

AUDIT

Audit of potential aspects of fraud

RUAG MRO Holding AG

KEY FACTS

In August 2023, the irregularities in the purchase of 100 Leopard 1 tanks and the ongoing criminal proceedings in Germany concerning the trade in Leopard 2 spare parts caused the Board of Directors of RUAG MRO Holding AG (RUAG MRO) to mandate the law firm Niederer Kraft Frey (NKF) to undertake a broadly defined investigation.

The Finance Delegation (FinDel) subsequently requested the Swiss Federal Audit Office (SFAO) to provide an independent assessment of any potential aspects of fraud at RUAG MRO in the transactions surrounding the Leopard 1 and 2 battle tanks. The reason for this was that RUAG, as the concerned party, issued the investigation mandate and this resulted in risks of an appearance of bias.

The SFAO decided to use NKF's ongoing investigation to answer the FinDel's questions. The collaboration between the parties (SFAO, NKF and Board of Directors of RUAG MRO) was regulated in a tripartite agreement. It ensured that the SFAO was closely involved in the role of contracting authority. In this way, the SFAO can guarantee that NKF's investigation is independent. The Board of Directors of RUAG MRO ensured internal independence through the delegation of the Head of the ARC. Furthermore, the SFAO's report to the FinDel ensures transparency concerning the investigation findings and the chosen approach means that duplications and additional costs can be avoided.

NKF's investigation is multi-layered and ongoing. Important data sets and related interviews with individuals of interest to the investigation are pending. For instance, legal issues mean that data from the German subsidiary RUAG GmbH is missing. Likewise, it has not been possible to decrypt part of the emails from the Federal Office of Information Technology, Systems and Telecommunication (FOITT), as the mandated data processor, due to legal reasons. These are interim findings which could still change. Despite this background, there were sufficient indications of fraud at reporting date of 23 December 2024. At least one manager with a dual function at RUAG MRO and RUAG GmbH in Germany is concerned. There were significant organisational shortcomings and failures within the then RUAG Holding AG, RUAG MRO and RUAG GmbH in Germany. As a result of the interim investigation findings, the Board of Directors of RUAG MRO has taken initial measures. The SFAO did not take these measures into account when producing this report.

Depending on the valuation of the materials, the potential financial damage from the cases known to date could be in the double-digit millions, although this is the SFAO's own estimate. This concerns suspected losses due to sales of parts at well below market price, potential claims for compensation due to unfulfilled delivery obligations, economically implausible transactions to the detriment of RUAG, and VAT-related back payments and fines for business activities in Italy. Taking into account the internal and external costs of reviewing these cases, and the reputational damage, the overall financial damage is significantly higher, but cannot be quantified.

The SFAO's answers to the questions raised by the FinDel are as follows:

Question 1: Do any indications of conduct of a criminal nature exist in the various stages of the business transactions surrounding the Leopard 1 and 2 deals?

Substantial indications of suspected criminal conduct exist in multiple cases.

The cases concern spare parts that were valued unfavourably to the detriment of RUAG and sold at a lower price. It is suspected that some invoices were falsified and different material designations used.

The was facilitated by an accumulation of functions in Switzerland and Germany and a lack of end-to-end computer systems: the same ex-manager acquired, valued and largely completed the transactions.

There are indications that this ex-manager worked together with his wife and a German intermediary. In Germany, criminal proceedings on suspicion of aggravated corruption and bribery in business dealings are pending.

The suspicion of a nexus of a criminal nature in Switzerland within the framework of the ongoing investigation ranges from criminal mismanagement, fraud, forgery, violation of commercial and industrial secrets, passive bribery, industrial espionage through to suspicion of money laundering.

These findings require the matter to be referred to the prosecution authorities. In addition, relevant civil claims in Switzerland and abroad are to be reviewed and, where appropriate, asserted.

Question 2: Can any misconduct on the part of the bodies or employees of RUAG be identified?

There is suspicion of misconduct by at least one ex-manager and insufficient implementation of the requirements suggests that misconduct occurred.

In August 2019, a whistleblower reported improper transactions concerning spare parts for the Leopard 1 and 2 tanks to the Head of the DDPS and to the President of the Board of Directors of RUAG Holding AG – the predecessor to RUAG MRO Holding AG. The report was not sent directly to the Whistleblowing Reporting Office at the SFAO, nor did RUAG or the DDPS inform the SFAO of this case. It contained specific information on the type and location of the transactions, as well as those involved, such as a German scrap dealer. The main allegation is that spare parts and materials were sold at well below market price and thus for personal gain.

RUAG received the report by post on 3 September 2019. On the same day, the then CEO of RUAG Holding AG informed various managers of the report at internal level. The line manager of the accused ex-manager in the German proceedings forwarded the report to this ex-manager even though the report described which areas were concerned by the accusations and it was to be implicitly assumed that the manager himself was directly involved. He expressed his position on the accusations made by email and this assessment was largely accepted by the management. The very next day, it was sent as the official position to the entire Board of Directors of RUAG Holding AG. It was also sent to the GS-DDPS.

At the time, RUAG Holding AG did not investigate the report independently, and did not initiate the necessary steps to uncover the potential irregularities and avoid further damage.

It is not clear to the SFAO to what extent the GS-DDPS processed the report and position statement.

Furthermore, the interim findings from NKF's investigations have revealed numerous violations of the rules concerning requirements and processes. The compliance requirements were not adhered to with the necessary consistency and significance – this mainly relates to economically implausible transactions. Multiple transactions contain indications that spare parts and vehicles were entered incorrectly in the warehouse accounts, or not at all. This led to materials having unclear origins and movements.

Numerous contractual transactions lack the authorisations from the governing bodies. It is suspected that procurements were made without the original armaments manufacturers having the necessary permits. The duty to register for VAT for the warehouse in Italy was only met seven years later. It is also questionable whether the owner requirements (in particular compliance with export control regulations) and international regulations for armaments were respected.

The facts should be clarified and passed on to the prosecution authorities. Civil claims should be made against the individuals and companies responsible.

Potential derivative corporate liability is part of NKF's ongoing investigation. This investigation is clarifying the responsibility of the Board of Directors, RUAG management and the audit and review bodies. Any transgressions should be discussed with the owner and reported to the prosecution authorities.

Question 3: Are there are indications that a culture was established and promoted which supported compliance with guidelines and requirements?

Based on the potential fraudulent actions identified and other SFAO audits, it can be concluded that RUAG MRO was not able to ensure consistent compliance with the guidelines and requirements.

An examination of the transactions investigated by NKF reveals that the culture of compliance with regulations and requirements is a weak point. The SFAO already carried out an audit on conformity and compliance with regulations and requirements at RUAG Holding AG in 2016.¹ It came to the conclusion that the risks for RUAG and the Confederation from possible cases of corruption and violations of regulations were too high. The report also highlighted liability and reputational risks for foreign transactions in terms of export restrictions, potential conflicts of interest, critical accumulation of functions and considerable risks of corruption, among other things. Eight years later, the main compliance instruments and measures are in place at RUAG. However, as the specific events have shown, they were not effective, at least in the cases identified.

With the completion of this audit mandate, the SFAO has completed the FinDel's audit mandate. The SFAO will reassess the tripartite agreement with the Board of Directors of RUAG MRO and NKF. The Board of Directors of RUAG MRO is responsible for pursuing the investigation mandate until it is completed. It is also in charge of initiating all criminal and civil proceedings, and of introducing, managing and monitoring the measures that result from the investigation findings.

¹ Audit mandate 16532 "Audit of compliance management system", available on the SFAO website.