



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 2018  
Framework Nations Budget

December 2019

# I. Audit identification data

Audit number and title	P/19/037/01– Execution of the Framework Nations Budget 2018 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 <sup>1</sup> of 5 September 1998 and the Agreement concluded by SAI Poland, SAI Denmark and SAI Germany <sup>2</sup> , 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 <sup>3</sup> .
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 <sup>4</sup> .
General information on contributions and budget execution of HQ MNC NE	In 2018 HQ MNC NE received contributions made by the Framework Nations in the total amount of PLN 26.999.500. The 2018 budget, amounting to PLN 34.213.500 was used in the amount of PLN 24.143.187, i.e. in 70,6% (without carry forwards 2016-2017).

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<sup>1</sup> 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).

<sup>2</sup> Agreement of 2 February 2001.

<sup>3</sup> Journal of Laws of 2019, item 489.

<sup>4</sup> 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 2018, 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 standards<sup>5</sup> 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 opinion<sup>6</sup>.**

**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 2018.**

**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 SAI<sup>7</sup> 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 2018, in line with the International Public Sector Accounting Standards IPSAS,

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

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

<sup>7</sup> Supreme Audit Institution.

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

under the cash basis of accounting. The Commander HQ MNC NE also produced and submitted for approval the budget estimates and was responsible for the budget execution and internal control over the whole process.

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 authorities<sup>8</sup>. 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.

### 1. Financial Statements for 2018

Facts, comments and conclusions regarding the audited area

All receipts of HQ MNC ME consisting of the contributions of the Framework Nations, VAT reimbursements and excise duty reimbursements, amounting to 98,0% of the total 2018.

In FY 2018 HQ MNC NE issued two calls for funds (22 December 2017 and 8 June 2018)<sup>9</sup>. based on National guidance received by the delegates of the Budget and Finance Group.

In 2018 Denmark paid the contribution in the amount of PLN 6.000.000, Poland payed PLN 9.999.500, Germany PLN 11.000.000. Denmark paid the remaining part of the contribution for the year 2018 in the amount of PLN 1.784.083 in 2019<sup>10</sup>. The amounts of national contributions for 2018 were set based on the agreement of the BFG<sup>11</sup>.

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<sup>8</sup> HQ MNC NE regulations, rules, procedures, standards, and good practice.

<sup>9</sup> Based on the regulation in the Corp Agreement the Calls for Funds should be issued by HQ MNC NE 60 days in advance of the due date in order to enable a timely payment by the Framework Nations.

<sup>10</sup>Annex D to the Corps Agreement, Paragraph VII – “At three dates during the year, The Commander of the Corps will call in partial contributions from the national armed forces’ staffs. The amount of the payments to be made will be determined on the basis of the expected requirements of funds which the Commander of the Corps expects until the next regular calling of funds. Calling for funds must be submitted to the national armed forces’ staffs at the following dates: February 1, June 1, October 1.

<sup>11</sup> BFG Meeting 17-19 October 2017 and 04-06 June 2018.

The Framework Nations finally agreed on a cost share formula on 30th April 2019 taking effect from 1 January 2019<sup>12</sup>.

In our opinion in the FY2018 the contribution of should be pay by Nations based on the applicable current Corps' policy<sup>13</sup>

## 2. Framework Nations Budget for 2018

The HQ MNC NE budget without the carry forward (2016-2017) was established in the amount of PLN 34.213.500. 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 2018, including the amounts carried forward to 2019, was executed in the amount of PLN 24.143.187, i.e. in 70,6%, (without the carry forward 2016-2017). The payments made in 2018 enabled to perform all HQ MNC NE tasks.

In course of the 2018 budget execution, HQ MNC NE transferred funds within particular cost categories and among them.

While auditing the expenditure of HQ MNC NE 96 accounting records and documents were examined, in the total amount of PLN 15.849.849, constituting 62,9% of the payments made by HQ MNC NE in 2018. The monetary unit sampling (MUS<sup>14</sup>) method was applied on 10 670 accounting records concerning the HQ MNC NE expenditure in 2018.

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).

**Observation: 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.

Criteria:

- 1) NATO Financial Rules and Regulations - Review of NATO Financial Regulations, Note by the Secretary General, 24 April 2015,

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<sup>12</sup> Implementing Arrangement between the Ministry of Defence of the Kingdom of Denmark, the Federal Ministry of Defence of the Federal Republic of Germany and the Minister of National Defense of the Republic of Poland on the Funding, Manning, and Support of the Multinational Corps Northeast – “The cost share applicable to the Framework Nations of Denmark, Germany and Poland will be set to 20 pct. for Denmark, 40 pct. for Germany and 40 pct. for Poland.”

<sup>13</sup> Annex D to Corps Agreement, Paragraph III – “The funding of the Multinational budget will be equally shared by the Contracting Parties.

<sup>14</sup> Probability Proportional to size sampling.

- 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 costs 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 2018.
- 3.2 HQ MNC NE non-IT inventory was registered under the procedures of ANNEX E to SD 60-70.
- 3.3 In course of the payments’ audit it was determined that there were 11 bidding procedures conducted in 2018, totalling PLN 6.875.180, out of which

3 bidding procedures of different EFL<sup>15</sup> levels were selected by means of the non-probability sampling method, amounting to PLN 1.471.539.

- 3.4 In 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.
- 3.5 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 2018 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 Notes to the Financial Statements.
- 3.6 In the FY2018 HQ MNC NE made the temporary support of SMFB by cash assets FNB in the amount of PLN 1.200.000 for the prepayments for the reimbursable 2018 exercises' costs. Transaction was effected on 22 October 2018. The amount of temporary support was transferred back from SMFB account to the FNB account before the closure of the financial period 2018. BFG approved the temporary support of SMFB and requested HQ MNC NE to prepare the proposal of provisions in the financial regulations to cover this issue. We share the BFG position in this case and recommend introducing this issue in the Financial Administrative Procedures of HQ MNC NE.

#### **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 the Financial Statements for the year ended 31 December 2017 during preparation of the Financial Statements for the year ended 31 December 2018 Framework Nations Budget. The HOTO<sup>16</sup> meeting between SAIs of Denmark, Poland and Germany was held on 28 June 2017 and SAI of Poland got the mandate to conduct the audits of HQ MNC NE Financial Statements. Consequently the audits of FN 2017 and 2018 were performed by SAI of Poland in 2019.

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<sup>15</sup> Established Financial Limits (EFL) for the procurement of goods and services are annually defined by the NATO Allied Command Transformation (ACT).

<sup>16</sup> Handed Other-Taking Other

### Status of prior period audit recommendations

OBSERVATION/RECOMMENDATION	ACTION TAKEN	STATUS
<p>Rigsrevisionen - Audit Report on the Framework Budget Financial Statement 2015 Headquarters Multinational Corps Northeast, January 2017.</p> <p>Supreme Audit Office - Audit Report on the Framework Budget Financial Statement 2017 Headquarters Multinational Corps Northeast, December 2019.</p>		
<p>Observation: In line with the Corps Agreement, Financial 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: 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 NE<sup>17</sup> Framework Nations did not update the Agreement.</p>	<p>HQ MNC has informed the Framework Nations on necessary amendments at the BFG meetings in May 2013 and May 2014 and additionally at 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>Frame Nations signed on 30 April 2019 the Implementing Arrangement between the Ministry of Defence of the Kingdom of Denmark, the Federal Ministry of Defence of the Federal Republic of Germany, and the Minister of National Defence of the Republic of Poland, on the Funding, Manning, and Support of the Multinational Corps Northeast.</p> <p>The Arrangement will be the starting point to initiate the necessary adjustments to the policy and legal documents of Multinational Corps Northeast.</p> <p>Sob-Working Group Legal on the</p>	<p>IN PROGRESS</p>

<sup>17</sup> 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.

	meetings on 6-7 JUNE 2019 and 28-30 October 2019 agreed on the Time Schedule MNC NE documents revision process. The revision of the Corps Agreement (CA) is planned in 1 <sup>st</sup> Quarter 2020.	
<p>Observation:  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.  The accounts are not presented in the annex D to SD 60-70 dated 15 March 2016 Cost Categories and Account Structure  Recommendation:  It is recommended that Staff Directive 60-70 be updated in accordance with the NATO cost structure.</p>	<p>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.    HQ MNC NE will revise and update the Financial and Administrative Procedures SD 60-70.</p>	IN PROGRESS
<p>Observation:  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.  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 statements.  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>The columns "Note" on the face of the Financial Statements 2018 specify numbers of the annotations included in the Notes to the Financial Statements.</p>	CLOSED

## 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 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.

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

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

Director  
Marek Zająkała

Auditors

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Senior Public Audit Expert

Adam Gęstwicki  
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