

# Clearing House Process\*

NATO C-17  
Strategic Airlift Capability  
Financial Management:  
A Method for Multinational Funds Management  
and Payment Allocation



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# Addressing Complexities associated with Funds Management and Payment Allocation within a Multinational Environment

In addition to typical hurdles involving a major defence system acquisition programme, the NATO C-17 Strategic Airlift Capability (SAC) Consortium faces unique complexities associated with the joint procurement in a multinational environment. Although the programme's definition and construct will be determined in the foundational document, the consortium's Memorandum of Understanding (MOU), the document will not address the procedural detail necessary to accomplish immediate and effective programme management activities. Accordingly, the PricewaterhouseCoopers (PwC) Global Best Practices® Programme Management Office (PMO) Framework is a resource that may be used to verify that each required process is identified, defined, and all interfaces are addressed up-front and early in the programme (ideally before programme start). Specific financial management focus areas for the NATO C-17 SAC Programme include:

- **Programme Funding** - Our experience in other major defence programs such as the **US C-17 programme**, the **US F-15 programme**, and the **F-15 foreign military sale programme**, have clearly demonstrated the need for early, thorough planning to ensure the programme does not unnecessarily hold excessive and/or idle funds, yet has adequate funds available to cover current obligations. Robust planning will also reduce the programme's risk related to non-payment or late payment of validated invoices. As an integral part of the programme funding process necessary for a complex joint acquisition, planning must incorporate a predictable, repeatable, and auditable process. Planning must also provide the consortium the appropriate fidelity in periodic analyses along with the country specific funding profiles delivered to each SAC partner nation.
- **Payment and Expense Allocation** - The Programme must manage the processes associated with a number of activities to ensure timely and accurate payment allocation. Some of these activities include receiving and validating bills (i.e. Boeing, other suppliers, government entities, etc.) and allocating converted costs among SAC Partner Nations based on obligations determined in the MOU and emerging obligations. These activities enable the programme's ability to make prompt and accurate payments for goods and services rendered benefiting the NATO C-17 SAC Programme, as well as perform and track auditable currency conversions as specified in the MOU.
- **Internal Controls** – Given the complexities of the C-17 SAC Programme's financial management environment, internal controls are necessary in order to achieve effectiveness and efficiency of financial operations; reliability of financial reporting; and compliance with laws and regulations such as those defined by NATO. PwC provides financial services world-wide, performing audits and developing internal control solutions across multiple industries and multinational environments. The lessons PwC has learned from more than a century of experience enforces the need for robust and formal internal controls built into the organisation from the start to include repeatability and leadership commitment. Without properly defined and executed internal controls, inefficiencies, regulatory non-compliance, and exposure to unnecessary risk may result.

## PwC – Providing Financial Services World-wide

Clients include:

- 32% of the Fortune Global 500
- 34% of the FT Europe 500
- 42% of the S&P Latin America 100
- 38% of the S&P Asia Pacific 100



## Providing the C-17 SAC Programme with Content to Start-up and Operate Financial Management Processes

This paper provides the NATO C-17 SAC Procurement and Finance Working Group an example of how the PwC PMO Framework may be used to develop the processes and procedures necessary to effectively start and operate a PMO and “to create added value in an efficient and economical way.” The structure and approach are practical, risk based, and built upon best practices proven across multiple industries in complex multinational environments. In this case, the Financial Management function was chosen with an emphasis on Clearing House Process. In commercial terms, Clearing House is comparable to treasury operations of which this paper will draw from documented best practices.

*“Individual nations have chosen to team up and procure and deliver a critically needed Alliance capability - to create added value in an efficient and economical way”*

- Secretary General Jaap de Hoop Scheffer

## Framing a PMO Capability for Start-up and Operations of a Complex System Acquisition Programme

On 28-Aug-2007, the PwC Team presented a PMO Framework (Figure 1) to the NATO C-17 SAC Procurement and Finance Working Group. A well-managed and appropriately structured PMO is a significant factor in increasing the success of programmes. Best practices suggest the most effective PMOs are those staffed jointly with contractors and client personnel, driving the necessary collaboration and cross functional expertise to manage the multiple facets of a complex programme. In the case of the C-17 SAC programme, an integrated team of experienced contractors, Voluntary National Contribution (VNC), and NATO Maintenance and Supply Agency (NAMSA) personnel, is recommended to ensure desired outcomes.

The columns of the Framework represent major Elements of the PMO consisting of Programme Planning, Financial Management, Communications, Programme Control, Quality and Standards, and Logistics Life Cycle Support. Box 1 and Box 2 represent the phase associated with designing, staffing, and standing up the PMO. Boxes 3 through 26 represent activities within each PMO element. Clearing House Process (Figure 1, box 10) is an integral part of the overall Financial Management element and set of activities.

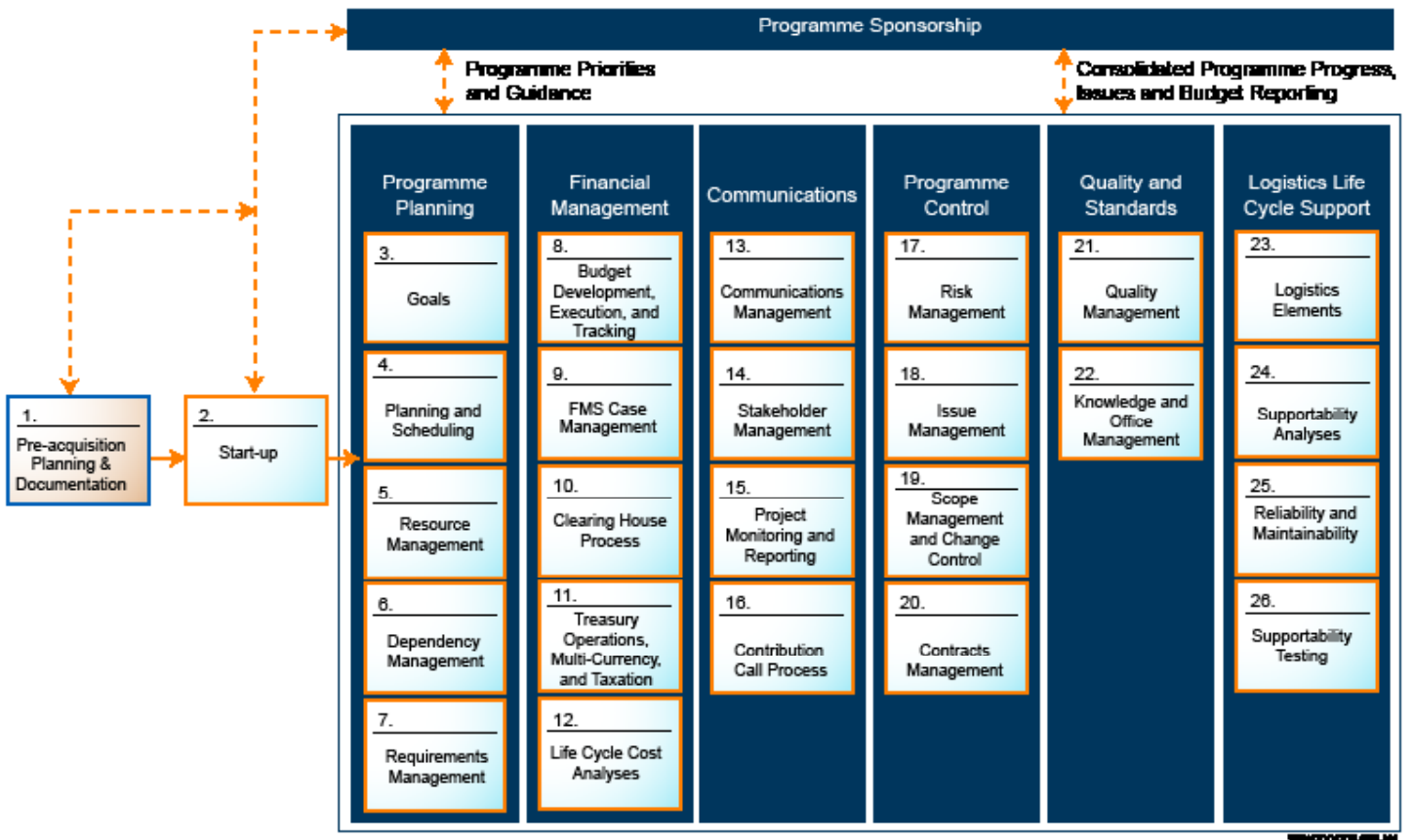


Figure 1: A Comprehensive and Mature PMO Capability

# Detailing Clearing House Process: An Integrated Set of Activities for Funds Management and Payment Allocation for the Multinational C-17 SAC Programme

The Clearing House process (Figure 2) may be the most demanding of the Financial Management activities. The challenges arise largely from the need to implement a clearly understood process that ensures transparency for the partner nations and is fully auditable against various international standards. Duplicate, erroneous, too frequent, or frequently contested contribution calls are the driving forces requiring a set of financial management processes that are carefully and knowledgeably constructed. Likewise, unnecessarily holding excess idle funds in order to minimize contribution calls is an inefficient use of the member's treasury.

Having experienced personnel define the processes with care, using best practices inputs, the programme can ensure the system and the interfaces of processes yield repeatable, verifiable, and auditable results enabling the programme's initial capability to operate effectively and efficiently with low risk.

## PwC Global Best Practices®

**Performance Measures.** Best in class organisations use robust indicators to demonstrate the value-added impact of their financial management and treasury or clearing house processes. These indicators or performance measures are most effective if they measure the performance of the activity along with the value-added to the overall organisation. Global Best Practices® such as *European Treasury Survey 2006: Measuring Value from Treasury*, which includes input from 166 multinational organisations operating in Europe will be used. Potential performance measures will be identified for each activity identified in Figure 3.

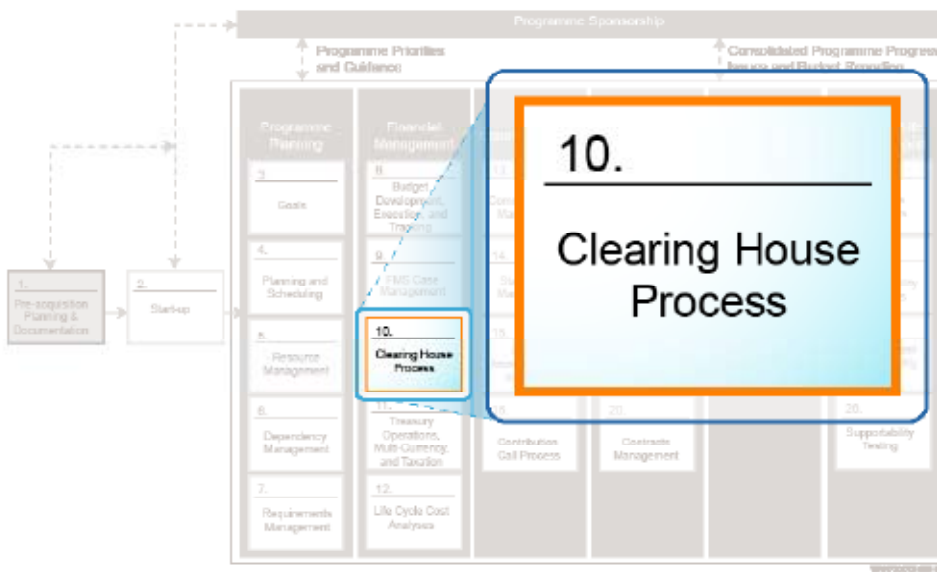


Figure 2: Ensuring Financial Transparency for C-17 SAC Partner Nations

The flowchart in Figure 3, illustrates the key activities within Clearing House process and associated financial management processes. The most effective way to describe Clearing House process is within the context of the broader set of Financial Management major activities.

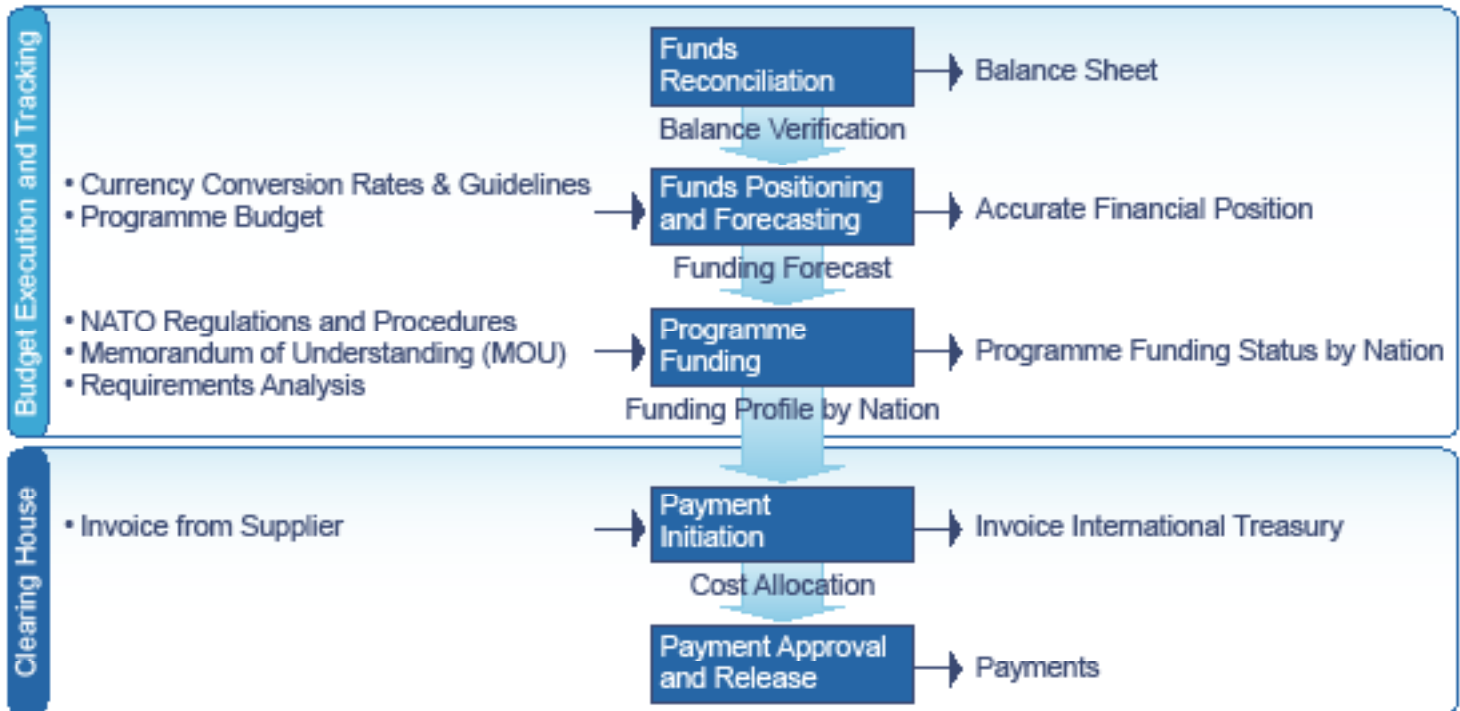


Figure 3: Enabling Funds Management and Payment Allocation

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### Budget Execution and Tracking: Funds Reconciliation (Figure 4)

Funds reconciliation is a significant internal control that provides the base from which the Clearing House operations begin. It is an auditable starting point for all financial operations. Although basic, the process of balancing the accounts payable with the accounts receivable to verify adequate funds are available, is a critical process feature.

Sample performance measures include: percentage of balance accuracy; margin of error in financial reports; and Standard reporting formats used.

#### **PwC Global Best Practices®**

- Streamline reconciliation procedures using automated reports and online tools.
- Perform timely account reconciliations.
- Identify and resolve reconciliation discrepancies in a timely manner.
- Segregate allocation and reconciliation duties.

### Budget Execution and Tracking: Funds Positioning and Forecasting (Figure 4)

Funds forecasting is the process of using historical and current data to project receipts and disbursements of cash flow in order to determine the optimal liquidity for growth and operations. In addition to increased visibility and more efficient financial planning, forecasting allows for: a more effective treasury organisation; increased awareness of multinational currency exchange fluctuations; lower risk of over-funding the programme's accounts payable and maintaining excess balances; and greater funding access to sustain operations.

Sample performance measures include: variance of actual against forecast; multiple time horizon forecasts; and forecasting errors.

#### **PwC Global Best Practices®**

- Use short-term, medium-term, and long-term forecasts.
- Clearly state assumptions.
- Track funds forecast accuracy monthly, comparing actual funds position to forecast funds position.
- Verify reporting and preparation responsibilities and timing are clearly defined.

## PricewaterhouseCoopers experience

For a \$6.3 billion global leader in the Agrochemical segment, created by the merger of two agribusinesses, PwC assisted the company in establishing an entire Treasury function. The company needed to put in place transitional fixes and permanent infrastructure

to integrate two different approaches to treasury, including organisation structure, policy, processes, banking structure, and a treasury system to meet the requirements of the businesses. The engagement included the successful development of all funds

### Budget Execution and Tracking: Programme Funding (Figure 4)

For the C-17 SAC Programme, NATO Regulations and Procedures and the MOU will dictate the funding and budget requirements for all associated functions. In accordance with the NATO Handbook, a major task of the Financial Controller is to ensure that the funds required to finance execution of the budget are periodically called up from contributing member countries in accordance with their agreed cost shares and in amounts calculated to avoid the accumulation of excessive cash holdings in the international treasury.

Sample performance measures include: shortfall vs. excess funds; savings on foreign exchange transactions; and cost shares and calculated amounts.

#### PwC Global Best Practices®

- Establish well-defined business objectives and risk appetite.
- Set and monitor performance measurements and standards.
- Monitor funds forecasting to identify the amount and timing of excess or shortfall of funds.

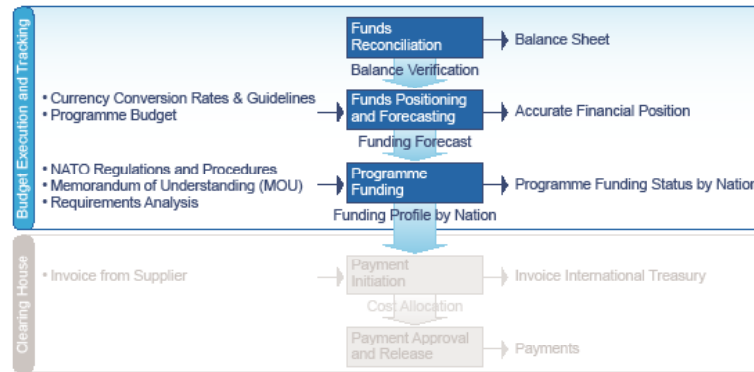


Figure 4: Budget Execution and Tracking

management operations, policies and procedures, and the implementation of a management system. PwC recommended new processes that would meet “best practices” and provide added control to the management of the company’s funds operation, and a structure that

would supply the platform for growth to the global firm. In the process of the engagement, PwC identified areas for improvements in funds management, forecasting, overall cash utilisation, and automation of manual activities.

### Clearing House: Payment Initiation (Figure 5)

Payment initiation is the process of receiving and verifying invoices to be true and accurate. Accounts Payable (A/P) and electronic funds transfer (EFT) activities should be managed with multiple goals in mind: certify the accuracy and authenticity of invoices; verify strict and documented segregation of duties; prevent duplicate payments and duplicate vendors; protect the vendor master file; ensure proper payment allocation to the various C-17 SAC partner nations; pay invoices on a schedule that is acceptable to both the organisation and the supplier without paying them 'early' and impacting working capital; and minimize the time and cost for processing A/P transactions.

Sample performance measures include: transaction processing speed; cost of processing receipts; and number of processing errors.

#### **PwC Global Best Practices®**

- Achieve 90%+ of invoices ready for payment within 2 days of receipt.
- Implement clean desk policy: all incoming mail is actioned within 24 hours.
- Date stamp in mailroom to establish actual date of receipt on premises.
- Track the number of incoming invoices in backlog (awaiting entry into A/P system) as a measure of productivity and workflow.
- Bypass the matching process for receipts less than a specified amount -- it is cheaper to accept and pay than perform the three-way match.
- Use results from matching resolution to establish materiality limits for initial matching process.
- Image processing of invoices for records keeping.

#### **PricewaterhouseCoopers experience**

For a large multi-national pharmaceutical company based in Europe, PwC was brought in to assist in the implementation of a finance shared services centre (SSC) leveraging an enterprise IT system. The current environment was de-centralized with banking arrangements managed by each individual country

with an "overlay" banking structure for Group Treasury. Additionally, each country managed its own funds, periodically transmitting status to Group Treasury. This resulted in inefficient and ineffective treasury and funds management operations. PwC started by conducting data gathering and analysis exercise to define the business

### Clearing House: Payment Approval and Release (Figure 5)

Once invoices have been audited and reviewed to ensure that authorized billing has occurred only for goods or services received and accepted in compliance with the terms and conditions of the contract, they are entered into the A/P system and are then ready for payment.

Sample performance measures include: percentage of invoices paid on time; days sales outstanding, duplicate payments or overpayments.

#### PwC Global Best Practices®

- Implement stringent payment approval, release, and stop-pay procedures. Ensure that only authorized personnel are performing these functions, and that all procedures are documented and kept up-to-date.
- Limit access to the Accounts Payable system input function. Limited access minimizes security breach opportunities and improves input audit trails.
- Perform a periodic treasury/internal audit review. Ensure that payment procedures are reviewed for effectiveness and that actual practices comply with mandated policy.
- Segregate allocation and reconciliation duties.
- Use integrated voice response (IVR) with fax back capability to simplify invoice status checking.
- On-line inquiry capabilities are provided for responding to calls from vendors and suppliers.

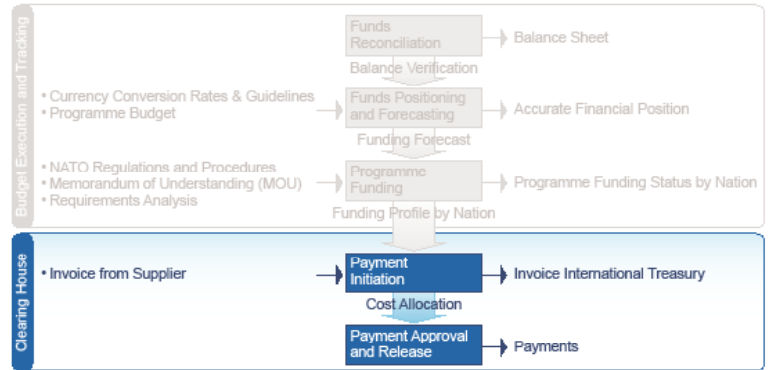


Figure 5: Clearing House

need for banking and funds operations. Based on this analysis, PwC, using banking expertise, designed a banking structure with Group Treasury taking into account the objectives of the SSC. Concurrent to the SSC design process, PwC assisted in the selection of a banking provider for comprehensive funds management services

for all businesses. The results included an efficient and flexible banking structure for all collections and payments as well as cash concentration in Europe; reduction in the number of banking relationships in Europe; automation of the daily cash concentration process; and improved corporate control.

## Internal Controls - Mitigating Risk in Financial and Clearing House Processes

Internal controls to mitigate risk are an important focus area for each Financial Management sub-process. In many organisations, controls are informal. Consequently, controls may not be known or adhered to, or may not be accomplishing their objectives. While management may believe controls are in place, they may not be functioning as intended, may not be fully implemented, or may not have been initially implemented at all.

For example, lack of segregation of duties can exacerbate control problems. In short, organisations with inadequate internal controls remain unprotected against risks they thought were being mitigated. Therefore, organisations are now actively seeking to enhance their internal controls, ensure the credibility of financial information, and receive the operating benefits that a strong system of internal controls can provide.

## Benefits of Internal Controls: A Closer Look

- Operational benefits
  - Clarity on roles and responsibilities
  - Reduced costs obtained from greater operating efficiency
  - Maximized operating performance
- Financial reporting benefits
  - Heightened credibility provided to all stakeholders
  - Better information to manage the business
  - Reduced risk of errors
- Regulatory benefits
  - Decreased risk of litigation or business disruption
  - Increased credibility with regulators
  - More credibility in contractual relationships





## Delivering Programme Success - Robust Financial Management Capability that is Worthy of Unprecedented SAC Partner Nation Commitment

The benefit of designing and implementing a PMO Framework as it relates to Financial Management and Clearing House is to expand the traditional view of programme success from viewing project outputs, to viewing the success of the programme-related business outcomes and benefits realisation. Generally, there is a relatively short timeframe to ensure that the programme benefits are captured and are integrated as a permanent part of an organisation's day-to-day activities. Anticipated benefits and outcomes of PwC's approach to PMO Clearing House and Financial Management activities include:

Together with the NATO C-17 SAC Procurement and Finance Working Group, programme success can be further ensured by integrating Financial Management capabilities as part of the project from its inception, all designed "to create added value in an efficient and economical way."

### Provides SAC partner nations the tools to plan, program, and execute funds

It is necessary for the PMO to establish processes that allow for adequate financial planning for each of the partner nations. This ensures proper cash flow into the PMO for payment disbursement, but also allows partners to justify the programme's expenses and plan for the long-term. The ability for partners to plan for future payments provides the overall programme a greater sense of stability and certifies long-term capital support from participating nations.

### Financial risk mitigation

Proper financial risk mitigation allows for additional funds to support operational requirements as opposed to financial overruns or unforeseen programme missteps. A detailed financial risk identification and mitigation plan verifies all aspects of the programme are being addressed from a risk perspective and provides greater clarity in the programme's overall financial picture.

### Improved flow of financial information permitting better business decisions

A timely and accurate financial picture allows the programme's leadership to make better business decisions, ultimately leading to the best use for all funding available to the consortium. This improved flow of financial information provides transparency in the financial management process and allows the programme to apply the funds available to the highest priority items.

### Integrity and reliability in financial governance and reporting

Integrity and reliability in the programme's financial management process is a derivative of the previous three benefits. Providing the tools to plan, program and execute, identifying and mitigating risk, while providing timely and accurate financial data to the programme decision-makers are the pillars to providing an honest and reliable assessment of the programme's financial picture.

## Call to action

The challenges with managing financial information on any large defence system can be significant given the size, scope and complexities associated with planning, execution and tracking, reporting, compliancy with laws and regulations, and managing accounts payable. Add to this 17 different 'owners' with different currencies; potentially significant tax and trade concerns; and a complex set of commitments and obligations defined by an MOU and complexities are magnified requiring a mature, robust and auditable financial management process.

Because of the complexity and because the Programme has an aggressive timeline, the financial management and PMO process definitions should begin as early as possible not just as a risk reduction effort, but as a means of moving quickly and smoothly into a full operational posture.



## The PwC Team - Unique Capabilities to support the NATO C-17 SAC Programme

The PwC Team includes PricewaterhouseCoopers LLP and BizDynamics LLC. Together, the Team brings world-class and global expertise in developing and operating programme management solutions for complex multinational environments. Our major weapon systems acquisition expertise includes hands-on experience transforming the C-17 Programme into a flagship acquisition programme, as well as many other major programmes.

### About PricewaterhouseCoopers LLP

PricewaterhouseCoopers (PwC) is the world's largest professional services organisation with more than 140,000 staff in 144 countries with strong residence in each of the 17 SAC Partner Nations. PwC has the world's largest Worldtrade Management Services practice in the industry with offerings to include international trade, multinational currency, and international tax optimization. PwC's global programme management capabilities include the start-up and operations of complex programmes for defence, homeland security/affairs, and commercial clients. Our dedicated Aerospace and Defence practice, working with the largest defence systems manufacturers globally, provides PwC a true end-to-end perspective on large defence systems acquisition. Finally, PwC's Global Best Practices® capability is the most robust in the industry built on data from nearly 3,000 organisations.

### About BizDynamics LLC

BizDynamics (BzD), founded as a programme management consulting organisation in 2003, possesses deep programme, acquisition management support, and training experience. BzD has extensive programme management credentials serving as Programme Director for the Joint Service Advanced Tactical Air Reconnaissance System (ATARS) programme and as the DoD Chair to the Defense Acquisition University Executive Institute. In addition, the firm's principal staff has served as the Deputy Programme Director for the C-17 and F-15 programmes. BzD has also provided services for the Secretary of the Air Force, the Assistant Secretary of the Army and the Commander of Air Force Materiel Command (AFMC) on acquisition leadership issues within the past year.

For further information, please contact:

Jiri Halouzka  
jiri.halouzka@cz.pwc.com  
+420 251 152 042

Jos Verstraten  
jos.verstraten@nl.pwc.com  
+31 10 407 5671

Jeff Affuso  
jeffrey.affuso@us.pwc.com  
+1 703 918 3664

Photo Credit(s):

Master Sgt. Burke Baker (cover)  
Tech. Sgt. Russell E. Cooley IV  
Tech. Sgt. Russell Gardner

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