	NATO	NORTH ATLANTIC COUNCIL
	OTAN	CONSEIL DE L'ATLANTIQUE NORD

NATO UNCLASSIFIED

5 February 2019

DOCUMENT
C-M(2019)0002-AS1

**IBAN AUDIT ON THE 2017 FINANCIAL STATEMENTS OF THE NATO ALLIANCE
GROUND SURVEILLANCE MANAGEMENT ORGANISATION**

ACTION SHEET

On 4 February 2019, under the silence procedure, the Council noted the IBAN report on the 2017 financial statements of NAGSMO attached to C-M(2019)0002, endorsed the RPPB report, and agreed to the public disclosure of the report, the IBAN audit report and associated 2017 financial statements of NAGSMO.

(Signed) Jens Stoltenberg
Secretary General

NOTE: This Action Sheet is part of, and shall be attached to C-M(2019)0002.

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28 January 2019

DOCUMENT
C-M(2019)0002
Silence Procedure ends:
4 Feb 2019 17:30

**IBAN AUDIT ON THE 2017 FINANCIAL STATEMENTS OF THE NATO ALLIANCE
GROUND SURVEILLANCE MANAGEMENT ORGANISATION**

Note by the Secretary General

1. I attach the International Board of Auditors for NATO (IBAN) report on the audit of the 2017 financial statements of the NATO Alliance Ground Surveillance Management Organisation (NAGSMO). The IBAN audit produced an unqualified opinion on the financial statements and a qualified opinion on compliance for NAGSMO.
2. The IBAN report has been reviewed by the Resource Policy and Planning Board (RPPB) (see Annex 1).
3. I do not believe this issue requires further discussion. Therefore, **unless I hear to the contrary by 17:30 hours on Monday, 4 February 2019**, I shall assume the Council noted the IBAN report on the 2017 financial statements of NAGSMO, endorsed the RPPB report, and agreed to the public disclosure of this report, the IBAN audit report and associated 2017 financial statements of NAGSMO.

(Signed) Jens Stoltenberg

Annex 1: RPPB report
Enclosure 1: IBAN audit + financial statements

1 Annex
1 Enclosure

Original: English

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-1-



**IBAN AUDIT ON THE 2017 FINANCIAL STATEMENTS OF THE NATO ALLIANCE
GROUND SURVEILLANCE MANAGEMENT ORGANISATION**

Report by the Resource Policy and Planning Board (RPPB)

References:

- | | |
|--------------------|--|
| A. IBA-A(2018)0139 | IBAN Audit on the 2017 Financial Statements of NAGSMO |
| B. CM(2015)0025 | NATO Financial Regulations (NFRs) |
| C. PO(2015)0052 | Wales Summit tasker on transparency and accountability |

BACKGROUND

1. This report addresses the IBAN audit of the 2017 financial statements and compliance of NAGSMO. The IBAN audit sets out an unqualified opinion on the financial statements and a qualified opinion on compliance of NAGSMO (reference A).

DISCUSSION

2. The IBAN found the information reflected in the financial statements is correct and NAGSMO was in compliance the NATO Civilian Personnel Regulations and NATO Financial Regulations with one exception. The exception, late submission of the financial statements, resulted in the IBAN issuing a qualified audit opinion on compliance. NFR Article 35.1 (reference B) states that the Financial Controller (FC) shall submit an annual financial statement for the NATO body not later than 31 March following the end of the financial year and the NAGSMO financial statements were submitted on 12 June 2018 due to Finance Department personnel unexpectedly leaving NAGSMA at year-end. The Finance Department is now staffed appropriately and the Financial Controller does not expect the delay to recur. No other observations were noted by the IBAN in 2017.

3. The IBAN followed up on the status of the only prior year observation and found some progress being made to achieve compliance with the NFRs, particularly those articles on internal control, risk management and internal audit. The RPPB notes that this is a common theme in the IBAN audits on the 2017 financial statements of many NATO Bodies and that NAGSMO will continue its efforts to ensure full compliance with the NFRs.

CONCLUSION

4. The IBAN issued an unqualified opinion on the financial statements and a qualified opinion on compliance for financial year 2017 due to the late submission of the financial statements. The RPPB stresses the importance of timely issuance of the financial statements and supporting information to the IBAN.

RECOMMENDATIONS

5. The RPPB recommends the Council:
 - 5.1. note the IBAN report (reference A);
 - 5.2. endorse the conclusion at paragraph 4; and
 - 5.3. approve the public disclosure of this report, the IBAN audit report and the associated 2017 financial statements of NAGSMO.



NORTH ATLANTIC TREATY ORGANIZATION
ORGANISATION DU TRAITÉ DE L'ATLANTIQUE NORD
INTERNATIONAL BOARD OF AUDITORS
COLLÈGE INTERNATIONAL DES COMMISSAIRES AUX COMPTES



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IBA-A(2018)0139
14 December 2018

To: Secretary General
(Attn: Director of the Private Office)

Cc: Chairman, NAGSMO Board of Directors
General Manager, NAGSMA
Financial Controller, NAGSMA
Chairman, Resource Policy & Planning Board (RPPB)
Head, Plans and Policy Branch, NATO Office of Resources (NOR)
Private Office Registry

Subject: ***International Board of Auditors for NATO (Board) Auditor's Report and Letter of Observations and Recommendations on the audit of the Financial Statements of the NATO Alliance Ground Surveillance Management Organisation (NAGSMO) for the year ended 31 December 2017 – IBA-AR(2018)0036***

The Board submits herewith its approved Auditor's Report (Annex 2) and Letter of Observations and Recommendations (Annex 3) with a Summary Note for distribution to the Council (Annex 1). A draft note by the Secretary General is attached.

The Board's report sets out an unqualified opinion on the Financial Statements of the NATO Alliance Ground Surveillance Management Organisation (NAGSMO) and a qualified opinion on compliance for financial year 2017.

Yours sincerely,

A handwritten signature in blue ink, appearing to read "Hervé-Adrien Metzger".

Hervé-Adrien Metzger
Chairman

Attachment: As stated above.



**Summary Note for Council
by the International Board of Auditors for NATO (Board)
on the audit of the Financial Statements
of the NATO Alliance Ground Surveillance Management Organisation
(NAGSMO)
for the year ended 31 December 2017**

The Board audited the Financial Statements for the year ended 31 December 2017. The NATO Alliance Ground Surveillance Management Organisation (NAGSMO) was created within NATO for the acquisition of the Alliance Ground Surveillance (AGS) Core System. NAGSMO is responsible for the overall management of the AGS program. It comprises a Board of Directors (BoD) and Working Groups with representatives from the participating Nations. It also comprises a NATO Management Agency led by a General Manager.

The budgetary expenditure for the administrative budget in 2017 was EUR 9.3 million. The budgetary expenditure for the operational budget in 2017 was EUR 7.7 million and USD 90.7 million.

The Board issued an unqualified opinion on the Financial Statements and a qualified opinion on compliance for the year ended 31 December 2017.

During the audit, the Board made one observation and provided a recommendation. The finding is in the Letter of Observations and Recommendations (Annex 3). This observation impacts the audit opinion on compliance.

1. Improvements needed in the financial reporting and audit readiness process.

The Board also followed up on the status of the observation from the previous year's audit and noted that the observation was outstanding.

NAGSMO had no formal comments.

14 December 2018

INTERNATIONAL BOARD OF AUDITORS FOR NATO

AUDITOR'S REPORT ON THE FINANCIAL STATEMENTS OF THE

**NATO ALLIANCE GROUND SURVEILLANCE
MANAGEMENT ORGANISATION**

(NAGSMO)

FOR THE YEAR ENDED 31 DECEMBER 2017

**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 (referred to as the Board) audited the accompanying financial statements of the NATO Alliance Ground Surveillance Management Organization (NAGSMO), which comprised the Statement of Financial Position as at 31 December 2017, and the Statement of Financial Performance, Statement of Changes in Net Assets/Equity and Cash Flow Statement for the year then ended, and a summary of significant accounting policies and other explanatory notes. The Board also audited the Budget Execution Statements for the year ended 31 December 2017.

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. 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 qualified opinion on the financial statements.

Opinion on Financial Statements

In our opinion, the financial statements present fairly, in all material respects, the financial position of NAGSMO as at 31 December 2017, and of its financial performance and its cash flows for the year then ended in accordance with the NATO Accounting Framework.

Report on Compliance

Management's Responsibility for Compliance

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

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 authorized 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 qualified audit opinion on compliance.

Basis for Qualified Opinion on Compliance

The NFRs require the financial statements to be submitted for audit to the Board by the Financial Controller no later than 31 March following the end of the financial year. The financial statements of the NAGSMO for the year ended 31 December 2017, though, were only submitted on 12 June 2018.

Qualified Opinion on Compliance

In our opinion, except for the matters 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, 14 December 2018

A handwritten signature in blue ink, appearing to read 'H. Metzger', with a long horizontal stroke extending to the right.

Hervé-Adrien Metzger
Chairman

14 December 2018

INTERNATIONAL BOARD OF AUDITORS FOR NATO

LETTER OF OBSERVATIONS AND RECOMMENDATIONS

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

(NAGSMO)

FOR THE YEAR ENDED 31 DECEMBER 2017

Introduction

The International Board of Auditors for NATO (referred to as the Board) audited the NATO Alliance Ground Surveillance Management Organisation (NAGSMO) Financial Statements for the year ended 31 December 2017, and issued an unqualified opinion on those financial statements and a qualified opinion on compliance.

Observations and Recommendations

During the audit, the Board made one observation and recommendation. This observation impacts the audit opinion on compliance.

1. Improvements needed in the financial reporting and audit readiness process.

The Board also followed up on the status of the observation from the previous year's audit and noted that the observation was outstanding.

The Board also issued a Management Letter (reference IBA-AML(2018)0020) to NAGSMO management with three observations for management's attention.

This Letter of Observations and Recommendations was formally cleared with NAGSMO.

OBSERVATIONS AND RECOMMENDATIONS

1. IMPROVEMENTS NEEDED IN THE FINANCIAL REPORTING AND AUDIT READINESS PROCESS

Reasoning

1.1 Article 35 of the NFRs states that annual financial statement for each NATO body, consolidated where applicable and appropriate, should be submitted for audit to the International Board of Auditors for NATO by the Financial Controller not later than 31 March following the end of the financial year.

1.2 It is NAGSMO's responsibility to prepare in a timely manner financial statements that are auditable and free from material errors or misstatements. This responsibility includes conducting an analysis and providing supporting explanations for all account balances and disclosures reported in the financial statements.

Observation

1.3 NAGSMA experienced difficulties related to the preparation of the 2017 Financial Statements of NAGSMO due to Finance Department personnel unexpectedly leaving the Agency at year-end. Although, NAGSMA was able to contract consultancy services, these difficulties led NAGSMA to submit the 2017 Financial Statements of NAGSMO to the Board on 12 June 2018, therefore not respecting the 31 March deadline as required by the NFRs. The late issuance of the financial statements therefore results in a qualification of the audit opinion on compliance.

1.4 Furthermore, the outstanding balance relating to advances from Nations at 31 December 2017 amounting to EUR 77.3 million (note B06) was not fully supported by detailed reconciliations prior to the start of the audit. It is important to ensure that all balances and disclosures in the financial statements are fully reconciled and supported by documentation because this demonstrates financial stewardship and helps to ensure the overall efficiency of the financial reporting and audit process.

Recommendation

1.5 The Board recommends that NAGSMA improves its financial reporting and audit readiness process. This can be achieved by ensuring that auditable financial statements are produced in a timely manner and that all balances and disclosures in the financial statements are fully reconciled and supported by documentation prior to the start of the audit.

FOLLOW-UP OF PREVIOUS YEAR'S OBSERVATION

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

OBSERVATION / RECOMMENDATION	ACTION TAKEN	STATUS
<p>(1) NAGSMO FY 2016 IBA-AR(2017)20, paragraph 1.7 SOME PROGRESS BEING MADE TO ACHIEVE COMPLIANCE WITH THE NATO FINANCIAL REGULATIONS, PARTICULARLY THOSE ARTICLES ON INTERNAL CONTROL, RISK MANAGEMENT AND INTERNAL AUDIT</p> <p>Board's Recommendation The Board recommends that:</p> <p>a) NAGSMA perform a systematic and detailed assessment and documentation of its internal control procedures to support compliance with its recently approved internal control framework, COSO.</p> <p>b) NAGSMA's outsourced Internal Audit function fully evaluate internal control throughout NAGSMA, and that this work be clearly documented so as to be able to conclude as to NAGSMA's compliance against COSO.</p>	<p>a) The internal control procedures have been documented, but these should be more specific and related to the entity's own objectives, control environment and risks.</p> <p>b) No evaluation by the Internal Audit has been performed yet.</p>	<p>Observation Outstanding (In-Progress).</p>

NAGSMO

2017

FINANCIAL STATEMENTS



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NATO ALLIANCE GROUND SURVEILLANCE MANAGEMENT AGENCY

NAGSMA



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Tel: +32 2 707 1801 Email: nagsma@nagsma.nato.int

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NATO ALLIANCE GROUND SURVEILLANCE MANAGEMENT AGENCY

NAGSMA



NAGSMA/FC/L/(2018)003362
12 June 2018

International Board of Auditors for NATO

Attention: NAGSMO Board of Directors - Chairman and National Representatives

Subject: **NAGSMO Financial Statements - Year ending 31 December 2017**

Enclosed are the NAGSMO 2017 Financial Statements. Please note that the enclosed statements are subject to audit by the International Board of Auditors for NATO.

For the General Manager

A handwritten signature in blue ink, reading 'Grazia M. D'Arcangelo'.

Grazia M. D'Arcangelo
NAGSMA Financial Controller

Encl.: NAGSMO Financial Statements for the year ending 31 December 2017.

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NAGSMA NATO HQ
Boulevard Léopold III
B-1110 Brussels - Belgium
Tel: +32 2 707 1801 Email: nagsma@nagsma.nato.int

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

THE NATO ALLIANCE GROUND SURVEILLANCE PROGRAMME

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

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

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

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

THE AGS CORE

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

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

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

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

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

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

NATO ALLIANCE GROUND SURVEILLANCE MANAGEMENT ORGANISATION

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

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

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

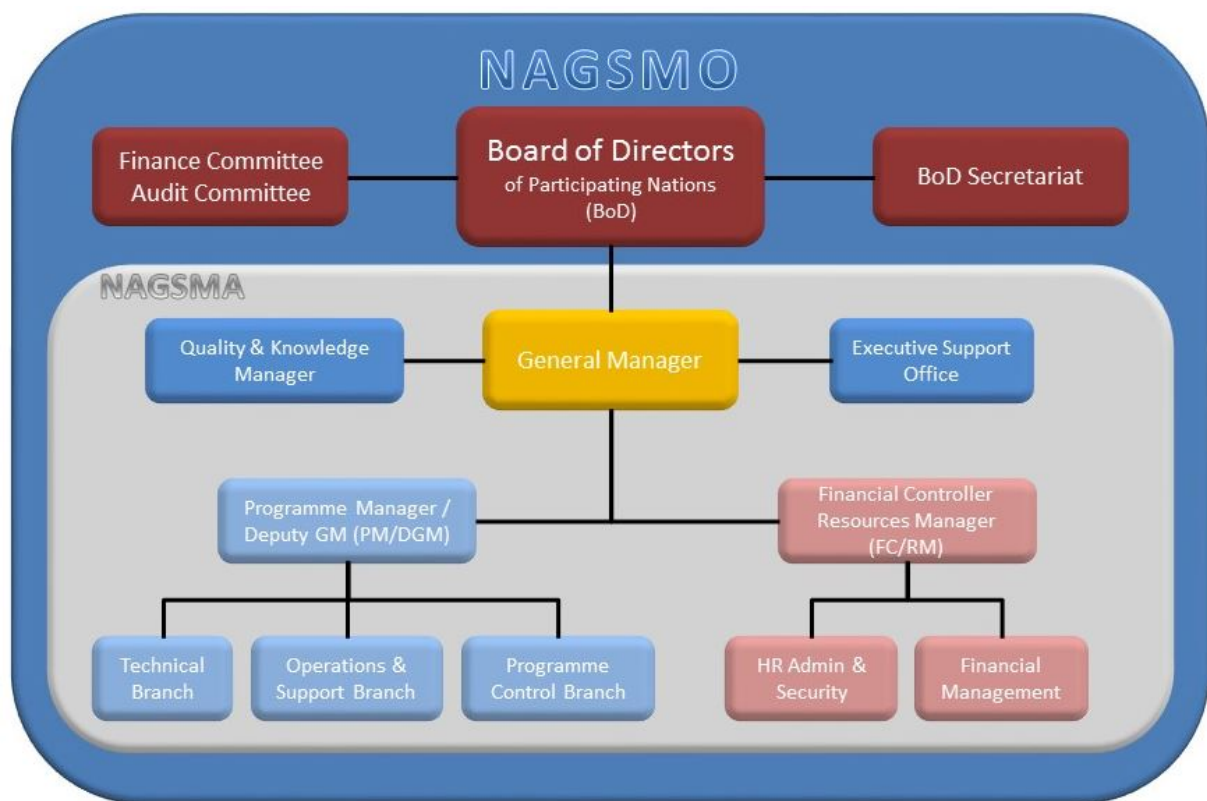
The principal task of the NAGSMO is to ensure the planning and implementation of a harmonised AGS Programme, which satisfies the operational requirements, in accordance

with the provisions of the PMOU, and with due regard to the NAGSMO Member States' views on political, economic, industrial and technological factors. NAGSMO shall assume the functions of overall management of the AGS Programme, including:

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

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

The diagram below depicts the NAGSMO and NAGSMA organizational structure in 2017.



NAGSMA and Service Support/Level Agreement

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

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

The NAGSMO BoD approved the revised NAGSMO FMPD-FRP in June 2016 to comply with revised NATO Financial Regulations. The NAGSMO FMPD-FRP recognises the withdrawal of Canada and the re-entry of Denmark, the conversion parameters from Then-Year to Base-Year, the call for contribution structure and the proposed structure of the Operational Budget. The NAGSMO FMPD-FRP conforms to the provision of the NATO Financial Regulations.

NAGSMA 2017 Administrative Budget

In December 2016 the NAGSMO BoD approved the 2017 NAGSMA Administrative Budget. The 2017 Administrative Budget funded NAGSMA's expenditures from 1 January to 31 December 2017. In 2017 NAGSMA continued finding cost-effective manpower and increased performance solutions. In accordance with the extension of the NAGSMA Administrative Budget into 2019 and 2020 and NAGSMA Staffing Plan for 2019 and 2020, NAGSMA extended staff contracts through 2019 and 2020 in order to retain personnel and maintain needed support for the execution of the programme. Notwithstanding the efforts of the Agency, it has been challenging to recruit new and to keep current staff members in the Agency.

In 2017 NAGSMA's administrative expenditures were considerably lower than what had been anticipated. 55% of the total savings were in Chapter I. The majority of savings were generated in basic salary, consultancy, and education allowance. Savings in basic salary resulted from early departures of staff and lower actual personnel strength than what was approved in the NAGSMA Staffing Plan 2017.

In Chapter II, Operations and Maintenance, the Agency successfully negotiated two amendments for the Service Support Agreement and an annual Service Support Package with the NCI Agency for external administrative and IT support. It also received administrative and operational support from the NATO IS under the Memorandum of Agreement. 35% of savings in Chapter II were primarily related to a delayed move to the New NATO HQ and travel on duty. The remaining 9% of administrative savings were in risk management.

NAGSMA 2017 Operational Budget

In December 2016, the NAGSMO BoD approved the 2017 NAGSMA Operational Budget. The budget was approved to fund prime contract related AGS Core acquisition expenditures in 2017.

The NAGSMA EUR Operational Budget was increased at no cost to Nations to cover Danish Industrial Participation, approved in December 2016 (NAGSMA-CON-0100).

In April 2012, the NAGSMO BoD approved the request by Estonia to apply Pre-PMOU Contributions (PPC) credits towards the 2013-2017 Financial Year (FY) Operational Budget. In November 2015, the NAGSMO BoD approved the requests of Germany and Italy to apply their PPC credits to 2016-2017 FY Operational Budgets. In June 2016, the NAGSMO BoD approved for Lithuania to apply their PPC credits to Lithuania's contribution to the NAGSMA Operational Budget.

The NAGSMO BoD authorized in February 2012 the USA Non-Financial Contributions (NFC) to be expensed from the Operational Budget from 2013 to 2017 upon confirmation of support costs incurred at Edwards Air Force Base (EAFB). At the NAGSMO BoD meeting in March 2013, the NFC proposal from Italy was accepted and Italy was granted authorization to expense the Non-Financial Contributions for the airworthiness certification (AWC) efforts. In May 2017, the NAGSMO BoD approved additional funding for Italy's NFC. These costs have been expensed in 2017 based on the presentation of invoices from Nations of the actual costs incurred in support of programmatic needs.

Major Achievements FY 2017:

In 2017, the AGS Programme achieved the following important milestones:

- Air Vehicle component manufacturing production complete.
- All aircraft are now in final assembly or test at Palmdale or Edwards Air Force Base.
- Radar production complete, MP-RTIP radars 1-5 delivered.
- Started MP-RTIP-Radar integration on aircraft NA-04 & NA-05 in the fall.
- Contractor Development Test Flights through Flight #8. With a total flight time of 10.8 hours, Flight #8 demonstrated end-to-end system and sensor checks, including AVMC2 control from MOB Sigonella and MGGS reception of live GMTI data.
- MOS, MGGS and TGGS installation and integration testing, including system-level activities, at MOB Sigonella.

- Test and Verification made significant progress. As of the end of 2017, percent (%) complete as follows:

<i>Element</i>	<i>% Complete</i>
AVMC2	4%
MGGS	75%
MOS	83%
TGGS	69%
Trainer	0%
UAV	16%
Entity-Level	47%
System-Level	0%
Overall	43%

- Warehouse setup in Sigonella started and near completion.
- SATCOM facility activation in Sigonella completed, authorization to radiate provided by the ITA MOD AIRSTAFF with some limitation (to be removed in 2018 following further tests).
- Initiated procurement of 21 Connex containers to be used as Office and Lab space (CAFX). Delivery should be completed by June, 2018.
- Provisioning conferences for the identification of spare parts continued in 2017. Air Segment 98% complete (US Eyes Only Items still to be finalized), MGGS completed.
- Peculiar Support Equipment delivery to Sigonella progressed to 75%.
- The Combined Validation and Verification (CVV) of the Air Segment Technical Publications begun, giving priority to the Airworthiness relevant Data Modules (DMs).
- DAAA norms to be used for Continued & Continuing Airworthiness (post Air Segment acceptance) are being translated and tailored to the NATO AGS specific case. Ten (10) norms have been given higher priority and have been translated; three have been fully tailored and formally approved by DAAA General Director.
- Both Deployable UAV Command and Control Elements (DUCE) were functionally complete (one at Palmdale, one at EAFB).
- Approximately 90% of the MGGS subsystem Hardware items (MGEC, MGCC) have been completed at the sub-sub-suppliers (RETIA, Konstrukta) and have been accepted by Airbus Defence and Space.
- The MOS development unit assembled in Torino is in use for integration testing, including supporting formal T&V activities.
- The TGGS development items and components were procured and assembled to support verification testing in Torino.
- The Wide Band Data Link (WBDL) continues development and integration testing and is the subject of delay. Leonardo redesigned the Ground Data Terminal trailer to meet environmental requirements.

- In support of AGS Core System acquisition contract Rebaselining activities, NAGSMA reduced individual event T&V execution by 90 calendar days, eliminating redundant contract information reporting requirements, streamlining event preparation and documentation reviews, and leveraging contactor development testing.
- Several training activities together with the NATO AGS Force took place in 2017. Among them were the NATO Test Team Training for UAV Maintenance and Communications Maintenance for AVMC2, Mission Common, Pilot Initial Qualification Training (IQT)/Mission Qualification Training (MQT), Surveillance Operator AVMC2 IQT/MQT, Surveillance Operator MGGS IQT/Human Mission Interface, IQT Deployment and MGGS IQT Deployment Training at MOB.
- Contract Amendment 20 to the AGS Core Contract for Installation and Testing (UAV 05) and 4 retrofit kits (UAV 01-04) of Link 16 was signed in December, 2017.
- Contract Amendment 21 to the AGS Core Contract for definitization of the REAs for Block Load, Lot 11 & Triton EOQ, Triton LSA and was signed in June, 2017.
- Contract Amendment 22 to the AGS Core Contract for Initial – In Service Support (I-ISS) non-recurring SLPV spare parts, warehousing and a correction to the Peculiar Support Equipment List was signed in December, 2017.
- For I-ISS non-recurring spare parts, a budgetary ceiling to cover up to 10 Work-Orders (WO) was approved with CCO 016 in April, 2016. The first FFP for WO #03 was received on 21 Dec 2016 and definitized. FFPs for WO #2 and #04 have been received in November, 2017 and will be included in the next Contract Amendment together with WO #03.
- For I-ISS recurring (phase II), three separate Requests For Proposals (RFPs) were issued to NGISSII, AIRBUS (to include Kongsberg) and LEONARDO to procure 15 Months of Maintenance Services for Air and Ground Segments following SDDQ complete. The RFPs were supported by several Workshops involving Industry and NATO Stakeholders.
- A contract with the Danish company TERMA was signed 20 September 2016 to design/develop/qualify/produce the Phase I of the Automatic Target Recognition/Identification (ATR/ATID) software and is under execution. Conducted an Integration Technical Interchange Meeting & continuing coordination.
- A contract with the Polish company EXENCE was signed on 6 December 2016 to design/develop/qualify/produce the NATO TSEC training management system. Started Critical Design Review (CDR); received and reviewing supporting documentation; conducted 2nd Verification Planning Working Group (VPWG) Meeting, and conducted Sigonella Site Survey and Usability Assessment.
- A contract with the Polish company PIT-RADWAR was signed on 5 September 2017 to design/develop/qualify/produce the CSOP (Core Software Only Package).
- A contract with the Polish company ITWL was signed on 17 October 2017 to design/develop/qualify/produce the Battle-Laboratory. Contract work has begun.
- A contract with the Norwegian company Kongsberg was signed on 03 November 2017 to provide support to the SMARF.

NAGSMA Assets

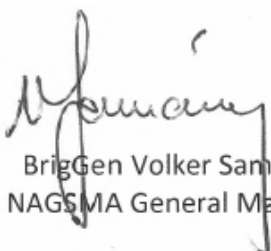
Office space, including furniture, IT and other equipment is provided by the NCI Agency via the SSA.

NAGSMO & NAGSMA Acting as a Procurement Agent

The North Atlantic Council (NAC) established NAGSMO by approving its Charter. The Charter clearly establishes that NAGSMO is a subsidiary body of NATO and states that the objective is to procure the AGS Core which will be owned, controlled and operated by NATO. NAGSMA is an entity acting as an agent with no control over the assets procured. The AGS Participating Nations reiterated the specific nature of the AGS Programme: temporary existence of the Agency and that the Agency will not own any asset. In order to comply with the NATO Accounting Framework, the end-user of AGS system will account for all NAGSMA procured assets in the future. NAGSMA will fully disclose and provide at the end of each reporting period to relevant end-user NATO entity all financial data regarding the assets procured. NAGSMA responded to this year's request for information that no assets were procured for the financial year ending in December 2017.

CERTIFICATION

1. The NAGSMO 2017 Financial Statements are submitted to the International Board of Auditors for NATO.
2. The Financial Statements will be audited in accordance with the following reference documents:
 - a. The NAGSMO FMPD-FRP conform to the NFRs, Part II as approved by the North Atlantic Council (NAC) in C-M(2015)0025.
 - b. PO(2002)109, dated 23 July 2002: the document from the NAC adopting IPSAS, including the accrual and going concern assumptions, as the applicable accounting standards for all NATO entities effective for the financial year of 2006.
 - c. The NATO Accounting Framework has been developed to provide minimum requirements for financial reporting for all NATO Reporting Entities following approval of C-M(2016)0023 by the North Atlantic Council on 29 April 2016 of an IPSAS-adapted accounting framework for the Alliance.
3. The NAGSMO Financial Statements are certified by the NAGSMA Financial Controller to the best of her knowledge and according to the applicable accounting standards to give a true and fair view of the assets, liabilities, financial position and financial performance of NAGSMO and to be in accordance with the books and records maintained by the NCI Agency and NAGSMA.
4. The NAGSMO Financial Statements may be disclosed to the general public.



BrigGen Volker Samanns
NAGSMA General Manager



Grazia M. D'Arcangelo
NAGSMA Financial Controller

STATEMENT ON INTERNAL CONTROL

This statement of internal control applies to the Financial Statements of NAGSMA, as the executive body of NAGSMO, for the year ended 31 December 2017.

Scope of responsibility

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

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

Purpose of the System of Internal Control

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

The process within NAGSMA accords with the NAGSMO FMPD-FRP and has been in place for the year ending 31 December 2017 and up to the date of approval of the Financial Statements.

Risk and Control Framework

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

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

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

Review of Effectiveness

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

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

Appropriate action is in place to address any weaknesses identified and to ensure the continuous improvement of the system. During 2017, no material instances of failure to the internal control system were reported that should be brought to your attention.



BrigGen Volker Samanns
NAGSMA General Manager



Grazia M. D'Arcangelo
NAGSMA Financial Controller

NAGSMO – Statement of Financial Position
as at 31 December 2017
(all amounts in Euro)

	Notes	Current Year	Prior Year
	ANNEX B	31-Dec-17	31-Dec-16
ASSETS			
Cash and cash equivalents	B01	326,482,728	358,284,643
Short-term investments	B02	0	0
Receivables	B03	10,970,437	36,378,945
Other current assets and prepayments	B04	144,398	138,665
Current assets		337,597,563	394,802,253
TOTAL ASSETS		337,597,563	394,802,253
LIABILITIES			
Payables	B05	1,395,944	3,670,674
Advances and deferred revenue	B06	174,051,593	246,067,627
Short term provisions	B07	139,211	138,665
Other current liabilities	B08	162,010,815	144,925,287
Current liabilities		337,597,563	394,802,253
NET ASSETS/EQUITY			
Accumulated surpluses/(deficits)		0	0
Net Assets/Equity		0	0
TOTAL LIABILITIES		337,597,563	394,802,253

NAGSMO – Statement of Financial Performance
for the year ended 31 December 2017
(all amounts in Euro)

	Notes	Current Year	Prior Year
	ANNEX C	2017	2016
REVENUE			
Revenue from non-exchange transactions	C01	9,275,725	9,738,884
Revenue		9,275,725	9,738,884
EXPENSES			
Personnel	C02	6,743,211	7,468,607
Contractual supplies and services	C03	2,532,514	2,270,277
Expenses		9,275,725	9,738,884
NET SURPLUS/(DEFICIT)		0	0
NET SURPLUS/(DEFICIT) ALLOCATION			
Reserves		0	0
Accumulated surpluses/(deficits)		0	0
Net surplus/(deficit) allocation		0	0

NAGSMO – Cash Flow Statement (Indirect Method)
for the year ended 31 December 2017
(all amounts in Euro)

	Notes	Current Year	Prior Year
	ANNEX D	2017	2016
CASH FLOW FROM OPERATING ACTIVITIES			
Cash flow from operating and other activities			
Net surplus/(deficit)		0	0
Total cash flow from operating and other activities		0	0
Decrease/(increase) Current assets			
Decr./(incr.) Other current assets and prepayments		(5,734)	(22,479)
Decr./(incr.) Receivables		25,408,508	23,210,325
Decr./(incr.) Short-term investments		0	0
Total decrease/(increase) Current assets		25,402,774	23,187,846
Increase/(decrease) Current liabilities			
Incr./(decr.) Provisions		546	22,479
Incr./(decr.) Other current liabilities		17,085,528	141,296,928
Incr./(decr.) Payables		(2,274,729)	3,200,420
Incr./(decr.) Advances and deferred revenue		(72,016,034)	(141,664,048)
Total increase/(decrease) Current liabilities		(57,204,689)	2,855,779
NET CASH FLOW FROM OPERATING ACTIVITIES		(31,801,915)	26,043,625
NET CASH FLOW FROM INVESTING ACTIVITIES		0	0
NET CASH FLOW FROM FINANCING ACTIVITIES		0	0
NET INCREASE/(DECREASE) CASH AND CASH EQUIVALENTS		(31,801,915)	26,043,625
CASH AND CASH EQUIVALENTS AT THE BEGINNING OF THE PERIOD		358,284,643	332,241,018
CASH AND CASH EQUIVALENTS AT THE END OF THE PERIOD		326,482,728	358,284,643

**NAGSMO – Statement of Changes in Net Assets/Equity
for the year ended 31 December 2017
(all amounts in Euro)**

BALANCE AT 31-DECEMBER-2016	0
Net surplus for the period	0
BALANCE AT 31-DECEMBER-2017	0
NET CHANGE IN ASSETS/EQUITY (OPERATING FUND) FOR THE YEAR ENDED 31-DECEMBER-2017	0

NAGSMO Budget Execution Statement - Administrative Budget
for the year ended 31 December 2017
(All amounts in Euro)

Notes	Initial Authorisation	Mid-year Review (MYR)	Final Approval - MYR	Transfers	Final Authorisation	Net Commitment	Actual Expenses	Total	Carry Forward	Lapsed
ANNEX E										
				MYR	FA					
Personnel										
E01	0	0	0	0	0	0	(730)	(730)	0	730
E02	9,049,365	(1,381,792)	7,667,573	0	7,667,573	0	6,743,395	6,743,395	0	924,178
Total Personnel	9,049,365	(1,381,792)	7,667,573	0	7,667,573	0	6,742,665	6,742,665	0	924,908
Contractual supplies and services										
E03	0	0	0	0	0	0	(4,815)	(4,815)	0	4,815
E04	3,612,091	(484,481)	3,127,610	0	3,127,610	0	2,537,127	2,537,127	0	590,483
Total Contractual supplies and services	3,612,091	(484,481)	3,127,610	0	3,127,610	0	2,532,312	2,532,312	0	595,298
Capital and investment budgeting										
E05	0	0	0	0	0	0	0	0	0	0
2017 - Capital and investment	5,000	0	5,000		5,000	0	201	201	0	4,799
Total Capital and investment budgeting	5,000	0	5,000	0	5,000	0	201	201	0	4,799
Budget contingencies										
E06	0	0	0	0	0	0	0	0	0	0
2016 - Budget contingencies	200,000	(50,000)	150,000		150,000	0	0	0	0	150,000
Total Budget contingencies	200,000	(50,000)	150,000	0	150,000	0	0	0	0	150,000
TOTAL BUDGET EXECUTION	12,866,456	(1,916,273)	10,950,183	0	10,950,183	0	9,275,179	9,275,179	0	1,675,004

NAGSMO Budget Execution Statement - Operational Budget Total
for the year ended 31 December 2017
(All amounts in Euro equivalent)

Notes	Initial Authorisation	Mid Year - Review (MYR)	Final Approval - MYR	Transfers	Final Authorisation	Net Commit-ment	Actual Expenses	Total Spend	Carry Forward	Lapsed
ANNEX F										
		MYR			FA					
AGS Core System Procurement										
2014 - AGS Core System Procurement	11,485,647	0	11,485,647	0	11,485,647	1,046,302	0	1,046,302	1,046,302	10,439,345
2015 - AGS Core System Procurement	78,480,689	0	78,480,689	0	78,480,689	1,055,797	2,719,983	3,775,781	1,055,797	74,704,909
2016 - AGS Core System Procurement	50,684,616	0	50,684,616	0	50,684,616	9,232,112	2,497,559	11,729,671	9,232,112	38,954,945
2017 - AGS Core System Procurement	148,771,152	(22,313,086)	126,458,066	(0)	126,458,065	3,411,910	82,714,432	86,126,342	3,411,910	40,331,723
TOTAL AGS Core System Procurement	289,422,104	(22,313,086)	267,109,018	0	267,109,017	14,746,121	87,931,975	102,678,096	14,746,121	164,430,921

ECB Rate avg. from Jan 1 2017 to Dec 31 2017 was 1.1297

NAGSMO Budget Execution Statement - Operational Budget (EUR part)
for the year ended 31 December 2017
All amounts in Euro

Notes	Initial Authorisation	Mid Year - Review (MYR)	Final Approval - MYR	Transfers	Final Authorisation	Net Commitment	Expenses	Total Spend	Carry Forward	Lapsed*
ANNEX F			MYR		FA					
System Design, Development and Qualification										
2014 - System Design, Development and Qualification	2,182,711	0	2,182,711	0	2,182,711	0	0	0	0	2,182,711
2015 - System Design, Development and Qualification	8,584,980	0	8,584,980	0	8,584,980	1,000,000	200,000	1,200,000	1,000,000	7,384,980
2016 - System Design, Development and Qualification	15,654,183	0	15,654,183	0	15,654,183	2,000,000	(1,147,480)	852,520	2,000,000	14,801,663
2017 - System Design, Development and Qualification	0	137,173	137,173	140,000	277,173	137,173	140,000	277,173	137,173	0
Total System Design, Development and Qualification	26,421,874	137,173	26,559,047	140,000	26,699,047	3,137,173	(807,480)	2,329,693	3,137,173	24,369,354
Production										
2014 - Production	1,374,166	0	1,374,166	0	1,374,166	0	0	0	0	1,374,166
2015 - Production	9,949,193	0	9,949,193	0	9,949,193	0	0	0	0	9,949,193
2016 - Production	8,264,963	0	8,264,963	0	8,264,963	0	0	0	0	8,264,963
2017 - Production	0	5,034,450	5,034,450	0	5,034,450	0	0	0	0	5,034,450
Total Production	19,588,322	5,034,450	24,622,772	0	24,622,772	0	0	0	0	24,622,772
Management Reserve										
2015 - Management Reserve	1,269,777	0	1,269,777	0	1,269,777	0	1,269,777	1,269,777	0	0
2016 - Management Reserve	416,209	0	416,209	0	416,209	219,370	196,839	416,209	219,370	0
2017 - Management Reserve	18,386,286	(7,581,032)	10,805,254	(1,140,000)	9,665,254	746,486	715,961	1,462,447	746,486	8,202,807
Total Management Reserve	20,072,272	(7,581,032)	12,491,240	(1,140,000)	11,351,240	965,856	2,182,576	3,148,433	965,856	8,202,807
CAFX										
2015 - CAFX	0	0	0	0	0	0	(9,058)	(9,058)	0	9,058
2016 - CAFX	213,385	0	213,385	0	213,385	1,156	(96,932)	(95,776)	1,156	309,161
2017 - CAFX	215,000	0	215,000	0	215,000	47,833	159,310	207,143	47,833	7,857
Total CAFX	428,385	0	428,385	0	428,385	48,989	53,320	102,309	48,989	326,076
IIS										
2017 - IIS	25,096,417	(12,475,289)	12,621,128	(0)	12,621,128	271,992	389,610	661,602	271,992	11,959,526
Total IIS	25,096,417	(12,475,289)	12,621,128	(0)	12,621,128	271,992	389,610	661,602	271,992	11,959,526
ATR / ATID										
2017 - ATR / ATID	0	3,600,000	3,600,000	0	3,600,000	0	3,600,000	3,600,000	0	0
Total ATR / ATID	0	3,600,000	3,600,000	0	3,600,000	0	3,600,000	3,600,000	0	0
NCB										
2017 - NCB	0	2,409,409	2,409,409	1,000,000	3,409,409	1,169,409	2,240,000	3,409,409	1,169,409	0
Total NCB	0	2,409,409	2,409,409	1,000,000	3,409,409	1,169,409	2,240,000	3,409,409	1,169,409	0
	91,607,269	(8,875,289)	82,731,981	(0)	82,731,980	5,593,419	7,658,026	13,251,445	5,593,419	69,480,535

* Includes EUR 126,090 of unused DNK fund (not for distribution to the 14 AGS Nations)

NAGSMO Budget Execution Statement - Operational Budget (USD part)
for the year ended 31 December 2017
All amounts in USD

Notes	Initial Authorisation					Mid Year - Review (MYR)	Final Approval - MYR	Transfers	Final Authorisation	Net Commit-ment	Expenses	Total Spend	Carry Forward	Lapsed
	ANNEX F													
	MYR													
	FA													
System Design, Development and Qualification	2014 - System Design, Development and Qualification	3,722,930	0	3,722,930	0	3,722,930	0	3,722,930	1,182,007	0	1,182,007	1,182,006	2,540,923	
	2015 - System Design, Development and Qualification	36,147,305	0	36,147,305	0	36,147,305	0	209,344	209,344	0	209,344	6,845,552	35,937,961	
	2016 - System Design, Development and Qualification	10,622,245	0	10,622,245	0	10,622,245	0	3,091,069	9,936,621	6,845,552	3,091,069	685,621	685,621	
	2017 - System Design, Development and Qualification	0	37,544,962	37,544,962	50,152,196	87,697,158	98,941	84,178,217	84,277,158	98,941	84,277,158	98,941	3,420,000	
	Total System Design, Development and Qualification	50,492,480	37,544,962	88,037,442	50,152,196	138,189,638	8,126,500	87,478,630	95,605,130	8,126,499	87,478,630	8,126,499	42,584,508	
Production	2014 - Production	5,234,201	0	5,234,201	0	5,234,201	0	10,000	10,000	0	10,000	10,000	5,234,201	
	2015 - Production	28,809,939	0	28,809,939	0	28,809,939	0	513,000	773,488	260,488	513,000	260,488	28,799,939	
	2016 - Production	17,687,639	0	17,687,639	0	17,687,639	0	935,736	1,056,129	120,393	935,736	120,393	16,914,151	
	2017 - Production	0	20,420,605	20,420,605	(10,412,388)	10,008,217	120,393	1,448,736	1,839,617	390,881	1,448,736	390,881	8,952,088	
	Total Production	51,731,779	20,420,605	72,152,384	(10,412,388)	61,739,996	390,881	1,448,736	1,839,617	390,881	1,448,736	390,881	59,900,379	
Management Reserve	2015 - Management Reserve	1,249,177	0	1,249,177	0	1,249,177	0	1,185,589	1,185,589	(0)	1,185,589	(0)	63,588	
	2017 - Management Reserve	50,591,565	(49,488,462)	1,103,103	(152,160)	950,943	950,943	0	950,943	950,943	0	950,943	0	
	Total Management Reserve	51,840,742	(49,488,462)	2,352,280	(152,160)	2,200,120	950,943	1,185,589	2,136,532	950,943	1,185,589	950,943	63,588	
	CAFX	2015 - CAFX	80,692	0	80,692	0	80,692	0	53,034	80,692	53,034	27,658	53,038	0
		2016 - CAFX	1,215,816	0	1,215,816	0	1,215,816	0	814,949	1,215,816	814,938	400,867	814,938	0
2017 - CAFX		249,910	0	249,910	0	249,910	0	3,500	147,500	3,500	144,000	3,500	102,410	
Total CAFX		1,546,418	0	1,546,418	0	1,546,418	0	871,483	1,444,008	871,483	572,525	871,376	102,410	
IIS	2017 - IIS	67,860,000	(23,657,785)	44,202,215	(39,587,648)	4,614,567	0	0	0	0	0	0	4,614,567	
	Total IIS	67,860,000	(23,657,785)	44,202,215	(39,587,648)	4,614,567	0	0	0	0	0	0	4,614,567	
	TOTAL BUDGET EXECUTION	223,471,419	(15,180,680)	208,290,739	(0)	208,290,739	10,339,807	90,685,480	101,025,287	10,339,699	90,685,480	10,339,699	107,265,451	

Notes to the Financial Statements for the year ending 31 December 2017

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

ANNEX A Basis of Preparation and Accounting Policies

A01 Basis of preparation

The financial statements of the NAGSMO, including NAGSMA being the executive body of the NATO Alliance Ground Surveillance Management Organisation (NAGSMO), have been prepared on the accrual basis of accounting in accordance with the International Public Sector Accounting Standards (IPSAS) and based on International Financial Reporting Standards (IFRS/IAS), as adopted by the North Atlantic Council (NAC) in 2002. In 2013 and in 2016, the NAC approved an adaptation to IPSAS to better suit the specific requirements of the Alliance and an associated NATO Accounting Framework.

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

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

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

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

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

A02 Use of estimates

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

A03 Significant Accounting Policies

Accounting as a Procurement Agent

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

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

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

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

NAGSMA provides contract administration function to NAGSMO. NAGSMA acts as an agent in accordance with a mandate set by the NAGSMO Participating Nations in the PMOU, which defines the role of the Agency in the procurement of a NATO owned and operated core AGS capability. NAGSMO is as well considered an Agent in respect of its operations, as a subsidiary body of NATO, with the sole objective to procure the AGS Core which will be owned, controlled and operated by the 29 Nations of NATO. NAGSMO and its executive body NAGSMA do not have and will not have control in the future of the assets procured as per the criteria in the NATO Accounting Framework. Transactions are treated accordingly in the NAGSMO Financial Statements.

Foreign Currency Translation

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

Financial Instruments

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

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

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

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

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

Credit Risk: There is a very limited credit risk as the contributing Nations generally have a high credit rating. NAGSMA uses two banks to deposit its cash holdings. Credit ratings of those banks are as following:

DNB Bank ASA: A+ (S&P)

Banque et Caisse d'Épargne de l'État: AA+ (S&P)

Cash and Cash Equivalents

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

Receivables

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

Other Current Assets and Prepayments

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

Payables

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

Advances and Unearned Revenue

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

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

Provisions and Contingent Liabilities

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

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

Budget Execution Statement

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

Revenue and Expense Recognition

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

Revenue for the Administrative Budget

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

Interest

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

Representation Allowance

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

*Post-employment benefits**Defined Contribution Plans*

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

Defined Benefit Plans

NAGSMA employees who have joined NATO before 1 July 2005 are members of the NATO Coordinated Pension Scheme which is a funded defined benefit plan. Under the plans and upon completion of 10 years employment with NATO, the employees are entitled to retirement benefits of 2% per year of service of final basic salary on attainment of a retirement age of 65. No other post-retirement benefits are provided to these employees. Staff members whose length of service is not sufficient to entitle them to a retirement pension are eligible for a leaving allowance. The assets and liability for NATO's Defined Benefit Plan are accounted for centrally at NATO Headquarters and therefore are not recognised in these financial statements.

ANNEX B Notes to the Statement of Financial Position

Notes Reference	Current Year	Prior Year
	31-Dec-17	31-Dec-16
The Statement of Financial Position details the assets and liabilities of NAGSMA as of 31 December.		
B01 Cash and cash equivalents	326,482,728	358,284,643
Cash and Cash equivalents are short-term liquid assets. NAGSMA operates highly reliable and interest bearing bank accounts: an administrative and an operational account that have EUR and USD currency sub-accounts.		
B02 Short-term investments	0	0
Short-term investments are bank deposits maturing in less than 3 months.		
B03 Receivables	10,970,437	36,378,945
Accounts receivable are kept in separate sub-ledgers that provide detailed insight into the outstanding calls for contribution and provide accurate and up-to-date cash forecast information. The receivables as of 31 December 2017 are primarily outstanding calls for contributions towards the Administrative Budget 2018 and the Operational Budget 2018 which are not yet past their due date.		
B04 Other current assets and prepayments	144,398	138,665
Other current assets match provisions for annual leave entitlements accrued but untaken at year-end.		
B05 Payables	1,395,944	3,670,674
These short-term payables are open liabilities for goods and services received in 2017 such as consulting contracts, communication, travel and personnel related invoices. The decrease is primarily due to 2017 accrued invoices related to the procurement effort.		

B06	Advances and deferred revenue	174,051,593	246,067,627
	Advances from NATO entities	1,785,268	2,054,809
	Advances from Nations	77,330,631	54,264,446
	Deferred revenue	94,935,693	189,748,372

Advances from NATO entities relate to NSIP contribution provided through NSPA for ALIS implementation, which is co-funded by NAGSMA.

Advances from Nations are funds called and/or received from Nations in respect of 2018 Administrative and Operational Budgets and unrealised exchange rate gains and losses. Advances include future budget funding.

Deferred revenue comprises unspent funding from prior periods.

B07	Short-term provisions	139,211	138,665
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The provision includes annual leave entitlements accrued matched with Other current assets and prepayments.

Balance at 1 January 2017	138,665
Provision increase	546
Balance at 31 December 2017	139,211

B08	Other current liabilities	162,010,815	144,925,287
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Other payables mainly include lapsed credits 2017 and the 2017 financial result that will have to be refunded upon national decision. The increase is primarily caused by lapses of the 2017 Operational Budget funds.

B09	Contingent Liabilities
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In the year 2017, NAGSMA received two separate assertions from NGISSII: (a) Claim related to Airworthiness Certification; and (b) Changes Notification concerning Verification activities. Although it is intended to resolve these aforementioned issues within a contract amendment, there is a small possibility that, if the contract amendment not agreed to and these issues unresolved, it could create the liability. The costs in case of materialization of the contingent liability will be borne by NAGSMO Nations.

ANNEX C Notes to the Statement of Financial Performance

Notes Reference	Current Year	Prior Year	
	2017	2016	
The Statement of Financial Performance details the revenue and expenses that NAGSMA incurred during the year ending 31 December.			
C01	Revenue from non-exchange transactions	9,275,725	9,738,884
Revenue represents funding from Nations for expenses incurred during the financial year.			
C02	Personnel	6,743,211	7,468,607
Personnel costs are for staff members hired under the NATO Civilian Personnel Regulations as well as for consultants and contractors.			
The figures represent the costs of personnel including basic salary, allowances, insurance and pension plan contributions.			
NAGSMA had 40 staff members at the year-end 2017 (2016: 53 staff members).			
The breakdown of wages, salaries and employee benefits is as follows:			
	Year ended 31/12/17	Year ended 31/12/16	
	EUR	EUR	
Employee benefits expense, consultants and contractors	6,231,547	6,881,361	
Post-employment benefits			
for defined contribution pension scheme	511,118	564,767	
for defined benefit pension scheme	0	0	
Termination benefits	0	0	
Provision for annual leave entitlements accrued	546	22,479	
Total employee benefits expense	6,743,211	7,468,607	
C03	Contractual supplies and services	2,532,514	2,270,277
Supplies and consumables are costs of goods and services used by NAGSMA associated with the general management and administrative activities under the SSA and SLA, such as information management, finance, human resources, building and facilities, security, travel expenses, etc. These costs are linked to the approved NAGSMA Staffing Plan. It also includes hospitality funds, communications services (i.e. telephones), and NATO Headquarters support (MOA).			

ANNEX D Notes to the Cash Flow Statement

The Cash Flow Statement is prepared using the indirect method.

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

ANNEX E Notes to the Budget Execution Statement – Administrative Budget

NAGSMO - Budget Execution Statement - Administrative Budget for the year ended 31 December 2017 (All amounts in Euro)

Notes Reference	Initial Authorisation	Mid Year Review (MYR)	Final Approval - MYR	Transfers	Final Authorisation	Net Commitment	Actual Expenses	Total Spend	Carry Forward	Lapsed	
The Administrative Budget is prepared and presented using the accrual basis.											
The classification basis adopted for the Administrative Budget is to show expenditure in three chapters for Personnel costs, Contractual supplies and services costs as well as Capital and investment expenditure.											
The actual expenses presented in the budget execution statement include accruals (expenses for goods and services delivered before the year-end but not yet invoiced) and therefore reconcile to the expenses in the statement of financial performance after deducting the provision for annual leave entitlement of 546 EUR. The net commitments are those commitments for which a contractual obligation has been created before the year-end without the goods and services delivered before the year-end.											
E01	2016 - Personnel	0	0	0	0	0	(730)	(730)	0	730	
E02	2017 - Personnel	9,049,365	-1,381,792	7,667,573	0	7,667,573	0	6,743,395	6,743,395	0	924,178
Lapses are due to savings that were generated in basic salary, consultancy, and education allowance.											
Savings in basic salary resulted from early departures staff and lower actual personnel strength than what was approved in the NAGSMA Staffing Plan 2017.											
E03	2016 - Contractual supplies and services	0	0	0	0	0	(4,815)	(4,815)	0	4,815	
E04	2017 - Contractual supplies and services	3,612,091	-484,481	3,127,610	0	3,127,610	0	2,537,127	2,537,127	0	590,483
Lapses are primarily due to a delayed move to the New NATO HQ.											
E05	2017 - Capital and investment budgeting	5,000	0	5,000	0	5,000	0	201	201	0	4,799
E06	2017 - Budget contingencies	200,000	-50,000	150,000	0	150,000	0	0	0	0	150,000
Lapses are due to unused contingencies.											

ANNEX F Notes to the Budget Execution Statement – Operational Budget

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

The classification basis adopted for the Operational Budget is to show expenditure for AGS Core System Procurement.

The exchange rate used to translate the USD portion of expenditure to the presentation currency EUR in the Operational Budget Total table is the average exchange rate in 2017 of 1.1297.

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

System Design, Development and Qualification

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

Production

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

Management Reserve

The Management Reserve was used to expense NAGSMO BoD approved Pre-PMOU Contributions (PPC); Milestones 249, 250, and 251 of Contract Change Order (CCO) 0023; Non-Financial Contributions (NFC); the NAGSMA part of the ALIS co-funding of the Work Package 1 and Work Package 3 and NAGSMA Contract No NAGSMA-CON-0020 for the Collaborative Environment (a temporary solution for the ALIS interface system). A Rebaseline

Framework agreement was established with CCO-0023 and briefed to the NAGSMO BoD in October 2017.

CAFX

Funds to provide items for the Prime Contractor in accordance with Contracting Authority Furnished Property. Commitments and expenditures for the NCI Agency were for the AGS Implementation Support and NATO CIS support to the AGS programme. The services included inspections and certifications of the Main Operating Base facilities and accreditation activities. CAFX funds were also used to procure equipment, support, and training, agreed in the Prime Contract through the Foreign Military Sales (FMS), TEMPEST testing of the UAV by the U.S. Navy's Certified TEMPEST Authority, and transportation of CAFX equipment already purchased through various FMS cases.

ATR/ATID

Danish funds committed and expensed for contractual milestones for the acquisition of the NATO AGS Automatic Target Recognition/ Automatic Target Identification Capability Development & Integration Phase I.

NCB

Expenditures comprise one contractual milestone was expensed for the acquisition of the NATO AGS Test System Environment Capability Phase I.

There are no commitments carried forward from 2012 and 2013. In December 2017, the NAGSMO Finance Committee provided an exceptional extension of the carry forward of 2014 and 2015 commitments for the Prime Contract milestones to be expensed in 2018. The exceptional carry forward of funds was requested for commitments associated to a number of AGS Core Contract milestones and CAFX (for Foreign Military Sales) due to a delay in program execution.

Carry forwards from 2016 are primarily milestones related to Contract Amendment 22, COMSEC & Repair, Link16 Terminals, support and training, TGGs & MOS Parts and the Collaborative Environment Part I.

Carry Forwards from 2017 relate mainly to the US and Italian Non-Financial Contributions, the TGGs/MOS SLPV Spares, MOS SLPV Spares, PMR 18, 2017 Collaborative Environment and Common costs software and travel.

The Table below represents the cumulative NAGSMA Operational budget per year from 2012 to 2017 expended, carried forward and lapsed in two currencies EUR and USD.

In 2017, part of the Operational Budget was lapsed due to the rebaseline of the main contract with NGISSII and the finalization of the Initial-In-Service-Support contract. In 2017 milestones have been delayed and are being re-planned as part of a program restructure that creates a new baseline to complete the remainder of the program. The rebaseline impacts all areas across SDDQ, Production, IISS and MR.

The Budgets are presented below by currency showing the actual expenditures, carry forwards and lapses as of the 31.12.2017.

NAGSMA Operational Budget EUR

	Budget	Actual Expenses	Carry Forward	Lapsed
2012	107,086,412	107,086,412	0	0
2013	137,794,865	137,794,865	0	0
2014	122,977,865	117,257,630	0	5,720,236
2015	109,014,294	90,671,063	1,000,000	17,343,231
2016	63,924,048	12,541,620	2,220,526	49,161,902
2017	34,822,414	7,244,880	2,372,893	25,204,641
Total	575,619,898	472,596,470	5,593,419	97,430,009

NAGSMA Operational Budget USD

	Budget	Actual Expenses	Carry Forward	Lapsed
2012	204,865,340	204,865,340	0	0
2013	238,445,262	238,445,262	0	0
2014	373,468,465	364,507,386	1,182,006	7,779,073
2015	169,456,878	104,592,357	63,038	64,801,483
2016	193,990,813	50,675,533	7,920,878	135,394,402
2017	103,520,795	85,257,953	1,173,777	17,089,065
Total	1,283,747,553	1,048,343,830	10,339,699	225,064,024

Note to the table:

The Carry Forwards from the Financial Statements 2014-2016 which have been expended in 2017 have been added to the Actual Expenses of 2014, 2015 and 2016 respectively.

ANNEX G General Notes to the Financial Statements

G01 Related Party Disclosures

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

Transactions with NATO bodies

	Current Year 2017	Prior Year 2016
	EUR	EUR
NATO Communications and Information Agency	1,619,061	1,279,698
NATO Support Agency	8,093	144,608
NATO International Staff	176,148	154,750
SHAPE	1,300	500
NATO School	1,800	900
	1,806,402	1,580,456

In 2017, the NCI Agency provided administrative services for NAGSMA under the Support Services and Service Level Agreements. NCI Agency also provided NAGSMA with an internal audit and ILS.

NSPA provided logistics support services.

NATO IS provided operating, administrative, medical and telephone services for NAGSMA.

SHAPE and NATO School provided NAGSMA with training support.

Compensation of key management personnel

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

	Current Year 2017	Prior Year 2016
	EUR	EUR
Basic salaries	635,040	723,839
Allowances	145,042	166,478
Post-employment benefits	59,182	72,441
Employer's contribution to Insurance	77,085	87,469
	916,349	1,050,227

The decrease in compensation of key management personnel is primarily due to their turnover.

	Current Year 2017	Prior Year 2016
Number of individuals at year-end on a full time equivalent basis		
General Manager	1	1
Programme Manager	1	0
Key management personnel	3	4
	5	5

G02 Representation Allowance

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

As from 1 June 2013, a new procedure is in place in respect of Representation Allowance; as all recipients are now reimbursed permitted expenses within the limits of their individual Representation Allowance allocation. All representation allowance disbursements for the 2017 reporting period were administered by the Agency.

Expenditures	EUR
Rental Supplement	2,673
Functions	833
Total	3,506
Entitlements	EUR
Representation Allowance annual entitlement	10,692
<i>of which: Rental Supplement annual entitlement</i>	2,673
Transactions	EUR
Rental Supplement January-December	2,673
Dinners and Luncheons	833
Total	3,506

G03 Approval of Financial Statements

The financial statements were approved by the Financial Controller and authorised to be issued on 12 June 2018.

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NATO Alliance Ground Surveillance
Management Organisation
(NAGSMO)

NAGSMO
NATO Headquarters
1110 Brussels
Belgium