	<b>NATO</b>	NORTH ATLANTIC COUNCIL
	<b>OTAN</b>	CONSEIL DE L'ATLANTIQUE NORD

**NATO UNCLASSIFIED**

25 March 2022

**DOCUMENT**  
PO(2022)0118-AS1

**IBAN SPECIAL REPORTS**  
**RELATED TO THE CLOSE-OUT OF NSIP PROJECT**

**ACTION SHEET**

On 24 March 2022, under the silence procedure, the Council noted the RPPB report attached to PO(2022)0118 and its recommendations and agreed to the public disclosure of the RPPB report and the two IBAN Special Reports

(Signed) Jens Stoltenberg  
Secretary General

NOTE: This Action Sheet is part of, and shall be attached to PO(2022)0118.

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10 March 2022

**DOCUMENT**

PO(2022)0118

**Silence Procedure ends:  
24 Mar 2022 17:30**

To: Permanent Representatives (Council)

From: Secretary General

**IBAN SPECIAL REPORTS**

**RELATED TO THE CLOSE-OUT OF NSIP PROJECT**

1. I enclose the report by the Resource Policy and Planning Board (RPPB) on two Special Reports from International Board of Auditors for NATO (IBAN) related to the close-out of investment projects funded from the NATO Security Investment Programme (NSIP). The RPPB report at Enclosure 1 also incorporates the Investment Committee assessment and its newly agreed measures aimed at improving transparency, accountability and compliance with agreed close-out procedures.

2. I do not believe that this matter requires discussion in the Council. Therefore, **unless I hear to the contrary by 17:30 hours on Wednesday, 24 March 2022**, I shall assume that the Council has noted the RPPB report and its recommendations and agreed to the public disclosure of the RPPB report and the two IBAN Special Reports

(Signed) Jens Stoltenberg

3 Enclosures

Original: English

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NORTH ATLANTIC COUNCIL

CONSEIL DE L'ATLANTIQUE NORD

## NATO UNCLASSIFIED

17 December 2021

**DOCUMENT**

AC/335-D(2021)0088

**Silence Procedure ends:**

**17 Jan 2022 15:00**

### RESOURCE POLICY AND PLANNING BOARD

#### IBAN SPECIAL REPORTS

#### RELATED TO THE CLOSE-OUT OF NSIP PROJECTS

##### Note by the Chair

1. On Thursday, 25 November 2021, the Board considered the presentations from the International Board of Auditors for NATO (IBAN) related to two Special Reports, one on the new approach to NSIP financial audits and its impact on accountability, and another one on NSIP lump sum conversions. The Board also addressed a report from the Investment Committee presenting its assessment of the two IBAN Special Reports and its newly agreed measures aimed at improving the close-out of NSIP projects.

2. The Board's views are captured in the attached report to Council. As concluded during our meeting, I am seeking agreement to the report under the silence procedure. Consequently, unless I hear to the contrary by **15:00 hours on Monday, 17 January 2022**, it will be assumed that the RPPB can agree the recommendations and to forward the report to Council for notation and approval of the recommendation on the public disclosure as set out in paragraph 8.5.

(Signed) Tomas Graziunas

1 Annex  
1 Enclosure

Action Officer: B. Haane, Ext. 2717  
Original: English

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## IBAN SPECIAL REPORTS RELATED TO THE CLOSE-OUT OF NSIP PROJECTS

### Report by the Resource Policy and Planning Board

References: (a) C-M(2020)0010  
 (b) IBA-A(2021)0047-REV1 & IBA-AR(2021)0002  
 (c) IBA-A(2020)0037 & IBA-AR(2020)0004  
 (d) C-M(2014)0052; C-M(2017)0030; C-M(2020)0045  
 (e) PO(2015)0052

## INTRODUCTION

1. Investment projects funded from the NATO Security Investment Programme (NSIP) are subject to technical and financial close-out processes following physical completion. Experience has shown that in too many cases NSIP project close-out occurs several years after project completion, thus causing a significant backlog of non-inspected and non-audited projects.

2. Over the past two years, there has been renewed focus on NSIP project close-out. The International Board of Auditors for NATO (IBAN) submitted three reports to Council. The first recommended a new approach to NSIP financial audits and was agreed by Council with reference (a). This report was followed up by an IBAN Special Report to describe the experience gained with the new approach (reference (b)). The third report is a Special IBAN Report on NSIP lump sum conversions (reference (c)).

3. The Investment Committee's (IC) assessment of the findings in the two IBAN Special Reports and agreement to some explicit measures to improve Host Nation compliance with NSIP project close-out procedures is presented at Enclosure 1.

## AIM

4. This report highlights the Board's key observations emanating from the two IBAN Special Reports and the related IC assessment.

## DISCUSSION

5. The Board considers that the observations and recommendations in the IBAN Special Reports have been adequately dealt with by the IC. The Board supports the explicit measures agreed by the IC that aim at improving Host Nation compliance in closing out NSIP funded investment projects. The measures represent a step in the right direction.

6. Notwithstanding, the Board expresses serious concern that in too many cases NSIP close-out occurs several years after project completion, causing a significant backlog of non-inspected and non-audited projects. Over the years, these have built up to an amount of

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ANNEX 1  
AC/335-D(2021)0088

EUR 5,000 million. In this context, the Board recalls that the Council mandated a specific tasking in 2014 to close-out all projects that were physically complete at the time within a dedicated timeframe<sup>1</sup> (reference (d)). The Board counts on the IC to fully exercise its governance responsibility to improve the close-out of NSIP projects. Host Nations must fully comply with agreed NSIP procedures and must be held accountable when this is not the case.

7. The Board highlights that not accounting for the use of NSIP funds is not in line with best practice. Governments contributing to NSIP funded investments must be able to satisfy their legislatures and public that their contributions to the NSIP were used in an economically justified manner. Accountability is not only a core value of NATO but also one of the three elements highlighted in the context of the NATO 2030 agenda, along with affordability and sustainability, and the need for efficiency measures. The Board will therefore continue monitoring future developments in this area. Should the new measures not lead to visible progress by the end of 2022, more robust instruments will be needed to improve compliance and accountability in closing out NSIP projects.

**RECOMMENDATIONS**

8. The Resource Policy and Planning Board recommends that the Council:

8.1. note this report and the International Board of Auditors for NATO (IBAN) Special Reports at references (b) and (c);

8.2. note the significant amounts that remain unaudited, and the political and reputational risk that this represents;

8.3. note the new measures agreed by the Investment Committee to improve compliance, transparency and accountability in closing out NATO Security Investment Programme (NSIP) funded investment projects, as set out in paragraph 29 of Enclosure 1;

8.4. note that more robust instruments will be needed should the newly agreed measures not lead to visible progress by the end of 2022;

8.5. agree to the public disclosure of the IBAN Special Report on the new approach to NSIP financial audits and its impact on accountability, the IBAN Special Report on NSIP lump sum conversions and this report in line with agreed policy at reference (e).

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<sup>1</sup> The original tasking foresaw the completion of the tasking by 2016; this date has since been extended twice to now the end of 2022.



NORTH ATLANTIC COUNCIL  
CONSEIL DE L'ATLANTIQUE NORD

**NATO UNCLASSIFIED**

23 November 2021

**DOCUMENT**  
AC/4-D(2021)0011-FINAL

**INVESTMENT COMMITTEE  
IMPROVING NSIP CLOSE-OUT -  
ASSESSMENT OF SPECIAL IBAN REPORTS  
AND AGREEMENT TO NEW MEASURES  
REPORT TO THE RPPB**

**Note by the Secretary**

References: (a) IBA-A(2021)0047-REV1 & IBA-AR (2021)0002  
(b) C-M(2020)0010  
(c) IBA-A(2020)0037 & IBA-AR (2020)0004  
(d) C-M(2014)0052; C-M(2017)0030; C-M(2020)0045

1. Please find attached at Annex 1 the Investment Committee Report on Improving NSIP Close-Out - Assessment of Special IBAN Reports and Agreement to New Measures, agreed by the Committee at its meeting on 23 November 2021. The latest modification to paragraph 29.8 is incorporated in this version, as decided at the meeting.

2. This document presents the Committee's input to the RPPB ahead of the Board's deliberations on two Special Reports by the International Board of Auditors for NATO. Both Special Reports deal with NSIP close-out matters. One report describes the one-year experience gained from application of a new approach to NSIP financial audits (reference (a)), agreed by Council in June 2020 (reference (b)); a second report is on NSIP Lump Sum Conversions (reference (c)).

3. The document further includes, at Appendix 1, an update on the progress achieved since agreement to extend the deadline for completing the close-out of projects that were physically complete in 2014 (reference (d)).

(Signed) E. PASCANU

1 Annex

Action Officer: B. Haane, ext: 2717  
A. Voia, ext: 2430  
Original: English

1 Appendix

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**IMPROVING NSIP CLOSE-OUT –  
ASSESSMENT OF IBAN SPECIAL REPORTS  
AND AGREEMENT TO NEW MEASURES  
REPORT TO THE RPPB**

References: (a) C-M(2020)0010  
(b) IBA-A(2021)0047-REV1 & IBA-AR(2021)0002  
(c) IBA-A(2020)0037 & IBA-AR(2020)0004  
(d) AC/4-D(2020)0009; AC/335-D(2020)0074  
(e) AC/4-DS(2021)0010, item 2.1.1.  
(f) AC/4-WP(2021)0004; -DS(2021)0019, item 1.1  
(g) C-M(2014)0052; C-M(2017)0030; C-M(2020)0045

**INTRODUCTION**

1. Investment projects funded from the NATO Security Investment Programme (NSIP) are subject to technical and financial close-out processes following physical completion. Experience has shown that in too many cases NSIP project close-out occurs several years after project completion, thus causing a significant backlog of non-inspected and non-audited projects. This situation has been a matter of recurring concern to the International Board of Auditors for NATO (IBAN), the Council, the Resource Policy and Planning Board (RPPB) and the Investment Committee (IC) alike.

2. Over the past two years, there has been renewed focus on NSIP project close-out. The IBAN submitted three reports to Council. The first recommended a new approach to NSIP financial audits and was agreed by Council with reference (a). This report was followed up by an IBAN Special Report to describe the experience gained with the new approach (reference (b) refers). The third report is a Special IBAN Report on NSIP Lump Sum Conversions (reference (c) refers).

3. The IC in its own right has agreed to actively consider how the timeliness of NSIP project close-out processes and adherence to existing procedures could be improved. This was done in the context of its agreement to higher Advance Planning Funds and National Administrative Expenditure for projects submitted within the framework of the 2018 agreed Common Funded Capability Governance Model (reference (d)).

4. The Committee decided to address the above work strands as one comprehensive endeavour and invited the International Staff to develop an ambitious and robust approach to enable and sustain a close-out process in accordance with agreed policies and procedures (reference (e)). The Staff's proposals were considered during an IC Working Group meeting on 22 September 2021 (reference (f) refers). The views expressed by Nations form the basis for the IC report to the RPPB.

**AIM**

5. The aim of this report is to present the IC's assessment of the findings in two IBAN Special Reports on NSIP close-out processes and its agreement to some explicit measures to improve Host Nation compliance with NSIP close-out procedures. The report also includes, at Appendix 1, a progress update on the close-out of projects that were physically complete in 2014 and are the subject of a dedicated Council tasking.

**BACKGROUND**

6. The close-out of NSIP-funded investment projects encompasses a technical<sup>1</sup> and financial<sup>2</sup> verification and validation process, and a formal discharge process by the IC. The process involves different stakeholders with distinct roles and responsibilities:

6.1. Implementing Host Nations are responsible and accountable for submitting their requests for technical inspection and acceptance and audit and must do so no later than 12 months following project completion. At each project authorisation stage, the Host Nation further commits to the project-specific submission timelines as part of the overall implementation schedule. Without Host Nation submission, the close-out process cannot start.

6.2. The International Staff undertakes the technical verification and validation and prepares a joint final inspection and formal acceptance (JFAI) report for IC consideration.

6.3. The IBAN undertakes the financial verification and validation and provides an Independent External Auditor's Report for IC consideration on behalf of Council.

6.4. The IC is the responsible governance body for NSIP implementation under its delegated authority from Council. Within this wider role, the IC also discharges Host Nations from their implementation and financial responsibilities. This is done based on a Staff report confirming that the project was implemented in conformity with the authorisation, is physically complete and militarily and technically acceptable, and an IBAN independent assurance on the compliance of NSIP expenditures with regulations in force. The formal Host Nation discharge occurs at two stages, through the IC acceptance of a delivered capability/asset into the NATO Inventory, and through IC notation of a List of Financially Completed Projects.

7. Experience has shown that NSIP project close-out often occurred many years after project completion and thus resulted in a backlog of non-inspected and non-audited projects. In 2014, a backlog of 5 billion Euro of physically complete projects led to a dedicated Council tasking to close these projects by 2016; this deadline has since been extended twice to now

<sup>1</sup> I.e. Joint Final Inspection and Formal Acceptance (JFAI) as per AC/4-D/2074 (1988 Edition).

<sup>2</sup> I.e. financial audit to provide "independent assurance to Council on expenditures incurred by Host Nations on individual investment projects funded by the NSIP in accordance with International Auditing Standards" (IBAN Charter; C-M(2015)0032 refers).



end of 2022 with projects worth 2.2 billion Euro remaining to be closed (reference (g)). The Committee's update to the RPPB on the achieved progress since Council agreement to the extension in December 2020 is provided at Appendix 1.

8. In the meantime, a new backlog of physical complete projects worth 2.5 billion Euro is building up. An assessment of Host Nation submissions between 2010 and 2020 showed that only 35% of requests for technical inspection and only 22% of requests for audit were received within the agreed timelines<sup>3</sup>.

9. These numbers reflect a persistent problem and illustrate that Host Nations do not submit requests for technical inspection and acceptance and audit within set timelines and thus do not act in compliance with Committee agreed procedures. This is not a new situation; delays in NSIP project close-out have been continuously highlighted by the IBAN and resulted in specific Council reports and taskings over the past forty years<sup>4</sup>. Still, these have not led to any tangible and sustainable improvements and, up to now, failure by Host Nations to comply with the close-out timelines has had no consequences.

### **IBAN SPECIAL REPORTS**

10. The IBAN submitted two Special Reports in 2020 and 2021 respectively that address the close-out of NSIP projects. One report describes the experience gained with a new approach to NSIP financial audits (reference (b)), agreed in June 2020 (reference (a) refers); a second report is on NSIP Lump Sum Conversions (reference (c) refers).

#### **IBAN Special Report on the New Approach to NSIP Financial Audits and its Impact on Accountability**

11. The IBAN proposed and Council agreed changes to NSIP financial audits focused on some practical improvements to the audit of NSIP expenditures. The objective was to better align the reporting with the IBAN Charter and the principles of international auditing standards as well as clarifying roles and responsibilities and strengthening overall accountability of NSIP.

12. The new approach was applied for audit reports issued as of 2020. In the past, the IBAN would issue a Certificate of Final Financial Acceptance<sup>5</sup>; these have been replaced by an independent external auditor's report stating an unmodified or modified audit opinion. In 2020, the IBAN issued 72 independent external auditor's reports. Out of 72 audit opinions,

<sup>3</sup> IS-NOR presentations to the IC on 16 March (AC/4-DS (2021)0006, item 3.2.1) and 7 May 2021 (reference (f) refers).

<sup>4</sup> C-M (79)52, C-M (90)46, PO (2013)0253, C-M (2014)0052, C-M (2017)0030 and PO (2018)0259.

<sup>5</sup> Including for projects for which no audit was undertaken and which had been subject to a lump sum conversion decision by the IC.

44 were unmodified and 28 audit opinions were modified<sup>6</sup>. The main reason for issuing modified audit opinions was due to missing documentation. The missing documentation illustrates a second element of non-compliance because Host Nations are responsible for maintaining technical project and financial documentation until the financial audit is complete and they are formally discharged from their Host Nation responsibilities.

13. The IBAN states that in cases of missing documentation, Host Nations are not able to fully account for the NATO common funds received and, as a result, do not fulfil all of their regulatory responsibilities related to the implementation of the NSIP project as expenditures reported in the cost statement cannot be substantiated by relevant documentation. The IBAN therefore considers the expenditures reported not to be compliant with NSIP Regulations and therefore non-eligible from a financial audit perspective, subject to decision by the IC. The IBAN stresses that the NSIP regulations require that financial records and documents are kept until final project closure and discharge of the Host Nation by the IC, on behalf of Council.

14. Other reasons for modified audit opinions related to non-eligible costs claimed, eligible costs not claimed or eligible costs claimed in excess of authorisations. For these cases, the IBAN points out that sufficient verification and internal controls should be in place in Host Nations when preparing the cost statement to avoid similar errors or mistakes occurring in the future.

15. The IBAN further noted that in two of 72 cases Host Nations were technically discharged and the related capabilities accepted into the NATO Inventory despite the fact that there was insufficient information in the JFAI report to confirm whether the project had been implemented in line with the conditions for formal acceptance or that the delivered asset was militarily acceptable. The IBAN took the view that the expenditures reported for those two cases not to be compliant with NSIP Regulations and therefore non-eligible from a financial audit perspective, subject to decision by the IC.

16. In light of its findings, the IBAN recommends to: develop and document a formal discharge procedure setting out more clearly roles and responsibilities of each party in the process (including when the IC refuses the discharge of host nations), and, annual reporting through the RPPB to Council on the (non)discharge granted by IC. The IBAN further

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<sup>6</sup> IBAN issues a modified audit opinion in those case where it detected, *inter alia*, issues of non-compliance of expenditures incurred in the Cost Statement (affecting some or all elements of the Cost Statement), or where the Cost Statement is missing, documentation intentionally not provided or where material uncertainties severely limit the scope of the audit. The IBAN may issue three types of modified audit opinions in line with international auditing standards.

recommends that all tasking decisions by Council should clearly identify those responsible to take action and set deadlines for the delivery of the expected outcomes<sup>7</sup>.

### IBAN Special Report on Lump Sum Conversions

17. Lump sum conversions refer to those “exceptional cases where the accounting documents for works carried out and accepted into the NATO Inventory, no longer existed due to the long time span between the completion of the works and the audit”<sup>8</sup>. Projects for which lump sum authorisations<sup>9</sup> are granted are not subject to audit. An IC decision converting the original authorisation for a completed project *a posteriori* into a lump sum authorisation implies that the respective project would not have to undergo an audit. In the past, the IC agreement to an *a posteriori* lump sum conversion paved the way for the IBAN not to conduct an audit and simply issue a Certificate for Final Financial Acceptance.

18. In its Special Report on NSIP Lump Sum Conversions at reference (c), the IBAN concluded that out of a total amount of 4.3 billion Euro related to closed NSIP projects between 2015-2019, 9% (or 389 million Euro) were financially closed based on an IC lump sum conversion decision for reasons of missing documentation.

19. The lump sum conversion decisions owing to missing documentation came in addition to a further 8% (or 334 million Euro) in lump sum conversions agreed by the IC as a specific measure to accelerate the close-out of long completed projects to be able to comply with the Council agreed close-out timelines at reference (g). In light of a total percentage of 17% (or 723 million Euro) of projects closed following a lump sum conversion, the IBAN concluded that “the use of lump sum conversions is no longer exceptional, but has become common practice”.

20. In light of its findings, the IBAN recommends: to develop and regularly update a compendium of applicable rules related to the NSIP including responsibilities of Host Nations for implementing NSIP projects; formal Host Nation acknowledgement that roles, responsibilities and applicable rules and procedures are understood; Host Nation confirmation that their archiving policies are fully aligned with NSIP rules or, if not, that these are adjusted accordingly; introduction of a mechanism to improve Host Nation accountability for timely project closure including through the withholding of project management funds; and, to ensure that all NSIP funded projects are subject to audit.

<sup>7</sup> In the context of its advice to the Council on the Handling Arrangements for 2020 Financial Statements Audit Reports, the RPPB expressed concerns regarding the qualified opinions and open observations especially those that have remained open for more than three years. It therefore invited the IS-NOR, in coordination with IBAN, to advise the Board whether further discussion with the management/governance of those entities or more focused Board recommendations to Council are necessary to accelerate actions on those outstanding items (AC/335-D(2021)0044-REV1 refers).

<sup>8</sup> AC/4-D/2948 & Addendum; AC/4-R/751 refer.

<sup>9</sup> A lump sum is defined as a fix, final comprehensive authorisation reflecting all cost elements (AC/4-D/2948 refers).

**ASSESSMENT**

21. The Committee welcomes both IBAN Special Reports as a pertinent and timely contribution to its own deliberations on how to improve NSIP close-out. First of all, the Committee reiterates that Host Nations are accountable to submit a request for JFAI and audit within explicit timelines. These are clearly spelled out: Host Nations must submit a request for JFAI as soon as the works are completed and in any case not later than six<sup>10</sup> months after project completion<sup>11</sup>. Host Nations must further submit a request for audit not later than six months following the JFAI request<sup>12</sup>.

22. In terms of formal acknowledgement, the JFAI and audit timelines are part of the project's implementation schedule, and at each authorisation stage, the Host Nation formally commits to adhere to these timelines or is otherwise under the obligation to inform the IC of any significant changes in the agreed schedule. The Committee expects Host Nations to follow the agreed timelines and adhere to the obligation to retain project documentation until a Host Nation is discharged from its responsibilities.

23. The Committee strongly welcomes and supports the IBAN decision to audit all NSIP projects regardless of whether documentation is missing or incomplete. Looking at the significant number of lump sum conversions granted over the past years, the Committee recognises that this could give an impression of laxness. On the other hand, it is important to note that prior to mid-2020, when the IBAN agreed its changed approach to also audit projects with incomplete/missing documentation, an *a posteriori* lump sum conversion was believed the only alternative to financially close out an NSIP project with incomplete or missing documentation.

24. As responsible governance body for NSIP implementation, the Committee is firmly committed to improve financial accountability and to exercise firm stewardship over the NSIP. As part of this important role, the IC ensures and actively monitors that Host Nations comply with their close-out responsibilities and adhere to agreed policies and procedures. In this vein, the Committee established a distinct monitoring mechanism whereby it is presented at every other IC meeting with a progress update of the close-out status of projects that are subject to the dedicated Council tasking at reference (g).

25. The Committee acknowledges that NSIP close-out processes are not followed in line with set timelines and recognises that without measures a rapid improvement to the current situation is not to be expected. The Committee is thus strongly in favour of any measure that positively encourages and enables, through a better understanding of NSIP rules and

<sup>10</sup> Three months for Alliance Operations and Mission projects.

<sup>11</sup> Project completion is defined as "The project completion date is the date on which technical acceptance (provisional or not) vis-à-vis the contractor (or contractors) is performed by the Host Nation, i.e. the date on which the Host Nation checks that the works have been built according to the contract (or contracts) specifications." (Implementation Management Procedure – AC/4-D(2017)0006-FINAL refers).

<sup>12</sup> Implementation Management Procedure – AC/4-D (2017)0006-FINAL refers.

procedures, Host Nation compliance and brings full transparency to governance on Host Nation close-out activities including through additional and more focused reporting.

26. On the other hand, the Committee also recognises that adherence to close-out processes poses challenge to territorial Host Nations in particular. It considers that this has several reasons: lack of staff within territorial Host Nations to perform the close-out processes in a timely manner, a too limited level of project management funding which is considered inadequate to resource the required close-out activities, insufficient focus within Host Nation organisations owing to other, national priorities, and, finally, situations outside the Nations' control such as claims or lawsuits prohibiting close-out. The latter are considered isolated exceptional cases. With a view to enabling a timely close-out of these cases as well, the IBAN could be approached to undertake a partial audit pending the outcome of the claim or lawsuit. Some Nations have also advocated undertaking a root cause and problem analysis prior to considering any more substantial measures.

27. In discussing different measures put forward by the Staff, several Nations indicated that they would have great difficulty to agree to any measure that would involve the financial retention, or deauthorisation, of funds. The Staff had recommended promoting timely Host Nation submissions for JFAI and audit through retention of funds at the authorisation stage and strengthening accountability through deauthorisation of funds when Host Nation submissions are lacking and no explanation is provided, and where the IBAN issues a modified opinion.

28. Nonetheless, the Committee is committed to initiate a number of measures that encourage Host Nation accountability and compliance with NSIP rules and procedures. These include a more nuanced approach in those cases where there is insufficient information at the JFAI stage to confirm whether a given project had been implemented in line with the conditions for formal acceptance or that the delivered asset was militarily acceptable applicable. The current approach foresees that if a project is physically completed and there are no outstanding deficiencies, the delivered capability/asset would normally be accepted into the NATO Inventory. This would have also been the case in those circumstances when the delivered product did not fully meet the user's requirements<sup>13</sup>.

## **NEW MEASURES TO IMPROVE NSIP CLOSE-OUT**

29. In light of its assessment and taking into account the IBAN findings, with the present document the IC agree to the following measures that aim at improving visibility, transparency and accountability and that put in place additional safeguards to avoid incomplete/missing documentation:

<sup>13</sup> For future projects implemented under the 2018 agreed Common Funded Capability Delivery Governance Model, a project not delivering the expected capability should not normally occur. This is owing to the close Host Nation – User interaction within the Capability Management Function and because any deviations would have been identified during the implementation process or identified during user acceptance.

29.1. For all projects subject to an IBAN independent auditor's report with a modified opinion, the IC will decide whether to discharge a Host Nation or not in light of the nature of the IBAN modified opinion. Up to now, all Host Nations have been systematically discharged from their technical and financial responsibilities no matter the results of the audit and the level of completeness of the JFAI and audit documentation. The related projects for which no Host Nation discharge was granted will still be closed but recorded in CIRIS and reported on as a separate category.

29.2. The Committee will no longer agree to a *posteriori* lump sum conversions. In the past, Host Nation requests for lump sum conversions were directly submitted to the IS-NOR, and the IS-NOR prepared a report for the Committee's consideration. Host Nations should submit all projects for audit regardless of whether the related financial documentation is incomplete or missing. This provision is applicable to all projects that are not yet financially closed<sup>14</sup>. Based on the modified opinion in the independent external auditor's report and the Host Nation justification, the Committee will decide whether to discharge a Host Nation from its responsibilities or not.

29.3. In cases where the JFAI report revealed insufficient information to confirm whether the project had been implemented in line with the conditions for formal acceptance or that the delivered asset was militarily acceptable, the IC will invite ACO, as the accountable user, to confirm the operational usability of the equipment covered by the JFAI report. Based on the user confirmation, the Committee will decide whether a Host Nation will be discharged or not.

29.4. The Committee's new approach to discharge or not a Host Nation from its technical and financial Host Nation responsibilities requires procedural clarity. As recommended by the IBAN, the IC invites the International Staff to develop and document a formal discharge procedure setting out more clearly roles and responsibilities of each party in the process, including when the IC does not discharge a Host Nation. This procedure should also comprise an administrative process to ensure that the related projects do not stay 'on the books' and are closed out. Given that this is a new approach, the new procedure should take into account the lessons identified with the new approach and be agreed no later than end-2022. In the interim, the International Staff will develop clear recommendations in the Committee's decision-making documents.

29.5. The IS-NOR produces quarterly reports on missed implementation milestones. In the future, the International Staff will prepare additional reporting with a focus on completed projects, organised by Host Nation. The Committee invites the International Staff to implement this new measure starting 2022. This reporting will enable the Committee to hold Host Nations to account by seeking clarifications for a significant number of outstanding JFAI and audit requests or long-overdue requests.

29.6. The annual NSIP Financial Activity Reports as at end of December of a given year already provide visibility on the number of closed NSIP projects and a posteriori lump sum conversions granted by the IC. In the future, this report should also include information to illustrate which Host Nations were discharged from their Host Nation responsibilities and

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<sup>14</sup> This will also include 79 projects from NCIA with a total value of 701 million Euro.

which were not. This is to provide visibility and strengthen accountability both of which represent key elements of good organisational governance. The Committee invites the International Staff to implement this new measure starting with the 2021 report. In response to the IBAN recommendation to provide additional visibility to the Council, the IC will send its annual report to the RPPB ahead of the Board's and Military Committee's deliberations on its joint annual report to Council.

29.7. The IC invites its Chair to send a letter to all Host Nations, at senior responsible official level, presenting an overview of their respective projects which require close-out and highlighting the importance to comply with NSIP rules and procedures. A similar approach was followed in 2020 to encourage improvements to Host Nation forecasting.

29.8. The IC will consider introducing, as a mitigating measure against the possible loss of contract documentation, a new approach whereby Host Nations could be invited in the future to upload contract-related information via a template when recording their contract notification in CIRIS. Such a measure would enable Host Nations to access their contract-related information at project completion, if not retained in-house, and could serve as an opportunity to streamline the requirements for contract notification recordings in CIRIS. The Committee invites the International Staff to prepare such a template for further Committee deliberation in early 2022.

29.9. The IC reiterates that the International Staff is due to review the 2012 NSIP Manual<sup>15</sup>, notably to reflect the changes in roles and responsibilities arising from the 2018 agreed Governance Model. In light of the IBAN recommendation, the IC invites the International Staff to put a particular focus on applicable rules related to the NSIP including responsibilities of Host Nations for implementing NSIP projects.

29.10. With a view to ensuring compliance with NSIP retention rules, invite Host Nations to confirm in a letter to the IC Chair by 31 March 2022 that their archiving policies are fully aligned with NSIP rules or, if not, what steps will be undertaken to adjust these accordingly.

## RECOMMENDATIONS

30. The Resource Policy and Planning Board is invited to:

30.1. note the IC assessment of the findings on the IBAN Special Reports on NSIP close-out processes as a contribution to the Board's deliberations on the IBAN Special Reports;

30.2. note the IC progress update at Appendix 1 on the close-out of projects that were physically complete in 2014 and that are the subject of a dedicated Council tasking;

30.3. note the IC agreed measures to improve Host Nation compliance with NSIP close-out processes.

<sup>15</sup> IC Operationalisation Roadmap for the Common Funded Capability Delivery Governance Model (AC/4-N(2019)0027-REV2 refers.

**CLOSE-OUT OF COMPLETED PROJECTS**  
**SITUATIONAL UPDATE AS AT OCTOBER 2021**  
**REPORT TO THE RESOURCE POLICY AND PLANNING BOARD**

References: (a) C-M(2014)0052  
(b) AC/4-N(2017)0011-FINAL (INV)  
(c) C-M(2017)0030  
(d) AC/4-N(2020)0021-FINAL  
(e) C-M(2020)0010  
(f) C-M(2020)0045  
(g) AC/4(PP)N(2015)0024+ADD1+ADD2+ADD3+ADD4  
(h) AC/4(PP)N(2016)0068+ADD1+ADD2+ADD3+ADD4

**INTRODUCTION**

1. In August 2014, as part of the assessment of the International Board of Auditors for NATO (IBAN) report on the Audit of the NATO Security Investment Programme (NSIP) for 2012, the Investment Committee (IC) received a Council tasking to close, by mid-2016, projects that were physically complete by mid-2014 (reference (a)). At that time, these physically completed projects had an estimated value of € 5 billion.

2. The Committee provided an update on the tasking and requested an extension of the deadline to 2020 (reference (b)). The Resource Policy and Planning Board (RPPB) agreed the proposed extension, and Council endorsed it at reference (c).

3. In 2020, the Committee requested an additional extension of the tasking deadline to end 2022 (reference (d)). The report noted that close-out efforts were impacted by the COVID-19 pandemic as well as by the implementation of the new audit procedure (reference (e)). The RPPB agreed the request and Council endorsed the Board's recommendation at reference (f).

**AIM**

4. The 2020 situational report (reference (d)) foresees updates from the Investment Committee to the Board on achieved progress. Therefore, the purpose of this report is to provide information on the status of projects in the tasking as at October 2021, as well as to provide information on actions taken by the Committee.

**BACKGROUND**

5. The Investment Committee agreed on dedicated action plans to comply with the Council tasking and to monitor its progress (references (g) and (h)). The approach taken was to treat the closure of completed projects in support of ISAF and of completed NSIP projects programmed before 2011 as separate exercises. The overall value to be closed was approximately € 5 billion as depicted in the next table:



Close-out exercise	No. of sub-projects	Value	Status
ISAF Projects	530	€ 1.5 billion	Completed
Projects programmed before 2011	1,111	€ 3.6 billion	Ongoing

## SITUATION UPDATE AS AT OCTOBER 2021

6. With the ISAF portion closed (as per reference (d)), the present update focuses on the projects programmed before 2011 that are as part of the close-out tasking. This work strand includes **1,111 sub-projects** with a value of approximately **€ 3.6 billion**, managed in four categories:

- projects with an authorised amount below € 3 million;
- projects with an authorised amount above € 3 million;
- projects that were technically accepted (or partially accepted) at the time the close-out exercise began; and
- “special cases” for projects that do not fit any of the three categories above (for example projects that needed to be de-programmed or that reported operational deficiencies at the time of the technical acceptance).

7. The two tables below present an overview of projects programmed before 2011 that are part of the tasking. The summary information relates to the full list of projects, from the technical acceptance (JFAI<sup>16</sup>) and financial closure perspective.

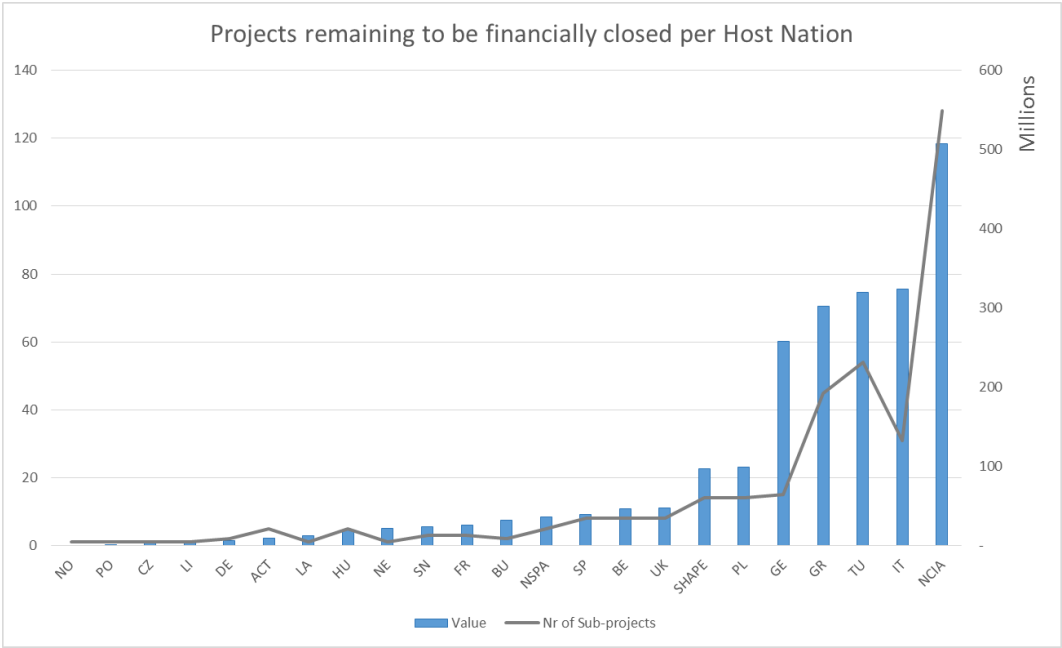
Close-out overview	
of 1,111 projects:	of € 3.6 billion:
JFAI'd	
87%	75%
Financially closed	
68%	38%

Close-out category	Number of Sub-projects	Value (MEUR)	JFAI perspective			Financial Closure perspective		
			HN to Submit	Submitted not yet JFAI'd	JFAI'd	HN to Submit	Submitted not yet Financially Closed	Financially Closed
Below EUR 3M	357	199	0	0	357	0	0	357
Above EUR 3M	196	1,427	35	41	120	106	75	15
Already JFAI'd (or partially JFAI'd)	374	1,629	11	6	357	34	53	287
Special cases	184	337	25	24	135	67	21	96
<b>TOTAL</b>	<b>1,111</b>	<b>3,592</b>	<b>71</b>	<b>71</b>	<b>969</b>	<b>207</b>	<b>149</b>	<b>755</b>
			Value (€ million)			Value (€ million)		
			484	429	2,680	1,459	782	1,350

<sup>16</sup> JFAI stands for Joint Formal Acceptance Inspection which is the technical acceptance of NSIP projects

8. As of October 2021, 356 sub-projects with a value of approximately € 2.2 billion are pending closure. The next sections of the paper provide further breakdowns of these projects.

9. The figure below depicts projects pending closure and provides information on the financial volume and the number of sub-projects for each Host Nation. The information is organized by financial volume, with the higher values on the far right of the chart.



10. The next section includes a summary table from the JFAI and Audit perspective. This information complements the figure presented under the previous paragraph, by showing where these projects are in the closure process.

Close-out overview	JFAI Status			Audit Status		
	HN to submit	Submitted not yet JFAI'd	JFAI'd	HN to Submit	Submitted not yet Audited <sup>17</sup>	Audit Completed
No. of sub-projects	71	71	214	207	87	62
Value (€ million)	483	429	1,329	1,459	454	327
To close: € 2.2 billion; 356 sub-projects						

<sup>17</sup> Of this group, projects with a value of ~ € 109 million are pending JFAI acceptance; therefore, an audit will be planned once the projects are technically accepted.

**CONSIDERATIONS**

11. With the tasking deadline of end-2022 rapidly approaching, the technical acceptance portion of the process seems to be on a better track than the financial closure. To date, concerning the portion pending closure (€ 2.2 billion), about 60% of the projects have undergone a full JFAI; in terms of value, this amounts to about 59%. This is not the case for the financial closure, where the opposite applies, with about 58% of projects pending an audit request; in terms of value, this represents about 65%. However, considering that the deadline is in approximately one year, the submission pace needs to increase significantly for both JFAI and audit stages. Looking at past submission trends, the target cannot be met unless efforts to complete the tasking are increased.

12. Bearing in mind that the audit takes place after technical acceptance, and to allow time for subsequent activities, it is important that outstanding JFAIs are processed as soon as possible. It is also worthwhile to note that Host Nations are not required to wait for the JFAI report in order to submit an audit request.

13. The Committee is closely monitoring the situation in the form of regular status updates. This has been set up as of end-May 2021 and the updates occur every other IC meeting. The Committee receives overviews on the projects pending full closure and on the number of requests for JFAI and Audit received since the previous update.

14. Additionally, during June 2021, the IC Chair initiated a series of meetings with representatives from Nations, concentrating on Nations with high value projects in their list (above € 20 million). As shown in the chart under paragraph nine, a significant portion of the value pending closure is divided among few Nations. The aim of the meetings was to achieve some immediate results by focusing on projects with a high value. Naturally, the effort to close these projects is not limited to Nations having high value projects; all Host Nations that have outstanding actions are to submit requests as soon as possible in order to meet the deadline.

15. The result of these meetings is still materializing; however, Nations expressed their commitment to complete the tasking. During the June-October interval, the value of projects pending a JFAI submission decreased by 28%. Throughout the same period, the value of projects for which an audit was requested increased by 10%.

16. These are good signals; however, a significant workload lays ahead of stakeholders. The Committee continues to closely monitor the situation and the IC Chair resumed, in October, the series of bilateral meetings on the topic with representatives of nations with pending high-value projects. The Chair equally foresees to coordinate and send to these nations, on behalf of the IC, written communications to increase the momentum and visibility on the tasking and its deadline, and emphasise the specific actions that can help improve close-out for their respective portfolios.

17. The Committee will keep the Board informed on progress at the beginning of 2022.



NORTH ATLANTIC TREATY ORGANIZATION  
ORGANISATION DU TRAITÉ DE L'ATLANTIQUE NORD  
INTERNATIONAL BOARD OF AUDITORS  
COLLÈGE INTERNATIONAL DES AUDITEURS EXTERNES DE L'OTAN

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ENCLOSURE 2  
PO(2022)0118

IBA-A(2021)0047-REV1  
19 May 2021

To: Secretary General  
Attn: Director of the Private Office

Cc: NATO Permanent Representatives  
Supreme Allied Commander Europe  
Supreme Allied Commander Transformation  
General Manager, NATO Support and Procurement Agency  
General Manager, NATO Communication and Information Agency  
Financial Controller, Allied Command Operations  
Financial Controller, Allied Command Transformation  
Financial Controller, NATO Support and Procurement Agency  
Financial Controller, NATO Communication and Information Agency  
Chairman, Resource Policy and Planning Board  
Chairman, Investment Committee  
Resource Policy and Planning Board representatives, NATO delegations  
Private Office Registry

Subject: ***International Board of Auditors for NATO (IBAN) Special Report on the new approach to NATO Security Investment Programme financial audits and its impact on accountability – IBA-AR(2021)0002***

IBAN submits herewith its approved Special Report for distribution to the Council.

Yours sincerely,

Daniela Morgante  
Chair

Attachment: As stated above.

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# IBAN SPECIAL REPORT

on the new approach on NATO Security  
Investment Programme (NSIP)  
Financial Audits and its impact on  
accountability

**FOREWORD BY THE CHAIR**

On behalf of the International Board of Auditors for NATO, it is my pleasure to share with you the Special Report to Council on our new approach to NATO Security Investment Programme (NSIP) financial audits and its impact on accountability.

The Report sets out the main changes approved by Council in June 2020 and their purpose, the main findings arising in the first year of implementation in 2020, the impact on accountability of the new approach, as well as recommendations for improving overall NSIP accountability.

The NSIP is NATO's core capital investment programme. It is an essential common funded resource pillar, designed to enhance and upgrade NATO assets, in order to obtain military capabilities that exceed national defence requirements of individual Nations. In June 2018, NATO adopted a new governance model for common funded capability delivery, which, among others, aims to ensure clearer roles, responsibilities and increased accountability. IBAN believes that the new approach to NSIP financial audits contributes to further strengthening the overall accountability of NSIP from a corporate governance perspective, as well as to clarifying the responsibility of Host Nations, governance, and external audit.

Through this more innovative and informative way of reporting, our goal is to further enhance Council's ability to oversee and account for the NSIP, thereby strengthening the transparency and accountability of the use of NATO's resources.



Daniela Morgante  
Chair  
International Board of Auditors for NATO

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## 1. INTRODUCTION AND BACKGROUND

### 1.1 IBAN's mandate regarding NSIP audits

1.1.1 In accordance with Article 1 of its Charter, the International Board of Auditors for NATO (IBAN) is mandated to audit the NATO Security Investment Programme (NSIP) on behalf of the North Atlantic Council (the Council). IBAN's mandate regarding NSIP audits covers NATO member Nations as well as NATO entities receiving common funding from NSIP. The function of IBAN regarding NSIP in accordance with Article 2 of the IBAN Charter is:

*“To provide independent assurance and advice to the Council and, through their Permanent Representatives, the Governments of member countries that [...] the expenditures incurred by member countries (Host Nations) or NATO bodies in respect of the NSIP have been carried out in compliance with the regulations in force (NSIP audit).”*

1.1.2 IBAN may also, through its performance audits, analyse and evaluate the economy, efficiency and effectiveness of the programme's management and procedures.

### 1.2 Report objective

1.2.1 In accordance with Article 14 of its Charter, IBAN may issue a special report to Council on any relevant matter it considers to be worthy of attention. The objective of this report is to provide Council with a first overview of the new approach to NSIP financial audits approved by Council in June 2020 and its impact on accountability as well as identifying ways to improve overall accountability. The report sets out the main changes and their purpose, the main findings arising in the first year of implementation in 2020, the first impact on accountability of the new approach as well as recommendations for improving overall accountability. The data used in this report is based on auditor's reports issued in the period June-December 2020.

### 1.3 The purpose of NSIP and IBAN's role in auditing NSIP expenditures

#### The purpose of NSIP

1.3.1 Established in 1951, the NSIP is NATO's core capital investment programme. It is an essential common funded resource pillar, designed to enhance and upgrade NATO assets in order to obtain military capabilities that exceed national defence requirements of individual Nations. The Nations share the NSIP costs with an agreed percentage for each participating Nation.

1.3.2 The programme funds the development, construction and implementation of military capabilities required by the Strategic Commanders to complete their missions. Common funding eligibility rules state it will focus on the provision of infrastructure requirements, which are over and above requirements that could be expected to be made available by individual Nations. For example, NSIP can be used to provide, restore or enhance fixed infrastructure (such as new buildings or repairing airfields), communication information



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system (CIS) equipment (such as new software and hardware) or deployable strategic equipment (such as military transport vehicles). NSIP may also fund Alliance Operations and Mission (AOM) requirements based on special eligibility rules where common funds are provided to cover costs that are not attributable to a single nation.

1.3.3 Apart from Council, the NSIP main stakeholders include the Resource Policy and Planning Board (RPPB), the Investment Committee (IC), the Military Committee (MC) and the Strategic Commands, supported by the International Staff (IS) and International Military Staff (IMS), and Host Nations. NSIP projects are implemented by a NSIP Host Nation which can be the country on whose territory the project is implemented or a NATO agency or Strategic Command. Host Nations are responsible for managing the implementation of authorised projects.

1.3.4 In June 2018, Council agreed on a new governance model for common funded capability delivery (PO(2018)0259). The model is expected to improve governance aspects of common funded capability delivery, accelerate delivery of common funded capabilities as well as ensuring clearer roles, responsibilities, and increased accountability. The model is applied to all new common-funded capabilities and programmes and existing projects will be adapted as per the RPPB and MC agreed transition approach (AC/335-D(2021)0011-FINAL; IMSM-0051-2021).

IBAN's role in auditing NSIP expenditures

1.3.5 IBAN's mandate to audit NSIP expenditures dates back to the early 1950's when Council established two separate audit Boards; the Board of Auditors for NATO Accounts and the International Board of Auditors for Infrastructure Accounts. The main reason for the establishment of an audit mechanism regarding expenditures on investment projects was the need for a procedure by which the member Nations would receive final clearance for the total expenditures charged to common funding in respect of individual projects.

1.3.6 IBAN's role in auditing NSIP expenditures is important for accountability purposes as our independent assurance on the compliance of NSIP expenditures with regulations in force allows the IC, on behalf of Council, to formally discharge Host Nations from financial responsibility. Therefore, since 1958, IBAN issued Certificates of Final Financial Acceptance (COFFAs) to the Host Nations after auditing individual projects on their request. Based on these COFFAs and the IC notation of a list of financially completed projects, the IC discharged Host Nations from their responsibilities on individual projects, on behalf of Council.

1.3.7 However, the issuance of these COFFAs, based on procedures dating back to 1958, no longer reflected current applicable auditing standards of the International Organisation of Supreme Audit Institutions (INTOSAI), which IBAN applies as required by Article 15 of our Charter. In light of the new governance model, IBAN decided to review its role in auditing NSIP expenditures in order to address any inconsistencies and at the same time strengthen roles and responsibilities around the discharge of accountability.

## 2. IBAN'S NEW APPROACH TO NSIP FINANCIAL AUDITS

### 2.1 Introduction

2.1.1 In 2019, IBAN made a proposal to Council with some practical improvements to the audit of NSIP expenditures, with no changes to the core task established by our Charter. On 02 June 2020 (C-M(2020)0010), Council approved the changes and IBAN immediately implemented them.

### 2.2 The main changes and their purpose

2.2.1 The purpose of this new approach is to better align the reporting of the audit of NSIP expenditures with our Charter and with international auditing standards and to contribute to the strengthening of NSIP responsibility, accountability and transparency. The main changes can be categorised into two areas: (1) assurance provided to Governance on expenditures presented in the cost statements and (2) Host Nation's responsibility for the preparation of a cost statement.

#### Assurance provided to Governance on expenditures presented in the cost statements

2.2.2 As the external auditor, IBAN provides independent assurance to governance level that NSIP expenditures incurred by member countries or NATO entities (Host Nations) are carried out in compliance with the regulations in force. This independent assurance assists governance in discharging Host Nations from their financial responsibilities for their projects.

2.2.3 The main change proposed by IBAN and approved by Council is the replacement of the COFFA with an Independent External Auditor's Report providing an audit opinion and audit findings, if any. This document serves as input to the IC allowing them, on behalf of Council, to decide on the discharge of Host Nation responsibilities, including financial closure of the project. From IBAN's perspective, expressing an audit opinion rather than delivering an audit certificate is in accordance with the Charter and more in line with modern international auditing standards. Furthermore, an audit opinion is better designed to provide assurance to governance bodies in order to discharge responsibility and accountability.

2.2.4 Differently from the old COFFA, the new audit report provides a stronger regulatory framework for our audits of NSIP expenditures, in line with international auditing standards and without changing our core task established by our Charter and the underlying financial audit work. The Independent External Auditor's Report clearly sets out the scope and objective of the audit, the audit opinion and the basis for the opinion, the auditor's responsibility for expressing an independent opinion and the responsibility of the Host Nation.

2.2.5 In the Auditor's report, IBAN provides an audit opinion which may be unmodified or modified. IBAN expresses an unmodified audit opinion when our audit finds nothing that causes us to believe that the expenditures incurred were not carried out in compliance with the NSIP Regulations in force. A modified opinion is expressed if, for example, expenditures incurred did not comply with NSIP Regulations or if the impact of missing documentation is so pervasive and material that IBAN concludes that all expenditures incurred did not comply

with NSIP Regulations. The different types of audit opinions that we issue are presented in Appendix 2 to this Report.

2.2.6 Currently, we issue the Independent External Auditor's Report to the IC, which acts on behalf of Council, copying the Host Nation, whereas the old COFFA was submitted only to the Host Nation. By reporting to Council, through the IC, we adhere to our Charter and, at the same time, increase transparency to governance on the result of the audit and the independent assurance provided. This also serves as input to the discharge process.

#### Host Nation's responsibility for the preparation of a cost statement

2.2.7 Clear roles and responsibilities are an important element in ensuring accountability of Host Nations. According to NSIP Regulations, a Host Nation is responsible and accountable for the implementation of the NSIP project. This includes the responsibility for maintaining complete records and documentation to fully justify expenditures incurred and to allow for an audit. It also includes the responsibility for the preparation of a cost statement with all expenditures incurred for the project implementation, and for submitting it to IBAN for audit.

2.2.8 One other change proposed by IBAN and approved by Council is the requirement for Host Nations to sign the cost statement prior to submitting it for audit. Previously, this was not a requirement and IBAN would audit un-signed cost statements. Cost statements are the means through which the Host Nation presents a completed project for financial audit and we consider signed cost statements to be an essential requirement for our audit. By signing the cost statement, the Host Nation confirms that sufficient verification and internal controls are in place to ensure that all expenditures incurred are complete, correct, and compliant with the terms of the authorisation and NSIP Regulations agreed by the IC.

2.2.9 Furthermore, on 09 January 2020, the IC agreed to a cost statement template as guidance for Host Nations, including the need to sign the cost statements. A responsible staff member at an accountable level (authorised representative) from the Host Nation should sign the cost statements.

2.2.10 We believe the above signatory process assists in clarifying the financial responsibility of the Host Nation in relation to incurring expenditures on NSIP projects and it strengthens the accountability of Host Nations. IBAN includes the signed cost statements with our Independent External Auditor's Report, which further provides visibility and transparency to governance on NSIP project expenditures. Under the old COFFA approach, the cost statement was submitted to IBAN for the audit, but not to governance.

### **2.3 Main findings from our audits under the new approach**

2.3.1 IBAN implemented the new approach to NSIP financial audits as from June 2020 and 2020 was therefore the first year when we issued the Independent External Auditor's Report and did not issue COFFAs any longer. In cooperation with the International Staff's NATO Office of Resources, some system changes were also made to the Common Funded Integrated Resources Information System (CIRIS) to adapt to the new audit approach.

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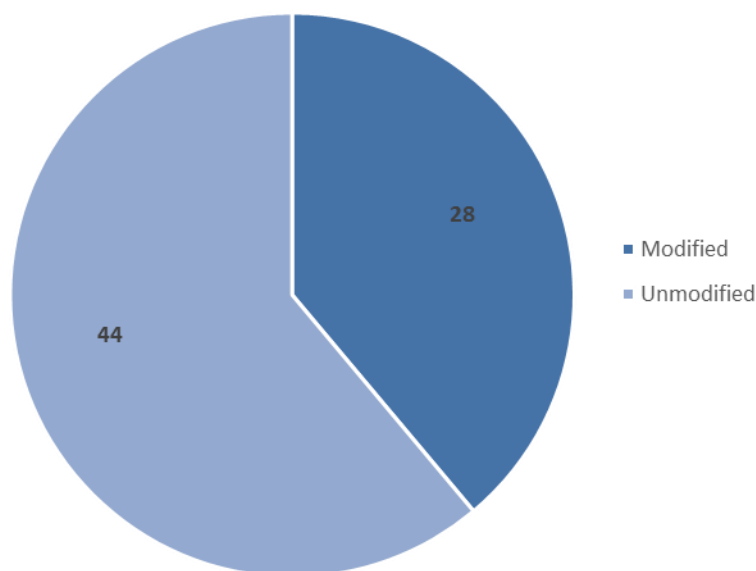
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2.3.2 This section provides an overview of the main findings from our audits in 2020 under the new approach. Such overview makes it possible to draw since now some important, although initial, conclusions on common issues regarding NSIP financial audits under the new approach.

2.3.3 The new audit approach did not fundamentally change the way we audit NSIP expenditures. IBAN's NSIP financial audit involves, among other things, conducting financial audit fieldwork at the premises of the Host Nation, establishing extensive dialogue and interaction with the Host Nation, and reviewing detailed supporting documentation for the expenditures incurred and presented in the project cost statement.

2.3.4 In 2020, we issued 72 auditor's reports on Cost Statements presented by member countries or NATO entities (Host Nations). Out of 72 audit opinions issued by IBAN, 44 were unmodified and 28 were modified. The 44 unmodified audit opinions concerned well prepared and documented cost statements where all expenditures were compliant with the regulations in force. As a percentage of the total number of issued auditor's reports, 61% had unmodified audit opinions and 39% had modified audit opinions. Of the 28 modified audit opinions, 11 related to territorial Host Nations and 17 related to NATO entities. Chart 1 below shows the total number of auditor's reports issued in 2020 by type of audit opinion provided.

**Chart 1: Total Number of Auditor's Reports issued in 2020 by type of Audit Opinion**



Source: IBAN data

2.3.5 The reasons for providing modified audit opinions were basically due to missing documentation, non-eligible costs claimed, eligible costs not claimed, or eligible costs claimed in excess of authorisations. The 28 modified audit opinions contained 29 audit findings. The table below provides an overview of the different types of audit findings.

**Table 1: Overview of Audit Findings by Category**

IBAN Audit finding per category	Total number of IBAN findings	
	Territorial Host Nation	NATO Entity
1. Missing documentation	2	17
2. Non-eligible costs claimed	4	
3. Eligible cost not claimed	1	
4. Eligible cost in excess of authorisation	5	
	29	

Source: IBAN data

*Missing documentation*

2.3.6 Missing documentation accounted for 68% of the modified audit opinions issued by IBAN in 2020. This concerned also cases where a long time between the physical completion of the project and its technical acceptance and financial audit had elapsed, as well as cases of re-organisations or restructurings within the Host Nations. The NSIP Regulations require that financial records and documents are kept until final project closure, audit and discharge of the Host Nation by the IC, on behalf of Council. In these cases, Host Nations were not able to fully account for the NATO common funds received and, as a result, did not fulfil all of their regulatory responsibilities related to the implementation of the NSIP project.

2.3.7 When supporting documentation, such as the signed contracts, amendments, bidding documentation and contract award decision reports are missing and therefore expenditures reported in the cost statement are not adequately supported, we consider the expenditures to be non-compliant with NSIP Regulations and therefore non-eligible from a financial audit perspective, subject to decision by the IC. Because of the missing documentation affecting some or all elements of the cost statement by a scope limitation, we are not able to verify whether the expenditures incurred were within the authorised scope or whether the bidding procedure carried out complied with the authorised method of procurement. Typically, invoices provide only limited information about the scope of work and therefore, contracts, amendments, change orders, acceptance reports and other documents detailing the work performed are key elements in a financial audit of NSIP projects.

2.3.8 Prior to the financial audit of the cost statement, a Joint Final Inspection and Formal Acceptance (JFAI) of NSIP funded projects is performed. The inspection constitutes formal agreement that the works are physically complete and militarily and technically acceptable, and that the responsibility of the Host Nation for completion of the works has been fully discharged (AC/4-D/2074(1988 Edition)). IBAN performs the financial audits only after a final JFAI is approved by the IC, covering the full scope of the project. The JFAI report forms

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part of our financial audit evidence to support the underlying expenditures incurred and presented in the cost statement.

2.3.9 In two out of the 19 modified audit opinions related to missing documentation, IBAN noted that the JFAI report concluded that the works did not meet the conditions for formal acceptance. This was because there was not sufficient information to establish if the implemented works met the conditions for formal acceptance laid down in AC/4-D/2074(1988 Edition) or if the asset delivered was deemed not acceptable from a military point of view. The IC formally accepted the JFAI report and its conclusion. Formal acceptance allows the project to be financially closed. In these cases, from a financial audit perspective, IBAN considers that the expenditures reported in the Cost Statement are not compliant with NSIP Regulations and therefore non-eligible from a financial audit perspective, subject to decision by the IC.

2.3.10 In the past, when key documentation was missing, thus not allowing us to issue a COFFA, IBAN would not perform an audit. This was because the COFFA was a certificate certifying that project expenditures were incurred and settled in compliance with NSIP Regulations. However, the COFFA approach did not allow for situations where IBAN would have audit findings and therefore not be in a position to confirm full compliance with NSIP Regulations. Under the COFFA approach, in situations where key documentation was missing, IBAN would therefore not provide independent assurance to governance assisting them in deciding on the discharge of the Host Nation. Instead, the Host Nations would directly request the IC to approve a conversion of reported expenditures into a lump sum amount, without the involvement of IBAN.

2.3.11 With the new audit approach to NSIP financial audits, IBAN will systematically perform the financial audit and provide independent assurance to governance on expenditures incurred and their compliance with regulations in force, regardless of the existence of documentation. The independent assurance is provided in the form of an audit opinion, which may or may not be unmodified depending on the result of the audit. This is in line with our Special Report to Council on NSIP Lump Sum Conversions (IBA-AR(2020)0004), where we recommended Council to ensure that all NSIP funded projects are subject to a financial audit.

Non-eligible costs claimed

2.3.12 Audit findings under this category refers to cases where some expenditures presented in the cost statement are not eligible according to NSIP Regulations or the specific project authorisations. For example, expenditures outside of the scope authorised, the use of incorrect exchange rates, or the inclusion of expenditures related to Value Added Tax. It may also include errors in the cost statement leading to mistakes in the expenditures claimed.

2.3.13 Under the COFFA approach, our audit would reveal the same ineligible expenditures, but these would not be reported in the COFFA. The COFFA would report only the final expenditures after deduction of any ineligible costs found during the audit. The new audit approach therefore provides more visibility to governance on the audit findings.

Eligible costs not claimed

2.3.14 This category refers to cases where, by mistake, some expenditures were not included in the cost statement, although the expenditures incurred related to the project and were within the authorisations granted. It may also relate to calculation mistakes in the cost statement leading to adjustment in favour of the Host Nation. If sufficient verification and internal controls are in place in the Host Nation when preparing the cost statement, we would expect these types of audit findings to be an exception.

Eligible cost in excess of authorisation

2.3.15 One of the key principles in NSIP is that *no payments will be made in connection with common funded infrastructure projects, unless work has been authorised by the Payments and Progress Committee [today IC] in advance* (C-M(53)18 and AC/4-D/1070 (1987 Edition) and its addenda).

2.3.16 Five modified audit opinions were due to expenditures presented in the cost statements that exceeded authorised funds. This mainly related to Architect and Engineering fees (A/E fees) where the expenditures claimed exceeded the specific authorisation for A/E fees. We consider these expenditures non-compliant with NSIP Regulations and non-eligible pending the Host Nation obtaining additional funds authorisation from the IC. Furthermore, it is not in compliance with NSIP Regulations to incur expenditures prior to authorisation from the IC and thereby to exceed the authorisations granted. If, during the implementation of a project, it becomes evident that project costs will change and exceed original authorisations, the Host Nation must inform the IC in a timely manner and seek an additional authorisation prior to incurring any additional expenditures.

2.3.17 Under the old COFFA approach, our audit would also identify expenditures in excess of authorisation. Prior to issuing a COFFA, we would issue a Letter of Observations to the Host Nation recommending them to obtain an additional authorisation from the IC. With the new audit approach for NSIP financial audits, these findings are reported in the Independent External Auditor's Reports addressed to governance.

### 3. IMPACT ON ACCOUNTABILITY AND RESPONSIBILITY

3.1 We believe that the new approach to NSIP financial audits contributes to the strengthening of overall accountability of NSIP from a corporate governance perspective as well as to clarifying the responsibility of governance, Host Nations, and IBAN.

3.2 The overall purpose of public sector accounting and financial reporting is to provide financial information for decision-making and allow for the discharge of accountability. When it comes to financial accountability, there are three key stakeholders: governance, management and external auditors. Governance is responsible for discharging management of accountability. Governance discharges management based on information from various sources, including input from management and independent assurance provided by the external auditor. These key corporate governance principles on financial reporting and accountability also apply to NSIP.

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3.3 IBAN (the external auditor) issues the Independent External Auditor's Report to the IC, on behalf of Council (governance). The independent assurance provided by IBAN in the form of an audit opinion assists IC, on behalf of Council, in discharging the Host Nation (management). The actual discharge of Host Nations is based on the IC approval of a List of Completed Projects, in accordance with agreed NSIP Regulations. This document is the final step in the project implementation process and, once approved by IC, discharges the Host Nations from the financial responsibilities for these projects, on behalf of Council. After the approval of this document, the International Staff performs a technical closure of the NSIP project in CIRIS.

3.4 The preparation of a List of Completed Projects serving as the IC discharge of Host Nations is not a new procedure. It exists since the early 1960's and was prepared based on the COFFAs issued by IBAN. Recently, the wording of the document was strengthened to make it explicit that the IC, on behalf of Council, discharges the Host Nation from financial responsibilities. This new wording in the List of Completed Projects assists in clarifying the role of governance, Host Nations and IBAN.

3.5 Nevertheless, we found that there are no written procedures or regulations setting out the formal discharge mechanism and the roles and responsibilities of each party in the process. Existing NSIP Regulations governing the procedures for the List of Completed Projects do not explicitly refer to the discharge mechanism nor to the roles and responsibilities of each party in the process.

3.6 In addition, there may be situations where governance does not wish to discharge the Host Nation, for example based on modified audit opinions provided by IBAN or if the JFAI report concludes that the works implemented do not meet the conditions for formal acceptance. We found that the IC currently does not have a written procedure for how to deal with situations where the discharge may be refused. If the discharge is refused, the IC may wish to obtain a statement from the Host Nation addressing the issue and what measures are being implemented to avoid similar situations in the future. The IC will also need to consider any potential consequences for the Host Nation and the common funds provided. When the discharge is refused, the IC may nevertheless agree to an administrative and technical closure of the NSIP project in CIRIS. By clarifying the purpose of a discharge mechanism, including the roles and responsibilities of each party, and establishing procedures for refusal of discharge, we believe that the accountability of the Host Nations will be strengthened over time.

3.7 In addition, we note that the IC, on behalf of Council, discharges Host Nations from their financial responsibilities. The IC does not presently report, through the RPPB, to Council on the discharge granted to Host Nations. Therefore, Council does not have information about the discharge granted to Host Nations, although the Council is ultimately responsible. Such a reporting to Council, through RPPB, could include information on how many Host Nations were discharged in a year and, if it occurred, when discharge was refused or concerns raised. Although the IC prepares an annual NSIP Financial Activity report which includes information on discharge, and which is made publicly available, this report is not submitted to Council, through the RPPB.

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3.8 We believe that providing an audit opinion may encourage Host Nations to present projects for audit in a timelier manner. In addition, situations where all supporting documentation is available for audit may increase in order to avoid modified audit opinions. When IBAN issues a modified audit opinion this may lead to discussions in the IC prior to a decision on discharge and discharge may be refused. Host Nations may therefore wish to avoid modified audit opinions in order to be granted discharge. Over time, we also expect that the quality of the cost statements presented for audit will increase, resulting in fewer errors being found in our audits. This is due to the new requirement for cost statements to be signed, which should encourage Host Nations to increase the verification and internal controls in place when preparing the cost statements. The requirement to sign cost statements therefore emphasises the responsibility and accountability of the Host Nations for expenditures incurred on NSIP projects.

## 4. CONCLUSIONS AND RECOMMENDATIONS

### 4.1 Conclusions

4.1.1 In 2019, IBAN proposed to Council to make some practical improvements to the audit of NSIP expenditures, without changing the core task established by our Charter. On 02 June 2020, Council agreed to these changes and IBAN implemented them. The purpose of the new approach for NSIP financial audits is to better align the reporting of the audit of NSIP expenditures with our Charter and international auditing standards and to contribute to the strengthening of responsibility, accountability and transparency regarding NSIP.

4.1.2 As the external auditor, IBAN provides independent assurance to governance that NSIP expenditures incurred by Host Nations are carried out in compliance with regulations in force. This independent assurance assists governance in discharging Host Nations. The main change implemented is the replacement of the COFFA with an Independent External Auditor's Report providing an audit opinion. The report is issued to the IC, which acts on behalf of Council, copying the Host Nation, and including the Host Nation's signed cost statements. Compared to the old COFFA, the auditor's report provides a stronger regulatory framework for our audits of NSIP expenditures and is more in line with international auditing standards as required by our Charter. It also increases transparency to governance on the result of our audits and aligns the reporting lines with our Charter.

4.1.3 In 2020, we issued 72 of the new auditor's reports on Cost Statements presented by member countries or NATO entities (Host Nations). Out of 72 audit opinions in the Independent External Auditor's Reports, 44 were unmodified and 28 audit opinions were modified. The main reason for issuing modified audit opinions was due to missing documentation. The NSIP regulations require that financial records and documents are kept until final project closure and discharge of the Host Nation by the IC, on behalf of Council. In these cases, Host Nations were not able to fully account for the NATO common funds received and, as a result, did not fulfil all of their regulatory responsibilities related to the implementation of the NSIP project. Therefore, we consider the expenditures reported in the cost statement not to be compliant with NSIP Regulations and therefore non-eligible from a financial audit perspective, subject to decision by the IC. Other reasons for modified audit opinions related to non-eligible costs claimed, eligible costs not claimed or eligible costs

claimed in excess of authorisations. Sufficient verification and internal controls should be in place in Host Nations when preparing the cost statement to avoid similar errors or mistakes occurring in the future.

4.1.4 The final step in the project implementation process is the discharge of the Host Nations from their financial responsibilities by the IC on behalf of Council. The Independent External Auditor's Report serves as the primary input to this process. The discharge is based on a List of Completed Projects approved by the IC. Recently, the wording of this document was strengthened to make it explicit that the IC, on behalf of Council, discharges the Host Nation from financial responsibilities. We found that there are no written procedures or regulations setting out the formal discharge mechanism or the roles, responsibilities, purpose and objective of each party in the process. The existing NSIP Regulations governing the procedures for the List of Completed Projects do not explicitly refer to the discharge mechanism nor to roles and responsibilities of each party in the process. In addition, there are no written procedures for how to deal with situations where discharge may be refused by governance, based on modified audit opinions from IBAN, for example. Further, we noted that the IC does not currently report, through the RPPB, to Council on the discharge granted to Host Nations. Therefore, Council does not have information about the discharge granted to Host Nations by the IC, although the Council is ultimately responsible for this.

## **4.2 Recommendations**

4.2.1 IBAN recommends Council to task the appropriate governance body to develop and document a formal discharge procedure regarding NSIP. This should include:

- a) Setting out roles and responsibilities of each party in the process. It should also cover situations where discharge of Host Nations may be refused, for example based on audit findings.
- b) Annual reporting, through the RPPB, to Council on the discharge granted by IC, on behalf of Council, to Host Nations. Such a reporting could include information on how many Host Nations were discharged in a year and, if it occurred, where discharge was refused.

4.2.2 All tasking decisions by Council should clearly identify those responsible to take action and set deadlines for the delivery of the expected outcomes.

**Abbreviations**

AOM	Alliance Operations and Mission
CIRIS	Common Funded Integrated Resources Information System
COFFA	Certificate of Final Financial Acceptance
Council	North Atlantic Council
IBAN	International Board of Auditors for NATO
IC	Investment Committee
INTOSAI	International Organisation of Supreme Audit Institutions
IS	International Staff
JFAI	Joint Final Acceptance Inspection
IMS	International Military Staff
MC	Military Committee
NOR	NATO Office of Resources
NSIP	NATO Security Investment Programme
RPPB	Resource, Policy and Planning Board

**NATO UNCLASSIFIED**APPENDIX 2  
IBA-AR(2021)0002**GLOSSARY OF TERMS**

In accordance with auditing standards, audit opinions on the expenditures incurred presented in the cost statements of the projects can be either unmodified or modified:

- An unmodified opinion is when IBAN issues an opinion on compliance of expenditures incurred in the Cost Statement and prepared by the Host Nation stating that nothing has come to our attention that causes us to believe that the expenditures incurred have not been carried out in compliance with the NSIP Regulations in force.
- A modified opinion means one of the following:
  - IBAN issues an opinion on compliance of expenditures incurred presented in the cost statement and prepared by the Host Nation stating that some elements of the Cost Statement are affected by a scope limitation, or that specific issues have come to our attention that causes us to believe that some expenditures incurred have not been carried out in compliance with the NSIP Regulations in force.
  - IBAN issues an opinion on compliance of expenditures incurred presented in the cost statement prepared by the Host Nation, stating that the effect of an error, missing documentation or a disagreement is so pervasive and material that IBAN concludes that all expenditures incurred on the project have not been carried out in compliance with the NSIP Regulations in force.
  - IBAN cannot express an opinion on the expenditures incurred because the cost statement is missing, the inherent documentation was intentionally not provided, or because the scope of the audit is severely limited due to material uncertainties affecting whether expenditures incurred have been carried out in compliance with the NSIP Regulations in force.



NORTH ATLANTIC TREATY ORGANIZATION  
ORGANISATION DU TRAITÉ DE L'ATLANTIQUE NORD  
INTERNATIONAL BOARD OF AUDITORS  
COLLÈGE INTERNATIONAL DES AUDITEURS EXTERNES DE L'OTAN

ENCLOSURE 3  
PO(2022)0118

**NATO UNCLASSIFIED**

IBA-A(2020)0037  
3 June 2020

To: Secretary General  
Attn: Director of the Private Office

Cc: NATO Permanent Representatives  
Supreme Allied Commander Europe  
Supreme Allied Commander Transformation  
General Manager, NATO Support and Procurement Agency  
General Manager, NATO Communication and Information Agency  
Financial Controller, Allied Command Operations  
Financial Controller, Allied Command Transformation  
Financial Controller, NATO Support and Procurement Agency  
Financial Controller, NATO Communication and Information Agency  
Chairman, Resource Policy and Planning Board  
Chairman, Investment Committee  
Resource Policy and Planning Board representatives, NATO delegations  
Private Office Registry

Subject: ***International Board of Auditors for NATO (IBAN) Special Report on NATO Security Investment Programme lump sum conversions – IBA-AR(2020)0004***

IBAN submits herewith its approved Special Report (Annex 2) with a Summary Note for distribution to the Council (Annex1).

In accordance with Article 15 of the NATO Financial Rules and Regulations, I have referred the documents to the Resource Policy and Planning Board (RPPB) for examination, comments and recommendations.

Yours sincerely,

Daniela Morgante  
Chairman

Attachment: As stated above.



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**NATO UNCLASSIFIED****ANNEX 1**

**Summary Note for Council  
by the International Board of Auditors for NATO (IBAN)  
on the Special Report on  
NATO Security Investment Programme Lump Sum Conversions**

**Background**

The NATO Security Investment Programme (NSIP) was established in 1951 as NATO's core capital investment programme. It is an essential common funded resource pillar, designed to enhance and upgrade NATO assets, in order to obtain military capabilities that exceed the national defence requirements of individual Nations.

The final phase of an NSIP project is the period during which the Investment Committee (IC) technically accepts the completed works and the financial records are audited by IBAN. The final financial closure of a project and formal discharge of the Host Nations are performed by the IC, on behalf of Council, based on the notation of a list of completed projects. This relieves and discharges the Host Nation from its financial responsibilities for the project.

Host Nations are responsible for maintaining complete financial and technical project documentation until the final project closure and formal discharge. This is important for accountability purposes.

In exceptional cases and at the request of a Host Nation, the IC may decide to convert reported expenditures of an authorised completed project into an "a posteriori" lump sum amount, if the financial records no longer exist or are insufficient or incomplete. A lump sum is defined as a fixed, final, comprehensive authorisation reflecting all cost elements and is not subject to audit by IBAN.

**Report objectives**

The objective of the report is to provide an overview of the number, nature and reasons for NSIP lump sum conversions in the period 2015 to 2019. We conducted the audit in accordance with Article 14 of our charter.

**Audit findings**

Over the period 2015 to 2019, NSIP projects with a total value of EUR 723 million were financially closed based on an "a posteriori" lump sum conversion of expenditures. This equals 17% of all projects financially closed in the period. Out of this amount, EUR 389 million or 54% related to "a posteriori" lump sum conversions of reported expenditures due to missing financial records. EUR 334 million or 46% related to an IC agreed accelerated closure process whereby reported expenditures were converted to lump sum amounts. Although according to NSIP rules, authorisations for lump sum conversion of expenditures should be granted only in exceptional cases, the use of lump sum conversions is no longer exceptional, but has become common practice.

**NATO UNCLASSIFIED****ANNEX 1**

One of the reasons for the lump sum conversions of reported expenditures is missing or incomplete financial project documentation in the Host Nations, not allowing for the preparation of a Cost Statement of actual expenditures incurred on the project. Therefore, the Host Nations did not comply with the NSIP rules for retaining financial records until the audit and the final approval of the completed project by the IC. In these cases, Host Nations were not able to fully account for the NATO common funds received and, as a result, did not fulfil all of their regulatory responsibilities related to the implementation of the NSIP project.

The other reason for lump sum conversion of reported expenditures is an IC agreed accelerated closure process in order to reduce the backlog of NSIP projects not yet technically inspected or audited. We do not know if the financial records were missing or if the Host Nations could have prepared Cost Statements and accounted for the expenditures incurred.

**Recommendations**

IBAN recommends Council to task the appropriate governance body to:

1. Develop and regularly update a compendium of applicable rules related to NSIP, including the responsibilities as a Host Nation for implementing NSIP projects. This compendium should be widely communicated and be made available to Host Nations' organisations.
2. Put in place measures whereby the Host Nation formally confirms, for example with an acknowledgement letter, its responsibilities at every project level authorisation stage of the NSIP project cycle. This confirmation should cover the responsibility for implementing NSIP projects in accordance with NSIP Rules, and specifically for maintaining complete technical and financial project documentation and for presenting NSIP projects for technical inspection and audit within agreed timelines.
3. Require the NATO Agencies and Strategic Commands to adjust their archiving policies so that they are fully aligned with the NSIP rules for retention of technical and financial project documentation for NSIP projects.
4. Invite Territorial Host Nations to confirm that national rules are in line with NSIP rules for retention of financial records, to the greatest extent possible, for NSIP projects.
5. Consider the feasibility of introducing a mechanism with a view to improving Host Nation accountability for timely project closure, whereby a part of the authorised project management funds for the project is withheld until the final project closure and discharge of the Host Nation. Such a mechanism would also need to consider situations where a Host Nation seeks a lump sum conversion.
6. Ensure that all NSIP funded projects are subject to a financial audit, even in those cases where the documentation is lost or incomplete, and that the

external auditor's opinion should be available prior to any decision by the IC on a potential lump sum conversion.

All tasking decisions by Council should clearly identify those responsible to take action and set deadlines for the delivery of the expected outcomes.



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**ANNEX 2  
IBA-AR(2020)0004**

3 June 2020

**INTERNATIONAL BOARD OF AUDITORS FOR NATO**

**SPECIAL REPORT ON  
NATO SECURITY INVESTMENT PROGRAMME LUMP SUM CONVERSIONS**

**PUBLICLY DISCLOSED - PDN(2022)0013 - MIS EN LECTURE PUBLIQUE**

**NATO UNCLASSIFIED**

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IBA-AR(2020)0004**1. INTRODUCTION****1.1 IBAN's mandate regarding NSIP audits**

1.1.1 In accordance with Article 1 of its Charter, the International Board of Auditors for NATO (IBAN) is mandated to audit the NATO Security Investment Programme (NSIP) on behalf of the North Atlantic Council (the Council). IBAN's mandate regarding NSIP audits covers NATO Bodies and Reporting Entities as well as NATO member Nations receiving common funding from the NSIP. The function of IBAN regarding NSIP in accordance with Article 2 of the IBAN Charter is:

*“To provide independent assurance and advice to the Council and, through their Permanent Representatives, the Governments of member countries that [...] the expenditures incurred by member countries (Host Nations) or NATO bodies in respect of the NSIP have been carried out in compliance with the regulations in force (NSIP audit).”*

1.1.2 IBAN may also, through its performance audits, analyse and evaluate the economy, efficiency and effectiveness of the programme's management and procedures.

**1.2 Report objective**

1.2.1 In accordance with Article 14 of its Charter, IBAN may issue a special report to the Council on any relevant matter it considers to be worthy of attention. The objective of this report is to provide an overview of the number, nature and reasons for NSIP lump sum conversions in the period 2015 to 2019. The data used in this report are based on NSIP projects with a Certificate of Final Financial Acceptance (COFFA) issued in the period 2015 to 2019.

**2. BACKGROUND****2.1 The purpose of NSIP**

2.1.1 The NSIP was established in 1951 as NATO's core capital investment programme. It is an essential common funded resource pillar, designed to enhance and upgrade NATO assets' in order to obtain military capabilities that exceed the national defence requirements of individual Nations. The Nations share the NSIP costs with an agreed percentage for each participating Nation.

2.1.2 The programme provides the funds for the development, construction and implementation of military capabilities required by the Strategic Commanders to complete their missions. Common funding eligibility rules state that it will focus on the provision of infrastructure requirements, which are over and above requirements that could be expected to be made available by individual Nations. For example, NSIP can be used to provide, restore or enhance fixed infrastructure (e.g., new buildings or repairing airfields),

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communication information system (CIS) equipment (e.g., new software and hardware) or deployable strategic equipment (e.g., military transport vehicles).

2.1.3 Apart from the Council, the NSIP main stakeholders include the Resource, Policy and Planning Board (RPPB), the Investment Committee (IC) and the Military Committee (MC), supported by the International Staff (IS) and International Military Staff (IMS) and 'Host Nations'. A Host Nation is defined in the NSIP terminology to be either the country on whose territory the project is implemented (Territorial Host Nation) or a NATO agency or Strategic Command. A Host Nation is responsible for managing the implementation of the projects authorised.

2.1.4 Unlike activities funded through the civil or military budget, the NSIP is not controlled and overseen via the execution of a budget. Rather, the NSIP comprises funding of multi-annual projects from within annual limits, referred to as contribution 'ceilings', as approved by Council. Nations provide funding through quarterly calls for contribution approved by the IC. The IS's NATO Office of Resources (NOR) manages the allocation of the disbursement of funds through a system of multilateral compensation. In this system, Nations pay and receive funds from each other directly to implement the NSIP projects.

## 2.2 Applicable NSIP rules

### Project Closure and Financial Accountability Rules

2.2.1 The final phase of an NSIP project is the period during which the IC technically accepts the completed works and the financial records are audited by IBAN. The purpose of the financial audit is to verify that the NSIP expenditures presented in the Cost Statement by the Host Nation are eligible for NATO funding and in compliance with the NSIP rules in force. The audit provides independent assurance to the IC, on behalf of Council, assisting them in discharging the Host Nations from further financial responsibility.

2.2.2 At the end of the audit, IBAN issues an audit report (previously named COFFA). The final financial closure of a project and formal discharge of the Host Nations are performed by the IC, on behalf of Council, based on the notation of a list of completed projects. This relieves and discharges the Host Nation from its financial responsibilities for the project.

2.2.3 On 02 June 2020, the Council, based on advice from the RPPB and IC, approved a number of IBAN proposed changes to its NSIP financial audits (C-M(2020)0010-AS1). The main change relates to the replacement of the audit certificate (COFFA) with an "Independent External Auditor's Report". This report will present an audit opinion including audit findings where applicable. This new report provides a stronger regulatory framework for our audits of NSIP expenditures and is better aligned with IBAN's Charter and international auditing standards.

2.2.4 The overall responsibilities of a Host Nation is outlined in C-M(55)77, *Execution of Infrastructure Projects*, dated 08 September 1955. As part of its responsibilities, the Host Nation is responsible for maintaining complete financial and technical project documentation and requesting audits from IBAN. For accountability purposes, it is essential that Host

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Nations maintain all financial records and documents until the financial audit is complete and the IC has noted the completion of the project and finally discharges the Host Nation. The financial records allow IBAN to perform the financial audit and assess whether the expenditures claimed by the Host Nation are eligible for common funding and in compliance with the NSIP rules in force. It is therefore the responsibility of the Host Nation to ensure that all financial records are kept until project closure, so that the use of NATO common funds can be properly accounted for.

2.2.5 It should be noted that each Host Nation, whether a Territorial Host Nation or a NATO Agency, is provided funds as part of the overall authorised funds for the project, to cover project management activities throughout the life cycle of a project. Territorial Host Nations receive funds to cover National Administrative Expenses (NAE) related to their project management activities. The NATO Communications and Information Agency (NCIA) receives funds to cover Project Service Costs (PSC) and the NATO Support and Procurement Agency (NSPA) receives funds to cover Project Management Costs (PMC). These funds also cover administrative activities related to technical and financial project closure, which is an integral part of the Host Nation responsibilities. The NATO Strategic Commands acting as Host Nations do not receive any project management funds.

2.2.6 Current NSIP rules agreed by the IC require the Host Nations to request a technical inspection (referred to as a Joint Final Acceptance Inspection (JFAI)) no later than six months after project completion (three months for Alliance Operations and Missions) and to request an audit at the latest six months after formal acceptance by the IC of the JFAI.

#### NSIP Lump Sum Conversion Rules

2.2.7 An NSIP project authorisation is granted to a Host Nation based on a decision taken by the IC authorising the Host Nation to disburse NATO funds. It can cover planning and project execution. This project authorisation establishes the physical scope that the Host Nation is authorised to execute and the amount (financial scope) that NATO accepts to pay from common NSIP funds.

2.2.8 In exceptional cases and at the request of a Host Nation, the IC may decide to convert reported expenditures of an authorised completed project into an “a posteriori” lump sum amount if the financial records no longer exist, are insufficient, or are incomplete. A lump sum is defined as a fixed, final, comprehensive authorisation reflecting all cost elements (AC/4-D/2948, *Exchange rates applicable to lump sums dated 20 August 1986*).

2.2.9 The overall principle is that authorisations for a lump sum amount are in general granted only in exceptional cases. Projects authorised for lump sum (or partial lump sum) are subject to technical inspection (JFAI), but are not subject to audit since the authorised funds are a fixed, final amount (AC/4-R/751, *Summary Record of a meeting held at NATO Headquarters, Brussels, on 13 January, 1970*).

2.2.10 The procedures for authorisations of lump sum amounts date back to the 1950s and are addressed in several policy documents. There is no comprehensive basic document or compendium providing a general policy for lump sum authorisations and conversions. This situation is reflected in document AC/4-N(2000)001+COR1 (10 January 2000), *Conversion into lump sums of user-pre-financed projects*, which states that “Nations have always been reluctant to institutionalise something that should be considered as an exception to the rule”.

### **3. MAIN FINDINGS RELATED TO LUMP SUM CONVERSIONS**

#### **3.1 Introduction**

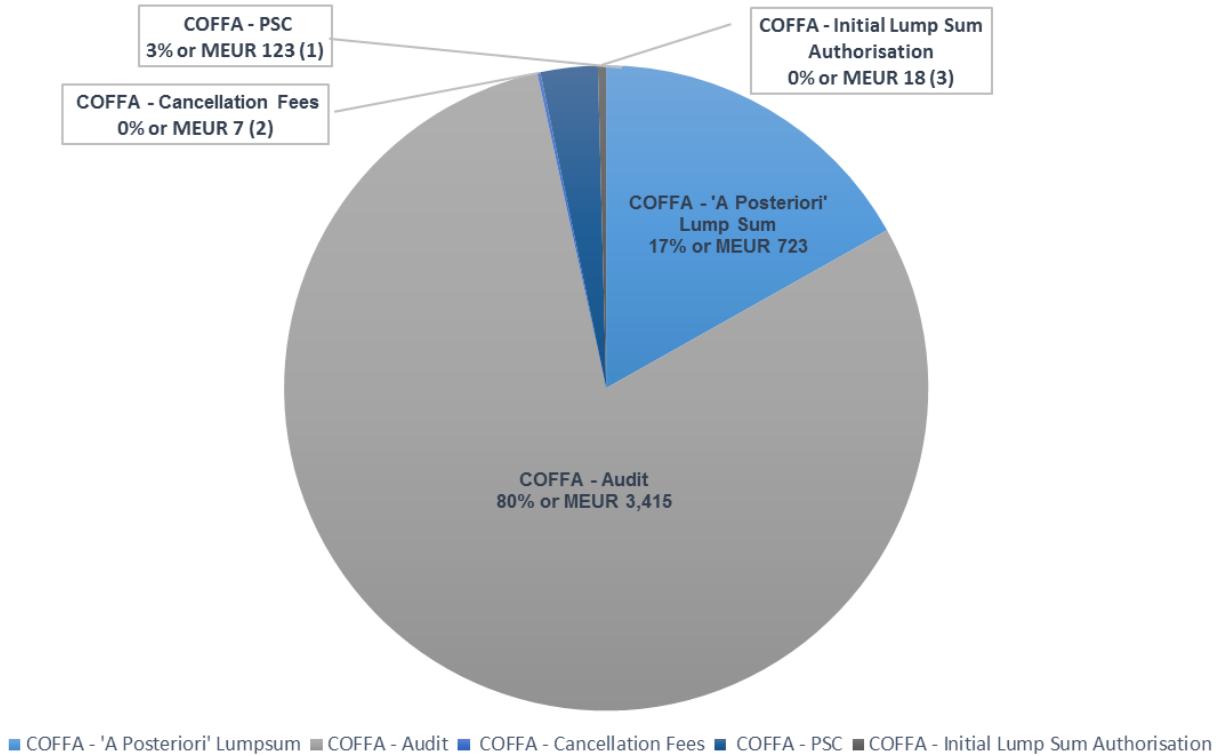
3.1.1 Using data from the period 2015-2019, IBAN reviewed NSIP projects with an audit certificate (COFFA) issued in this period and analysed the main reasons for the “a posteriori” conversion of reported expenditures into a lump sum amount.

#### **3.2 Overview of lump sum conversions in the period 2015 to 2019**

3.2.1 In the period 2015 to 2019, the total value of projects financially closed, based on an “a posteriori” lump sum conversion, was Euro (EUR) 723 million. These projects were not audited by IBAN in compliance with current NSIP rules.

3.2.2 In the same period, the total value of projects audited by IBAN was EUR 3.4 billion. The total value of all projects financially closed in the period is EUR 4.3 billion.

Chart 1: Total value of projects financially closed by category - 2015-2019



Source: IBAN data (rounded figures)

- Notes:
- (1) PSCs are funds provided to NCIA to cover project management activities throughout the life cycle of a project. PSCs have a separate project authorisation and are authorised as a firm fixed price. Therefore, they are not subject to audit.
  - (2) Cancellation fees apply in the event that an approved project no longer meets a minimum military requirement and is subsequently de-programmed.
  - (3) Initial Lump Sums may be authorised in cases where it is impossible to separate the NATO scope and cost of a project from the national scope and cost.

3.2.3 The above chart shows that, out of a total amount of financially closed projects of EUR 4.3 billion, 17% (EUR 723 million) were financially closed based on an authorised “a posteriori” lump sum conversion.

3.2.4 In total, 24 out of 33 Host Nations benefited from lump sum conversions, including NSPA, NCIA and Supreme Headquarters Allied Powers Europe (SHAPE). The table below shows the value of financially closed projects by category and per Host Nation.

**Table 1: Value of projects financially closed by category and by Host Nation – 2015-2019**

Host Nation	COFFA – Lump Sum Conversion Euro thousand	COFFA - Cancellation Fees, PSC & Initial Lump Sum Authorisation Euro thousand	COFFA - Audit Euro thousand	Total COFFA per Nation Euro thousand
AL	-	-	-	-
BE	32,804	106	39,430	72,340
BU	702	-	5,466	6,168
CA	736	6	-	741
CR	-	-	-	-
CZ	4,405	-	1,102	5,508
DE	23,289	40	34,347	57,676
ES	-	-	2,947	2,947
FR	235	-	-	235
GE	69,096	14,518	199,307	282,921
GR	77,011	105	243,905	321,021
HU	-	-	80,039	80,039
IC	-	-	-	-
IT	85,797	1,296	215,109	302,202
LA	-	-	32,838	32,838
LI	542	-	1,413	1,955
LU	-	-	-	-
MO	-	-	-	-
NCIA	50,627	123,002	1,110,337	1,283,965
NE	2,821	17	28,018	30,855
NM	-	-	-	-
NO	7,432	1	280,018	287,451
NSPA	136,013	2,544	401,111	539,668
PL	3,587	81	151,408	155,075
PO	4,522	30	219,608	224,160
RO	156	-	5,201	5,357
SHAPE	53,498	51	14,206	67,756
SK	6,062	-	25,594	31,656
SP	2,197	2,986	72,199	77,382
SN	5,523	-	-	5,523
TU	43,696	824	209,753	254,273
UK	82,393	244	16,243	98,879
US	29,646	1,624	25,740	57,010
<b>TOTAL</b>	<b>722,787</b>	<b>147,473</b>	<b>3,415,341</b>	<b>4,285,601</b>

Source: IBAN data (rounded figures)

3.2.5 The above table shows that NCIA, NSPA and SHAPE account for 33% of total lump sum conversions, whereas territorial Host Nations account for 67% of lump sum conversions. NSPA was the single highest beneficiary of lump sum conversions.

### 3.3 Main reasons for “a posteriori” lump sum conversions

3.3.1 IBAN analysed the main reasons for lump sum conversions. An already authorised completed project may be converted into an “a posteriori” lump sum based on approval by

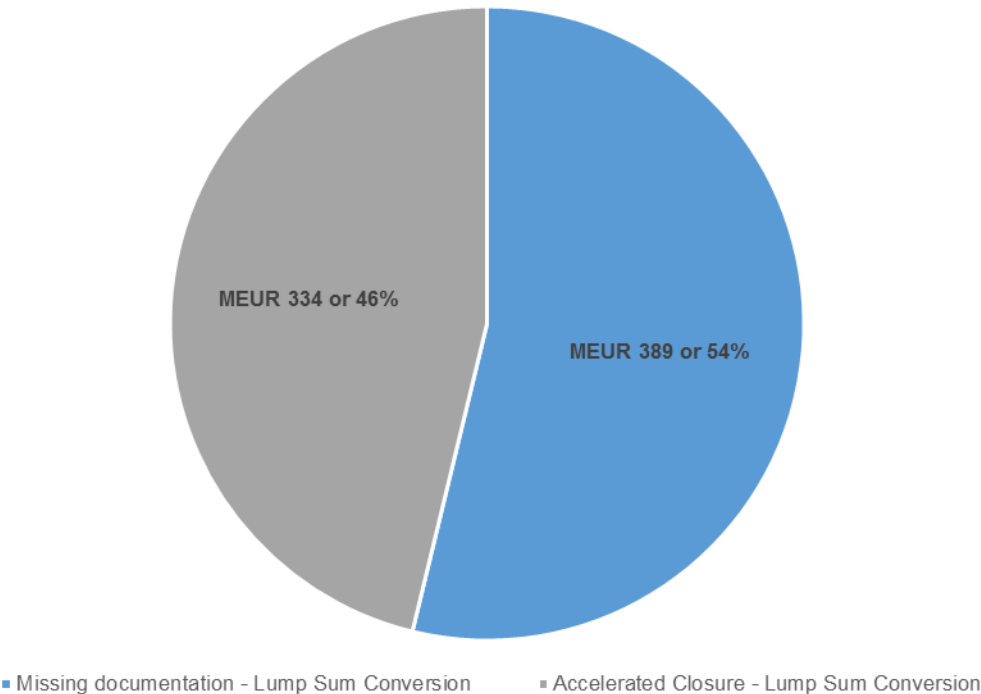


the IC. In the period 2015-2019, reported project expenditures of EUR 723 million was converted into a lump sum. This was due to one of the following two reasons:

- IC accelerated closure of projects (EUR 334 million).
- Missing documentation (EUR 389 million).

3.3.2 The chart below shows the total value of lump sum conversions of EUR 723 million by category.

**Chart 2: Value of projects converted to lump sum by category – 2015-2019**



Source: IBAN data (rounded figures)

*IC accelerated closure of projects (EUR 334 million)*

3.3.3 In the period 2015-2019, projects of a total of EUR 334 million were closed based on an IC approved lump sum conversion as part of an agreed accelerated closure process. These projects were technically accepted, but not subject to audit in accordance with NSIP rules.

3.3.4 In 2014, on the basis of an RPPB recommendation, Council tasked the IC to develop a plan with the objective of closing out by 30 June 2016 existing completed NSIP projects amounting to EUR 5 billion (C-M(2014)0052). The deadline for closing out these projects was later extended until 2020 (C-M(2017)0030). The IC was requested to provide semi-annual progress reports to the RPPB on the status of closure of projects.

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3.3.5 The IC agreed plan for close-out of completed projects focused on two areas:

- Close-out of projects programmed in support of International Security and Assistance Force (ISAF) operations.
- Close-out of other completed NSIP projects programmed before 2011.

3.3.6 The IC agreed that for projects with an authorised scope of less than EUR 3 million, an accelerated technical acceptance procedure would take place and the project expenditures would be converted to lump sum. Projects above the agreed threshold of EUR 3 million would be subject to standard technical inspection procedures and financial audit.

3.3.7 The initiative to implement an accelerated closure process was due to the significant backlog of projects completed, but not yet technically inspected or audited. Some of these projects were authorised prior to 1994. The purpose of this initiative was to reduce the backlog of NSIP projects not yet technically inspected and audited and to allow Host Nations to focus on ensuring that newly completed projects would be closed following agreed timelines.

3.3.8 For projects closed following the IC agreed accelerated closure process, the reported expenditures were converted into a lump sum amount. We do not know whether the financial records were missing or if the Host Nations could have prepared Cost Statements and accounted for the actual expenditures incurred.

Missing documentation (EUR 389 million)

3.3.9 In the period 2015-2019, NSIP projects with a total value of EUR 389 million were converted into an “a posteriori” lump sum amount, based on case-by-case requests made by Host Nations to the IC, because of insufficient or incomplete financial records. As a result of this missing documentation, Host Nations were not able to prepare Cost Statements of actual expenditures incurred on these projects and IBAN did not conduct a financial audit in accordance with existing NSIP rules.

3.3.10 In total, nine out of 33 Host Nations requested and received an approval by the IC of a conversion of the reported expenditures into a lump sum due to missing documentation. Out of these nine Host Nations, three Host Nations accounted for 63% of total lump sum conversions due to missing documentation. NSPA accounted for the highest amount of lump sum conversions due to missing documentation (EUR 116 million or 30%).

3.3.11 Total NSIP projects of EUR 389 million for the period 2015-2019 converted into an “a posteriori” lump sum amount due to missing documentation do not include any request from NCIA. However, in 2019, NCIA informed the IC that it does not have all the financial records available for up to 79 projects with a total value of EUR 701 million, and therefore may submit a request for lump sum conversion of up to that amount (see AC/4-DS(2019)0013).

3.3.12 Projects not yet financially closed are outside the scope of this report. Considering that projects programmed before 2011 of a total value of EUR 2.3 billion are not financially closed, it is worth noting that there is a further risk that Host Nations may no longer have sufficient and complete financial records to be able to account for those NATO common funds received.

3.3.13 We reviewed the individual requests made by the Host Nations to the IC for lump sum conversion. One of the main reasons why the financial records were no longer available is that the Territorial Host Nation or NATO Agency archiving policies require the documentation to be kept for a period shorter than the one prescribed by the NSIP rules, which require all documentation to be kept until audit and final closure of the project. NSIP projects are implemented over a long period of time, which often exceeds the national archiving requirements for financial records. Therefore, Host Nations did not always apply NSIP document archiving rules and disposed of financial records related to NSIP projects in accordance with their respective national or agency rules.

3.3.14 Another common reason for the request to authorise conversion of expenditures into a lump sum is due to re-organisations and restructurings within the Host Nations, leading to financial records being lost or misplaced without ensuring compliance with the NSIP rules for retention of financial records.

3.3.15 Although these projects were not yet financially closed, because the documentation was no longer available, the Host Nations could not account for the use of the NATO common funds received from NSIP and requested the IC to approve a lump sum conversion of the reported expenditures.

3.3.16 In addition, one of the common factors contributing to financial records not being retained until audit and project closure is the fact that the agreed timelines according to the NSIP rules for the request for a technical inspection and audit are not respected. A technical inspection should be requested no later than six months after project completion and the audit requested at the latest six months after formal acceptance by the IC of the technical inspection. In many cases though, there is a significant time gap between actual physical completion of the project and the request for technical and financial closure.

3.3.17 Table 2 below shows the total value of lump sum conversion due to missing documentation by Host Nation for the period 2015-2019.

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ANNEX 2  
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per host nation for the period 2015-2019**

Host Nation	Missing documentation - Lump Sum Conversion Euro thousand
AL	
BE	29,249
BU	
CA	
CR	
CZ	
DE	7,227
ES	
FR	
GE	39,704
GR	37,701
HU	
IC	
IT	64,738
LA	
LI	
LU	
MO	
NCIA	
NE	
NM	
NO	
NSPA	116,018
PL	
PO	1,286
RO	
SHAPE	
SK	
SP	
SN	
TU	
UK	64,909
US	27,933
<b>Total</b>	<b>388,765</b>

Source: IBAN data (rounded figures)

### 3.4 Main implications when authorising lump sum conversion

3.4.1 Host Nations are responsible for maintaining complete financial and technical project documentation until the financial audit is complete and until the IC has noted and finally discharged the Host Nation for the completed project. It is against good practice and principles of accountability to be unable to account for public funds received. Therefore, when the IC agrees to convert reported expenditures into a lump sum, this has a number of implications. These implications are the same whether the lump sum conversion is due to an IC agreed accelerated closure process or due to missing financial records.

3.4.2 When authorisations for lump sums are granted “a posteriori”, Host Nations are discharged from their financial responsibilities without having properly accounted for the NATO common funds received. There is a risk that NATO common funds were used for ineligible expenditures that are outside the authorised scope or not in compliance with the rules.

3.4.3 When IBAN conducts the financial audit of NSIP projects, we may find errors in the accuracy of the Cost Statement presented for audit by the Host Nation. In the past, the most common errors related to the inclusion of ineligible expenditure, erroneous cost sharing calculations between NATO and the Host Nation, incorrect currency conversion or mathematical errors. Based on the audit, a financial adjustment is made and funds identified as ineligible expenditures are returned to the NSIP. As no audit takes place of amounts converted to lump sum, there is a risk that the actual expenditures may be more or less than the lump sum converted amount.

3.4.4 The NSIP rules setting out the overall Host Nation responsibilities for the management of the implementation of NSIP projects dates back to 1955. There is no reference to the specific responsibilities of a Host Nation at each single project level authorisation stage or an acknowledgement by the Host Nation prior to the IC approval of individual projects. Recognising the rotation of staff in Host Nations, there is a risk that Host Nations are not fully aware of their NSIP regulatory responsibilities.

3.4.5 Finally, and up to now, when the IC agreed to convert reported expenditures into a lump sum, a Host Nation was discharged from its financial responsibilities without the projects being subject to a financial audit. However, it is not good practice not to allow the external auditor to conduct a financial audit of all reported expenditures and provide its opinion and assurance to governance, prior to any decision on a conversion of reported expenditures into lump sum. The audit opinion may be modified in cases where not all financial records are available, but this still provides valuable assurance to governance about the actual expenditures incurred and the inherent documentation.

**4. CONCLUSIONS AND RECOMMENDATIONS****4.1 Conclusions**

4.1.1 Over the period 2015 to 2019, NSIP projects with a total value of EUR 723 million were financially closed based on an “a posteriori” lump sum conversion of expenditures. This equals 17% of all projects financially closed in the period. Out of this amount, EUR 389 million (54%) related to “a posteriori” lump sum conversions of reported expenditures due to missing financial records. EUR 334 million (46%) were related to an IC agreed accelerated closure process, whereby reported expenditures were converted to lump sum amounts. Although according to NSIP rules, authorisations for lump sum conversion of expenditures should be granted only in exceptional cases, the use of lump sum conversions is no longer exceptional, but has become common practice in the NSIP.

4.1.2 One of the reasons for the lump sum conversions of reported expenditures is missing or incomplete financial project documentation in the Host Nations, not allowing for the preparation of a Cost Statement of actual expenditures incurred on the project. Therefore, the Host Nations did not comply with the NSIP rules for retaining financial records until the audit and the final approval of the completed project by the IC. The Host Nations were not able to fully account for the NATO common funds received and did not fulfil all of their regulatory responsibilities related to the implementation of the NSIP project.

4.1.3 The other reason for lump sum conversion of reported expenditures is an IC agreed accelerated closure process, which aimed to reduce the backlog of NSIP projects not yet technically inspected or audited. We do not know whether the financial records were missing or if the Host Nations could have prepared Cost Statements and accounted for the actual expenditures incurred.

**4.2 Recommendations**

4.2.1 IBAN recommends Council to task the appropriate governance body to:

1. Develop and regularly update a compendium of applicable rules related to NSIP, including the responsibilities as a Host Nation for implementing NSIP projects. This compendium should be widely communicated and be made available to Host Nations organisations.
2. Put in place measures whereby the Host Nation formally confirms, for example with an acknowledgement letter, its responsibilities at every project level authorisation stage of the NSIP project cycle. This confirmation should cover the responsibility for implementing NSIP projects in accordance with NSIP Rules, and specifically for maintaining complete technical and financial project documentation and for presenting NSIP projects for technical inspection and audit within agreed timelines.
3. Require the NATO Agencies and Strategic Commands to adjust their archiving policies, so that they are fully aligned with the NSIP rules for retention of technical and financial project documentation for NSIP projects.

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4. Invite Territorial Host Nations to confirm that national rules are in line with NSIP rules for retention of financial records, to the greatest extent possible, for NSIP projects.
5. Consider the feasibility of introducing a mechanism with a view to improving Host Nation accountability for timely project closure, whereby a part of the authorised project management funds for the project is withheld until the final project closure and discharge of the Host Nation. Such a mechanism would also need to consider situations where a Host Nation seeks a lump sum conversion.
6. Ensure that all NSIP funded projects are subject to a financial audit, even in those cases where the documentation is lost or incomplete, and that the external auditor's opinion should be available prior to any decision by the IC on a potential lump sum conversion.

4.2.2 All tasking decisions by Council should clearly identify those responsible to take action and set deadlines for the delivery of the expected outcomes.

**Abbreviations**

ACO	Allied Command Operations
ACT	Allied Command Transformation
COFFA	Certificate of Final Financial Acceptance
Council	North Atlantic Council
IBAN	International Board of Auditors for NATO
IC	Investment Committee
IMS	International Military Staff
IS	International Staff
ISAF	International Security and Assistance Force
JFAI	Joint Final Acceptance Inspection
MC	Military Committee
NAE	National Administrative Expenses
NCIA	NATO Communications and Information Agency
NOR	NATO Office of Resources
NSIP	NATO Security Investment Programme
NSPA	NATO Support and Procurement Agency
PMC	Project Management Cost
PSC	Project Service Cost
RPPB	Resource, Policy and Planning Board
SHAPE	Supreme Headquarters Allied Power Europe
SACT	Supreme Allied Command Transformation