

GAO/IBAN

U.S. General Accounting Office
International Board of Auditors for NATO

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May 9, 1996

The Honorable William V. Roth, Jr.
Chairman, U.S. Senate Delegation to the
North Atlantic Assembly

The Honorable Douglas Bereuter
Chairman, U.S. House of Representatives Delegation
to the North Atlantic Assembly

The Honorable Karsten Voigt
President, North Atlantic Assembly

The Honorable Peter Corterier
Secretary General, North Atlantic Assembly

In response to your request, the U.S. General Accounting Office (GAO) and the International Board of Auditors for the North Atlantic Treaty Organization (IBAN) performed a joint management review to assess the internal financial and management controls at the North Atlantic Assembly's (NAA) International Secretariat in Brussels, Belgium. GAO and IBAN are in unanimous agreement on all findings, conclusions, and recommendations in this letter.

BACKGROUND

The North Atlantic Assembly is a body of parliamentary delegates selected from the members of national parliaments of NATO countries. The Assembly links NATO with the legislatures of member countries. It is funded directly by the member nations, with a small contribution from NATO, but otherwise is administratively and financially independent of NATO.

NAA functions through five committees that meet in plenary sessions at least twice a year at various national capitals. There are six Assembly officers: five

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are elected each year by delegates in plenary session (the President, three Vice Presidents, and the Treasurer). The Secretary General is elected every 2 years by the Standing Committee. The NAA is governed by the Standing Committee, which comprises the heads of each alliance delegation.

Based in Brussels, Belgium, NAA's International Secretariat organizes two annual plenary sessions as well as committee meetings and related activities. The Secretary General is the International Secretariat's top manager, supervising about 30 permanent employees and managing an annual budget of about Belgian francs (BEF) 120 million (U.S. dollars (USD) 4 million). One U.S. dollar is equivalent to about 30 Belgian francs.

RESULTS IN BRIEF

For a period beginning about 1988 and leading up to mid-1995, senior management at the International Secretariat lost significant control of its financial records to the Assembly's financial officer. During this period, there was abuse and misuse of NAA's funds. Internal control weaknesses were such that additional improprieties could exist that have not come to light. Following the termination of the contract with its former finance officer in May 1995, NAA became aware of these irregularities and has initiated procedures to strengthen its internal management controls.

Despite these improvements, NAA's internal controls for its financial management systems are still seriously inadequate. For example, NAA lacks a system for documenting and approving the obligations of resources; a budget that shows how travel funds are spent for individual expense items; policies that adequately segregate duties; properly documented and executed administrative procedures over areas such as personnel, travel, and purchases; and compliance with law requiring the payment of income tax on overtime wages paid to Belgian employees. Also, NAA's provident (retirement) fund, with a balance of more than BEF 100 million, has not been properly administered and has not been audited for several years.

In addition, according to NAA rules, the financial officer reports directly to the Treasurer, who is not located at the Assembly headquarters, rather than the Secretary General or his staff. Because of this anomaly in the reporting line of authority, the Secretary General did not always have access to key financial data.

As a result of these continuing internal control weaknesses, an environment has evolved that has permitted the abuse and misuse of Assembly resources. As these weaknesses are continuing, NAA is still vulnerable to future improprieties. GAO and IBAN's recommended actions, if effectively implemented, should correct the problems.

NAA LACKS ADEQUATE INTERNAL CONTROLS

In May 1995, NAA began to establish systems and procedures to better safeguard its resources. However, despite these ongoing efforts, NAA still lacks an adequate integrated system of basic internal controls that work together to protect the agency's resources. Examples follow:

- NAA's accounting systems lack the ability to record and document commitments and obligations in advance against its approved budget categories to ensure that funds are committed and spent only for authorized purposes. As a result, NAA expenses exceeded amounts approved by the Assembly in several budget categories.
- NAA's budget does not provide visibility and transparency over travel expenses, which are the second largest expense of the Assembly (salaries are the first). Rather, travel expenses are divided into numerous budget categories and activities and are never shown by single expense item.
- NAA's finance office operates with inadequate segregation of duties. Almost all financial activities are controlled by one person. As a result, improper and illegal financial activities can easily be conducted without detection. For example, until May 1995 one person allegedly diverted about BEF 6.5 million (USD 216,000) from NAA in a tax withholding scheme that benefited certain employees. NAA is attempting to recover these funds through legal actions.
- NAA lacks documented administrative procedures and policies in some areas, such as travel and payroll, and because of inadequate managerial control has not always complied with existing procedures for the approval of travel and purchase orders. These weaknesses led to an organizational culture allowing unauthorized uses of agency funds for salary advances and private travel. During 1994 and 1995, there were about 225 transactions involving about BEF 2.7 million (USD 90,000), many of which were not formally authorized.

- NAA failed to comply with Belgian tax law. NAA withholds and pays taxes on regular salaries for Belgian employees as required by applicable tax laws. However, overtime wages in 1994 and 1995—about BEF 785,000 (USD 26,000)—were paid directly to employees without deductions, including Belgian taxes, as required by law. About 43 percent of the overtime was paid to one employee.
- NAA has not had an adequate external audit. Although the NAA auditor certifies the accounts and has performed internal studies of NAA, his authority and independence were restricted by the former finance officer. These restrictions, though, were not identified in his report to the NAA. For example, the NAA auditor did not state that he had not obtained all information and explanations necessary to certify the annual financial statements. The lack of a sufficient external audit may have contributed to improper transactions being undisclosed. For example, an audit of the provident (retirement) fund should have disclosed that required monthly deposits of about BEF 800,000 (USD 27,000) were not made for an 18-month period. To date, the provident fund has not been audited.
- The NAA's Rules of Procedures state that the financial officer is to report directly to the Treasurer, an elected official who does not work at the Assembly. As a result, prior to May 1995, NAA management, including the Secretary General, did not always have access to key financial data.

Finally, we noted several instances where, in our opinion, agency funds were spent extravagantly or without due regard for economy. For example, travel related to plenary sessions is a major NAA expense item, since about 60 permanent and temporary staff members attend. When planning the plenary sessions, (1) NAA staff make several pre-trips (up to five) to organize and prepare for each plenary session; (2) with one or two exceptions all NAA staff attend the sessions; and (3) temporary staff members, including some relatives of NAA permanent staff, are hired to help prepare the sessions. For example, for the four sessions in 1994-95, NAA paid about BEF 256,000 (USD 8,500) for one individual from Germany to serve as a temporary assistant to the Secretary General.

We found other areas where NAA spent funds that might have been saved through better economy. These include the following:

- operation of two official vehicles,
- overtime payments,
- a salary increase to replace children's allowances,

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- use of agency telephones for personal calls,
- entertainment expenses by NAA employees,
- use of expensive hotels,
- use of business and first class travel, and
- security system at Secretary General's residence.

RECOMMENDATIONS

To preclude future financial improprieties, we recommend that the Secretary General of NAA establish an integrated system of basic internal controls that, together, would adequately protect the Agency's resources. This should include an obligations system, a transparent budget that shows each major expense item, policies that segregate duties, better documented personnel and travel procedures and policies, and a requirement for a fully independent external audit.

We recommend that until NAA establishes an integrated system of internal controls, it should obtain outside assistance for administrative services and audit support. One possibility might be to seek assistance from NATO for administrative support, thereby subjecting itself to the NATO financial rules and regulations and civilian personnel regulations and regular audit by the International Board of Auditors for NATO. Further, we recommend that NAA amend its Rules of Procedures to provide for the finance officer to report to the Secretary General. There should be a reporting line from the finance officer directly to elected officials as well. We also recommend that the NAA Standing Committee define its standards for due regard for economy.

AGENCY COMMENTS

The NAA Secretary General provided written comments on our letter. The comments were noted by the President of the NAA.

The Secretary General generally agreed with the findings in this letter, but he disagreed on some technical points. Nonetheless, the Secretary General endorsed all the recommendations, including our overall recommendation to set up an integrated system of internal controls. His comments are reprinted in enclosure III.

The ultimate responsibility for internal control and the avoidance of irregularities rests with the management of the Secretariat. The Secretary General's reply to the observations raised in this letter in our view confirms

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that this responsibility was not adequately discharged for a number of years up to the time of this management review.

SCOPE AND METHODOLOGY

GAO and IBAN jointly reviewed NAA's internal controls for financial management. To assess NAA's internal controls, we used as criteria NAA policies and regulations, NATO policy, and good management practice as the basis for our joint audit. We conducted our review in accordance with generally accepted government auditing standards.

In conducting this review, three auditors from GAO and two auditors from the International Board spent 5 days in 1996 reviewing records and interviewing NAA managers and staff at the International Secretariat in Brussels, Belgium. We received full staff cooperation and complete access to the financial books and records and to the operating policies and procedures necessary to conduct this review.

Enclosure I contains detailed evidence and specific recommendations on each area reviewed, and enclosure II contains a detailed description of the areas where we believe economies could be achieved.

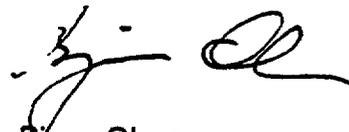
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We plan no further distribution of the letter until 30 days from its date. At that time, copies will be made available to others upon request.

Please contact us on (202) 512-4300 (GAO) or 011-32-2-707.4236 (IBAN) if you or your staff have any questions about this letter. Major contributors to this letter were GAO auditors F. James Shafer, Charnel F. Harlow, and Cary B. Russell and IBAN auditors P. Maertens and R. Brisebois.



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LACK OF INTERNAL CONTROLS AT NAAOVERALL CONTROL ENVIRONMENT

The assessment of the overall control environment included looking at the NAA management's philosophy and operating style, control over compliance with applicable laws, control over budget formulation and execution, and ability to promptly identify and react to changing conditions. The following seven problems were identified in this area.

Inadequate Funds Control System

An adequate means for controlling the budget would include a commitments and obligations system to ensure that payments are made only for the purposes approved in the budget and limited to those amounts. Further, budget transfers between activity accounts should not be made without specific prior authorization as specified in the NAA financial regulations.

NAA's accounting system lacks the ability to record and document commitments and obligations in advance to ensure that funds are available in the budget before funds are expended. For years, while the total spending was within the budget ceiling, funds have been expended from several budget categories in excess of approved budgetary levels and without proper transfer and authorization by the Treasurer and Standing Committee. This had been pointed out on a number of occasions by the NAA auditor.

NAA should implement a system of commitments and obligations and follow NAA procedures for the expenditures of budgeted funds.

Inadequate Segregation of Duties in the Finance Department

Article 7 of NAA's financial regulations requires that internal controls be set up, as necessary, to maintain a continuous check of all financial transactions. In addition, good management practices require adequate segregation of duties.

NAA has inadequate segregation of duties in its finance office. The accounting clerk there controls the per diem calculations, the travel advance forms and calculations, the cash for advances, the advance ledgers, the bank debit/credit forms, and the travel expense records. This person also has access to the safe holding various countries' currencies and records on computer travel expenses, advances to employees, and liquidation of travel claims. As a result, transactions occurred without management authority, approval, or knowledge.

NAA should set up a system of internal controls that ensures the adequate segregation of duties over financial records, cash, and bank reconciliations.

Improper Control Over NAA Finances by Former Finance Officer

Article 7 of NAA's financial regulations requires that internal controls be set up, as necessary, to maintain a continuous check on all financial transactions. In addition, good internal controls require the adequate segregation of duties.

From 1988 to mid-1995, senior management at the International Secretariat lost control of NAA's financial records and the issuance of funds to the finance officer. Under the management of the finance officer, two improper financial schemes were initiated that remained undetected until the finance officer was dismissed in 1995.

The first scheme involved the overwithholding of Belgian taxes, which NAA pays separately. The funds overwithheld were later remitted to the finance officer and several other employees. The amount overwithheld amounted to BEF 6,484,230 (USD 216,141), and NAA is attempting to recover these funds from the former finance officer through legal actions. Under the second scheme, the finance officer stopped making monthly payments to the provident fund and granted herself large withdrawals from her share of the money from the NAA account. The provident fund has not been audited to determine whether individual retirement accounts reflect the proper balances or whether the accounts are fully funded. These schemes went undetected by NAA management until about May 1995.

NAA should provide for the adequate segregation and rotation of duties in the finance department and should establish an internal control system as required by Article 7 of NAA financial regulations to maintain a continuous check of all financial transactions.

Unclear Lines of Authority

Good management practices call for clear lines of authority in authorizing, recording, and reporting agency financial transactions. Roles at all levels should be clearly defined and should provide for an unbroken chain of authority through the levels of management and agency oversight.

For several years, NAA's senior-level management officials have not worked completely in accord with the Treasurer. The former finance officer, supported by the Treasurer, asserted too much control over NAA's financial records, bank accounts, and the provident fund and did not report directly to or cooperate with, among others at the International

Secretariat level, the Secretary General and Deputy Secretary General. This problem emanated from NAA's formal rules of procedure, which provided for the finance officer to report directly to the Treasurer, thereby bypassing senior-level management. As a result, senior NAA management lost control over financial transactions, and the finance officer was able to conduct improper activities such as the tax withholding and provident fund schemes.

NAA should establish clear lines of reporting authority and clearly defined roles by amending the Assembly's rules of procedure. The amended rules should require the finance officer to report to the Secretary General, but with an appropriate direct line of reporting to the NAA elected officials.

Lack of External Audit

Good management practices call for an external audit of financial records to (1) express an opinion on the financial statements; (2) provide to oversight bodies (that is, the Standing Committee) an external analysis of financial condition; and (3) periodically examine all records to ensure that only authorized transactions occur and that transactions are properly recorded and reported to management

NAA is not subject to an adequate external audit. The NAA auditor functions somewhere between an internal and external auditor, and his authority and independence were sometimes restricted by the former finance officer. NAA procedures state that the auditor is to certify that he has "obtained all the information and explanation that he has required." He was unable to provide that certification, yet this was not stated in his reports. The lack of an adequate external audit may have contributed to improper and/or illegal transactions being undisclosed for long periods of time. For example, an audit of the provident fund should have disclosed the fact that required monthly deposits were not made for 18 months.

A proper external audit of NAA should be done by fully independent auditors.

Falsification of NAA Records

Good management practices dictate that accurate and complete records be maintained to reflect the status of agency receipts and disbursements. There should also be an adequate system of internal controls to prevent and detect fraud, waste, and abuse.

One NAA employee was making fraudulent claims by falsifying expense vouchers. The former finance officer knew about these claims and eventually reported the situation to the Treasurer. However, she did not report it to senior management.

NAA should establish an adequate system of internal controls that includes the proper segregation of duties, clear lines of authority, and routine external audit.

Unauthorized Use of the Secretary General's Signature Stamp

Good management practices require (1) clearly defined levels of signature authority and (2) strict physical controls over the custody and use of signature stamps.

For several years, payments of invoices, payroll authorizations, and other transactions were made in excess of authorized levels through the uncontrolled use of the Secretary General's signature stamp. This stamp was withdrawn after the departure of the previous finance officer.

Internal controls at NAA should be strengthened to ensure that the delegation of authority is properly enforced. Signature stamps should not be used for financial transactions.

PAY AND BENEFITS

Weaknesses in the Administration and Management of the NAA Provident Fund

The NAA provident (retirement) fund should be administered and managed in accordance with NAA's regulations governing the fund. These regulations require that withdrawals from individual accounts be made only when approved by the Treasurer and only for limited reasons. However,

- for several years, unauthorized withdrawals were made from the provident fund without authorization and full explanation;
- for an 18-month period ending in June 1995, monthly deposits were not made as required;
- the determination and the method of distribution of the interest earned by the provident fund is unclear and not documented—while the interest earned is distributed to members every year, how the actual interest was calculated is not known;
- the NAA provident fund has not been audited; and

- prior to May 1995, there were no meetings between NAA representatives and the fund investment manager.

As a result of this situation, deposits, loans, and interest calculations in the provident fund have not been made in accordance with prescribed procedures. However, the total effect on the overall fund balance and the individual employee accounts is unknown because a complete audit has not been done.

Therefore, (1) the provident fund and individual employee balances should be audited immediately to determine the effect of improper transactions; (2) the provident fund should be subject to an annual external audit; and (3) NAA should make deposits and withdrawals from the provident fund in accordance with prescribed procedures.

Inadequate Personnel Records and Procedures

Good management practices require that there be centralized, complete, and regularly updated personnel files for each employee and personnel procedures.

NAA's personnel records and procedures are not kept centrally. Several different files contain personnel information such as resumes, leave cards, medical questionnaires, hiring reports, and personal history cards. Some personal information such as numbers of children and marital status were not updated on a regular basis until October 1995. As a result, it is difficult for NAA staff to (1) ensure the completeness of and safeguard the records and (2) compute and/or audit salary allowances and benefits. This enabled the previous finance officer to destroy certain personnel records. Also, in at least one case, the allowance for an employee's dependent children was incorrectly computed. This situation is further discussed in enclosure 2 under "salary increase to replace dependent children allowance."

NAA should centralize personnel records, ensure their completeness, and update them regularly. Additionally, there should be a complete and centralized manual of NAA's personnel regulations and procedures.

Inadequate Leave and Attendance Records of the Secretary General

Good management practices require leave and attendance records for all employees.

NAA maintains leave and attendance records for all employees except the Secretary General. As a result, it is difficult to determine the leave balances and allowances of the Secretary General. It is also difficult to differentiate between his personal and official missions.

NAA should establish control over the leave and attendance records of the Secretary General.

Inadequate Control Over Salary Advances to Employees

Good management practices require strict control and management approval over salary advances.

NAA employees may be advanced salary payments without prior authorization, and several employees were receiving salary advances regularly. In 1994 and 1995, over 50 salary advances were paid, totaling about BEF 1.9 million (USD 60,000). While some were appropriate, such as to help the employees to meet the initial costs of settling in Brussels, the majority were not. As a result, (1) agency funds were used without proper authorization and approval, (2) funds were tied up in advances rather than available for other agency needs, (3) interest income for the amounts of advances was lost, and (4) NAA was subject to potential losses because the advances may not have been properly recorded and/or repaid.

Personnel regulations should include specific criteria for the granting, approving, and recovery of salary advances.

Overtime Paid to Belgian Employees Without Deduction of Belgian Tax

For Belgian employees, taxes should be deducted in accordance with Belgian law. However, income tax was not deducted for the overtime NAA paid to Belgian employees. In 1994 and 1995, NAA paid about BEF 785,000 (USD 26,000) in overtime directly to Belgian employees without deducting taxes. About 43 percent of the overtime was paid to one employee. As a result, financial transactions were not made in accordance with applicable laws and procedures, and NAA could be subject to fines and recovery of back taxes.

NAA must comply with all applicable laws regarding salary taxes. Further, NAA should seek tax and/or legal advice on the resolution of this matter with the Belgian government.

Representation Allowance of the Secretary General

The Secretary General should account for his representation allowance in the same manner as a NATO Assistant Secretary General. NATO requires that this allowance be audited annually and that receipts be provided for at least 75 percent of the allowance. The other 25 percent would be for using his residence for entertaining. However, from

1988 to 1994, the Secretary General did not account for his representation allowance in accordance with NATO requirements. Additionally, he submitted his entertainment bills for payment directly from the NAA budget. Thus, the allowance, which was not used to pay his entertainment bills, effectively became a supplement to his salary. In May 1993, according to the NAA auditor, he informed the Treasurer that the representational allowance was not being accounted for in accordance with NATO rules. However, no change was made until 1995. In 1995, the NAA auditor reported on the representation allowance of about BEF 349,000 for the first time and determined that entertainment receipts covered only about 47 percent of the allowance received.

NAA should adhere to NATO regulations regarding the representation allowance. Additionally, NAA should consider recovery of the amount of entertainment expenses that were charged to the Assembly when they should have been covered by the representation allowance.

TRAVEL

Weaknesses in Approving , Controlling, and Reimbursing Travel Costs

According to NAA financial regulations, travel costs should be authorized, controlled, and paid in accordance with the strictest economy compatible with the proper functioning of the Assembly.

Travel costs are a major expense of NAA but were inadequately controlled and monitored by management. Specifically,

- required mission orders were not always filled out and properly approved;
- there was no numeric or equivalent control over mission orders to determine how much travel was authorized and how much is outstanding;
- mission orders did not include the total cost of travel, nor were they matched against actual expense vouchers;
- hotel rates in some instances exceeded standard allowances without prior authorization;
- there was no final approval for the total cost of a mission; and
- airline tickets were not required to be turned in with expense claims, nor were they matched with what the agency booked for travel.

NAA should establish a system of internal controls over travel that addresses the conditions outlined above.

NAA Funds and Personnel Resources Used for Private Travel

Assembly funds and personnel resources should be used only for official purposes. However, at NAA, official funds and personnel resources were used to reserve and pay for personal travel subject to future reimbursement. For example, some employees made frequent trips out of the country for personal reasons, but NAA booked and paid for these trips. During our review, we identified 169 transactions totaling about 865,000 BEF. In other instances, Assembly resources were used to reserve and book personal travel, but agency funds were not used.

As a result of this practice, (1) NAA funds were used without proper authorization and approval, (2) funds were tied up in personal travel payments rather than available for other needs, (3) interest income was lost on the amounts of personal travel paid, and (4) NAA is subject to potential losses because personal travel payments may not have been properly recorded and/or repaid.

NAA should use its funds and resources only for official purposes.

Inadequate Reporting of Travel Expenses

Good management practices require transparency, accountability, and routine management reports for major expense categories to ensure that expenditures are controlled, reported, and cost-effective.

After salaries, travel is the largest expense category for NAA. Travel statistics are not available to either internal or external management on a regular basis (monthly, quarterly, and/or annually) to show such things as total travel costs by time period; travel costs by senior management (Secretary General, Deputy Secretary General, Senior Director), other permanent staff, temporary employees, consultants and speakers, and the President and Treasurer; travel costs by session or to prepare for sessions; and other meaningful categories of expense.

In addition, mission orders are not prepared or documented in advance of travel of the Secretary General. Therefore, it is difficult to determine the extent of his travel and to distinguish between private and official travel compared to that which was envisioned.

In March 1994, some members of the Bureau requested that a report be published on the expenditures for the trips and activities of the leaders of the Assembly and members of the International Secretariat. A report was produced for 1993, but none was done for 1994 and 1995. The Assembly has recently started to collect the data to produce regular reports from 1996.

NAA should establish procedures for collecting and reporting travel expenditures. Additionally, mission orders should be prepared and documented for all staff, including the Secretary General.

PURCHASING AND DISBURSEMENTS

Weaknesses in Purchasing and Disbursement Procedures

Expenditures should be authorized, controlled, and paid in accordance with the strictest economy compatible with the proper functioning of the Assembly. However, NAA management did not control and monitor purchases and disbursements. Specifically,

- there was no segregation of duties among personnel for requesting, ordering, and receiving goods and services;
- when payment of an invoice was made, the requisition and invoice were not matched together or filed together;
- there were no policies for obtaining competitive bids or using approved vendors;
- bank statements were not reconciled to the NAA ledger accounts by an independent party (that is, other than the bookkeeper/preparer);
- policies and procedures for processing and recording transactions were not documented; and
- the policy for approval signatures on purchase orders was not consistently followed. In some cases, the orders did not have the appropriate signature, given the level of expenditure, and in other cases, no purchase order or any other authorization had been prepared.

NAA should establish a system of internal controls over purchasing and disbursing that addresses the conditions outlined above.

AUTOMATED DATA PROCESSINGWeaknesses in Controls Over Automated Data Processing

Adequate internal controls call for planning and controlling the automated data processing (ADP) function within the Assembly. This should be documented.

NAA has no written plan that compares and costs the options available and provides a clear vision of where it wants to be regarding ADP in the next few years. Additionally, NAA has no written ADP system descriptions or procedures regarding safeguards or backup mechanisms. For example, in a test of ADP safeguards, we entered the computer system, made hypothetical changes to stored data, and might have been able to save these changes without NAA management knowing about it. As a result, NAA could not demonstrate (1) what its future estimated costs are or whether all users' needs will be addressed; (2) whether there is a risk that it could purchase equipment that does not adequately meet future Assembly needs; and (3) whether there is risk of unauthorized access, manipulation, and/or loss of NAA data.

NAA should prepare and adopt an ADP plan. Further, NAA should obtain or prepare system descriptions that include built-in safety mechanisms and train staff accordingly.

AREAS WHERE THE INTERNATIONAL SECRETARIAT
COULD REDUCE EXPENDITURES

Article 5 of NAA's financial regulations states that the Assembly will observe the strictest economy compatible with the proper functioning of NAA. In addition, the NAA Standing Committee ruled that the Secretary General's salary and all applicable allowances are linked to those of a NATO Assistant Secretary General. Although NAA management has not further defined this standard of economy, we believe that the International Secretariat often spends NAA funds extravagantly. During our audit, we noted instances in which funds were spent without what we would consider due regard for economy. We believe that if these practices were amended, the Assembly could save money, depending on the scale of economy desired by NAA management.

TWO OFFICIAL CARS THAT ARE NEVER USED SIMULTANEOUSLY

The International Secretariat has two official cars. The driver uses one car (a Ford) to drive from his home in Wavre to Brussels to pick up the morning newspapers and then to drive to the Secretary General's residence in Tervuren. He leaves that car at the Secretary General's house and drives the Secretary General in the second car (a Mercedes) to the International Secretariat in Brussels. After taking the Secretary General home in the evening in the Mercedes, the driver returns home in the Ford. The two cars are rarely used for official business at the same time. The cost of operating and maintaining the two cars is about BEF 300,000 per year, excluding depreciation and the cost of the driver.

When the Secretary General is away, the driver uses the Ford to drive to and from work. Furthermore, the Secretary General has personal use of the Mercedes in the evenings and during weekends. NATO transportation policies do not provide similar benefits to Assistant Secretaries General or NATO drivers.

OVERTIME PAID TO DRIVER

NAA policy requires that employees be given compensatory time instead of overtime payments unless there are exceptional circumstances. However, the Secretary General's driver regularly gets paid overtime. For example, in an 8-month period in 1995, he was paid an average of about BEF 25,000 per month for overtime. Given that the Secretary General travels extensively, it appears reasonable that the driver could use compensatory time when the Secretary General is away on travel, thus saving all overtime payments.

SALARY INCREASE TO REPLACE DEPENDENT CHILDREN ALLOWANCE

The Secretary General's driver has received annual cost of living increases and significant salary increases during his employment (a monthly increase of BEF 6,593 in January 1987 and BEF 13,623 in July 1987). In January 1995, the driver's monthly salary was increased by BEF 15,772 (USD 525) to replace the dependent children allowance he was no longer entitled to receive. As a result, the driver's 1996 gross salary, including overtime, will be almost BEF 2 million (USD 66,000). Such a precedent could lead to salary increases for other employees without regard to merit or other legitimate reasons. This is a continuation of the conditions that led the NAA Treasurer to request a study of the salary structure at NAA. The report on this study, issued in January 1995 and prepared by the NAA auditor, explains that the NAA salary structure was totally distorted by repeated irrational adjustments from 1987 to 1993.

PRIVATE TELEPHONE CALLS MADE AT NAA'S EXPENSE

NAA policy requires NAA employees to use their telephones economically. However, because NAA does not have a system for filtering personal calls from official calls, employees can and do make personal long-distance calls at NAA's expense. The NATO telephone system tracks these personal calls so that employees pay for them. In 1994 and 1995, NAA spent a total of BEF 4.3 million (USD 143,000) for telephone, fax, and telex services and does not know how much of this was for personal use.

QUESTIONABLE TRAVEL COSTS

Travel related to plenary sessions is a major NAA expense item. Many of the travel expenses of planning and conducting the two annual plenary sessions are unavoidable. However, the Assembly has not minimized travel costs by using host country staff to provide temporary support and assistance. International Secretariat staff generally made three, and up to five, trips to organize sessions, and almost all staff attended the two annual sessions. Additionally, numerous temporary employees, including some relatives of permanent staff, were hired from Belgium and other countries to help prepare these meetings. For example, the Assembly regularly hired a person who lives in Germany as a temporary assistant to the Secretary General. Table 1 lists expenses we identified, which total about BEF 256,000 (USD 8,500), of the personal assistant who attended the four sessions held in 1994 and 1995.

Table 1: Itemized Expenses of the Temporary Assistant to the Secretary General (1994-95)

Expenses in Belgian francs

Cost per NAA records	Session				Total
	May 1994 Oslo	Nov. 1994 Washington	May 1995 Budapest	Nov. 1995 Turin	
Transportation	16,750	15,100	21,010	6,946	59,806
Hotel	11,600	27,113	22,594	3,670	64,977
Per diem	14,500	14,008	14,400	12,385	55,293
Salary	13,250	13,250	15,000	15,000	56,500
Travel allowance	1,325	5,300	1,325	3,000	10,950
Miscellaneous (taxi, etc.)	1,418	2,520	436	0	4,374
Newspapers for Secretary General	1,605	124	480	0	2,209
Drinks for Secretary General	1,710	0	0	0	1,710
Total	62,158	77,415	75,245	41,001	255,819

PAYMENT OF QUESTIONABLE ENTERTAINMENT EXPENSES

Several members of the International Secretariat's staff were reimbursed for questionable hospitality expenses. While management took action in 1995 to control these expenses, in several instances, questionable entertainment expenses were still being charged to and paid by the Assembly. For example, the travel clerk charged expenses for entertaining Lufthansa agents at lunch.

NAA should consider disallowing these charges.

BUSINESS AND FIRST CLASS TRAVEL

Generally, NAA follows travel regulations similar to those prescribed by NATO. However, we noted some differences. In some instances, the Secretary General was allowed to travel first class. Under NATO rules, Assistant Secretaries General are allowed only business class travel. Also, NAA allowed staff to fly business class in some instances when such travel would be unacceptable under NATO rules.

NAA may want to consider following NATO guidelines on the use of first and business class travel.

PAYMENT FOR SECURITY SYSTEM AT SECRETARY GENERAL'S RESIDENCE

The International Secretariat has paid for the security system at the private residence of the Secretary General. NATO rules do not authorize such a payment for the Assistant Secretary General. Excluding the initial installation cost, NAA paid in 1994-95 a total of BEF 311,266 (USD 10,375) for the operation and maintenance of the system.

COMMENTS FROM THE NORTH ATLANTIC ASSEMBLY



NORTH ATLANTIC ASSEMBLY
ASSEMBLÉE DE L'ATLANTIQUE NORD
(NATO Parliamentarians - Parlementaires de l'OTAN)

The Secretary General
Le Secrétaire général

Mr. Bjørn Olsen
Chairman IBAN
NATO
Brussels

2 May 1996

Dear Mr. Olsen,

This paper has been discussed with the President of the North Atlantic Assembly and is forwarded to you with his approval.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'Peter Corterier', written over a light blue horizontal line.

Peter Corterier

Comments on the GAO/IBAN Management Review of Internal Controls

2 May 1996

This paper represents a preliminary reaction that may need to be corrected in the light of further audits or Bureau deliberations.

Introduction

The International Secretariat discovered the abuse and misuse of funds shortly after the termination of the former finance officer's contract in May 1995. Legal advice was sought immediately. Legal proceedings to recover the losses were initiated and are continuing. Many, though not all, of the shortcomings listed in the report were identified by the International Secretariat during 1995 and the International Secretariat was well aware that substantial corrective measures were needed. These, however, had to be introduced with the minimum disruption of the Assembly's normal work. At the same time, several factors operated to slow down reforms. Instructions for operating accounts had been removed and many files had disappeared.¹ Preparations for the legal case and detailed investigations into the activities of the former finance officer placed extremely severe demands on Assembly staff during the second half of 1995. In addition, personnel in the finance department were reorganized and had to familiarize themselves with matters which had been performed exclusively by the former finance officer. Furthermore, the Secretary General underwent serious surgery during the summer of 1995 which resulted in a prolonged absence.

The key problems were reported to the Bureau at the first meeting in Turin in October 1995 that took place following the termination of the former finance officer's contract. The Bureau decided to invite GAO and IBAN to conduct a financial management review, a decision that was welcomed by the International Secretariat. When the GAO/IBAN team conducted its review, the International Secretariat was pleased to explain all shortcomings that it had identified (and others identified by GAO/IBAN) and it greatly appreciated the professional advice and assistance that the GAO/IBAN team provided on these shortcomings.

"Results in Brief"

The matters raised in the section entitled "Results in Brief" are addressed in detail under the relevant headings.

"NAA LACKS ADEQUATE INTERNAL CONTROLS"

In the opinion of the International Secretariat adequate financial controls as outlined in the report were impossible to implement before May 1995 because of the former finance officer's exclusive control over financial matters. The International Secretariat is now reviewing its procedures for registering budgetary commitments and obligations. Since

¹ Accounts data had also been deleted from the computer system but this was rapidly recovered from a back-up.

May 1995, details of expenditure in each budget category have been provided to all budget holders much more rapidly. Individual budget holders are responsible for ensuring that their orders do not exceed the available budget. Those budget categories that have been overspent have been for items such as legal advice and recruitment which vary unpredictably. The overwhelming majority of budget categories are underspent.

The International Secretariat closely examined the performance of its accounting software upon the departure of the finance officer in May 1995. One result of this was the more rapid preparation of information on spending and another was the introduction of an up-grade introduced on 1 January 1996² which – among other things – enables the preparation of detailed statistics on items such as travel.

The audit report quite rightly points to the inadequate segregation of duties that existed in the finance office and the lack of managerial control in the finance department. The former finance officer's monopoly on financial management was challenged on several occasions but these challenges were successfully rebuffed with the support of the former Treasurer. Naturally, duties have now been segregated.

Overtime payments applied to two members of staff in 1995 and were made in accordance with practices that had been in place for over two decades. It appears that these were initiated with the tacit approval of the Belgian authorities at the time. Senior management was never subsequently informed of any potential problems in this area. Legal consultations are in progress on this matter.

The single employee who regularly received large overtime payments was the driver. This funding was explicitly requested and approved in NAA budgets until 1994 when the budget item was moved from "Transport" to "Salaries" at the request of the NAA's auditor. Another employee received overtime payments during 1995 and early 1996 due to the exceptional circumstances in the period of transition in the finance department. (Article 5 of the Regulations Governing Overtime states, "Generally speaking, overtime is compensated for in days and hours. In very special circumstances, the Secretary General may authorise payment instead..."). The issue of overtime was never debated in the Standing Committee.

Audit arrangements were established by the Treasurer and approved by the Standing Committee. Auditors have been recently-retired NATO auditors who have worked under the authority of the Treasurer. The auditor himself is best placed to explain why he did not report restrictions on his authority and independence, and his opinion that his mandate was not adequate.

² It was not possible to perform the up-grade while the 1995 accounts were still open.

Regarding the Rules of Procedure, the International Secretariat strongly supports changes that would ensure that the Secretary General has full access to financial data.

Regarding matters of economy, the audit team has no experience of an Assembly Session. Sessions do require a great deal of liaison between the host nation and the International Secretariat. All the NAA staff that attend Sessions have duties to perform at Sessions. Only one relative of the permanent staff has been employed at Sessions. The relatives that assist in Session preparations are students – some of whom are related to permanent staff members – who assemble dossiers and load freight before Sessions.

A review is underway of the staff requirements and of job functions for sessions. Substantial cuts were already made in 1987. In 1984 the total number of staff was 90. This was reduced to 80 in 1985. In 1987 a further 20 posts were cut at the request of the new Secretary General, Peter Corterier, and through the elimination of certain services. The number has grown slightly again, (67 in Turin), due mainly to the substantial increase in participants (up by 30%).

The specific cases referred to at the end of this section are addressed as appropriate in the commentary on the Enclosure.

RECOMMENDATIONS

The International Secretariat endorses the recommendations.

It should be noted that if the NAA International Secretariat were to become administratively linked to NATO, the financial implications would have to be calculated very precisely. Considerable savings in taxes would be realized but salary costs could increase since all but three NAA staff salaries fall well below the NATO standard.

However, the financial implications would depend on the type of relationship established.

ENCLOSURE 1***LACK OF INTERNAL CONTROLS AT NAA******OVERALL CONTROL ENVIRONMENT******Inadequate Funds Control System***

Article 7 of the Assembly's financial regulations states that "The Treasurer shall set up such internal controls as may be necessary to maintain a continuous check of all financial transactions."

The Assembly introduced new accounting software in 1992. The former Treasurer and the former finance officer together set the specifications and requirements which did not include a system for registering commitments and obligations. In addition, they insisted on separating this system from the main computer system and on complete confidentiality in finance. After May 1995, the International Secretariat greatly improved the speed with which budget holders were provided with information. The International Secretariat will investigate whether budget holders can themselves monitor commitments and obligations or whether and how these should be monitored centrally. As noted earlier, overspending has only occurred in very few budget categories such as recruitment and legal advice where spending is particularly difficult to predict.

The former Treasurer and former finance officer rejected the Secretary General's efforts to introduce even basic additional controls such as a double signature on cheques.

Inadequate Segregation of Duties in the Finance Department

The International Secretariat greatly appreciates the professional advice offered by the audit team. Duties have been segregated accordingly.

Improper Control Over NAA Finance by Former Finance Officer

This assessment supports the discoveries made by the International Secretariat of the activities of the former finance officer.

Unclear Lines of Authority

Again, this assessment is in line with the views of the International Secretariat on the need to clarify and re-define the roles of the Treasurer, the Secretary General and the finance officer.

Lack of External Audit

The International Secretariat agrees that an external audit should be performed regularly.

"Falsification of NAA Records"

This refers to the situation prior to May 1995 whereby the former finance officer did not report irregularities to the Secretary General. The case came to light in November 1994. The Bureau was briefed in February 1995 and decided on an appropriate course of action which was implemented by the Secretary General.

"Unauthorized Use of the Signature Stamp"

It is surprising the bank did not question this practice in view of the evident artificial nature of the signature produced by the stamp which was normally used for bulk mail. The use of the signature stamp was discontinued in July 1995 as soon as this practice was uncovered by the International Secretariat.

"PAY AND BENEFITS"**"Weaknesses in the Administration and Management of the NAA Provident Fund"**

This was the first irregularity uncovered by the International Secretariat following the departure of the former finance officer. The International Secretariat fully supports the recommendations in the report. The International Secretariat began preparing new rules for the Provident Fund during 1995 and will propose a number of short-term measures for the Standing Committee's consideration at the Athens Session. New statutes for the Provident Fund can then be adopted at the Annual Session. Since June 1995, the Provident Fund has been administered in accordance with the existing rules, drawing where necessary on appropriate NATO guidelines and with the Treasurer's agreement.

"Inadequate Personnel Records and Procedures"

The former finance officer prevented consolidation of these files and prior to her departure destroyed or removed a great deal of material in her care. Even so, better consolidation should have been achieved during 1995 and this is now being rectified.

"Inadequate Leave and Attendance Records of the Secretary General"

These practices were in place when the current Secretary General was appointed. Such records are now kept.

"Inadequate Control over Salary Advances to Employees"

For many years, the previous finance officer had taken it upon herself to grant salary advances (including to herself) and not to report these to senior management while junior staff assumed that the finance officer was complying with appropriate procedures.

The statistics in the report do not adequately distinguish between the situation before and after the departure of the former finance officer.

Any request for salary advances must now be referred to the Secretary General.

"Overtime Paid to Belgian Employees Without Deduction of Belgian Tax"

As noted earlier, legal consultations are taking place on this matter. Whatever the outcome, the Secretary General has discontinued paid overtime to avoid any future problems.

"Representation Allowance of the Secretary General"

On taking up his appointment, the Secretary General was informed by the then Treasurer and finance officer that entertainment bills should be submitted for reimbursement. The "duty allowance" and the reimbursement of entertainment expenses were operated in the same way as they had been for the Secretary General's predecessor.

When the Treasurer at the Bureau meeting in Washington DC in November 1994 pointed out that the allowance was handled differently at NATO and the NAA, the Secretary General – who was never informed of this before 1994 – agreed to adopt the NATO practice for his allowance as of 1995, a decision approved by the Bureau.

The Secretary General was unable to fully use his representation allowance in 1995 due to a prolonged illness. As soon as the precise figures became available (in the auditor's report on the representation allowance) the Secretary General arranged with the Treasurer to reimburse the appropriate sum.

The Assembly's lawyer has determined that it is not possible to claim for the recovery of the entertainment expenses charged to the Assembly.

"TRAVEL"

"Weaknesses in Approving, Controlling and Reimbursing Travel Costs"

Practices were tightened up greatly by the present Secretary General. The audit team's advice on procedures is very helpful and most of the measures mentioned have been adopted. The remainder could be implemented in a variety of ways and the advice of the NATO Financial Controller's office is being sought to establish the most efficient and effective.

Regarding the choice of hotels, NAA staff do not usually have any choice in the matter. National delegations select the hotels and staff members are required to be in the same hotel as their members, as is the standard practice in member parliaments. If members wish NAA staff to stay at other hotels during Sub-Committee visits, the International Secretariat will, of course, comply with that wish.

"NAA funds and Personnel Resources Used for Private Travel"

This was a long-standing practice whereby payment for personal travel would be deducted from the staff member's salary. Unfortunately, with certain staff making almost weekly train journeys home or for study, the number of transactions became quite high. No instances have been found where the finance department failed to deduct a personal travel bill from the appropriate salary. The practice has now ceased.

"Inadequate Reporting of Travel Expenses"

As noted earlier, the auditors' advice on practices and procedures relating to travel has been very helpful. The software up-grade introduced on 1 January 1996 enables detailed statistics on travel to be prepared.

The Secretary General now prepares mission orders.

The appropriate procedures for the authorisation and subsequent reporting of the travel of the President and Secretary General still have to be discussed by the Bureau.

"PURCHASES AND DISBURSEMENTS"**"Weaknesses in Purchasing and Disbursement Procedures"**

As noted earlier, advice on the segregation of duties in the finance department has been implemented. Every effort is being made to segregate duties for requesting, ordering and receiving goods and services but this is more problematic in a relatively small office. The International Secretariat has, however, introduced closer supervision by senior management pending more detailed advice from NATO personnel.

All other points mentioned under this heading have been or are being addressed. It should be noted that although procedures for competitive bids were not well-documented, large purchases were regularly made via competitive bids.

"AUTOMATED DATA PROCESSING"

The NAA's computer system was replaced in May 1992 and at the insistence of the former Treasurer and the former finance officer, the accounts system was separated from the rest of the system a few months later. In January 1996, the accounts system was reintegrated to the main system. The system architecture is well documented and work-station up-grades have been listed. A full back-up is performed automatically every 24 hours and this includes all financial data. Internal communications on equipment and software are extremely good and the likelihood of purchases being made that do not meet Assembly needs is very low.

The audit team was only able to enter the system by being given an authorized user password. The accounts software manufacturer has reassured the NAA that the type of data manipulation mentioned would be extremely difficult to conceal. Many separate but co-ordinated changes would have to be to several sets of data.

It is certainly true that the NAA should have a written ADP plan. This will be prepared as soon as possible.

"AREAS WHERE THE INTERNATIONAL SECRETARIAT COULD REDUCE EXPENDITURES"

"TWO OFFICIAL CARS THAT ARE NEVER USED SIMULTANEOUSLY"

The Ford station wagon is being offered for sale.

A record will be kept of the use of the official car.

"OVERTIME PAID TO DRIVER"

Overtime payments for the driver were explicitly listed and approved in the NAA's budget under "Transport" until the auditor requested that this sum be listed under the heading "Salaries". As already noted, the Secretary General has decided to discontinue the practice of paying overtime.

"SALARY INCREASE TO REPLACE DEPENDENT CHILDREN'S ALLOWANCE"

The previous Secretary General undertook to replace the driver/messenger children's allowance with salary. Legal opinion has confirmed that this was a legally binding commitment so that the Assembly could have been sued for breach of contract had it not been honoured. No other employees received a similar commitment so there is no question of this setting a precedent.

"PRIVATE TELEPHONE CALLS MADE AT NAA'S EXPENSE"

All telephone calls are automatically registered showing the extension, the number called and the call's time, duration, and cost. Private calls must now be reimbursed.

"QUESTIONABLE TRAVEL COSTS"

Sessions require a great deal of preparation. NAA staff and staff from other organizations such as national parliaments are assigned a variety of duties at Sessions. Expertise and continuity are important. Only one relative of a member of permanent staff has assisted at Sessions in recent years. A list of duties has been prepared for review by the Bureau and the Standing Committee. The personal assistant mentioned has not been engaged for the Athens Session and the International Secretariat is conducting a detailed review of staff required for Sessions. Some reductions have already been made for the Athens Session.

"PAYMENT OF QUESTIONABLE ENTERTAINMENT EXPENSES"

It is not normally the practice to invite private sector representatives to lunch but there are occasions when it is warranted. The NAA does not have the same volume of travel and therefore leverage as, for example, NATO. Nevertheless, it has been able to negotiate very favourable terms, particularly with Lufthansa. The lunch in question was authorized by the Secretary General. This occasion was used to discuss a very favourable rate for NAA staff travel from Brussels to Turin for the 1995 Annual Session. Indeed, the price was better than competing prices proposed by Sabena and Alitalia. Good contacts with Lufthansa have also led to penalties being waived and even for refunds on Apex and Pex tickets when associate delegations have changed arrangements at the last minute or have missed connections.

"BUSINESS AND FIRST CLASS TRAVEL"

The NAA's travel rules are not, at present, identical to NATO's. The NAA has abided by its own rules. These can, of course, be reviewed and altered.

"PAYMENT FOR SECURITY SYSTEM AT SECRETARY GENERAL'S RESIDENCE"

In 1985, the headquarters of the North Atlantic Assembly was badly damaged by a terrorist bomb. The NATO Office of Security and the Belgian Foreign Ministry both recommended that a security system be installed at the residence of the Secretary General in 1987. The NATO Office of Security has expressed its continued support for the operation of this system. Options for reducing operating costs for this system are being studied.

During the Ottawa meetings, the Bureau and the Standing Committee agreed that the system should be maintained.

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