	NATO	NORTH ATLANTIC COUNCIL
	OTAN	CONSEIL DE L'ATLANTIQUE NORD

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03 December 2018

DOCUMENT
C-M(2018)0058-AS1

IBAN AUDIT ON THE 2017 FINANCIAL STATEMENTS OF NATO MULTI-ROLE COMBAT AIRCRAFT DEVELOPMENT, PRODUCTION AND IN SERVICE SUPPORT MANAGEMENT ORGANISATION (NAMMO) AND NATO EF2000 AND TORNADO DEVELOPMENT, PRODUCTION AND LOGISTICS MANAGEMENT AGENCY (NETMA)

ACTION SHEET

On 30 November 2018, under the silence procedure, the Council noted the IBAN report on the 2017 financial statements of NAMMO and NETMA, endorsed the related RPPB report attached to C-M(2018)0058, and agreed to the public disclosure of this report, the IBAN audits and associated 2017 financial statements of NAMMO and NETMA.

(Signed) Jens Stoltenberg
Secretary General

NOTE: This Action Sheet is part of, and shall be attached to C-M(2018)0058.

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19 November 2018

DOCUMENT

C-M(2018)0058

Silence Procedure ends:

30 Nov 2018 15:30

IBAN AUDIT ON THE 2017 FINANCIAL STATEMENTS OF NATO MULTI-ROLE COMBAT AIRCRAFT DEVELOPMENT, PRODUCTION AND IN SERVICE SUPPORT MANAGEMENT ORGANISATION (NAMMO) AND NATO EF2000 AND TORNADO DEVELOPMENT, PRODUCTION AND LOGISTICS MANAGEMENT AGENCY (NETMA)

Note by the Secretary General

1. I attach the International Board of Auditors for NATO (IBAN) reports on the audits of the 2017 financial statements of NAMMO and NETMA. The IBAN audits produced unqualified opinions on both the financial statements and compliance for NAMMO and NETMA.
2. The IBAN reports have 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 15:30 hours on Friday, 30 November 2018**, I shall assume the Council noted the IBAN report on the 2017 financial statements of NAMMO and NETMA, endorsed the related RPPB report, and agreed to the public disclosure of this report, the IBAN audits and associated 2017 financial statements of NAMMO and NETMA.

(Signed) Jens Stoltenberg

1 Annex
1 Enclosure

Original: English

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IBAN AUDIT ON THE 2017 FINANCIAL STATEMENTS OF NATO MULTI-ROLE COMBAT AIRCRAFT DEVELOPMENT, PRODUCTION AND IN SERVICE SUPPORT MANAGEMENT ORGANISATION (NAMMO) AND NATO EF2000 AND TORNADO DEVELOPMENT, PRODUCTION AND LOGISTICS MANAGEMENT AGENCY (NETMA)

Report by the Resource Policy and Planning Board (RPPB)

References:

- | | |
|-------------------------|--|
| A. IBA-A(2018)0046 | IBAN Audit on the 2017 Financial Statements of NAMMO |
| B. IBA-A(2018)0095-REV1 | IBAN Audit on the 2017 Financial Statements of NETMA |
| C. AC/335-N(2018)0036 | Handling of the 2017 Financial Statement audit reports |
| D. PO(2015)0052 | Wales Summit tasker on transparency and accountability |

BACKGROUND

1. This report by the RPPB addresses the IBAN audits of the 2017 financial statements and compliance of NAMMO and NETMA. The IBAN audits set out unqualified opinions on the financial statements and on compliance for both NATO entities (references A and B).
2. In accordance with the handling arrangements agreed by the RPPB (reference C) these audit reports have been grouped together into a single overarching RPPB report.

DISCUSSION

3. The RPPB notes the IBAN did not identify any current year observations during NAMMO's 2017 audit and no previous years' observations exist.
4. The IBAN made two observations during NETMA's 2017 audit and found that the one prior year observation was settled. The two observations identified were that the roles and responsibilities of the Head of Internal Audit do not ensure the appropriate segregation of duties and that internal controls over financial reporting need to be improved.
5. The RPPB notes the IBAN's recommendation to ensure that the Head of Internal Audit at NETMA is not involved and responsible for business operations to ensure compliance with the segregation of duties principle. The RPPB further understands that the segregation of duties issue is minimised, if not eliminated, by the mitigating controls NETMA's management has put in place. This topic was further discussed at the NETMA Audit Advisory Panel on 23 October 2018, where the four member Nations (Germany, Italy, Spain and the United Kingdom) agreed to take action to remediate the observation.

CONCLUSION

6. The IBAN issued unqualified audit opinions on the 2017 financial statements and on compliance of NAMMO and NETMA. The RPPB notes that NETMA's Audit Advisory Panel reviewed the segregation of duties issue identified by the IBAN and agreed to take action to remediate the observation.

RECOMMENDATIONS

7. The RPPB recommends that the Council:
 - 7.1. note the IBAN reports at references A and B;
 - 7.2. endorse the conclusion at paragraph 6; and
 - 7.3. agree to the public disclosure of this report, the IBAN audits and the associated 2017 financial statements of NAMMO and NETMA in line with the agreed policy in reference D.



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)0096
29 August 2018

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

Cc: General Manager, NETMA
Division Leader, Finance Division, NETMA
Chairman, Resource Policy & Planning Board (RPPB)
Branch 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 NATO Multi-Role Combat Aircraft Development Production and In-Service Support Management Organisation (NAMMO) Financial Statements for the year ended 31 December 2017 – IBA-AR(2017)0018***

The Board herewith submits its approved Auditor's Report and a Letter of Observations and Recommendations with a Summary Note for distribution to the NATO Council.

Yours sincerely,

Hervé-Adrien Metzger
Chairman

Attachments: 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 Multi-Role Combat Aircraft Development Production
and In-Service Support Management Organisation (NAMMO)
for the year ended 31 December 2017**

NAMMO is a NATO Production and Logistic Organisations. The participating nations for NAMMO are Germany, Italy and the United Kingdom. The NATO EF 2000 and Tornado Development, Production and Logistics Management Agency (NETMA) manages this programme and the related budget.

The Board audited the NAMMO Financial Statements for the year ended 31 December 2017. Expenditure from the operational budget amounted to EUR 397 million.

The Board issued an unqualified opinion on the NAMMO Financial Statements and on compliance for the year ended 31 December 2017. There are no current year observations and no observation from previous years' audit to follow up on.

The Auditor's Report (Annex 2) and the Letter of Observations and Recommendations (Annex 3) were issued to the NETMA who had no factual or formal comments.

29 August 2018

INTERNATIONAL BOARD OF AUDITORS FOR NATO

AUDITOR'S REPORT ON THE FINANCIAL STATEMENTS OF

**THE NATO MULTI-ROLE COMBAT AIRCRAFT DEVELOPMENT PRODUCTION
AND IN-SERVICE SUPPORT MANAGEMENT ORGANISATION**

(NAMMO)

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 (Board) audited the accompanying Financial Statements of NAMMO, which comprised the Statement of Financial Position as at 31 December 2017, and the Statement of Financial Performance, the Cash Flow Statement and the Statement of Changes in Net Assets/Equity for the year then ended, and the notes to the financial statements, including a summary of significant accounting policies. The Board also audited the Statement of Budget Execution 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 opinion.

Opinion on Financial Statements

In our opinion, the financial statements present fairly, in all material respects, the financial position of NAMMO 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 authorised 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 authorised expenditure and whether their operations have been carried out in compliance with the financial and personnel regulations in force. Such procedures include the assessment of the risks of material non-compliance.

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

Opinion on Compliance

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

Brussels, 29 August 2018



Hervé-Adrien Metzger
Chairman

29 August 2018

INTERNATIONAL BOARD OF AUDITORS FOR NATO

LETTER OF OBSERVATIONS AND RECOMMENDATIONS

**FOR THE NATO MULTI-ROLE COMBAT AIRCRAFT DEVELOPMENT PRODUCTION
AND IN-SERVICE SUPPORT MANAGEMENT ORGANISATION**

(NAMMO)

FOR THE YEAR ENDED 31 DECEMBER 2017

Introduction

The International Board of Auditors for NATO (Board) audited the NAMMO Financial Statements for the year ended 31 December 2017, and issued an unqualified opinion on the financial statements and on compliance.

Observations and Recommendations

During the audit, the Board made no observations and there were no observations from previous years' audits to follow up on.

The Board also issued a Management Letter (reference IBA-AML(2018)0013) to the NETMA General Manager with observations for management's attention.

NAMMO ANNUAL FINANCIAL STATEMENTS

PERIOD ENDED 31 DECEMBER 2017



NETMA

**NATO EF2000 AND TORNADO DEVELOPMENT, PRODUCTION
AND LOGISTICS MANAGEMENT AGENCY**

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Introduction to the 2017 Financial Statements



NATO Multi-Role Combat Aircraft Development, Production and In Service Support Management Organisation (NAMMO) is a subsidiary body created within the framework of NATO. NAMMO is based at Hallbergmoos, Germany and is a NATO Production and Logistics Organisation (NPLO) formed by the nations of Germany, Italy and United Kingdom to develop, produce and support the Tornado aircraft.

A NAMMO Board of Directors (BoD), comprising of representatives from the three NAMMO nations, provides strategic direction and governance to the Tornado Programme and NETMA provides support in the delivery of this direction. In this activity, NAMMO is acting as a principal and these accounts

are put together on this basis.

Funding for NAMMO is wholly through contributions made by the three NATO member nations. As a NATO organisation two NAMMO nations are exempt from taxation relating to operating revenue and expenses. However in the case of the Federal Republic of Germany VAT is levied.

The Tornado has been deployed extensively throughout 2017 including involvement in coalition operations against Daesh in Iraq and Syria and involvement in a number of national and joint exercises.

Key points from the Annual Financial Statements

In 2016 the UK formally announced its intent to withdraw its Tornado fleet from service in March 2019.

NETMA has very positive expectations that the ongoing transformation programme to accommodate the Out of Service Date of the UK fleet in March 2019 will deliver a sustainable way forward which will benefit all Nations.

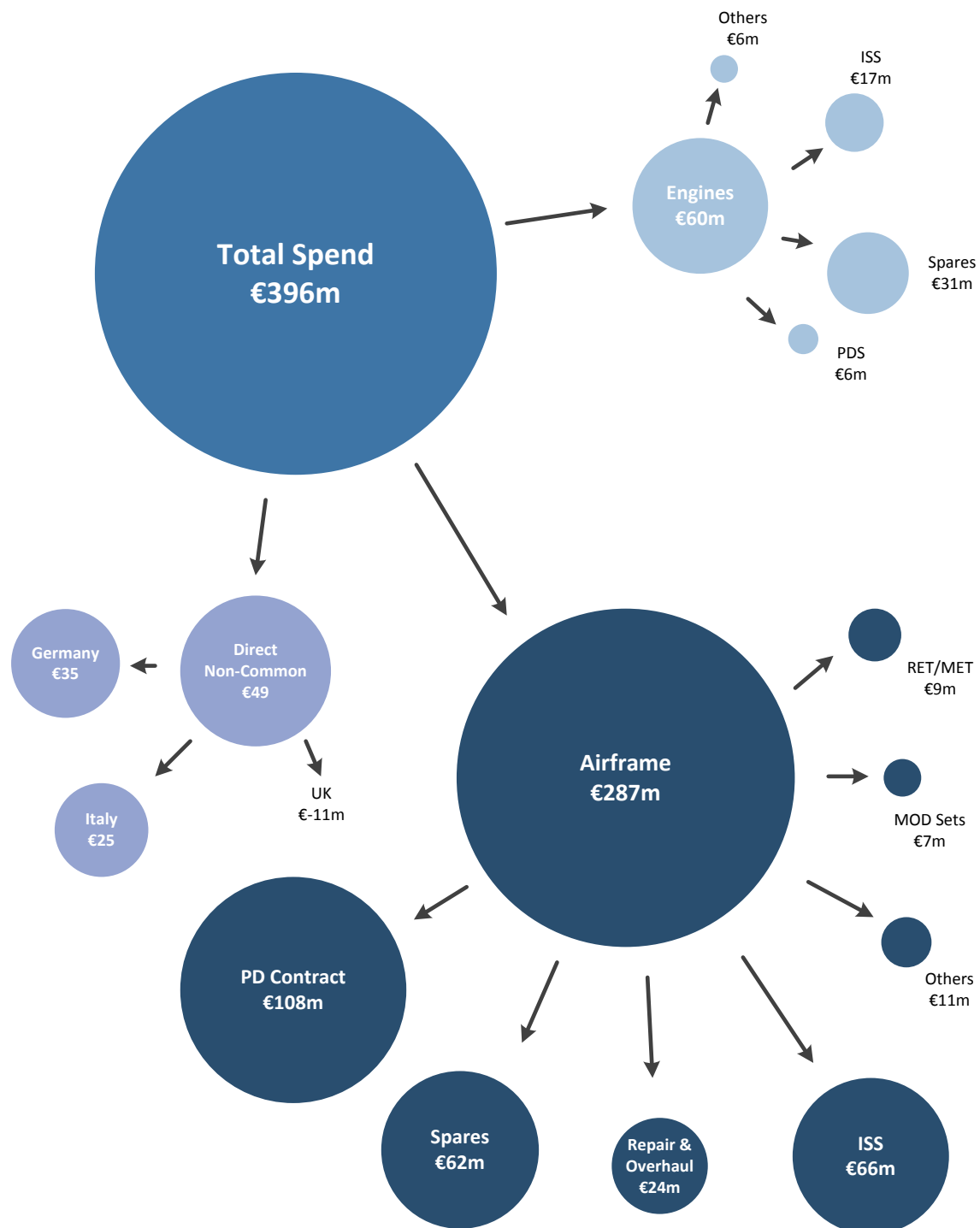
Key to this has been the recent agreements on programme principles including budgets and structure that clearly indicate that the three Nations intend to remain together in partnership following the retirement of the UK fleet.

NETMA is now working hard to ensure that by the forthcoming ad-hoc Joint Steering Committee meeting at the Berlin Air Show, all necessary actions have been completed to enable the final formal agreements to be reached between the nations.

The UK decision to withdraw its fleet from service does not affect NAMMO's status as a going concern for accounting purposes. Both Italy and Germany will maintain fleets in active service, managed through NAMMO and it is expected that NAMMO will continue as an active management agency for the foreseeable future.

NAMMO Expenditure Breakdown 2017

The total spend on the Tornado programme through NETMA in 2017 was €396m, a €15m decrease from 2016. The spend on Tornado is dominated by the airframe with 15% of the annual spend relating to the engine. Additionally, there are significant areas of direct non-common contracting for national support.



Statement of Internal Control



As General Manager of NETMA, I have responsibility for maintaining a effective system of internal control that supports the achievement of my Agency's policies, aims and objectives, set by NETMA's Four Nations and BoD, whilst safeguarding the funds and assets for which I am personally responsible, in accordance with the responsibilities assigned to me.

The system of internal control is designed to manage the risk of failure to achieve the organisation's policies, aims and objectives but it can only provide reasonable and not absolute assurance of effectiveness. The system of internal control is based on an ongoing evidence based process designed to identify the principal risks to the achievement of my Agency's policies, aims and objectives, to evaluate the nature and extent of those risks and to manage them efficiently and effectively on a continual year round basis. The board has established appropriate structures, reporting lines and responsibilities to support the delivery of objectives.

As General Manager, I have responsibility for reviewing the effectiveness of the system of internal control. The processes in place to achieve this are summarised below:

- NETMA has a Management Plan which identifies NETMA's objectives. The Management Plan focuses on business change objectives and Program risks. Key Business risks have now been identified, mitigated and owners have been appointed to monitor and report on these on a regular basis.
- Management checks are undertaken and the internal audit function performs a range of audit activities, based on an annual audit plan agreed by the Audit Advisory Panel alongside the detailed audit of property held in industry, to ensure appropriate internal controls are in place and adhered to. The Internal Audit has been updated to ensure compliance with the International Standards for the Professional Practice of Internal Auditing in accordance with previous IBAN recommendations.

During 2016 the agency, under recommendation from the IBAN and as agreed by the Audit Advisory Panel, introduced the integrated framework for internal control developed by the Committee of Sponsoring Organisations of the Treadway commission (COSO Framework) as a mechanism for formally documenting the internal control system and providing assurance that it is functioning effectively. The annual COSO review was undertaken as scheduled in 2017.

My review of the effectiveness of the system of internal control is informed by the work of the executive managers within the organisation who have responsibility for the development and maintenance of the internal control framework, comments made by the external auditors in their management letters and other reports together with the results of the annual COSO review.

I am content that the processes in place within the organisation provide reasonable assurance of the effectiveness and efficiency of the organisations operations, the reliability of its financial information and its integrity with regards to application and compliance to applicable rules and regulations. Whilst we always seek to improve our processes each year there are no material internal control weaknesses currently identified that need specific intervention from Senior Management in 2017.

MR GABRIELE SALVESTRONI
General Manager

MR MARK GANFIELD
Financial Controller

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STATEMENT OF FINANCIAL POSITION

AS AT 31 DECEMBER 2017

(in thousands of Euros)

	Notes	2017	2016
Assets			
Current assets			
Cash and cash equivalents	B1	159,005	193,442
Short term investments		0	0
Receivables		2,058	31
Prepayments		0	0
Inventories		0	0
		<u>161,063</u>	<u>193,473</u>
Non-current assets			
Property, plant & equipment		0	0
Intangible assets		0	0
		<u>0</u>	<u>0</u>
Total assets		<u>161,063</u>	<u>193,473</u>
Liabilities			
Current liabilities			
Payables	B2	33,239	27,771
Deferred revenue		0	0
Advances	B3	127,824	165,702
		<u>161,063</u>	<u>193,473</u>
Non-current liabilities			
Provisions		0	0
		<u>0</u>	<u>0</u>
Total liabilities		<u>161,063</u>	<u>193,473</u>
Surplus/deficit		0	0
Reserves		0	0
Total net assets		<u>0</u>	<u>0</u>

The financial statements on pages 7 to 11 and their associated notes were issued to the International Board of Auditors for NATO on 28th March 2018.



MR GABRIELE SALVESTRONI
General Manager



MR MARK GANFIELD
Financial Controller

STATEMENT OF FINANCIAL PERFORMANCE

FOR THE YEAR ENDED 31 DECEMBER 2017

(in thousands of Euros)

	Notes	2017	2016
Revenue			
Revenue	C1	397,136	399,786
Financial revenue		0	0
Other revenue		0	0
Total revenue		397,136	399,786
Expenses			
Personnel		0	0
Contractual supplies and services	C2	(396,436)	(400,653)
Depreciation and amortisation		0	0
Impairment		0	0
Provisions		0	0
Other expenses		0	0
Finance costs	C3	(700)	867
Total expenses		(397,136)	(399,786)
Surplus/(deficit) for the period		0	0

STATEMENT OF CASH FLOW

FOR THE YEAR ENDED 31 DECEMBER 2017

(in thousands of Euros)

	Notes	2017	2016
Cash flow from operating activities			
Surplus/(deficit)	D1	0	0
Non-cash movements			
Depreciation/ amortisation		0	0
Impairment		0	0
Increase /(decrease) in payables	D2	5,468	(4,447)
Increase/ (decrease) in advances	D3	(37,878)	(78,727)
Increase/ (decrease) in other current liabilities		0	0
Increase/ (decrease) in provisions		0	0
(Gains)/losses on sale of property, plant and equipment		0	0
Decrease/ (increase) in receivables	D4	(2,027)	(31)
Net cash flow from operating activities		(34,437)	(83,205)
Cash flow from investing activities			
Purchase of property plant and equipment / Intangible assets		0	0
Proceeds from sale of property plant and equipment		0	0
Net cash flow from investing activities		0	0
Cash flow from financing activities		0	0
Net cash flow from financing activities		0	0
Net increase/(decrease) in cash and cash equivalents		(34,437)	(83,205)
Cash and cash equivalents at the beginning of the period		193,442	276,647
Cash and cash equivalents at the end of the period		159,005	193,442

STATEMENT OF CHANGE IN NET ASSETS/EQUITY

FOR THE YEAR ENDED 31 DECEMBER 2017

(in thousands of Euros)

	PP&E Asset Reserve	Revaluation Reserves	Accumulated surplus/deficit	Total
Balance at the beginning of the period 2016	0	0	0	0
Changes in accounting policy	0	0	0	0
Restated balance	0	0	0	0
Transfer from Accumulated Surplus / Deficit	0	0	0	0
Surplus/(deficit) for the period	0	0	0	0
Balance at the end of the period 2016	0	0	0	0
Changes in accounting policy	0	0	0	0
Restated balance	0	0	0	0
Transfer from Accumulated Surplus / Deficit	0	0	0	0
Surplus/(deficit) for the period	0	0	0	0
Balance for the period ended 2017	0	0	0	0

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STATEMENT OF BUDGET EXECUTION

FOR THE YEAR ENDED 31 DECEMBER 2017

(in thousands of Euros)

		Initial budget	Transfers	Bud Adj 1	Bud Adj 2	Bud Adj 2	Final budget	Commitments	Expenses	Carry forward	Lapsed
Budget 2017											
All nations	E1	431,449	0	19,200	0	0	450,649	395,743	395,743	0	54,906
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Total FY 2017		431,449	0	19,200	0	0	450,649	395,743	395,743	0	54,906
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A. Significant Accounting Policies

Basis of preparation

The financial statements of NAMMO have been prepared in accordance with the International Public Sector Accounting Standards (IPSAS) and based on International Financial Reporting Standards (IFRS/IAS), as adopted by the North Atlantic Council (NAC) in 2002. In 2013, the NAC adopted an adaptation to IPSAS to better suit the specific requirements of the Alliance and an associated NATO accounting framework, applicable for financial reporting periods beginning on 1 January 2013.

The financial statements comply with the accounting requirements of the NATO Financial Regulations (NFRs) and the relevant NAMMO directives and policies. In instances where there is a conflict between IPSAS and the NFRs this has been noted.

The financial statements have been prepared on a going-concern basis. NATO Agency reform, which was approved by the Heads of State and Government at the Lisbon Summit in 2010, continues to mature. A new integrated NATO Procurement entity will be established to meet the needs of new procurement programmes, but none of the existing NATO agencies intend to integrate into this new organisation. In addition, at this stage, there is no intent to merge additional NATO agency support activity into the NATO Support Agency (NSPA). It is considered that there are no impediments to continuing on a going concern basis for the foreseeable future.

The financial statements have been prepared on a historical cost basis except for financial instruments that are measured at fair value at the end of each reporting period. The principal accounting policies are set out below. They have been applied consistently to all periods presented. The accounting principles recognised as appropriate for the recognition, measurement and reporting of the financial position, performance and cash flows on an accrual based accounting system using historical costs have been applied consistently throughout the reporting period.

In accordance with Article 2.1 of the NFRs, the financial year of NAMMO is 1 January to 31 December.

Accounting estimates and judgments

In accordance with IPSAS and generally accepted accounting principles, the financial statements necessarily include amounts based on estimates and assumptions made by the management and based on historical experience as well as on the most reliable information available. In exercising the judgements to make the estimates, a degree of caution was included in light of the principle of 'prudence' required by IPSAS in order not to overstate assets or revenue or understate liabilities or expenses.

The estimates and underlying assumptions are reviewed on an ongoing basis. These estimates and assumptions affect the amounts of assets, liabilities, revenue and expenses reported. By their nature, these estimates are subject to measurement uncertainty. The effect of changes to such estimates and assumptions in future periods could be significant to the financial statements.

Changes in accounting policy and standards

The same accounting policies are applied within each period and from one period to the next, unless a change in accounting policy meets one of the criteria set in IPSAS 3. For the 2017 financial statements, the accounting policies have been applied consistently throughout the reporting period. There have been no changes to NAMMO accounting policy in 2017.

Restatements

NAMMO has not restated any balances in the 2016 financial statements.

Changes in financial rules and regulations

During 2015 NATO adopted new financial rules and regulations. During 2017 there were no additional changes. These financial statements have been produced in line with these financial rules and regulations.

Foreign currency

These financial statements are presented in Euros, which is the NAMMO functional and reporting currency. Foreign currency transactions are translated into Euros at the NATO exchange rates prevailing at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at year-end are translated into Euros using the NATO exchange rates applicable at 31 December 2017, resulting realised and unrealised gains and losses are recognised in the Statement of Financial Performance.

Consolidation

The NAMMO financial statements are not consolidated in-line with the NETMA Agency charter.

Financial Instruments disclosure/presentation

NAMMO uses only non-derivative financial instruments as part of its normal operations. These financial instruments include cash and cash equivalents, accounts receivable, liabilities, provisions and loans between NATO entities. Financial instruments are recognised in the statement of financial position at fair value.

*Financial risk factors***Credit risk**

There is very limited credit risk as the contributing nations generally have a high credit rating. The risk of financial loss due to a participating nations' failure to raise funds is still assessed as very low. In the event that there is a shortage of funds by one or more nations to meet financial obligations, other nations will be expected to provide the necessary funding.

Liquidity risk

The liquidity risk is based on the assessment of whether the organisation will encounter difficulties in meeting its obligations associated with financial liabilities. There is limited exposure to liquidity risk because of the budget mechanism that seeks to guarantee contributions for the total approved budget. The accuracy of forecasts that result in the calls for contributions as well as the delay in receiving payments represent the main liquidity risks.

Currency risk

To limit the exposure to foreign currency risk, NAMMO forecasts yearly expected expenditures in foreign currencies where it is material (i.e. Great British Pound - GBP). In order to have the required funding, NAMMO asks the nations to provide their contributions in either Euros or GBP. Therefore the currency risk is deemed to be minimal and hedging the foreign currency exposure is not considered necessary. The transactions in foreign currencies are denominated in the functional currency at the date of the transaction.

Interest rate risk

NAMMO is restricted from entering into borrowings and investments, and therefore there is no significant interest rate risk identified.

Assets

The entity holds the following types of current assets:

Cash and cash equivalents

Cash and cash equivalents include cash on hand and current bank accounts.

Receivables

Receivables are stated at net realisable value, after provision for doubtful and uncollectible debts. It can also include amounts due by other NATO entities.

Contributions receivable are recognised when a call for contribution has been issued to the member nations. No allowance for impairment loss is recorded with respect to member nations' assessed contributions receivable.

Inventories

NAMMO does not hold any inventory assets. Any inventories held in industry to be consumed in the production process are expensed and any inventory assets held in the ordinary course of operations to support Tornado are owned by the benefiting nations.

Property, Plant and Equipment

In accordance with IPSAS 17, Property, Plant and Equipment (PP&E) are recognised as tangible assets when it is probable that future economic benefits or service potential associated with the item will flow to the entity and the cost or fair value can be measured reliably. PP&E with the exception of land are stated at cost less accumulated depreciation and accumulated impairment losses. NAMMO's capitalisation threshold is €200,000, items with a purchase cost or fair value on acquisition above this threshold are capitalised and items falling below this threshold are fully expensed in the year of procurement.

For new asset additions during the year, the gross value of an asset is capitalised as PP&E on the Statement of Financial Position. The revenue for the full amount of the asset is accounted for in the year of purchase on the Statement of Financial Performance with a surplus on the Statement of Financial Performance being generated in the first year of purchase and transferred to the PP&E asset reserve account to increase accumulated asset reserves.

Depreciation is recognised so as to write off the cost of the assets less their residual values over their estimated useful lives, using the straight-line method. The estimated useful lives, residual values and depreciation method are reviewed at the end of each reporting period, with the effect of any changes in estimate accounted for on a prospective basis. Depreciation is accounted for as an expense which generates a deficit on the Statement of Financial Performance. This deficit is transferred to PP&E asset reserves at the end of each year to reduce the accumulated asset reserve.

An item of PP&E is derecognised upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising on the disposal or retirement of an item of PP&E is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognised in the Statement of Financial Performance.

Aircraft, government owned in-service equipment or nationally modified equipment are not included within NAMMO PP&E as these are national assets owned by the benefiting nation and are included within national financial statements and accounts accordingly.

The ownership of all Turbo Union assets has been handed over to industry and for PANAIA an assessment has been made on information available. The asset base of PANAIA and its sub-contractors is large and consists of rigs, jigs, tools and test equipment. At the request of nations, the NAMMO Cost Reduction and Asset Rationalisation Programme was set up to develop a disposal strategy for rigs and tooling to reduce costs and identify rigs and tooling that are required to meet nations requirements up to the out of service dates. The assets to be retained are those required to support the remaining aircraft configurations and reduced fleet size.

Due to the age of these special type of assets and the evidence available as to their value, either initially or currently, it was not possible to establish reliable values for them and as such, in line with IPSAS 17 and the NATO Accounting Framework, the organisation has not recognised any assets acquired prior to 1st January 2013 on the financial statements. There were no new asset additions or modifications acquired during 2017 that meet the capitalisation criteria.

The major rigs, jigs and test equipment that are retained to support the programme are identified as part of the rigs disposal strategy. The NAMMO tooling strategy and implementation plan is still being developed with industry to determine the range and scale of tooling that is required to be retained to meet repair and overhaul and aircraft support tooling requirements of each nation. Given the age and value of the majority of tooling assets, it is assumed that the asset pool has been fully depreciated over the production period and any remaining residual value is negligible, small quantities of in-use tooling continue to be replaced or refurbished as required. When the tooling strategy and implementation plans have been agreed with nations, a reassessment will be made and adjustment included in future financial statements if considered material.

Leases

The costs for operating the Agency's headquarters are accounted for in the NETMA administration budget and this includes leases and rental payments.

Intangible assets

There are no intangible assets to be capitalised for NAMMO under IPSAS 31 as they are not separately identifiable costs and are deemed to be an integral part of the production equipment construction costs. Development costs associated with the aircraft are delivered and accounted for as part of aircraft delivered and therefore owned by the nations.

Impairment of tangible and intangible assets

At the end of each accounting period, NAMMO reviews the carrying amounts of its tangible and intangible assets to determine whether there is any indication of impairment. If any such indication exists, the recoverable amount of the asset is estimated at the greater of the asset's fair value less costs to sell and value in use. Impairment losses, if any, are recognised in the statement of financial performance.

As there are no assets on the asset register for 2017 there has been no need to conduct an impairment review.

Liabilities

Payables

Payables (including amounts due to other NATO entities) are amounts due to third parties for goods and services received that remain unpaid as of the reporting date. They are recognised at their fair value. This includes estimates of accrued obligations for goods and services received at year-end but not yet invoiced.

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Deferred revenue

Deferred revenue represents contributions from member nations and/or third parties that have been called for current or prior years' budgets and that have not yet been recognised as revenue.

Advances

Advances are contributions from member nations called or received related to future years' budgets. Funds are called for in advance of their need because NAMMO has no capital that would allow it to pre-finance any of its activities. Unearned revenue includes miscellaneous income that nations have instructed remain on the programme accounts rather than be returned to the respective National Treasuries.

Employee benefits

The personnel costs for operating the Agency's headquarters are accounted for in the NETMA Administration Budget.

Provisions

Provisions are recognised when NAMMO has a legal or constructive obligation as a result of past events, where it is probable that an outflow of resources will be required to settle the obligation and where a reliable estimate of the amount of the obligation can be made.

Net assets

Net assets represent the residual interest in the assets of NAMMO after deducting its liabilities.

NATO entities perform their activities on a no-profit / no-loss basis globally over the reporting period. However, this does not prohibit the realisation of operating surplus or deficit in the financial reporting period.

*Revenue and expense recognition***Revenue**

Revenue comprises contributions from member nations to fund NAMMO budgets. It is recognised in the year when these contributions are used for their intended purpose as envisioned by NAMMO budgets and is usually called for in advance on a quarterly basis. Revenue is recognised to the extent that it is probable that the economic benefits will flow to NAMMO and the revenue can be measured reliably. Unused contributions and other revenue that relate to future periods are deferred accordingly.

Interest income is accrued on a time basis, by reference to the principal outstanding and at the effective interest rate applicable.

Bank interests earned and accrued as of 31 December 2017, exchange rate revenue due to transactions in foreign currency and realised exchange rate revenue in accordance with NAMMO Policy and IPSAS 4 – Effect of the foreign exchange rate are recognised as financial revenue.

Expenses

NAMMO operates comparable to a construction manager for the purposes of IPSAS and payments made to industry are expensed accordingly. All expenses incurred on the Tornado Weapons System Programme are for the in-service support of the aircraft.

Cash flow statement

The cash flow statement is prepared using the indirect method and the format follows the layout provided by IPSAS 2 (Cash Flow Statement).

B. Notes to Statement of Financial Position

(in thousands of Euros)

1. Cash and cash equivalents

	2017	2016
Cash accounts	0	0
Clearing cash accounts	0	0
Petty cash and advances	0	0
Current bank accounts	159,005	193,442
Cash equivalents	2,058	31
Clearing-bank accounts	0	0
Total	161,063	193,473

Current bank accounts

The Tornado Weapons System Program has a number of bank accounts relating to the various funding offices from which payments are made and contributions received. These include accounts for payments to be made in GBP, USD, SEK, USD and EUR.

The accounting system (PARMIS) functionality necessitates that each cash and bank account separately identified has an associated clearing account to enable the sub-ledger to interface with the general ledger. The carrying balance on all clearing accounts is zero.

The overall levels of cash holdings have decreased over the year as NETMA actively worked with nations to lower cash holdings following previous IBAN audit observations.

Cash equivalents

Receivables include credit invoices received on PARMIS payables which will be offset against payables in 2017 (€167K) and an additional credit due from industry (€1.890M).

2. Payables

	2017	2016
Payables to suppliers	27,584	22,926
Payables to non-consolidated entities	0	0
Payables to staff members	0	0
Payables to governments	0	0
Other payables	5,656	4,845
Total	33,239	27,771

Payables to suppliers

Payables to suppliers include invoices received from commercial vendors not settled but accrued per reporting date. This account is reconciled to the payables sub-ledger within the financial system operated by NAMMO on a monthly basis. Any outstanding currency liabilities have been translated at the respective closing exchange rates as promulgated by NATO. The payable as at 31 December 2017 is €0.9M compared with the 2016 amount of €3.1M.

A manual accrual has been assessed by analysing PARMIS invoices paid in January and the first 2 weeks of February 2018 with 2017 (and earlier) invoice dates. Central Automatic Data Processing System (CADPS) invoices and other material invoices during the same period were also reviewed to ensure they were accrued in the correct year. The estimated accrual for goods and services as at 31 December 2017 is €26.7M compared with the 2016 accrual of €19.8M.

Other payables

There are no cash in transit invoices that have been paid but not cleared from the bank in 2016. Other payables include bank interest payable to National Treasuries (€0.767M) and income generated from levies (€4.889M). Income generated from levies has increased by €0.817M since 2016.

3. Advances

	2017	2016
Other advances	127,824	165,702
Total	127,824	165,702

Other advances

Other advances equal accumulated unearned revenue which represents the excess of national contributions and miscellaneous revenue over expenditure on the NAMMO programme to date and is similarly reflected in the level of cash holdings within the NAMMO bank accounts.

The movement on unearned revenue can be reconciled as follows:

	2017	2016
Unearned revenue b/f	165,702	244,429
National contributions	359,258	321,058
Miscellaneous revenue (excl bank interest)	19,174	5,763
Bank interest	2	10
<i>Less:</i>		
Operational expenditure	(407,462)	(402,940)
Other operational revenue	(8,148)	(3,476)
Bank interest returned to nations	(1)	(7)
<i>Add:</i>		
Miscellaneous financial charges / (income)	(1)	(1)
Foreign exchange gains / (losses)	(700)	866
Unearned revenue c/f	127,824	165,702

C. Notes to Statement of Financial Performance

1. Revenue

	2017	2016
National contributions	359,258	321,058
National contributions to be called for	0	0
Other reimbursements	37,878	78,728
Total	397,136	399,786

National contributions represent the funds provided by nations to support NAMMO in fulfilling its objectives.

Other reimbursements are the movement on unearned revenue which represents the excess of revenue over expenditure in the financial year. The practice is to adjust revenue to reduce it accordingly and account for it on the Statement of Financial Position within advances.

2. Expenses

Personnel

The costs for operating the Agency's headquarters are accounted for in the NETMA administration budget.

Contractual supplies and services

	2017	2016
Operating expenses	(396,436)	(400,653)
PPE movement	0	0
Total	(396,436)	(400,653)

Expenditure on the NAMMO programme is booked upon the validation of invoices received from industry and identified by funding office.

Where expenses have been generated from one nation undertaking work on behalf of another those expenses have been excluded in accordance with IPSAS 23.

3. Finance costs

	2017	2016
Foreign exchange gain / loss	(700)	866
Other financial income & charges	0	1
Total	(700)	867

Translation gains and losses occur when assets and liabilities held in foreign currencies are converted to a Euro value at the closing NATO-promulgated exchange rates for the financial period. Translation adjustments have been applied to the bank balance held in GBP and outstanding liabilities and advances.

Realised gains and losses occur when currency transactions are paid or received at a different rate to that which the expense or income was accounted or accrued for.

Other financial income includes bank interest earned on the accounts held to fund the NAMMO program. Where income has not been refunded to National Treasuries the remaining balance is treated as unearned revenue. The value of bank interest received is slightly lower in 2017 compared to 2016 due to low rates and reduced bank balances.

D. Notes to Statement of Cash Flow

1. Surplus / (deficit) from operating activities

	2017	2016
Surplus / (deficit)	0	0
Total	0	0

This represents the surplus or deficit from normal operating activities before interest, depreciation and financial charges such as exchange differences arising from transactions.

2. Increase / (decrease) in payables

	2017	2016
Payables to suppliers	4,657	(2,434)
Other payables	811	(2,013)
Total	5,468	(4,447)

Payables to suppliers represent validated invoices presented but not yet paid and the manual accruals identified.

Other payables include bank interest and levy's generated from defence programmes.

3. Increase / (decrease) in advances

	2017	2016
Advance contributions	0	0
Unearned revenue	(37,878)	(78,727)
Total	(37,878)	(78,727)

Advance contributions represent the funds received from nations for the next financial year. The movement on unearned revenue represents the accumulated excess of contributions over expenditure for the financial year.

4. Decrease / (increase) in receivables

	2017	2016
National contributions	0	0
Other receivables	(2,027)	(31)
Total	(2,027)	(31)

The movement on contributions due represents the change in the nations' debt to the programme from the previous financial year.

Receivables include credit invoices received on PARMIS payables which will be offset against payables in 2017.

E. Notes to Statement of Budget Execution

1. Budget analysis - 2017

	2017	2016
All nations initial approved budget	431,449	361,816
In year budget adjustments	19,200	64,224
Total	450,649	426,040

The basis used for the budget and actual numbers in the budget execution statement is the cash basis and is therefore different to the accrual basis used to prepare the financial statements. The budget is compiled based on the advice and assistance of a number of sources including nations, commercial and technical staff within NETMA and industry. It has been based on the best information available and takes into account known payment plans and estimates of new work in line with advice on technical progress. No carry forward from 2016 was included in the estimate and no unused budget will be carried into 2018 with credits lapsing accordingly.

2. Reconciliation between Statement of Cash Flow and Statement of Budget Execution

	2017	2016
NET CASH INFLOW FROM OPERATING ACTIVITIES	(34,437)	(83,205)
- Cash contributions received in year	(359,258)	(321,058)
- Bank interest in year	(2)	(10)
- Other reimbursements	(22,643)	(6,089)
GROSS CASH OUTFLOW FROM OPERATING ACTIVITIES	(416,339)	(410,362)
- Bank interest returned to Italy in year	7	11
- Other disbursements	20,432	6,216
EXPENSES PRE EXCHANGE RATE VARIATIONS	(395,900)	(404,135)
- Foreign exchange gains and losses	(77)	518
- Operational budget vs actual exchange gains and losses	(9,832)	(3,770)
PREDICTED BUDGET CASH PAYMENTS	(405,809)	(407,387)
SCHEDULE 5: EXPENSES	(395,743)	(411,320)

In accordance with IPSAS 24 – Presentation of Budget Information in Financial Statements the above reconciliation has been carried out for the financial year ending 31 December 2017. Under IPSAS 24 the reconciliation is carried out between the Statement of Cash Flow (net cash flow from operating activities) and the Statement of Budget Execution. To present budgeted and actual amounts on a comparable basis, as required under the IPSAS, actual amounts have been converted using the Operational Budget (OB) rates for the comparison with budgeted amounts.

The difference between expenses stated at the OB and the actual exchange rate is included as a reconciling movement.

3. Reconciliation between Statement of Financial Performance and the Statement of Budget Execution

	2017	2016
SCHEDULE 2: OPERATING EXPENSES	397,136	399,786
Add: opening payables and accruals	22,926	26,297
Less: closing payables and accruals	(27,584)	(22,926)
Exchange rate difference (OB v corporate)	9,832	3,770
Foreign exchange gains and losses	77	(518)
PREDICTED BUDGET CASH PAYMENTS	402,386	406,409
SCHEDULE 5: EXPENSES	395,743	411,320

The above reconciliation is carried out between the Statement of Financial Performance and the Statement of Budget Execution for the financial year ending 31 December 2017. This reconciles accrual based expenditure that is reported on the Statement of Financial Position and cash based expenditure reported as expenses on the Statement of Budget Execution. The residual variance between cash and budget is approx. 1.7% (€6.6M) and results from timing differences in payments.

F. Contingent Liabilities / Provisions

NAMMO has no contingent liabilities or provisions.

G. Related Parties Disclosure

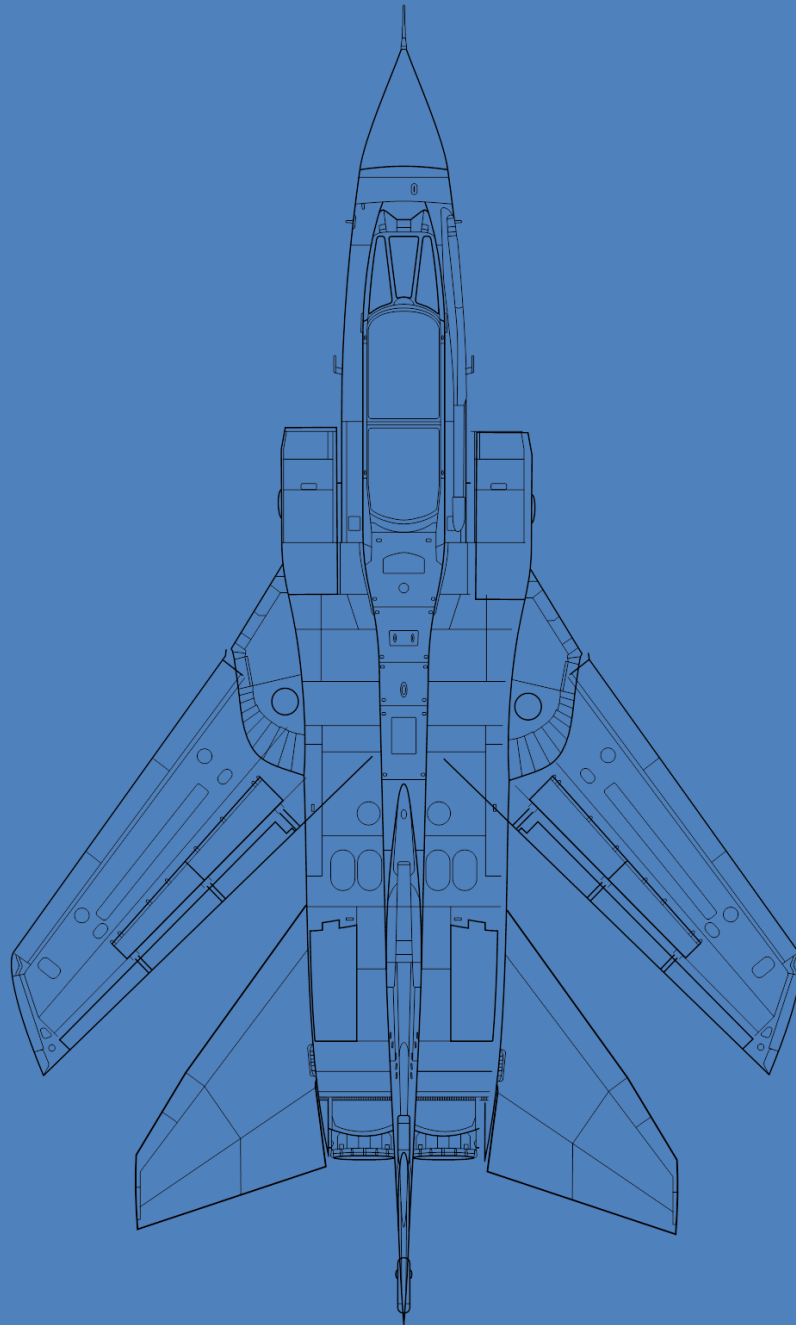
The key management personnel of NAMMO have no significant related party relationships that could affect the operation of NAMMO. Board members receive no remuneration and senior management is remunerated in accordance with the published NATO pay scales. Both do not receive loans that are not available to all staff.

H. Write-Off and Donations

In accordance with the NATO Financial Regulations, where a global statement of write-offs and donations shall be reported in the Annual Financial Statements NETMA can report that 2,462 items were submitted and approved for write-off through the NETMA Internal Audit section in 2017 in accordance with NETMA delegated authorities. These write offs cover items that are obsolete, damaged beyond economic repair or lost.

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

NATO UNCLASSIFIED



IBA-A(2018)0095-REV1
10 September 2018

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

Cc: General Manager, NETMA
Division Leader, Finance Division, NETMA
Chairman, Resource Policy & Planning Board (RPPB)
Branch 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 NATO EF 2000 and TORNADO Development, Production and Logistics Management Agency (NETMA) Restated Financial Statements for the year ended 31 December 2017 – IBA-AR(2018)0021***

The Board herewith submits its approved Auditor's Report and a Letter of Observations and Recommendations with a Summary Note for distribution to the NATO Council.

Yours sincerely,

Hervé-Adrien Metzger
Chairman

Attachments: As stated above.



**Summary Note for Council
by the International Board of Auditors for NATO (Board)
on the audit of the Restated Financial Statements of the
NATO EF2000 and Tornado Development,
Production and Logistics Management Agency (NETMA)
for the year ended 31 December 2017**

NETMA manages the NAMMO and NEFMO Production and Logistics Organisations programmes and their related budgets.

The Board audited the Restated Financial Statements of the Administrative Budget of NETMA for the year ended 31 December 2017. The total expenditure in 2017 for the Administrative Budget amounted to EUR 43 million.

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

During the audit, the Board made two observations with recommendations. These observations do not impact the audit opinion:

1. Roles and responsibilities of Head of Internal Audit does not ensure segregation of duties and independence.
2. Internal Controls over Financial Report need to be improved.

The Board also followed up on the status of the observations from the previous year's audit and found that one recommendation was settled.

The Auditor's Report (Annex 2) and the Letter of Observations and Recommendations (Annex 3) were issued to the NETMA whose comments have been included, with the Board's position on those comments where necessary, see Appendix to Annex 3.

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ANNEX 2
IBA-AR(2018)0021-REV1

29 August 2018

INTERNATIONAL BOARD OF AUDITORS FOR NATO

AUDITOR'S REPORT ON THE RESTATED FINANCIAL STATEMENTS OF

**THE NATO EF 2000 AND TORNADO DEVELOPMENT,
PRODUCTION AND LOGISTICS MANAGEMENT AGENCY**

(NETMA)

FOR THE YEAR ENDED 31 DECEMBER 2017

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

Report on the Restated Financial Statements

The International Board of Auditors for NATO (Board) audited the accompanying restated Financial Statements of NETMA, which comprised the Statement of Financial Position as at 31 December 2017, and the Statement of Financial Performance, the Cash Flow Statement and the Statement of Changes in Net Assets/Equity for the year then ended, and the notes to the financial statements, including a summary of significant accounting policies. The Board also audited the Statement of Budget Execution 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 opinion.

Opinion on Restated Financial Statements

In our opinion, the restated financial statements present fairly, in all material respects, the financial position of NETMA 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 authorised by the North Atlantic Council.

Auditor's Responsibility

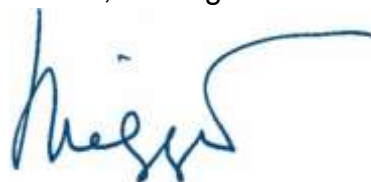
In addition to the responsibility to express an opinion on the financial statements described above, our responsibility includes expressing an opinion on whether the financial transactions and information reflected in the financial statements are, in all material respects, in compliance with the NATO 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 authorised expenditure and whether their operations have been carried out in compliance with the financial and personnel regulations in force. Such procedures include the assessment of the risks of material non-compliance.

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

Opinion on Compliance

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

Brussels, 29 August 2018



Hervé-Adrien Metzger
Chairman

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**ANNEX 3
IBA-AR(2018)0021-REV1**

29 August 2018

INTERNATIONAL BOARD OF AUDITORS FOR NATO

LETTER OF OBSERVATIONS AND RECOMMENDATIONS

**FOR THE NATO EF 2000 AND TORNADO DEVELOPMENT,
PRODUCTION AND LOGISTICS MANAGEMENT AGENCY**

(NETMA)

FOR THE YEAR ENDED 31 DECEMBER 2017

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Introduction

The International Board of Auditors for NATO (Board) audited the Restated NETMA Financial Statements for the year ended 31 December 2017 and issued an unqualified opinion on the financial statements and on compliance.

Observations and Recommendations

The Board's audit resulted in two observations and recommendations.

These observations do not impact the audit opinion:

1. Roles and responsibilities of Head of Internal Audit does not ensure segregation of duties and independence.
2. Internal Controls over Financial Report need to be improved.

The Board also followed up on the status of the observations from the previous year's audit and found that one recommendation was settled.

The Board also issued a Management Letter (reference IBA-AML(2018)0013) to the NETMA General Manager with observations for management's attention.

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

OBSERVATIONS AND RECOMMENDATIONS

1. ROLES AND RESPONSIBILITIES OF HEAD OF INTERNAL AUDIT DOES NOT ENSURE SEGREGATION OF DUTIES AND INDEPENDENCE

Reasoning

1.1 According to Article 13 of NATO Financial Regulations (NFRs) all NATO bodies shall undertake internal audit activities in order to evaluate risk exposures and the effectiveness of internal controls in managing risk within the organisation's governance, operations and information systems regarding: a) Reliability and integrity of financial and operational information; b) effectiveness and efficiency of operations and internal controls c) safeguarding of assets; and d) compliance with rules and regulations. Paragraph 12.3 mentions that internal control activities shall include among others: a) segregation of duties, and b) avoidance of conflicts of interests.

1.2 The International Standards for the Professional Practice of Internal Auditing (Standards) state that the internal audit activity must be independent and internal auditors must be objective in performing their work. Independence is the freedom from conditions that threaten the ability of the internal audit activity to carry out internal audit responsibilities in an unbiased manner. Internal auditors must have an impartial, unbiased attitude and avoid any conflict of interest. If independence or objectivity is impaired in fact or appearance, the details of the impairment must be disclosed to appropriate parties.

Observation

1.3 The Board found that the Head of Internal Audit is also the Section Leader of the Treasury, Accounting, Invoice Processing and Audit Section (Section F3). Therefore, the Head of Internal Audit is involved in very important daily operations of the entity. This is against the segregation of duties principle, which is a key preventive control against fraud and error.

1.4 In addition, the roles and responsibilities that the Head of Internal Audit has, being also the Section Leader of the Finance Department, increases the risk of impairing the organizational independence of the Internal Audit team and create a conflict of interest. Internal audit should have no authority and responsibility for activities it reviews.

Recommendation

1.5 The Board recommends NETMA to ensure compliance with the segregation of duties principle. NETMA should strengthen the organisational independence of Internal Audit by ensuring the Head of Internal Audit and audit staff is not involved and responsible for business operations of the entity.

2. INTERNAL CONTROLS OVER FINANCIAL REPORTING NEED TO BE IMPROVED

Reasoning

2.1 Financial Statements shall be free of misstatements, mathematical errors, non-reconciling items, or any other errors or omissions caused by lack of control during preparation. Entities should have proper internal controls, including reviews and reconciliations in place to ensure the consistency and the accuracy of information presented in the Financial Statements.

Observation

2.2 NETMA issued 2017 Financial Statements on 28 March 2018 to the Board for audit. We found material misstatements and mathematical errors in these financial statements.

2.3 Following the correction of the misstatements identified during the audit, NETMA submitted restated Financial Statements to the Board on 09 July 2018.

Recommendation

2.4 The Board recommends NETMA to strengthen the verification procedures of figures and information provided in the financial statements and to improve the internal control procedures in order to prevent or detect these mistakes before the issuance of the Financial Statements.

FOLLOW-UP OF PREVIOUS YEARS' OBSERVATION

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

OBSERVATION / RECOMMENDATION	ACTION TAKEN	STATUS
<p>(1) NETMA FY 2016 IBA-AR(2017)21, paragraph 1</p> <p>GOOD 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 recommended that:</p> <p>a) the draft NETMA Internal Audit Manual be finalised, and that NETMA Internal Audit should ensure that it is able to demonstrate compliance with the auditing standards included in the manual (International Standards for the Professional Practice of Internal Auditing), and is fully evaluating risk management and internal control throughout NETMA, and that this work is clearly documented so as to demonstrate compliance against NETMA's chosen Internal Control Framework, COSO.</p>	<p>NETMA finalised their Internal Audit Manual in 2017.</p> <p>Also, NETMA Internal Audit annually assesses the risk management and internal control system in place in NETMA against COSO.</p>	<p>Observation Settled.</p>

**NATO EF 2000 AND TORNADO DEVELOPMENT, PRODUCTION AND LOGISTICS
MANAGEMENT AGENCY (NETMA) FORMAL COMMENTS
ON THE LETTER OF OBSERVATIONS AND RECOMMENDATIONS AND THE
INTERNATIONAL BOARD OF AUDITORS (BOARD) POSITIONS**

**OBSERVATION 1:
ROLES AND RESPONSIBILITIES OF HEAD OF INTERNAL AUDIT DOES NOT
ENSURE SEGREGATION OF DUTIES AND INDEPENDENCE**

NETMA's Formal Comments

The IBAN audit reports of the 2015 and 2016 Annual Financial Statements for NETMA recommended that NETMA should be able to demonstrate compliance with the International Standards for the Professional Practice of Internal Auditing (ISPPIA), relating to organisational independence.

During the audit of the 2017 Annual Financial Statements NETMA demonstrated, in detail, to the IBAN that the NETMA Internal Audit function is in full compliance with the ISPPIA standards for organisational independence as recommended.

This included a demonstration that the potential for conflicts of interest was identified and robust mitigations were in place as recommended by the ISPPIA standards. With respect to the Head of Internal Audit these mitigations include several points of independent review both internally with the Internal Audit Committee and externally with the Audit Advisory Panel. These points of independent review limit the ability of the Head of Internal Audit to act autonomously to influence either the subjects, scope or outcome of audits. Additionally, as discussed during the audit, for audits relating to activities under the control of Section Leader F3, an alternative Section Leader takes his place in leading the audit to ensure impartiality.

The NETMA Internal Audit function is delivering real value to the nations and internal stakeholders with its integrated approach to internal control, linking the COSO review process, risk management and internal audit.

I am content that the NETMA Internal Audit function is fully in compliance with the ISPPIA standards in respect of Organisational Independence, as previously recommended by the IBAN, but I will nevertheless ensure that the feasibility of this new recommendation is discussed at the next Audit Advisory Panel meeting in October 2018.

Board's Position

The Board acknowledges that NETMA Head of Internal Audit presented to the Board the NETMA procedures and the measures that NETMA considers as adequate to mitigate the risks that arise from conflicts of interest, segregation of duties and independence issues related to the NETMA Head of Internal Audit being the Section Leader F3. However, the Board maintains its position as the Head of Internal Audit and audit staff should not be involved and responsible for business operations. We welcome the initiative of the General Manager to address the Board's recommendation to the Audit Advisory Panel meeting in October 2018.

NETMA ANNUAL FINANCIAL STATEMENTS

PERIOD ENDED 31 DECEMBER 2017



NETMA

NATO EF2000 AND TORNADO DEVELOPMENT, PRODUCTION
AND LOGISTICS MANAGEMENT AGENCY

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Introduction

NATO EF2000 and Tornado Development, Production and Logistics Management Agency (NETMA) is an agency formed jointly by NAMMO (NATO Multi-Role Combat Aircraft Development, Production and In-Service Support Management Organisation) and NEFMO (NATO European Fighter Aircraft Development, Production and Logistics Support Management Organisation) in 1996 to manage procurement for and the administration of the two programmes within the framework of NATO. The operations of NETMA concerning NAMMO and NEFMO are controlled by a Joint Steering Committee of the three NAMMO nations and the four NEFMO nations involved in the programmes.



NETMA is based in Hallbergmoos, Germany and is an Executive Body created by charter to administer the functions of two NATO Production and Logistic Organisations (NPLOs). The two NPLOs are NAMMO and NEFMO.

The budgetary organisation of NETMA is funded by the four member nations – Germany, Italy, Spain and United Kingdom. Budget approval is given jointly by the Boards of Directors of NAMMO and NEFMO. As a NATO agency, NETMA is exempt from taxation relating to operating revenue and expenses, where VAT is incurred this is recovered directly from the host nation's tax office.

Key points from the Annual Financial Statements

NETMA Liabilities

The agency's office accommodation is the subject of an operating lease and is therefore not capitalised as PP&E. The office accommodation has been determined as an operating lease and, in accordance with IPSAS 13, must be expensed on a straight line basis over the lease term. IPSAS 13 mandates that operating leases are accounted for in this way irrespective of cash payments made. As NETMA were able to negotiate a rent free period at the start of the lease, these expenses are accrued as a long term liability which will be unwound over the term of the lease. This only impacts on the Financial Statements and does not impact on either the budget or cash spent in 2017.

Addressing Previous Audit Observations

The IBAN audit report for the 2016 NETMA Financial Statements included one recommendation associated with the adoption of the new NATO Financial Regulations in 2015:

"To finalise the Internal Audit Manual and ensure that Internal Audit is fully evaluating risk management and internal control throughout NETMA"

NETMA has introduced significant improvements to the Internal Audit process during 2017. The Internal Audit Manual and Internal Audit Charter have been fully updated to ensure compliance with the International Standards for the Professional Practice of Internal Auditing, which were revised in 2017, and to provide clear guidance to the Internal Audit team. In addition, the Internal Audit function has successfully implemented the Committee of Sponsoring Organisations of the Treadway commission (COSO Framework) to provide assurance to the board that internal controls within the organisation are appropriate and the approach taken by NETMA has been endorsed by the IBAN.

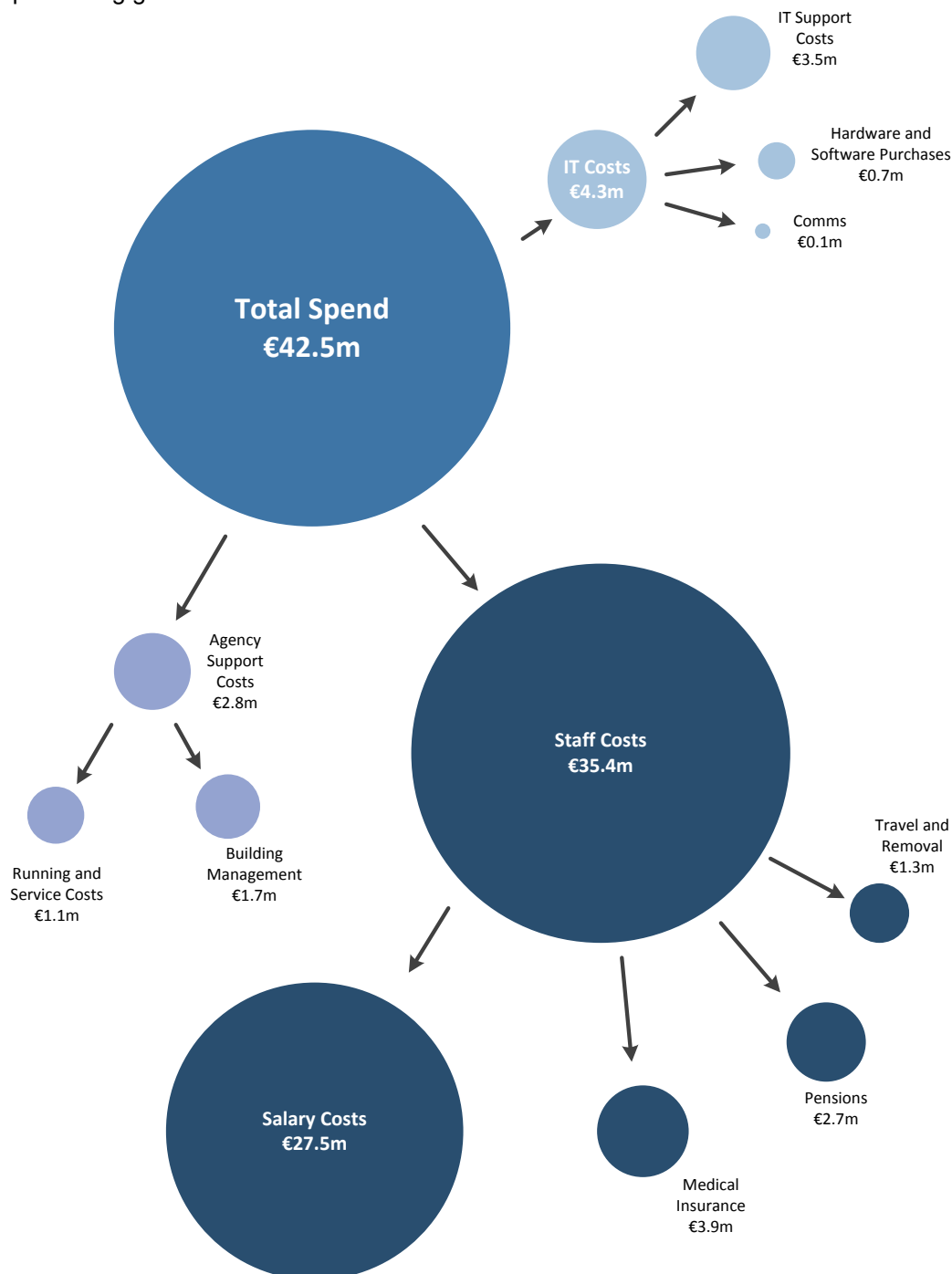
NETMA will be working with the IBAN during the audit of the Annual Financial Statements to understand what further improvements, if any, are required to ensure compliance with the NATO Financial Regulations.

NETMA Expenditure Breakdown 2017

The NETMA spend in the Administration Budget, as reported in the NETMA financial statements, was €42.5m in 2017. The majority (83%) of this expenditure is taken up in the staffing costs of the agency with the remainder spent on the rent and running costs of the NETMA Headquarters at Hallbergmoos and the provision and support of IT and communications equipment and infrastructure.

NETMA continues to look for opportunities to increase efficiency in the admin budget and the 2017 figures already reflect a reduction in the cost of IT consultancy support brought about by a robust negotiation of the existing support contract during 2014 as well as a reduced cost of property rental following relocation to Hallbergmoos in 2015

In total, the costs of running the agency equate to a little over one cent per programme Euro spent representing good value to our customer nations.



Statement of Internal Control



As General Manager of NETMA, I have responsibility for maintaining a effective system of internal control that supports the achievement of my Agency's policies, aims and objectives, set by NETMA's Four Nations and BoD, whilst safeguarding the funds and assets for which I am personally responsible, in accordance with the responsibilities assigned to me.

The system of internal control is designed to manage the risk of failure to achieve the organisation's policies, aims and objectives but it can only provide reasonable and not absolute assurance of effectiveness.

The system of internal control is based on an ongoing evidence based process designed to identify the principal risks to the achievement of my Agency's policies, aims and objectives, to evaluate the nature and extent of those risks and to manage them efficiently and effectively on a continual year round basis. The board has established appropriate structures, reporting lines and responsibilities to support the delivery of objectives.

As General Manager, I have responsibility for reviewing the effectiveness of the system of internal control. The processes in place to achieve this are summarised below:

- NETMA has a Management Plan which identifies NETMA's objectives. The Management Plan focuses on business change objectives and Program risks. Key Business risks have now been identified, mitigated and owners have been appointed to monitor and report on these on a regular basis.
- Management checks are undertaken and the internal audit function performs a range of audit activities, based on an annual audit plan agreed by the Audit Advisory Panel alongside the detailed audit of property held in industry, to ensure appropriate internal controls are in place and adhered to. The Internal Audit has been updated to ensure compliance with the International Standards for the Professional Practice of Internal Auditing in accordance with previous IBAN recommendations.

During 2016 the agency, under recommendation from the IBAN and as agreed by the Audit Advisory Panel, introduced the integrated framework for internal control developed by the Committee of Sponsoring Organisations of the Treadway commission (COSO Framework) as a mechanism for formally documenting the internal control system and providing assurance that it is functioning effectively. The annual COSO review was undertaken as scheduled in 2017.

My review of the effectiveness of the system of internal control is informed by the work of the executive managers within the organisation who have responsibility for the development and maintenance of the internal control framework, comments made by the external auditors in their management letters and other reports together with the results of the annual COSO review.

I am content that the processes in place within the organisation provide reasonable assurance of the effectiveness and efficiency of the organisation's operations, the reliability of its financial information and its integrity with regards to application and compliance to applicable rules and regulations. Whilst we always seek to improve our processes each year there are no material internal control weaknesses currently identified that need specific intervention from Senior Management in 2017.

MR GABRIELE SALVESTRONI
General Manager

MR MARK GANFIELD
Financial Controller

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STATEMENT OF FINANCIAL POSITION

AS AT 31 DECEMBER 2017

(in thousands of Euros)

	Notes	2017	2016
Assets			
Current assets			
Cash and cash equivalents	B1	7,978	23,649
Short term investments		0	0
Receivables	B2	12,151	859
Prepayments	B3	0	160
Inventories		0	0
		<u>20,129</u>	<u>24,668</u>
Non-current assets			
Property, plant & equipment	B4	6	76
Intangible assets		0	0
		<u>6</u>	<u>76</u>
Total assets		<u>20,135</u>	<u>24,744</u>
Liabilities			
Current liabilities			
Payables	B5	4,238	6,716
Deferred revenue	B6	9,877	6,516
Advances	B7	4,906	10,167
		<u>19,021</u>	<u>23,399</u>
Non-current liabilities			
Provisions		0	0
Other Long Term Liabilities	B8	1,108	1,269
		<u>1,108</u>	<u>1,269</u>
Total liabilities		<u>20,129</u>	<u>24,668</u>
Surplus/Deficit	B9	(70)	(139)
Reserves	B10	76	215
Total net assets		<u>6</u>	<u>76</u>

The financial statements on pages 7 to 11 and their associated notes were issued to the International Board of Auditors for NATO on 28th March 2018.



MR GABRIELE SALVESTRONI
General Manager



MR MARK GANFIELD
Financial Controller

STATEMENT OF FINANCIAL PERFORMANCE

FOR THE YEAR ENDED 31 DECEMBER 2017

(in thousands of Euros)	Notes	2017	2016
Revenue			
Revenue	C1	42,982	43,726
Financial revenue		0	0
Other revenue		0	0
Total revenue		42,982	43,726
Expenses			
Personnel	C2	36,015	36,099
Contractual supplies and services - Buildings & Maintenance	C3	2,766	2,862
Contractual supplies and services - IT Services	C4	4,415	4,596
Depreciation and amortisation	C5	70	139
Impairment		0	0
Provisions		0	0
Other expenses		0	0
Finance costs	C6	(214)	169
Total expenses		43,052	43,865
Surplus/(Deficit) for the period		(70)	(139)

STATEMENT OF CASH FLOW

FOR THE YEAR ENDED 31 DECEMBER 2017

(in thousands of Euros)

	Notes	2017	2016
Cash flow from operating activities			
Surplus/(deficit)	D1	(70)	(139)
Non-cash movements			
Depreciation/ amortisation	D2	70	139
Impairment		0	0
Increase /(decrease) in payables	D3	(2,478)	5,620
Increase/ (decrease) in advances	D4	(5,261)	(9,703)
Increase/ (decrease) in other liabilities	D5	(161)	485
Increase/ (decrease) in provisions	D6	160	(160)
Increase/ (decrease) in deferred revenue	D7	3,361	6,516
Decrease/ (Increase) in receivables	D8	(11,292)	(362)
Net cash flow from operating activities		(15,671)	2,396
Cash flow from investing activities			
Purchase of property plant and equipment / Intangible assets		0	0
Proceeds from sale of property plant and equipment		0	0
Net cash flow from investing activities		0	0
Cash flow from financing activities		0	0
Net cash flow from financing activities		0	0
Net increase/(decrease) in cash and cash equivalents		(15,671)	2,396
Cash and cash equivalents at the beginning of the period		23,649	21,253
Cash and cash equivalents at the end of the period		7,978	23,649

STATEMENT OF CHANGE IN NET ASSETS/EQUITY

FOR THE YEAR ENDED 31 DECEMBER 2017

(in thousands of Euros)

		PP&E Asset Reserve	Revaluation Reserves	Accumulated surplus/deficit	Total
Balance at the beginning of the period 2016		351	0	(136)	215
Changes in accounting policy		0	0	0	0
Restated balance		351	0	(136)	215
Transfer from Accumulated Surplus / Deficit		(136)	0	136	0
Surplus/(deficit) for the period		0	0	(139)	(139)
Balance at the end of the period 2016		215	0	(139)	76
Changes in accounting policy		0	0	0	0
Restated balance		215	0	(139)	76
Transfer from Accumulated Surplus / Deficit	D1	(139)	0	139	0
Surplus/(deficit) for the period	D1	0	0	(70)	(70)
Balance for the period ended 2017		76	0	(70)	6

STATEMENT OF BUDGET EXECUTION

FOR THE YEAR ENDED 31 DECEMBER 2017

(in thousands of Euros)

		Initial budget	Transfers	BA1	Transfers	Final budget	Commitments	Expenses	Carry forward	Lapsed
Budget 2017										
Chapter 1										
Personnel costs	E1	38,066	0	0	0	38,066	35,482	35,393	89	2,584
Chapter 2										
Agency support costs	E1	3,053	0	0	0	3,053	2,761	2,625	136	292
Chapter 3										
Process and IT management	E1	4,748	0	0	0	4,748	4,254	3,681	573	495
Total FY 2017		45,867	0	0	0	45,867	42,496	41,698	798	3,371
Chapter 1 c/o from 2016		58	0	0	0	58	52	42	10	7
Chapter 2 c/o from 2016		299	0	0	0	299	296	222	74	2
Chapter 3 c/o from 2016		438	0	0	0	438	402	402	0	36
Historical c/o		7	0	0	0	7	5	5	0	2
Total		46,670	0	0	0	46,670	43,251	42,369	882	3,419

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A. Significant Accounting Policies

Basis of preparation

The financial statements of NETMA have been prepared in accordance with the International Public Sector Accounting Standards (IPSAS) and based on International Financial Reporting Standards (IFRS/IAS), as adopted by the North Atlantic Council (NAC) in 2002. In 2013, the NAC adopted an adaptation to IPSAS to better suit the specific requirements of the Alliance and an associated NATO accounting framework, applicable for financial reporting periods beginning on 1 January 2013.

The financial statements comply with the accounting requirements of the NATO Financial Regulations (NFRs) and the relevant NETMA directives and policies. In instances where there is a conflict between IPSAS and the NFRs this will be noted.

The financial statements have been prepared on a going concern basis. NATO Agency reform, which was approved by the Heads of State and Government at the Lisbon Summit in 2010, continues to mature. A new integrated NATO Procurement entity will be established to meet the needs of new procurement programmes, but none of the existing NATO agencies intend to integrate into this new organisation. In addition, at this stage, there is no intent to merge additional NATO agency support activity into the NATO Support Agency (NSPA). The route to implement shared services across NATO continues to develop, with the decision to implement shared services for Human Resource and General Procurement activities mandatory for the core NATO Bodies. The broadening of the use of these services to other NATO entities could be agreed at an appropriate time and NETMA, like other similarly funded NATO Agencies, has taken the view that integration with these activities could be considered when a proven benefits case for the specific activity can be demonstrated. In the light of the anticipated impact of these initiatives on the programme it is considered that there are no impediments to continuing on a going concern basis for the foreseeable future.

The financial statements have been prepared on a historical cost basis except for financial instruments that are measured at fair value at the end of each reporting period. The principal accounting policies are set out below. They have been applied consistently to all periods presented. The accounting principles recognised as appropriate for the recognition, measurement and reporting of the financial position, performance and cash flows on an accrual based accounting system using historical costs have been applied consistently throughout the reporting period.

In accordance with Article 2.1 of the NFRs, the financial year of NETMA is 1 January to 31 December.

Accounting estimates and judgments

In accordance with IPSAS and generally accepted accounting principles, the financial statements necessarily include amounts based on estimates and assumptions made by the management and based on historical experience as well as on the most reliable information available. In exercising the judgments to make the estimates, a degree of caution was included in light of the principle of 'prudence' required by IPSAS in order not to overstate assets or revenue or understate liabilities or expenses.

The estimates and underlying assumptions are reviewed on an ongoing basis. These estimates and assumptions affect the amounts of assets, liabilities, revenue and expenses reported. By their nature, these estimates are subject to measurement uncertainty. The effect of changes to such estimates and assumptions in future periods could be significant to the financial statements.

Changes in accounting policy and standards

The same accounting policies are applied within each period and from one period to the next, unless a change in accounting policy meets one of the criteria set in IPSAS 3. For the 2017 Financial Statements the accounting policies have been applied consistently throughout the reporting period. There have been no changes to NETMA accounting policy in 2017.

Changes in pronouncements

No accounting standard has been adopted earlier than the application date as stated in the IPSAS standards. The following IPSAS are not relevant for the NETMA Financial Statements 2017: IPSAS 26 (Impairment of Cash-Generating Assets), IPSAS 27 (Agriculture). The following IPSAS have no material effect on the financial statements: IPSAS 5, IPSAS 10, IPSAS 11, IPSAS 16, IPSAS 18 and IPSAS 32. Several new IPSAS became effective 1st January 2017: IPSAS 34 (Separate Financial Statements) and IPSAS 35 (Consolidated Statements) both superseded IPSAS 6; IPSAS 36 (Investments in Joint Ventures) superseded IPSAS 7; and IPSAS 37 (Joint Arrangements) superseded IPSAS 8. In addition, IPSAS 38 (Disclosure of interests in other entities) revises disclosure requirements previously covered by IPSAS 6, 7 and 8. None of these new IPSAS standards have a material impact on the presentation of the NETMA Financial Statements. IPSAS 39 (Employer benefits)

becomes effective January 1st 2018 and will replace IPSAS 25. IPSAS 40 (Public Sector Combinations) will become effective January 1st 2019. Neither has been adopted by NETMA for the 2017 Financial Statements.

Restatements

Due to a change in accounting treatment, the 2016 Receivables, Payables and Deferred Revenue values have been adjusted.

Changes in financial rules and regulations

During 2015 NATO adopted new financial rules and regulations. During 2017 there were no additional changes. These financial statements have been produced in line with the 2015 changes to financial rules and regulations.

Foreign currency

These financial statements are presented in Euros, which is the NETMA functional and reporting currency. Foreign currency transactions are translated into Euros at the NATO exchange rates prevailing at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at year-end are translated into Euros using the NATO exchange rates applicable at 31 December 2017. The resulting realised and unrealised gains and losses are recognised in the Statement of Financial Performance.

NETMA used the following exchange rates as at 31st Dec 2017:

EUR – GBP = 1: 0.8799

EUR – USD = 1: 1.186

Consolidation

The NETMA financial statements are not consolidated in-line with the NETMA Agency charter.

Financial instruments disclosure/presentation

NETMA uses only non-derivative financial instruments as part of its normal operations. These financial instruments include cash and cash equivalents, accounts receivable, liabilities, provisions and loans between NATO entities. Financial instruments are recognised in the statement of financial position at fair value.

Financial risk factors

Credit risk

There is very limited credit risk as the contributing nations generally have a high credit rating. The risk of financial loss due to a participating nation's failure to raise funds is still assessed as very low. In the event that there is a shortage of funds by one or more nations to meet financial obligations, other nations will be expected to provide the necessary funding.

Liquidity risk

The liquidity risk is based on the assessment of whether the organisation will encounter difficulties in meeting its obligations associated with financial liabilities. There is limited exposure to liquidity risk because of the budget 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 receiving payments represent the main liquidity risks.

Currency risk

The majority of transactions associated with the administrative budget are contracted in Euros and in order to have the required funding, NETMA also asks nations to provide their contributions in Euros. Therefore the exposure of financial instruments to foreign currency exchange risk associated with the administrative budget is considered negligible.

Interest rate risk

NETMA is restricted from entering into borrowings and investments, and therefore there is no significant interest rate risk identified.

Assets

The entity holds the following types of current assets:

Cash and cash equivalents

Cash and cash equivalents include cash on hand and current bank accounts.

Receivables

Receivables are stated at net realisable value, after provision for doubtful and uncollectible debts. It can also include amounts due by other NATO entities.

Contributions receivable are recognised when a call for contribution has been issued to the member nations. No allowance for impairment loss is recorded with respect to member nations' assessed contributions receivable. Other receivables include those from staff and external sources such as German MoD in relation to VAT receivable.

Property, Plant and Equipment

The categories of Property, Plant and Equipment (PP&E) relevant for NETMA are detailed below:

Land and Buildings: The agency's office accommodation is subject of a building lease and therefore not capitalised as PP&E. The office accommodation has been determined as an operating lease and, in accordance with IPSAS 13 - Leases, is expensed on a straight-line basis over the lease term. In 2015 this resulted in the creation of a long term liability due to a rent free period at the start of the contract on the new premises in Hallbergmoos. This liability will be unwound against rental payments on a straight line basis over the 10 year duration of the lease.

Office Furniture and Equipment: This includes items of non-aggregated office furniture and other miscellaneous office items (i.e. lamps, fans, projectors, printing equipment). Items in this category are depreciated on a straight line basis over a ten year period which equates to their useful life. It is assumed an item is fully depreciated with nil residual value at the end of its useful life.

IT and Communications Equipment: This consists of Commercial-Off-The-Shelf (COTS) purchase of computer systems (hardware and software), and communications equipment (i.e. telephones, faxes and accessories). Items in this category are depreciated on a straight line basis over a three year period. It is assumed an item is fully depreciated with nil residual value at the end of its useful life.

In accordance with IPSAS 17, PP&E are recognised as tangible assets when it is probable that future economic benefits or service potential associated with the item will flow to the entity and the cost or fair value can be measured reliably. PP&E with the exception of land are stated at cost less accumulated depreciation and accumulated impairment losses. NETMA's capitalisation threshold is €15,000, items with a purchase cost or fair value on acquisition above this threshold are capitalised and items falling below this threshold are fully expensed in the year of procurement.

For new asset additions during the year, the gross value of an asset is capitalised as PP&E on the Statement of Financial Position. The revenue for the full amount of the asset is accounted for in the year of purchase on the Statement of Financial Performance with a surplus on the Statement of Financial Performance being generated in the first year of purchase and transferred to the PP&E asset reserve account to increase accumulated asset reserves. A full months depreciation is only charged if the item is purchased in the first half of the month (ie: before 15th Month), otherwise the first month of depreciation starts from the following period.

Depreciation is recognised so as to write off the cost of the assets less their residual values over their estimated useful lives, using the straight-line method. The estimated useful lives, residual values and depreciation method are reviewed at the end of each reporting period, with the effect of any changes in estimate accounted for on a prospective basis. Depreciation is accounted for as an expense which generates a deficit on the Statement of Financial Performance. This deficit is transferred to PP&E Asset Reserves at the end of each year to reduce the accumulated asset reserve.

An item of PP&E is derecognised upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising on the disposal or retirement of an item of PP&E is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognised in the Statement of Financial Performance.

Leases

As stated above the office accommodation has been determined as an operating lease and, in accordance with IPSAS 13 - Leases, is expensed on a straight-line basis over the lease term.

Liabilities

Payables

Payables (including amounts due to other NATO entities) are amounts due to third parties for goods and services received that remain unpaid as of the reporting date. They are recognised at their fair value. This includes estimates of accrued obligations for goods and services received at year-end but not yet invoiced.

Unearned revenue

Unearned revenue represents contributions from member nations and/or third parties that have been called for in current or prior years' budgets and that have not yet been recognised as revenue. Unearned revenue also includes miscellaneous income that nations have instructed remain on the programme accounts rather than be returned to the respective National Treasuries.

Advances

Advances are contributions from member nations called or received related to future years' budgets. Funds are called for in advance of their need because NETMA has no capital that would allow it to pre-finance any of its activities.

*Revenue and expense recognition***Revenue**

Revenue comprises of contributions from the four contributing nations: Germany, Italy, Spain and United Kingdom and other revenue earned during the period. Contributions from the four nations are called for in advance on a quarterly basis. Other revenue earned during a financial period includes bank interest and miscellaneous recoveries from staff for car parking and telephone calls.

Revenue is recognised to the extent that it is probable that economic benefits will flow to NETMA and revenue can be measured reliably. Where a transfer is subject to conditions that, if unfulfilled, require the return of the transferred resources, NETMA recognises a liability until the condition is filled.

Nation's contributions to the administrative budget are initially recorded as unearned revenue liabilities. They are recognised as revenue on the statement of financial performance when such contributions are used for their intended purpose as envisioned within the approved budget.

Expenses

The NETMA financial statements cover the running costs of the agency and of the NAMMO and NEFMO programmes. These costs cover pay and personnel, utilities, rental payments and those costs associated with information management support.

Cash flow statement

The cash flow statement is prepared using the indirect method and the format follows the layout provided by IPSAS 2 (Cash flow statement).

B. Notes to Statement of Financial Position

(in thousands of Euros)

1. Cash and cash equivalents

	2017	2016
Cash accounts	7,977	23,648
Clearing cash accounts	0	0
Petty cash and advances	1	1
Current bank accounts	0	0
Cash equivalents	0	0
Bank accounts interest	0	0
Total	7,978	23,649

NETMA operates two bank accounts into which all contributions are received and payments to suppliers are made. Interest earned is accumulated on an associated account and in the subsequent year is transferred to the main account to offset future Calls for Funds where permitted under National procedures. The petty cash accounts enable small, essential purchases to be made quickly and are reconciled on a monthly basis.

The reasons for the variance between 2017 and 2016 on the main accounts is that compared to previous years, the first quarter of 2018 Call For Funds has not arrived as an advance. Also a full lapsed credit adjustment was made in 2017 (which did not occur during 2016) meaning less funds were received from nations.

2. Receivables

	2017	2016
Contribution receivable from nations current year	3	0
Receivables from non-consolidated entities	649	408
Contribution receivable from nations following year	11,456	441
Receivables from staff members	43	9
Other receivables	0	0
Total	12,151	859

Receivables from non-consolidated entities

Represent receivables recoverable from MoD Germany with regards to VAT charged in 2017.

Contributions receivable from nations current year

Represent receivables from nations in the current year.

Contributions receivable from nations following year

Represent receivables from nations that have been called for relating to the following years budget within the current year but not yet received as at 31st December 2017.

Receivables from staff members

Receivables from staff members relate to the outstanding recoveries from advances of salaries made in the year. This account has been reconciled with payroll records at year end.

3. Prepayments

	2017	2016
Suppliers	0	160
Staff	0	0
Total	0	160

NATO UNCLASSIFIED

No material prepayments were made to suppliers in 2017 (value of €497 was paid in 2017 relating to 2018).

4. Property, Plant and Equipment

	2017	2016
PP&E	6	76
Total	6	76

The office accommodation in Hallbergmoos is deemed to be under an operating lease arrangement and therefore is not capitalised. The Agency controls two types of PP&E and is responsible for replacement and maintenance of these assets; Office Furniture & Equipment, and IT & Communications Equipment. The capitalisation threshold for all PP&E is €15,000. Upon moving to Hallbergmoos, the Agency took a view that integrated purchases (Cabling, Air Con Units, Security enhancements etc) were not to be capitalised due to no clear future ownership lines being in place and the ability to use such items if the Agency were to move premises.

As at 31 December 2017 only items within IT and Communications Equipment met the criteria for capitalisation. This consists of Commercial Off The Shelf purchase of (COTS) computer systems (hardware and software), and communications equipment (i.e. telephones, faxes and accessories). IT and Communications assets are measured at cost less depreciation. Depreciation is calculated on a straight-line basis over the useful life of IT and Communications Equipment.

In accordance with IPSAS 17, below is a reconciliation of the carrying amounts for Property, Plant and Equipment:

	2017	2016
Cost		
Opening Balance	76	215
Additions	0	0
Disposals	0	0
Depreciation	(70)	(139)
Closing Balance	6	76
Gross carrying amount	1,240	1,240
Accumulated depreciation	(1,233)	(1,163)
Net Carrying Amount	6	76

5. Payables

	2017	2016
Payables to suppliers	8	3
Payables to non-consolidated entities	0	0
Payables to staff members	0	0
Lapsed Credits to be offset from future CFFs	3,419	5,501
Other payables	811	1,212
Total	4,238	6,716

Payables to suppliers

Amounts payable to suppliers represents invoices for work undertaken but not yet paid. This account is reconciled to the payables sub-ledger within the financial system operated by NETMA on a monthly basis.

Lapsed Credits to be offset from future CFF's

These values align to the value reported in the Budget execution statement, showing budget called for but not spent that will be offset from the following years call for funds.

Other payables

Other payables are made up of the manual accrual figure which is made up of two elements. The first element relates to goods and services provided during 2017, an estimate is undertaken by reviewing invoices paid in January and the first 2 weeks of February 2018. The estimated accrual for goods and services as at 31 December 2017 is €350K. The other element is the estimated accrual relating to unpaid leave, this is based on

the untaken leave carried forward as at 31 December 2017 multiplied by the average salary costs per day. This results in an accrual of €461K.

6. Deferred Revenue

	2017	2016
Deferred Revenue	9,877	6,516
Total	9,877	6,516

Deferred Revenue represents accumulated unearned revenue which is the excess of national contributions and miscellaneous revenue over expenditure on the NETMA program to date. This value has increased for 2017 inline with the large receivable due from nations in relation to the 1st quarter Call for Funds made in December 2017 but not received at year end.

	2017	2016
Unearned revenue b/f	7,316	6,954
National Contributions	33,159	48,252
Miscellaneous Revenue (excl Bank Interest)	86	97
Movement in Receivable from nations for following year	10,215	441
Less:		
Operational Expenditure	43,156	42,950
Movement in Lapsed Credits from Budget Execution	(2,082)	5,501
Bank Interest returned to Nations	0	0
Miscellaneous Financial Charges / (Income)	600	0
Foreign Exchange Gains / (Losses)	(775)	776
Unearned revenue c/f	9,877	6,516

7. Advances

	2017	2016
Advance contributions	4,906	10,167
Total	4,906	10,167

Advance contributions

Advances include funding received above the budget for that year, for NETMA relocation and nations individual travel requirements.

8. Other long term liabilities

	2017	2016
Operating lease liability	1,108	1,269
Total	1,108	1,269

In May 2015 the agency moved into new office accommodation in Hallbergmoos. Due to delays in this move, rent was not charged until September 2016, despite the lease being signed from 1st December 2014. Therefore in accordance with IPSAS 13, a liability for rental payments over the rent free period has been created and will be unwound against actual payments over the life of the lease.

9. Surplus / (deficits)

	2017	2016
Surplus / (deficits)	(70)	(139)
Total	(70)	(139)

The accumulated deficit balance represents in year movements relating to PP&E. The deficit for 2017 results solely from in year depreciation charges totalling (€70K). This deficit is transferred to Reserves at the close of each financial year.

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10. Reserves

	2017	2016
PP&E asset reserve	76	215
Total	76	215

The PP&E asset reserve represents the nation's equity in PP&E. IT & Communications equipment assets are capitalised and accounted for at their net carrying amount (i.e. gross historical purchase costs less accumulated depreciation). At the end of 2016, the PP&E asset reserve was decreased by the accumulated deficit of €139K resulting in an opening Net Assets balance as at 1st January 2017 of €76K.

C. Notes to Statement of Financial Performance

1. Revenue

	2017	2016
National contributions	41,036	48,252
National contributions to be called for	0	0
Other reimbursements	1,945	(4,526)
Total	42,982	43,726

National contributions represent the funds provided by nations to support NETMA in fulfilling its objectives under the administrative budget. Funding is normally called for in advance on a quarterly basis.

Other reimbursements includes recoveries from nations in support of the overall NETMA Programme, the movement on unearned revenue represents the deficit of revenue over expenditure in the financial year and recoveries from staff employed by the agency.

2. Personnel

	2017	2016
Pay and overtime	22,720	22,647
Allowance	4,900	5,096
Pension	2,710	2,684
Medical and insurance	3,883	3,987
Travel	1,801	1,685
Total	36,015	36,099

Personnel expenses include civilian and military personnel expenses as well as other non-salary related expenses, in support of common funded activities. The amounts include expenses for salaries and emoluments for approved NATO permanent civilian positions and temporary personnel, for other salary related and non-related allowances including overtime, medical examinations, recruitment, installation, removal and for contracted consultants and training.

NATO introduced the Defined Contribution Pension Scheme (DCPS) on 1st July 2005. The scheme is a money purchase pension scheme which is funded by NETMA and the staff member. This pension scheme is compulsory for all new entrants. NETMA's contribution is 12% (Staff contribution is 8% of Basic Salary and the Additional Voluntary Contribution AVC (up to 5% of Basic Salary). Pension costs are predominantly for those members in the DCPS. The scheme is administered and accounted for centrally by NATO IS.

Travel costs include duty travel, home leave travel, removals and travel for interviews and repatriation.

At the year-end, NETMA has 254 established posts (same as 2016). A breakdown of wages, salaries and employee benefits is provided below. Costs remained largely consistent in 2017 as although there was a pay rise applied to all staff, a number of senior staff on high pay bands left the organisation.

	2017	2016
Employee benefits expense	31,494	31,720
Post employee benefits		
- For defined contribution pensions scheme	2,710	2,684
Untaken leave accrued	461	437
Total employee benefits expense	34,665	34,841

Untaken leave

Untaken leave at year-end may be carried over to the following year. NETMA has taken measures to ensure all leave is taken by 30 April of the following year in accordance with the CPRs.

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Related Parties Disclosure

The key management personnel of NETMA have no significant related party relationships that could affect the operation of NETMA. NETMA is led by 4 directors, one for each participating Nation. They are remunerated in line with NATO pay scales as is all other NETMA staff.

	2017	2016
Key management remuneration	844	916

The figure for 2017 is lower than 2016 due to the change in senior management resulting in lower step points in pay.

Representation allowance

As per PO(2014)0154 dated 27 March 2013, expenditure on the representation allowance by the qualifying officials totalled €9,922 and is broken out below.

	2017	2016
Rent supplement	3,173	3,173
Hospitality expenses	6,749	8,566
Total	9,922	11,739

3. Buildings and maintenance**Contractual supplies and services**

	2017	2016
Building rent and maintenance	1,789	1,887
Security	607	578
Other costs	369	397
Total	2,766	2,862

Building costs include rent of the Agency's accommodation (€1.789M), utilities and cleaning. Security costs are predominantly those of the contracted out guard service. Other costs include office supplies, the rental of reprographic equipment and the costs for the canteen services that have been outsourced.

During 2015, NETMA moved from its previous accommodation in Unterhaching Munich to Hallbergmoos, North of Munich. For the new accommodation NETMA signed a contract on 27th September 2013 to lease the new office building to 30th November 2024. Although a firm price has been agreed, the contract incorporates a clause whereby a rental increase or reduction can be triggered after the first three years if inflation in Germany varies by more than 5% based on the consumer price index. Utility payments are subject to an annual review and can vary on the basis of actual usage of the previous year (they have not changed in this reporting period). The contract includes an option to extend the lease for a further two periods of 5 years.

In accordance with IPSAS 13 – Leases, the table below details obligations under the Operating Leases as at 31 December 2016: (For the new building, both building and garage costs are combined). For this reconciliation an assumption has been made that the lease will be extended for the later than five years calculation.

	2017	2016
Buildings: (Includes Garage Charges)		
Not later than one year	239	239
Later than one year and not later than five years	3,537	3,537
Later than five years	4,347	4,347
Utilities:		
Not later than one year	272	272
Later than one year and not later than five years	1,089	1,089
Later than five years	1,338	1,338

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4. IT services**Contractual supplies and services**

	2017	2016
Communication	112	165
Information technology support	4,304	4,431
Total	4,415	4,596

The major cost elements in this category are for consultancy and outsourced support costs for the Agency's information systems.

5. Depreciation and amortisation

	2017	2016
Depreciation and amortisation	70	139
Total	70	139

PP&E is depreciated on a straight-line basis over the useful life of the asset. The depreciation charge relates to IT and Communication Equipment assets capitalised by NETMA.

6. Finance costs

	2017	2016
Foreign exchange gain /loss	0	(7)
Other charges	(214)	176
Total	(214)	169

Translation gains and losses occur when assets held in foreign currencies are converted to a Euro value at the closing NATO-promulgated exchange rates for the financial period. Due to the steady nature of the Euro : GBP exchange rate in 2017 only immaterial values of €151 were incurred.

Realised gains and losses occur when currency transactions are paid or received at a different rate to that which the expense or income was accounted when accrued for.

Other charges include VAT expensed during the year and expensed movements in the manual accrual.

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D. Notes to Statement of Cash Flow

1. Surplus / (deficit) from operating activities

	2017	2016
Surplus / (deficit)	(70)	(139)
Total	(70)	(139)

This represents the deficit from normal operating activities before interest, depreciation and financial charges such as exchange differences arising from transactions. The previous year's balance is transferred from Surplus / Deficit into Nation Reserves in PP&E in the following year.

2. Depreciation / amortisation

	2017	2016
Depreciation and amortisation	70	139
Total	70	139

This represents the annual depreciation on PP&E which is calculated on a straight line basis.

3. Increase / (decrease) in payables

	2017	2016
Payables to suppliers	(396)	119
Other payable	(2,082)	5,501
Total	(2,478)	5,620

The movement on payables to suppliers in 2017 represents an decrease in the outstanding liabilities from 2016. The decrease is attributable to a lower estimate for accrued expenditure based on a review of invoices accounted for in early 2018 with 2017 invoice dates. The movement on other payable represents the movement on the lapsed credits due to nations for unexpended budgets.

4. Increase / (decrease) in advances

	2017	2016
Advance contributions	0	(1,592)
Other contributions	(5,261)	(8,111)
Total	(5,261)	(9,703)

Other Contributions represent the movement on Italian Duty Travel and expenditure on relocation from Unterhaching to Halbergmoos. 2017 is expected to be the last year expenditure on relocation occurs and remaining funds will be transferred to the respective nation.

5. Increase / (decrease) in other liabilities

	2017	2016
Operating lease liability	(161)	485
Total	(161)	485

This reflects the movement created by the operating lease liability explained at Note B7.

6. Increase / (decrease) in prepayments

	2017	2016
Prepayments	160	(160)
Total	160	(160)

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Prepayments in 2016 equated to rent paid on the first quarter of 2017 accommodation in Hallbergmoos. This did not happen in 2018 and as such creates a movement in pre-payments shown in the cash flow.

7. Increase / (decrease) in deferred revenue

	2017	2016
Deferred revenue	3,361	6,516
Total	3,361	6,516

Deferred Revenue represents accumulated unearned revenue which is the excess of national contributions and miscellaneous revenue over expenditure on the NETMA program to date.

8. (Increase) / decrease in receivables

	2017	2016
National contributions	(11,016)	(442)
VAT	(247)	78
Other receivables	(29)	2
Total	(11,292)	(362)

The increase in National receivables is explained in Note B2, but relates to national contributions received relative to the annual budget in 2017 and future budgets for 2018 called for in 2017. The increase in VAT receivable relates to monies owed to the Agency from the German VAT office regarding VAT reclaimable spends in 2017. Other receivables relate to monies owed from NETMA Staff members.

E. Notes on Statement of Budget Execution

1. Budget analysis - 2017

	2017	2016
Chapter 1 -2017	38,066	39,446
Total	38,066	39,446

There was an underspend of €2.673M against the budget for 2017 due to lower than budgeted staff costs, lower removals and lower education allowance expenditure than previously anticipated. The return of the lapsed credits will be agreed with nations in 2018.

	2017	2016
Chapter 2 – 2017	3,053	3,226
Total	3,053	3,226

In 2017 for Chapter 2 NETMA spent 14% less than budget due to lower than expected security costs, reduced canteen charges and lower rental charges on new equipment. The return of the lapsed credits will be agreed with nations in 2018.

	2017	2016
Chapter 3 – 2017	4,748	4,930
Total	4,748	4,930

In 2017 for Chapter 3 NETMA spent 22% (€1.067M) less than the approved budget. This was caused by lower than budgeted costs for IT Consultancy and software purchases. Where applicable the return of the lapsed credits will be agreed with nations in 2018.

2. Reconciliation between Statement of Cash Flow and Statement of Budget Execution:

	2017	2016
NET CASH INFLOW FROM OPERATING ACTIVITIES	(15,671)	2,396
- Cash contributions received in year	(34,999)	(48,252)
- Bank interest in year	0	0
- VAT reimbursement from Germany MoD	(723)	(893)
- Other cash revenue in year	(11,645)	404
GROSS CASH OUTFLOW FROM OPERATING ACTIVITIES	(63,038)	(46,345)
- Recoverable VAT paid in year	648	401
- Lapsed credits returned to Nations	12,819	8
- Prepayments to Suppliers	0	160
- Other Movements	(2,934)	2,798
- Other Cash payments in year	10,806	388
PREDICTED BUDGET CASH PAYMENTS	(41,699)	(42,589)
SCHEDULE 5: EXPENSES	(42,369)	(42,085)

3. Reconciliation between Statement of Financial Performance and the Statement of Budget Execution:

	2017	2016
SCHEDULE 2: EXPENSES	43,052	43,865
Add: opening payables and accruals	1,215	1,096
Less: closing payables and accruals	(4,238)	(1,215)
Property, Plant and Equipment adjustments	(70)	(139)
Repayment of UK Advance	0	355
Operating lease liability	(160)	484
CASH PAYMENTS	39,799	44,447
Closing payables and accruals included in/(excluded from) budget	(592)	(1,365)
Less: Lapsed Credits to be returned to Nation	3,419	0
Less: Italian duty travel expenses excluded from budget	(576)	(415)
Less: NETMA relocation costs excluded from budget	0	(387)
PREDICTED BUDGET CASH PAYMENTS	42,049	42,280
SCHEDULE 5: EXPENSES	42,369	42,085

F. Contingent Liabilities / Provisions

NETMA has no contingent liabilities or provisions.

G. Write-Off and Donations

In accordance with the NATO Financial Regulations, where a global statement of write-offs and donations shall be reported in the Annual Financial Statements NETMA can report that 295 items were submitted and approved for write-off through the NETMA Internal Audit section in 2017 in accordance with NETMA delegated authorities. These write offs cover items that are obsolete, damaged beyond economic repair or lost.

