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|  | <b>NATO</b> | NORTH ATLANTIC COUNCIL       |
|   | <b>OTAN</b> | CONSEIL DE L'ATLANTIQUE NORD |

**NATO UNCLASSIFIED**

25 January 2018

**DOCUMENT**  
C-M(2018)0002-AS1

**IBAN AUDIT ON THE 2016 FINANCIAL STATEMENTS OF THE NATO SUPPORT AND  
PROCUREMENT ORGANISATION (NSPO)**

**ACTION SHEET**

On 24 January 2018, under the silence procedure, the Council noted the IBAN report on the 2016 financial statements of the NSPO attached to C-M(2018)0002 and agreed to the public disclosure of the report, the IBAN audit and the associated redacted 2016 financial statements.

(Signed) Jens Stoltenberg  
Secretary General

NOTE: This Action Sheet is part of, and shall be attached to C-M(2018)0002.

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15 January 2018

**DOCUMENT**  
C-M(2018)0002  
**Silence Procedure ends:**  
**24 Jan 2018 17:30**

**IBAN AUDIT ON THE 2016 FINANCIAL STATEMENTS OF THE NATO SUPPORT AND  
PROCUREMENT ORGANISATION (NSPO)**

**Note by the Secretary General**

1. I attach the International Board of Auditors for NATO (IBAN) report on the audit of the 2016 financial statements of the NATO Support and Procurement Organisation (NSPO).
2. The IBAN report sets out a qualified opinion on the financial statements and on compliance for the financial year 2016.
3. The IBAN report has been reviewed by the Resource Policy and Planning Board (RPPB) (see Annex). Unless I hear to the contrary by **17:30 hrs on Wednesday, 24 January 2018**, I shall assume that the Council has noted the IBAN report on the 2016 financial statements of the NSPO and agreed to the public disclosure of this report, the IBAN audit and the associated redacted 2016 financial statements.

(Signed) Jens Stoltenberg

Annex 1: RPPB report  
Enclosure 1: IBAN NSPO 2017  
Enclosure 2: Audit NSPO 2016  
Enclosure 3: NSPO FS 2016

Original: English

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**IBAN AUDIT ON THE 2016 FINANCIAL STATEMENTS OF THE NATO SUPPORT AND  
PROCUREMENT ORGANISATION (NSPO)**

**Report by the Resource Policy and Planning Board (RPPB)**

References:

- |                   |   |                                    |
|-------------------|---|------------------------------------|
| A. IBA-AR(2017)12 | - | IBAN audit report                  |
| B. CM(2015)0025   | - | NATO Financial Regulations (NFRs)  |
| C. CM(2017)0048   | - | Implementation of the NFRs by NSPO |
| D. SEC/2017/0008  | - | Letter from Head NSPO Secretariat  |

**INTRODUCTION**

1. This report contains the RPPB's observations and recommendations on the IBAN audit of the 2016 financial statements of NSPO (reference A).
2. The RPPB acknowledges that the issues highlighted in the IBAN audit report have already been dealt with by the appropriate governing bodies of NSPO (the Finance, Administration and Audit Committee (FAAC) and the Agency Supervisory Board (ASB)). That said, the Board is still mandated under Article 15 of the NFRs (reference B) to provide Council with comments and recommendations on the audit opinion.

**DISCUSSION**

3. The IBAN have issued a qualified opinion on the financial statements and on compliance for the 2016 financial year. The IBAN identified seven observations during the audit. The IBAN issued a qualified opinion on the financial statements and on compliance because of material weaknesses in internal control over financial reporting. The IBAN found that there had been much improvement in the preparation of the 2016 NSPO financial statements compared with the previous year but nevertheless still identified a number of material and other issues in them.
4. The remaining six observations did not impact the audit opinion. The IBAN also followed up on the status of observations and recommendations from previous years' audits. While 12 had been settled and five had been superseded by a current year observation the IBAN was concerned that 20 remained outstanding. The IBAN also noted that a very high number of recommendations from prior year management letters remain outstanding, including some that have been outstanding for many years. Finally, the IBAN also highlighted in its audit opinion some limitations in the reporting by the National Organisations of the Central European Pipeline System (CEPS).
5. The RPPB notes that the Agency FAAC and ASB have had detailed discussions about the status of all of the recommendations made by the IBAN based on a thorough review of each of them by NSPA management. The Board notes that in several instances the Agency does not agree with the audit observations and that in these cases discussions with the IBAN are continuing. NSPA management has classified all of the outstanding audit observations as follows:

- a) open: management is currently reviewing how best to address the audit recommendation or will address it at a later date;
- b) in-progress: management is actively working on the resolution of the issue and good progress is being made;
- c) closed: management considers the issue satisfactorily closed or considers it is unable to take further corrective action.

More information on each of these including the management action being taken by the Agency to address these has been provided to the ASB and a copy of this detailed submission can be found at enclosure 1.

6. The ASB approved (reference D) a redacted version of the 2016 financial statements for public disclosure.

## **CONCLUSIONS**

7. The IBAN have submitted a qualified opinion on the NSPO financial statements for 2016 which follows on from the qualified opinions issued since 2013. The RPPB acknowledges the efforts that the Agency is making to address the issues identified by the IBAN and recognises the authority and responsibilities of the NSPO FAAC and ASB to monitor the status of outstanding observations. The RPPB is satisfied that sufficient attention is being paid by NSPA management and at the governance level in NSPO to deal with all of the outstanding audit observations.

8. The Board notes the complexity of some of the challenges involved and the technical nature of some of the audit observations. The RPPB welcomes the engagement of senior Agency management (not just the Financial Controller) to address the issues identified in the latest IBAN audit and expects to see progress made in several areas to settle recurring audit themes. The RPPB believes that implementation of the NSPO Financial Rules and Procedures approved by the ASB in June and endorsed by Council in October 2017 (reference C) should also help to address many of the audit observations.

## **RECOMMENDATIONS**

9. The RPPB recommends that the Council:
- (a) note the IBAN report IBA-AR(2016)12;
  - (b) note the conclusions in paragraphs 7-8; and,
  - (c) approve the public disclosure of this report, the IBAN audit (reference A) and the associated redacted 2016 financial statements of NSPO.

**NSPO FINANCIAL STATEMENTS 2016**  
**STATUS OF OUTSTANDING IBAN AUDIT REPORT RECOMMENDATIONS**  
**AS AT 1 NOVEMBER 2017**

Reference: IBA-AR(2017)12 dated 25 August 2017 “*International Board of Auditors for NATO (Board) Auditor’s Report and Letter of Observations and Recommendations on the audit of the NATO Support & Procurement Organisation (NSPO) Financial Statements for the year ended 31 December 2016*”

**1. BACKGROUND**

1.1 A Key Performance Indicator (KPI) of the Agency relates to its accountability; one of the ways in which the Agency’s management monitors its accountability is through proactively addressing recommendations made by its external auditors, the International Board of Auditors for NATO (IBAN).

1.2 This report provides details of the status of the outstanding recommendations reflected in the latest available IBAN audit report on NSPO (reference).

**2. STATUS OF OUTSTANDING IBAN OBSERVATIONS**

2.1 IBAN makes recommendations in the spirit of attempting to enhance NSPA’s internal control environment or through helping to ensure that the information provided in its financial statements is compliant with the NATO Accounting Framework. IBAN recommendations are non-binding on NSPO and it is up to the ASB whether NSPA management should implement a recommendation or not; NSPA management reviews all recommendations in detail and advises the ASB on whether it believes it can, or should, implement the recommendation at the time the General Manager issues his comments on the draft IBAN Audit Report.

2.2 The Appendix to this document provides the status of outstanding IBAN recommendations based on the 2016 audit report (Reference) and how these are being addressed by NSPA management. Management classifies the status of recommendations as follows:

2.2.1 **Open** – NSPA management is currently reviewing how best to address the recommendation or will address the recommendation at a later date.

2.2.2 **In-progress** – NSPA management is actively working on the resolution of the recommendation and has made good progress in resolving the issue.

2.2.3 **Closed** – NSPA management considers the issue satisfactorily closed or considers it is unable to take further corrective action.

2.3 In its 2016 Audit Report, the IBAN issued 7 new recommendations and followed up on the status of recommendations from previous years' audits, noting that 12 had been settled, 7 had been superseded by a current year observation and 18 were still fully outstanding. This gives a total of 25 recommendations that the IBAN consider to be open.

2.4 When NSPA management reviews the IBAN recommendations it breaks some recommendations into their component parts for ease of tracking (e.g. Recommendation 1 in 2016 had 12 distinct components which are tracked as 12 separate recommendations). This means that whereas the IBAN considers that there are 25 recommendations that are open, NSPA management is currently tracking 38 recommendations. Of these 38 recommendations (in brackets the status of the recommendations when discussed at the spring 2017 meeting is included), NSPA management considers that:

- 8 are Open (spring 2017: 6)
- 21 are In-progress (spring 2017: 15)
- 9 are Closed (spring 2017: 19)

### **3. RECOMMENDATION**

The Finance, Administration and Audit Committee is requested to note this report.

**SUMMARY OF THE PRIOR YEARS OUTSTANDING IBAN OBSERVATIONS  
WITH MANAGEMENT'S COMMENTS**

| No. | OBSERVATION / RECOMMENDATION  | NSPA MANAGEMENT COMMENT   | INTERNAL STATUS OF RECOMMENDATION |
|-----|---|---|-----------------------------------|
|     | <b>2016 NSPO Audit Report</b>   |   |                                   |
| 1   | <b>Recommendation 1 (para 1.12)</b><br>Referring to the reporting of FMS balances, the Board recommends that:<br>a) FMS expenditures incurred should be netted from prepaid expenses (asset) rather than being recorded as a liability.   | <p>There is a difference of opinion between the IBAN and the Agency in this regard. The Agency considers that the accounting is in accordance with the NATO Accounting Framework.</p> <p>The Agency met with the IBAN on 2 October 2017 to discuss the Agency's position. The IBAN did not agree with the Agency's position. The Agency will therefore implement the IBAN recommendation for the production of the 2017 Financial Statements.</p> | <b>In Progress</b>                |
| 2   | <b>Recommendation 1 (para 1.12)</b><br>Referring to the reporting of FMS balances, the Board recommends that:<br>b) The notes to the financial statements define more specifically what is meant by "modified cash basis" when recording FMS activities.                                  | <p>The Agency has drafted wording to be incorporated in the 2017 financial statements.</p>  | <b>In Progress</b>                |
| 3   | <b>Recommendation 1 (para 1.13)</b><br>Referring to PPE reporting, the Board recommends that:<br>a) CEPS Programme Board ensure that sufficient and relevant control procedures are performed by the German National Organisation to ensure that there is a well-documented assessment of | <p>a) It is not possible to gain further information in this area. The NATO Accounting Framework's Accounting Policy on Property, Plant and Equipment, which will be in effect on 1 January</p>   | <b>In Progress</b>                |

| No. | OBSERVATION / RECOMMENDATION  | NSPA MANAGEMENT COMMENT  | INTERNAL STATUS OF RECOMMENDATION |
|-----|---|--|-----------------------------------|
|     | pipeline assets in progress.  | 2018, means that this issue will disappear with the 2018 Financial Statements.   |                                   |
|     | <p>b) CEPS Programme Board liaise with the French National Organisation and its private company service provider to ensure that appropriate and up to date control is being performed by the National Organisation.</p> <p>c) NSPO Financial Statements record the estimate of dismantling, removing and restoring costs related to the pipeline assets or disclose why an assessment of the costs is not possible.</p> | <p>b) The CEPS Programme Board will take this forward.</p> <p>c) The Agency has drafted further disclosures for incorporation in the 2017 Financial Statements</p> |                                   |
| 4   | <p><b>Recommendation 1 (para 1.14)</b></p> <p>The Board recommends NSPA to determine which Customer Advances are current and which are non-current, and present them appropriately in the Statement of Financial Position. This could impact the audit opinion in the future if this is not carried out.</p>  | The Agency is looking into how to do this.   | Open                              |
| 5   | <p><b>Recommendation 1 (para 1.15)</b></p> <p>The Board recommends NSPA to liaise with the French tax administration to be able to support why this liability still exists.</p>   | CEPS considers that such taxes no longer meet the definition of an accrual and therefore accrued amounts will be reversed in the 2017 financial statements.        | In Progress                       |
| 6   | <p><b>Recommendation 1 (para 1.16)</b></p> <p>The Board recommends that NSPO take appropriate follow-up actions when requests for declarations of related parties are not answered.</p>   | This is an issue for the ASB to take forward.  | Open                              |



| No. | OBSERVATION / RECOMMENDATION  | NSPA MANAGEMENT COMMENT  | INTERNAL STATUS OF RECOMMENDATION |
|-----|---|--|-----------------------------------|
| 7   | <p><b>Recommendation 1 (para 1.17)</b></p> <p>The Board recommends that the NSPO Financial Statements separately disclose CEPS military and non-military operational activities from those coming from budget appropriations from the CEPS nations.</p>   | <p>The Agency will make extra disclosures in the notes to the 2017 Financial Statements.</p>   | <p><b>In Progress</b></p>         |
| 8   | <p><b>Recommendation 1 (para 1.18)</b></p> <p>Referring to the inaccuracies and errors identified in the reporting, the Board recommends that:</p> <ul style="list-style-type: none"> <li>a) NSPA ensure a presentation of the financial statements that is compliant with the requirements of the NATO Accounting Framework.</li> <li>b) Sufficient and appropriate procedures be set-up to avoid the risk of errors in the Financial Statements and to be in compliance with the NFRs in respect to internal controls.</li> </ul> | <p>The Agency continues to work diligently in this area with the aim of achieving an unqualified audit opinion in respect of both the financial statements and compliance with underlying regulations.</p> | <p><b>Open</b></p>                |
| 9   | <p><b>Recommendation 2 (para 2.7)</b></p> <p>The Board recommends that NSPO:</p> <ul style="list-style-type: none"> <li>a) Choose a specific internal control framework that it will use to assess its system of internal control. Since other NATO entities, including NCIO and ACO, have already adopted COSO as their internal control framework, and it is a framework that can be used by entities of all types, NSPO should consider adopting COSO as their internal control framework.</li> </ul>                            | <ul style="list-style-type: none"> <li>a) The Agency will base its internal control system on COSO.</li> </ul>   | <p><b>Open</b></p>                |

| No. | OBSERVATION / RECOMMENDATION   | NSPA MANAGEMENT COMMENT  | INTERNAL STATUS OF RECOMMENDATION |
|-----|--|--|-----------------------------------|
|     | <p>b) Assess and document the system of internal control and risk management procedures to support compliance with the NFRs, FRPs and the internal control framework that it chooses.</p> <p>c) Prepare an entity-wide risk management policy throughout the organisation and that risk registers are developed and employed throughout all NSPO segments and operations.</p> <p>d) Perform internal audit activities that fully evaluate internal control and risk management throughout NSPO, and that this work be clearly documented so as to be able to conclude as to NSPO's compliance against the NFRs and FRPs.</p> | <p>b) This will be done as part of the implementation of the internal control system. An internal Process Working Group has this task for action. As agreed in the Transition Plan the Agency has up to 24 months to implement a system of internal control.</p> <p>c) The Agency is required by both its Charter and the NATO Financial Regulations to have risk management in place. The Agency has had an entity-wide risk management policy in place since 2015. The Agency is currently drafting further operating guidance which will provide more detailed information about the implementation of the policy, as well as provide information on how to access, input, and retrieve information from the Risk Management tool developed by IT. The Agency aims to have fully embedded risk management by the end of 2018.</p> <p>d) The 2018 Internal Audit Plan will address the implementation of a risk management policy and an internal control framework. The scope of the audits in both these areas will be necessarily limited given the maturity of both.</p> |                                   |

| No. | OBSERVATION / RECOMMENDATION   | NSPA MANAGEMENT COMMENT  | INTERNAL STATUS OF RECOMMENDATION |
|-----|--|--|-----------------------------------|
| 10  | <b>Recommendation 3 (para 3.5)</b><br>The Board recommends that the Audit Advisory Panel (as described in Article 16 of the revised NFRs) shall only be a consultative and advisory body with no approval required before the issuance of the Internal Audit plan.   | The Terms of Reference of The Audit Advisory Panel require it to be consultative and advisory only. While it endorses the internal audit plan, this is a recommendation to the General Manager to approve the plan, rather than an approval in itself.   | Closed                            |
| 11  | <b>Recommendation 3 (para 3.6)</b><br>The Board recommends that the Auditor General report functionally to the General Manager and also have the ability to report directly to the Audit Committee at ASB level.   | This Auditor General already reports functionally to the General Manager. Procedure XIV of the NSPO Financial Rules and Procedures already foresees the Auditor General reporting to the Finance, Administration and Audit Committee.  | Closed                            |
| 12  | <b>Recommendation 4 (para 4.5)</b><br>The Board recommends that NSPA:<br>a) Improve the control environment over accrual estimates, including training of non-finance staff on how to identify, keep records and communicate transactions of an accrual nature at year-end.<br>b) <i>This is separately tracked – please refer to No. 13</i> | a) The Agency agrees that additional training of personnel involved in the determination of accrued liabilities at the year-end would be beneficial, and will conduct such training in 2017. In addition, Finance and Logistics will start work on reviewing accruals data before the year-end to ensure that less time needs to be spent on reviewing accrual data after the year-end.<br>b) <i>This is separately tracked – please refer to No. 13</i> | Open                              |

| No. | OBSERVATION / RECOMMENDATION   | NSPA MANAGEMENT COMMENT  | INTERNAL STATUS OF RECOMMENDATION |
|-----|--|--|-----------------------------------|
|     | <p>c) Discontinue the use of the 15% mark-up methodology by improving the process to ensure that accrual estimates are based on the receipt of goods and services before year-end.</p> <p>d) Develop control activities which would prevent the possibility to cancel purchase order for items that have already been delivered.</p> | <p>c) The Agency disagrees with the generalized comment to discontinue an accrual estimation process based on historical data. The Agency believes that our methodology to estimate accruals is sound and is based on historic trends. We will engage with the IBAN to evaluate other best practice methodologies for possible implementation within NSPA.</p> <p>d) The Agency will look into this further.</p>   |                                   |
| 13  | <p><b>Recommendation 4 (para 4.5)</b></p> <p>The Board recommends that NSPA:</p> <p>a) Ensure a systematic electronic filling of evidence received and used to validate the date of the receipt of goods and services into the accounting system.</p>  | <p>a) The current practice of extracting data from the Agency's Enterprise Resource Planning (ERP) system and issuing that information via electronic mail to programs for validation will continue for the foreseeable future. Although this process is not fully automated in SAP, there is no cost-effective method by which the Agency can verify the receipt of goods and services at a myriad of locations (often the customers' sites).</p> <p>The IBAN has been invited to review the efficacy of the current process.</p> | In-progress                       |

| No. | OBSERVATION / RECOMMENDATION   | NSPA MANAGEMENT COMMENT   | INTERNAL STATUS OF RECOMMENDATION |
|-----|--|---|-----------------------------------|
| 14  | <p><b>Recommendation 5 (para 5.4)</b></p> <p>The Board recommends that NSPA:</p> <ul style="list-style-type: none"> <li>a) Develop, in coordination with ACO, a common approach with appropriate references to ensure efficient and effective confirmation and reconciliation of transactions and positions.</li> <li>b) Perform, with ACO, a reconciliation at least twice a year.</li> </ul> | <ul style="list-style-type: none"> <li>a) The Agency is currently working with ACO to improve the process through the addition of common data elements to allow for reconciliation at the customer level, which is what NSPA uses for tracking at the transaction level.</li> <li>b) The Agency has conducted the first reconciliation process for 2017.</li> </ul>                           | In-progress                       |
| 15  | <p><b>Recommendation 6 (para 6.11)</b></p> <p>The Board recommends that NSPA:</p> <ul style="list-style-type: none"> <li>a) Liaise with Nations to determine the preferred way to return the EUR 67 million of credits above that are not backed by financial commitments to the Nations, either through reimbursement or reductions in future calls for contributions.</li> </ul>             | <ul style="list-style-type: none"> <li>a) Projects are closed by Support Partnerships or other relevant governing bodies as and when they determine. Any remaining funds are credited to the customers and are available for their use, as they indicate to the Agency.</li> </ul> <p>The Agency will provide extra disclosures in the 2017 financial statements to explain this process.</p> | In-progress                       |
|     | <ul style="list-style-type: none"> <li>b) Set up procedures to close projects that have no activity and reimburse the funds to the Nations.</li> <li>c) Ensure the appropriate use of credits that are held for over 5 years.</li> </ul>   | <ul style="list-style-type: none"> <li>b) Monthly financial situation reports are issued to all customers. Customers indicate to the Agency how they wish to use their funds.</li> <li>c) The Agency has conducted the first reconciliation process for 2017.</li> </ul>  |                                   |

| No. | OBSERVATION / RECOMMENDATION  | NSPA MANAGEMENT COMMENT   | INTERNAL STATUS OF RECOMMENDATION |
|-----|---|---|-----------------------------------|
| 16  | <p><b>Recommendation 6 (para 6.12)</b></p> <p>The Board recommends that the CEPS Programme:</p> <ul style="list-style-type: none"> <li>a) Provides an estimate of non-appropriated military and non-military revenue when preparing the annual budget, and that this be documented and supported by a robust estimation methodology.</li> <li>b) Restricts currency holdings to the minimum required to meet forecast payments prior to receipt of the following contribution instalment.</li> <li>c) Requests that the National Organisation to use a separate bank account for NATO funded activities. The Board should be able to request an independent confirmation to this bank.</li> </ul> | <ul style="list-style-type: none"> <li>a) The CEPS Programme Board noted the increasing available cash at the end of 2015 as reported in the CEPS Financial Statements. Therefore, the CEPS Programme Board decided in 2016 to estimate more accurately the non-military revenues with effect from 2017 onwards.</li> <li>b) The CEPS Programme Board decided to reduce the yearly contributions by more than 4 MEUR per annum with an impact on 2018 and the four following years. When preparing future budgets, CEPS will be vigilant on the current trend to adjust the future expected revenues to the best available estimates.</li> <li>c) The CEPS Programme Office is in discussion with National Organisations on how to achieve this.</li> </ul> | <p><b>In-progress</b></p>         |

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|-----|--|--|-----------------------------------|
| 17  | <p><b>Recommendation 7 (para 7.5)</b></p> <p>The Board recommends NSPO to reinforce the controls over access rights and segregation of duties within the ERP by filling in the vacant position, updating the SoD Matrix, implementing the Governance Risk Compliance module within the accounting system and ensuring that regular SAA WG meetings are held.</p> | <p>While the Segregation of Duties (SoD) Matrix has not been finalized, access rights by post are reviewed by a number of personnel across different directorates and divisions to ensure that there are no conflicts of interest before new or revised roles are authorized.</p> <p>NSPA currently lacks the resources to dedicate to the full scope of the Governance, Risk and Compliance (GRC) tool within the Agency's ERP, but believes its current processes provide a reasonable assurance that violations of SoD are not occurring.</p> <p>The IBAN will review the current process during its audit of the 2017 Financial Statements to assess if it considers the current process to provide adequate controls.</p> | In-progress                       |
|     | 2015 NSPO Audit Report   |  |                                   |
| 18  | <p><b>Recommendation 1(a)</b></p> <p>Internal control activities be developed to ensure appropriate second level control for improved quality using reasonableness checks before the final issuance of the NSPO Financial Statements.</p>  | <p>While there was improved "second level control" over the production of the financial statements in 2016, there were still some errors.</p> <p>The Agency will continue to work on improving the quality of its financial statements.</p>  | Open                              |

| No. | OBSERVATION / RECOMMENDATION   | NSPA MANAGEMENT COMMENT  | INTERNAL STATUS OF RECOMMENDATION |
|-----|--|--|-----------------------------------|
| 19  | <p><b>Recommendation 1(b)</b></p> <p>As a follow up of the observation 1.3 of the audit report on the 2014 NSPO Financial Statements, the Board reiterates its recommendation to prepare a detailed accounting manual where common chart of accounts, accounting policies, accounting estimates, the intercompany reconciliation process, timelines, and details of journal entries booked at both the segment and central levels are detailed.</p> <p>This should also detail the information to be requested from the segments in order to ensure a proper combination into NSPO, such as segment cash flow information.</p> | <p>While the Agency has in place a detailed plan to produce the financial statements, each task is currently not documented in detail.</p> <p>The Agency is currently in the process of recruiting a staff member whose post will include implementing this recommendation; implementation will commence when the post is filled.</p>  | Open                              |
| 20  | <p><b>Recommendation 1(d)</b></p> <p>In order to ensure a better control environment over open positions and accruals, NSPO develops documented procedures to ensure a comprehensive and reliable reconciliation process for all balances and activities with NATO bodies. The results should be monitored and controlled at a central level.</p>  | <p>The Finance Division has been working to reconcile open positions between NSPA and other NATO bodies. NSPA sent confirmation letters to all NATO bodies, but received limited responses. NSPA works directly with ACO through an agreed procedure to reconcile open accounts payables, accounts receivables and purchase orders.</p> <p>This task has proved extremely difficult in practice because different NATO bodies account for information in different ways and some NATO bodies have not proved able to validate NSPA customer account figures.</p> | In-progress                       |



| No. | OBSERVATION / RECOMMENDATION   | NSPA MANAGEMENT COMMENT   | INTERNAL STATUS OF RECOMMENDATION |
|-----|--|---|-----------------------------------|
| 21  | <p><b>Recommendation 1(e)</b></p> <p>The NSPA Director of Finance ensure that all legal issues are reported and communicated by all directorates to the NSPA legal advisor if any, as part of his new responsibilities under the art. 12 of the NFRs.</p>  | <p>The Financial Controller issued an Operating Instruction in late 2016 to deal with this issue. However, the Agency was unable to implement all of the requirements of the Operating Instruction in time for the production of the 2016 Financial Statements. Full implementation is envisaged for the 2017 Financial Statements.</p> | <p><b>In-progress</b></p>         |
| 22  | <p><b>Recommendation 1(h)</b></p> <p>Information, including open positions at 31 December, between NSPA and other NATO bodies be fully confirmed and reconciled. This process should be monitored and controlled at a centralised level.</p>   | <p>Please refer to No 20.</p>   | <p><b>In-progress</b></p>         |
| 23  | <p><b>Recommendation 4(b)</b></p> <p>The Competition Advocate, in protecting the interests of NSPA, monitor and control the risks related to potential conflict of interests among staff, including contractors, consultants, and technical experts that are involved in the procurement process and develop procedures which take in to account the following criteria (as best practices).</p> <ul style="list-style-type: none"> <li>Establishing clear and objective criteria for assessment of declarations of interest and applying them consistently.</li> <li>Ensure affidavits on independence are signed by all stakeholders before the signature of contracts.</li> </ul> | <p>Human Resource related issues will be addressed through a future internal Operating Instruction on the NSPA Code of Conduct.</p> <p>The Competition Advocate is drafting an internal Operating Instruction on the use of affidavits on independence.</p>   | <p><b>In-progress</b></p>         |

| No. | OBSERVATION / RECOMMENDATION   | NSPA MANAGEMENT COMMENT   | INTERNAL STATUS OF RECOMMENDATION |
|-----|--|---|-----------------------------------|
|     | <ul style="list-style-type: none"> <li>Ensuring comprehensive and compulsory training on conflict of interest.</li> <li>Addressing and monitoring post-employment related risks by including cool down periods and non-competition clauses for all actors involved in the award of a contract.</li> <li>Use of whistle-blower procedures.</li> </ul> | <p>The Competition Advocate has provided training to Procurement Division staff on conflicts of interest and this will be repeated on an annual basis. Human Resources are investigating including appropriate training as part of the Common Interest Training for all NSPA employees.</p>   |                                   |
| 24  | <p><b>Recommendation 4(e)</b></p> <p>In relation to Articles 3 and 32 of the revised NFRs, and ensuring the segregation of functions between the Directors of Finance and Procurement, that the Director of Finance (or delegate) ensure that the appropriate funding and procurement procedures have been followed before contracts are signed.</p> | <p>The NSPO Financial Rules and Procedures clearly delineate the respective roles of the Financial Controller and the Director of Procurement in the area of procurement.</p> <p>The Financial Controller will ensure that the appropriate funding procedures have been followed, and the Director of Procurement will ensure that the appropriate procurement procedures have been followed.</p> <p>This view has been endorsed by the North Atlantic Council through its endorsement of the NSPO Financial Rules and Procedures.</p> <p>The status remains “in progress” until fully implemented.</p> | <p><b>In-progress</b></p>         |

| No. | OBSERVATION / RECOMMENDATION   | NSPA MANAGEMENT COMMENT   | INTERNAL STATUS OF RECOMMENDATION |
|-----|--|---|-----------------------------------|
| 25  | <p><b>Recommendation 4(f)</b></p> <p>The Director of Finance also chair the Contracts Awards Committee when he or she, based on his /her assessment of risks, deems necessary and as allowed under the revised NFRs.</p>   | <p>Procedure XXXII of the NSPO Financial Rules and Procedures acknowledges that the Director of Procurement will normally chair the Contracts Award Committee for amounts greater than 2.5 x Financial Level E (i.e. 2 MEUR).</p> <p>Rule 32 retains the NFR requirement that the Financial Controller may chair the Contracts Award Committee.</p> <p>The NSPO Financial Rules and Procedures have been endorsed by the North Atlantic Council.</p>  | Closed                            |
| 26  | <p><b>Recommendation 5</b></p> <p>The Board recommends NSPA to ensure that prepayments to vendors are identified as such in SAP and that their use is properly monitored and controlled by using the prepayments module to limit the risk of overpayment or improper accounting treatment.</p> | <p>The Agency has decided not to use the prepayment module because it believes it has a controlled process in place.</p> <p>The Finance Division ensures that purchase orders which require prepayments are flagged in the system which makes them easy to monitor. In addition, the continued validity of prepayments is checked with procurement.</p> <p>The IBAN will review the current process during its audit of the 2017 Financial Statements to assess if it considers that the current process provides adequate control.</p> | In-progress                       |

| No. | OBSERVATION / RECOMMENDATION  | NSPA MANAGEMENT COMMENT   | INTERNAL STATUS OF RECOMMENDATION |
|-----|---|---|-----------------------------------|
| 27  | <p><b>Recommendation 6(c)</b></p> <p>NSPA proactively coordinate with customers to use available customer advances that aren't legally committed for another purpose to fund re-billings before sending additional invoices for payment to the customers.</p> | <p>The Agency considers that it closely coordinates with its customers on the uses of the customers' advances.</p> <p>When allowed by the customer and documented in writing, the Agency will offset the rebilled invoices against the customer advances.</p> <p>Without specific agreement from the customer, the Agency is not in a position to automatically offset amounts due from customers with amounts held for the customers by the Agency.</p> <p>The Agency will provide clarification of this in the supporting notes to the 2017 Financial Statements.</p> | In-progress                       |
| 28  | <p><b>Recommendation 6(d)</b></p> <p>NSPA ensure that, for accounting presentation purposes, customer advances are being properly net from billed and unbilled receivables as appropriate.</p>  | <p>The Agency believes that it accounts in accordance with the NATO Accounting Framework in this area; however, it shall review whether the accounting presentation recommended by the IBAN can be met.</p>   | In-progress                       |
| 29  | <p><b>Recommendation 7(a)</b></p> <p>LN and the other NSPO programmes identify all candidates for closure and release the reserved funds back to the customers and Nations.</p>   | <p>The LN programme has made a concerted effort to reduce the value of open commitments. The closure of fund reservations, where LN is the only programme to use them, is no longer a manual process but fully automated now in the system.</p>   | Closed                            |

| No. | OBSERVATION / RECOMMENDATION   | NSPA MANAGEMENT COMMENT  | INTERNAL STATUS OF RECOMMENDATION |
|-----|--|--|-----------------------------------|
|     |  | In respect of the release of reserved funds back to the customers, it is the Agency's view is that it is for its customers to decide whether their cash holdings at the Agency are reasonable for their purposes.  |                                   |
| 30  | <b>Recommendation 7(c)</b><br>The programmes follow a stricter policy on cash holdings and relate them to current and future legal commitments. They should contact the customers and Nations to identify any cash balances in excess of these commitments and reduce them via returns to the customers and Nations or a reduction in future calls or invoicing. | The North Atlantic Council has endorsed the NSPO Financial Rules and Procedures which reflect the Agency's and the Nation's view on cash holdings.   | Closed                            |
| 31  | <b>Recommendation 7(d)</b><br>NAM programme continue budget related measures to reduce the calls and that a documented action plan be put in place to reduce the amount of cash held on behalf of Nations. This should include a return to the Nations of any unused and uncommitted funds remaining in the Acquisition budget.                                  | The North Atlantic Council has endorsed the NSPO Financial Rules and Procedures, which reflect the Agency's and the Nation's view on cash holdings.<br><br>The NAM Programme has in place a plan to reduce cash balances.  | Closed                            |
| 32  | <b>Recommendation 7(e)</b><br>NSPA return the customer and replenishment credits to the customers and Nations. This would include for the CEPS programme, where such credits equals approximately 7 years of the budgetary contributions needed to fund operations based on the current level of military and non-military revenues.                             | The North Atlantic Council has endorsed the NSPO Financial Rules and Procedures, which reflect the Agency's and the Nation's view on cash holdings.<br><br>The CEPS Programme Board has put in place plans to reduce cash balances (refer to comments on No 16) which will reduce future calls to nations. | Closed                            |

| No. | OBSERVATION / RECOMMENDATION   | NSPA MANAGEMENT COMMENT   | INTERNAL STATUS OF RECOMMENDATION |
|-----|--|---|-----------------------------------|
| 33  | <p><b>Recommendation 7(f)</b> [shown in report under 7.8]</p> <p>The Board also recommends that the National Organisations in Germany and France create and use a bank account that is specifically for the NATO related activities only, and that the National Organisation in Belgium ensures that monthly cash reconciliations are performed and documented, and if possible, request to create and use a bank account that is not a direct account at the Ministry of Finance.</p> | <p>The Agency is discussing the issue with the respective National Organisations.</p>   | <p><b>In-progress</b></p>         |
|     | <p><b>2014 NSPO Audit Report</b></p>   |   |                                   |
| 34  | <p><b>Section 1.13</b></p> <p>The Board reiterates its recommendation that NSPA develop a detailed, written accounting manual that includes details of the consolidation process such as timelines, inter-segment account reconciliation and specific consolidation entries.</p>   | <p>Please refer to No 19.</p>   | <p><b>Open</b></p>                |
| 35  | <p><b>Section 8.3</b></p> <p>The Board recommends that NSPA implements appropriate procedures to ensure that any [..inventory..] differences observed during the reconciliation process between the confirmations received from the national depots or contractors and the figures reported by NSPA are resolved in a timely manner and are accurately reported to both the third party owners and in the notes to the financial statements.</p>                                       | <p>The Agency contacts third parties, including National Depot Commanders, at the year-end to confirm inventory holdings and performs a number of inventory audits each year.</p> <p>The Agency does not consider it has the ability to take this recommendation any further and therefore considers it closed.</p> | <p><b>Closed</b></p>              |

| No. | OBSERVATION / RECOMMENDATION   | NSPA MANAGEMENT COMMENT  | INTERNAL STATUS OF RECOMMENDATION |
|-----|--|--|-----------------------------------|
|     |  | <p>If this recommendation is not considered closed by the IBAN after its next audit, the Agency will consider escalating the matter to the ASB for resolution.</p>   |                                   |
| 36  | <p><b>Section 10.8</b></p> <p>The Board recommends that NSPO allocate the unallocated customer credits as soon as possible and return this excess cash to nations. In the future, such an allocation should be performed more timely. It should be done before the issuance of the financial statements.</p> | <p>The allocation of unallocated customer credits can be complicated and resource intensive (e.g. the allocation of interest earned). While the Agency is committed to doing this in as timely a way as possible, it is not currently foreseen that this can be done before the issuance of the financial statements because key personnel involved in allocating credits are also supporting the preparation of the financial statements.</p> <p>In addition, excess cash would only be returned to customers on their instruction.</p> | <p><b>In-progress</b></p>         |

|    | 2011 NAMSO Audit Report  |  |             |
|----|--|--|-------------|
| 37 | <p><b>Section 5.3</b></p> <p>The Board recommends that the NSPA analyses the existing situation [...in respect of apportioning costs on project dissolution...] especially for the activities supported by a limited number of Nations or by non-NATO Nations to make sure that at all times members supporting NSPA activities clearly understand the potential future liabilities.</p> | <p>This is addressed through Procedure XIX (13) d) of the NSPO Financial Rules and Procedures, which requires that,</p> <p><i>“Liabilities stemming from the closure of a project (including personnel costs for direct and indirect manpower as well as indemnities for loss of job or any other administrative and operating expenditure) shall be charged to the members of the project at the time of its closure in accordance with the cost allocation procedures outlined in paras a) to c). This follows the NATO principle that ‘costs lie where they fall’.”</i></p> | Closed      |
|    | 2008 CEPMO Audit Report  |  |             |
| 38 | <p><b>Section 5.6</b></p> <p>FBG [...the German National Organisation...] should determine the cause of the plug account. Additionally, a separate set of books for the international activities should be created in SAP and should be used to process the international FBG transactions.</p>  | <p>It is anticipated that this long-standing issue will be resolved before the issuance of the NSPO Financial Statements 2017.</p>   | In progress |



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**ANNEX 1**

**Summary Note for Council  
by the International Board of Auditors for NATO (Board)  
on the audit of the Financial Statements of the  
NATO Support and Procurement Organisation (NSPO)  
for the year ended 31 December 2016**

NSPO consists of the NATO Support and Procurement Agency (NSPA) and its governance structure. The mission of NSPA is to provide responsive, effective and cost-efficient acquisition, including armaments procurement; logistics; operational and systems support and services to NATO Member States, NATO Military Authorities and partner nations. In 2016, NSPO generated revenues of EUR 2.42 billion and incurred expenses of EUR 2.46 billion.

The Board audited the 2016 NSPO Financial Statements and issued a qualified opinion on the financial statements and on compliance.

During the audit, the Board made seven observations with recommendations which are summarised below:

One observation impacts the audit opinion on the financial statements and on compliance:

1. Material weaknesses in internal control over financial reporting.

The remaining six observations do not impact the audit opinions:

2. Efforts to achieve compliance with the NATO Financial Regulations, particularly those articles on Internal Control, Risk Management and Internal Audit.
3. Structural weakening in the position of Internal Audit.
4. Accrual estimates within NSPO are to be improved.
5. Weaknesses in the reconciliation and reporting of inter-NATO entities.
6. Weaknesses in cash control and management.
7. Weaknesses in IT general computer controls.

The Board also included in its audit opinion, without further modifying its opinion, other matters paragraph highlighting to the reader of some limitations of sufficient and appropriate evidence for the reporting by the Central Europe Pipeline System (CEPS) National Organisations.

The Board followed up on the status of observations and recommendations from previous years' audits. The observations and their status are summarised in the appendix. The Board noted that twelve of the observations have been settled, five have been superseded by a current year observation, twenty remain outstanding, and one is partially settled. Despite efforts made by NSPA to implement the recommendations and the ASB's interest in the status of implementation, there are still a very high number of observations that remain outstanding. The Board is not satisfied with this, and expects more progress to be made on these superseded and outstanding observations in the future.

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**ANNEX 1**

The Board issued a Management Letter (reference IBA-AML(2017)09) to NSPA management with five observations for management's attention. The Board also notes that a very high number of recommendations from prior year management letters remain outstanding, including some that have been outstanding for many years.

The Auditor's Report and the Letter of Observations and Recommendations were issued to NSPA whose comments have been included, with the Board's position on those comments where necessary, see the Appendix to Annex 3.

The Agency Supervisory Board did not endorse the agency's comments on the IBAN Auditor's Report and Letter of Observations and Recommendations.

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25 August 2017

**INTERNATIONAL BOARD OF AUDITORS FOR NATO**

**AUDITOR'S REPORT ON THE FINANCIAL STATEMENTS OF THE**

**NATO SUPPORT AND PROCUREMENT ORGANISATION**

**(NSPO)**

**FOR THE YEAR ENDED 31 DECEMBER 2016**

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**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 Support and Procurement Organisation (NSPO), which comprised the Statement of Financial Position as at 31 December 2016, the Statement of Financial Performance, the Statement of Changes in Net Assets and the Statement of Cash Flows for the year then ended, and Notes to the Financial Statements, including a Statement of Accounting Policies. The Board also audited the NSPO Financial Plan Execution Statements included as an annex to the financial statements.

*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.

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*Basis for Qualified Opinion on the Financial Statements*

Foreign Military Sales (FMS) prepayments (asset) and related liabilities are overstated by USD 58 million. FMS goods and services procured from the United States Government are funded in advance, meaning that there should not be a liability recorded when receiving a billing for such goods and services as there is no expected future outflow of economic resources since the payment was already made.

The financial statements report CEPS pipeline assets in progress. For the portion related to the German National Organisation, which is reported at EUR 14.6 million, no sufficient and appropriate evidence could be provided to the Board to support the amount reported. The full extent of the impact is not known due to the scope limitation.

Also, the financial statements do not include comparative information with respect to the Statement of Change in Net Assets, Note 3 Property, Plant and Equipment (PP&E), and Note 4 Intangible Assets and inter-business segment eliminations.

*Qualified Opinion on the Financial Statements*

In our opinion, except for the effects and possible effects of the matters described in the Basis for Qualified Opinion on the Financial Statements paragraph, the financial statements present fairly, in all material respects, the financial position of NSPO as of 31 December 2015, and of its financial performance and its cash flows for the year then ended are in accordance with the NATO Accounting Framework.

*Other Matters*

EUR 46.3 million of the CEPS pipeline system reported as an asset is in France. A private company maintains this portion of the CEPS pipeline system on behalf of the French National Organisation, which is part of NSPO. In accordance with an agreement signed between the two parties, the National Organisation should perform a control on the information provided by the private company. However, the Board found that this control was not being fully performed, resulting in inaccurate reporting of the pipeline assets. The Board's opinion is not modified as a result of this matter.

EUR 0.8 million of cash is reported as being held for NSPO by the French and German CEPS National Organisations, which are part of NSPO. The Board draws the attention of the reader to the limitation of obtaining sufficient and appropriate third party evidence on the separate cash positions of these National Organisations because common bank accounts are used by them for their both their NATO and non-NATO activities. The Board's opinion is not modified as a result of this matter.

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**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.

*Basis for Qualified Opinion on Compliance*

The NATO Financial Regulations require the establishment of a system of internal control. The Board found material weaknesses in internal control over financial reporting at NSPO. Material misstatements and other errors and omissions were identified by the Board during the audit which had not been prevented and detected by internal controls over financial reporting.

*Opinion on Compliance*

In our opinion, except for the matter described above in the Basis for Qualified Opinion on Compliance paragraph, 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, 25 August 2017



Hervé-Adrien Metzger  
Chairman

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25 August 2017

**INTERNATIONAL BOARD OF AUDITORS FOR NATO**

**LETTER OF OBSERVATIONS AND RECOMMENDATIONS**

**FOR THE NATO SUPPORT AND PROCUREMENT ORGANISATION**

**(NSPO)**

**FOR THE YEAR ENDED 31 DECEMBER 2016**

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**Introduction**

The International Board of Auditors for NATO (Board) audited the NATO Support and Procurement Organisation (NSPO) Financial Statements for the year ended 31 December 2016, and issued a qualified opinion on the financial statements and a qualified opinion on compliance. The reasons for the qualified opinion, as well as other observations and recommendations, are summarised in the Observations and Recommendations section below.

**Observations and Recommendations:**

One observation impacts the audit opinion on the financial statements and on compliance:

1. Material weaknesses in internal control over financial reporting.

The remaining six observations do not impact the audit opinions:

2. Efforts to achieve compliance with the NATO Financial Regulations, particularly those articles on Internal Control, Risk Management and Internal Audit.
3. Structural weakening in the position of Internal Audit.
4. Accrual estimates within NSPO are to be improved.
5. Weaknesses in the reconciliation and reporting of inter-NATO entities.
6. Weaknesses in cash control and management.
7. Weaknesses in IT general computer controls.

The Board also included in its audit opinion, without further modifying its opinion, other matters paragraph highlighting to the reader of some limitations of sufficient and appropriate evidence for the reporting by the Central Europe Pipeline System (CEPS) National Organisations.

The Board followed up on the status of observations and recommendations from previous years' audits. The observations and their status are summarised in the appendix. The Board noted that twelve of the observations have been settled, five have been superseded by a current year observation, twenty remain outstanding, and one is partially settled. The Board expects more progress to be made on these superseded and outstanding observations in the future.

The Board also issued a Management Letter (reference IBA-AML(2017)09) to NSPA management with 5 observations for management's attention.

This Letter of Observations and Recommendations was formally cleared with NSPA, and the formal comments are included, with the Board's position on those comments where necessary, see Appendix (Annex 3).

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**OBSERVATIONS AND RECOMMENDATIONS**

**1. MATERIAL WEAKNESSES IN INTERNAL CONTROL OVER FINANCIAL REPORTING**

**Reasoning**

1.1 The NATO Financial Regulations (NFRs) require the Financial Controller (FC) to exercise the responsibility of budgeting, accounting and reporting activities of the NATO entity. This includes being responsible for the financial internal control system established, and for the preparation of the financial statements in accordance with the NATO Accounting Framework.

**Observations**

1.2 The Board found that there has been much improvement in the preparation of the 2016 NSPO Financial Statements compared with previous year. Specifically, the following improvements were notable:

- The NATO Airlift Management Programme (NAMP) financial reporting is more understandable and thoroughly supported, and with an appropriate process of combining the NAMP balances and activities into the NSPO Financial Statements.
- Significant efforts and important progress made in 2016 to record, for the first time, the CEPS related pipeline assets as from 1 January 2013 in accordance with the NATO Accounting Framework. The net book value of such assets is approximately EUR 120 million, including almost EUR 50 million of assets in progress.
- The issuance of an Operating Instruction to increase the control of FC over the reporting of provisions and contingent liabilities.
- Improved support for the Cash Flow Statement, which was prepared using the direct method.
- A decrease in number of miscellaneous errors which led to the issuance of several versions of the 2015 Financial Statements during the Board's audit.

1.3 Nevertheless, while important progress was made, the Board still identified a number of material and other issues in the 2016 Financial Statements. These are as follows:

Foreign Military Sales (FMS) related liabilities recorded when a prepayment had already been paid

1.4 The Board found a material overstatement of FMS prepaid expenses (asset) and related liabilities in the amount of USD 58 million. FMS goods and services procured from the United States Government are funded in advance, meaning that there should not be a liability recorded when receiving a billing for such goods and services as there is no expected future outflow of economic resources (i.e. payment was already made).

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This will ensure that the same FMS expenditure is not being reported as both a prepaid expense (asset) and as an expense. This was also reported in the prior year audit.

Comparative balances not fully presented

1.5 The NATO Accounting Framework requires that comparative balances be presented in the financial statements. The Board found that there were no comparative balances presented for the Statement of Changes in Net Assets, Note 3 Property, Plant and Equipment, Note 4 Intangible Assets and the inter-business unit eliminations included in the Statement of Financial Position, Statement of Financial Performance and Note 12.

Reporting of the CEPS pipeline assets

1.6 Despite the efforts made to record these assets for the first time. Some improvements in the process of reporting these pipeline assets can be made in the following areas:

- The methodology used by the German National Organisation to measure assets in progress is different compared with the other National Organisations. It is based on an estimate of percentage of progress for each project whereas the others were able to base it on invoice received. The Board found that there was not sufficient and appropriate documented audit evidence to support these asset in progress estimates. The weakness remains systemic at this location, but due to the scope limitation noted, the correct amount is not known.
- An agreement between the French National Organisation and the private company that maintains the CEPS pipeline located in France on behalf of it states that all information prepared by the private company shall be reviewed by the National Organisation before being provided to the Board for audit. However, the Board found systematic differences between the information provided by the National Organisation to the Board and the information provided directly by the private company to CEPS on the valuation of the pipeline assets. The weakness remains systemic at this location, but the current year impact of these differences is not material.
- As part of the elements of costs (IPSAS 17 paragraph 30), the Board found that NSPO was not yet able to include an estimate of the costs of dismantling, removing and restoring the site to its original conditions.

No assessment of Customer Advances to determine whether current or non-current

1.7 The Board found that no assessment of the EUR 3.3 billion of Customer Advances reported as current liabilities in the Statement of Financial Position was made to determine whether they were current or non-current liabilities. As a result, NSPA did not provide the Board with assurance that all Customer Advances should be reported as current liabilities.

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Lack of evidence that a payable to French tax authorities remains a liability

1.8 The Board did not obtain sufficient and appropriate evidence to support that a EUR 8 million payable for French taxes reported by CEPS and disclosed in Note 8 of the NSPO Financial Statements remains a liability. Legal discussions with the French tax authorities have been stopped since 2009.

Completeness and control over related party declarations

1.9 The NATO Accounting Framework requires the disclosure of related parties and related party transactions. Note 14 of NSPO Financial Statements discusses related parties. Related party declarations were asked from various NSPA employees and governing body members. The Board found that some governing body members did not reply to this request. The Board was informed by NSPA that no further investigation was performed.

Disclosing of CEPS revenue from different sources

1.10 The Board found that the NSPO Financial Statements do not separately disclose the CEPS funding coming from military and non-military operational activities from those coming from budget appropriations from the nations. The Board's opinion is that this information is relevant to an understanding of the entity, and should be presented in accordance with the NATO Accounting Framework, specifically paragraph 106 of IPSAS 1.

Inaccuracies and errors identified in the 2016 NSPO Financial Statements

1.11 The Board found numerous inaccuracies and errors in the 2016 NSPO Financial Statements that had not been corrected before the issuance of the financial statements:

- There is no accounting policy disclosed for receivables.
- The deficit reported in the Statement of Changes in Net Assets for Log Ops does not reconcile with the amount reported in the Statement of Financial Performance (EUR 2,919 million vs EUR 5,066 million). The Board notes that a note at the bottom of the Statement of Changes in Net Assets states that much of the difference is due to a bad debt provision which does not impact Net Assets. Provisions increasing the net deficit should also reduce net assets, so there appears to be an accounting inconsistency.
- The Cash Flow Statement includes an understatement of cash from investing activities for EUR 1.9 million related to the purchase of PP&E.
- Note 3 on PP&E discloses information on a restatement of the opening balances in respect to the CEPS Pipeline System, but the amounts presented are not reconcilable to the PP&E movement schedule presented in the note.
- Note 4 on Intangible Assets is incomplete as it includes two amounts stated as 'Euro XX million'

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- In Note 8 on Accounts Payable and Accruals, the Other line item is understated by the netting of receivables related to Fuel Management surcharge and repair for EUR 4.6 million (EUR 4.3 million in 2015).
- In Note 13 on Employee Disclosures, there is a mathematical error in the NSPO total personnel number, disclosing 3,953 instead of 1,937. In addition, there is a mapping error related to the French National Organisation healthcare/pension contribution with an impact of EUR 8.2 million. Also, the 2015 original figures presented could not be fully reconciled with the latest version of the 2015 Financial Statements.
- Note 22 on Non-NSPA controlled inventories managed on behalf of third parties reports EUR 335 million such inventory managed for NATO bodies. However, this number doesn't include AWACS and SOC Taranto inventory that is managed by NSPA on behalf of ACO.
- Note 23 on Restatements of 2015 Financial Statements due to the correction of prior-period errors does not disclose the impact of the change in accounting policies and correction of errors in the Statement of Changes in Net Assets.
- Annex 1 Log Ops Business Unit – Administrative costs elements – incorrectly presents the 2016 authorized credits and lapsed credits as the transfers made throughout the year were not considered; however, the total is presented correctly.
- Annex 2 Log Ops Business Unit – Jointly and Commonly Funded Operational Projects include an overstatement in the MMF-MULT MRTT Fleet unused credits in amount of EUR 19.5 million and understated commitments made in 2016 for the same amount.

**Recommendations**

1.12 Referring to the reporting of FMS balances, the Board recommends that:

- a) FMS expenses incurred (including accruals) be netted from FMS prepayments (asset) rather than being recorded as a liability. This principle should also apply to non-FMS activities when the prepayment is for a specific good or service and those specific goods or services are received (including accruals).
- b) The notes to the financial statements define more specifically what is meant by “modified cash basis” when recording FMS activities.

1.13 Referring to PPE reporting, the Board recommends that:

- a) CEPS Programme Board ensure that sufficient and relevant control procedures are performed by the German National Organisation to ensure that there is a well-documented assessment of pipeline assets in progress.
- b) CEPS Programme Board liaise with the French National Organisation and its private company service provider to ensure that appropriate and up to date control is being performed by the National Organisation.
- c) NSPO Financial Statements record the estimate of dismantling, removing and restoring costs related to the pipeline assets or disclose why an assessment of the costs is not possible.

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1.14 The Board recommends NSPA to determine which Customer Advances are current and which are non-current, and present them appropriately in the Statement of Financial Position. This could impact the audit opinion in the future if this is not carried out.

1.15 The Board recommends NSPA to liaise with the French tax administration to be able to support why this liability still exists.

1.16 The Board recommends that NSPO take appropriate follow-up actions when requests for declarations of related parties are not answered.

1.17 The Board recommends that the NSPO Financial Statements separately disclose CEPS military and non-military operational activities from those coming from budget appropriations from the CEPS nations.

1.18 Referring to the inaccuracies and errors identified in the reporting, the Board recommends that:

- a) NSPA ensure a presentation of the financial statements that is compliant with the requirements of the NATO Accounting Framework.
- b) Sufficient and appropriate procedures be set-up to avoid the risk of errors in the Financial Statements and to be in compliance with the NFRs in respect to internal controls.

**2. EFFORTS TO ACHIEVE COMPLIANCE WITH THE NATO FINANCIAL REGULATIONS, PARTICULARLY THOSE ARTICLES ON INTERNAL CONTROL, RISK MANAGEMENT AND INTERNAL AUDIT**

**Reasoning**

2.1 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.”

2.2 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

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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; and Article 25 authorizes the commitment of budgetary credits for goods and services to be rendered during the financial year.

2.3 The revised NFRs provide an opportunity for NATO bodies to solidify and codify their overall internal control frameworks, including risk management. They also provide internal audit functions 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. Importantly they also required a robust control environment in place around the preparation of Financial Statements to ensure the quality and accuracy of the financial information is of the highest standard as it is now publicly available.

**Observations**

2.4 The Board found that NSPO made efforts towards achieving full compliance with all of the revised NFRs, but that more proactive and effective steps are still needed. This result is not unexpected considering that, over two years after the approval of the revised NFRs, the more detailed FRPs, which were required by Article 4 of the revised NFRs, have not yet been approved. Furthermore, these changes to the NFRs are significant, and the Board appreciates that some time is needed to implement them properly. It is expected that doing so will increase the likelihood that the benefits accruing to NSPO will be real, rather than it just being an exercise to demonstrate compliance with the revised NFRs.

2.5 As a result, 2016 continues to be a transition year for NSPO. The Board expects compliance to be achieved in 2017. It has again 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 2016 as a result of these observations.

2.6 The Board reports the status of the following areas:

Article 3 Responsibility and Accountability

2.6.1 The Board found that both the Head of NATO body and the acting Financial Controller signed the 2016 NSPO Financial Statements.

Article 11 Risk Management and Article 12 Internal Control

2.6.2 The Board found that NSPO has not yet adopted an Internal Control Framework, including risk assessment. NSPA reported that risk management pilot programmes were introduced in two LogOps programmes in 2016. Full implementation is not expected until the end of 2018. A number of other NATO bodies, including ACO, ACT, NCIO, NETMA and NAPMA, have adopted COSO (The Committee of Sponsoring Organisations of the Treadway Commission) Framework. The adoption of a specific framework by these

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NATO bodies is an important step forward. It is essential in order to ensure and to clearly demonstrate to others that a complete system of internal control and risk management is in place. Until NSPO adopts a specific internal control framework, and completes its documentation, 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.

2.6.3 Once NSPO adopts a specific Internal Control Framework, the important work of assessing and documenting specific internal control and risk management procedures remains to be completed. The Board expects to see more demonstrative progress on this in the coming year. Such documentation is essential in order to ensure and to clearly demonstrate to others that a complete system of internal control and risk management is in place. Until this assessment and documentation is completed, the Board will not be in a position to state that there is a full system of internal control, including risk management, in place that is in accordance with Articles 11 and 12 of the revised NFRs.

Article 13 Internal Audit

2.6.4 The Board found that NSPO Internal Audit has not yet fully evaluated, 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. Part of the reason for this is that NSPO, as already stated earlier, has not yet documented their internal control and risk management procedures.

2.6.5 The Board understands that the budget of the Internal Audit department will now be common funded and independent from funding from the Programmes and that it has been accepted that they will perform audits of CEPS, including the National Organisations.

2.6.6 The Board found that Internal Audit independence is threatened due to the structure of the Audit Advisory Panel, as stated in observation 3 below.

Article 16 Audit Advisory Panel

2.6.7 Please refer to observation 3 below.

**Recommendations**

2.7 The Board recommends that NSPO:

- a) Choose a specific internal control framework that it will use to assess its system of internal control. Since other NATO entities, including NCIO and ACO, have already adopted COSO as their internal control framework, and it is a framework that can be used by entities of all types, NSPO should consider adopting COSO as their internal control framework.
- b) Assess and document the system of internal control and risk management procedures to support compliance with the NFRs, FRPs and the internal control framework that it chooses.

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- c) Prepare an entity-wide risk management policy throughout the organisation and that risk registers are developed and employed throughout all NSPO segments and operations.
- d) Perform internal audit activities that fully evaluates internal control and risk management throughout NSPO, and that this work be clearly documented so as to be able to conclude as to NSPO's compliance against the NFRs and FRPs.

### **3. STRUCTURAL WEAKENING IN THE POSITION OF THE INTERNAL AUDIT**

#### **Reasoning**

3.1 Article 16 of the revised NFRs requires the establishment of an Audit Advisory Panel which is supposed to gather internal and external audit conclusions for discussion with the Head of NATO body and management boards.

3.2 NSPA Internal Audit has adopted the International Standards for the Professional Practice of Internal Auditing. In accordance with standard 1110 - Organizational Independence, the "Internal audit activity must be free from interference in determining the scope of internal auditing, performing work and communication results". In addition, the organizational independence "is effectively achieved when the chief audit executive reports functionally to the board".

#### **Observations**

3.3 NSPO Operating Instruction 4600-21, issued in October 2016, provides for the input of the General Manager, Directors and Audit Advisory Panel in the internal audit plan. This internal audit plan would be further validated by the General Manager and the Audit Advisory Panel and communicated by the Auditor General to the Audit Committee of the ASB.

3.4 The Board found weakening of the organizational independence of the Internal Audit function with regard to International Standard for the Professional Practice of Internal Auditing 1110 as the audit plan is subject to modification and approval by NSPA management which could lead to conflicts of interest.

#### **Recommendations**

3.5 The Board recommends that the Audit Advisory Panel (as described in Article 16 of the revised NFRs) shall only be a consultative and advisory body with no approval required before the issuance of the Internal Audit plan.

3.6 The Board recommends that the Auditor General report functionally to the General Manager and also have the ability to report directly to the Audit Committee at ASB level.



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**4. ACCRUAL ESTIMATES WITHIN NSPO ARE TO BE IMPROVED**

**Reasoning**

4.1 The NATO Accounting Framework requires the adoption of the accrual basis of accounting. A sound control environment over the identification and reporting of transactions at the year-end is necessary. This includes the identification of goods received and services provided before year-end for which no invoice was received by year-end (i.e., accrued liability).

**Observations**

4.2 The Board found that the reported accruals in the financial statements is based on a process that is heavily manual, with the identification and confirmation of accrual transactions at programme level by non-finance staff.

4.3 The Board also found a EUR 13 million understatement of accrued liabilities at 31 December 2016 that was due to a misunderstanding related to the cancellation of a purchase order for an already delivered item and the re-issuance of the purchase order in the following year.

4.4 Furthermore, the Board found the use of a mark-up of 15% on accrual estimates reported at the end of the cut off period (mid-February) which amounted to EUR 7.6 million. According to NSPA, this estimate is based on prior year information. The Board does not concur with the use of a mark-up methodology that is not supported by estimates of individual receipts of goods and services.

**Recommendations**

4.5 The Board recommends that NSPA:

- a) Improve the control environment over accrual estimates, including training of non-finance staff on how to identify, keep records and communicate transactions of an accrual nature at year-end.
- b) Ensure a systematic electronic filling of evidence received and used to validate the date of the receipt of goods and services into the accounting system.
- c) Discontinue the use of the 15% mark-up methodology by improving the process to ensure that accrual estimates are based on the receipt of goods and services before year-end.
- d) Develop control activities which would prevent the possibility to cancel purchase order for items that have already been delivered.

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**5. WEAKNESSES IN THE RECONCILIATION AND REPORTING OF INTER-NATO ENTITIES**

**Reasoning**

5.1 Referring to a prior year Board observation, the Board recommended that NSPA and ACO should develop an action plan to reach a formal agreement to ensure reliable information be provided in appropriate timeframes.

**Observation**

5.2 The Board also found that the process of confirming and reconciling year-end positions (e.g. inventories, payables, receivables) between ACO and NSPA is cumbersome due to the lack of a common approach or references for reporting and communication issues and has led to errors and the inability to fully reconcile and confirm information with each other.

**Recommendations**

5.3 The Board recommends that NSPA:

- a) Develop, in coordination with ACO, a common approach with appropriate references to ensure efficient and effective confirmation and reconciliation of transactions and positions.
- b) Perform, with ACO, a reconciliation at least twice a year.

**6. WEAKNESSES IN CASH CONTROL AND MANAGEMENT**

**Reasoning**

6.1 NSPO maintains high levels of cash (EUR 2.4 billion at 31 December 2016) while an effective management of cash would ensure that sufficient cash is held at the agency level, and any unused funds would be timely returned to Nations.

6.2 CEPS expenditures are funded by both non-appropriated military and non-military revenue and from budget appropriations. The amount called from budget appropriations is based on taking into account an estimate of non-appropriated military and non-military revenue.

6.3 Bank confirmations from an independent third party bank is a sufficient and appropriate evidence in order to give reasonable assurance on the cash held.

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**Observations**

6.4 The Board found that there was EUR 56.9 million of credits, allocated to specific Nations, of which EUR 47.49 million relates to before 2012 and EUR 31.06 million relates to before 2007, and that these balances are not backed by financial commitments. These relate to bank interests that have been earned and other unused funds. There is also an additional EUR 9 million of credits that have not yet been allocated to a specific Nation and that are also not backed by financial commitments. These also relate to bank interest and other unused funds.

6.5 The Board found that the Statement on Internal Control states that 'While the Agency manages significant sums of money on behalf of its customers, these are controlled and backed by financial commitments.' This statement is misleading in that not all of the money held on behalf of its customers is backed by financial commitments, as shown in the previous paragraph.

6.6 The Board found that the amount of advances received by Nations before 2010 and still not used amounts to EUR 7 million.

6.7 As previously stated in paragraph 1.7, the Board found that no assessment of Customer Advances was made to determine whether they were current or non-current liabilities. As a result, NSPA didn't provide the Board with assurance that all Customer Advances should be reported as current liabilities.

6.8 The Board found that CEPS consistently underestimates the amount of non-appropriated military and non-military revenue when preparing the annual budget, thereby resulting in a higher level of budgetary appropriations needed (calls for contributions to the Nations). For example, the underestimation amounted to EUR 14 million in 2016 (non-appropriated military and non-military revenue amounting to EUR 96 million vs a budget based on such revenue of EUR 82 million). This, in large part, explains why the CEPS Programme has accumulated EUR 167 million of Customer and Replenishment Credits.

6.9 As a follow up of observation 7.6 from the 2015 audit report, the cash balance of the CEPS French National Organisation at year-end is confirmed by the private company providing maintenance services. The accounting is performed by this company and provided to the National Organisation for control. Therefore, the cash position at year-end is not confirmed by an independent third party. The limitation of control over activities and the lack of assurance on the cash position at year-end is not sufficient for IBAN to have a reasonable assurance that the cash position at year-end is true and fair.

6.10 The Board found similar limitations at both the German and Belgian National Organisations.

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**Recommendations**

6.11 The Board recommends that NSPA:

- a) Liaise with Nations to determine the preferred way to return the EUR 67 million of credits above that are not backed by financial commitments to the Nations, either through reimbursement or reductions in future calls for contributions.
- b) Set up procedures to close projects that have no activity and reimburse the funds to the Nations.
- c) Ensure the appropriate use of credits that are held for over 5 years.

6.12 The Board recommends that the CEPS Programme:

- a) Provides an estimate of non-appropriated military and non-military revenue when preparing the annual budget, and that this be documented and supported by a robust estimation methodology.
- b) Restricts currency holdings to the minimum required to meet forecast payments prior to receipt of the following contribution instalment.
- c) Requests that the National Organisation to use a separate bank account for NATO funded activities. The Board should be able to request an independent confirmation to this bank.

**7. WEAKNESSES IN GENERAL COMPUTER CONTROLS**

**Reasoning**

7.1 The NSPO Enterprise Resource Planning (ERP) system requires a sound control environment over the authorized access, software updates and administrators' rights in order to prevent any risk of control breaches. Identified threats of weak control over the ERP are breaches in the segregation of duties, data leaks, reduced reliability on the completeness, valuation, and existence of some operations, all of which may lead to financial reporting errors and possible risks of fraud.

7.2 General computer control related risks should be mitigated as part of the risk assessment, control and monitoring of activities. NSPA control activities over the ERP include the following:

- a) A Segregation of Duties (SoD) Matrix which enables the identification of potential conflicts in the segregation of duties in authorized roles; and
- b) An SAP Access Authorization Working Group (SAA WG) which analyses and corrects the access granted within programs and divisions.

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**Observations**

7.3 The Board found that the identification, monitoring and control over ERP access and risks on breaches of segregation of duties is not satisfactory due to the following issues:

- a) The SoD Matrix is not complete.
- b) The Board did not find any activity of the SAA WG in 2016.
- c) Most of the NSPO divisions and programs still have to review their access rights.
- d) The person in charge of granting and reviewing the access rights in the ERP resigned in January 2017.

7.4 This has been a long-outstanding observation by the Board, with very little action for a number of years now. This lack of action increases the risk of fraud and error within NSPA, which could result in events occurring in the future that lead to modifications of the Board's audit opinion.

**Recommendation**

7.5 The Board recommends NSPO to reinforce the controls over access rights and segregation of duties within the ERP by filling in the vacant position, updating the SoD Matrix, implementing the Governance Risk Compliance module within the accounting system and ensuring that regular SAA WG meetings are held.

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**FOLLOW-UP OF PREVIOUS YEARS' OBSERVATIONS**

The Board followed up on the status of observations and recommendations from previous years' audits. The observations and their status are summarised in this appendix. The Board noted that 12 have been settled, seven have been superseded by a current year observation and 18 remain outstanding.

| OBSERVATION / RECOMMENDATION  | ACTION TAKEN  | STATUS  |
|---|---|---|
| <p><b>NSPO 2015 AUDIT REPORT – ANNEX II IBA-AR(2016)12, SECTION 1</b></p> <p><b>Material weaknesses in internal control over financial reporting</b></p> <p><b>Recommendations</b></p> <p>1.23 a) internal control activities be developed to ensure appropriate second level control for improved quality using reasonableness checks before the final issuance of the NSPO Financial Statements.</p> <p>1.23 b) as a follow up of the observation 1.3 of the audit report on the 2014 NSPO Financial Statements, the Board reiterates its recommendation to prepare a detailed accounting manual where common chart of accounts, accounting policies, accounting estimates, the intercompany reconciliation process, timelines, and details of journal entries booked at both the segment and central levels are detailed. This should also detail the information to be requested from the segments in order to ensure a proper combination into NSPO, such as segment cash flow information.</p> <p>1.23 c) NSPA issue the NSPO Financial Statements to the NSPO Finance Committee at the same time they are issued to the Board for audit, referring to them as “unaudited” at that time. This has been requested by the NSPO Finance Committee during their May 2016 meeting.</p> <p>1.23 d) in order to ensure a better control environment over open positions and accruals, NSPO develops documented procedures to ensure a comprehensive and reliable reconciliation process for all balances and activities with NATO bodies. The results should be monitored and controlled at a central level.</p> | <p>While the Board found some improvements in internal control over financial reporting, it continued to find some weaknesses as noted in observation 2 of the current audit report</p> <p>The Board did not identify progress.</p> <p>This was done for the 2016 financial statements.</p> | <p>Observation <b>Outstanding.</b></p> <p>Observation <b>Outstanding.</b></p> <p>Observation <b>Settled.</b></p> <p>Observation <b>Outstanding.</b></p> |

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| <b>OBSERVATION / RECOMMENDATION</b>  | <b>ACTION TAKEN</b>  | <b>STATUS</b>  |
|--|--|--|
| 1.23 e) the NSPA Director of Finance ensure that all legal issues are reported and communicated by all directorates to the NSPA legal advisor if any, as part of his new responsibilities under the art. 12 of the NFRs.   |  | Observation<br><b>Partially Settled.</b>                           |
| 1.23 f) NSPA fully comply with the requirements of the NATO Accounting Framework in respect to related party disclosures, including making inquiries of governing bodies to ensure the completeness of related party transactions. Key management personnel disclosures should include remuneration and, in the Board's view, should also include NAMP and CEPS Programme Managers and the NSPA Competition Advocate.  | The Board found that some requested related party declarations had not been completed and there was no further follow-up actions taken.  | Observation<br><b>Superseded by current year observation 1.16.</b> |
| 1.23 g) the detailed impact of changes in accounting policies, the correction of errors and reclassification be separately disclosed.  | The Board found improvements were made, although the impact of the correction of errors on the Statement of Changes in Net Assets was not disclosed.   | Observation<br><b>Settled.</b>                                     |
| 1.23 h) information, including open positions at 31 December, between NSPA and other NATO bodies be fully confirmed and reconciled. This process should be monitored and controlled at a centralised level.  | There continued to be unresolved discrepancies.  | Observation<br><b>Outstanding.</b>                                 |
| <b>NSPO 2015 AUDIT REPORT – ANNEX II<br/>IBA-AR(2016)12, SECTION 2</b><br><br><b>Incomplete reporting of assets of the Central Europe Pipeline system (CEPS) programme</b><br><br><b>Recommendation</b><br>2.3 The Board recommends that NSPO continue working ensure that Pipeline System related PP&E can be presented in the 2016 NSPO Financial Statements. This should include ensuring that there are understandable, reliable and consistent recognition criteria for the accounting and presentation of such assets. | The Board found that the CEPS pipeline assets related assets have been reported in the Financial Statements, although some improvements are necessary in the French and German National Organisations. | Observation<br><b>Superseded by current observation 1.13</b>       |

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| <p><b>NSPO 2015 AUDIT REPORT – ANNEX II<br/>IBA-AR(2016)12, SECTION 3</b></p> <p><b>Further steps are required to achieve full compliance with the revised NATO Financial Regulations, particularly those Articles on Internal Control, Risk Management and Internal Audit</b></p> <p><b>Recommendations</b></p> <p>3.8 a) NSPO ensure that its Risk Management Operating Procedure is embedded throughout the organisation. Risk registers should be developed and employed throughout all of the NSPO segments' divisions and operations, and be centralised at the NSPO level.</p> <p>3.8 b) NSPO develops a specific, internationally accepted standards based, Internal Control Framework, and that there be a systematic and detailed documentation of internal control procedures supporting the framework. In the Board's opinion, this should be coordinated to ensure consistent frameworks are adopted across NATO bodies.</p> <p>3.8 c) NSPO ensure that NSPA Internal Audit is fully evaluating risk management and internal control throughout NSPO, and that this work is clearly documented so as to demonstrate compliance against NSPO's chosen Internal Control Framework. Furthermore, NSPO should ensure that the independence of the Internal Audit function is safeguarded, including sufficient funding, and that the Internal Audit plan includes the CEPS Programme as a whole with no restrictions in his scope of work.</p> | <p>NSPA reported to the Board that risk management pilot programmes were introduced in two LogOps programmes in 2016. Full implementation in not expected until the end of 2018.</p> <p>The Board observed that COSO is adopted by ACO, NCIO, NETMA, NAPMA and ACT; NSPO still has not adopted an internal control framework.</p> <p>NSPA Internal Audit has not yet fully evaluated risk management and internal control throughout NSPO.</p> <p>The Board also believes the structure of the Audit Advisory Panel threatens to the independence of Internal Audit.</p> | <p>Observation<br/><b>Superseded by current year observation 2.</b></p>           |
| <p><b>NSPO 2015 AUDIT REPORT – ANNEX II<br/>IBA-AR(2016)12, SECTION 4</b></p> <p><b>Improvements needed in the monitoring and control over potential conflicts of interest in procurement</b></p> <p><b>Recommendations</b></p> <p>4.8 a) the position of the Competition Advocate is put outside the area of influence of procurement to ensure a real independence of the position and fairness in the procurement process</p> <p>4.8 b) the Competition Advocate, in protecting the interests of NSPA, monitor and control the risks related to potential conflict of interests among staff, including contractors, consultants,</p>   | <p>The position of competition advocate will be moved to the another division to better ensure protection of the independence of the competition advocate</p>  | <p>Observation<br/><b>Settled.</b></p> <p>Observation<br/><b>Outstanding.</b></p> |



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|--|---|---|
| <p>and technical experts that are involved in the procurement process and develop procedures which takes in to account the following criteria (as best practices):</p> <ul style="list-style-type: none"> <li>- establishing clear and objective criteria for assessment of declarations of interest and applying them consistently.</li> <li>- ensure affidavits on independence are signed by all stakeholders before the signature of contracts.</li> <li>- ensuring comprehensive and compulsory training on conflict of interest.</li> <li>- addressing and monitoring post-employment related risks by including cool down periods and non-competition clauses for all actors involved in the award of a contract.</li> <li>- use of whistle-blower procedures.</li> </ul> <p>4.8 c) the Competition Advocate keeps records of exceptions in the sourcing and contract terms and conditions</p> <p>4.8 d) the Competition Advocate issues an annual report on its activities to NSPA Senior Management and the Agency Supervisory Board.</p> <p>4.8 e) in relation to Articles 3 and 32 of the revised NFRs, and ensuring the segregation of functions between the Directors of Finance and Procurement, that the Director of Finance (or delegate) ensure that the appropriate funding and procurement procedures have been followed before contracts are signed.</p> <p>4.8 f) the Director of Finance also chairs the Contracts Awards Committee when he or she, based on his/her assessment of risks, deems necessary and as allowed under the revised NFRs.</p> |   | <p>Observation<br/><b>Settled.</b></p> <p>Observation<br/><b>Settled.</b></p> <p>Observation<br/><b>Outstanding.</b></p> <p>Observation<br/><b>Outstanding.</b></p> |
| <p><b>NSPO 2015 AUDIT REPORT – ANNEX II<br/>IBA-AR(2016)12, SECTION 5</b></p> <p><b>Improvement needed in the monitoring and control over prepayments made to vendors</b></p> <p><b>Recommendation</b></p> <p>5.5 The Board recommends NSPA to ensure that prepayments to vendors are identified as such in SAP and that their use is properly monitored and controlled by using the prepayments module to limit the risk of overpayment or improper accounting treatment.</p>   | <p>The Board maintains its position for computer assisted controls, even if NSPA considers that its manual controls are sufficient.</p> | <p>Observation<br/><b>Outstanding.</b></p>  |

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| <p><b>NSPO 2015 AUDIT REPORT – ANNEX II<br/>IBA-AR(2016)12, SECTION 6</b></p> <p><b>Improvement needed in monitoring and control over the process of billing customers</b></p> <p><b>Recommendations</b><br/>6.6 a) the re-billing process shall start when the invoice is posted (i.e. agreed for payment).</p> <p>6.6 b) manual interventions in the billing process shall only happen on exceptional cases and that any such delays should be documented without delay at Division and Programme level.</p> <p>6.6 c) NSPA proactively coordinate with customers to use available customer advances that aren't legally committed for another purpose to fund re-billings before sending additional invoices for payment to the customers.</p> <p>6.6 d) NSPA ensure that, for accounting presentation purposes, customer advances are being properly net from billed and unbilled receivables as appropriate.</p> | <p>The re-billing process generally starts when the supplier invoice is paid. This is considered acceptable.</p> <p>Manual interventions occurred in 4% of billings in 2016.</p> | <p>Observation <b>Settled</b>.</p> <p>Observation <b>Settled</b>.</p> <p>Observation <b>Outstanding</b>.</p> <p>Observation <b>Outstanding</b>.</p>     |
| <p><b>NSPO 2015 AUDIT REPORT – ANNEX II<br/>IBA-AR(2016)12, SECTION 7</b></p> <p><b>Monitoring of the cash held at NSPO</b></p> <p><b>Recommendations</b><br/>7.7 a) LN and the other NSPO programmes identify all candidates for closure and release the reserved funds back to the customers and Nations.</p> <p>7.7 b) the final invoice indicator be reactivated in SAP.</p> <p>7.7 c) the programmes follow a stricter policy on cash holdings and relate them to current and future legal commitments. They should contact the customers and Nations to identify any cash balances in excess of these commitments and reduce them via returns to the customers and Nations or a reduction in future calls or invoicing.</p> <p>7.7 d) NAM programme continue budget related measures to reduce the calls and that a documented action plan be put in place to reduce the amount of cash held on behalf of</p>   | <p>The Board notes some improvement in the LN programme, but was not made aware of efforts in other programmes.</p>  | <p>Observation <b>Outstanding</b>.</p> <p>Observation <b>Settled</b>.</p> <p>Observation <b>Outstanding</b>.</p> <p>Observation <b>Outstanding</b>.</p> |

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|--|--------------|---|
| <p>Nations. This should include a return to the Nations of any unused and uncommitted funds remaining in the Acquisition budget.</p> <p>7.7 e) NSPA return the customer and replenishment credits to the customers and Nations. This would include for the CEPS programme, where such credits equals approximately 7 years of the budgetary contributions needed to fund operations based on the current level of military and non-military revenues.</p> <p>7.8 The Board also recommends that the National Organisations in Germany and France create and use a bank account that is specifically for the NATO related activities only, and that the National Organisation in Belgium ensures that monthly cash reconciliation are performed and documented, and if possible, request to create and use a bank account that is not a direct account at the Ministry of Finance.</p>  |              | <p>Observation<br/><b>Outstanding.</b></p> <p>Observation<br/><b>Outstanding.</b></p> |
| <p><b>NSPO 2014 AUDIT REPORT – ANNEX II IBA-AR(2015)23, SECTION 1</b></p> <p><b>Recommendations</b></p> <p>1.11 The Board recommends that the NSPA Director of Finance, as a matter of urgency and without further delay, implement the Improvement Plan in respect to the NAM Programme. This may also require a critical reconsideration of how best to address these long-standing weaknesses.</p> <p>1.12 The Board further recommends the following in respect to the NAM Programme:</p> <ul style="list-style-type: none"> <li>• Detailed written policies and procedures be developed and implemented as soon as possible.</li> <li>• Responsibilities need to be clarified in writing and those responsible should be managed and held accountable.</li> <li>• Detailed control activities should be developed, including a monthly financial closure and reconciliation process, timely management reviews, periodic reporting to NSPA senior management, and internal audit monitoring.</li> <li>• Improvements in the communication between the NSPA Finance Directorate, the NSPA Finance Division and the NAM Programme.</li> </ul> |              | <p>Observation<br/><b>Settled.</b></p> <p>Observation<br/><b>Settled.</b></p>         |

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| <b>OBSERVATION / RECOMMENDATION</b>  | <b>ACTION TAKEN</b>  | <b>STATUS</b>                      |
|--|--|------------------------------------|
| 1.13 The Board reiterates its recommendation that NSPA develop a detailed, written accounting manual that includes details of the consolidation process such as timelines, inter-segment account reconciliation and specific consolidation entries.  | There is no detailed accounting manual yet; observation superseded with observation 1.23(b) of the 2015 audit report   | Observation<br><b>Outstanding.</b> |
| <b>NSPO 2014 AUDIT REPORT – ANNEX II<br/>IBA-AR(2015)23, SECTION 2</b><br><br><b>Recommendation</b><br>2.8 The Board recommends that NSPO be in a position to quickly implement NAC decisions regarding the financial reporting of the CEPS Programme.   |  | Observation<br><b>Settled.</b>     |
| <b>NSPO 2014 AUDIT REPORT – ANNEX II<br/>IBA-AR(2015)23, SECTION 8</b><br><br><b>Recommendation</b><br>8.3 The Board recommends that NSPA implements appropriate procedures to ensure that any differences observed during the reconciliation process between the confirmations received from the national depots or contractors and the figures reported by NSPA are resolved in a timely manner and are accurately reported to both the third party owners and in the notes to the financial statements. | There continues to be weaknesses in the reconciliation process as differences exist and are not corrected on time for the issuance of the financial statements.      | Observation<br><b>Outstanding.</b> |
| <b>NSPO 2014 AUDIT REPORT – ANNEX II<br/>IBA-AR(2015)23, SECTION 9</b><br><br><b>Recommendation</b><br>9.6 The Board recommends that NSPO gives priority to this review of its internal audit function.  |  | Observation<br><b>Settled.</b>     |
| <b>NSPO 2014 AUDIT REPORT – ANNEX II<br/>IBA-AR(2015)23, SECTION 10</b><br><br><b>Recommendation</b><br>10.8 The Board recommends that NSPO allocate the unallocated customer credits as soon as possible and return this excess cash to nations. In the future, such an allocation should be performed more timely. It should be done before the issuance of the financial statements.  | NSPO's formal comments on this observation reported time constraints preventing the allocation of credits.<br>The Board did not observe improvement during the year. | Observation<br><b>Outstanding.</b> |
| <b>NAMSA 2011 AUDIT REPORT<br/>C-M(2013)0015 &amp; IBA-AR(2012)29, SECTION 5.3</b><br><br><b>Potential future liabilities for Nations upon withdrawal from activities</b><br><br><b>Recommendation 4</b><br>The Board recommends that the NSPA analyses the existing situation especially for the activities supported by a limited number of Nations or by non-NATO Nations to make sure that at all times  | It is NSPA's intention to propose amendments to programme directives for customers and to obtain Agency Supervisory Board  | Observation<br><b>Outstanding.</b> |

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|--|--|------------------------------------|
| members supporting NSPA activities clearly understand the potential future liabilities.  | (ASB) approval to ensure that future liabilities related to the dissolution of a project are funded over time. This will ensure that nations that leave a project pay their fair share of liquidation costs prior to leaving. However, it is not foreseen that NSPA will retroactively charge liquidation costs to customers that have already left a project. |                                    |
| <p><b>CEPMO 2008 AUDIT REPORT<br/>C-M(2011)0016 &amp; IBA-AR(2009)28,<br/>SECTION 5.6</b></p> <p><b>Observation</b><br/><b>FBG: Existence of a plug account in other payables</b></p> <p><b>Recommendation</b><br/>FBG should determine the cause of the plug account. Additionally, a separate set of books for the international activities should be created in SAP and should be used to process the international FBG transactions.</p> | NSPA has stated that FBG is currently working on this long-standing issue and plans to have the issue resolved by 2017.  | Observation<br><b>Outstanding.</b> |

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**NATO SUPPORT AND PROCUREMENT AGENCY (NSPA)  
FORMAL COMMENTS ON THE  
LETTER OF OBSERVATIONS AND RECOMMENDATIONS  
AND THE INTERNATIONAL BOARD OF AUDITORS (BOARD) POSITIONS**

**OBSERVATION 1:  
MATERIAL WEAKNESSES IN INTERNAL CONTROL OVER FINANCIAL REPORTING**

***NSPA Formal Comments***

*The Agency does not agree that there are material weaknesses in internal control over financial reporting. The Agency has a highly controlled process for the production of the financial statements, which includes detailed timelines for the production and review of the statements and their underlying data. When there are difficult financial reporting decisions to be made, they are made through discussions between senior team members based on a review of the NATO Accounting Framework. These internal controls aim to reduce and manage the risk of producing materially misstated financial statements, but are unable to eliminate all human errors, which are possible due to the manual methods of producing the financial statements and the tight reporting deadline.*

**Board's position**

The Board maintains its position.

The agency still has progress to be done to ensure quality of the financial statements produced, and to be more pro-active in improving the quality of information reported in the disclosure notes. However, the Board noted improvements compared with the previous year.

**OBSERVATION 1.4:  
FOREIGN MILITARY SALES (FMS) RELATED LIABILITIES RECORDED WHEN A  
PREPAYMENT HAD ALREADY BEEN PAID**

***NSPA Formal Comments***

*The Agency does not agree with this IBAN observation which has led to a qualification of the financial statements.*

*As noted in the Agency's comments on the IBAN Letter of observations and recommendations for the NSPO Financial Statements for the year ended 31 December 2015, the majority of the Agency's United States FMS purchases are funded through prepayments to the United States Government; however, on occasions, the United States Government does not deduct invoiced amounts from prepayments and hence the Agency's Accounts Payable to the United States Government can increase.*

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*From an accounting perspective, when the United States Government requests a prepayment from the Agency it creates a financial liability with the Agency which the Agency extinguishes when it transfers money to make the prepayment. In its year-end accounting the Agency raises another financial liability (an accrual) with the United States Government based on the Department of Defense (DD) Form 645 which shows goods and services received in the year. The DD645, FMS billing statement issued by Defense Security Cooperation Agency (DSCA) represents an official claim for payment by the United States Government (USG). As the DD645 is received after the year-end, amounts owing are shown as accruals in the financial statements. Once the DD645 is received the Agency is able to offset the accrual, which then becomes an account payable, with the prepayment.*

*This accounting is in line with Section 47<sup>1</sup> of IPSAS 28, "Financial Instruments: Presentation", which forms part of the NATO Accounting Framework, and which outlines the requirements for the offsetting of financial assets (e.g. a prepayment) against a financial liability (e.g. an account payable).*

*The Agency does not consider the requirements of IPSAS 28 to be met and therefore the Agency considers its accounting treatment to be correct.*

*<sup>1</sup> A financial asset and a financial liability shall be offset and the net amount presented in the statement of financial position when, and only when, an entity:*  
*(a) Currently has a legally enforceable right to set off the recognized amounts;*  
*(b) Intends either to settle on a net basis, or to realize the asset and settle the liability simultaneously.*

*In accounting for a transfer of a financial asset that does not qualify for derecognition, the entity shall not offset the transferred asset and the associated liability (see IPSAS 29, paragraph 38).*

**Board's position**

The Board maintains its position, and had also done so in the prior year audit report.

Since NSPA is generally required to make prepayments to the United States Government before FMS goods or services are delivered, the Board's opinion is that there is no liability because there will be no subsequent cash outflow. As there is no liability (financial or otherwise), the reference made by NSPA to IPSAS 28 does not apply.

If, on occasion, the United States Government does not deduct invoiced amounts from prepayments, then those can be presented as a liability because an additional payment will be required to be made to the United States Government.

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**OBSERVATION 1.5:  
COMPARATIVE BALANCES NOT FULLY PRESENTED**

***NSPA Formal Comments***

*While the Agency agrees that comparative balances for the beginning and ending of 2015 and of 2016 should have been presented in the Statement of Changes in Net Assets, this statement was designed with the support of the IBAN when the Agency restated its 2015 Financial Statements, and the same presentation did not lead to an observation or qualification of the 2015 Financial Statements. This will be easily corrected in next year's financial statements.*

*The Statement of Financial Position and Statement of Financial Performance, which had comparative balances for 2015 and 2016 for all business segments, did not include the 2015 comparative balances for the inter-business unit eliminations. IPSAS indicates that comparative information shall be disclosed in respect of the previous period for all amounts reported in the financial statements, it also states that comparative information included in narrative and descriptive information (notes, for example) shall be included when that information is relevant for an understanding of the current period's financial statements.*

*The reporting of Note 3 Property, Plant and Equipment and Note 4 Intangible Assets, which clearly shows opening and closing period balances, is in accordance with IPSAS and generally accepted accounting principles.*

**Board's position**

Notes 3 and 4 are not in accordance with IPSAS as they do not disclose a reconciliation of the carrying amount at the beginning and end of the comparative period (2015). The illustrative example in IPSAS 17, Property, Plant and Equipment, demonstrates such a disclosure.

**OBSERVATION 1.6:  
REPORTING OF THE CEPS PIPELINE ASSETS**

***NSPA Formal Comments***

*The German National Organisation (FBG) is unable to support the pipeline valuation of Assets in the Course Of Construction with the same level of supporting documentation as other National Organisations. This constraint is due to processes through which the German Host Nation undertakes investment projects for both NSIP and CEPS financed projects.*

*The NATO Accounting Policy on Property Plant and Equipment, which will become applicable on 1 January 2018, states that, "If a territorial Host Nation constructs an asset and the NATO entity does not receive timely the complete*

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*and reliable financial information, the NATO entity is allowed to capitalise these assets after construction has been completed and the assets have been handed over". This policy, which anticipates the issue that has arisen with FBG, will be implemented for the production of the 2018 financial statements and should lead to the removal of the observation.*

*The CEPS Programme Office recognises the issue encountered by the IBAN audit team. It will discuss the issue with the French National Organisation (SNOI) and its private company contractor (TRAPIL) in order to improve the situation in the future.*

*IPSAS 17 specifies that initial estimates for dismantling, removing and site restoring are to be recognized for qualifying PPEs. However, it also specifies that it only applies if the entity has an obligation that it incurs on acquisition of the asset or as a result of using the asset.*

*CEPS has no legal or contractual obligation regarding such costs; the obligation remains with the Host Nations which remain responsible to comply with the National legislation in case of dismantling.*

*This point will be disclosed in future NSPO Financial Statements.*

**Board's position**

The Board will assess the implementation of the new PP&E accounting policy and its compliance with the NATO Accounting Framework during its audit of the 2018 financial statements. As a result, it is too early to determine whether the observation will be removed.

**OBSERVATION 1.7:**

**NO ASSESSMENT OF CUSTOMER ADVANCES TO DETERMINE WHETHER CURRENT OR NON-CURRENT**

***NSPA Formal Comments***

*The Agency agrees that customer advances, which are properly recorded as liabilities of NSPA have not been analysed whether those advances are current or non-current. When advances are requested, there is a current or pending commitment by the Agency, but the disbursement of those funds may extend beyond one financial year.*

*The Agency will look into this going forward.*

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**OBSERVATION 1.8:  
LACK OF EVIDENCE THAT A PAYABLE TO FRENCH TAX AUTHORITIES REMAINS  
A LIABILITY**

***NSPA Formal Comments***

*The NATO Office of Legal Affairs has been responsible for discussing these issues with the French tax authorities. CEPS has not paid these taxes since November 2007 and the French Tax Authorities have not requested taxes. CEPS considers that such taxes no longer meet the definition of an accrual and accrued amounts will be reversed in 2017 and credited to the Nations' funds.*

**OBSERVATION 1.10:  
DISCLOSING OF CEPS REVENUE FROM DIFFERENT SOURCES**

***NSPA Formal Comments***

*Paragraph 106 of IPSAS 1, "Presentation of Financial Statements" states that "when items of revenue and expense are material, their nature and amount shall be disclosed separately". Paragraph 107 gives circumstances which would give rise to separate disclosure; the Agency does not consider that these circumstances, apply in respect of CEPS.*

**Board's position**

Upon considering NSPA's comment, the more appropriate paragraph from IPSAS 1 that the Board should have referred to is paragraph 104, which states that "Additional line items, headings, and subtotals shall be presented on the face of the statement of financial performance when such presentation is relevant to an understanding of the entity's financial performance." The different sources of NSPA's revenue is an important element to understand the financial performance. The Board maintains its recommendation.

**OBSERVATION 1.11:  
INACCURACIES AND ERRORS IDENTIFIED IN THE 2016 NSPO FINANCIAL  
STATEMENTS**

***NSPA Formal Comments***

*In order to properly account for the provision of a probable expense related to losses associated with Microsoft licenses unsold or sold and for which no revenue will be forthcoming, the Agency recorded an expense of 2.1 MEUR in its Statement of Financial Performance with an offsetting liability for Bad and Doubtful Accounts. The Agency also disclosed its treatment of the Microsoft licenses in Note 20 of the Financial Statements. The provision also effected the liability, Credits to be Allocated, at the year-end, which neutralized the changes*

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*in the Log Ops business segment Net Assets. This is similar to the treatment of other customer accounts receivable write-offs.*

*The Agency is currently reviewing whether it can reduce the size of the Microsoft licenses provision; the results of this review will be reported to our governing board. In addition, the Agency will be implementing controls to ensure that such an event will not be repeated.*

*The Agency agrees that the Cash Flow Statement had a mismatching of the categorization due to an error in the evaluation of a supporting schedule used to build the report. The effect understated the Cash Flows from Investing Activities by a non-material 1.9 MEUR (1.28%) out of a total of 149 MEUR, and overstated the Cash Flows from Operating Activities by 1.9 MEUR (0.74%) out of a total of 257 MEUR. The Cash and Cash Equivalents at the Beginning of the Period and End of Period were stated correctly at 2.2 BEUR and 2.44 BEUR, respectively.*

*Note 22 was rewritten in respect of the 2015 Financial Statements based on the guidance of the IBAN. In the 2017 Financial Statements, the note shall either be deleted, as it is not required by the NATO Accounting Framework, or shall be rewritten to clarify that it pertains to inventory which is managed by NSPO and can be used by SACEUR but which does not appear in the Financial Statements of either NSPO or ACO.*

*The impact of changes in accounting policy, which resulted from the correction of errors in prior year financial statements, is disclosed directly in the Statement of Changes in Net Assets.*

*The Agency agrees that “Annex 1 – Log Ops Business Unit – Administrative Cost Elements”, which includes information on authorized credits, commitments consumed and lapsed during 2016, did not include transfers between Chapters. This was noted by the auditor during their fieldwork, and was corrected by the Finance Division, and submitted to IBAN before the audit report was issued. As noted, the totals in the annex were correctly stated.*

*The Agency agrees that Annex 2 – Log Ops Business Unit – Jointly and Commonly Funded Operational Projects understated the commitments made in 2016 for the MMF-Multirole Tanker Transport Fleet by 19.5 MEUR, with a corresponding overstatement of the unused credits at year-end.*

*This was caused by human error in not finalizing an amendment to a Purchase Order within the Agency ERP system which would have correctly created the commitment. It should be noted too that the issuance of a Purchase Order (or amendment thereto) by NSPA for the MRTT is a formality to ensure commitments are properly reported, but is not required in the business relationship between OCCAR (acting for and on behalf of NSPA GM) and Airbus Defence and Space.*

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**Paragraph 1.12:  
NSPA Formal Comments**

*Please refer to comment at 1.4.*

**Paragraph 1.13:  
NSPA Formal Comments**

*Please refer to comment at 1.6.*

**Paragraph 1.14:  
NSPA Formal Comments**

*Please refer to comment at 1.7.*

**Paragraph 1.15:  
NSPA Formal Comments**

*Please refer to comment at 1.8.*

**Paragraph 1.17:  
NSPA Formal Comments**

*Please refer to comment at 1.10.*

**Paragraph 1.18:  
NSPA Formal Comments**

*Please refer to comment at 1.11.*

**OBSERVATION 2:  
EFFORTS TO ACHIEVE COMPLIANCE WITH THE NATO FINANCIAL  
REGULATIONS, PARTICULARLY THOSE ARTICLES ON INTERNAL CONTROL,  
RISK MANAGEMENT AND INTERNAL AUDIT**

**Paragraph 2.4:  
NSPA Formal Comments**

*The Agency Supervisory Board approved the NSPO Financial Rules and Procedures on 27 June 2017. The ASB has allowed the Agency up to 24 months to implement a number of rules and procedures which require significant changes to Agency resources, processes and systems.*

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**Paragraph 2.6:**  
**Article 13 – Internal Audit**  
**NSPA Formal Comments**

*The Agency does not agree that the structure of the Audit Advisory Panel threatens the independence of Internal Audit. Please refer to comments in respect of Section 3.*

**Board's position**

The Board maintains its position. The Board highlights the fact that Internal Audit is a pillar of a strong control environment.

**Paragraph 2.7(a):**  
**NSPA Formal Comments**

*The General Manager has requested that the Agency's internal Process Working Group provides him with recommendations for implementing an internal control system in July and this will include a recommendation on an appropriate framework to be adopted. The implementation of an internal control system will lead to an increase in resource requirements.*

**Paragraph 2.7(b)(c):**  
**NSPA Formal Comments**

*The Agency is required by both its Charter and the NATO Financial Regulations to have risk management in place.*

*The Agency has had an entity-wide risk management policy in place since 2015. The Agency is currently drafting further operating guidance which will provide more detailed information about the implementation of the policy, as well as provide information on how to access, input, and retrieve information from the Risk Management tool developed by IT.*

*The Agency aims to have fully embedded risk management by the end of 2018.*

**Paragraph 2.7(d):**  
**NSPA Formal Comments**

*The Agency agrees with the recommendation. The 2018 Internal Audit Plan will address the implementation of a risk management policy and an internal control framework. The scope of the audits in both these areas will be necessarily limited given the maturity of both.*

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**OBSERVATION 3:  
STRUCTURAL WEAKENING IN THE POSITION OF THE INTERNAL AUDIT**

**Paragraph 3.3:  
NSPA Formal Comments**

*The Agency does not agree with IBAN's observation.*

*The IBAN notes that the "internal audit plan would be further validated by the General Manager and the Audit Advisory Panel". While the Audit Advisory Panel reviews the annual internal plan and the General Manager approves it, the Audit Advisory Panel does not validate the plan; this is stated in the Agency's Internal Audit Charter (section 7.1 of the Internal Audit Charter).*

*Additionally, the role of the Audit Advisory Panel does not allow for it to approve or reject the audit plan but rather to "Identify areas where additional assurance is required in order to inform or propose updates of the Internal Audit Plan". [Audit Advisory Panel Terms of Reference, paragraph 4].*

*Advice offered by the Panel is "presented periodically to, and discussed with, the NSPA General Manager and the Agency's Executive Management Board for consideration." (Audit Advisory Panel Terms of Reference, paragraph 1).*

**Board's position**

The Board notes NSPA management's comments that, in their view, the Audit Advisory Panel does not approve the Internal Audit Plan, but rather offers advice and proposals. The Board will follow-up on this observation in future audits to assess whether this is also the case in practice.

**Paragraph 3.4:  
NSPA Formal Comments**

*The IBAN notes that the "audit plan is subject to modification and approval by NSPA management which could lead to conflicts of interest", and that this in turn leads to a weakening of the organisational independence of the Internal Audit function.*

*The General Manager is responsible for approving the internal audit plan. In performing this role, however, the General Manager may seek the advice of senior management to ensure that areas which are considered important to management are included in the plan. Therefore, while senior management may suggest changes, they can neither modify nor approve the audit plan.*

*During the development of the audit plan, the Auditor General seeks the advice of senior management prior to submitting the draft to the General Manager. In this way, the Auditor General is able to consider senior management's*

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*assessment of risk, as well as his own assessment of risk gained through the conduct of audits and as an advisory member of the Risk Management Working Group, in the drafting of the audit plan.*

**Board's position**

The Board notes NSPA management's comments that, in their view, the Audit Advisory Panel does not approve the Internal Audit Plan, but rather offers advice and proposals. The Board will follow-up on this observation in future audits to assess whether this is also the case in practice.

**Paragraph 3.5:  
NSPA Formal Comments**

*The Agency agrees in part with the observation.*

*As recommended by the IBAN, the Audit Advisory Panel is only a consultative and advisory body and does not have the authority to approve the Internal Audit plan. The Audit Advisory Panel's Terms of Reference make clear that its role is to "provide objective advice" and its findings are presented to the General Manager and the Executive Management Board "for consideration." Only the General Manager has the authority to approve the Internal Audit plan.*

*Within the NSPA Operating Instruction 4600-21 "Operating Instruction for Internal Audit", dated 15 November 2016, the term "endorse" is used with respect to the audit plan in 5.9.3(vi). The term must be read in context with paragraph 5.8.2 which notes that the plan will be developed using input from the Directors, the Audit Advisory Panel and the Terms of Reference. An endorsement of the Internal Audit plan by the Audit Advisory Panel is an advice to the General Manager that the plan should be approved by him.*

*Paragraph 5.8.2 of the Operating Instruction needs to be revised as it is inconsistent with the other parts of the Operating Instruction, the NSPO Charter, and the Terms of Reference. The first sentence states, "After approval of the internal audit plan by the General Manager and the NSPA Advisory Panel...." This is, as noted, contrary to the other documents and to actual practice.*

**Paragraph 3.6:  
NSPA Formal Comments**

*The Agency partly agrees with the observation.*

*The IBAN recommended that the Auditor General report functionally to the General Manager. This is already the case. The Auditor General is part of the General Manager's office and as noted in the part of the NSPA Internal Audit*

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*Charter which concerns the independence of the Internal Auditor, "The Auditor General reports functionally and administratively to the NSPA General Manager" (Charter 6.2).*

*This is also stated in the NSPA Operating Instruction 4600-21 Operating Instruction for Internal Audit, para 5.5, "The Auditor General reports functionally to the NSPA General Manager. Independence of the position ensures the degree of independence essential to the effectiveness of internal auditing."*

*IBAN also recommended that the Auditor General also "have a direct reporting line to the Audit Committee at ASB level." This is addressed by the NSPO Financial Rules and Procedures which permit the Finance, Administration and Audit Committee to review and provide comments on the internal audit plan, as well as in Procedure XIII (14) which requires:*

*"The Head of Internal Audit shall present a report, in restricted session if considered necessary, at the formal Finance, Administration and Audit Committee meetings. The report shall include the internal audit activity's purpose, authority, responsibility, and performance relative to the Internal Audit Plan. The report shall also include significant risk exposures and control issues, fraud risks, governance issues, and any other matters of relevance to the Finance, Administration and Audit Committee."*

*The Finance, Administration and Audit Committee is considered the most appropriate forum for discussion with the Head of Internal Audit; however, the committee can always escalate any concerns it has to the Agency Supervisory Board.*

**Board's position**

In respect to Internal Audit direct reporting to the Audit Committee at the ASB level, the Board further clarifies its recommendation by adding that Internal Audit should have unfettered and direct access to the Audit Committee at ASB level as and when determined necessary by the Auditor General. The Board will follow-up on this observation in future audits to assess whether this is the case in practice.

**OBSERVATION 4:  
ACCRUAL ESTIMATES WITHIN NSPO ARE TO BE IMPROVED**

**Paragraph 4.5(a):  
NSPA Formal Comments**

*The Agency agrees that additional training of personnel involved in the determination of accrued liabilities at the year-end would be beneficial, and will conduct such training in 2017. This will include finance and non-finance*

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*personnel and will reinforce the importance of validating accrual information for the NSPO Financial Statements.*

*In addition, Finance and Logistics will start work on reviewing accruals data before the year-end to ensure that less time needs to be spent on reviewing accrual data after the year-end.*

**Paragraph 4.5(b):  
NSPA Formal Comments**

*The current practice of extracting data from the Agency's Enterprise Resource Planning (ERP) system and issuing that information via electronic mail to programs for validation will continue for the foreseeable future. Although this process is not fully automated, there is no cost-effective method by which the Agency can verify the receipt of goods and services at a myriad of locations (often the customers' sites). Close coordination between finance and logistics personnel, and communications with customers are required to achieve the objectives of acknowledging what goods and services were received before year-end, but for which an invoice was received in the subsequent year. Given the high volume of transactions, the Agency believes the error rate (missing, incomplete or inaccurate data) is low.*

**Board's position**

The Board maintains its position.

**Paragraph 4.5(c):  
NSPA Formal Comments**

*The Agency disagrees with the generalized comment to discontinue an accrual estimation process based on historical data. The Agency believes that our methodology to estimate accruals is sound and is based on historic trends. We will engage with the IBAN to evaluate other best practice methodologies for possible implementation within NSPA.*

*The methodology used took an average of three financial years, 2012-2014, realizing that for those goods and services for which we had no invoice at year-end, 95% of the invoices would be received during the first two months of the following year. Five (5%) percent of the invoices would arrive after the first two months, but usually within the next 1-3 months.*

*The Agency previously had four months to produce the annual financial statements, and used the first two months of the year as a timeframe in which those invoices would be validated against the year-end accruals. When the timeline for the production of NATO agencies financial statements was reduced by one month (25% of the available time), the Agency made a conscious decision*

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*to reduce the timeframe available for accrual estimation by two weeks (25% of the previous available time). Further, we analyzed the inflows of those invoices and determined that 85% of the invoice values were received within the first six (6) weeks, 10% of the values were received in the seventh and eighth week, and 5% of the invoice values were received over a period of some weeks subsequent to the first two months. Thus, the 15% “mark-up” that IBAN refers to was an estimate by the Agency of the value of the invoices that would be received after the cut-off date of mid-February, and that was a reasonable estimate to allow the Agency to determine its accrual value for use in the annual financial statements.*

**Board’s position**

The Board maintains its position. A reliable estimate of accruals should be based on an assessment of specific goods or services that are known, or were expected, to have been received before the end of the current reporting period but not yet invoiced.

**Paragraph 4.5(d):  
NSPA Formal Comments**

*The Agency will look into this in further detail.*

**OBSERVATION 5:  
WEAKNESSES IN THE RECONCILIATION AND REPORTING OF INTER-NATO ENTITIES**

**Paragraph 5.4(a):  
NSPA Formal Comments**

*The Agency agrees that enhancements are beneficial and needed in order to reconcile open accounts receivable and accounts payable between ACO and NSPA. The Agency performed two iterative reconciliations during 2016, but still had unresolved variances at the cut-off time for the finalization of the 2016 financial statements. The Agency is currently working with ACO to improve the process through the addition of common data elements to allow for reconciliation at the customer level, which is what NSPA uses for tracking at the transaction level.*

**Paragraph 5.4(b):  
NSPA Formal Comments**

*The Agency agrees, and is currently in the process of conducting the first reconciliation process for 2017. The goal is to identify lessons learned that will improve the timeliness and accuracy of the end of year reconciliation of open accounts receivable and accounts payable between the two NATO entities.*

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**OBSERVATION 6:  
WEAKNESSES IN CASH CONTROL AND MANAGEMENT**

**Paragraph 6.1:  
NSPA Formal Comments**

*The Agency does not consider that cash balances are high considering its total business volume of 3.65 BEUR in 2016. The Agency considers that funds are allocated to customers on a timely basis.*

*Effective cash management ensures solvency by maintaining adequate cash on hand, reducing the length of time required to collect outstanding accounts receivable and selecting appropriate short-term investment opportunities. Maintaining high levels of cash is not a weakness in cash control.*

**Board's position**

The Board maintains its position.

**Paragraph 6.5:  
NSPA Formal Comments**

*The Agency does not believe it is "misleading" the IBAN when the total commitments made by the Agency are less than the advances provided by customers. There are a number of ongoing procurement actions that are not yet finalized through a contract or purchase order, but where a price acceptance has been made with the customer and the customer advances the funds for that pending order.*

**Board's position**

The Board maintains its position.

**Paragraph 6.6:  
NSPA Formal Comments**

*It is for customers (nations) to decide how they will use assets held on their behalf by NSPA. NSPA provides monthly financial situation reports to all customers, and has regular dialogue with many of these customers on the disposition of their assets and liabilities.*

**Board's position**

The Board maintains its position.

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**Paragraph 6.7:  
NSPA Formal Comments**

*Please refer to comment at 1.7.*

**Paragraph 6.8:  
NSPA Formal Comments**

*CEPS accepts the IBAN remark. A mitigating cause in 2016 was the loss of the Carling contract for 2 million M3 of Nafta, which was approximately 15% of the average transport activity of CEPS. Compensating contracts were established and signed months after the establishment of the 2016 budget.*

*The CEPS PB has already decided on action to correct the situation.*

- *For 2017 and following years the revenues will be estimated at approximately 100 MEUR, compared to 82 MEUR originally in 2016.*
- *The contributions for 2017 were decided at the level of 26.8 MEUR, already much lower than the level of approximately 35 MEUR in 2016.*
- *The CEPS PB has decided on contributions for a total of 20 MEUR for 2018 to 2022 which, based on statistical data and taken separately, should reduce the funds by 4 MEUR per year.*

**Paragraph 6.10:  
NSPA Formal Comments**

*The CEPS Programme Office will continue its efforts to have FBG, RAPIL/SNOI and BPO use separate bank accounts for their CEPS activity.*

**Paragraph 6.11(a)(b):  
NSPA Formal Comments**

*Projects are closed by Support Partnerships or other relevant governing bodies as and when they determine. Any remaining funds are credited to the customers and are available for their use, as they indicate to the Agency.*

**Paragraph 6.11(c):  
NSPA Formal Comments**

*Monthly financial situation reports are issued to all customers. Customers indicate to the Agency how they wish to use their funds.*

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**Paragraph 6.12:**  
**NSPA Formal Comments**

*The CEPS Programme Board had noted the increasing available cash at the end of 2015 as reported in the CEPS Financial Statements. Therefore, the CEPS Programme Board has decided in 2016 to estimate more accurately the non-military revenues with effect from 2017 onwards.*

*The CEPS Programme Board also has decided to reduce the yearly contributions by more than 4 MEUR per annum with an impact on 2018 and the four following years. When preparing future budgets, CEPS will be vigilant on the current trend to adjust the future expected revenues to the best available estimates.*

**OBSERVATION 7:**  
**WEAKNESSES IN GENERAL COMPUTER CONTROLS**

**Paragraph 7.5:**  
**NSPA Formal Comments**

*The SAP Access Authorizations Working Group is an internal working group established in June 2015 by the General Manager:*

*“in order to function as the single entity to clean the past by analysing access rights granted by data owners to users as well as to improve the access rights management in order to reinforce internal controls and protect the Agency against misuse of our IT system from potential errors or frauds.”*

*While the Agency acknowledges that the Segregation of Duties (SoD) Matrix has not been finalized, access rights by post are reviewed by a number of personnel across different directorates and divisions to ensure that there are no conflicts of interest before new or revised roles are authorized. This thorough review of access rights granted to personnel led the SAP Access Authorizations Working Group at its July 2015 meeting to observe, in response to an internal audit report on the subject that it is not correct to consider that SoD is not correctly applied and the risk of fraud is increased.*

*NSPA currently lacks the resources to dedicate to the full scope of the Governance, Risk and Compliance (GRC) tool within the Agency's ERP, but believes its current practices provide a reasonable assurance that violations of SoD are not occurring.*

**Board's position**

The Board maintains its position.

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**FOLLOW-UP OF PREVIOUS YEARS' OBSERVATIONS**

**OBSERVATION:**

**NSPO 2015 AUDIT REPORT – ANNEX II, IBA-AR(2016)12, SECTION 4  
IMPROVEMENTS NEEDED IN THE MONITORING AND CONTROL OVER  
POTENTIAL CONFLICTS OF INTEREST IN PROCUREMENT**

**4.8 – NSPA Formal Comments**

*The Competition Advocate provided this report at the May 2017 FAA meeting and June 2017 ASB meeting.*

*This has been addressed in the NSPO Financial Rules and Procedures which were approved by the Agency Supervisory Board on 27 June 2017.*

**Board's position**

The Board maintains its position.

**OBSERVATION:**

**NSPO 2015 AUDIT REPORT – ANNEX II, IBA-AR(2016)12, SECTION 5  
IMPROVEMENT NEEDED IN THE MONITORING AND CONTROL OVER  
PREPAYMENTS MADE TO VENDORS**

**5.5 – NSPA Formal Comments**

*The Agency considers that manual controls over the control of prepayments are sufficient and cost-effective.*

**Board's position**

The Board maintains its position.

**OBSERVATION:**

**NSPO 2015 AUDIT REPORT – ANNEX II, IBA-AR(2016)12, SECTION 6  
IMPROVEMENT NEEDED IN MONITORING AND CONTROL OVER THE PROCESS  
OF BILLING CUSTOMERS**

**6.6 – NSPA Formal Comments**

*The Agency is in regular contact with customers over how to deploy their advances.*

*The Agency considers that it accounts for customer advances in accordance with the NATO Accounting Framework.*

**Board's position**

The Board maintains its position.

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**OBSERVATION:  
NSPO 2015 AUDIT REPORT – ANNEX II, IBA-AR(2016)12, SECTION 7  
MONITORING OF THE CASH HELD AT NSPO**

**7.7 – NSPA Formal Comments**

*While the NAM Programme has undertaken to offset calls for contributions against excess cash holdings, the return of unused funds is entirely at the Nations' discretion. The Agency can only propose but not enforce the return of funds.*

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# NATO SUPPORT AND PROCUREMENT ORGANISATION ORGANISATION OTAN DE SOUTIEN ET D'ACQUISITION



AC/338-D(2017)0008

## Financial Statements 2016 (Redacted Version)





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## Overview of the NATO Support and Procurement Organisation's Operations and Environment

The NATO Support and Procurement Organisation (NSPO) stood up on 1 April 2015 with the merger of the NATO Support Organisation and the NATO Procurement Organisation.

The NSPO consists of Log Ops Business Unit, the Central Europe Pipeline System Programme Business Unit, the NATO Airlift Management Programme Business Unit plus the Agency Supervisory Board's Chairperson's Office.

The mission of the NSPO is to provide responsive, effective and cost-efficient logistics, operational and systems support and services to the Allies, NATO Military Authorities and partner Nations, individually and collectively, in time of peace, crisis and war, and where required, to maximize the ability and flexibility of their armed forces, contingents, and other relevant organisations, within the guidance provided by the North Atlantic Council (NAC), to execute their core missions.

All NATO Nations are members of the NSPO. Non-NATO Nations may apply for association with the NSPO if they wish to participate in NSPO activities. Their participation shall be subject to such conditions, consistent with present Regulations and the NSPO Charter, as the participating NATO Nations and the non-NATO Nations agree.

NSPO is headquartered in Luxembourg with some of its staff located in Hungary (NATO Airlift Management Programme), France (Central Europe Pipeline System Programme), and a Southern Operational Centre in Italy. NSPO shares the same legal identity as NATO.

### Role of the NATO Support and Procurement Agency

The NATO Support and Procurement Agency (NSPA) is the executive arm of NSPO and is chartered to execute the NSPO's mission. The responsibilities of NSPA

include the following tasks, while continuously striving for improved effectiveness, efficiency and cost savings:

- conducting agency mission required specific procurement;
- acting as Host Nation for NATO Security Investment Programme (NSIP) projects as assigned by the Resource Policy and Planning Board (RPPB) or the Investment Committee (IC);
- planning and management of contracting for NATO operations, including in support of Allied Command Operations, including contracting for required strategic lift in all transport modes;
- providing logistics support for operations, including in support of Allied Command Operations, including real-life support and environmental solutions; providing supply management;
- performing maintenance, including sustainment management;
- providing services to contribute to life-cycle support of assigned systems; conducting off-the-shelf agency mission required specific procurement; providing technical assistance;
- supporting to organic airlift capabilities;
- managing the provision of lift/transport capabilities;
- fulfilling the operational requirements during peace, crisis and war for the transport, storage and delivery of fuel for military and civilian customers; and,
- performing other missions as assigned by the NAC.

## The Activities of the NATO Support and Procurement Organisation's Business Units

### Chairperson's Office

The Chairperson's Office is the secretariat of the Agency Supervisory Board and the NAMP and CEPS Programme Boards.

### **Log Ops Business Unit**

The Log Ops Business Unit provides a number of capabilities which are available to participating nations. It provides support to NATO operations, procures and facilitates the exchange of goods and services for at the most advantageous rates, and, provides support to twenty-eight active Support Partnerships.

Log Ops activities are paid through customer-funding on a no profit, no loss basis. All costs incurred by Log Ops activities are borne by NSPO Member Nations, by NATO bodies, or, by other authorised customers.

Support and/or Procurement Partnerships can be established within the NSPO, subject to precise terms and conditions, on the initiative of two or more NATO nations wishing to organize jointly, or commonly, the support and services of activities within the scope of the NSPO's Mission and guidance provided by the Council.

At times, the partnerships will procure goods and/or services through a commonly (i.e. all twenty-eight NATO nations) or jointly (i.e. more than one but less than twenty-eight NATO nations) agreed budget, while at other times, members of the partnership will procure goods and services individually through purchase requests. NSPA procures goods and/or services for the Support Partnerships.

For financial reporting purposes, the Log Ops Business Unit segment incorporates the NSPA Headquarters, Logistics Operations, and NSPA Support Divisions.

### **Central Europe Pipeline System (CEPS) Programme Business Unit**

Under the authority of the CEPS Programme Board, the CEPS Programme manages a NATO pipeline system which crosses the host nations of Belgium, France, Germany, Luxembourg and the Netherlands and is responsible for the transportation, storage and delivery of petroleum products in Central Europe for military and non-military activities. For that purpose, the CEPS Programme operates and maintains the Central Europe Pipeline System, a pipeline network, pump stations, input and delivery points, and storage depots.

CEPS is funded through various channels. Income is generated by its authorised activities which are the sales of transport and storage activities for military and non-military customers. The NATO Security Investment Programme (NSIP) supports some of the costs of the acquisition and restoration of pipeline assets required to support military requirements. Contributions by Member Nations cover that part of the budget not financed by generated revenue or NSIP funding.

### **NATO Airlift Management Programme (NAMP) Business Unit**

The mission of the NAMP is to meet to the best advantage the requirements of the Nations contributing to the NATO Airlift Management Programme as described in the Strategic Airlift Capability Memorandum of Understanding. The NAMP participants are: Bulgaria, Estonia, Finland, Hungary, Lithuania, the Netherlands, Norway, Poland, Romania, Slovenia, Sweden and the United States of America.

The Strategic Airlift Capability (SAC) Programme was created by ten NATO and two Partnership for Peace Nations (Finland and Sweden). Strategic airlift capability is provided by three Globemaster C-17 aircraft that are flown and operated by multinational military aircrew, and supported by military and civilian staff of the twelve Participating Nations. In addition, the SAC Programme obtains logistic and maintenance services for C-17 operations under a Contractor Logistic Support contract arranged through U.S. Foreign Military Sales procedures. The SAC Participating Nations control and use SAC flying hours generated by NAMP owned aircraft, within pre-agreed parameters, to meet national requirements including those in support of NATO and multinational commitments.

The NAMP is governed by the NAM Programme Board. This Board exercises all rights of ownership of assets but aircraft operation is outside scope of the NSPO Charter. The NAMP's overall activities are funded by the Participating Nations through SAC Acquisition, Operations and Administrative financial plans that are endorsed annually by the NAM Programme Board, after endorsement by the SAC Steering Board.

## How NSPO's operating environment affects its Financial Statements

NSPO makes available the following capabilities which can be used for the benefit of NATO:

- Support to Operations and Exercises
- Strategic Transport and Storage
- Logistics Services and Project Management
- Fuel Management
- System Procurement and Life Cycle Management

Those charged with the governance of NSPO do not set management targets in relation to the expected business it should generate and hence NSPO's revenue and expenditures are purely dependent on NATO nations and partner nations making use of its capabilities. As such, the financial position and performance of NSPO depends on the operational requirements of NATO nations and its partner nations.

## Compliance with Financial Regulations

The Financial Regulations that are applicable to NSPO are described in the Charter under General Provisions (Section 46):

*"The NATO Support and Procurement Organisation shall be governed by the provisions of the NATO Financial Regulations, subject to such derogations as may be approved by the NAC upon recommendation by the Resource Policy and Planning Board".*

The North Atlantic Council issued revised NATO Financial Regulations on 4 May 2015 with the goal that they would be implemented in full by the end of 2015.

However, by the end of 2016 the revised NATO Financial Regulations have not been fully implemented; a working group of the NSPO's Finance, Administration and Audit Committee is currently finalising detailed Financial Rules and Procedures for NSPO, which are consistent with the NATO Financial Regulations. Further details on the Agency's compliance with the NATO Financial Regulations are found in the Statements of Internal Control (page 6).

Until revised NSPO Financial Procedures and Rules are in place, the Log Ops, CEPS and NAMP Business Units are following the Financial Procedures and Rules of their former organisations where they are not in contradiction to the NATO Financial Regulations.

## How NSPO's mission and strategies relate to its financial position, financial performance and cash flows

As noted above, NSPO makes capabilities available to NATO nations and partner nations. It does not have any financial objectives, such as a private sector enterprise could, in relation to its financial position, financial performance and its cash flows, other than to have enough funding available to cover its administration costs and the operational requirements of its customers.

## Risks and Uncertainties that affect NSPO's Financial Position and Performance

NSPO's Financial Position and Financial Performance is based on the usage made of its capabilities by NATO nations and its partner nations. As such, its performance is impacted by NATO operations and the demand of its nations and partner for the capabilities that it offers.

## Public Disclosure of Financial Information

At the Wales Summit of 2014, the nations tasked NATO bodies to increase their financial transparency. While I am content for all the information in the financial statements to be publically disclosed, the decision on what to make publically available rests with the NSPO Agency Supervisory Board and the North Atlantic Council.



**NSPA General Manager**

## Statement on Internal Control

### Background

The North Atlantic Council issued revised NATO Financial Regulations (NFRs) in May 2015, which increased the emphasis on internal control and risk management within NATO entities.

The NFRs stipulate that the Agency's General Manager is responsible and accountable for sound financial management, and to that end, shall put in place the necessary governance arrangements to ensure and maintain a strong system of internal control.

These arrangements include, but are not limited to, the establishment and maintenance of financial governance, resource management practices, internal controls and financial information systems to achieve the efficient and effective use of resources.

### Internal Control

#### Scope of Responsibility and Purpose of Internal Control

The General Manager is responsible and accountable to the Agency Supervisory Board (ASB) for ensuring that the necessary internal management functions are in place to support effective internal control, and are designed to provide reasonable assurance that the Agency will achieve its internal control objectives in the following categories:

- safeguarding assets;
- verifying the accuracy and reliability of accounting data and records;
- promoting operational efficiency; and,
- complying with established managerial policies.

The Agency's Financial Controller reports to the General Manager and operates within the system of internal controls established by the General Manager. The Financial Controller is accountable to the NSPO Finance, Administration and Audit Committee on the management of appropriated and non-appropriated funds. The NFRs require that in order to meet the desired internal control standards, the Financial Controller shall:

- establish a system of internal financial and budgetary controls, embracing all aspects of financial management including transactions for which appropriations have been approved and those funded from such non-appropriated fund accounts as they may authorise within their jurisdiction;
- designate and formally delegate authority to officials who may authorize commitments, disburse and receive funds on his behalf; and,
- establish and maintain comprehensive accounting records of all assets and liabilities.

While the General Manager and the Financial Controller have specific responsibilities in relation to internal control, all Agency staff have a responsibility for complying with the internal controls in place to ensure NSPA is being a good steward of the funds entrusted to it by the Nations.

#### The Limitations of a System of Internal Control

A system of internal control is designed to reduce and manage, rather than eliminate, the risk of failure to achieve an entity's aims and objectives. It can provide reasonable but not absolute assurance that an entity's aims and objectives will be achieved. It is based on a continuous process designed to: identify the principal risks that threaten the achievement of objectives; evaluate the nature and extent of those risks; and manage them effectively, efficiently and economically. The cost of the internal controls should not outweigh the risks they are mitigating.

#### Compliance with the NATO Financial Regulations

Revised NFRs were issued in May 2015 and the Secretary General anticipated that NATO Bodies would implement them in full by the end of 2015.

The Revised NFRs introduced a number of requirements which were new to the Agency. The Agency had not been able to fully implement the following provisions of the NFRs by the time these Financial Statements were issued;:

- Accruals-based budgeting under certain circumstances (*not implemented*);
- The prior-approval of commitments by the Financial Controller (*not implemented*);

- Involvement of the Financial Controller in procurement (*not implemented*);
- Implementation of Risk Management (*implemented in part*); and,
- Implementation of a standardised and fully documented system of Internal Control (*not implemented*).

These requirements are not yet fully implemented because the Agency is awaiting the approval of NSPO Financial Rules and Procedures, which will establish how these requirements are to be implemented in practice within the Agency.

Currently, a Working Group of the Finance, Audit and Administration Committee is in the process of submitting draft proposals for consideration at the Finance, Audit and Administration Committee's May 2017 meeting. Subject to the endorsement of the Finance, Audit and Administration (FAA) Committee, it will recommend the proposals for consideration and approval by the ASB at its June 2017 meeting.

Before approval by the ASB, the draft document will be reviewed for consistency with the NATO Financial Regulations by the NATO Head of Financial Reporting Policy, who will take account of any comments made by the International Board of Auditors for NATO (IBAN).

In practice, we consider that the full implementation of these new requirements will require a transition period of between 18 and 24 months after their approval.

### Agency Internal Control Weaknesses and Remediation

As part of its work on considering how to implement a system of internal control, the Agency's Financial Controller assessed where established controls were not effective or where processes could be deficient.

This work was mainly limited to the Agency's administrative budgets, which are approximately five percent of Agency turnover, and highlighted a small number of transactions which were not in compliance with governing rules or procedures.

*We are not aware that any of the areas of non-compliance have led to a loss of customer funds or assets, and do not consider that these issues have led to a material or significant misstatement of the numbers provided in the Financial Statements.*

We have assessed the causes of non-compliance and conclude that they arose because:

- the Agency has not yet been able to implement the NFRs;
- some rules and procedures have not taken into account evolving business requirements;
- some rules and procedures were open to interpretation;

- there is a lack of awareness training in respect of rules and procedures.

### Internal Control - General Manager Priorities

The General Manager has set a tone at the top to highlight the importance of internal controls in all areas of NSPA operations. He has set the following priorities to focus on internal control over the coming year:

- Remediation of known internal control weaknesses as highlighted by internal Agency reviews as well as reviews conducted by the International Board of Auditors NATO (IBAN)

*The Agency will enhance internal controls to ensure that known weaknesses are remediated. In addition, the General Manager directed the Financial Controller to review operational budgets to provide me with assurance that the internal control system in respect of these budgets is working effectively.*

- The implementation of the NFRs  
*The Agency will work on plans to implement specific rules which are currently implemented under review by the Nations*
- The implementation of IBAN recommendations where they are seen to add value to the Agency in enhancing the control environment

*A Key Performance Indicator of the Executive Management Board is the implementation of IBAN recommendations and this is monitored on a monthly basis. Significant progress has been made on implementing recommendations from prior audit reports, with management considering that over 80 percent of observations are closed or resolution is in-progress.*

- The choosing and implementation of an internal control system  
*A cross functional working group to include the Financial Controller, Internal Auditor, Quality Review, and Program Managers will begin work this year to conduct a full review and develop an implementation plan for the Agency's Internal Control Program. This advisory group which will look in detail at: possible internal control weaknesses or process deficiencies within the agency; remediation of known internal control weaknesses or process deficiencies; establishment of a process for implementing an internal control system.*

*Our goal is to have selected an internal control framework for implementation by the end of the year and a plan for its implementation.*

At the NATO level, the NATO Working Group of Financial Controllers, with the support of the NATO Head of Financial Reporting Policy, has established a working group to promulgate best practices; the Agency will be an active participant in these meetings.

### **Control over the preparation of the Financial Statements**

The Agency has implemented controls to ensure that the financial statements reflect accurate and complete financial information pertaining to the Agency before issuance to the IBAN.

The Agency's Financial Controller lacks access to financial data at a number of the CEPS National Organisations whose data form part of the Financial Statements.

Going forward in 2017, the Financial Controller plans to work with National Organisations to increase his access to critical financial accounting and financial reporting data.

### **Control over financial management**

We believe that strong controls exist over financial management functions such as treasury functions, accounts payable and receivable. While the Agency manages significant sums of money on behalf of its customers, these are controlled and backed by financial commitments. While the Agency has uncollected debts, these are controlled through regular review and dealings with customers.

### **Risk Management**

The Agency is required to have risk management processes in place by:

- The NSPO Charter, which states that the ASB will "ensure that effective risk management measures are in place and monitor performance execution on that basis";
- The NATO Financial Regulations, which require that Heads of NATO bodies shall ensure effective, efficient and economical risk management procedures are in place to support the achievement of objectives as set by the Nations, and shall identify, assess and mitigate the risks to the achievement of these objectives.;
- ISO 9001:2015, which requires a comprehensive risk management culture across the Agency;

- AQAP 2110 D(2016) NATO Quality Assurance requirements for design, developments and production, which mandates adhering to ISO31000; and,
- NATO 2005 Guidelines on Corporate Governance.

In 2015, Agency management issued an internal operating instruction dealing with Risk Management. This instruction introduced Enterprise Risk Management (ERM) to the Agency, which is the internal process of identifying, analysing and managing risks. The operating instruction provides the methodology for mitigating risk at every level within the Agency.

The Agency's Executive Management Board will review current risks and approve and monitor proposed risk reduction action plans on a quarterly basis. In exceptional circumstances, key and emerging risks will be highlighted to the Executive Management Board if the identified risk exceeds acceptable limits.

NSPA management provides annual updates to the ASB which highlight to those charged with its governance the top risks faced by the Agency. At the December 2016 meeting of the ASB, Agency management highlighted its top 6 risks as:

1. Cyber security
2. Physical security
3. Continuity of operations
4. Continued relevance
5. Compliance
6. Inadequate resourcing

Currently the Agency is focusing its efforts on capturing Agency Risks from the bottom-up and is using the approach on a pilot programme. Progress is unfortunately slower than anticipated due to the limited resources allocated to this work; however, the Agency aims to meet a 2018 target for implementing the risk management requirements of the NATO Financial Regulations ISO 9001 and AQAP 2110.



## Internal Audit

Internal Audit's role is to provide assurance to management that internal controls are designed appropriately and operating effectively. Internal audit is not an internal control in itself but provides independent assurance on internal control.

Internal Audit undertakes its activities based on a risk based methodology which is still maturing; this is because a risk-based approach is partly dependent on an embedded risk management approach across the Agency and this is still in the process of implementation. Since January 2017 and in accordance with the NATO Financial Regulations, the Agency has implemented an Audit Advisory Panel which will meet four times a year and report its findings to the General Manager

### Statement of the General Manager and the Financial Controller

All internal controls have inherent limitations, including the possibility of circumvention, and therefore can provide only reasonable assurance. Further, because of changing conditions, the effectiveness of internal controls may vary over time.

Based on the above, we consider, to the best of our knowledge and information, that the Agency operated satisfactory systems of internal control for the year ended 31 December 2016 and up to the date of approval of the financial statements, in respect of:

- safeguarding assets;
- promoting operational efficiency; and
- verifying the accuracy and reliability of accounting data and records.

We are currently unable to attest that the Agency is:

- complying consistently with all established managerial and command policies.

While the Agency has not complied consistently with all established managerial and command policies, it is committed to, and working hard in the area of ensuring that all personnel are aware of policies and are implementing them in their work.



**General Manager**

**31 March 2017**



**Acting Financial Controller**

**31 March 2017**

## NSPO Statement of Financial Position

*As of 31 December*  
*(all figures are in Euro '000)*

|                                    |      | NSPO TOTAL       |                  |                  |
|------------------------------------|------|------------------|------------------|------------------|
|                                    |      | Restated         |                  | Original         |
|                                    | Note | 2016             | 2015             | 2015             |
| <b>Current Assets</b>              |      |                  |                  |                  |
| Cash and Cash Equivalents          | 2    | 2,443,042        | 2,204,215        | 2,204,215        |
| Accounts Receivable                | 6    | 1,079,113        | 1,045,664        | 1,045,954        |
| Prepayments                        | 7    | 226,406          | 196,094          | 196,094          |
| <b>Long Term Receivables</b>       |      | 6,531            | 9,354            | 9,354            |
| <b>Inventory</b>                   | 5    | 364,878          | 362,641          | 362,641          |
| <b>Fixed and Intangible Assets</b> |      |                  |                  |                  |
| Property Plant and Equipment       | 3    | 741,140          | 605,119          | 503,383          |
| Intangible Assets                  | 4    | 24,491           | 21,624           | 21,624           |
| <b>Total Assets</b>                |      | <b>4,885,601</b> | <b>4,444,711</b> | <b>4,343,265</b> |
| <b>Current Liabilities</b>         |      |                  |                  |                  |
| Accounts Payable and Accruals      | 8    | 396,920          | 401,472          | 400,756          |
| Customer Advances                  | 9    | 3,318,346        | 3,022,753        | 3,023,759        |
| <b>Provisions</b>                  | 16   | 6,845            | 6,872            | 6,872            |
| <b>Total Liabilities</b>           |      | <b>3,722,111</b> | <b>3,431,097</b> | <b>3,431,387</b> |
| <b>Net Assets</b>                  |      | <b>1,163,490</b> | <b>1,013,614</b> | <b>911,878</b>   |

**Restatement:** Further details on 2015 comparative “Restated” figure restatements can be found within the Accounting Policies (page 17) and in Note 23 (pages 40 to 42).

The financial statements on pages 10 to 51 were issued to the International Board of Auditors for NATO on 31 March 2017.

  
NSPA General Manager

  
NSPA Acting Financial Controller

## NSPO Segments' Statement of Financial Position

As of 31 December  
(all figures are in Euro '000)

|                                    |      | Chairperson's Office |          | Log Ops          |                  | NAM            |                | CEPS           |                | Inter-business<br>unit<br>eliminations * | NSPO TOTAL       |                  |                  |
|------------------------------------|------|----------------------|----------|------------------|------------------|----------------|----------------|----------------|----------------|--|------------------|------------------|------------------|
|                                    | Note | 2016                 | 2015     | 2016             | 2015             | 2016           | 2015           | 2016           | 2015           | 2016                                     | 2016             | 2015             | Original<br>2015 |
| <b>Current Assets</b>              |      |                      |          |                  |                  |                |                |                |                |  |                  |                  |                  |
| Cash and Cash Equivalents          | 2    | 0                    | 0        | 2,044,302        | 1,799,143        | 216,381        | 237,621        | 182,359        | 167,451        | 0  | 2,443,042        | 2,204,215        | 2,204,215        |
| Accounts Receivable                | 6    | 0                    | 0        | 1,052,313        | 1,006,768        | 6,691          | 14,612         | 22,692         | 24,284         | (2,583)                                  | 1,079,113        | 1,045,664        | 1,045,954        |
| Prepayments                        | 7    | 0                    | 0        | 69,994           | 55,850           | 156,339        | 140,190        | 73             | 54             | 0  | 226,406          | 196,094          | 196,094          |
| <b>Long Term Receivables</b>       |      | 0                    | 0        | 3,857            | 3,857            | 0              | 0              | 2,674          | 5,497          | 0  | 6,531            | 9,354            | 9,354            |
| <b>Inventory</b>                   | 5    | 0                    | 0        | 355,958          | 355,090          | 2,538          | 1,207          | 6,382          | 6,344          | 0  | 364,878          | 362,641          | 362,641          |
| <b>Fixed and Intangible Assets</b> |      |                      |          |                  |                  |                |                |                |                |  | 0                |                  |                  |
| Property Plant and Equipment       | 3    | 0                    | 0        | 114,102          | 12,702           | 494,798        | 479,410        | 132,240        | 113,007        | 0  | 741,140          | 605,119          | 503,383          |
| Intangible Assets                  | 4    | 0                    | 0        | 0                | 0                | 22,118         | 19,052         | 2,373          | 2,572          | 0  | 24,491           | 21,624           | 21,624           |
| <b>Total Assets</b>                |      | <b>0</b>             | <b>0</b> | <b>3,640,526</b> | <b>3,233,410</b> | <b>898,865</b> | <b>892,092</b> | <b>348,793</b> | <b>319,209</b> | <b>(2,583)</b>                           | <b>4,885,601</b> | <b>4,444,711</b> | <b>4,343,265</b> |
| <b>Current Liabilities</b>         |      |                      |          |                  |                  |                |                |                |                |  | 0                |                  |                  |
| Accounts Payable and Accruals      | 8    | 0                    | 0        | 326,476          | 360,393          | 54,847         | 21,114         | 18,180         | 19,965         | (2,583)                                  | 396,920          | 401,472          | 400,756          |
| Customer Advances                  | 9    | 0                    | 0        | 2,811,357        | 2,479,475        | 322,096        | 372,829        | 184,893        | 170,449        | 0  | 3,318,346        | 3,022,753        | 3,023,759        |
| <b>Provisions</b>                  | 16   | 0                    | 0        | 2,120            | 0                | 0              | 0              | 4,725          | 6,872          | 0  | 6,845            | 6,872            | 6,872            |
| <b>Total Liabilities</b>           |      | <b>0</b>             | <b>0</b> | <b>3,139,953</b> | <b>2,839,868</b> | <b>376,943</b> | <b>393,943</b> | <b>207,798</b> | <b>197,286</b> | <b>(2,583)</b>                           | <b>3,722,111</b> | <b>3,431,097</b> | <b>3,431,387</b> |
| <b>Net Assets</b>                  |      | <b>0</b>             | <b>0</b> | <b>500,573</b>   | <b>393,542</b>   | <b>521,922</b> | <b>498,149</b> | <b>140,995</b> | <b>121,923</b> | <b>0</b>                                 | <b>1,163,490</b> | <b>1,013,614</b> | <b>911,878</b>   |

**Restatement:** Further details on 2015 comparative "Restated" figure restatements are found within the Accounting Policies (page 17) and in Note 23 (pages 40-42).

\* Inter-Business Unit Eliminations are already incorporated within the relevant Business Unit for 2015; details of eliminations relevant to the respective Business Unit for 2016 can be found in Note 12 (page 31)

The financial statements on pages 10 to 51 were issued to the International Board of Auditors for NATO on 31 March 2017.

  
NSPA General Manager

  
NSPA Acting Financial Controller

## NSPO Statement of Financial Performance

*For the year-ended 31 December  
(all figures are in Euro '000)*

|   |      | NSPO TOTAL         |                    |                    |
|---|------|--------------------|--------------------|--------------------|
|   |      | Restated           |                    | Original           |
| Revenue                                 | Note | 2016               | 2015               | 2015               |
| Services and Support to Customers       |      | 2,274,332          | 2,315,157          | 2,314,178          |
| Administrative Support                  |      | 144,265            | 149,170            | 148,811            |
| Bank interest                           |      | 291                | 621                | 621                |
| Unrealised foreign currency effects     | 10   | (441)              | 3,036              | 3,036              |
| Miscellaneous Revenue                   |      | 5,129              | 6,157              | 6,157              |
| <b>Total Revenue</b>                    |      | <b>2,423,576</b>   | <b>2,474,141</b>   | <b>2,472,803</b>   |
| <b>Expenses</b>                         |      |                    |                    |                    |
| Services and Support to Customers       | 11   | (2,100,744)        | (2,140,140)        | (2,141,233)        |
| Commercial Discounts Earned *           |      | 3,833              | 3,813              | 3,813              |
| USA Foreign Military Sales **           | 11   | (84,884)           | (96,806)           | (96,806)           |
| Personnel                               | 13   | (160,085)          | (166,375)          | (165,682)          |
| Depreciation and Amortisation           |      | (41,064)           | (37,015)           | (33,198)           |
| Provisions                              |      | (2,120)            | (2,617)            | (2,617)            |
| Other Expenses                          | 11   | (49,365)           | (50,598)           | (50,239)           |
| Transfers to customer credits           |      | (29,907)           | (20,028)           | (18,649)           |
| <b>Total Expenses</b>                   |      | <b>(2,464,336)</b> | <b>(2,509,766)</b> | <b>(2,504,611)</b> |
| <b>Surplus / (Deficit) for the year</b> |      | <b>(40,760)</b>    | <b>(35,625)</b>    | <b>(31,808)</b>    |

**Restatement:** Further details on 2015 comparative “Restated” figure restatements are found within the Accounting Policies (page 17) and in Note 23 (pages 40 to 42)

\* “Commercial discounts Earned” reduce the costs incurred in delivering “Services and Support to Customer”.

\*\* The figure given in respect of USA Foreign Military Sales are presented on a “modified cash” (i.e. non-accruals) basis; more information can be found in the Accounting Policies (see page 19).

## NSPO Segments' Statement of Financial Performance

For the year-ended 31 December  
(all figures are in Euro '000)

|   |      | Chairperson's Office |              | Log Ops            |                    | NAM              |                  | CEPS             |                  | Inter-business<br>unit<br>eliminations | NSPO TOTAL         |                    |                    |
|---|------|----------------------|--------------|--------------------|--------------------|------------------|------------------|------------------|------------------|--|--------------------|--------------------|--------------------|
|   |      |                      |              |                    |                    |                  |                  | Restated         |                  |  | Restated           |                    | Original           |
| Revenue                                 | Note | 2016                 | 2015         | 2016               | 2015               | 2016             | 2015             | 2016             | 2015             | 2016                                   | 2016               | 2015               | 2015               |
| Services and Support to Customers       |      | 0                    | 0            | 2,035,498          | 2,124,395          | 123,345          | 77,564           | 115,779          | 113,198          | (290)                                  | 2,274,332          | 2,315,157          | 2,314,178          |
| Administrative Support                  |      | 754                  | 850          | 124,646            | 123,961            | 6,614            | 9,554            | 14,735           | 14,805           | (2,484)                                | 144,265            | 149,170            | 148,811            |
| Bank interest                           |      | 0                    | 0            | 20                 | 0                  | 0                | 0                | 271              | 621              | 0                                      | 291                | 621                | 621                |
| Unrealised foreign currency effects     | 10   | 0                    | 0            | (612)              | 3,580              | 171              | (544)            | 0                | 0                | 0                                      | (441)              | 3,036              | 3,036              |
| Miscellaneous Revenue                   |      | 0                    | 0            | 0                  | 0                  | 0                | 0                | 5,130            | 6,157            | (1)                                    | 5,129              | 6,157              | 6,157              |
| <b>Total Revenue</b>                    |      | <b>754</b>           | <b>850</b>   | <b>2,159,552</b>   | <b>2,251,936</b>   | <b>130,130</b>   | <b>86,574</b>    | <b>135,915</b>   | <b>134,781</b>   | <b>(2,775)</b>                         | <b>2,423,576</b>   | <b>2,474,141</b>   | <b>2,472,803</b>   |
| <b>Expenses</b>                         |      |                      |              |                    |                    |                  |                  |                  |                  |  | 0                  |                    |                    |
| Services and Support to Customers       | 11   | 0                    | 0            | (2,009,079)        | (2,080,099)        | (59,541)         | (26,704)         | (32,414)         | (33,337)         | 290                                    | (2,100,744)        | (2,140,140)        | (2,141,233)        |
| Commercial Discounts Earned *           |      | 0                    | 0            | 3,817              | 3,795              | 0                | 0                | 16               | 18               | 0                                      | 3,833              | 3,813              | 3,813              |
| USA Foreign Military Sales **           | 11   | 0                    | 0            | (23,532)           | (45,837)           | (61,352)         | (50,969)         | 0                | 0                | 0                                      | (84,884)           | (96,806)           | (96,806)           |
| Personnel                               | 13   | (694)                | (768)        | (96,753)           | (97,340)           | (3,763)          | (4,255)          | (58,875)         | (64,012)         | 0                                      | (160,085)          | (166,375)          | (165,682)          |
| Depreciation and Amortisation           |      | 0                    | 0            | (5,199)            | (5,454)            | (28,189)         | (25,741)         | (7,676)          | (5,820)          | 0                                      | (41,064)           | (37,015)           | (33,198)           |
| Provisions                              |      | 0                    | 0            | (2,120)            | 0                  | 0                | 0                | 0                | (2,617)          | 0                                      | (2,120)            | (2,617)            | (2,617)            |
| Other Expenses                          | 11   | (60)                 | (82)         | (31,752)           | (30,520)           | (5,303)          | (5,191)          | (14,735)         | (14,805)         | 2,485                                  | (49,365)           | (50,598)           | (50,239)           |
| Transfers to customer credits           |      | 0                    | 0            | 0                  | 0                  | 0                | 0                | (29,907)         | (20,028)         | 0                                      | (29,907)           | (20,028)           | (18,649)           |
| <b>Total Expenses</b>                   |      | <b>(754)</b>         | <b>(850)</b> | <b>(2,164,618)</b> | <b>(2,255,455)</b> | <b>(158,148)</b> | <b>(112,860)</b> | <b>(143,591)</b> | <b>(140,601)</b> | <b>2,775</b>                           | <b>(2,464,336)</b> | <b>(2,509,766)</b> | <b>(2,504,611)</b> |
| <b>Surplus / (Deficit) for the year</b> |      | <b>0</b>             | <b>0</b>     | <b>(5,066)</b>     | <b>(3,519)</b>     | <b>(28,018)</b>  | <b>(26,286)</b>  | <b>(7,676)</b>   | <b>(5,820)</b>   | <b>0</b>                               | <b>(40,760)</b>    | <b>(35,625)</b>    | <b>(31,808)</b>    |

**Restatement:** Further details on 2015 comparative "Restated" figure restatements are found within the Accounting Policies (page 17) and in Note 23 (pages 40 to 42)

Inter-Business Unit Eliminations are already incorporated within the relevant Business Unit for 2015; details of eliminations relevant to the respective Business Unit for 2016 can be found in Note 12 (page 31)

\* "Commercial discounts Earned" reduce the costs incurred in delivering "Services and Support to Customer".

\*\* The figure given in respect of USA Foreign Military Sales are presented on a "modified cash" (i.e. non-accruals) basis; more information can be found in the Accounting Policies (see page 19).

## NSPO Cash Flow Statement for the year-ended 31 December

|   | 2016                    | 2015                    |
|---|-------------------------|-------------------------|
|   |                         | Restated                |
| <b>Cash Flows from Operating Activities</b>             |                         |                         |
| Cash Receipts from Customers                            | 2,687,521,200.80        | 2,650,165,687.77        |
| Bank Interest Received                                  | 4,723,609.06            | 4,841,359.71            |
| Cash Paid to Suppliers                                  | (2,321,477,058.15)      | (2,225,032,092.12)      |
| Cash Paid to Employees and on behalf of                 | (154,850,395.61)        | (156,261,343.37)        |
| Net Other Payments and Receipts                         | 41,290,641.00           | (17,254,011.97)         |
| <b>Net Cash Flows from Operating Activities</b>         | <b>257,207,997.11</b>   | <b>256,459,600.02</b>   |
| <b>Cash Flows from Investing Activities</b>             |                         |                         |
| Net purchase of PPE, Intangible Assets and Inventory    | (148,738,225.94)        | (49,937,057.75)         |
| <b>Net Cash Flows from Investing Activities</b>         | <b>(148,738,225.94)</b> | <b>(49,937,057.75)</b>  |
| <b>Cash Flows from Financing Activities</b>             |                         |                         |
| Net proceeds from borrowings                            | (654,843.56)            | 654,843.56              |
| Capital Contributed by Countries                        | 121,260,285.63          | 30,974,101.09           |
| <b>Net Cash Flows from Financing Activities</b>         | <b>120,605,442.07</b>   | <b>31,628,944.65</b>    |
| <b>Foreign currency effects</b>                         | <b>9,751,604.52</b>     | <b>30,797,063.75</b>    |
| <b>Cash and Cash Equivalents at Beginning of Period</b> | <b>2,204,215,122.95</b> | <b>1,935,266,572.28</b> |
| Net Increase/(Decrease) in Cash and Cash Equivalents    | 238,826,817.76          | 268,948,550.67          |
| <b>Cash and Cash Equivalents at End of Period</b>       | <b>2,443,041,940.70</b> | <b>2,204,215,122.95</b> |

**Restatement:** 2015 comparative figures have been restated and are not directly comparable to those in the 2015 Financial Statements because the basis of preparation has changed from the “indirect method” to the “direct method” of cash flows. Further details can be found within the Accounting Policies (pages 17) and in Note 23 (pages 40 to 42).

## NSPO Statement of Changes in Net Assets

| NSPO  | Capital contributions | Revaluation Reserves | Other Reserves | Accumulated surplus/deficit | Total            |
|---|-----------------------|----------------------|----------------|-----------------------------|------------------|
| Balance at the end of 2015                            | 874,128               | 2,880                | 34,870         | 0                           | 911,878          |
| Changes in accounting policy                          | 101,724               | 12                   | 0              | 0                           | 101,736          |
| <b>Balance at 31 December 2015</b>                    | <b>975,852</b>        | <b>2,892</b>         | <b>34,870</b>  | <b>0</b>                    | <b>1,013,614</b> |
| Net gains/(losses) recognised directly in net assets  | 146,817               | (83)                 | 23,984         | 0                           | 170,718          |
| Depreciation and Amortisation                         | (41,064)              | 0                    | 0              | 41,064                      | 0                |
| Exchange difference on translating foreign operations | 17,791                | 0                    | (20)           | 0                           | 17,771           |
| Net Unrealised Foreign exchange gains and losses      | 0                     | 0                    | (441)          | 441                         | 0                |
| Inventory disposals, donations and increases          | 0                     | 0                    | 866            | (866)                       | 0                |
| Inventory sales                                       | 0                     | 0                    | 2,026          | (2,026)                     | 0                |
| Surplus/(deficit) for the period *                    | 0                     | 0                    | 0              | (38,613)                    | (38,613)         |
| <b>Change in net assets for the year ended 2016</b>   | <b>123,544</b>        | <b>(83)</b>          | <b>26,415</b>  | <b>0</b>                    | <b>149,876</b>   |
| <b>Balance at 31 December 2016</b>                    | <b>1,099,396</b>      | <b>2,809</b>         | <b>61,285</b>  | <b>0</b>                    | <b>1,163,490</b> |

| Log Ops Business Unit                                 | Capital contributions | Revaluation Reserves | Other Reserves | Accumulated surplus/deficit | Total          |
|---|-----------------------|----------------------|----------------|-----------------------------|----------------|
| Balance at the end of 2015                            | 357,825               | 0                    | 35,717         | 0                           | 393,542        |
| Changes in accounting policy                          | 0                     | 0                    | 0              | 0                           | 0              |
| <b>Balance at 31 December 2015</b>                    | <b>357,825</b>        | <b>0</b>             | <b>35,717</b>  | <b>0</b>                    | <b>393,542</b> |
| Net gains/(losses) recognised directly in net assets  | 85,966                | 0                    | 23,984         | 0                           | 109,950        |
| Depreciation and Amortisation                         | (5,199)               | 0                    | 0              | 5,199                       | 0              |
| Exchange difference on translating foreign operations | 0                     | 0                    | 0              | 0                           | 0              |
| Net Unrealised Foreign exchange gains and losses      | 0                     | 0                    | (612)          | 612                         | 0              |
| Inventory disposals, donations and increases          | 0                     | 0                    | 866            | (866)                       | 0              |
| Inventory sales                                       | 0                     | 0                    | 2,026          | (2,026)                     | 0              |
| Surplus/(deficit) for the period *                    | 0                     | 0                    | 0              | (2,919)                     | (2,919)        |
| <b>Change in net assets for the year ended 2016</b>   | <b>80,767</b>         | <b>0</b>             | <b>26,264</b>  | <b>0</b>                    | <b>107,031</b> |
| <b>Balance at 31 December 2016</b>                    | <b>438,592</b>        | <b>0</b>             | <b>61,981</b>  | <b>0</b>                    | <b>500,573</b> |

\* The Surplus/(deficit) for the year also included Euro 19k which was allocated to "Customer and replenishment credits (allocated or to be allocated)" (see Note 9), and a "Provision for Bad and Doubtful Debts" of Euro 2,120k, which do not impact upon Net Assets.

## NSPO Statement of Changes in Net Assets (continued)

| NAMP Business Unit                                    | Capital contributions | Revaluation Reserves | Other Reserves | Accumulated surplus/deficit | Total          |
|---|-----------------------|----------------------|----------------|-----------------------------|----------------|
| Balance at the end of 2015                            | 498,996               | 0                    | (847)          | 0                           | 498,149        |
| Changes in accounting policy                          | 0                     | 0                    | 0              | 0                           | 0              |
| <b>Balance at 31 December 2015</b>                    | <b>498,996</b>        | <b>0</b>             | <b>(847)</b>   | <b>0</b>                    | <b>498,149</b> |
| Net gains/(losses) recognised directly in net assets  | 34,020                | 0                    | 0              | 0                           | 34,020         |
| Depreciation and Amortisation                         | (28,189)              | 0                    | 0              | 28,189                      | 0              |
| Exchange difference on translating foreign operations | 17,791                | 0                    | (20)           | 0                           | 17,771         |
| Net Unrealised Foreign exchange gains and losses      | 0                     | 0                    | 171            | (171)                       | 0              |
| Inventory disposals, donations and increases          | 0                     | 0                    | 0              | 0                           | 0              |
| Inventory sales                                       | 0                     | 0                    | 0              | 0                           | 0              |
| Surplus/(deficit) for the period *                    | 0                     | 0                    | 0              | (28,018)                    | (28,018)       |
| <b>Change in net assets for the year ended 2016</b>   | <b>23,622</b>         | <b>0</b>             | <b>151</b>     | <b>0</b>                    | <b>23,773</b>  |
| <b>Balance at 31 December 2016</b>                    | <b>522,618</b>        | <b>0</b>             | <b>(696)</b>   | <b>0</b>                    | <b>521,922</b> |

| CEPS Business Unit                                    | Capital contributions | Revaluation Reserves | Other Reserves | Accumulated surplus/deficit | Total          |
|---|-----------------------|----------------------|----------------|-----------------------------|----------------|
| Balance at the end of 2015                            | 17,307                | 2,880                | 0              | 0                           | 20,187         |
| Changes in accounting policy                          | 101,724               | 12                   | 0              | 0                           | 101,736        |
| <b>Balance at 31 December 2015</b>                    | <b>119,031</b>        | <b>2,892</b>         | <b>0</b>       | <b>0</b>                    | <b>121,923</b> |
| Net gains/(losses) recognised directly in net assets  | 26,831                | (83)                 | 0              | 0                           | 26,748         |
| Depreciation and Amortisation                         | (7,676)               | 0                    | 0              | 7,676                       | 0              |
| Exchange difference on translating foreign operations | 0                     | 0                    | 0              | 0                           | 0              |
| Net Unrealised Foreign exchange gains and losses      | 0                     | 0                    | 0              | 0                           | 0              |
| Inventory disposals, donations and increases          | 0                     | 0                    | 0              | 0                           | 0              |
| Inventory sales                                       | 0                     | 0                    | 0              | 0                           | 0              |
| Surplus/(deficit) for the period *                    | 0                     | 0                    | 0              | (7,676)                     | (7,676)        |
| <b>Change in net assets for the year ended 2016</b>   | <b>19,155</b>         | <b>(83)</b>          | <b>0</b>       | <b>0</b>                    | <b>19,072</b>  |
| <b>Balance at 31 December 2016</b>                    | <b>138,186</b>        | <b>2,809</b>         | <b>0</b>       | <b>0</b>                    | <b>140,995</b> |



# Accounting Policies

## Basis of preparation

These financial statements have been prepared in accordance with the NATO Accounting Framework as adopted by the NATO Council.

The NATO Accounting Framework is based upon International Public Sector Accounting Standards (IPSAS). IPSAS 12 – Inventories, IPSAS 17 - Property, Plant and Equipment and IPSAS 31 - Intangible Assets were adapted by the North Atlantic Council (the “Council”) in August 2013 for reporting periods beginning on 1 January 2013. IPSAS 1 – Presentation of Financial Statements, was adapted the Council in April 2016 and was applied by the Agency from its 2015 Financial Statements.

The Financial Statements are prepared on the going-concern basis which means that those charged with the governance of NSPO and its integral Programmes and Support and/or Procurement Partnerships consider that NSPO will continue in existence for at least a year from the date the financial statements are issued.

The preparation of financial statements in compliance with the NATO Accounting Framework requires the use of certain critical accounting estimates and requires that those responsible for preparing and presenting the financial statements of NSPO use judgement in applying these accounting policies. The areas where significant judgements and estimates have been made in preparing the financial statements and their effect are disclosed in the Note 1 to the financial statements.

## Changes in Accounting Policies to correct errors

The following changes in accounting policy were required to correct errors stemming from the audit of the 2015 Financial Statements. These changes in accounting policy have been applied to the comparative figures for 2015 which have been restated:

### **1. Capitalisation of CEPS Pipeline Property, Plant and Equipment and Intangible Assets**

In light of an anticipated Council decision to capitalise the Central Europe Pipeline System’s assets and liabilities, and to reflect its associated revenues and expenses, NSPO included the Pipelines System’s revenues and expenses in the Financial Statements of 2015, and from the 2016 financial year has capitalised the Pipeline System Property, Plant and Equipment and Intangible Assets.

### **2. Method underpinning cash flow statement**

*IPSAS 2 – Cash Flow Statements* allows the choice between presenting the cash flow statement based on the direct method or indirect method. In 2015 the Agency presented the Cash Flow Statement according to the indirect method; however it was unable to do this successfully and this led to a qualification of the 2015 Financial Statements. In 2016, the Agency has changed its accounting policy to present the cash flow statement according to the direct method.

More information in respect of how changes in Accounting Policies have affected comparative year figures is shown in *Note 23 - Restatements of 2015 Financial Statements due to the correction of prior period errors*.

Another error in the 2015 Financial Statements in relation to the inability to reconcile depreciation and amortisation amounts in the PPE and intangible Assets is still in the process of implementation.

### **Other Changes in Accounting Policies: Provisions for bad and doubtful debts**

In previous years, provisions for bad and doubtful debts were only made once a legal process was started against a debtor and this was limited to only private sector entities; no provisions were made against national customer debts, as they were always deemed collectable.

From 2016 going forward, the Agency will also make provisions for bad and doubtful debts for national customer debts in exceptional circumstances when it considers the reimbursement of debts cannot be made by national customers (see Note 16 for further information).

This change in accounting policy does not affect 2015 comparative figures

#### **Other restatements in respect of the 2015 Financial Statements**

The CEPS Business Unit's German National Organisation has reviewed historical accounting data and made a number of restatements to correct historical errors and omissions. Further details can be found in Note 23.

#### **Deviation from IPSAS 12 - Inventories (as adapted by the North Atlantic Council)**

NSPO holds strategic stocks on behalf of its customers which often, due to their nature, are slow moving. NSPA management, with the approval of the ASB, has chosen to value these stocks on the weighted average cost (WAC).

#### **Basis of consolidation**

The Agency Supervisory Board (ASB) considers that the consolidated financial statements of NSPO present the results of NSPO and its segment parts as a single entity. The ASB controls segment parts of the NSPO through its Charter. Inter-business unit transactions and balances between NSPO segment parts are therefore eliminated in full at both the consolidation level and the relevant segment level.

#### **Segment Reporting**

A segment is a distinguishable activity or group of activities of an entity for which it is appropriate to separately report financial information for the purpose of (a) evaluating the entity's past performance in achieving its objectives and (b) making decisions about the future allocation of resources. In the primary statements NSPO discloses its performance and position by the following segments: Chairperson's Office, Log Ops Business Unit, CEPS Programme Business Unit and NAM Programme Business Unit.

#### **Changes in Accounting Standards**

At the end of the 2016 financial year, the following IPSAS had been issued which will become effective in future financial years:

- IPSAS 33 - First-time Adoption of Accrual Basis IPSASs
- IPSAS 34 - Separate Financial Statements
- IPSAS 35 - Consolidated Financial Statements
- IPSAS 36 - Investments in Associates and Joint Ventures
- IPSAS 37 - Joint Arrangements
- IPSAS 38 - Disclosure of Interests in Other Entities
- IPSAS 39 – Employee Benefits
- IPSAS 40 - Public Sector Combinations

When these standards do become effective, the Agency does not consider that they shall impact on NSPO's financial reporting.

#### **Revenue Recognition**

NSPO Financial Statements are prepared on the accruals' basis of accounting. The effects of transactions (transfer of property of goods or services and others) are recognised when they occur (not only when cash is received) and they are recorded as revenues in the fiscal year to which they relate. For the contributions, the revenue is recognized when called.

The expensed amount of the contributions received from the member Nations is indicated in the Statement of Financial Performance, as it is a source of funds. The non-expensed portion of revenue is accounted for as deferred revenue.

The contributions called in the current year, for the following year are recognized as contributions called in advance, and only accounted for as revenue in the following year.

Income received for the purchase of PPE, intangible assets and inventory does not pass through the Statement of Financial Performance, but is reflected directly in Net Assets.

### Revenue measurement and timing

Revenue for goods and services delivered is recognised when NSPO segments have transferred the significant risks and rewards of ownership and it is probable that NSPO segments will receive the previously agreed upon payment for delivering goods and services. These criteria are considered to be met when the goods or services are delivered meeting the customers' requirements. For all segments other than Log Ops, revenue is recognised at the moment an expense is incurred as the revenue is guaranteed to be funded by member nations.

### Foreign Military Sales

In accordance with the NATO Accounting Framework's adaption of *IPSAS 1 - Presentation of Financial Statements*, the Agency reports data on a modified cash basis where the Agency is unable to satisfy itself that the data is presented on a reliable accrual basis.

### **Expenses Recognition**

Expenses are recognized when the transaction or event causing the expense occurs regardless of the timing of the payment, in accordance with accrual basis principle.

### **Financial Plan Execution**

*IPSAS 24 - Presentation of Budget Information in Financial Statements* applies to public sector entities which are required or elect to make their approved budgets publically available.

NSPO does not make its approved financial plans publicly available; NSPO is not therefore required to follow IPSAS 24. Instead, NSPO presents a high-level summary of the financial plan execution of its main segments as well as for the parts of its projects which are funded jointly or commonly by more than one national customer.

### **Foreign currency**

Transactions entered into by NSPO segments in a currency other than the currency of the primary economic environment in which they operate (their "functional currency"; which is Euro for all segments of the NSPO except for the NAM Programme and some Log Ops projects where it is USD) are recorded at the

exchange rates ruling when the transactions occur. The use of exchange rates does not materially impact the financial statements.

For all segments of NSPO, except the CEPS Programme, the ruling exchange rate is set in SAP and is only adjusted in SAP when there is a movement of 2.25 per cent or more against the reporting currency. The CEPS Programme uses ruling exchange rates set by NATO Headquarters in Brussels which are updated on a weekly basis.

Foreign currency assets and liabilities are translated at the rates ruling at the reporting date. For all parts of NSPO, except the CEPS Programme, the ruling exchange rate is that of the European Central Bank. The CEPS Programme uses rates set by the NATO Headquarters.

Unrealised foreign currency exchange differences arising on the translation of monetary assets and liabilities are recognised immediately in the Statement of Financial Performance.

The functional currency of the NAM Programme is USD. The financial performance and financial position of the NAM Programme are recorded in the NSPO financial statements by:

- translating assets and liabilities on opening and closing reporting dates at the respective exchange rates ruling at the date of the statement of financial position (2016: 1.0541 USD to Euro, 2015: 1.0887 USD to Euro);
- translating its revenue and expenses into Euros at the average yearly exchange rates for the Euro relative to the USD (2016: 1.1069 USD to Euro, 2015: 1.1095 USD to Euro).

### **Current Assets:**

#### **Cash and Cash Equivalents**

NSPO holds cash and cash equivalents in financial institutions as current and time deposits accounts, and certificates of deposits, and at the Agency in petty cash and cash on hand for operational requirements. These cash balances are held in Euro, US dollar and Hungarian Forint.

### **Prepayments**

When the Agency makes advance payments to vendors and employees these are reflected as prepayments in the Statement of Financial Position.

## Inventories

IPSAS allows different types of inventory to be valued on different basis; each segment of NSPO can hold different types of inventory.

- For the Log Ops segment most inventories are recognised at weighted average cost (the “WAC”). The exception is fuel which is measured at current replacement cost and Patriot Programme operational inventories maintained at a contractor premise which are valued at historical cost.
- NAM Programme inventories are measured on a First-In, First-Out (FIFO) basis.
- CEPS Programme inventories are measured on a weighted average cost (the “WAC”) basis.

Capitalisation thresholds for all inventory are Euro nil.

## Non-current Assets:

Income received for the purchase of PPE, intangible assets and inventory does not pass through the Statement of Financial Performance, but is reflected directly as Capital Contributed in Net Assets.

## Property, Plant and Equipment (PPE)

NSPO follows the NATO Accounting Framework for PP&E, which uses an adaption of IPSAS 17 for its accounting treatment.

PP&E is valued at initial cost less accumulated depreciation. Any subsequent expenditure on the asset, which enhances its value, is included in the amount. The only exception is the CEPS Program Office building at [REDACTED], which was revalued at fair market value (FMV).

Depreciation is calculated on a straight-line basis on all PP&E other than land.

The expected lives of PPE and their associated capitalisation thresholds per item are:

- Buildings – 40 Years, Euro 1,000 (USD 1,000 for NAMP Business Unit)
- Other Infrastructure – 40 Years, Euro 1,000 (USD 1,000 for NAMP Business Unit)

- Installed equipment – 10 Years, Euro 1,000 (USD 1,000 for NAMP Business Unit)
- Mission equipment – 10 Years, Euro 1,000 (USD 1,000 for NAMP Business Unit)
- Machinery – 10 years, Euro 1,000 (USD 1,000 for NAMP Business Unit)
- Vehicles – 5 Years, Euro 1,000 (USD 1,000 for NAMP Business Unit)
- Aircraft – 26 years, Euro 200k
- Furniture - 10 years, Euro 1,000 (USD 1,000 for NAMP Business Unit)
- Communications - 3 years, Euro 1,000 (USD 1,000 for NAMP Business Unit)
- Automated IT systems - 5 years, Euro 1,000 (USD 1,000 for NAMP Business Unit)
- Office Automation Equipment – 3 years, 1,000 (USD 1,000 for NAMP Business Unit)
- Pipeline System – 10 to 40 years depending on type of component, Euro 1,000

## PPE - Land and Buildings

The NSPO site at [REDACTED] is not controlled by NSPO. The CEPS Programme site at [REDACTED] is controlled by the CEPS Programme and parts of the NAM Programme site in [REDACTED] are controlled by the NAM Programme.

As NAM Programme was established for 26 years, this means the maximum useful economic life of Buildings and Other Infrastructure assets is limited to 2034 (26 years after the establishment of the programme).

Starting with the 2016 Financial Statements, NSPO has capitalised the additions made to the Central Europe Pipeline System since 1 January 2013.

## Externally acquired intangible assets

Externally acquired intangible assets represent information systems used by NSPO segments and the NAM Programme’s rights to a spare engine. They are recognised at cost and subsequently amortised on a straight-line basis over their useful economic lives.

The useful economic lives of information and communication systems are deemed to be 4 years.

The NAM Programme's rights to its spare engine are amortised over the life of the Aircraft, which is 26 years.

The NAM Programme re-values intangible assets in line with changes in the Euro relative to USD and HUF respectively.

### **Financial liabilities**

The financial liabilities of NSPO segments are accounts payables and accruals, and customer advances. They are measured at fair value. Changes in fair value are recognised in the Statement of Financial Performance.

### **Accounts Payable and Accruals**

Accounts Payable represent amounts for which goods and services, supported by an invoice, have been received at the year-end but which remain unpaid. Accruals represent amounts owing for goods and services, which are not supported yet by an invoice at the year-end.

### **Advances**

In order to ensure that customer requirements can be met, NSPO segments can call for money in advance of need. The advance is shown as an asset at the NSPO consolidated and segment level but is matched by a liability because, until the funds are used, they are owed back to the customer who provided the funding.

### **Retirement benefits: Defined contribution scheme**

Contributions to NATO defined contribution pension scheme are charged to the Statement of Financial Performance in the year to which they relate. NSPO segments are not exposed directly to any liabilities that may arise on the scheme and have no control over the assets of the scheme.

### **Retirement benefits: Defined benefit scheme**

Contributions to the NATO defined benefit pension scheme are charged to the Statement of Financial Performance in the year to which they relate. NSPO is not exposed directly to any liabilities that may arise on the scheme and has no control over the assets of the scheme.

### **Other long-term service benefits**

Employment of NATO civilian staff is governed by the NATO Civilian Personnel Regulations. Different rules apply depending on the circumstances of employment. Where there is a liability for potential long-term service benefits at the year-end they are described and disclosed in the notes to the financial statements.

### **Leased assets**

Where substantially all of the risks and rewards incidental to ownership of a leased asset have been transferred to NSPO segments (a "finance lease"), the asset is treated as if it had been purchased outright.

Where substantially all of the risks and rewards incidental to ownership are not transferred to NSPO segments (an "operating lease"), the total rentals payable under the lease are charged to the statement of financial performance on a straight-line basis over the lease term. Examples of operating leases can include photocopiers and cars.

### **Provisions**

NSPO segments recognise provisions for liabilities of uncertain timing or amount including those for legal disputes. The provision is measured at the best estimate of the expenditure required to settle the obligation at the reporting date.

### **Contingent Liabilities**

NSPO discloses in the notes to the financial statements any contingent liabilities common to the whole or specific to a project where:

- the NSPO segment is exposed to possible financial liabilities that arose from events which occurred before the year-end, and where the confirmation of the existence of the liability will only be known through the occurrence or non-occurrence of one or more uncertain future events not wholly within the organisation's control, or,
- the NSPO segment is exposed to a current financial liability which arose from events which occurred before the year-end where NSPO does not believe it will be required to pay for the financial liability, or, the amount of the financial liability cannot be measured with sufficient reliability.

### **Operating Surplus / (deficit) in the year**

Operating surpluses and deficits occur when non-budgeted expenses or revenues occur; of which examples are depreciation, changes in provisions, the sales and disposals of inventory, and the unrealised results of foreign exchange transactions

For the Log Ops and NAMP Business Units only, unrealised foreign currency translation effects impact the Statement of Financial Performance. Bank interest and realised foreign exchange effects “pass through” the Log Ops and NAMP Business Units only, and belong to customers, rather than NSPO, and hence do not affect revenue.

### **NSPO Net Assets**

Net Assets reflected in the Financial Statements represent the net assets of NSPO’s customers. These net assets comprise the capital contributed by customers to fund the acquisition of PPE, intangible assets and inventories. Capital contributed is reduced by the effects of depreciation and amortisation and can be increased or decreased due to the effects of currency translation effects.

## NOTES TO THE FINANCIAL STATEMENTS

### 1. Critical Accounting Estimates and Judgements

NSPO makes certain estimates and assumptions regarding the future. Estimates and judgements are continually evaluated based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. In the future, actual experience may differ from these estimates and assumptions. Some balances such as accruals and unbilled sales need to be assessed at the year-end to estimate the value of work and services delivered at the year-end. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below.

#### Estimates and assumptions

##### a) Revenue and expenditure recognition for goods and services delivered under the United States Foreign Military Sales Program

The Agency purchases goods and services through the United States Foreign Military Sales Program. On a quarterly basis, the United States Government provides the Agency with reports which detail goods and services delivered. The Agency reconciles the delivery of goods to these quarterly reports and is content that in respect of goods delivered the reports represent reliable accruals based accounting data.

NSPA management has chosen to account for the value of the services delivered based on the values provided in the reports, and which are based on cash payments made by the United States Government to contractors in the period. In 2016, the Agency expensed Euro 85m under this basis compared to Euro 97m in 2015.

##### b) NAMP Mission Costs

The costs of NAMP missions (e.g. Fuel and Airport Services) are made with the best estimates available at the time the financial statements are produced.

##### c) Accruals and cut-off date

Revised NATO Financial Regulations issued in May 2015 moved the date for the issuance of the NSPO Financial Statements for audit from 30 April after the financial year end to 31 March. This requires a subsequent bringing forward of the cut-off date for capturing year-end accruals supported by invoices and increased the need to estimate non-invoiced accruals after this cut-off date.

##### d) Legal proceedings both real and possible

In accordance with the NATO Accounting Framework, NSPO recognises a provision where there is a present obligation from a past event, a transfer of economic benefits is probable and the amount of costs of the transfer can be estimated reliably. In instances where the criteria are not met, a contingent liability may be disclosed in the notes to the financial statements. Obligations arising in respect of contingent liabilities that have been disclosed, or those which are not currently recognised or disclosed in the financial statements could have a material effect on NSPO's financial position.

Application of these accounting principles to legal cases requires NSPA's management to make determinations about various factual and legal matters beyond its control. The Agency reviews outstanding legal cases following developments in the legal proceedings and at each reporting date, in order to assess the need for provisions and disclosures in its financial statements. Among the factors considered in making decisions on provisions are the nature of litigation, claim or assessment, the legal process and potential level of damages in the jurisdiction in which the litigation, claim or assessment has been brought, the progress of the case (including the progress after the date of the financial statements but before those statements are issued), the opinions or views of legal advisers, experience on similar cases and any decision of the ASB to how it will respond to the litigation, claim or assessment.

## 2. Cash and Cash Equivalents

|                          | Log Ops          |                  | NAM            |                | CEPS           |                | NSPO TOTAL       |                  |
|--------------------------|------------------|------------------|----------------|----------------|----------------|----------------|------------------|------------------|
|                          | 2016             | 2015             | 2016           | 2015           | 2016           | 2015           | 2016             | 2015             |
| Cash available on demand | 304,729          | 228,802          | 7,716          | 17,175         | 13,759         | 22,165         | 326,204          | 268,142          |
| Short-term deposits      | 1,739,573        | 1,570,341        | 208,665        | 220,446        | 168,600        | 145,286        | 2,116,838        | 1,936,073        |
| <b>Total</b>             | <b>2,044,302</b> | <b>1,799,143</b> | <b>216,381</b> | <b>237,621</b> | <b>182,359</b> | <b>167,451</b> | <b>2,443,042</b> | <b>2,204,215</b> |

The value of cash and cash equivalents controlled by NSPA should be considered in the context of the total liabilities, actual and potential for all NSPA customers at the year-end being Euro 2.3 billion.

Cash available on demand is considered to be cash that can accessed at very-short notice (e.g. 1 working day) while a short-term deposit is invested from one day to twelve months. Cash balances are restricted to the use for which customers have provided the cash; NSPA has no unrestricted usages of the cash balances or parts thereof.



### 3. Property, Plant and Equipment (PPE)

|                                      | Cost at 1<br>January 2016 | Additions in<br>Year | Transfer | Disposal<br>/Impairment<br>in Year | Currency<br>Transaction<br>Adjustment | Cost at 31<br>December<br>2016 | Depreciation<br>at 1 January<br>2016 | Change in<br>Depreciation | Currency<br>Transaltion<br>Adjustment | Depreciation<br>at 31<br>December<br>2016 | Net book<br>value at 1<br>January<br>2016 | Net book<br>value at 31<br>December<br>2016 |
|--------------------------------------|---------------------------|----------------------|----------|------------------------------------|---------------------------------------|--------------------------------|--------------------------------------|---------------------------|---------------------------------------|---|---|---|
| Land                                 | 195                       | 0                    | 0        | 0                                  | 0                                     | 195                            | 0                                    | 0                         | 0                                     | 0   | 195                                       | 195   |
| Buildings                            | 25,632                    | 13,591               | 12,399   | 0                                  | 1,821                                 | 53,443                         | (6,429)                              | (1,961)                   | (124)                                 | (8,514)                                   | 19,202                                    | 44,929                                      |
| Installed Equipment                  | 5,023                     | 699                  | 0        | (66)                               | 127                                   | 5,783                          | (3,239)                              | (987)                     | (109)                                 | (4,335)                                   | 1,784                                     | 1,448                                       |
| Machinery                            | 100,341                   | 1,444                | 133      | (447)                              | 0                                     | 101,472                        | (92,610)                             | (2,234)                   | 0                                     | (94,844)                                  | 7,731                                     | 6,627                                       |
| Vehicles                             | 8,560                     | 1,192                | 0        | (881)                              | 70                                    | 8,941                          | (6,340)                              | 250                       | (44)                                  | (6,135)                                   | 2,220                                     | 2,806                                       |
| Aircraft                             | 580,834                   | 11,178               | 0        | 0                                  | 19,625                                | 611,636                        | (140,329)                            | (22,119)                  | (5,714)                               | (168,162)                                 | 440,505                                   | 443,475                                     |
| Pipeline System                      | 70,129                    | 5,264                | 8,079    | 0                                  | 0                                     | 83,472                         | (6,392)                              | (5,387)                   | 0                                     | (11,779)                                  | 63,736                                    | 71,693                                      |
| Mission Equipment                    | 30,042                    | 1,361                | 51       | (482)                              | 574                                   | 31,546                         | (18,016)                             | (1,744)                   | (308)                                 | (20,068)                                  | 12,026                                    | 11,479                                      |
| Furniture                            | 5,917                     | 471                  | 0        | (143)                              | 29                                    | 6,274                          | (4,558)                              | (224)                     | (16)                                  | (4,798)                                   | 1,359                                     | 1,476                                       |
| Automated information System         | 23,134                    | 2,380                | 0        | (113)                              | 44                                    | 25,444                         | (18,321)                             | (2,588)                   | (52)                                  | (20,960)                                  | 4,813                                     | 4,484                                       |
| Communication System                 | 3,197                     | 216                  | 11       | (66)                               | 51                                    | 3,409                          | (2,967)                              | (58)                      | (51)                                  | (3,076)                                   | 230                                       | 333   |
| Assets in the course of construction | 51,316                    | 121,755              | (20,672) | 0                                  | (204)                                 | 152,195                        | 0                                    | 0                         | 0                                     | 0   | 51,316                                    | 152,195                                     |
| <b>Total</b>                         | <b>904,321</b>            | <b>159,552</b>       | <b>0</b> | <b>(2,199)</b>                     | <b>22,136</b>                         | <b>1,083,810</b>               | <b>(299,202)</b>                     | <b>(37,051)</b>           | <b>(6,418)</b>                        | <b>(342,670)</b>                          | <b>605,119</b>                            | <b>741,140</b>                              |

NSPO capitalises all PPE which its segment parts control. Log Ops capitalises PPE which it controls as part of its administration duties or which are controlled by Support or Procurement Partnerships collectively. The Chairman's Office uses PPE which is controlled by Log Ops and as such are shown as part of the Log Ops Segment.

Assets in the Course of Construction are measured based on the stage of completion; this is based either on the results of a technical inspection or on contracted milestone payments. The main items include the milestone payments in the Log Ops Business Unit for the purchase of the MMF totalling Euro 103m, and Euro 49m of Pipeline System assets based on technical inspections.

#### *Restatement of opening balances in respect of the Central Europe Pipeline System*

For the first time in 2016, NSPA has capitalised Central Europe Pipeline System PPE which has been added since 1 January 2013. This results in a restated opening balance on PPE: The opening balance of cost at 1 January 2016 increased from Euro 792,532m to Euro 792,321m and the opening balance on depreciation increased from Euro 289,149m to Euro 289,202m.

#### 4. Intangible Assets

|                                  | Cost at 1 January 2016 | Additions in Year | Transfer | Disposal / Impairment in Year | Currency Transaction Adjustment | Cost at 31 December 2016 | Amortisation at 1 January 2016 | Change in Amortisation | Currency Transaltion Adjustment | Amortisation at 31 December 2016 | Net book value at 1 January 2016 | Net book value at 31 December 2016 |
|----------------------------------|------------------------|-------------------|----------|-------------------------------|---------------------------------|--------------------------|--------------------------------|------------------------|---------------------------------|----------------------------------|----------------------------------|------------------------------------|
| Software                         | 6,166                  | 1,842             | 2,001    | (10)                          | 154                             | 10,153                   | (4,986)                        | (1,242)                | (61)                            | (6,289)                          | 1,180                            | 3,864                              |
| Rights to Spare Engine           | 21,519                 | 2,428             | 0        | 0                             | 828                             | 24,776                   | (3,816)                        | (896)                  | (170)                           | (4,882)                          | 17,703                           | 19,893                             |
| Assets in course of Construction | 2,740                  | 4                 | (2,001)  | 0                             | (9)                             | 734                      | 0                              | 0                      | 0                               | 0                                | 2,740                            | 734                                |
| <b>Intangible Assets</b>         | <b>30,425</b>          | <b>4,274</b>      | <b>0</b> | <b>(10)</b>                   | <b>973</b>                      | <b>35,662</b>            | <b>(8,802)</b>                 | <b>(2,138)</b>         | <b>(231)</b>                    | <b>(11,171)</b>                  | <b>21,624</b>                    | <b>24,491</b>                      |

The intangible assets of NSPO are:

- Various instances of SAP Enterprise Resource Planning (ERP) which are used within all segments
- The NAM Programme's right of use to a spare engine for its C-17 Aircraft
- The CEPS Programme's management, planning and coordination systems

For the first time in 2016, NSPA has capitalised Central Europe Pipeline System Intangible Assets which has been added since 1 January 2013. This results in a restated opening balance on Intangible Assets as at 1 January 2016 increasing by Euro xx million and the closing balance on Intangible Assets as at 31 December 2016 increasing by Euro xx million.

#### 5. Inventories

|                 | Log Ops        |                | NAM          |              | CEPS         |              | NSPO TOTAL     |                |
|-----------------|----------------|----------------|--------------|--------------|--------------|--------------|----------------|----------------|
|                 | 2016           | 2015           | 2016         | 2015         | 2016         | 2015         | 2016           | 2015           |
| Consumables     | 170            | 165            | 322          | 364          | 2,698        | 3,219        | 3,190          | 3,748          |
| Spare parts     | 0              | 0              | 2,216        | 843          | 3,684        | 3,125        | 5,900          | 3,968          |
| Strategic stock | 355,788        | 354,925        | 0            | 0            | 0            | 0            | 355,788        | 354,925        |
| <b>Total</b>    | <b>355,958</b> | <b>355,090</b> | <b>2,538</b> | <b>1,207</b> | <b>6,382</b> | <b>6,344</b> | <b>364,878</b> | <b>362,641</b> |

Each Business Unit carries different types of inventory to reflect their different business lines of activity:

##### Log Ops

- Log Ops Support or Procurement Partnerships control inventories paid for jointly or commonly by members of the Support or Procurement Partnerships. Most of these inventories are considered strategic stocks in that they are held for potential military operational use as part of weapon systems.

### CEPS Programme

- The CEPS Programme's inventories include raw materials, spare-parts and consumables.

### NAM Programme

- The NAM Programme controls inventories for its aircraft; these include oils and lubricants. The NAM Programme capitalises spare parts in relation to its C-17s as Property Plant and Equipment, rather than showing them an inventory, which is in accordance with the NATO Accounting Framework.

## 6. Accounts Receivable – current assets

|                             | Log Ops          |                  | NAM          |               | CEPS          |               | Inter-business unit eliminations | NSPO TOTAL       |                  |                  |
|-----------------------------|------------------|------------------|--------------|---------------|---------------|---------------|----------------------------------|------------------|------------------|------------------|
|                             |                  |                  |              |               | Restated      |               |                                  | Restated         |                  | Original         |
|                             | 2016             | 2015             | 2016         | 2015          | 2016          | 2015          | 2016                             | 2016             | 2015             | 2015             |
| Receivables                 | 411,087          | 373,467          | 4,131        | 13,032        | 22,669        | 24,201        | (2,583)                          | 435,304          | 410,700          | 410,991          |
| Personnel                   | 0                | 0                | 0            | 0             | 0             | 0             | 0                                | 0                | 0                | 0                |
| Recoverable taxes           | 2                | 1                | 1,322        | 797           | 0             | 0             | 0                                | 1,324            | 798              | 798              |
| Other NATO Entities         | 16,922           | 14,444           | 0            | 0             | 4             | 7             | 0                                | 16,926           | 14,451           | 14,450           |
| Unbilled sales to customers | 624,057          | 618,146          | 0            | 0             | 0             | 0             | 0                                | 624,057          | 618,146          | 618,146          |
| Bank interest               | 245              | 710              | 1,238        | 783           | 19            | 76            | 0                                | 1,502            | 1,569            | 1,569            |
| <b>Total</b>                | <b>1,052,313</b> | <b>1,006,768</b> | <b>6,691</b> | <b>14,612</b> | <b>22,692</b> | <b>24,284</b> | <b>(2,583)</b>                   | <b>1,079,113</b> | <b>1,045,664</b> | <b>1,045,954</b> |

Receivables should be taken in the context that while customers owe amounts to the Agency, the same customers often have made substantial advances to the Agency; however, such amounts can only be "netted-off" each other with the permission of the customer.

Receivables includes an amount due of Euro 8 million from a vendor which provided services to NSPA in Theatre and which is currently involved in a legal dispute with NATO (see Note 17).

Unbilled sales represent amounts that have been paid to suppliers of goods and services but which have not yet been re-billed to individual customers (rather than common-funded sales to more than one customer which are billed through calls for contributions) at the year-end.

## 7. Prepayments

|   | Log Ops       |               | NAM            |                | CEPS      |           | NSPO TOTAL     |                |
|---|---------------|---------------|----------------|----------------|-----------|-----------|----------------|----------------|
|   | 2016          | 2015          | 2016           | 2015           | 2016      | 2015      | 2016           | 2015           |
| Prepayments to employees                  | 101           | 153           | 9              | 62             | 0         | 0         | 110            | 215            |
| Prepayments to vendors                    | 63,114        | 56,033        | 1              | 1,578          | 73        | 54        | 63,188         | 57,665         |
| Prepayments to USA Foreign Military Sales | 6,779         | (336)         | 156,329        | 138,550        | 0         | 0         | 163,108        | 138,214        |
| <b>Total</b>                              | <b>69,994</b> | <b>55,850</b> | <b>156,339</b> | <b>140,190</b> | <b>73</b> | <b>54</b> | <b>226,406</b> | <b>196,094</b> |

On occasions, the Log Ops Business Unit is contractually required to provide advance payments to vendors which are providing its customers with goods and services. The NAMP Business Unit uses United States Foreign Military Sales (FMS) to manage and support its airlift assets; FMS requires NAM to pre-finance its activities.

## 8. Accounts Payable and Accruals

|  | Log Ops        |                | NAM           |               | CEPS          |               | Inter-business unit eliminations | NSPO TOTAL     |                |                |
|--|----------------|----------------|---------------|---------------|---------------|---------------|----------------------------------|----------------|----------------|----------------|
|  |                |                |               |               | Restated      |               |                                  | Restated       |                | Original       |
|  | 2016           | 2015           | 2016          | 2015          | 2016          | 2015          | 2016                             | 2016           | 2015           | 2015           |
| Payables to vendors                          | 76,486         | 85,206         | 128           | (318)         | 1,932         | 5,622         | (2,583)                          | 75,963         | 90,510         | 90,510         |
| Health care contributions                    | 778            | 797            | 0             | 0             | 0             | 0             | 0                                | 778            | 797            | 797            |
| Pension contributions                        | 109            | 582            | 0             | (37)          | 0             | 0             | 0                                | 109            | 545            | 545            |
| Accruals                                     | 244,114        | 269,481        | 54,719        | 21,475        | 7,016         | 5,405         | 0                                | 305,849        | 296,361        | 296,361        |
| Taxes  | 0              | 0              | 0             | 0             | 8,514         | 7,565         | 0                                | 8,514          | 7,565          | 7,565          |
| Short-term borrowings (overdraft facilities) | 0              | 0              | 0             | 0             | 0             | 655           | 0                                | 0              | 655            | 655            |
| Other  | 4,989          | 4,327          | 0             | (6)           | 718           | 718           | 0                                | 5,707          | 5,039          | 4,323          |
| <b>Total</b>                                 | <b>326,476</b> | <b>360,393</b> | <b>54,847</b> | <b>21,114</b> | <b>18,180</b> | <b>19,965</b> | <b>(2,583)</b>                   | <b>396,920</b> | <b>401,472</b> | <b>400,756</b> |

## 9. Customer Advances

|   | Log Ops          |                  | NAM            |                | CEPS           |                | NSPO TOTAL       |                  |                  |
|---|------------------|------------------|----------------|----------------|----------------|----------------|------------------|------------------|------------------|
|   |                  |                  |                |                | Restated       |                | Restated         |                  | Original         |
|   | 2016             | 2015             | 2016           | 2015           | 2016           | 2015           | 2016             | 2015             | 2015             |
| Customer advance payments   | 2,676,436        | 2,336,955        | 309,810        | 358,288        | 17,148         | 16,925         | 3,003,394        | 2,712,168        | 2,712,168        |
| Customer and replenishment credits (allocated or to be allocated) | 134,921          | 142,520          | 12,286         | 14,541         | 167,745        | 153,524        | 314,952          | 310,585          | 311,591          |
| <b>Total</b>  | <b>2,811,357</b> | <b>2,479,475</b> | <b>322,096</b> | <b>372,829</b> | <b>184,893</b> | <b>170,449</b> | <b>3,318,346</b> | <b>3,022,753</b> | <b>3,023,759</b> |

Customer credits represent amounts owned by customers and consist of bank interest earned, realised exchange rate gains and losses, and miscellaneous income; in the case of the CEPS Programme Business Unit, it also includes surpluses for the period which are transferred to customer credits before they impact the “bottom line”. Replenishment credits represent amounts owned by customers of the Log Ops Business Unit for the replenishment of spare parts.

“Customer Advance Payments” often represent the offsetting legal commitments entered into by the Agency to purchase goods or services on Customers’ behalf which have either not been re-billed to the customer at the year-end (considered “potential liabilities”), or are actual liabilities billed but not yet settled against customer advances. For the 28 NATO nations and NATO entities, this amount of actual and potential liabilities at 31 December 2016 which were offsetting customer advance payments was Euro 2.293 Billion.

## 10. Bank Interest, Unrealised foreign currency effects, and, Financial Revenue

For the Log Ops Business Unit and NAMP Business Unit, bank interest and any realised foreign exchange returns do not belong to the respective Business Unit but to their respective customers; these returns “pass through” those business units and are reflected in the Statement of Financial Position under Customer Advances (Note 9) as “Customer and replenishment credits (allocated or to be allocated)”. These amounts are not shown in the Statement of Financial Performance. However, for the CEPS Business Unit, these balances are considered to belong to the Programme and as such are shown in both the Statement of Financial Position and the Statement of Financial Performance.

The only type of financial revenue which impacts directly upon the surplus or deficit for the year is unrealised foreign exchange gains and losses. As customers are financially liable for any losses made in the year, and share in any gains made in the year, unrealised gains or losses will ultimately impact upon Customer Advances (Note 9) as “Customer and replenishment credits (allocated or to be allocated)”. These surplus/gains related to unrealised foreign exchange gains and losses are transferred to “Customer and replenishment credits (allocated or to be allocated)” through the Statement of Changes in Net Assets.

## 11. Expenses

### *Services and Support to Customers*

|  | Chairperson's Office |          | Log Ops          |                  | NAM           |               | CEPS          |               | Inter-business unit eliminations | NSPO TOTAL       |                  |                  |
|--|----------------------|----------|------------------|------------------|---------------|---------------|---------------|---------------|----------------------------------|------------------|------------------|------------------|
|  |                      |          |                  |                  |               |               | Restated      |               |                                  | Restated         |                  | Original         |
| Services and Support to Customers        | 2016                 | 2015     | 2016             | 2015             | 2016          | 2015          | 2016          | 2015          | 2016                             | 2016             | 2015             | 2015             |
| Common Support (including ACO and AWACS) | 0                    | 0        | 174,049          | 194,346          | 0             | 0             | 0             | 0             | 0                                | 174,049          | 194,346          | 194,346          |
| Individual brokerage                     | 0                    | 0        | 637,572          | 560,957          | 0             | 0             | 0             | 0             | (80)                             | 637,492          | 560,957          | 560,957          |
| Individual maintenance and services      | 0                    | 0        | 569,019          | 546,621          | 0             | 0             | 0             | 0             | (2)                              | 569,017          | 546,621          | 546,621          |
| Operational logistics support            | 0                    | 0        | 304,052          | 368,788          | 0             | 0             | 0             | 0             | 0                                | 304,052          | 368,788          | 368,788          |
| Transportation services                  | 0                    | 0        | 84,924           | 90,684           | 0             | 0             | 0             | 0             | (208)                            | 84,716           | 90,684           | 90,684           |
| Airlift Services                         | 0                    | 0        | 0                | 0                | 59,541        | 26,704        | 0             | 0             | 0                                | 59,541           | 26,704           | 26,704           |
| Fuel Management                          | 0                    | 0        | 230,476          | 310,816          | 0             | 0             | 32,414        | 33,337        | 0                                | 262,890          | 344,153          | 345,246          |
| Net proceeds from changes in inventory   | 0                    | 0        | 8,987            | 7,887            | 0             | 0             | 0             | 0             | 0                                | 8,987            | 7,887            | 7,887            |
| Other services                           | 0                    | 0        | 0                | 0                | 0             | 0             | 0             | 0             | 0                                | 0                | 0                | 0                |
| <b>Total</b>                             | <b>0</b>             | <b>0</b> | <b>2,009,079</b> | <b>2,080,099</b> | <b>59,541</b> | <b>26,704</b> | <b>32,414</b> | <b>33,337</b> | <b>(290)</b>                     | <b>2,100,744</b> | <b>2,140,140</b> | <b>2,141,233</b> |
| USA Foreign Military Sales               | 0                    | 0        | 23,532           | 45,837           | 61,352        | 50,969        | 0             | 0             | 0                                | 84,884           | 96,806           | 96,806           |

Many of the expenses in relation to “Commons Support (including ACO and AWACS)” may also appear in the financial statements of other NATO entities such as ACO and NAPMA.

### *Other Expenses*

Other expenses, shown on the face of the Statement of Financial Performance, are the expenses incurred in administering the respective Business Units; they include items such as communications, information systems, services and supplies, travel, transportation, non-operational consultants, public relations, training, utilities, and care of buildings.

## 12. Inter-Business Unit Eliminations on consolidation

The following represent inter-business unit eliminations in the consolidation process to create the NSPO Financial Statements 2016

| Statement of Financial Position       |      |                                       |                                       |                                  |
|---------------------------------------|------|---------------------------------------|---------------------------------------|----------------------------------|
| Current Assets                        | Note | Receivable<br>by Log Ops<br>from NAMP | Receivable<br>by Log Ops<br>from CEPS | Total Inter-<br>business<br>unit |
| Accounts Receivable: Receivables      | 6    | 2,581                                 | 2                                     | 2,583                            |
|                                       |      |                                       |                                       |                                  |
| Current Liabilities                   |      | Payable<br>from NAMP<br>to Log Ops    | Payable<br>from CEPS<br>to Log Ops    | Total Inter-<br>business<br>unit |
| Accounts Payable: Payables to vendors | 8    | 2,581                                 | 2                                     | 2,583                            |

| Statement of Financial Performance  |      |                                   |                                   |                                  |
|-------------------------------------|------|-----------------------------------|-----------------------------------|----------------------------------|
| Revenue                             | Note | Log Ops<br>revenue<br>from NAMP   | Log Ops<br>revenue<br>from CEPS   | Total Inter-<br>business<br>unit |
| Services and Support to Customers   |      |                                   |                                   |                                  |
| Individual Brokerage                |      | 62                                | 18                                | 80                               |
| Individual Maintenance and Services |      | 2                                 | 0                                 | 2                                |
| Airlift Services                    |      | 208                               | 0                                 | 208                              |
| Administrative Support              |      | 2,484                             | 0                                 | 2,484                            |
| Miscellaneous Revenue               |      | 0                                 | 1                                 | 1                                |
| Total                               |      | 2,756                             | 19                                | 2,775                            |
|                                     |      |                                   |                                   |                                  |
| Expenditure                         |      | NAMP<br>expenditure<br>at Log Ops | CEPS<br>expenditure<br>at Log Ops | Total Inter-<br>business<br>unit |
| Services and Support to Customers   |      |                                   |                                   |                                  |
| Individual Brokerage                | 11   | 62                                | 18                                | 80                               |
| Individual Maintenance and Services | 11   | 2                                 | 0                                 | 2                                |
| Airlift Services                    | 11   | 208                               | 0                                 | 208                              |
| Other Expenses                      |      |                                   |                                   |                                  |
| Information Systems                 |      | 2,484                             | 0                                 | 2,484                            |
| Training                            |      | 0                                 | 1                                 | 1                                |
| Total                               |      | 2,756                             | 19                                | 2,775                            |

### 13. Employee Disclosures

#### Personnel Costs (including key management personnel)

|                                | Chairperson's Office |            | Log Ops       |               | NAM          |              | CEPS          |               | NSPO TOTAL     |                |                |
|--------------------------------|----------------------|------------|---------------|---------------|--------------|--------------|---------------|---------------|----------------|----------------|----------------|
|                                |                      |            |               |               |              |              | Restated      |               | Restated       |                | Original       |
|                                | 2016                 | 2015       | 2016          | 2015          | 2016         | 2015         | 2016          | 2015          | 2016           | 2015           | 2015           |
| Salaries                       | 534                  | 590        | 67,800        | 68,221        | 2,435        | 2,662        | 34,022        | 38,234        | 104,791        | 109,707        | 109,962        |
| Allowances                     | 76                   | 79         | 15,669        | 15,698        | 546          | 751          | 9,372         | 9,802         | 25,663         | 26,330         | 26,396         |
| Pension contributions          | 26                   | 25         | 3,999         | 3,543         | 326          | 333          | 12,383        | 4,408         | 16,734         | 8,309          | 8,337          |
| Health care contributions      | 58                   | 70         | 8,494         | 8,791         | 389          | 395          | 1,841         | 10,432        | 10,782         | 19,688         | 19,763         |
| Loss-of-Job Indemnities (LOJI) | 0                    | 0          | 0             | 494           | 0            | 10           | 38            | 0             | 38             | 504            | 504            |
| Other                          | 0                    | 4          | 791           | 593           | 67           | 104          | 1,219         | 1,136         | 2,077          | 1,837          | 720            |
| <b>Total</b>                   | <b>694</b>           | <b>768</b> | <b>96,753</b> | <b>97,340</b> | <b>3,763</b> | <b>4,255</b> | <b>58,875</b> | <b>64,012</b> | <b>160,085</b> | <b>166,375</b> | <b>165,682</b> |

#### Personnel Numbers

At 31 December, the following posts were filled:

|                            | Chairperson's Office |          | Log Ops  |          | NAM      |          | CEPS     |          | NSPO TOTAL |          |
|----------------------------|----------------------|----------|----------|----------|----------|----------|----------|----------|------------|----------|
|                            | 2016                 | 2015     | 2016     | 2015     | 2016     | 2015     | 2016     | 2015     | 2016       | 2015     |
| NATO Contracts             | ■                    | ■        | ■        | ■        | ■        | ■        | ■        | ■        | ■          | ■        |
| NSPA Consultants           | ■                    | ■        | ■        | ■        | ■        | ■        | ■        | ■        | ■          | ■        |
| CEPS National Organisation | ■                    | ■        | ■        | ■        | ■        | ■        | ■        | ■        | ■          | ■        |
| <b>Total</b>               | <b>■</b>             | <b>■</b> | <b>■</b> | <b>■</b> | <b>■</b> | <b>■</b> | <b>■</b> | <b>■</b> | <b>■</b>   | <b>■</b> |

The personnel of the CEPS Programme National Organisations are not employed on NATO personnel contracts. In total NSPA employed ■ consultants throughout the year (2015: 105); the majority of these consultants were working in Theatre.



### ***Retirement benefits of NSPA Personnel***

NSPA personnel, past and present, are enrolled in various different NATO pension schemes. NSPA contributes to the schemes for existing employees at amounts laid out in the NATO Civilian Personnel Regulations.

NSPA does not control or manage any of the schemes or scheme assets and is not exposed to the risks and rewards of the schemes and hence does not record any assets or liabilities of the schemes on its statements of financial position.

### **14. Related Party Transactions**

NSPO has no related party relationships where significant influence or control of the related party exists from a financial reporting perspective. NSPO is a military logistics support organisation which exists for its member nations and partners. Many member nations and partner countries have financial and operating control, or, significant influence over military suppliers based in their territories; as such NSPO can trade with military suppliers which may be controlled by its member nations. However, NSPO trades with such suppliers at “arms-length” and under transparent procurement regulations; while it aims to get the best value for money for its customers it does not do this through exerting control or significant influence over its suppliers.

NSPO is an integral part of NATO and it transacts in its normal business activities with other NATO bodies and these transactions occur at cost. On occasions, NSPO segments transact with each other at the cost of providing goods or services; for example, Log Ops can provide services to the NAM and CEPS Programmes. The costs of inter-NSPO transactions are eliminated on the consolidation of the financial statements.

#### ***Related Party Transactions of Members of Boards and Committees***

The Chairperson contacted members of the Agency Supervisory Board, Logistics Committee, Finance, Administration and Audit Committee, CEPS Programme Board and NAM Programme Board respectively asking for details of any related party transactions they had with the Agency. At the level of the Agency Supervisory Board, Logistics Committee, and Finance, Administration and Audit Committee, 43 replies were received out of 65 requests. For the CEPS Programme Board 7 replies out of 7 requests were received. For the NAM Programme Board 11 replies out of 13 requests were received. No replies indicated related party transactions.

#### ***Related Party Transactions of Management Personnel***

The Financial Controller contacts all management personnel which he considers to have positions of influence at the end of the financial year to garner information in respect of possible related party transactions. The personnel contacted include key management personnel (see Note 15) and other personnel such as programme managers, the competition advocate, and the chiefs of support divisions. None of the personnel contacted considered that they had related transactions with the Agency in 2016.

## 15. Key Management Personnel

Key management personnel hold positions of responsibility within NSPA. They are responsible for implementing the strategic direction, which is approved by the ASB, and carrying out the operational management of NSPA; they are entrusted with significant authority.

In theory, their responsibilities may enable them to influence the benefits of office that flow to them or their related parties (such as family members) and hence certain financial reporting disclosures must be made about:

- the remuneration of key management personnel and close members of the family of key management personnel during the reporting period,
- loans made to them, and
- payments provided to them for services they provide to the entity other than as an employee.

| Name   | Nationality | Role  | Grade/step | Loans received from NSPA | Family members receiving income from NSPA | Other revenue from NSPA or NATO |
|--------|-------------|---|------------|--------------------------|---|---------------------------------|
| ██████ | NLD         | General Manager<br>(from 1 September 2016)                                    | A7/1       | Nil                      | Nil                                       | Nil                             |
| ██████ | USA         | General Manager<br>(until 4 July 2016)  | A7/4       | Nil                      | Nil                                       | Nil                             |
| ██████ | GBR         | Chief of Staff<br>(and General Manager from 5 July 2015 until 31 August 2016) | A6/6       | Nil                      | Nil                                       | Nil                             |
| ██████ | DEU         | Financial Controller<br>(retired on 28 February 2016)                         | A6/7       | Nil                      | Nil                                       | Nil                             |
| ██████ | FRA         | Director Procurement  | A6/8       | Nil                      | Nil                                       | Nil                             |
| ██████ | DEU         | Director Logistics  | A6/2       | Nil                      | Nil                                       | Nil                             |
| ██████ | BEL         | CEPS Programme Manager  | A6/2       | Nil                      | Nil                                       | Nil                             |
| ██████ | NLD         | NAM Programme Manager   | A6/4       | Nil                      | Nil                                       | Nil                             |

During the year there were seven Full-time Equivalent key management personnel; one FTE was of Grade A7 while six FTE staff were of Grade A6.

***Salaries and benefits paid to key management personnel in 2016***

| Remuneration type                    | 2016             |
|--------------------------------------|------------------|
| Basic salaries                       | 914,911          |
| Allowances                           | 187,729          |
| Employer's contribution to insurance | 119,611          |
| Employer's contribution to pension   | 91,781           |
| <b>Total</b>                         | <b>1,314,032</b> |

***Representative Allowance of the General Manager***

In 2016, NSPA had three General Managers. Mr Mike Lyden was in post from 1 January 2016 until 4 July 2016, Mr Christopher Rose, who is currently Chief of Staff, was in post from 5 July 2016 until 31 August 2016 and Mr Peter Dohmen has been in post since 1 September 2016. The General Managers, in addition to other allowances to which all staff are entitled, received a total combined representation allowance for 2016 of Euro 10,107 per-year (2015: Euro 10,107), due to the requirement to represent NSPA at events, of which Euro 8,827 was spent (2015: Euro 9,661). Expenditure made against this allowance is supported by invoices and is approved by the Financial Controller. This representation allowance includes a 25 per cent contribution to the rent of accommodation.

***Hospitality Allowances of Directors***

NSPA Directors receive a total hospitality allowance of Euro 5,000 (2015: Euro 6,000) between them, of which Euro 2,998 (2015: Euro 5,482) was spent in 2016.

***Hospitality Allowance of the ASB's Secretariat***

The ASB approved a Euro 20,000 (2015: Euro 21,000) hospitality allowance to its Secretariat for 2016 of which Euro 13,626 was spent (2015: Euro 17,073). Expenditure made against this allowance is supported by invoices. The Chairperson of the ASB and the Chairperson of the CEPS and NAM Programme Boards respectively, do not receive a Representation Allowance.

### *Remuneration of the Chairperson of the NSPO Agency Supervisory Board*

The Chairperson of the NSPO Agency Supervisory Board, Ms Jennifer Hubbard, does not receive a salary from NSPO. She is reimbursed her travel expenses while working on NSPO business in accordance with the NATO Civilian Personnel Regulations.

## **16. Provisions**

IPSAS defines a provision as “a liability of uncertain timing or amount”.

|   | Log Ops         |              |                |                 |
|---|-----------------|--------------|----------------|-----------------|
|   | Opening Balance | Additions    | Reductions     | Closing Balance |
| Bad and Doubtful Debts  | 0               | 2,120        | 0              | 2,120           |
|   |                 |              |                |                 |
|   | CEPS            |              |                |                 |
|   | Opening Balance | Additions    | Reductions     | Closing Balance |
| Bad and Doubtful Debts  | 267             | 0            | 0              | 267             |
| Early Retirement Provisions of the German National Organisation | 6,605           | 0            | (2,147)        | 4,458           |
| <b>Total</b>  | <b>6,872</b>    | <b>0</b>     | <b>(2,147)</b> | <b>4,725</b>    |
|   |                 |              |                |                 |
|   | NSPO            |              |                |                 |
|   | Opening Balance | Additions    | Reductions     | Closing Balance |
| Bad and Doubtful Debts  | 267             | 2,120        | 0              | 2,387           |
| Early Retirement Provisions of the German National Organisation | 6,605           | 0            | (2,147)        | 4,458           |
| <b>Total</b>  | <b>6,872</b>    | <b>2,120</b> | <b>(2,147)</b> | <b>6,845</b>    |

The Log Ops Business Unit has made a provision for Euro 2.12m relating to the purchase of software licences where it is considered highly improbable that the amount will be recovered from customers (see Note 18 for further details).

## 17. Contingent Liabilities

IPSAS defines a contingent liability as:

“A possible obligation that arises from past events, and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity, or a present obligation that arises from past events, but is not recognized because: 1) It is not probable that an outflow of resources embodying economic benefits or service potential will be required to settle the obligation; or 2) The amount of the obligation cannot be measured with sufficient reliability”.

The following represent contingent liabilities:

- The NATO Administrative Tribunal is currently considering one appeal lodged by a NSPA staff member in 2016; the issue is related to a former staff member’s request for an Invalidity Board be convened and the termination of her contract with NSPA. No estimation of the likely cost of settlement/financial liability to the Agency in the case of adverse rulings or outcomes can be provided at this stage; however, considering results of past appeal cases, the likelihood of an adverse outcome of the litigations is considered to be moderate.
- The NATO Administrative Tribunal is currently considering one appeal lodged by a former NSPA staff member in 2017, in relation to termination of her contract with NSPA in 2016. A complaint from the same person to the NSPA General Manager has been dealt with but might result in a further appeal before the NATO Administrative Tribunal. No estimation of the likely cost of settlement/financial liability to the Agency in the case of adverse rulings or outcomes can be provided at this stage; however, considering results of past appeal cases, the likelihood of an adverse outcome of the litigations is considered to be moderate.
- A customer of the Log Ops Business Unit may face a possible tax liabilities of approximately Euro 278k in relation to tax which may be due with a member nation.
- Log Ops has received a claim from a contractor relating to the deactivation of a Depot Level Maintenance Contract. The financial details of the claim are not being disclosed as this may be prejudicial to the NSPA customer concerned.
- NATO is currently in legal dispute with a contractor. This contractor provided service to the Agency in Theatre also owes the Agency Euro 8 million which has been outstanding for over a year. The Agency considers the non-recovery of this amount, or part of this amount, to be possible.

For details of a potential write-on of debt to Nations in respect of the purchases of software licences for which the Agency did not always have customers, refer to Note 20: “Write-offs” and “write-ons”.

The CEPS Programme is exposed to possible obligations that may require a collective outflow of resources if NSIP or national funding does not cover potential obligations in the in the following areas:

- In the course of its normal operations, the CEPS Programme holds some jet fuel that contains a level of Fatty Acid Methyl Ester (FAME) that exceeds current acceptable tolerance levels. Management believes that the remediation method in use is deemed sufficient and appropriate to ensure that there will be no material outflow of resources necessary in order to settle any obligation in connection with this issue.
- In one host nation, a decree dated 4 August 2006 was issued regarding minimum safety regulations for pipelines and which may have a financial impacts. It is not yet possible to quantify the efforts and costs of the implementation of those decrees.
- In 2005, an accident in one of the Programme's member nations led to a site being polluted for which a clean-up plan was foreseen to last until 2023. The costs of the clean-up are common funding eligible with an estimated cost of Euro 10.1m payable in 2 parts. It is not yet known if third parties will submit claims against Programme's member nation.
- In 2008, an accident in one of the Programme's member nations led to a site being polluted. The clean-up bill amounted to Euro 1.5m. The Member Nation's MOD is prosecuting the owner of the ground and the farmer using the ground. The company which did the clean-up work is now prosecuting the local administration which asked both cases to be juridically linked. In the meantime, the owners of the nearby land joined the prosecution. The litigation is pending.
- In 2015, an attempted theft on the pipeline system and resulted in damages and significant pollution. The repairs and depollution have already been budgeted by the CEPS for a value of Euro 1.4m and the repair of the line is complete. The owner of the ground has officially filed a complaint against the relevant member nation; although the amount of any future claim is not yet known.

## 18. Leases

IPSAS defines a lease as "An agreement whereby the lessor conveys to the lessee, in return for a payment or series of payments, the right to use an asset for an agreed period of time". Typical examples of leases are the rental of vehicles and photocopiers.

NSPO does not have any finance leases or significant operating leases.

## 19. Financial Instruments

NSPO's financial requirements are met from its customers who are members or partners of NATO. NSPO has no powers to borrow money; although the CEPS National Organisations have short-term borrowing facilities (see note 8). Other than financial assets and liabilities which are generated by day-to-day business activities, no financial instruments are held.

### *Liquidity risk*

NSPO's financial requirements and capital expenditure are met by its customers and are typically funded in advance. NSPO is therefore not exposed to material liquidity risks.

### ***Credit risk***

NSPO's customers are member and partner nations of NATO and hence NSPO is not exposed to material credit risks.

### ***Foreign currency risk***

NSPO has limited exposure to foreign currency risk which is borne by its customers.

## **20. "Write-offs" and "Write-ons"**

The NATO Financial Regulations require NATO entities to disclose any amounts written-off in the year. In 2016 the Log Ops Business Unit wrote-off assets with a value of Euro 19k (2015: Euro 172k).

The Agency wishes to bring to the reader's attention a future potential cost "write-on" in relation to the purchase of software licenses between 2011 and 2015. The Agency purchased software licenses for which it did not always have customers. The vendor was paid for the software licenses; however, for some of the licenses there was no customer to sell the licenses to, and for some of the licenses, where the Agency had a customer, amounts invoiced remain outstanding.

In the future, the Nations will be asked to "write-on", and hence become liable for, amounts that the Agency was not able to collect. The Agency currently estimates the potential future write-on of debts to nations at Euro 2.1m. As this amount will be written-on to national accounts, the Agency has also had to make a provision for this amount (Note 16) as it will be written-off the individual accounts to which the revenue was credited.

## **21. Financial Plan Execution**

NSPO is not required to follow "IPSAS 24 - Presentation of Budget Information in Financial Statements" because it prepares an Annual Financial Plan which includes a Statement of Planned Income and Expenditures. However, NSPA provides a high-level summary of the approved administrative cost elements of the financial plan of the Log Ops Business Unit, and full summary plans for the CEPS and the NAM Business Units, with the authorised commitments and expenditures made against them. In addition, NSPA chooses to show the amounts funded jointly by members of Support or Procurement Partnerships (individual national procurement activity is not shown). Details of Financial Plan Execution are found in the Annex.

## **22. Non-NSPA controlled inventories managed on behalf of third parties**

NSPA manages inventories on behalf of third parties such as NATO member states and other NATO Bodies; however, it does not control these inventories from a financial reporting perspective. Inventories are valued at weighted average costs. Third party inventories managed by NSPA include inventories held in [REDACTED], as well as those which have been certified by the respective commanders of national depots used by NATO at the year-end.

The value of inventories managed for third parties which are NATO bodies at the 2016 year-end were Euro 335 m (2015: Euro 338 m). Of this amount Euro 267 m (2015: Euro 264 m) were held on behalf of ACO.

## **23. Restatements of 2015 Financial Statements due to the correction of prior-period errors**

The Agency has restated elements of its 2015 Financial Statements to correct prior period errors.

### **a) Central Europe Pipeline System PPE and Intangible Assets**

In 2015 the Agency did not include the PPE and Intangible Assets of the Central Europe Pipeline System in the financial statements; this resulted in a qualification of the financial statements.

In 2016, the Agency changed its accounting policy to reflect the additions of PPE and intangible assets of the Central Europe Pipeline System since 1 January 2013. The result of this change of accounting policy is a correction of the error in the 2015 financial statements.

In addition, as part of the pipeline system recognition study the German National Organisation discovered and corrected some historical data errors.

This change in accounting policy and the correction of the 2015 errors impacts the comparative figures for 2015 in the following way:



As of 31 December  
(all figures are in Euro '000)

|                                     | Note | CEPS             |                  | Change  | Reason   |
|-------------------------------------|------|------------------|------------------|---------|--|
|                                     |      | Restated<br>2015 | Original<br>2015 |         |  |
| <b>Current Assets</b>               |      |                  |                  |         |  |
| Cash and Cash Equivalents           | 2    | 167,451          | 167,451          |         |  |
| Accounts Receivable                 | 6    | 24,284           | 24,574           | (290)   | German National Organisation data cleansing              |
| Prepayments                         | 7    | 54               | 54               |         |  |
| <b>Long Term Receivables</b>        |      | 5,497            | 5,497            |         |  |
| <b>Inventory</b>                    | 5    | 6,344            | 6,344            |         |  |
| <b>Fixed and Intangible Assets</b>  |      |                  |                  |         |  |
| Property Plant and Equipment        | 3    | 113,007          | 11,271           | 101,736 | Capitalisation of the Pipeline System for the first time |
| Intangible Assets                   | 4    | 2,572            | 2,572            |         |  |
| <b>Total Assets</b>                 |      | <b>319,209</b>   | <b>217,763</b>   |         |  |
| <b>Current Liabilities</b>          |      |                  |                  |         |  |
| Accounts Payable and Accruals       | 8    | 19,965           | 19,249           | 716     | German National Organisation data cleansing              |
| Customer Advances                   | 9    | 170,449          | 171,455          | (1,006) | German National Organisation data cleansing              |
| <b>Provisions</b>                   | 16   | 6,872            | 6,872            |         |  |
| <b>Total Liabilities</b>            |      | <b>197,286</b>   | <b>197,576</b>   |         |  |
| <b>Net Assets of NSPO Customers</b> |      | <b>121,923</b>   | <b>20,187</b>    |         |  |

For the year-ended 31 December  
(all figures are in Euro '000)

|   | Note | CEPS             |                  | Change  | Reason   |
|---|------|------------------|------------------|---------|--|
|   |      | Restated<br>2015 | Original<br>2015 |         |  |
| <b>Revenue</b>                          |      |                  |                  |         |  |
| Services and Support to Customers       |      | 113,198          | 112,219          | 979     | German National Organisation data cleansing              |
| Administrative Support                  |      | 14,805           | 14,446           | 359     | Capitalisation of the Pipeline System for the first time |
| Bank Interest                           |      | 621              | 621              |         |  |
| Unrealised Foreign Currency Effects     | 10   | 0                | 0                |         |  |
| Miscellaneous Revenue                   |      | 6,157            | 6,157            |         |  |
| <b>Total Revenue</b>                    |      | <b>134,781</b>   | <b>133,443</b>   |         |  |
| <b>Expenses</b>                         |      |                  |                  |         |  |
| Services and Support to Customers       | 11   | (33,337)         | (34,430)         | 1,093   | German National Organisation data cleansing              |
| Commercial Discounts Earned             |      | 18               | 18               |         |  |
| USA Foreign Military Sales*             |      | 0                | 0                |         |  |
| Personnel Costs                         | 13   | (64,012)         | (63,319)         | (693)   | German National Organisation data cleansing              |
| Depreciation and Amortisation           |      | (5,820)          | (2,003)          | (3,817) | Capitalisation of the Pipeline System for the first time |
| Provisions                              |      | (2,617)          | (2,617)          |         |  |
| Other Expenses                          | 11   | (14,805)         | (14,446)         | (359)   | Capitalisation of the Pipeline System for the first time |
| Transfers to customer credits           |      | (20,028)         | (18,649)         | (1,379) | Both the reasons given above                             |
| <b>Total Expenses</b>                   |      | <b>(140,601)</b> | <b>(135,446)</b> |         |  |
| <b>Surplus / (Deficit) for the year</b> |      | <b>(5,820)</b>   | <b>(2,003)</b>   |         |  |

## **b) Cash Flow Statement**

The Agency encountered difficulties producing a cash-flow statement based on the indirect method in 2015 and this led to a qualification of the Financial Statements for 2015. In 2015, the Agency had to use “balancing figures” to make the cash flow statement balance.

To address this audit qualification and to correct the financial reporting errors in the NSPO Financial Statements for 2015, the Agency has changed its accounting policy in respect of preparing its cash flow statement to use the “direct method”. While the Agency has restated its 2015 cash flows, it is not practicable to provide a comparison between the original and restated 2015 figures because line items in the direct and indirect method are not directly comparable.

The “direct method” shows major classes of gross cash receipts and gross cash payments, while the indirect method adjusts surplus or deficit for the effects of transactions of a noncash nature, any deferrals or accruals of past or future operating cash receipts or payments, and items of revenue or expense associated with investing or financing cash flows.

## **c) Note disclosures in respect of PPE (Note 3) and Intangible Assets (Note 4)**

In 2015, the IBAN was unable to reconcile amounts given in respect of depreciation on PPE and amortisation of intangible assets in Notes 3 and 4 respectively, to the Statement of Financial Performance, Statement of Cash Flows and Statement of Changes in Net Assets.

The Agency is still implementing a technical solution to this issue.

## **24. Events after the financial reporting date of 31 December 2016**

NSPO is required to disclose events, both favourable and unfavourable, that occurred between the reporting date of 31 December 2016 and the date when these financial statements were authorized for issue by the General Manager and the Financial Controller. IPSAS requires two types of events which should be identified:

- a. Those that provide evidence of conditions that existed at the reporting date (adjusting events after the reporting date); and
- b. Those that are indicative of conditions that arose after the reporting date (non-adjusting events after the reporting date).

While management considers there are no events categorised under (a), they consider that under category (b) one item should be disclosed:

Revised NATO Financial Regulations (NFRs) were issued by Council on 4 May 2015. The Secretary General’s cover letter to the Agency’s General Manager advised that

“The revised NFRs take immediate effect and supersede all previous versions. In terms of next steps, it is important that detailed implementing financial rules and procedures are developed and agreed as a matter of urgency. It is recognised that some articles, primarily those dealing with internal audit and with the management of appropriations, may require phased implementation during the course of 2015. If any amendments to the revised NFRs are needed by the Heads of NATO Procurement, Logistics and Support Organisations, it is important that these should be submitted to Council for approval as soon as possible. I look to you, and your Financial Controllers, to ensure that the necessary actions are taken to ensure that the NFRs are implemented in full by the end of 2015.”

At the time these Financial Statements were issued, the revised NFRs have not been implemented in full. A working group of the Organisation’s Finance Committee has drafted detailed rules and procedures for NSPO, which are consistent with the NFRs. The Chairman of the Agency Supervisory Board wrote to the Secretary General towards the end of 2015 to explain the process that the ASB is following. The Finance, Audit and Administration Committee will discuss the draft rules and procedures at its May 2017 meeting.

## Annex: NSPO Financial Plan Execution

### 1. Log Ops Business Unit – Administrative Costs Elements

These administrative cost elements do not include the costs charged by vendors for supplying goods and services to customers.

| All figures in Euro '000  | PRIOR 2016<br>UNPAID<br>COMMITMENTS<br>BROUGHT<br>FORWARD | 2016<br>AUTHORISED<br>CREDITS | PAYMENTS<br>AGAINST<br>COMMITMENTS<br>& CREDITS | UNPAID<br>COMMITMENTS<br>(i.e. LEGAL<br>OBLIGATIONS)<br>CARRIED<br>FORWARD | TOTAL<br>CREDITS<br>CONSUMED<br>IN YEAR | LAPSED<br>CREDITS |
|---|---|-------------------------------|---|--|---|-------------------|
| Personnel Expenditure   | 888   | 104,709                       | 97,078  | 518  | 97,596                                  | 8,001             |
| General Administrative,<br>Operating & Maintenance                              | 5,746   | 13,364                        | 11,446  | 6,049  | 17,495                                  | 1,615             |
| Project Specific Expenditure  | 5,886   | 21,773                        | 14,954  | 7,367  | 22,321                                  | 5,338             |
| Investments   | 2,123   | 3,777                         | 3,649   | 1,779  | 5,428                                   | 472               |
| Southern Operational Centre<br>Regularisation for<br>Administrative Expenditure | (705)   | 0                             | 38  | (646)  | (608)                                   | (97)              |
| <b>Total</b>  | <b>13,938</b>   | <b>143,623</b>                | <b>127,165</b>                                  | <b>15,067</b>  | <b>142,232</b>                          | <b>15,329</b>     |

## 2. Log Ops Business Unit – Jointly and Commonly Funded Operational Projects

Jointly funded projects are funded by between one and twenty-seven NATO nations, while commonly funded projects are funded by all twenty-eight NATO nations. The figures excludes individual customer requirements

| Operational Budget | Source of Funding          | PRIOR 2016 UNPAID COMMITMENTS BROUGHT FORWARD | 2016 PAYMENTS AGAINST PRIOR 2016 COMMITMENTS | PRIOR 2016 UNPAID COMMITMENTS CARRIED FORWARD | CREDITS AVAILABLE IN 2016 | COMMITMENTS MADE IN 2016 | ACCRUALS EXPENDITURE | UNPAID COMMITMENTS | UNUSED CREDITS |
|--------------------|----------------------------|---|--|---|---------------------------|--------------------------|----------------------|--------------------|----------------|
|                    | NSIP                       | 5,416   | 3,892  | 1,109   | 48,449                    | 5,406                    | 1,983                | 3,424              | 43,043         |
|                    | MULTINATIONAL              | 7,108   | 2,485  | 4,554   | 18,339                    | 7,656                    | 3,931                | 3,876              | 10,683         |
|                    | PARTNERSHIPS               | 1,879   | 584  | 970   | 543                       | 426                      | 71                   | 356                | 117            |
|                    | PARTNERSHIPS               | 3,587   | 1,410  | 1,976   | 6,057                     | 5,770                    | 2,267                | 3,504              | 287            |
|                    | PARTNERSHIPS               | 1,345   | 482  | 846   | 2,419                     | 2,142                    | 765                  | 1,377              | 277            |
|                    | PARTNERSHIPS               | 958   | 112  | 204   | 812                       | 385                      | 96                   | 289                | 427            |
|                    | NATO BODIES                | 0   | 50   | 26  | 646                       | 577                      | 136                  | 440                | 69             |
|                    | NATO BODIES                | 48,409  | 35,416                                       | 24,871  | 132,267                   | 81,884                   | 49,921               | 35,733             | 50,383         |
|                    | PARTNERSHIPS               | 70,689  | 19,502                                       | 22,778  | 29,965                    | 17,986                   | 1,321                | 16,665             | 11,979         |
|                    | PARTNERSHIPS               | 55  | 53   | 2   | 175                       | 125                      | 56                   | 69                 | 50             |
|                    | PARTNERSHIPS               | 0   | 0  | 0   | 2                         | 0                        | 0                    | 0                  | 2              |
|                    | OTHER AUTHORISED CUSTOMERS | 343   | 212  | 131   | 1,937                     | 1,192                    | 702                  | 490                | 745            |
|                    | PARTNERSHIPS               | 78  | 69   | 3   | 421                       | 276                      | 246                  | 31                 | 145            |
|                    | MULTINATIONAL              | 93  | 93   | 0   | 0                         | 0                        | 0                    | 0                  | 0              |
|                    | NATO BODIES                | 16,263  | 11,229                                       | 3,140   | 17,779                    | 17,779                   | 7,892                | 10,063             | 0              |
|                    | NATO BODIES                | 481   | 287  | 142   | 0                         | 0                        | 0                    | 0                  | 0              |
|                    | NSIP                       | 5,108   | 4,637  | 114   | 91,281                    | 2,290                    | 2,037                | 252                | 88,991         |
|                    | NATO BODIES                | 2   | 0  | 2   | 0                         | 0                        | 0                    | 0                  | 0              |
|                    | NATO BODIES                | 1,065   | 810  | 102   | 0                         | 0                        | 0                    | 0                  | 0              |
|                    | NATO BODIES                | 33  | 0  | 0   | 0                         | 0                        | 0                    | 0                  | 0              |
|                    | NATO BODIES                | 63  | 5  | 10  | 0                         | 0                        | 0                    | 0                  | 0              |
|                    | NATO BODIES                | 888   | 730  | 71  | 3,021                     | 2,754                    | 2,241                | 685                | 267            |
|                    | NSIP                       | 236   | 235  | 1   | 8,376                     | 0                        | 0                    | 0                  | 8,376          |
|                    | PARTNERSHIPS               | 3,085   | 2,957  | 94  | 9,026                     | 8,580                    | 1,891                | 6,689              | 446            |
|                    | PARTNERSHIPS               | 74  | 0  | 0   | 0                         | 0                        | 0                    | 0                  | 0              |
|                    | PARTNERSHIPS               | 1,144   | 328  | 816   | 365                       | 62                       | 14                   | 48                 | 303            |

Log Ops Business Unit – Jointly and Commonly Funded Operational Project Costs continues overleaf....

| Operational Budget | Source of Funding | PRIOR 2016<br>UNPAID<br>COMMITMENTS<br>BROUGHT<br>FORWARD | 2016<br>PAYMENTS<br>AGAINST<br>PRIOR 2016<br>COMMITMENTS | PRIOR 2016 UNPAID<br>COMMITMENTS<br>CARRIED<br>FORWARD | CREDITS<br>AVAILABLE IN<br>2016 | COMMITMENTS<br>MADE IN 2016 | ACCRUALS<br>EXPENDITURE | UNPAID<br>COMMITMENTS | UNUSED<br>CREDITS |
|--------------------|-------------------|---|--|--|---------------------------------|-----------------------------|-------------------------|-----------------------|-------------------|
|                    | PARTNERSHIPS      | 0   | 0  | 0  | 2                               | 0                           | 0                       | 0                     | 2                 |
|                    | NATO BODIES       | 4,800   | 0  | 0  | 0                               | 0                           | 0                       | 0                     | 0                 |
|                    | NATO BODIES       | 1,226   | 709  | 362  | 4,704                           | 4,540                       | 4,021                   | 520                   | 164               |
|                    | NATO BODIES       | 128   | 76   | 27   | 296                             | 280                         | 217                     | 68                    | 16                |
|                    | PARTNERSHIPS      | 1,359   | 687  | 673  | 168                             | 163                         | 0                       | 163                   | 5                 |
|                    | PARTNERSHIPS      | 65  | 1  | 64   | 35                              | 20                          | 5                       | 15                    | 15                |
|                    | NATIONAL          | 17,877  | 1,180  | 216  | 8,769                           | 8,906                       | 6,195                   | 2,865                 | -137              |
|                    | PARTNERSHIPS      | 116   | 2  | 114  | 0                               | 0                           | 0                       | 0                     | 0                 |
|                    | MULTINATIONAL     | 0   | 0  | 0  | 215                             | 215                         | 215                     | 0                     | 0                 |
|                    | PARTNERSHIPS      | 48,988  | 48,988   | 0  | 0                               | 0                           | 0                       | 0                     | 0                 |
|                    | PARTNERSHIPS      | 0   | 0  | 0  | 24,267                          | 4,261                       | 4,261                   | 0                     | 20,006            |
|                    | PARTNERSHIPS      | 33  | 11   | 0  | 52                              | 33                          | 30                      | 4                     | 19                |
|                    | PARTNERSHIPS      | 429   | 147  | 281  | 147                             | 112                         | 2                       | 109                   | 35                |
|                    | PARTNERSHIPS      | 1,307   | 398  | 909  | 1,632                           | 1,585                       | 1,401                   | 311                   | 47                |
|                    | PARTNERSHIPS      | 4,872   | 2,293  | 2,579  | 5,443                           | 3,571                       | 2,772                   | 1,454                 | 1,872             |
|                    | NATO BODIES       | 0   | 0  | 0  | 2,810                           | 2,810                       | 0                       | 2,810                 | 0                 |
|                    | NATIONAL          | 0   | 0  | 0  | 0                               | 0                           | 0                       | 0                     | 0                 |
|                    | PARTNERSHIPS      | 176   | 0  | 141  | 544,811                         | 502,326                     | 111,884                 | 390,442               | 42,485            |
|                    | NSIP              | 0   | 0  | 0  | 9,155                           | 4,319                       | 2,500                   | 1,819                 | 4,836             |
|                    | NATIONAL          | 10,376  | 10,139   | 49   | 48,714                          | 40,136                      | 39,457                  | 679                   | 8,578             |
|                    | NATIONAL          | 43,363  | 23,843   | 10,148   | 149,018                         | 122,939                     | 104,251                 | 18,859                | 26,079            |
|                    | NATIONAL          | 0   | 0  | 0  | 0                               | 0                           | 0                       | 0                     | 0                 |
|                    | NATO BODIES       | 26,537  | 20,575   | 5,065  | 2,665                           | 2,551                       | 2,403                   | 19                    | 114               |
|                    | NATIONAL          | 6,133   | 4,899  | 2  | 31,037                          | 23,574                      | 22,140                  | 6,179                 | 7,463             |
|                    | MULTINATIONAL     | 1,705   | 1,310  | 0  | 8,692                           | 6,392                       | 5,392                   | 1,223                 | 2,300             |

Log Ops Business Unit – Jointly and Commonly Funded Operational Project Costs continues overleaf....

| Operational Budget | Source of Funding            | PRIOR 2016 UNPAID COMMITMENTS BROUGHT FORWARD | 2016 PAYMENTS AGAINST PRIOR 2016 COMMITMENTS | PRIOR 2016 UNPAID COMMITMENTS CARRIED FORWARD | CREDITS AVAILABLE IN 2016 | COMMITMENTS MADE IN 2016 | ACCRUALS EXPENDITURE | UNPAID COMMITMENTS | UNUSED CREDITS |
|--------------------|------------------------------|---|--|---|---------------------------|--------------------------|----------------------|--------------------|----------------|
|                    | MULTINATIONAL                | 991   | 425  | 0   | 15,651                    | 10,219                   | 9,512                | 707                | 5,432          |
|                    | NATIONAL                     | 1,357   | 994  | 83  | 7,205                     | 5,572                    | 4,628                | 955                | 1,633          |
|                    | NATIONAL                     | 0   | 0  | 0   | 0                         | 0                        | 0                    | 0                  | 0              |
|                    | NATIONAL                     | 800   | 437  | 0   | 1,288                     | 1,194                    | 1,150                | 44                 | 94             |
|                    | MULTINATIONAL                | 2,736   | 2,654  | 82  | 1                         | 1                        | 1                    | 0                  | 0              |
|                    | NATIONAL                     | 0   | 0  | 0   | 85,624                    | 75,758                   | 64,023               | 16,761             | 9,866          |
|                    | NATIONAL                     | 0   | 0  | 0   | 6,840                     | 4,645                    | 3,896                | 963                | 2,195          |
|                    | NATIONAL                     | 0   | 0  | 0   | 13,797                    | 12,346                   | 4,426                | 9,269              | 1,451          |
|                    | NATIONAL                     | 0   | 0  | 0   | 8,028                     | 7,592                    | 7,565                | 54                 | 436            |
|                    | NATIONAL                     | 0   | 0  | 0   | 8,185                     | 7,851                    | 4,985                | 7,851              | 334            |
|                    | NATIONAL                     | 0   | 0  | 0   | 12,770                    | 7,271                    | 1,054                | 6,217              | 5,499          |
|                    | NATIONAL                     | 0   | 0  | 0   | 669                       | 627                      | 97                   | 530                | 42             |
|                    | NATIONAL                     | 0   | 0  | 0   | 1,024                     | 977                      | 98                   | 879                | 47             |
|                    | NATIONAL                     | 0   | 0  | 0   | 376                       | 310                      | 208                  | 102                | 66             |
|                    | MULTINATIONAL                | 8,257   | 5,045  | 2,189   | 89,487                    | 53,017                   | 47,413               | 5,788              | 36,470         |
|                    | MULTINATIONAL                | 0   | 0  | 0   | 5                         | 0                        | 0                    | 0                  | 5              |
|                    | PARTNERSHIPS / Replenishment | 345   | 153  | 120   | 2,117                     | 736                      | 262                  | 479                | 1,381          |
|                    | PARTNERSHIPS / Replenishment | 760   | 364  | 234   | 4,614                     | 2,562                    | 1,002                | 1,562              | 2,052          |
|                    | PARTNERSHIPS / Replenishment | 13  | 0  | 5   | 187                       | 23                       | 0                    | 23                 | 164            |
|                    | PARTNERSHIPS / Replenishment | 75  | 33   | 0   | 2,522                     | 74                       | 7                    | 67                 | 2,448          |
|                    | PARTNERSHIPS / Replenishment | 1,710   | 1,252  | 319   | 5,916                     | 2,517                    | 749                  | 1,768              | 3,399          |
|                    | PARTNERSHIPS / Replenishment | 0   | 0  | 0   | 173                       | 1                        | 1                    | 0                  | 172            |
|                    | PARTNERSHIPS / Replenishment | 0   | 0  | 0   | 23                        | 1                        | 1                    | 0                  | 22             |
|                    | PARTNERSHIPS / Replenishment | 476   | 439  | 25  | 2,574                     | 2,411                    | 909                  | 1,562              | 163            |
|                    | PARTNERSHIPS / Replenishment | 0   | 0  | 0   | 60                        | 0                        | 0                    | 0                  | 60             |

Log Ops Business Unit – Jointly and Commonly Funded Operational Project Costs continues overleaf....

| Operational Budget | Source of Funding                             | PRIOR 2016<br>UNPAID<br>COMMITMENTS<br>BROUGHT<br>FORWARD | 2016<br>PAYMENTS<br>AGAINST<br>PRIOR 2016<br>COMMITMENTS | PRIOR 2016<br>UNPAID<br>COMMITMENTS<br>CARRIED<br>FORWARD | CREDITS<br>AVAILABLE<br>IN 2016 | COMMITMENT<br>S MADE IN<br>2016 | ACCRUALS<br>EXPENDITUR<br>E | UNPAID<br>COMMITMEN<br>TS | UNUSED<br>CREDITS |
|--------------------|---|---|--|---|---------------------------------|---------------------------------|-----------------------------|---------------------------|-------------------|
|                    | NATO BODIES / Replenishment                   | 0   | 0  | 0   | 23                              | 0                               | 0                           | 0                         | 23                |
|                    | OTHER AUTHORISED<br>CUSTOMERS / Replenishment | 112   | 104  | 8   | 2,296                           | 201                             | 33                          | 168                       | 2,095             |
|                    | MULTINATIONAL / Replenishment                 | 0   | 0  | 0   | 3,389                           | 6                               | 3                           | 4                         | 3,383             |
|                    | PARTNERSHIPS / Replenishment                  | 7   | 0  | 7   | 975                             | 0                               | 0                           | 0                         | 975               |
|                    | PARTNERSHIPS / Replenishment                  | 809   | 685  | 43  | 2,479                           | 2,011                           | 546                         | 1,512                     | 468               |
|                    | PARTNERSHIPS / Replenishment                  | 0   | 0  | 0   | 1                               | 0                               | 0                           | 0                         | 1                 |
|                    | PARTNERSHIPS / Replenishment                  | 0   | 0  | 0   | 3                               | 0                               | 0                           | 0                         | 3                 |
| <b>GRAND TOTAL</b> |   | <b>356,340</b>  | <b>213,421</b>   | <b>85,707</b>   | <b>1,492,814</b>                | <b>1,081,946</b>                | <b>535,285</b>              | <b>568,798</b>            | <b>410,868</b>    |

\*For the "Transportation and FMS Charges" operational budget, the negative figure in respect of "unused credits" is because the credits authorised by the Agency Supervisory Board were surpassed in the year by customer-authorised purchases which were supported by customer funding.

The figures in the column "Prior 2016 unpaid commitments carried forward" do not represent the arithmetical differences between the amounts within column "Prior 2016 unpaid commitments brought forward" and "2016 payments against prior-2016 commitments"; these differences are mainly due to de-commitments/adjustments made during the reporting year 2013 against the open purchase orders/funds reservations from previous years forwarded in 2016. Unused Credits can be carried forward or lapsed depending on the rules governing the specific project of funder.



### 3. NAM Programme Business Unit

The NAM Programme bases its financial plan in USD and as such, the report on financial plan execution is reported here in USD.

| All figures in USD '000 | UNUSED AUTHORISED CREDITS AND UNPAID COMMITMENTS BROUGHT FORWARD | 2016 AUTHORISED CREDITS | PAYMENTS AGAINST COMMITTED AUTHORISED CREDITS | UNUSED AUTHORISED CREDITS AND COMMITMENTS CARRIED FORWARD | TOTAL CREDITS CONSUMED IN YEAR | LAPSED CREDITS  |
|-------------------------|--|-------------------------|---|---|--------------------------------|-----------------|
| Acquisition             | \$214,810  | \$7,907                 | \$31,364                                      | \$191,353   | \$222,717                      | \$0             |
| Operational             | \$361,530  | \$57,418                | \$89,790                                      | \$314,750   | \$404,540                      | \$14,408        |
| <b>Total</b>            | <b>\$576,340</b>   | <b>\$65,326</b>         | <b>\$121,154</b>                              | <b>\$506,103</b>  | <b>\$627,257</b>               | <b>\$14,408</b> |

| All figures in USD '000 | PRIOR 2016 UNPAID COMMITMENTS CARRIED FORWARD | 2016 AUTHORISED CREDITS | PAYMENTS AGAINST COMMITMENTS & AUTHORIZED CREDITS | UNPAID COMMITMENTS (i.e. LEGAL OBLIGATIONS) CARRIED FORWARD | TOTAL CREDITS CONSUMED IN YEAR | LAPSED CREDITS |
|-------------------------|---|-------------------------|---|---|--------------------------------|----------------|
| Administration          | \$401   | \$9,303                 | \$8,133   | \$175   | \$8,308                        | \$1,395        |

#### 4. Central Europe Pipeline System Business Unit

|                            | Budget Type               | PRIOR 2016<br>AUTHORISED<br>CREDITS<br>BROUGHT | 2016<br>AUTHORISED<br>CREDITS | BUDGETARY<br>EXPENDITURE<br>AGAINST<br>CREDITS | AUTHORISATI<br>ONS CARRIED<br>FORWARD | LAPSED<br>CREDITS |
|----------------------------|---------------------------|--|-------------------------------|--|---------------------------------------|-------------------|
| <b>Operational Budgets</b> |                           |  |                               |  |                                       |                   |
| Personnel                  | O&M                       | 392,956  | 58,779,300                    | 57,527,697                                     | 288,079                               | 1,356,481         |
|                            | NP2                       | 1,884,376                                      | -                             | 944,308  | 940,068                               | -                 |
|                            | NP3                       | 1,079,458                                      | 281,000                       | 518,614  | 557,419                               | 284,424           |
|                            | Business Case Germany     | 1,800  | 200,000                       | 156,653  | -                                     | 45,147            |
|                            | Business Case Netherlands | -  | 158,620                       | 158,477  | -                                     | 143               |
|                            | Depots                    | -  | 467,100                       | 450,075  | -                                     | 17,025            |
|                            |                           | <u>3,358,590</u>                               | <u>59,886,020</u>             | <u>59,755,824</u>                              | <u>1,785,566</u>                      | <u>1,703,221</u>  |
| Outside temporary staff    | O&M                       | 47,651   | 1,352,900                     | 1,177,219                                      | 133,057                               | 90,276            |
|                            | Business Case Germany     | -  | 26,000                        | 22,130   | -                                     | 3,870             |
|                            | Depots                    | 5,781  | 296,800                       | 290,554  | 2,724                                 | 9,303             |
|                            |                           | <u>53,433</u>                                  | <u>1,675,700</u>              | <u>1,489,903</u>                               | <u>135,781</u>                        | <u>103,449</u>    |
| Training of personnel      | O&M                       | 93,359   | 312,800                       | 311,317  | 75,201                                | 19,642            |
|                            |                           |  |                               |  |                                       |                   |
| Travel and transportation  | O&M                       | 29,613   | 3,710,100                     | 3,513,733                                      | 17,295                                | 208,685           |
|                            | Business Case Germany     | -  | 13,800                        | 3,147  | -                                     | 10,653            |
|                            | Business Case Netherlands | -  | 5,000                         | 1,657  | 500                                   | 2,843             |
|                            | Depots                    | -  | 72,000                        | 69,295   | -                                     | 2,705             |
|                            |                           | <u>29,613</u>                                  | <u>3,800,900</u>              | <u>3,587,833</u>                               | <u>17,795</u>                         | <u>224,886</u>    |
| Hospitality                | O&M                       | -  | 51,200                        | 41,612   | 2,506                                 | 7,082             |
| Operations                 | O&M                       | 2,460,739                                      | 20,409,800                    | 19,787,274                                     | 1,454,438                             | 1,628,827         |
|                            | Business Case Germany     | -  | 48,050                        | 40,602   | -                                     | 7,448             |
|                            | Business Case Netherlands | 1,284  | 21,700                        | 18,431   | 3,132                                 | 1,421             |
|                            | Depots                    | -  | 142,000                       | 134,819  | 4,727                                 | 2,454             |
|                            |                           | <u>2,462,023</u>                               | <u>20,621,550</u>             | <u>19,981,126</u>                              | <u>1,462,296</u>                      | <u>1,640,150</u>  |
| Maintenance                | O&M                       | 4,857,097                                      | 13,463,800                    | 12,226,162                                     | 5,043,870                             | 1,050,864         |
|                            | NP2                       | 4,081,590                                      | 2,500,000                     | 1,231,767                                      | 5,181,306                             | 168,518           |
|                            | NP3                       | 1,573,532                                      | 600,000                       | 512,670  | 1,107,239                             | 553,623           |
|                            | Business Case Germany     | 9,682  | 122,900                       | 32,124   | 92,537                                | 7,921             |
|                            | Business Case Netherlands | 38,623   | 285,000                       | 29,799   | 291,484                               | 2,340             |
|                            | Depots                    | 280,219  | 971,880                       | 795,395  | 424,298                               | 32,406            |
|                            |                           | <u>10,840,743</u>                              | <u>17,943,580</u>             | <u>14,827,917</u>                              | <u>12,140,733</u>                     | <u>1,815,673</u>  |

Central Europe Pipeline System Business Unit continued ....

| Budget Type                            |                           | PRIOR 2016<br>AUTHORISED<br>CREDITS<br>BROUGHT | 2016<br>AUTHORISED<br>CREDITS | BUDGETARY<br>EXPENDITURE<br>AGAINST<br>CREDITS | AUTHORISATI<br>ONS CARRIED<br>FORWARD | LAPSED<br>CREDITS       |
|--|---------------------------|--|-------------------------------|--|---------------------------------------|-------------------------|
| <b>Operational Budgets (continued)</b> |                           |  |                               |  |                                       |                         |
| General administrative expenses        | O&M                       | 1,557,582                                      | 10,785,040                    | 10,569,103                                     | 1,504,974                             | 268,545                 |
|  | Business Case Germany     | 60   | 7,800                         | 5,967  | 55                                    | 1,837                   |
|  | Business Case Netherlands | -  | 12,000                        | -  | 12,000                                | -                       |
|  | Depots                    | 25,165   | 118,000                       | 133,734  | 4,307                                 | 5,124                   |
|  |                           | <u>1,582,806</u>                               | <u>10,922,840</u>             | <u>10,708,804</u>                              | <u>1,521,336</u>                      | <u>275,506</u>          |
| <b>Capital</b>                         |                           |  |                               |  |                                       |                         |
| Fixed installations                    | NP2                       | 1,354,361                                      | -                             | -  | 1,354,361                             | -                       |
| Plant equipment                        | O&M                       | 241,766  | 1,587,000                     | 950,302  | 781,252                               | 97,213                  |
|  | Depots                    | 17,244   | 78,520                        | 85,852   | 1,608                                 | 8,304                   |
|  |                           | <u>259,010</u>                                 | <u>1,665,520</u>              | <u>1,036,154</u>                               | <u>782,860</u>                        | <u>105,516</u>          |
| Vehicles                               | O&M                       | 271,247  | 873,400                       | 806,436  | 288,675                               | 49,536                  |
| Office equipment                       | O&M                       | 1,313,998                                      | 1,173,660                     | 811,948  | 1,622,842                             | 52,868                  |
| <b>Long-Term Investments</b>           |                           |  |                               |  |                                       |                         |
| Modernisation 100%<br>CEPS             | O&M                       | 37,763,989                                     | 15,845,600                    | 15,253,522                                     | 36,772,723                            | 1,583,343               |
|  | Depots                    | 1,116,539                                      | 1,240,000                     | 1,149,423                                      | 1,203,105                             | 4,011                   |
|  |                           | <u>38,880,528</u>                              | <u>17,085,600</u>             | <u>16,402,945</u>                              | <u>37,975,828</u>                     | <u>1,587,354</u>        |
| INFRA projects - cost shares           | O&M                       | 1,046,325                                      | 102,250                       | 701,747  | 390,319                               | 56,508                  |
| <b>Grand Total</b>                     |                           | <u><b>61,546,035</b></u>                       | <u><b>136,115,020</b></u>     | <u><b>130,463,565</b></u>                      | <u><b>59,556,100</b></u>              | <u><b>7,641,391</b></u> |