



Auditing armament projects – the industry perspective

Klaus Neumann | Head of Accounting | Luxembourg | 15 May 2019

MOBILITY. SECURITY. [PASSION.](#)



Agenda

01 Rheinmetall Group

02 Audit and financial control overview

03 Financial controls on projects

04 Practical challenges for defence companies



01 Rheinmetall Group

MOBILITY. SECURITY. **PASSION.**



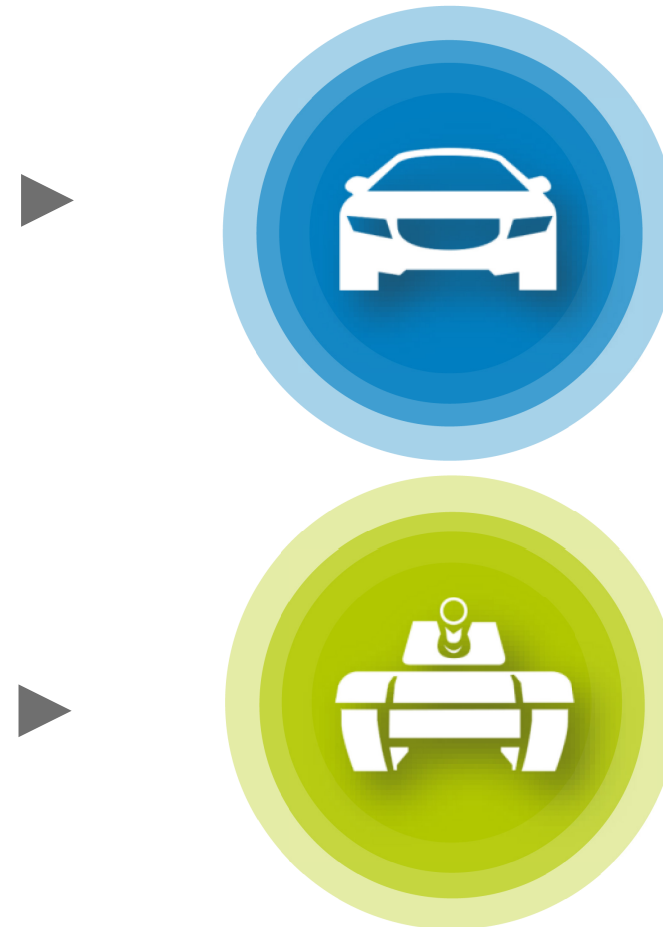
01 Rheinmetall Group

About Rheinmetall

Rheinmetall was established in 1889 as Rheinische Metallwaren- und Maschinenfabrik Aktiengesellschaft.

Today, Rheinmetall AG, publicly listed and based in Düsseldorf, is a powerful, internationally successful corporation and is the management holding company of the Rheinmetall Group. As an integrated technology group, Rheinmetall is a market leader in the areas of environmentally friendly mobility and threat-appropriate security technology.

The group's operating activities are split into the two corporate sectors, Rheinmetall Automotive and Rheinmetall Defence.



01 Rheinmetall Group

Mobility and security under one umbrella

Rheinmetall Group

6.1 €billion
SALES

492 €million
OPERATING RESULT

24,949
EMPLOYEES

Rheinmetall Automotive
Our heart beats for your engine

2,930 €million
SALES

12,855
EMPLOYEES

Rheinmetall Defence
Force protection is our mission

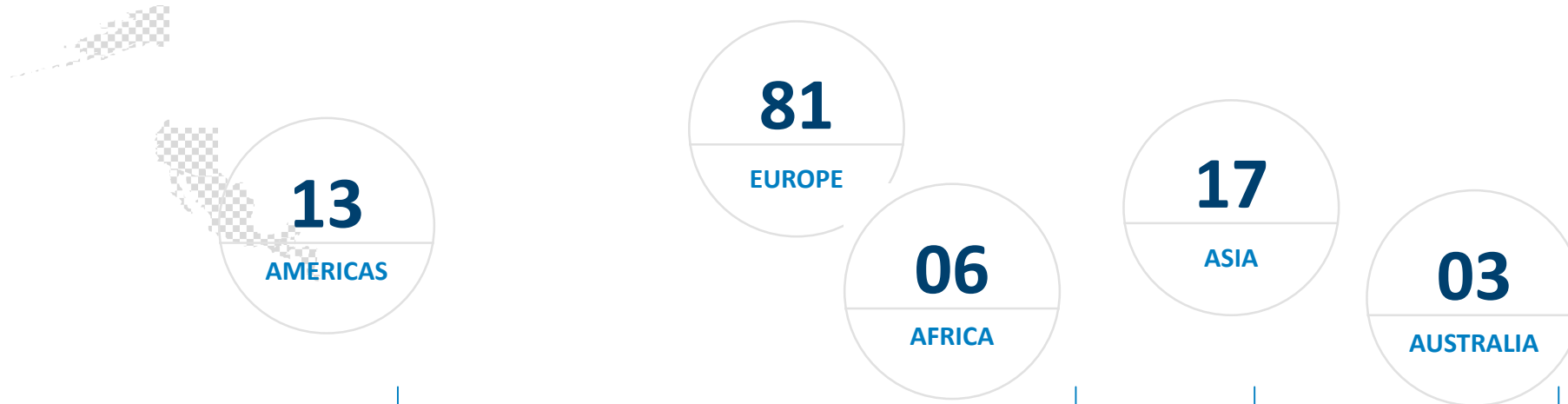
3,221 €million
SALES

11,832
EMPLOYEES

Fiscal year 2018

01 Rheinmetall Group

Rheinmetall locations *international*



AMERICAS	EUROPE GERMANY	EUROPE	AFRICA	ASIA	AUSTRALIA						
BRASIL Nova Odessa CANADA Ottawa St.-Richelieu MEXICO Celaya Mexiko-Stadt USA Auburn Hills / MI Biddeford / ME East Camden / AR Greensburg / IN Greenville / SC Marinette / WI Stafford / VA Wilmington / DE	GERMANY Aschau am Inn Berlin Bonn Bremen Dormagen Düren Düsseldorf Flensburg Gardelegen (Letzlingen) Gera Hallbergmoos Hamburg Hartha Harzgerode (Silberhütte)	Heilbronn Papenburg Jena Kassel Koblenz Kiel Krefeld Langenhagen Lohmar Mainz Munich Neckarsulm Neuenburg Neuenstadt Neuss	Oberndorf Rostock Röthenbach (Pregnitz) Schneizlreuth (Fronau) St. Leon-Rot Stockach Tamm Trittau Unterlüß Walldürn Wedel	BELGIUM Brussels FRANCE Le Blanc Mesnil Meyzieu Roissy (Villepinte) Thionville ITALY Domusnovas Ghedi Lanciano Livorno Pescara Rome	LITHUANIA Vilnius NETHERLANDS Ede Hengelo Nøtterøy AUSTRIA Schwanenstadt Vienna POLAND Gliwice Warsaw ROMANIA Campia Turzzi	RUSSIAN FEDERATION Moscow SWEDEN Stockholm SWITZERLAND Altdorf Bern Lohn-Ammannsegg Studen Thun Urdorf Wimmis Zurich	SPAIN Abadiano Amorebieta CZECH REPUBLIC Trmice Ústí nad Labem Chabařovice UNITED KINGDOM Bristol Isle of Wight Kirtlington London Swindon	SOUTH AFRICA Boskop Maitland Potchefstroom (Boksburg) Pretoria Somerset West Wellington	CHINA Chongqing Kunshan Shanghai Yantai INDIA Mumbai Pune (Takwe) Supa JAPAN Hiroshima (Takaya) Odawara (Kanagawa)	MALAYSIA Malacca SAUDI ARABIA Riyadh SINGAPORE Singapore SOUTH KOREA Seoul TURKEY Ankara Istanbul UAE Abu Dhabi SAIF-Zone, Sharjah	AUSTRALIEN Adelaide Brisbane Melbourne

01 Rheinmetall Group

Key facts 2018 Rheinmetall Defence

3,221

SALES €MILLION

254

OPERATIVE RESULT €MILLION

101

CAPITAL EXPENDITURE €MILLION

11,832

EMPLOYEES

8.6

ORDER BACKLOG €BILLION

4.4

R&D INTENSITY %

01 Rheinmetall Group

Leading European Defence Company



Weapon and Ammunition

Weapon and Munition

Propulsion Systems

Protection Systems

Electronic Solutions

Air Defence & Radar Systems

Integrated Electronic Systems

Technical Publications

Vehicle Systems

Logistic Vehicles

Tactical Vehicles

01 Rheinmetall Group

Rheinmetall Defence - Divisions

Corporate sector	Division	Areas of activity
Defence	Vehicle Systems	Armored tracked vehicles NBC protection systems Turret systems Wheeled logistics vehicles Wheeled tactical vehicles
	Weapon and ammunition	Large and medium caliber weapons and their ammunition Weapon stations Protection systems Propellants and powder
	Electronic solutions	Air defence systems Soldier systems Command, control and reconnaissance systems Fire control systems Sensors Land simulation, flight simulation, maritime and process simulation





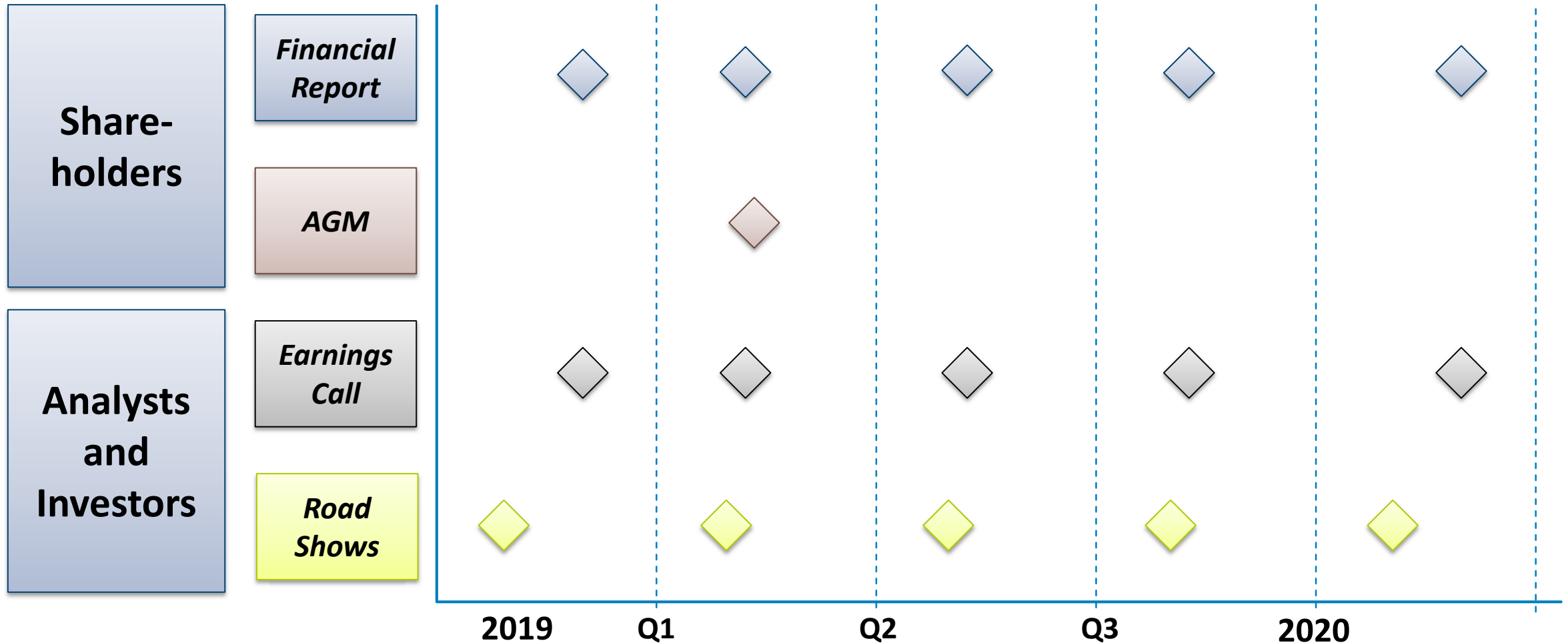
Practical challenges for defence companies

02 Audit and financial control overview

MOBILITY. SECURITY. **PASSION.**

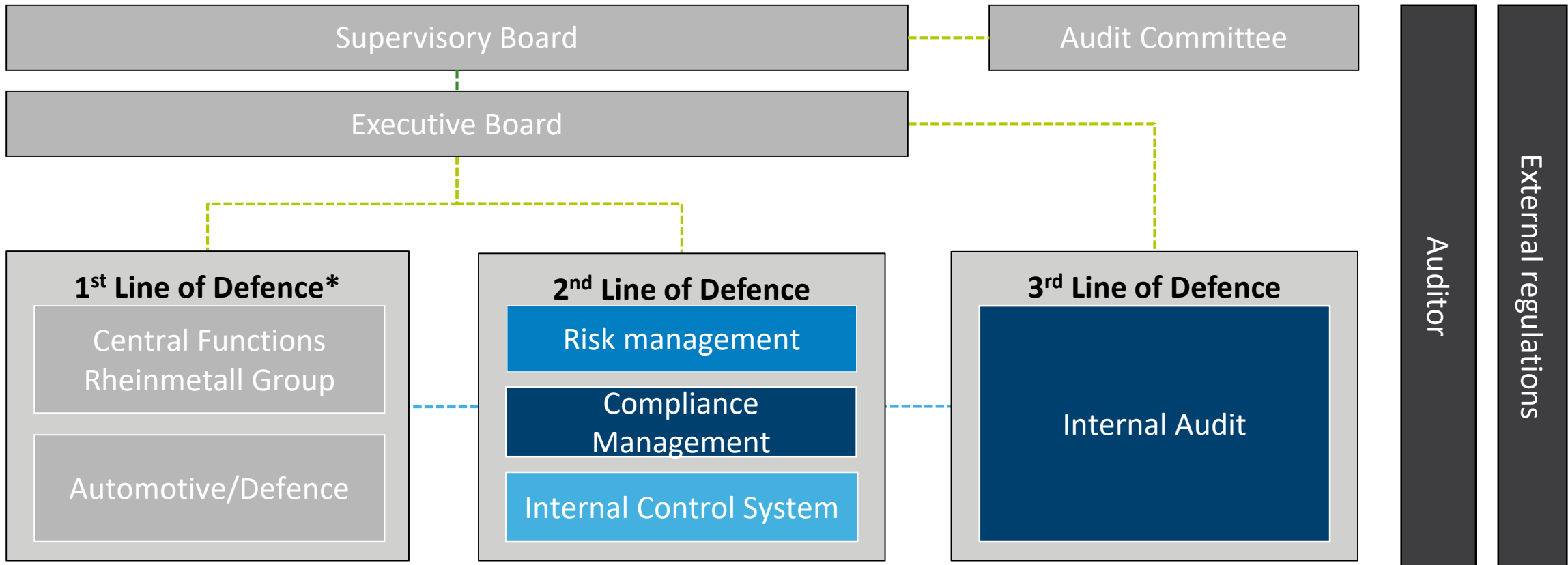
02 Audit and financial control overview

Financial communication to stakeholders



02 Audit and financial control overview

Three lines of defence

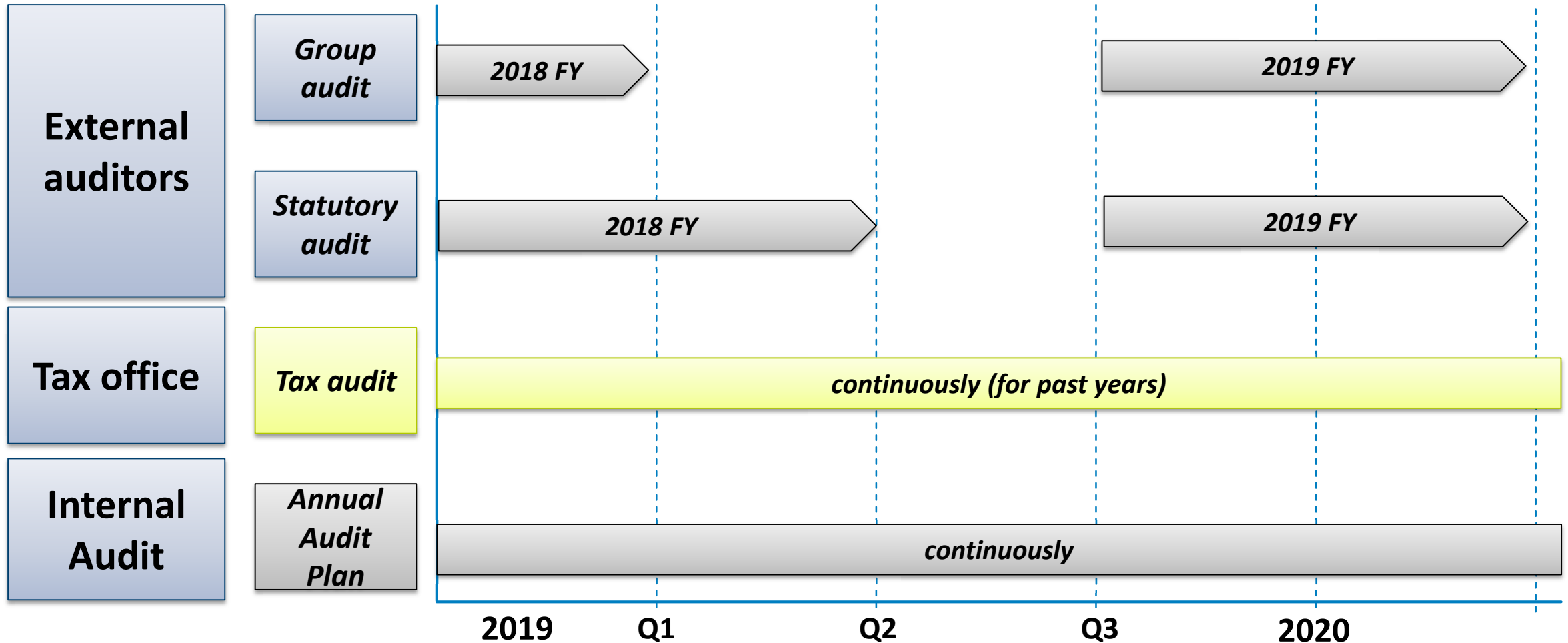


--- Functional reporting line
- - - Coordination

* Responsibility: Ensuring compliance with requirements;
Implementation of control measures

02 Audit and financial control overview

Internal and external audits



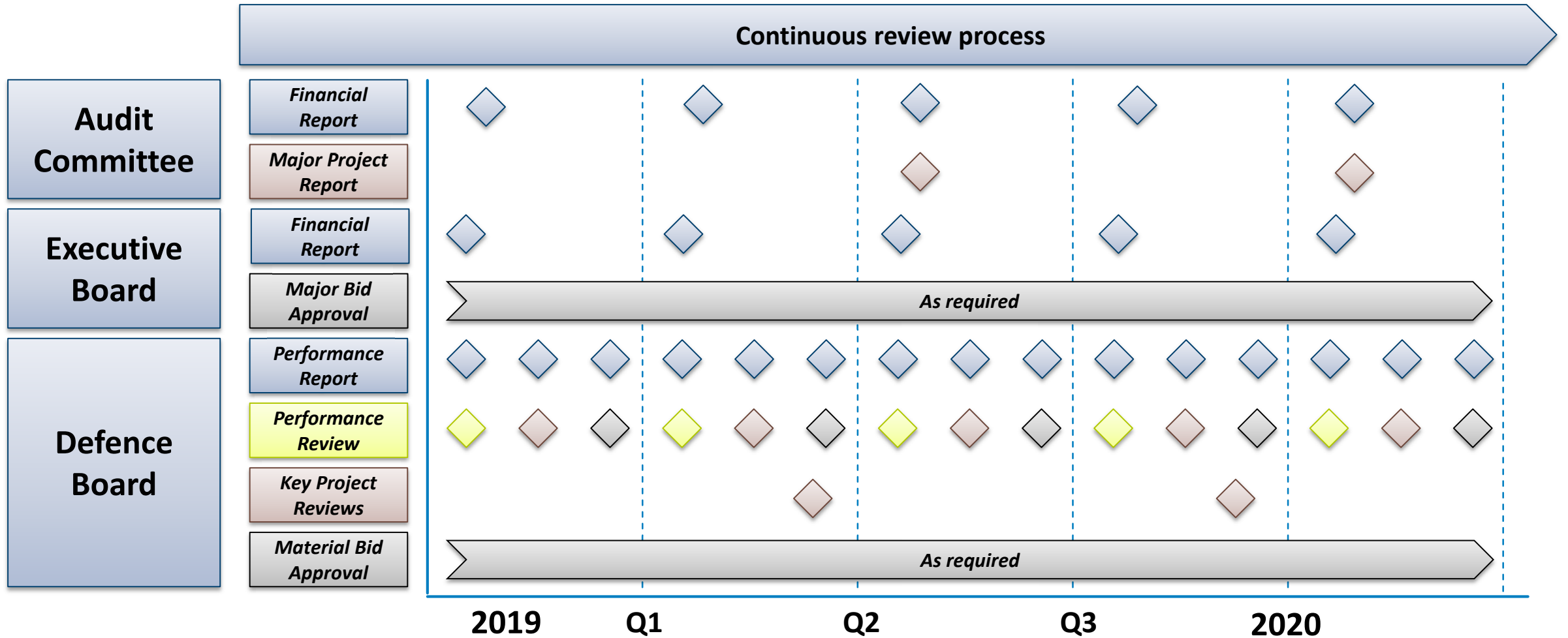


03 Financial controls on projects

MOBILITY. SECURITY. **PASSION.**

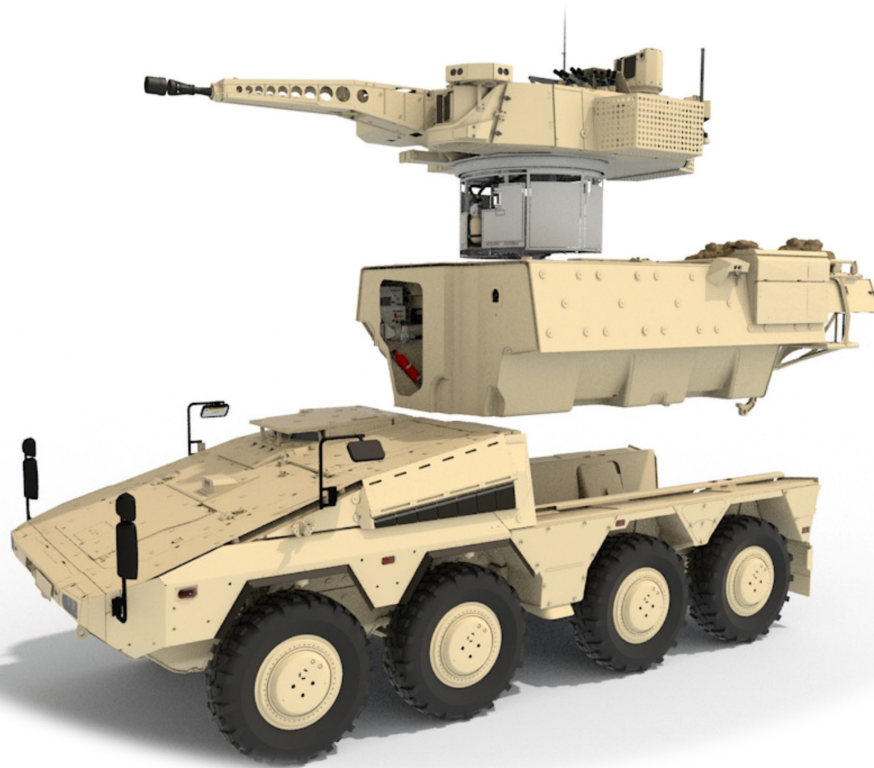
02 Audit and financial control overview

Project reviews at group level



03 Financial controls on projects

Audit focus of external auditors - illustrative



Determination of percentage of completion

Identification and valuation of offset obligations

Commissions and other contract acquisition costs

Onerous contracts

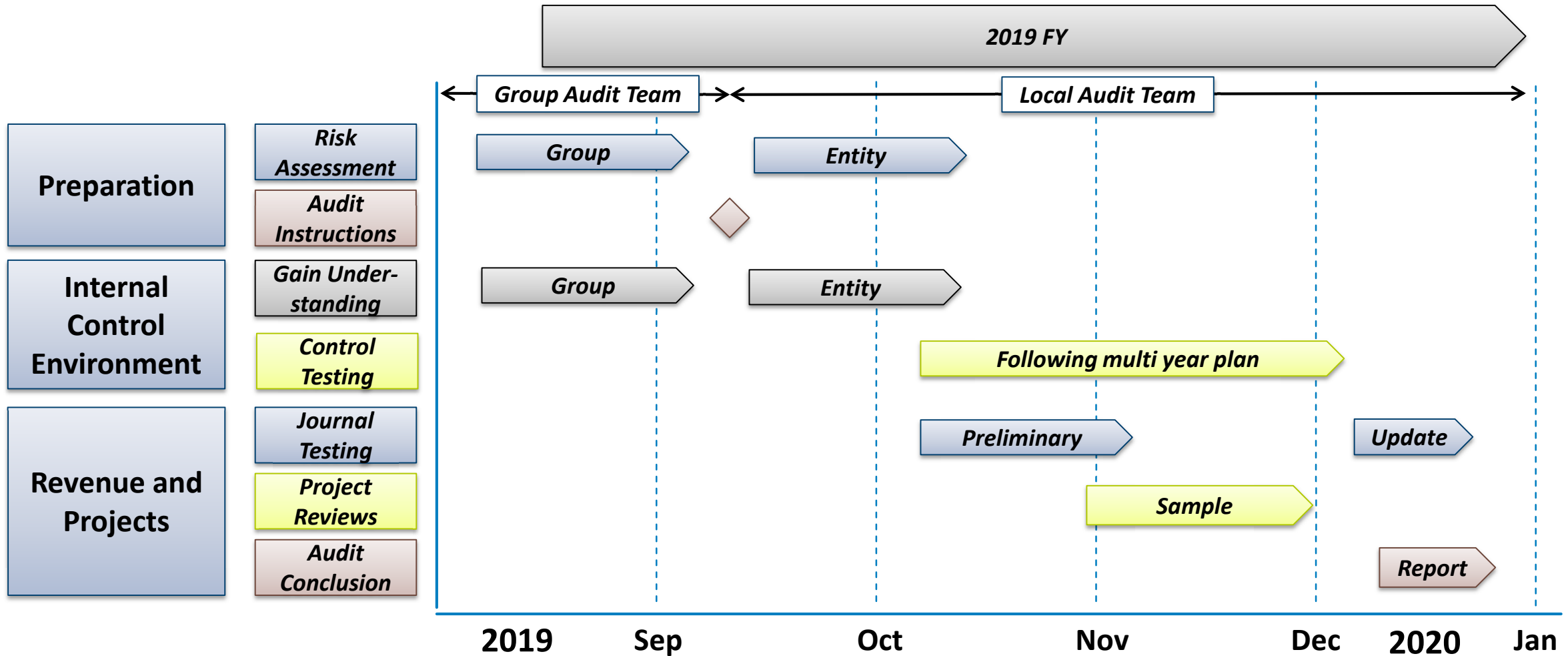
Penalties and variable consideration

Warranties

Project financing incl. interest and FX

03 Financial controls on projects

Audit approach by external auditors





04 Practical challenges for defence companies

MOBILITY. SECURITY. [PASSION.](#)

04 Practical challenges for defence companies

Case Study: Australia – Land 400 Phase 2 – Overview

What is LAND 400?

The Commonwealth of Australia is Rheinmetall's customer for LAND 400, a program that will deliver the next generation of armoured fighting vehicles for the Australian Army.

It is the biggest and most expensive acquisition project in both the Army's and Rheinmetall's history, as well as the first truly ONE Rheinmetall program – bringing together all elements of the Rheinmetall Group to make the most of our collective competencies and improve collaboration.

Phase 2 of LAND 400 is the Combat Reconnaissance Vehicle or CRV.



04 Practical challenges for defence companies

Case Study: Australia – Land 400 Phase 2 - Product

Lethality:

- MK30-2/ABM main canon (200 rounds)
- MAG58 7.62 coax machine gun (620 rounds)
- Air Burst Munition functionality

Fightability:

- Situational Awareness System (6x SCM 60)
- SEOSS P/S (obsolescence-cleaned)
- LWS (Laser Warning System)
- ROSY (Rapid Obscuring System)
- ASLS (Acoustic Shooter Locating System)

C4I:

- Radio fit (Harris & Raytheon)
- Battle Management System (Elbit & Thales)
- SOTAS intercom (Thales)

Sustainability:

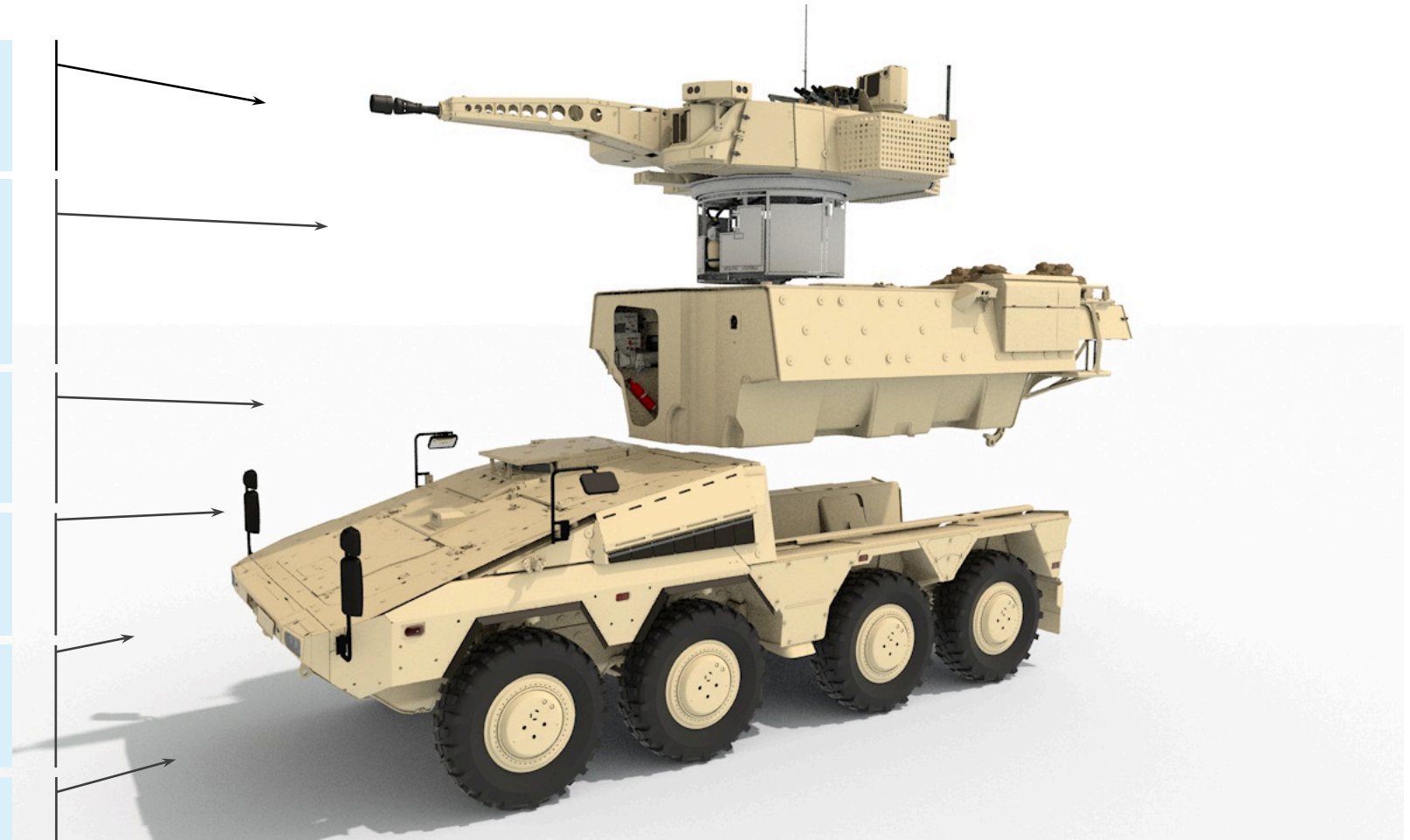
- Crew of 3 (Cdr, Gnr, Drv) and 4 dismounts
- Local Situation Awareness System (LSAS)
- RECON Mission Kit and CES

Survivability:

- BOXER JTS Ballistic Protection
- Applique Armour
- Mine deflector (KMW)

Mobility:

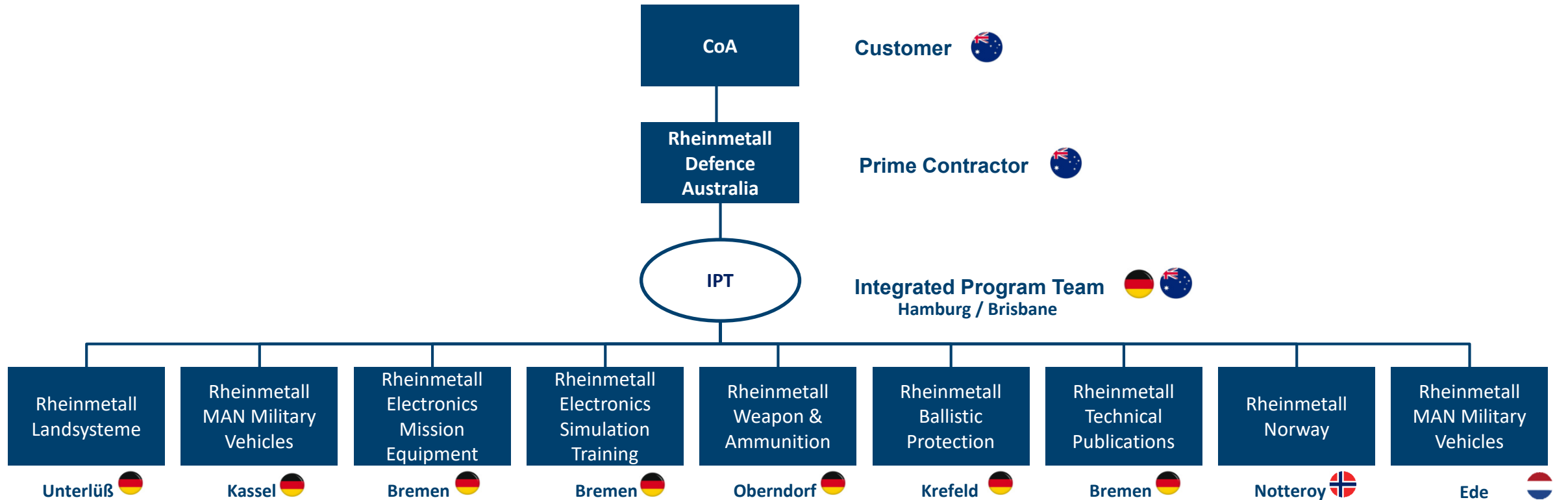
- 38.5 ton Drive Module (interim)



04 Practical challenges for defence companies

Case Study: Australia – Land 400 Phase 2 – Organisation

Project Management



04 Practical challenges for defence companies

Case Study: Australia – Land 400 Phase 2 – Challenges

For the complex contract and project setup ...

- Customer contract in five currencies
- Significant contribution of ten Rheinmetall entities in four countries with three currencies
- Ten different accounting systems
- Four different local GAAP
- Four different tax regimes
- Project specific costing concept that is different to existing costing systems
- Complex technical accounting topics (revenue recognition, hedge accounting, leasing, government grants, ...)

... ensuring transparency is challenging

- All information needs the context of the relevant reporting framework in order to be correctly understood.
- Group wide view of financial performance requires additional specific information to
 - eliminate intra-group profits on consolidation
 - determine the group wide percentage of completion

04 Practical challenges for defence companies

Limited standardization and project complexity lead to additional costs

Accounting and Tax

- Accounting
 - Harmonised standard for group reporting
 - Local GAAP different in all countries
- Tax
 - Regulations differ in all countries
 - Transfer pricing follow harmonised standards but regarding detailed negotiations especially for multi year contracts

Customer requirements

- Procurement and project management
 - Divergence in procurements practices
 - Divergence in project management requirements
- Product specifications
 - Different product specifications for basically identical products (e.g. for some ammunition)
 - Different product specifications for products that basically serve the same purpose (e.g. vehicles)
- Offset and local industrial content

04 Practical challenges for defence companies

Limited standardization: Focus on ammunition

Standards (e.g. NATO) exists for

- Ammunition types
- Ammunition colour coding

But ...

- countries have additional specific additional requirements for (colour) coding of ammunition
- countries have specific requirements for ammunition lots, e.g. size of lot, number of fuse lots in one ammunition lot.
- countries require audits of the production process during the production of their ammunition

As a consequence preproduction even of components is not possible. This leads to long lead time and additional costs.



MOBILITY. SECURITY. PASSION.