, the Government of the Kingdom of Denmark, and the Government of the Republic of Poland on the Multinational Corps Northeast signed on 5 September 1998 in Szczecin (Journal of Laws of 2000 No. 21, item 259, as amended).

² Agreement of 2 February 2001.

³ Journal of Laws of 2019, item 489.

⁴ Agreement between the Ministry of Defence of the Kingdom of Denmark, the Federal Ministry of Defence of the Federal Republic of Germany and the Ministry of National Defence of the Republic of Poland concerning Operation of the Multinational Corps Northeast of 16 April 2009, hereinafter “Agreement”.

III. Opinion of the Supreme Audit Office of Poland

Aim and scope of the audit

We have audited the Financial Statements of HQ MNC NE for 2017, including Statement of Cash Receipts and Payments, Statement of Budget and Actual Amounts and explanatory Notes to the Financial Statements, which were prepared in line with the International Public Sector Accounting Standards IPSAS, under the cash basis of accounting. The audit encompassed financial and executive aspects, in line with the procedures adopted by the Supreme Audit Institutions of Denmark, Germany and Poland, compliant with the standards⁵ of the International Organisation of Supreme Audit Institutions (INTOSAI), and all applicable rules and regulations of the MNC NE relating to gaining and spending the Corps' funds.

Audit Opinion

The Supreme Audit Office of Poland issues an unqualified opinion⁶.

In our opinion, the accompanying Financial Statements of the Headquarters Multinational Corps Northeast in the framework of the Framework Nations Budget present, in all material respects, true and fair view of the Corps' Cash Receipts and Payments, Budget and Actual Amounts, including explanatory Notes to the Financial Statements, for the year ended 31 December 2017.

In our opinion, transactions carried out by the Corps in the framework of the Framework Nations Budget were in compliance with Financial Administrative Procedures (Staff Directive No 60-70) and all other applicable rules and regulations. The financing principles set out in the Staff Directive No 60-70 as well as NATO regulations, according to which funds for the future expenditure are carried forward for the next years and lapsed funds are deducted from the due contributions of the Framework Nations, enable to fully and rationally use the budgetary funds and to ensure an undisturbed performance of the HQ MNC NE's tasks.

Basis for Opinion

We conducted our audit in accordance with the International Standards of Supreme Audit Institutions (ISSAIs). Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of our report. We are independent of the audited Organisation in accordance with the ISSAI 10 – Mexico Declaration of SAI⁷ Independence and ISSAI 30 – Code of Ethics, together with other requirements that are relevant to our audit of the financial statements of an international institution as stated in ISSAI 5000 – Audit of International Institutions – Guidance for SAIs, and we have fulfilled our ethical and other responsibilities in accordance with the said standards, including the Code of Ethics of the Supreme Audit Office of Poland. **In our opinion the audit evidence we have obtained was sufficient and appropriate to provide a basis for an unqualified opinion.**

Responsibility of the management for Financial Statements

The Commander HQ MNC NE was responsible for all budgetary and financial matters before the Corps Committee and the Budget Finance Group. Among other things, he is responsible for the preparation of the annual Financial Statements for 2017, in line with the International Public Sector Accounting Standards IPSAS, under the cash basis of accounting. The Commander HQ MNC NE also produced

⁵International Standards of Supreme Audit Institutions (ISSAI) and International Public Sector Accounting Standards (IPSAS).

⁶The Supreme Audit Office of Poland may issue: an unqualified opinion, qualified opinion, adverse opinion or a disclaimer of an opinion.

⁷ Supreme Audit Institution.

and submitted for approval the budget estimates and was responsible for the budget execution and internal control over the whole process.

Responsibility of auditors for the opinion on Financial Statements issued on the basis of the audit

In line with the procedures applied by the Supreme Audit Office of Poland, ethical requirements were complied with, and the audit was planned and performed in such a way, so as to obtain rational assurance that the Financial Statements do not contain any material irregularities. On the basis of the sampled accounts, the audit team checked, among other things, the data confirming the amounts and information presented in the Financial Statements. The auditors also reviewed, whether the transactions were made in compliance with the relevant authorisations and regulations.

The auditors selected audit procedures, including the risk assessment of material irregularities in the Financial Statements due to fraud or error. While conducting the risk analysis, the audit team took into consideration the internal control processes, essential to prepare reliable Financial Statements of HQ MNC NE. The applied accounting principles were also reviewed with regard to their adequacy. Finally the general presentation of the Financial Statements was assessed.

IV. Key Audit Matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements of the current period and of compliance authorities⁸. These matters were addressed in the context of our audit of the financial statement as a whole and compliance with authorities, and forming our opinion thereon.

Facts, comments and conclusions regarding the audited area

1. Financial Statements for 2017

All receipts of HQ MNC ME consisting of the contributions of the Framework Nations, VAT reimbursements and excise duty reimbursements, amounting to 95,9% of the total 2017 receipts, were audited. It was noted that Germany had paid the amount of PLN 1.056.515 as prepayment for its contribution for 2018.

Observation 1: Presentation of the Financial Statement

Situation:

The column "Note" on the face of the Financial Statements do not specify numbers of the annotations included in the Notes to the Financial Statements.

Criteria:

- 1) ISSAI 1.3.26: "Notes to the financial statements shall be presented in a systematic manner. Each item on the face of the statement of cash receipts and payments and other financial statements shall be cross referenced to any related information in the notes",
- 2) Best presentation practice: numbers of all notes are given on the face of the financial statements to provide easy reference to the accompanying explanatory notes.

⁸ HQ MNC NE regulations, rules, procedures, standards, and good practice.

Impact:

The lack of notes numbering on the face of the financial statements hinders the readability of the financial statements.

Recommendation:

It is recommended that all Note numbers be inserted in the column "Note" on the face of the Financial Statements to improve the presentation of data and facilitate their reading in the statements⁹.

2. Framework Nations Budget for 2017

The HQ MNC NE budget without the carry forward (2015-2016) was established in the amount of PLN 33.643.524. This amount resulted from the decisions of the Budget and Finance Group (BFG) concerning the amounts for investments related to the HQ MNC NE the construction of a new staff building and gymnasium development.

The HQ MNC NE budget for 2017, including the amounts carried forward to 2018, was executed in the amount of PLN 25.797.123, i.e. in 93,8%, (without the carry forward 2015-2016). The payments made in 2017 enabled to perform all HQ MNC NE tasks.

In course of the 2017 budget execution, HQ MNC NE transferred funds within particular cost categories and among them.

While auditing the expenditure of HQ MNC NE 88 accounting records and documents were examined, in the total amount of PLN 24.891.817, constituting 65,9% of the payments made by HQ MNC NE in 2017. The monetary unit sampling (MUS¹⁰) method was applied on 12 802 accounting records concerning the HQ MNC NE expenditure in 2017.

The conducted examination of the documents proved that the HQ MNC NE payments were made in line with the regulations in force, and they were used to perform the tasks of the Corps. The accounting records for particular payments were compliant, reliably linked with the accounting documents and presented in the accounting ledgers (on proper cost accounts).

Cash balances with bank and cash on hand were compliant with accounting records and data in the HQ MNC NE Financial Statements for 2017.

Observation 2: Discrepancy in rules and regulations in reference to expenditure/costs categories.

Situation:

Three categories of expenditures in the Statement of Cash Receipts and Payments and in the Statements of Comparison of Budget and Actual Amounts were presented in line with the NATO Financial Rules and Regulations and with Staff Directive Number 60-70 – Financial Administrative Procedures, which provide three cost categories that correspond with the said three categories of expenditures.

⁹ In accordance with best practice.

¹⁰ Probability Proportional to Size sampling.

Criteria:

- 1) NATO Financial Rules and Regulations - Review of NATO Financial Regulations, Note by the Secretary General, 24 April 2015,
- 2) Staff Directive Number 60-70 – Financial Administrative Procedures, Chapter 2, item 2-2 Budget Structure says that “Costs of the Corps elements are to be ascertained and estimated in accordance the NATO cost structure. The Multinational budget is to be divided into the following categories:
Chapter 1: Personnel costs
Chapter 2: Contractual supplies and services costs
Chapter 3: Capital and investments costs”,
- 3) Annex D to the Agreement between The Ministry of National Defence of the Republic of Poland, The Ministry of Defence of the Kingdom of Denmark, and The Federal Ministry of Defence of the Federal Republic of Germany concerning Operation of the Multinational Corps Northeast Finance and Multinational Budget, item II, sub-item 2. says that “The Multinational budget will be divide into the following cost categories:
a) cost category 1: Personnel costs
b) cost category 2: Material and administrative costs, including the cost of training projects
c) cost category 3: Exercise costs
d) cost category 4: Investments costs
e) cost category 5: Receipts”,
- 4) Minutes Budget and Finance Group – proposed changes to Corps Agreement Annex D agreed on the meeting held 19-21 October 2016.

Impact:

The foregoing criteria provide for different sets of cost categories whereas all of them are formally valid. Annex D to the Agreement between the Ministries shall be superior to other internal regulations. The current financial reporting practice in the Corps is based on the NATO Financial Regulations and the internal Directive 60-70 and, consequently, is not in compliance with the Annex D to the ministerial agreement.

Recommendations:

It is recommended that the amendments to the Annex D of the Agreement proposed during BFG Meeting of 19-21 October 2016 be implemented to remove discrepancy between the principal ministerial agreement and the internal Corps regulations and, consequently, the current practice in financial reporting.

3. Other observations

- 3.1 Cash balances with bank and cash on hand were compliant with accounting records and data in the HQ MNC NE Financial Statements for 2017.
- 3.2 In course of the payments’ audit it was determined that there were 23 bidding procedures conducted in 2017, totalling PLN 6.466.617, out of which 4 bidding procedures of different EFL¹¹ levels were selected by means of the non-probability sampling method, amounting to PLN 1.528.328.

¹¹ Established Financial Limits (EFL) for the procurement of goods and services are annually defined by the NATO Allied Command Transformation (ACT).

3.3 HQ MNC NE introduced new accounts to the chart of accounts implemented in 2017:

- 713131 Work clothes;
- 721111 Printing, photocopying, visual commercial services;
- 721116 Printing, photocopying, visual minor equipment;

and the accounts for funds for new staff building and gymnasium development:

- 738004-17P003 New Building;
- 738004-17P004 Development of Gymnasium.

Above mention accounts are not presented in the annex D to SD 60-70 dated 15 March 2016 Cost Categories and Account Structure.

The Financial Controller explained, that to enhance proper recording and transparency of cost' reporting HQ MNC NE introduced new accounts to the chart of accounts implemented in 2017. The accounts implemented in the financial year 2017 comply with the accounts in NATO cost structure.

It is recommended that Staff Directive 60-70 be updated in accordance with the NATO cost structure.

3.4 HQ MNC NE implemented an account 747501 (Conference Fees PLN10.057) not related to the budget, used for administration of all receipts and payment of conference fees for events organised by Corps.

It is recommended that Staff Directive 60-70 be updated in relation to Cost Categories and Account Structure.

3.5 The Note 5.2 Cash did not include a position concerning cash balance with bank of the social fund, which in our opinion hindered the analysis of Financial Statements.

3.6 The Table 5.4.3.2 in the explanatory Note 5.4.3 Cash Outflow did not include the total sum of the budget expenditures in 2017 and a column with the information concerning the actual amounts spent (payments together with the carry forwards for the next year), which in our opinion hindered the analysis of the statements and the Notes to the Financial Statements.

4. Implementation of audit recommendations

HQ MNC NE could not implement the observations and recommendations made by the auditors of Supreme Audit Office of Poland concerning to the Financial Statements for the year ended 31 December 2016 during the preparation of the Financial Statements for the year ended 31 December 2017 Framework Nations Budget. The HOTO¹² meeting between SAIs of Denmark, Poland and Germany was held on 28 June 2017 when SAI of Poland got the mandate to conduct the audits of HQ MNC NE Financial Statements. Consequently the audit of FN 2016 was performed by SAI of Poland in 2018.

Status of prior period audit recommendations

OBSERVATION/RECOMMENDATION	ACTION TAKEN	STATUS
Rigsrevisionen - Audit Report on the Framework Budget Financial Statement 2015 Headquarters Multinational Corps Northeast, January 2017.		
Observation In line with the Corps Agreement, Financial	HQ MNC informed the Framework Nations on necessary amendments at the BFG meetings in May 2013	

¹² Hand Over-Take Over.

<p>Statements shall be presented in five main cost groups, whereas HQ MNC NE applied the division into three such groups: personnel costs, contractual supplies and services, and capital and investments – in line with the relevant NATO regulations.</p> <p>Recommendation:</p> <p>The Supreme Audit Office of Denmark recommended ensuring consistency between the practice of HQ MNC NE and the provisions of the Corps Agreement by updating Annex D to the Corps Agreement concluded by the Framework Nations. This matter was raised in all previous audit reports. Despite the efforts made by HQ MNC NE¹³ Framework Nations did not update the Agreement.</p>	<p>and May 2014 and additionally in the Corps Committee meeting in May 2013, thereby initiating revision of the respective Corps documents including their annexes, the Sub-Working Group Legal was informed during the meeting held on 21-24 September 2015. The Framework Nations started a discussion on the future cost sharing of the Framework Nations in 2015. As a result, the revision of the financial regulations by the Sub-Working Group Legal was suspended until the final agreement on the sharing of costs was reached.</p> <p>Budget and Finance Group proposed changes to the Corps Agreement Annex D agreed at the meeting held on 19-21 October 2016 (Minutes from the meeting).</p>	<p>IN PROGRESS</p>
<p>Observation:</p> <p>The column "Note" on the face of the Financial Statements 2016 do not specify numbers of the annotations included in the Notes to the Financial Statements.</p> <p>Recommendation:</p> <p>It is recommended that all Note numbers be inserted in the column "Note" on the face of the Financial Statements to improve the presentation of data and facilitate their reading in the statements.</p> <p>Best presentation practice: numbers of all notes are given on the face of the financial statements to provide easy reference to accompanying explanatory notes.</p>		<p>IN PROGRESS</p>

V. Other information and instruction

The report was prepared in two identical copies in Polish, and in two identical copies in English, two for each of the parties.

Right to submit
objections

In line with Article 54 item 1 and 2 of the Supreme Audit Office Act, Commander MNC NE shall have the right to file substantiated reservations to the audit report in

¹³ HQ MNC NE informed the Framework Nations on the necessity to amend Annex D to the Corps Agreement at the meeting of the Budget and Finance Group (BFG) in May 2013 and 2014. At the meeting of the Corps Committee in May 2013 amendments to Annex D were presented, aimed to regulate the presentation of cost groups in financial statements, according to the NATO regulations. Moreover, the matter was presented to the Sub-Working Group Legal at the meeting on 21-24 September 2015, and further to the Corps Committee in 2016.

Obligation to inform
Supreme Audit Office
of Poland on the
utilisation of the
comments and
implementation of the
recommendations

writing, within 21 days of the receipt thereof. The reservations shall be submitted to the Director of the Department of Defence at the Supreme Audit Office of Poland.

In line with Article 62 of the Supreme Audit Office Act, please inform the Supreme Audit Office of Poland within 14 days of the audit report receipt, on how the audit comments and recommendations have been utilised, as well as on the measures taken or grounds for failing to take such measures.

Should reservations to the audit report be submitted, the aforementioned information shall be submitted within 14 days of the receipt of the NIK's resolution rejecting reservations in whole or the modified audit report.

Warsaw, 17 December 2019

Department of National Defence

Auditors

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