	NATO	NORTH ATLANTIC COUNCIL
	OTAN	CONSEIL DE L'ATLANTIQUE NORD

NATO UNCLASSIFIED
Releasable to Montenegro

21 November 2016

DOCUMENT
C-M(2016)0063-AS1 (INV)

**IBAN AUDIT ON THE 2015 FINANCIAL STATEMENTS OF THE NATO ALLIANCE
GROUND SURVEILLANCE MANAGEMENT ORGANISATION (NAGSMO)**

ACTION SHEET

On 18 November 2016, under the silence procedure, the Council noted the IBAN report on the 2015 financial statements of NAGSMO attached to C-M(2016)0063 (INV) and agreed the RPPB recommendation regarding public disclosure.

(Signed) Rose E. Gottemoeller
Deputy Secretary General

NOTE: This Action Sheet is part of, and shall be attached to C-M(2016)0063 (INV).

NATO UNCLASSIFIED



NATO UNCLASSIFIED
Releasable to Montenegro

14 November 2016

DOCUMENT
C-M(2016)0063 (INV)
Silence Procedure ends:
18 Nov 2016 16:00

**IBAN AUDIT ON THE 2015 FINANCIAL STATEMENTS OF THE NATO ALLIANCE
GROUND SURVEILLANCE MANAGEMENT ORGANISATION (NAGSMO)**

Note by the Deputy Secretary General

1. I attach the International Board of Auditors for NATO (IBAN) report on the audit of the 2015 financial statements of the NATO Alliance Ground Surveillance Management Organisation (NAGSMO).
2. The IBAN report on NAGSMO sets out an unqualified opinion on the financial statements and an unqualified opinion on compliance. The 2015 financial statements contain a clear statement, approved by the NAPMO Board of Directors, that they can be publicly disclosed.
3. The IBAN report has been reviewed by the Resource Policy and Planning Board (RPPB) (see Annexes) which has concluded that the unqualified audit opinion on the 2015 financial statements of NAGSMO reflects the hard work by the Agency's management and staff to implement the range of measures approved by Council in recent years to improve financial and accounting regulations, governance, transparency and accountability.
4. I do not believe that this matter requires discussion in the Council. Consequently, **unless I hear to the contrary by 16:00 hours on Friday 18 November 2016**, I shall assume that the Council has noted the IBAN report on the 2015 financial statements of NAGSMO and agreed the RPPB recommendation regarding public disclosure.

(Signed) Rose E. Gottemoeller

5 Annexes
1 Enclosure

Original: English

NATO UNCLASSIFIED

-1-



**IBAN AUDIT ON THE 2015 FINANCIAL STATEMENTS OF THE NATO ALLIANCE
GROUND SURVEILLANCE MANAGEMENT ORGANISATION (NAGSMO)**

Report by the Resource Policy and Planning Board

References:

- a) IBA-A(2016)86 – IBAN report
- b) C-M(2015)0025 – NATO Financial Regulations (NFRs)
- c) PO(2015)0052 – Wales Summit tasker on transparency and accountability

Introduction

1. This report contains the RPPB's observations and recommendations on the IBAN audit of the 2015 financial statements of NAGSMO (reference (a)).

Discussion

2. The Board is pleased to note that the IBAN have issued an unqualified opinion on the financial statements of NAGSMO and an unqualified opinion on compliance for the 2015 financial year.

3. The Board welcomes the progress that the IBAN have observed towards compliance with the articles in the NFRS (reference b)) on internal control, risk management and internal audit. The Board welcomes the commitment by NAGSMO to further improve the processes established. The Board invites the Head of Financial Reporting Policy to encourage the sharing of best practice across NATO entities in this area and invites NAGSMO to contribute in this regard.

4. The Board notes the IBAN observation on high cash holdings by the Agency and the action being considered by NAGSMO (at page 3-9 of reference (a)) to address this recurring issue.

5. The Board welcomes the clear declaration contained in the 2015 financial statements that they can be publicly disclosed. The Board takes this opportunity to remind NAGSMO of the decision by Council that, with effect from 1 January 2016, the unclassified annual reports prepared by customer-funded and/or multi-nationally funded NATO Agencies could be made publicly available (reference (c)).

Conclusions

6. The Board is pleased with the unqualified audit opinion on the 2015 financial statements of NAGSMO which reflects the hard work by the Agency's management and staff to implement the range of measures recommended by the Board and approved by Council in recent years to improve financial and accounting regulations, governance, transparency and accountability. The Board notes that further work needs to be done to fully implement these measures.

Recommendation

7. The RPPB recommends that Council:
- a) note the IBAN report on the 2015 financial statements of NAGSMO together with this report by the Board;
 - b) note the Board's conclusions at paragraph 6;
 - c) agree to the public disclosure of this report, the IBAN audit (reference (a)) and the associated 2015 financial statements of NAGSMO, in line with the policy set out at reference (c).

**Summary Note for Council
by the International Board of Auditors for NATO (Board)
on the audit of the Financial Statements
of the NATO Alliance Ground Surveillance Management Organisation
(NAGSMO)
for the year ended 31 December 2015**

The Board audited the Financial Statements for the year ended 31 December 2015. The NATO Alliance Ground Surveillance Management Organization (NAGSMO) was created within NATO for the acquisition of the Alliance Ground Surveillance (AGS) Core System. NAGSMO is responsible for the overall management of the AGS program. It comprises a Board of Directors (BoD) and Working Groups with representatives from the participating Nations. It also comprises a NATO Management Agency led by a General Manager.

The budgetary expenditure for the administrative budget in 2015 was EUR 9.4 million. The budgetary expenditure for the operational budget in 2015 was EUR 131.9 million and USD 210.2 million.

The Board issued an unqualified opinion on the Financial Statements and on compliance for the year ended 31 December 2015.

During the audit, the Board made two observations and provided recommendations. These findings are in the Letter of Observations and Recommendations (Annex 4).

The main findings are listed below:

1. Further steps are required towards full compliance with the revised NATO Financial Regulations on Internal Control, particularly those Articles on Internal Control and Internal Audit.
2. High level of cash holdings being held by the NAGSMO.

For the NAGSMO's Formal Comments, see Annex 5.

NATO UNCLASSIFIED
Releasable to Montenegro

ANNEX 2
C-M(2016)0063 (INV)

BLANK PAGE

INTERNATIONAL BOARD OF AUDITORS FOR NATO

AUDITOR'S REPORT ON THE FINANCIAL STATEMENTS OF THE

**NATO ALLIANCE GROUND SURVEILLANCE
MANAGEMENT ORGANISATION**

(NAGSMO)

FOR THE YEAR ENDED 31 DECEMBER 2015

**REPORT OF THE INTERNATIONAL BOARD OF AUDITORS
FOR NATO TO THE NORTH ATLANTIC COUNCIL**

Report on the Financial Statements

The International Board of Auditors for NATO (Board) audited the accompanying financial statements of the NATO Alliance Ground Surveillance Management Organisation (NAGSMO), which comprised the Statement of Financial Position as at 31 December 2015, and the Statement of Financial Performance, Statement of Changes in Net Assets/Equity and Cash Flow Statement for the year then ended, and a summary of significant accounting policies and other explanatory notes. The Board also audited the Budget Execution Statements for the year ended 31 December 2015.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with the NATO Accounting Framework and the requirements of the NATO Financial Regulations as authorized by the North Atlantic Council (NAC). This responsibility includes the design, implementation and maintenance of internal control relevant to the preparation and presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit, which is conducted in accordance with our Charter and international standards on auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, due to fraud or error. In making those risk assessments, internal control relevant to the entity's preparation and presentation of financial statements is considered in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of internal control. An audit also includes evaluating the appropriateness of accounting policies used, the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Opinion on Financial Statements

In our opinion, the financial statements present fairly, in all material respects, the financial position of NAGSMO as of 31 December 2015, and of its financial performance and its cash flows for the year then ended in accordance with the NATO Accounting Framework.

Report on Compliance

Management's Responsibility for Compliance

In addition to the responsibility for the preparation and presentation of the financial statements described above, management is also responsible for ensuring that the financial transactions and information reflected in the financial statements are in compliance with the NATO Financial Regulations and the NATO Civilian Personnel Regulations as authorised by the North Atlantic Council (NAC).

Auditor's Responsibility

In addition to the responsibility to express an opinion on the financial statements described above, our responsibility includes expressing an opinion on whether the financial transactions and information reflected in the financial statements are, in all material respects, in compliance with the NATO Financial Regulations and the NATO Civilian Personnel Regulations. This responsibility includes performing procedures to obtain reasonable assurance about whether the funds have been used for the settlement of authorised expenditure and whether their operations have been carried out in compliance with the financial and personnel regulations in force. Such procedures include the assessment of the risks of material non-compliance.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Opinion on Compliance

In our opinion, in all material respects the financial transactions and information reflected in the financial statements are in compliance with the NATO Financial Regulations and the NATO Civilian Personnel Regulations.

Brussels, 23 August 2016

Lyn Sachs
Chairman

INTERNATIONAL BOARD OF AUDITORS FOR NATO

LETTER OF OBSERVATIONS AND RECOMMENDATIONS

**FOR THE NATO ALLIANCE GROUND SURVEILLANCE
MANAGEMENT ORGANISATION**

(NAGSMO)

FOR THE YEAR ENDED 31 DECEMBER 2015

Introduction

The International Board of Auditors for NATO (Board) audited the NATO Alliance Ground Surveillance Management Organisation (NAGSMO) Financial Statements for the year ended 31 December 2015, and issued an unqualified opinion on those financial statements and an unqualified opinion on compliance.

Observations and Recommendations

During the audit, the Board identified the following observations:

1. Further steps are required to achieve full compliance with the revised NATO Financial Regulations, particularly those Articles on Internal Control and Internal Audit.
2. High level of cash holdings being held by the NAGSMO.

The Board also followed up on the status of the observation from the previous year's audit and noted that it was superseded by the new observation 2 in this report.

For the NAGSMO's Formal Comments, see Annex 5. The detailed formal comments provide further information to the reader, but do not change the Board's observations or recommendations.

OBSERVATIONS AND RECOMMENDATIONS

1. FURTHER STEPS ARE REQUIRED TO ACHIEVE FULL COMPLIANCE WITH THE REVISED NATO FINANCIAL REGULATIONS, PARTICULARLY THOSE ARTICLE ON INTERNAL CONTROLS AND INTERNAL AUDIT

Reasoning

1.1 The North Atlantic Council (Council) approved revised NATO Financial Regulations (NFRs) effective as from 4 May 2015. This was the first time in more than 30 years that the NFRs have been revised. While Article 36 of the revised NFRs states that *“the NFRs will take effect immediately (i.e. 4 May 2015)”*, Council also agreed that full implementation was only expected by the end of 2015. Furthermore, Article 4 of the revised NFRs states that *“the finance committee shall approve a set of Financial Rules and Procedures (FRPs) that provide additional guidance to ensure the effective implementation of the revised NFRs.”*

1.2 The revised NFRs are more explicit than the previous version in the areas of Risk Management (Article 11), Internal Control (Article 12), Internal Audit (Article 13) and the establishment of an Audit Advisory Panel (Article 16). They require the establishment of effective, efficient and economical risk management procedures, that there are necessary management functions in place to support effective internal control, and that NATO bodies have access to a permanent, adequately resourced, internal audit function that is compliant with internationally accepted Internal Auditing Standards. They also require the establishment of an Audit Advisory Panel. Furthermore, Article 3 requires, as a demonstration of responsibility and accountability, that both the annual Financial Statements and Statements of Internal Control be signed by both the NATO Head of Body and Financial Controller

1.3 These revised NFRs provide an opportunity for NATO bodies to solidify and codify their overall internal control framework, including risk management. They also provide internal audit functions, whether in-house or outsourced, with clear expectations that they must be in a position to fully evaluate the effectiveness and efficiency of operations and internal controls, including risk management. Finally, the Council will ensure that the detailed FRPs are consistent, to the maximum extent possible, across NATO.

Observations

1.4 The Board found that NAGSMA is well advanced in risk assessment, but that some more steps are still needed to achieve full compliance in terms of internal control and internal audit.

1.5 This result, though, is not unexpected considering that the revised NFRs were only approved by Council in May 2015 and that the more detailed FRPs, which were required by Article 4 of the revised NFRs, were not approved by the NAGSMO Board of Directors until December 2015. In 2014, the Board recommended to the Nations that it would be better to have the revised NFRs become effective as from the beginning of the year following approval, and that the revised NFRs and the more detailed FRPs should become effective as from the same date. However, the Nations did not agree with these recommendations.

1.6 Due to the lack of detailed regulations, based on the revised NFRs, throughout most of 2015, the Board considers 2015 to be a transition year. It has chosen to report on the progress against certain of these revised Articles of the NFRs, and to make recommendations against that progress. The compliance audit opinion will not be impacted in 2015 as a result of these observations. This will begin as from 2016, though.

1.7 The Board reports the status of the following areas:

Article 3 Responsibility and Accountability

1.7.1 The Board found that both the Financial Statements and the Statement of Internal Control were signed by both the NAGSMA Head of Body and Financial Controller.

Article 11 Risk Management

1.7.2 The Board found that the NAGSMO adopted a risk management framework that is based on the International Organization for Standardization (ISO) 31000:2009 and that its application within NAGSMO is mature. It includes a risk management policy, plan, process and resources. NAGSMO has established clear governance over the program risks and program risk management defining accountabilities and responsibilities, the escalation process and the decision process. NAGSMA is using a risk management database which is providing different types of reports, including a risk register that is updated on a regular basis.

1.7.3 NAGSMA has risk management at strategic and operational levels in place. The risk management process is covering the AGS Program and NAGSMA as an organization. The risk management process includes the escalation of program risks identified by the branches to a program level Risk Board. The risk mitigation action plans have been developed and monitored and are recorded within the database. In the risk management process, the risks are assessed and prioritized and the top financial risks are escalated to the Program/NAGSMA level.

Article 12 Internal Control

1.7.4 The Board's audit of the 2015 NAGSMO Financial Statements did not reveal significant weaknesses in internal control. However, the Board found that some improvements can be made in documenting its detailed internal control system. Also, no common NATO-wide Internal Control Framework has been chosen. Such a framework, with the appropriate supporting documentation and procedures, is essential in order to ensure and to clearly demonstrate to others that a complete system of internal controls is in place.

1.7.5 Until a systematic documentation of internal control procedures is in place, the Board will not be in a position to state that there is a full system of internal control in place that is in accordance with Article 12 of the revised NFRs.

Article 13 Internal Audit

1.7.6 As allowed under Article 13, NAGSMA engaged NCIA Internal Audit to undertake audits regarding various NAGSMA departmental activity groups. The NCIA Internal Audit submitted two reports during 2015, on NAGSMA Personnel Security, and the NAGSMA succession planning. Also, an Internal Audit Plan for 2015-2017 was developed taking into consideration the risks identified during a NAGSMA Financial Controller/Resources Management Division control self-assessment survey and risk assessment workshop.

1.7.7 These activities are a good start. However, it cannot yet be stated that NAGSMA has undertaken internal audit activities to fully evaluate, throughout the organisation, the risk exposures and the effectiveness of internal controls in managing risk within the governance, operations and information systems as required by Article 13.

Article 16 Audit Advisory Panel

1.7.8 The Board found that NAGSMA established on 5 June 2016 an Audit Advisory Panel as required by Article 16.

Recommendations

1.8 The Board recommends that:

- a) there be a systematic and detailed documentation of internal control procedures. In the Board's opinion, a specific, internationally accepted Internal Control Framework should be adopted and this should be coordinated with the Head of Financial Reporting Policy to ensure that a common framework is chosen across NATO Bodies.
- b) NAGSMA ensures internal audit activities are sufficiently focused on evaluating internal controls throughout NAGSMA.

2. CURRENCY HOLDINGS NOT RESTRICTED TO THE MINIMUM REQUIRED TO MEET FORECAST PAYMENTS AS REQUIRED BY THE NATO FINANCIAL REGULATIONS

Reasoning

2.1 Article 29.3 of the NFRs states that: *“each contribution instalment shall be calculated to restrict total currency holdings to the minimum required to meet forecast payments prior to receipt of the following contribution instalment”*. Furthermore, the NAGSMO Financial Rules and Procedures state that each call for contribution shall be calculated, as at the time of its issue, to yield the amount which, in addition to treasury holdings and amounts still receivable on previous calls, will be sufficient to cover the payments anticipated during the period covered by the call.

Observation

2.2 The Board found that NAGSMO held levels of cash that exceeded its cash requirements during 2015. The level of average cash holdings in 2015 was EUR 349 million based on a monthly calculation, which is about 105% of the 2015 expenses (EUR 331 million).

Recommendation

2.3 In the absence of a Council approved deviation, the Board recommends that NAGSMO complies with Article 29.3 of the NFRs.

FOLLOW-UP OF PREVIOUS YEAR'S OBSERVATION

The Board reviewed the status of the observation and recommendation arising from the previous audit. The observation and its status is summarised in the table below.

Status of previous year's observation

OBSERVATION / RECOMMENDATION	ACTION TAKEN	STATUS
<p>Audit Report FY 2014 IBA-AR(2015)33, paragraph 1 Excessive level of cash holdings as per NFRs</p> <p>Observation Article 13.3 of the NATO Financial Regulations (NFRs) states that "<i>each contribution instalment shall be calculated to restrict total currency holdings to the minimum required to meet forecast expenditures prior to receipt of the following contribution instalment.</i>" Furthermore, the NAGSMO Financial Rules and Procedures state that each call for contribution shall be calculated, as at the time of its issue, to yield the amount which, in addition to treasury holdings and amounts still receivable on previous calls, will be sufficient to cover the payments anticipated during the period covered by the call.</p> <p>The Board found that NAGSMO held levels of cash that exceeded its cash requirements during 2014. The level of average cash holdings in 2014 was EUR 335 million based on a monthly calculation, which is about 90% of the 2014 expenses (EUR 375 million).</p> <p>Board's recommendation The Board recommends that NAGSMO complies with Article 13.3 of the NFRs.</p>	<p>See current year observation 2 above.</p>	<p>Observation Superseded by current year observation 2.</p>

**NATO ALLIANCE GROUND SURVEILLANCE MANAGEMENT AGENCY (NAGSMA)
FORMAL COMMENTS ON THE
LETTER OF OBSERVATIONS AND RECOMMENDATIONS AND THE
INTERNATIONAL BOARD OF AUDITORS FOR NATO (BOARD) POSITIONS**

**OBSERVATION 1:
FURTHER STEPS ARE REQUIRED TO ACHIEVE FULL COMPLIANCE WITH THE
REVISED NATO FINANCIAL REGULATIONS, PARTICULARLY THOSE ARTICLE ON
INTERNAL CONTROLS AND INTERNAL AUDIT**

NAGSMO's Formal Comments

NAGSMA informs the Nations that the full implementation of the revised NATO Financial Regulations was only expected by the end of 2015, which has been acknowledged by the North Atlantic Council. In light of that, International Board of Auditors for NATO, has chosen to report on the progress against certain of these revised Articles of the NFRs, and to make recommendations against that progress. The compliance audit opinion will not be impacted in 2015 as a result of that observation.

International Board of Auditors for NATO concluded that, while 2015 NAGSMO Financial Statements did not reveal significant weaknesses in internal controls, some improvement can be made in documenting the internal control system in place.

NAGSMA will take appropriate steps to collate supporting documentation of internal control procedures in place to address the matter.

International Board of Auditors for NATO also observed that NAGSMA engaged NCIA Internal Audit to undertake audits regarding various NAGSMA departmental activity groups. However, at this moment it could not be stated that these activities fully evaluate, throughout the organisation, the risk exposures and the effectiveness of internal controls in managing risk within the governance, operations and information systems as required by Article 13.

NAGSMA informs the Nations that further engagement with NCIA Internal Audit services is foreseen as developed within the Internal Audit Plan for 2015-2017. In light of the observation the intent will be to sufficiently focus those internal audit activities on evaluating internal controls throughout NAGSMA.

**OBSERVATION 2:
CURRENCY HOLDINGS NOT RESTRICTED TO THE MINIMUM REQUIRED TO MEET
FORECAST PAYMENTS AS REQUIRED BY THE NATO FINANCIAL REGULATIONS**

NAGSMO's Formal Comments

The second observation was raised by the IBAN on the NAGSMO 2015 Financial Statements concerning excessive level of cash holdings as per NATO Financial Regulations.

This is a recurring observation that has been raised by IBAN in the year 2014, as well.

NAGSMA will again propose to NAGSMO Finance Committee a modification to NAGSMO FMPD-FRP, which would allow NAGSMA to hold operational funds to cover payments in sequential budgets of the Agency, and seek the required approvals for that deviation from the NFRs.

NAGSMO

2015

FINANCIAL STATEMENTS



PAGE LEFT INTENTIONALLY BLANK

These Financial Statements represent the consolidated activities of the NATO Alliance Ground Surveillance Management Organisation (NAGSMO) and its executive body NATO Alliance Ground Surveillance Management Agency (NAGSMA).

THE NATO ALLIANCE GROUND SURVEILLANCE PROGRAMME

NAGSMO is acquiring as an agent a NATO owned and operated Alliance Ground Surveillance (AGS) system that will give commanders an up-to-date picture of the situation on the ground throughout a wide area of interest. The AGS Core will be compliant with NATO Standardization Agreements (STANAGs) in order to ensure interoperability with interoperable national and NATO systems.

The AGS Core capability will enable the Alliance to perform persistent surveillance over wide areas from high-altitude, long-endurance, unmanned air platforms operating at considerable stand-off distances and in any weather or light condition. Using advanced radar sensors, the AGS Core will continuously detect and track moving objects throughout the observed areas, as well as providing radar imagery of areas and stationary objects.

The NAGSMO and its executive body NAGSMA are responsible for the procurement of the NATO AGS Core capability. The NAGSMA was established in September 2009, after all Participating Nations signed the AGS Programme Memorandum of Understanding.

In late 2011, NAGSMA completed negotiations of the AGS Core procurement contract which was subsequently approved by the Participating Nations. The AGS Programme contract award was signed on 20 May 2012 in the margins of the NATO Summit in Chicago. In parallel, all 28 NATO nations negotiated the AGS Programme's practical funding solution for the related Capability Package for the future operations and support of the system.

THE AGS CORE

The AGS Core will be an integrated system consisting of an air segment, a ground segment and a support segment.

The air segment will be based on the Block 40 version of the US RQ-4B Global Hawk high-altitude, long-endurance unmanned aerial vehicle (UAV). The UAV will be equipped with the state-of-the-art Multi-Platform Radar Technology Insertion Program (MP-RTIP) ground surveillance sensor, and also with an extensive suite of communications and data links. The air segment will also include the ground-based UAV control stations, which will be located at the AGS Main Operating Base (MOB) at Sigonella Air Base, Italy.

The ground segment will consist of deployable ground stations in mobile and transportable and maritime configurations, and dedicated mission operations support facilities at the MOB. The ground segment entities will provide data link connectivity, data processing and exploitation capabilities, and interoperable interfaces between the AGS Core System and a

wide range of NATO and national Command, Control, Intelligence, Surveillance and Reconnaissance systems. This will enable the AGS Core to interconnect with and provide data to multiple deployed and non-deployed operational users in a flexible, timely and effective manner.

The AGS support segment provides items needed to train the air and ground segment operators and maintainers, to maintain the AGS System at its main operating base, and to enable maintenance and repair during deployed operations.

The AGS Core System will be supplemented by interoperable national airborne ground surveillance systems from NATO countries, as part of NATO's broader Joint Intelligence, Surveillance and Reconnaissance capability.

NATO ALLIANCE GROUND SURVEILLANCE MANAGEMENT ORGANISATION

The NATO Alliance Ground Surveillance Management Organisation (NAGSMO) is a NATO body

- created within the framework of NATO for the acquisition of the AGS Core System and established by the North Atlantic Council pursuant to Article IX of the North Atlantic Treaty and within the meaning of the Agreement on the Status of the North Atlantic Treaty Organisation, National Representatives and International Staff, signed in Ottawa 20 September 1951;
- to which the North Atlantic Council grants, within the framework of the NATO, a clearly defined organisational, administrative and financial status as specified below; and
- established with a view to meeting the NATO requirement, by Bulgaria, Czech Republic, Denmark, Estonia, Germany, Italy, Latvia, Lithuania, Luxembourg, Norway, Poland, Romania, Slovakia, Slovenia, and the United States of America in the field of implementation of the NATO AGS Programme described in the AGS Programme Memorandum of Understanding (PMOU).

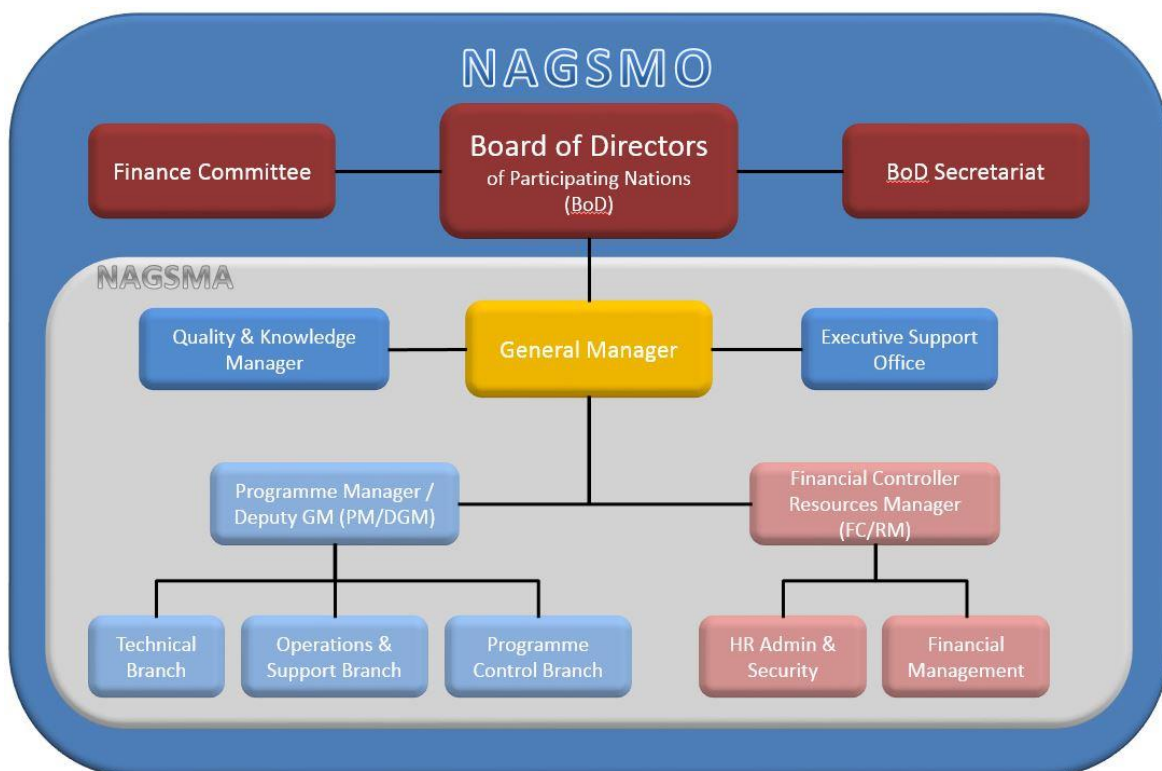
In June 2010, Denmark announced her intent to withdraw from the AGS Programme, a process that under the terms of the PMOU came into effect on 31 March 2011. Subsequently, in July 2011, Canada also announced her intent to withdraw, effective as of 30 April 2012. Later in 2012 Denmark announced her interest and intent to re-join the AGS Programme. Denmark re-joined the AGS Programme in December 2012. Poland announced to the NAGSMO Board of Directors their interest in joining the AGS Programme in August 2012. An amendment to the PMOU was sent to Participating Nations for signature in August 2013. Poland signed the Amendment 1 to the AGS PMOU in April 2014. With the signature of all of the Participating Nations, the Amendment 1 to the AGS PMOU has come into effect on the 19th of June 2014.

The principal task of the NAGSMO is to ensure the planning and implementation of a harmonised AGS Programme, which satisfies the operational requirements, in accordance with the provisions of the PMOU, and with due regard to the NAGSMO Member States' views on political, economic, industrial and technological factors. NAGSMO shall assume the functions of overall management of the AGS Programme, including:

- overall governance of the AGS Programme;
- general administration of the NAGSMA and procurement of the AGS Core System;
- examination of all issues that might impact the AGS Programme;
- coordination, as necessary, of the policy and working methods of the NAGSMO Member States' services, such as quality assurance and auditing; and
- support integration of the AGS Core System with the NATO Joint Intelligence, Surveillance and Reconnaissance architecture.

NAGSMO comprises a Board of Directors (BoD) with Representatives from the Participating Nations, and NAGSMA as the Executive Body, led by a General Manager (GM).

The diagram below depicts the NAGSMO and NAGSMA organizational structure in 2015.



NAGSMA and Service Support/Level Agreement

The NAGSMO BoD, represented by the NAGSMA GM, signed five formal agreements (an MOA, an SLA and three SSA's) with the NATO IS, NSPA and NCI Agency, for support services in a number of areas necessary for the day to day operations of the Agency. In all respects of NAGSMA related activities, the GM and his staff remain fully accountable for the responsibilities assigned to them and make the final decisions on all matters related to the execution of NAGSMA's mandate. The SSA with NCI Agency includes support services in the area of accounting and financial support in accordance with the NATO Financial Regulations (NFRs).

NAGSMO Financial Management Procedures Document and Financial Rules and Procedures (FMPD-FRP)

The NAGSMO BoD approved the revised NAGSMO FMPD-FRP in December 2015 to comply with updated NATO Financial Regulations. The amended NAGSMO FMPD-FRP recognises the withdrawal of Canada and the re-entry of Denmark, the conversion parameters from Then-Year to Base-Year, the call for contribution structure and the proposed structure of the Operational Budget. The NAGSMO FMPD-FRP conforms to the provision of the NATO Financial Regulations.

NAGSMA 2015 Administrative Budget

The NAGSMA 2015 Administrative Budget was approved by NAGSMO BoD in November 2014. The budget was approved to fund NAGSMA's expenditures from 1 January to 31 December 2015. In 2015 NAGSMA continued to reduce costs related to business operations, overhead activities and support functions. It successfully negotiated two Service Support Agreements (SSAs) with NATO Support Agency (NSPA), a Service Level Agreement (SLA) and SSA with the NATO Communications and Information Agency (NCIA) for external administrative support. Personnel related expenditures in the NAGSMA 2015 Administrative Budget were considerably lower than what had been anticipated, due to several staff members departing the Agency, lengthy recruitment campaigns and savings generated by changes in regulations for installation allowance. Notwithstanding the efforts of the Agency, it has been challenging to recruit new staff members. The main deterrents are the time required for security clearances to be granted and the concerns regarding the definite duration of the Agency. Expenditures in Operations and Maintenance were lower than what had been foreseen due to less support needed from NSPA in the areas of Configuration Status Accounting (CSA) and Information Logistics Support (ILS). Non-availability of data has resulted in less CSA support tasks and the ILS support tasks were delayed due to change of schedule of the AGS contract execution activities in logistics matters. Some savings were also obtained in travel related expenditures in Chapter II.

NAGSMA 2015 Operational Budget

The NAGSMA 2015 Operational Budget was approved by the NAGSMO BoD in November 2014. The budget was approved to fund prime contract related AGS Core acquisition expenditures in 2015. The NAGSMA USD Operational Budget was increased at no cost to Nations to cover Canadian Industrial Participation, approved in August 2014 (Amendment 0008).

The NAGSMO BoD approved in April 2012 the request by Estonia to apply Pre-PMOU Contributions (PPC) towards the 2013-2016 Financial Year (FY) Operational Budget. In April 2014 the NAGSMO BoD approved for the Czech Republic to apply their PPC credits to the Czech contribution to the 2015 NAGSMA Operational Budget. In November 2015 the NAGSMO BoD approved the requests of Germany and Italy to apply their PPC to 2016-2017 FY Operational Budget.

The NAGSMO BoD authorized the USA Non-Financial Contributions (NFC) to be expensed from the Operational Budget from 2013 to 2017 upon confirmation of support costs incurred at Edwards Air Force base (EAFB). At the BoD meeting in March 2013 the NFC proposal from Italy was accepted and Italy was granted authorization to expense the Non-Financial Contributions for the airworthiness certification (AWC) efforts. These costs have been expensed in 2015 based on the presentation of invoices from nations of the actual costs incurred in support of the programmatic needs.

Major Achievements FY 2015:

During the FY 2015, the AGS Programme achieved the following important milestones:

- AGS System Critical Design Review (CDR) was completed and full payment of milestones No 49 & 50 was approved in November 2015. In October 2015, NAGSMA received NGISSII's commitment letter for the implementation of all trading basket agreements and document updates on the remaining deliveries for configuration management, requirements traceability tables, General Dynamics Canada (GDC) Remote Work Stations, Failure Modes Effects and Criticality Analysis (FMECA) & Product Support and Support Segment CDR Actions.
- Mobile General Ground Station (MGGS) Formal Test & Verification activities (two MGGS Analysis Test & Verifications, two MGGS ISTAR and Hardware Environmental Tests) started in late 2015, proceeded by familiarization entity training and approval of test plans.
- During 2015 the parts and component manufacturing for all five aircrafts were completed (except for wings 4 and 5) and all aircraft are now in final assembly or test at Palmdale. Both Deployable UAV Command and Control Elements (DUCE) are functionally complete (one at Palmdale, one at EAFB). The Air Vehicle Mission Command and Control 2 (AVMC2) is currently being tested at Rancho Bernardo

before being delivered to Sigonella for Main Operating Base (MOB) integration. About 50% of the MGGs subsystem Hardware items (MGEC, MGCC) have been completed at the sub-sub-suppliers (RETIA, Konstrukta) and have been accepted by Airbus DS. The retained development unit of the Mission Operations Support (MOS) was assembled during 2015. For the Transportable General Ground Station (TGGs) the development items/components were assembled/procured for verification testing.

- NATO AGS First Flight occurred on 19 December 2015.
- Several training activities together with the AGS-SEIO took place in 2015 among which are the First Flight Familiarization Training, MOS Familiarization Training, MGGs Familiarization Training & several NATO Test Team Trainings involving primarily the user.
- Several meetings and a Technical Working Groups were held in coordination with AGS Contractor and Programme Stakeholders such as: Integration Technical Interchange Meetings (TIM), User System Interface Working Groups (USIWGs), Operational User Groups (OUGs), System Safety WGs (SSWGs), AGS Interoperability Meetings, Verification Planning Working Groups (VPWGs), AWWG (Air Worthiness Working Groups) Communication & Information System, and Training TIMs, Q4 User Group Meetings, ICT Meetings (monthly), Training Integrated Product Team (IPT) Meetings, CIS IPT Meetings, Logistic IPT Meetings, Infrastructure IPTs (IB-IPTs).
- Five Programme Management Reviews (PMRs) were conducted with the Contractor (four regular and one extraordinary).
- The AGS Logistics Information System (ALIS) Request for Proposals (RFP) in collaboration with NSPA and AGS-SEIO was completed in October 2015 and the Invitation For Bid (IFB) was released in December 2015. In parallel, a mitigation action (Collaborative Environment Contract Change Proposal (CCP) No 003) to compensate for the ALIS delay was launched in October 2015.
- The CCP for Initial – In Service Support (I-ISS) non-recurring (Long lead Items, Peculiar Support Equipment & Spare Parts) RFP was sent to NGISSII in October 2015.
- A direct contract with Danish Industry (ATR/ATID) was launched in October 2015 and Not to Exceed (NTE) Fixed Firm Proposal (FFP) including Authorization to Proceed (ATP) value was received in November 2015.
- Contract Change Order including the FFP NTE for L16 (Engineering Change Proposal No 007) was received in November 2015 and was provided to the NAGSMO BoD for approval under silence in December 2015 (approved by NAGSMO BoD in February 2016).
- Upon completion of the bridging facilities at Sigonella, the Hand-Over process to NATO Ground Surveillance Force (NAGSF) started in late 2015. All Major Programme Events Scheduled and subject to milestone payments are in line with the Milestone-Based Payment plan.

NAGSMA Assets

Office space, including furniture, IT and other equipment is provided by the NCI Agency via the SSA.

NAGSMO & NAGSMA Acting as a Procurement Agent

The North Atlantic Council (NAC) established NAGSMO by approving its Charter. The Charter clearly establishes that NAGSMO is a subsidiary body of NATO and states that the objective is to procure the AGS Core which will be owned, controlled and operated by NATO. NAGSMA is an entity acting as an agent with no control over the assets procured. The AGS Participating Nations reiterated the specific nature of the AGS Programme: temporary existence of the Agency and that the Agency will not own any asset. In order to comply with the NATO Accounting Framework, ACO will account for all NAGSMA procured assets in the future. NAGSMA will fully disclose and provide at the end of each reporting period to ACO all financial data regarding the assets procured. NAGSMA responded this year to ACO's request for information that no assets were procured for the financial year ending in December 2015.

CERTIFICATION

1. The NAGSMO 2015 Financial Statements are submitted to the International Board of Auditors for NATO.
2. The Financial Statements will be audited in accordance with the following reference documents:
 - a. The NAGSMO FMPD-FRP conform to the NFRs, Part II as approved by the North Atlantic Council (NAC) in C-M(2015)0025.
 - b. PO(2002)109, dated 23 July 2002: the document from the NAC adopting IPSAS, including the accrual and going concern assumptions, as the applicable accounting standards for all NATO entities effective for the financial year of 2006.
 - c. The NATO Accounting Framework has been developed to provide minimum requirements for financial reporting for all NATO Reporting Entities following approval of C-M(2013)0039 by the North Atlantic Council on 2 August 2013 of an IPSAS-adapted accounting framework for the Alliance.
3. The NAGSMO Financial Statements are certified by the NAGSMA General Manager and the NAGSMA Financial Controller to the best of their knowledge and according to the applicable accounting standards to give a true and fair view of the assets, liabilities, financial position and financial performance of NAGSMA and to be in accordance with the books and records maintained by the NCI Agency and NAGSMA.
4. The NAGSMO Financial Statements may be disclosed to the general public.



James E. EDGE
NAGSMA General Manager



Grazia M. D'Arcangelo
NAGSMA Financial Controller

STATEMENT ON INTERNAL CONTROL

This statement of internal control applies to the Financial Statements of NAGSMA, as the executive body of NAGSMO, for the year ended 31 December 2015.

Scope of responsibility

- The General Manager acknowledges responsibility to maintain a sound system of internal control that supports the achievement of NAGSMA's mandate under its NATO Charter.
- The Financial Controller acknowledges responsibility for the correct use of funds made available to NAGSMA and for maintaining a sound system of internal control that supports the achievement of NAGSMA's goals and objectives, whilst safeguarding the public funds and assets.
- Funds received are recorded, accounted and managed through the NCI Agency core financial system.

The NAGSMO Board of Directors approved the NAGSMO Financial Management Procedures Document-Financial Rules and Procedures (FMPD-FRP) to provide guidance on the proper handling and reporting of public funds. The FMPD-FRP sets out the relevant financial rules and procedures in accordance with the NATO Financial Regulations, emphasises the need for economy, efficiency and effectiveness, and promotes good practice and high standards of propriety.

Purpose of the System of Internal Control

The system of internal control is designed to ensure that NATO assets are used for the purposes intended and that the transactions relating to their usage reflect the highest standards of integrity to justify continued confidence of the AGS Programme Participating Nations.

The process within NAGSMA accords with the NAGSMO FMPD-FRP and has been in place for the year ending 31 December 2015 and up to the date of approval of the Financial Statements.

Risk and Control Framework

The NAGSMA system of internal control is based on an ongoing process designed to identify the key risks to the achievement of NAGSMA goals and objectives, to evaluate the nature and extent of those risks and to manage them efficiently and effectively.

NAGSMA is committed to a process of continuous development and improvement: developing systems in response to any relevant reviews and developments in best practice in this area.

Since the NCI Agency carries out transactions on behalf of NAGSMA under the Service Support Agreement, NAGSMA's processes need to be compatible to the NCI Agency financial management system.

Review of Effectiveness

The Financial Controller has responsibility for reviewing the effectiveness of the system of internal control. The review is informed by:

- The executive managers within the organisation who have responsibility for the development and maintenance of the internal control framework;
- Periodic Internal Audits performed on selected areas of activity within the FCRM division; and
- Comments made by the external auditors in their management letters and other reports.

Appropriate action is in place to address any weaknesses identified and to ensure the continuous improvement of the system. During 2015, no material instances of failure to the internal control system were reported that should be brought to your attention.



James E. EDGE
NAGSMA General Manager



Grazia M. D'Arcangelo
NAGSMA Financial Controller

NAGSMA – Statement of Financial Position
as at 31 December 2015
(all amounts in Euro)

	Notes	Current Year	Prior Year
	ANNEX B	31-Dec-15	31-Dec-14
ASSETS			
Cash and cash equivalents	B01	332,241,018	208,509,930
Short-term investments	B02	0	99,032,548
Receivables	B03	59,589,270	196,939,855
Other current assets and prepayments	B04	116,186	460,159
Current assets		391,946,474	504,942,492
TOTAL ASSETS		391,946,474	504,942,492
LIABILITIES			
Payables	B05	470,254	13,460,636
Advances and deferred revenue	B06	387,731,675	488,793,369
Short term provisions	B07	116,186	124,622
Other current liabilities	B08	3,628,359	2,563,865
Current liabilities		391,946,474	504,942,492
NET ASSETS/EQUITY			
Accumulated surpluses/(deficits)		0	0
Net Assets/Equity		0	0
TOTAL LIABILITIES		391,946,474	504,942,492

**NAGSMA – Statement of Financial Performance
for the year ended 31 December 2015
(all amounts in Euro)**

	Notes	Current Year	Prior Year
	ANNEX C	2015	2014
REVENUE			
Revenue from non-exchange transactions	C01	9,428,643	8,317,149
Revenue		9,428,643	8,317,149
EXPENSES			
Personnel	C02	6,837,755	6,257,410
Contractual supplies and services	C03	2,590,888	2,059,739
Expenses		9,428,643	8,317,149
NET SURPLUS/(DEFICIT)		0	0
NET SURPLUS/(DEFICIT) ALLOCATION			
Reserves		0	0
Accumulated surpluses/(deficits)		0	0
Net surplus/(deficit) allocation		0	0

NAGSMA – Cash Flow Statement (Indirect Method)
for the year ended 31 December 2015
(all amounts in Euro)

	Notes	Current Year	Prior Year
	ANNEX D	2015	2014
CASH FLOW FROM OPERATING ACTIVITIES			
Cash flow from operating and other activities			
Net surplus/(deficit)		0	0
Total cash flow from operating and other activities		0	0
Non-cash movements			
Decr./((incr.) Other current assets and prepayments		343,973	(166,048)
Decr./((incr.) Receivables		137,350,585	114,733,837
Decr./((incr.) Short-term investments		99,032,548	(99,032,548)
Total decrease/(increase) Current assets		236,727,106	15,535,241
Increase/(decrease) Current liabilities			
Incr./((decr.) Provisions		(8,436)	(32,222)
Incr./((decr.) Other current liabilities		1,064,494	(1,548,576)
Incr./((decr.) Payables		(12,990,382)	13,304,315
Incr./((decr.) Advances and deferred revenue		(101,061,694)	(37,538,753)
Total increase/(decrease) Current liabilities		(112,996,018)	(25,815,236)
NET CASH FLOW FROM OPERATING ACTIVITIES		123,731,088	(10,279,995)
NET CASH FLOW FROM INVESTING ACTIVITIES		0	0
NET CASH FLOW FROM FINANCING ACTIVITIES		0	0
NET INCREASE/(DECREASE) CASH AND CASH EQUIVALENTS		123,731,088	(10,279,995)
CASH AND CASH EQUIVALENTS AT THE BEGINNING OF THE PERIOD		208,509,930	218,789,925
CASH AND CASH EQUIVALENTS AT THE END OF THE PERIOD		332,241,018	208,509,930

**NAGSMA – Statement of Changes in Net Assets/Equity
for the year ended 31 December 2015
(all amounts in Euro)**

BALANCE AT 31-DECEMBER-2014	0
Net surplus for the period	0
BALANCE AT 31-DECEMBER-2015	0
NET CHANGE IN ASSETS/EQUITY (OPERATING FUND) FOR THE YEAR ENDED 31-DECEMBER-2015	0

NAGSMA Budget Execution Statement - Administrative Budget
for the year ended 31 December 2015
(All amounts in Euro)

	Notes		Initial Authorisation	Mid-year Review (MYR)	Final Approval - MYR	Transfers	Final Authorisation	Net Commitment	Expenses	Total	Carry Forward	Lapsed
	ANNEX E											
					MYR		FA					
Personnel												
2014 - Personnel	E01	131,826	0	131,826	0	131,826	131,826	0	104,364	104,364	0	27,462
2015 - Personnel	E02	8,831,373	-81,000	8,750,373	-22,000	8,728,373	8,728,373	0	6,741,829	6,741,829	0	1,986,544
Total Personnel		8,963,199	-81,000	8,882,199	-22,000	8,860,199	8,860,199	0	6,846,193	6,846,193	0	2,014,006
Contractual supplies and services												
2014 - Contractual supplies and services	E03	196,879	0	196,879	0	196,879	196,879	0	70,190	70,190	0	126,689
2015 - Contractual supplies and services	E04	2,773,151	195,000	2,968,151	22,000	2,990,151	2,990,151	0	2,476,361	2,476,361	0	513,790
Total Contractual supplies and services		2,970,030	195,000	3,165,030	22,000	3,187,030	3,187,030	0	2,546,551	2,546,551	0	640,479
Capital and investment budgeting												
2014 - Capital and investment budgeting	E05	0	0	0	0	0	0	0	0	0	0	0
2015 - Capital and investment budgeting		30,000	0	30,000		30,000	30,000	0	0	0	0	30,000
Total Capital and investment budgeting		30,000	0	30,000	0	30,000	30,000	0	0	0	0	30,000
Budget contingencies												
2014 - Budget contingencies		0	0	0	0	0	0	0	0	0	0	0
2015 - Budget contingencies	E06	200,000	-114,000	86,000		86,000	86,000	0	0	0	0	86,000
Total Budget contingencies		200,000	-114,000	86,000	0	86,000	86,000	0	0	0	0	86,000
TOTAL BUDGET EXECUTION		12,163,229	0	12,163,229	0	12,163,229	12,163,229	0	9,392,744	9,392,744	0	2,770,485

NAGSMO Budget Execution Statement - Operational Budget Total
for the year ended 31 December 2015
(All amounts in Euro equivalent)

Notes	Initial Authorisation	Mid Year - Review (MYR)	Final Approval - MYR	Transfers	Final Authorisation	Net Commit-ment	Actual Expenses	Total Spend	Carry Forward	Lapsed
Annex F										
			MYR		FA					
AGS Core System Procurement										
2012 - AGS Core System Procurement	1,022,208	0	1,022,208	0	1,022,208	127,678	894,531	1,022,208	127,678	0
2014 - AGS Core System Procurement	194,194,174	0	194,194,174	0	194,194,174	19,897,536	174,296,638	194,194,174	19,897,536	0
2015 - AGS Core System Procurement	317,782,283	-56,035,336	261,746,947	0	261,746,947	115,496,815	146,250,132	261,746,947	115,496,815	0
TOTAL AGS Core System Procurement	512,998,665	-56,035,336	456,963,329	0	456,963,329	135,522,029	321,441,300	456,963,329	135,522,029	0

ECB Rate avg. from Jan 1 2015 to Dec 31 2015 was 1.1095

NAGSMO Budget Execution Statement - Operational Budget (EUR part)
for the year ended 31 December 2015
All amounts in Euro

Notes	Initial Authorisation	Mid Year - Review (MYR)	Final Approval - MYR	Transfers	Final Authorisation	Net Commit- ment	Actual Expenses	Total Spend	Carry Forward	Lapsed
Annex F										
BL 6604011		MYR			FA					
System Design, Development and Qualification										
2014 - System Design, Development and Qualification	65,030,350	0	65,030,350	0	65,030,350	2,682,711	62,347,639	65,030,350	2,682,711	0
2015 - System Design, Development and Qualification	59,967,033	-24,837,393	35,129,640	984,329	36,113,969	15,330,603	20,783,365	36,113,968	15,330,603	0
Total System Design, Development and Qualification	124,997,383	-24,837,393	100,159,989	984,329	101,144,318	18,013,314	83,131,004	101,144,318	18,013,314	0
Production										
2014 - Production	4,836,250	0	4,836,250	0	4,836,250	1,374,166	3,462,084	4,836,250	1,374,166	0
2015 - Production	47,175,844	17,506,915	64,682,759	35,598	64,718,357	24,063,662	40,654,695	64,718,357	24,063,662	0
Total Production	52,012,094	17,506,915	69,519,009	35,598	69,554,607	25,437,828	44,116,779	69,554,607	25,437,828	0
Management Reserve										
2014 - Management Reserve	1,477,215	0	1,477,215	0	1,477,215	1,367,684	109,531	1,477,215	1,367,684	0
2015 - Management Reserve	10,719,274	-2,537,878	8,181,396	-211,053	7,970,343	3,985,172	3,985,171	7,970,343	3,985,172	0
Total Management Reserve	12,196,489	-2,537,878	9,658,611	-211,053	9,447,558	5,352,856	4,094,702	9,447,558	5,352,856	0
CAFX										
2014 - CAFX	360,986	0	360,985	0	360,985	20	360,965	360,985	20	0
2015 - CAFX	2,999,479	-2,478,979	520,500	-308,874	211,626	1,000	210,626	211,626	1,000	0
Total CAFX	3,360,464	-2,478,979	881,485	-308,874	572,611	1,020	571,591	572,611	1,020	0
IIS										
2015 - IIS	500,000	0	500,000	-500,000	0	0	0	0	0	0
Total IIS	500,000	0	500,000	-500,000	0	0	0	0	0	0
	193,066,430	-12,347,336	180,719,094	0	180,719,094	48,805,018	131,914,076	180,719,094	48,805,018	0

NAGSMO Budget Execution Statement - Operational Budget (USD part)
for the year ended 31 December 2015
All amounts in USD

Notes	Initial Authorisation	Mid Year - Review (MYR)	Final Approval - MYR	Transfers	Final Authorisation	Net Commitment	Actual Expenses	Total Spend	Carry Forward	Lapsed
Annex F										
BL 6604010					FA					
System Design, Development and Qualification										
2014 - System Design, Development and Qualification	103,253,002	0	103,253,002	0	103,253,002	10,819,194	92,433,808	103,253,002	10,819,194	0
2015 - System Design, Development and Qualification	112,807,747	-58,107,630	54,700,117	14,749,285	69,449,402	36,147,305	33,302,097	69,449,402	36,147,305	0
Total System Design, Development and Qualification	216,060,749	-58,107,630	157,953,119	14,749,285	172,702,404	46,966,499	125,735,905	172,702,404	46,966,499	0
Production										
2014 - Production	31,141,489	0	31,141,489	0	31,141,489	5,234,201	25,907,288	31,141,489	5,234,201	0
2015 - Production	80,424,606	-12,230,734	68,193,872	28,281,803	96,475,675	40,342,662	56,133,013	96,475,675	40,342,662	0
Total Production	111,566,095	-12,230,734	99,335,361	28,281,803	127,617,164	45,576,863	82,040,301	127,617,164	45,576,863	0
Management Reserve										
2014 - Management Reserve	1,134,140	0	1,134,140	0	1,134,140	141,659	992,482	1,134,140	141,659	0
2015 - Management Reserve	17,941,701	16,204,188	34,145,889	-30,738,371	3,407,518	3,407,518	0	3,407,518	3,407,518	0
Total Management Reserve	19,075,842	16,204,188	35,280,029	-30,738,371	4,541,658	3,549,177	992,482	4,541,658	3,549,177	0
CAFX										
2014 - CAFX	1,507,469	0	1,507,469	0	1,507,469	4,348	1,503,121	1,507,469	4,348	0
2015 - CAFX	1,954,660	5,662,340	7,617,000	-7,492,717	124,283	115,637	8,646	124,283	115,637	0
Total CAFX	3,462,129	5,662,340	9,124,469	-7,492,717	1,631,752	119,985	1,511,767	1,631,752	119,985	0
IISS										
2015 - IISS	4,800,000	0	4,800,000	-4,800,000	0	0	0	0	0	0
Total IISS	4,800,000	0	4,800,000	-4,800,000	0	0	0	0	0	0
	354,964,815	-48,471,837	306,492,978	0	306,492,978	96,212,524	210,280,454	306,492,978	96,212,524	0

Notes to the Financial Statements for the year ending 31 December 2015

Index Page

- A. Basis of Preparation and Accounting Policies
- B. Notes to the Statement of Financial Position
- C. Notes to the Statement of Financial Performance
- D. Notes to the Cash Flow Statement
- E. Notes to the Budget Execution Statement – Administrative Budget
- F. Notes to the Budget Execution Statement – Operational Budget
- G. General Notes to the Financial Statements

ANNEX A Basis of Preparation and Accounting Policies

A01 Basis of preparation

The financial statements of the NAGSMO, including NAGSMA being the executive body of the NATO Alliance Ground Surveillance Management Organisation (NAGSMO), have been prepared on the accrual basis of accounting in accordance with the International Public Sector Accounting Standards (IPSAS) and based on International Financial Reporting Standards (IFRS/IAS), as adopted by the North Atlantic Council (NAC) in 2002. In 2013, the NAC adopted an adaptation to IPSAS to better suit the specific requirements of the Alliance and an associated NATO Accounting Framework, applicable for financial reporting periods beginning on 1 January 2013.

The financial statements have been prepared in accordance with the NATO Accounting Framework, the NATO Financial Regulations (NFRs) and the Financial Rules and Procedures (FRPs) and the relevant entity directives and policies.

In accordance with Article 2.1 of the NFRs, the financial year at NAGSMA begins on 1 January and ends on 31 December of the year.

The NAGSMO financial statements have been prepared on a going concern basis. During the Lisbon Summit in 2010 the Heads of State and Government approved the consolidation and rationalisation of the functions and programmes of the 14 NATO agencies into three agencies and the reorganisation of the military commands. NAGSMA is recognized as the NATO Procurement, Logistics and Support Organisation (NPLSO) in the framework of NATO Agencies' Reform initiative.

These financial statements represent the consolidated activities of the NATO Alliance Ground Surveillance Management Organisation (NAGSMO) and its executive body NAGSMA.

NAGSMA's significant accounting policies are set out below. The accounting policies have been applied consistently to all periods presented.

A02 Use of estimates

In accordance with IPSAS and generally accepted accounting principles, the financial statements necessarily include amounts based on estimates and assumptions by management, based on historical experience as well as the most reliable information available, judgement and assumptions. Estimates include accrued revenue and expenses. The majority of goods and services are provided by third parties and other NATO entities; therefore, accrued expenses and the related revenue recognition are based on estimates. By nature, these estimates are subject to measurement uncertainty. Actual results could differ from those estimates. Changes in estimates are reflected in the period in which they become known.

A03 Significant Accounting Policies

Accounting as a Procurement Agent

IPSAS draws a distinction between transactions that an entity undertakes on its own behalf (principal) and those on behalf of others (agent). The distinction is whether the economic benefits arising from the procurement effort accrue to the entity or to the extent that a fee may be levied for providing an agency service.

Agency activities are those activities carried out by the reporting entity, but which are not its own activities. Where an entity undertakes agency activities, it is identified as the agent in relation to those activities.

NAGSMA is considered as a procurement agent in respect of its operations since:

- It was created for the sole purpose of procuring the AGS Core System on behalf of the AGS Participating Nations;
- It does not bear any inventory risk before or after the customer order;
- It does not bear the credit risk for the amounts receivable from the customer;
- It does carry out acceptance of goods and services on behalf of Nations/NATO;
- It does not receive a fixed fee per transaction or a stated percentage of the amount billed, as it is reimbursed for the running costs of the Agency via the Administrative Budget.

NAGSMA provides contract administration function to NAGSMO. NAGSMA acts as an agent in accordance with a mandate set by the NAGSMO Participating Nations in the PMOU, which defines the role of the Agency in the procurement of a NATO owned and operated core AGS capability. NAGSMO is as well considered an Agent in respect of its operations, as a subsidiary body of NATO, with the sole objective to procure the AGS Core which will be owned, controlled and operated by the 28 Nations of NATO. NAGSMO and its executive body NAGSMA do not have and will not have control in the future of the assets procured as per the criteria in the NATO Accounting Framework. Transactions are treated accordingly in the NAGSMO Financial Statements.

Foreign Currency Translation

The functional and reporting currency of NAGSMA is the EUR. Transactions in currencies other than EUR are translated into EUR at the prevailing NATO rates of exchange at the time of transaction. Monetary assets and liabilities denominated in currencies other than EUR are translated into EUR at the prevailing NATO year-end closing rate. Resulting foreign exchange unrealised gains and losses are recognised as Advances from Nations. Realised exchange differences are recognised as Payables to Nations in the Statement of Financial Position.

Financial Instruments

Financial instruments are recognised at the contract date and initially measured at fair value. Their subsequent measurement depends on their classification. Loans and receivables and other liabilities are not re-valued (except for changes in exchange rates which are included in

the Statement of Financial Performance). Financial instruments are not recognised on expiry or when all contractual rights and obligations are transferred.

Management is aware of the risks associated with financial instruments and is bound by NAGSMO's Financial Rules and Procedures to keep these risks very low. NAGSMA uses only non-derivative financial instruments as part of its normal operations, such as bank accounts, deposit accounts.

Currency risk: To limit the exposure to foreign currency exchange risk, NAGSMA is forecasting the yearly expected expenditures in foreign currencies. In order to have the required funding, NAGSMA asks the Participating Nations to provide their contributions in the necessary currencies.

Liquidity risk: The liquidity risk is based on the assessment of whether the organisation will encounter difficulties in meeting its obligation associated with financial liabilities. There is a very limited exposure to liquidity risk because of the budget funding mechanism that guarantees contributions for the total approved budget. The accuracy of forecasts that result in the calls for contributions as well as the delay in payment represents the main liquidity risks. There is a clause in the NAGSMO FRP art. 28 Payment of Contributions, that deals with unpaid contributions giving the Agency the authority to determine the appropriate course of action in case of a delay or a non-payment and the financial consequences of such, borne by the Participating Nation.

Credit Risk: There is a very limited credit risk as the contributing Nations generally have a high credit rating.

Cash and Cash Equivalents

Cash and cash equivalents includes cash held with the bank in current and savings accounts.

Receivables

Receivables are stated at net realisable value, after provision for doubtful and uncollectible debts. No allowance for loss is recorded with respect to Member States' assessed contributions receivable except for exceptional and agreed technical reasons.

Other Current Assets

Other current assets include prepayments which are payments in advance of the period to which it pertains as well as bank interest receivable at year-end.

Payables

Payables are amounts due to third parties based on goods received or services provided that remain unpaid. This includes an estimate of accrued obligation to third parties for goods and services received but not yet invoiced.

Advances and Unearned Revenue

Advances are contributions called or received related to future years' budgets. Advances include future budget funding.

Unearned revenue represents contributions from Nations and/or third parties that have been called for current or prior years' budgets but that have not yet been recognised as revenue. Funds are called in advance of their need because the entity has no capital that would allow it to pre-finance any of its activities.

Provisions and Contingent Liabilities

Provisions are recognised when NAGSMA has a present obligation as a result of a past event, and it is probable that NAGSMA will be required to settle that obligation. Provisions are measured at the General Manager's best estimate of the expenditure required to settle the obligation at the date of the statement of financial position, and are discounted to present value where the effect is material.

Other commitments, which do not meet the recognition criteria for liabilities, are disclosed in the notes to the financial statements as contingent liabilities when their existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events which are not wholly within the control of NAGSMA.

Budget Execution Statement

The Board of Directors approves the annual budgets which include budgeted amounts for the administration of the Agency and Programme costs. Budgets may be subsequently amended by the Board of Directors or through the exercise of delegated authority. The budget execution statement provides a comparison of budgeted and actual amounts calculated on accrual basis.

Revenue and Expense Recognition

Revenue comprises contributions from Participating Nations to fund the entity's budgets. Revenue is recognised to the extent that it is probable that the economic benefits will flow to the entity and the revenue can be measured reliably. Where a transfer is subject to conditions that, if unfulfilled, require the return of the transferred resources, NAGSMA recognises a liability until the condition is fulfilled.

Revenue for the Administrative Budget

Contributions to the budget are initially recorded as advances from nations. They are recognised as revenue in the statement of financial performance when such contributions are used for their intended purpose as envisioned in its approved budget.

Interest

Interest receivable is credited as payables to Participating Nations in the statement of financial position.

Representation Allowance

As from 1 June 2013, a summary of the operations related to the Representation Allowance are included in the Financial Statements. Transactions occurring in respect of Representation Allowance are expensed in the period to which they relate, and were paid directly from payroll.

Post-employment benefits

Defined Contribution Plans

NAGSMA employees are members of the NATO-wide Defined Contribution Pension Scheme (DCPS). The assets of the plans are held separately from those of NAGSMA in funds under the control of trustees. NAGSMA is required to contribute a specified percentage of payroll costs to the DCPS to fund the benefits. Payments to the DCPS are recognised as an expense when employees have rendered service entitling them to the contributions. The only obligation of NAGSMA with respect to the DCPS is to make the specified contributions.

Defined Benefit Plans

NAGSMA employees who have joined NATO before 1 July 2005 are members of the NATO Coordinated Pension Scheme which is a funded defined benefit plan. Under the plans and upon completion of 10 years employment with NATO, the employees are entitled to retirement benefits of 2% per year of service of final basic salary on attainment of a retirement age of 60. No other post-retirement benefits are provided to these employees. Staff members whose length of service is not sufficient to entitle them to a retirement pension are eligible for a leaving allowance. The assets and liability for NATO's Defined Benefit Plan are accounted for centrally at NATO Headquarters and therefore are not recognised in these financial statements.

ANNEX B Notes to the Statement of Financial Position

Notes Reference	Current Year	Prior Year
	31-Dec-15	31-Dec-14

The Statement of Financial Position details the assets and liabilities of NAGSMA as of 31 December.

B01	Cash and cash equivalents	332,241,018	208,509,930
------------	----------------------------------	--------------------	--------------------

Cash and Cash equivalents are short-term liquid assets.

NAGSMA operates highly reliable and interest bearing bank accounts: an administrative and an operational account that have three currency sub-accounts.

B02	Short-term investments	0	99,032,548
------------	-------------------------------	----------	-------------------

Short-term investments are bank deposits maturing in less than 3 months.

B03	Receivables	59,589,270	196,939,855
------------	--------------------	-------------------	--------------------

Accounts receivable are kept in separate sub-ledgers that provide detailed insight into the outstanding calls for contribution and provide accurate and up-to-date cash forecast information.

The receivables as of 31 December 2015 are primarily outstanding calls for contributions towards the Administrative Budget 2016 and the Operational Budget 2016 which are not yet past their due date.

The table below provides the overview of Receivables grouped by relevant maturity basket.

Aging detail	0-30 days	31-60 days	above 60 days	TOTAL
Receivables @ 31/12/2015	7,944,061	49,044,439	2,600,770	59,589,270

B04	Other current assets and prepayments	116,186	460,159
------------	---	----------------	----------------

Other current assets match provisions for annual leave entitlements accrued but untaken at year-end.

Similarly to the reclassification of the untaken leave provision from non-current to current, the asset matching the provision has been reclassified to current as well.

In the year 2014 the balance included interest accrued on the bank balances, which in 2015 does not exist as it has been settled before year-end.

In the year 2014 the balance included prepayment related to support contract payable in advance, which expired in 2015.

B05	Payables	470,254	13,460,636
------------	-----------------	----------------	-------------------

These short-term payables are open liabilities for goods and services received in 2015 such as consulting contracts, communication, travel and personnel related invoices. The reduction is primarily due to 2014 accrued invoices related to the procurement effort that have been settled in 2015.

B06	Advances and deferred revenue	387,731,675	488,793,369
------------	--------------------------------------	--------------------	--------------------

Advances from Nations	201,352,557	249,752,155
-----------------------	-------------	-------------

Deferred revenue	186,379,118	239,041,214
------------------	-------------	-------------

Advances from Nations are funds called and/or received from Nations in respect of 2016 Administrative and Operational Budgets and unrealised exchange rate gains and losses. Advances include future budget funding.

Unearned revenue comprises unspent funding from prior periods.

B07	Short-term provisions	116,186	124,622
------------	------------------------------	----------------	----------------

The provision represents annual leave entitlements accrued.

Untaken leave provision has been reclassified from non-current to current given restrictions placed by NATO Civilian Personnel

Regulations with regards to time that untaken leave has to be used.

Balance at 1 January 2015	124,622
Provision release	(8,436)
Balance at 31 December 2015	116,186

B08	Other current liabilities	3,628,359	2,563,865
------------	----------------------------------	------------------	------------------

Other payables include lapsed credits 2015 and the 2015 financial result that will have to be refunded upon national decision.

B09	Contingent Liabilities	
------------	-------------------------------	--

NAGSMA has assumed certain liabilities related to UAV tests in the fiscal year of 2015. The UAV tests may create the liability that NAGSMA has indemnified its main contractor against at this stage of AGS Programme execution. This was negotiated within the AGS Core Contract in order to assure financial affordability of the AGS Programme. The costs in case of materialization of the contingent liability will be borne by NAGSMO Nations. The outcome of this matter cannot be presently determined and cannot be measured reliably.

NAGSMA was involved in 2014 in an administrative proceeding in connection with certain events that have occurred in the year 2014. The ultimate outcome of that proceeding occurred in August 2015 where NAGSMA was required to make a payment of EUR 14,000. The respective payment has been recorded in the Statement of Financial Performance in the fiscal year of 2015.

ANNEX C Notes to the Statement of Financial Performance

Notes Reference	Current Year	Prior Year
	2015	2014
The Statement of Financial Performance details the revenue and expenses that NAGSMA incurred during the year ending 31 December.		
C01 Revenue from non-exchange transactions	9,428,643	8,317,149
Revenue represents funding from Nations for expenses incurred during the financial year.		
C02 Personnel	6,837,755	6,257,410
The costs in this Chapter are for staff members hired under the NATO Civilian Personnel Regulations as well as for consultants and contractors.		
The figures represent the costs of personnel including basic salary, allowances, insurance and pension plan contributions.		
NAGSMA had 53 staff members at the year-end 2015 (2014: 49 staff members).		
The breakdown of wages, salaries and employee benefits is as follows:		
	Year ended 31/12/15	Year ended 31/12/14
	EUR	EUR
Employee benefits expense, consultants and contractors	6,313,772	5,804,851
Post-employment benefits (see note F01)		
for defined contribution pension scheme	518,419	484,781
for defined benefit pension scheme	0	0
Termination benefits	14,000	0
Provision for annual leave entitlements accrued	(8,436)	(32,222)
Total employee benefits expense	6,837,755	6,257,410
C03 Contractual supplies and services	2,590,888	2,059,739
Supplies and consumables are costs of goods and services used by NAGSMA associated with the general management and administrative activities under the SSA and SLA, such as information management, finance, human resources, building and facilities, security, travel expenses, etc. These costs are linked to the approved NAGSMA Staffing Plan. It also includes hospitality funds, communications services (i.e. telephones), NSPA and NATO Headquarters support (MOA).		

ANNEX D Notes to the Cash Flow Statement

The Cash Flow Statement is prepared using the indirect method.

The Cash Flow Statement summarises the cash movements in and out of the Agency during the financial year.

ANNEX F Notes to the Budget Execution Statement – Operational Budget

The accounting basis used in preparation and presentation of the Operational Budget is the same as the one used in the financial statements, the accrual basis for recording of the actual expenditures. Due to the Agency's role as an agent acting with no control over the assets being procured, it is not accounting for the operational budget expenditures as an asset under construction. Rather, it is expected that the end-user, Allied Command Operations (ACO), will account for the AGS Core System when the system will be transitioned to ACO.

The classification basis adopted for the Operational Budget is to show expenditure for AGS Core System Procurement. In 2015, there was no planned expenditure in respect of Initial In-Service Support and the funds were transferred to SDDQ as approved by Participating Nations during the End of Year process.

The exchange rate used to translate the USD portion of expenditure to the presentation currency EUR in the Operational Budget Total table is the average exchange rate in 2015 of 1.1095. There are no lapses in the 2015 Operational Budget.

The Operational Budget is presented to Participating Nations in two currencies EUR and USD. The Budget Execution Statements by currency show the Budget's net commitments and expenditures by sub-categories, as presented to and approved by Participating Nations.

System Design, Development and Qualification

The AGS Core System Design, Development and Qualification covers the design and development for the AGS Core System. The Budget includes provisions for milestones which cover: Programme Design Review of the AGS Core System in accordance with the mandatory TRD requirements; Technical Interchange Meetings; the beginning of Critical Design Review and Working Group meetings and Programme design reviews.

Production

Contractual milestones under the production sub-category are related to production progress payments and advance procurement authority to meet the contract timeline for production of deliverable SSS items and related placement of purchase orders for long-lead-time items. Long lead items include parts, components, equipment and sub-assemblies that must be ordered by the Contractor well in advance of actual final assembly such as the structural carbon fibre and metal components, nacelles, communication equipment, navigation equipment.

Management Reserve

The Management Reserve was used to expense NAGSMO BoD approved Pre-PMOU Contributions (PPC) and Non-Financial Contributions (NFC), as well as allocating funding for Amendment 0008 and Wide Band Data Link (WBDL) as per the corresponding approved contractual milestones.

CAFX

Funds committed and expensed for Contracting Furnished Equipment (CAFE) were approved and expended for NATO CIS support to the program including inspections/certifications of MOB facilities in Sigonella and continuing accreditation activities. Additional cryptographic equipment were also procured during 2015 to support the approved ECP changes and securing the AGS core and deployable elements. Other 2015 expenditures include the Foreign Military Sales (FMS) case for TEMPEST testing of the UAV by the U.S. Navy's Certified TEMPEST Authority (CTTA) and system software license procurement and extensions for antivirus.

Carry forwards from 2012 in Management Reserve are commitments for payments for approved USA NFC. There are no Carry forwards from 2013. Carry forwards from 2014 are mostly correlated to pilot training, technical manuals, training courseware, AVMC2 Fabrication, and Formal Test Plans in 2014.

Carry forwards from 2015 are related to Formal Test Plans, training courseware, training, AVMC2 and UAV Command and Control Element (UCE) System Level Performance Verification (SLPV), Provision Guidance Conference, delivery of ship sets for Airborne and Ground WBDL, MOS Formal Entity and TGGs D1 Formal Entity Test Readiness Review.

The Table below represents the cumulative NAGSMA Operational budget per year from 2012 to 2015 expended and carried forward in two currencies EUR and USD. The Budgets are presented below by currency showing the actual expenditures and carry forward as of the 31.12.2015.

NAGSMA Operational Budget EUR

BL6604011	Budget	Actual Expenses	Carry Forward
2012	107,086,412	107,086,412	0
2013	137,794,865	137,794,865	0
2014	122,977,865	117,553,284	5,424,581
2015	109,014,294	65,633,857	43,380,437
Total	476,873,436	428,068,418	48,805,018

NAGSMA Operational Budget USD

BL6604010	Budget	Actual Expenses	Carry Forward
2012	204,865,340	204,723,682	141,659
2013	238,445,262	238,445,262	0
2014	373,468,465	357,410,722	16,057,743
2015	169,456,878	89,443,756	80,013,122
Total	986,235,945	890,023,421	96,212,524

Note to the table:

The Carry Forwards from the Financial Statements 2012-2014 which have been expended in 2015 have been added to the Actual Expenses of 2012 and 2014 respectively.

ANNEX G General Notes to the Financial Statements

G01 Related Party Disclosures

NAGSMO and NAGSMA have related party relationships with the Members of the NAGSMO Board of Directors and a number of other NATO bodies.

Transactions with NATO bodies

	Current Year 2015	Prior Year 2014
	EUR	EUR
NATO Communications and Information Agency	1,585,940	1,497,530
NATO Support Agency	(21,263)	131,000
NATO International Staff	144,268	136,661
SHAPE	2,300	450
NATO School	0	450
	1,711,245	1,766,091

In 2015, the NCI Agency performed certain administrative services for NAGSMA under the Service Support and Service Level Agreements, NATO IS performed other administrative services, NSPA performed additional administrative services for NAGSMA, which due to incomplete implementation resulted in a refund, and SHAPE provided training support.

Compensation of key management personnel

The remuneration of Directors and other members of key management personnel (NATO civilian grade A5 and above) is determined by the NATO salary scales and was as follows during the year:

	Current Year 2015	Prior Year 2014
	EUR	EUR
Basic salaries	706,285	685,338
Allowances	167,479	171,760
Post-employment benefits	70,659	68,873
Employer's contribution to Insurance	93,009	93,004
	1,037,432	1,018,975

The slight increase in compensation of key management personnel is primarily due to step increases.

	Current Year 2015	Prior Year 2014
Number of individuals at year-end on a full time equivalent basis		
General Manager	1	1
Programme Manager	1	1
Key management personnel	4	4
	<u>6</u>	<u>6</u>

G02 Representation Allowance

The purpose of the Representation Allowance is to help meet the reasonable representational expenses of certain designated high officials of the Organisation whose positions entail responsibility for establishing and maintaining relationships of value to NATO.

As from 1 June 2013, a new procedure is in place in respect of Representation Allowance; as all recipients are now reimbursed permitted expenses within the limits of their individual Representation Allowance allocation. All representation allowance disbursements for the 2015 reporting period were administered by the Agency.

Expenditures	EUR
Rental Supplement	2,673
Functions	<u>116</u>
Total	2,789
Entitlements	EUR
Representation Allowance annual entitlement	10,692
<i>of which: Rental Supplement annual entitlement</i>	2,673
Transactions	EUR
Rental Supplement January-December	2,673
Dinners and Luncheons	<u>116</u>
Total	2,789

G03 Approval of Financial Statements

The financial statements were approved by the Financial Controller and authorised to be issued on 29 February 2016.

PAGE LEFT INTENTIONALLY BLANK

PAGE LEFT INTENTIONALLY BLANK

PAGE LEFT INTENTIONALLY BLANK



NATO Alliance Ground Surveillance
Management Organisation
(NAGSMO)

NAGSMO
NATO Headquarters
1110 Brussels
Belgium