

NATO UNCLASSIFIED

22 September 2020

DOCUMENT
C-M(2020)0033-AS1

**IBAN AUDITOR'S REPORT ON THE AUDIT OF THE 2018 FINANCIAL STATEMENTS
OF NAMMO AND NETMA**

ACTION SHEET

On 21 September 2020, under the silence procedure, the Council noted the RPPB report, agreed its conclusions and recommendations, and agreed to the public disclosure of the report, the IBAN Auditor's Reports and the associated 2018 financial statements, attached to C-M(2020)0033.

(Signed) Jens Stoltenberg
Secretary General

NOTE: This Action Sheet is part of, and shall be attached to C-M(2020)0033

NATO UNCLASSIFIED



NATO UNCLASSIFIED

7 September 2020

DOCUMENT
C-M(2020)0033
Silence Procedure ends:
21 Sep 2020 17:30

**IBAN AUDITOR'S REPORT ON THE AUDIT OF THE 2018 FINANCIAL STATEMENTS
OF NAMMO AND NETMA**

Note by the Secretary General

1. I attach the International Board of Auditors for NATO (IBAN) Auditor's Reports on the 2018 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). The IBAN Auditor's Reports set out unqualified opinions on both the 2018 financial statements and on compliance for NAMMO and NETMA.
2. The IBAN reports have been reviewed by the Resource Policy and Planning Board (RPPB) (see Annex).
3. I do not believe this issue requires further discussion. Therefore, **unless I hear to the contrary by 17:30 hours on Monday, 21 September 2020**, I shall assume the Council noted the RPPB report, agreed its conclusions and recommendations, and agreed to the public disclosure of this report, the IBAN Auditor's Reports and the associated 2018 financial statements.

(Signed) Jens Stoltenberg

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

1 Annex
1 Enclosure

Original: English

NATO UNCLASSIFIED

-1-



**IBAN AUDITOR'S REPORT ON THE 2018 FINANCIAL STATEMENTS OF NAMMO
AND NETMA**

Report by the Resource Policy and Planning Board (RPPB)

References:

- | | | |
|----|-----------------|--|
| A. | IBA-A(2019)0105 | IBAN Auditor's Report on the audit of 2018 financial statements of the NATO Multi-Role Combat Aircraft Development Production and In-Service Support Management Organisation (NAMMO) |
| B. | IBA-A(2019)0099 | IBAN Auditor's Report on the audit of 2018 financial statements of the NATO EF2000 and Tornado Development, Production and Logistics Management Agency (NETMA) |
| C. | C-M(2015)0025 | NATO Financial Regulations (NFR) |
| D. | PO(2015)0052 | Wales Summit tasker on transparency and accountability |

INTRODUCTION

1. This report by the RPPB addresses the IBAN Auditor's Reports on the 2018 financial statement of the 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). The IBAN Auditor's Reports set out unqualified opinions on the financial statements and on compliance of NAMMO and NETMA in 2018 (reference A, B).

AIM

2. This report summarises the IBAN Auditor's Reports to enable the Board to reflect on strategic issues or concerns emanating from the audit of financial statements of NATO entities and to recommend courses of action to Council as applicable, which has the potential to improve transparency, accountability and consistency.

3. The Board acknowledges the observations highlighted in the Auditor's Reports have been discussed and dealt with by the participating Nations represented on the appropriate governing bodies. The RPPB is mandated under Article 15 of the NFRs (reference C) to examine the Auditor's Reports and to provide comments and recommendations as required.

DISCUSSION

4. No new observations and recommendations were issued as a result of the IBAN audit on the 2018 financial statements for NETMA. Three new observations were raised for NAMMO. As of the date of the respective IBAN Auditor's Reports a total of two prior year observations for NETMA were in-progress or open and no prior year observations were closed. No observations impacted the audit opinions in 2018.

5. NETMA manages the NAMMO production and logistics organisation programme and its related budgets. In response to the draft IBAN Auditor's Report, NETMA is provided the opportunity to develop an action plan for NAMMO.

6. Presentation of the budget execution statements. IBAN found that improvements were needed in the presentation of the budget execution statement for the operational budget of NAMMO. The NAMMO operational budget is based on forecasts from industry spanning several years. As per Article 44.2 of the NETMA financial regulations the budget execution statement should show the budget executed during a larger time frame than just the single year shown. Therefore IBAN found that the budget execution statement does not provide information on the legal obligations committed up to and including the 2018 financial year for the provision of goods and services for contracts in future financial years. Furthermore IBAN also found that the unexpended balance of committed credits are not disclosed in the budget execution statement and the notes do not provide supporting explanation of the budget executed in the year.

6.1. NETMA offered no formal comment on this observation within the Auditor's Report. The Board supports IBAN recommendations for NAMMO to disclose unexpended balances of committed credits in the budget execution statement and confirm the legal obligations committed up to the current financial year for the provision of goods and services for contracts in the future financial years.

7. Accounting of receivables. Due to mistakes and weaknesses in the accounting of receivables, IBAN found that the receivables values were understated. An increase in the receivables value is recognised when the call for contribution has been issued. For NAMMO a mistake was made leading to an understatement of EUR 2.45m. To improve the methodology of accruals and in respect of contributions, IBAN recommends that NAMMO should take into account the year-end adjustments and cash contributions received in the following year but related to the operational budget of the current year.

7.1. NETMA offered no formal comment on this observation within the Auditor's Report. To reduce the likelihood of these errors occurring again, the Board supports IBAN recommendations to develop controls and reconcile the revenues and receivables in line with the annual confirmation of contributions from Nations.

8. Prior year observations. In 2017 IBAN observed insufficient segregation of duties and independence for the Head of Internal Audit of NETMA. In response NETMA undertook some changes to the reporting line of the head of internal audit to demonstrate independence from the business. As part of the audit of the 2019 financial statements IBAN will review how organisational independence of the NETMA internal audit function has been operating in practice.

8.1. NETMA has not shown progression in respect of the prior year observation relating to implementing internal controls over financial reporting. The Board understands that staff turnover has contributed to errors in the financial statements but to mitigate associated risks, IBAN, supported by the Board, encourages cross reviews, analyses and comparison with prior years and undertaking an active review of financial statements.

CONCLUSIONS

9. No observations impacted the audit opinions for NAMMO and NETMA in 2018. Three new observations were raised for NAMMO. As of the date of the respective IBAN Auditor's Reports a total of two prior year observations for NETMA were in-progress or open and no prior year observations were closed.

10. The budget execution statement for NAMMO did not include the full value of legal obligations committed for future years. The Board supports the IBAN recommendation for NAMMO to disclose further information in the note to the budget execution statement on legal obligations committed up to and including the current financial year for the provision of goods and services for contracts in the future financial years.

11. NAMMO understated their receivables value due to not recognising the call for contributions in the correct year. To mitigate the likelihood of this issue occurring again the Board supports the IBAN recommendation for NETMA to develop controls and reconciliation of the revenues and receivables in line with the annual confirmation of contributions from Nations.

12. In respect of prior year observations, the Board notes the progress made by NETMA and welcomes IBAN findings for 2019 to verify if the Head of Internal Audit is adequately segregated from the business to offer sufficient independent advice to the organisation. The Board understands that the high rate of staff turnover in NETMA has contributed to the IBAN observation in relation to errors on the financial statements and to partly mitigate the associated risks would encourage cross reviews and comparison and analysis with prior year financial statements.

RECOMMENDATIONS

13. The Resource Policy and Planning Board recommends that the Council:

13.1. note this report and the IBAN Auditor's Reports at references A and B;

13.2. agree the conclusions at paragraphs 9 to 12; and

13.3. agree to the public disclosure of the 2018 financial statements for NAMMO and NETMA, their associated IBAN Auditor's Reports and this report in line with agreed policy at Reference D.



NORTH ATLANTIC TREATY ORGANIZATION
ORGANISATION DU TRAITÉ DE L'ATLANTIQUE NORD

INTERNATIONAL BOARD OF AUDITORS FOR NATO
COLLÈGE INTERNATIONAL DES AUDITEURS EXTERNES DE L'OTAN

NATO UNCLASSIFIED



IBA-A(2019)0105
28 August 2019

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

Cc: Chairman NAMMO Board of Directors
General Manager, NETMA
Division Leader, Finance Division, NETMA
Chairman, Resource Policy & Planning Board
Branch Head, Secretariat and Finance Branch, NATO Office of Resources
Private Office Registry

Subject: ***International Board of Auditors for NATO (IBAN) 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) Restated Financial Statements for the year ended 31 December 2018 – IBA-AR(2019)0013***

IBAN herewith submits its approved Auditor's Report (Annex 2) and a Letter of Observations and Recommendations (Annex 3) with a Summary Note for distribution to the NATO Council (Annex 1).

IBAN's report sets out an unqualified opinion on the Restated Financial Statements of the NAMMO and on compliance for the financial year 2018.

Yours sincerely,

Dr. Hans Leijdens
Chairman

Attachments: As stated above.



**Summary Note for Council
by the International Board of Auditors for NATO (IBAN)
on the audit of the Restated Financial Statements of the
NATO Multi-Role Combat Aircraft Development Production
and In-Service Support Management Organisation (NAMMO)
for the year ended 31 December 2018**

NAMMO is a NATO Production and Logistic Organisation. 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.

IBAN audited the NAMMO Restated Financial Statements for the year ended 31 December 2018. Expenditure from the operational budget amounted to EUR 413 million.

IBAN issued an unqualified opinion on the NAMMO Restated Financial Statements and on compliance for the year ended 31 December 2018. There are three current year observations. These observations do not impact the audit opinion.

1. Improvements needed in the presentation of the Statement of Budget execution for the Operational budget.
2. Weaknesses and errors in the accounting of NAMMO receivables.
3. Improvements needed in the determination of NAMMO accrued expenses.

IBAN also noted that there was 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 replied that they had no comments.

NATO UNCLASSIFIED

ANNEX 2
IBA-AR(2019)0013

28 August 2019

INTERNATIONAL BOARD OF AUDITORS FOR NATO

**AUDITOR'S REPORT ON THE RESTATED FINANCIAL STATEMENTS OF
THE NATO MULTI-ROLE COMBAT AIRCRAFT DEVELOPMENT PRODUCTION
AND IN-SERVICE SUPPORT MANAGEMENT ORGANISATION**

(NAMMO)

FOR THE YEAR ENDED 31 DECEMBER 2018

NATO UNCLASSIFIED

**INDEPENDENT AUDITOR'S REPORT
TO THE NORTH ATLANTIC COUNCIL**

Report on the Audit of the Financial Statements

Opinion on the Financial Statements

The International Board of Auditors for NATO (IBAN) has audited the Restated Financial Statements of NAMMO for the 12 month period ended 31 December 2018, issued and submitted to IBAN on 31 March 2019. These Restated Financial Statements comprise the Statement of Financial Position as at 31 December 2018, the Statement of Financial Performance, the Statement of Changes in Net Assets/Equity and the Statement of Cash Flow, for the 12 month period ended 31 December 2018, including a summary of significant accounting policies and other explanatory notes. In addition, the Financial Statements include a budget execution report for the 12 month period ended 31 December 2018.

In our opinion, the Restated Financial Statements give a true and fair view of the financial position of NAMMO as at 31 December 2018, and of its financial performance, its cash flows and budget execution for the 12 month period ended 31 December 2018, in accordance with accounting requirements and reporting standards consistent with the NATO Accounting Framework.

Basis for Opinion on the Financial Statements

In accordance with the NATO Financial Regulations (NFRs), external audit of the NATO bodies pursuant to the North Atlantic Treaty shall be performed by IBAN.

We have conducted our audit in accordance with the International Standards of Supreme Audit Institutions (ISSAIs 1000-1810) developed by the International Organisation of Supreme Audit Institutions (INTOSAI) and in accordance with the additional terms of reference defined in our Charter.

We are independent in accordance with the INTOSAI Code of Ethics and we have fulfilled our other ethical responsibilities in accordance with these requirements. The responsibilities of the members of IBAN are more extensively described in the section «Auditor's Responsibilities for the Audit of the Financial Statements» and in our Charter. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Management's Responsibility for the Financial Statements

Management's responsibility for the financial statements is laid down in the NFRs. The Restated Financial Statements of NAMMO are drawn up in accordance with accounting requirements and reporting standards consistent with the NATO Accounting Framework as approved by the Council. The Financial Controller is responsible for submitting the Financial Statements for audit to IBAN not later than 31st March following the end of the financial year.

The Financial Statements are signed by the Head of the NATO body and the Financial Controller. In signing the Financial Statements, the Head of NATO body and the Financial Control confirm the establishment and maintenance of financial governance, resource management practices, internal controls and financial information systems to achieve the efficient and effective use of resources.

This confirmation covers the design, implementation and maintenance of internal controls relevant to the preparation and presentation of financial statements that are auditable and free from material misstatement, whether due to fraud or error. This also covers reporting on the entity's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless there are plans to liquidate the entity or to cease its operations, or there is no realistic alternative but to do so.

Auditor's Responsibilities for the Audit of the Financial Statements

The objectives of the audit are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes an opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISSAIs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with ISSAIs, we exercise professional judgement and maintain professional scepticism throughout the planning and performance of the audit. This involves taking into account Considerations Specific to Public Sector Entities. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and

appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit 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 the entity's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of the use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the entity's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the entity to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We are required to communicate with the bodies charged with governance, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

Our Independent External Auditor's Report is prepared to assist North Atlantic Council in carrying out its role. We are therefore responsible solely to the North Atlantic Council for our work and the opinion we have formed.

Report on Compliance

Opinion on Compliance

Based on the procedures we performed, nothing has come to our attention, as part of our audit of the Financial Statements that causes us to believe that funds have not been properly used for the settlement of authorised expenditure or are not in compliance with the NATO Financial Regulations and the NATO Civilian Personnel Regulations.

Basis for Opinion on Compliance

We have conducted our compliance audit in accordance with the International Standards of Supreme Audit Institutions (ISSAI 4000) developed by the International Organisation of Supreme Audit Institutions (INTOSAI) and in accordance with the additional terms of reference defined in our Charter.

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

Management's Responsibility for Compliance

All NATO staff, military and civilian, are obligated to comply with the NATO Financial Regulations, associated Financial Rules and Procedures and internal implementing directives. These include the NATO Civilian Personnel Regulations.

The General Manager of NETMA is responsible and accountable for sound financial management. The financial administration of NATO bodies must incorporate the principles of propriety, sound governance, accountability, transparency, risk management and internal control, internal audit, external audit, and fraud prevention and detection.

Auditor's Responsibilities for Compliance

In addition to the responsibility to provide reasonable assurance about whether the financial statements as a whole are free from material misstatement, the IBAN Charter requires IBAN to provide independent assurance and report annually to the North Atlantic Council about whether funds have been properly used for the settlement of authorised expenditure (propriety) and are in compliance with the regulations in force (regularity). Propriety relates to the observance of the general principles governing sound financial management and the conduct of public officials. Regularity concerns the adherence to formal criteria such as relevant regulations, rules and procedures.

This responsibility includes performing procedures to obtain independent assurance about whether funds have been properly used for the settlement of authorized expenditure and whether they have been used in compliance with the regulations in force. Such procedures include consideration of the risks of material non-compliance.

Brussels, 28 August 2019

A handwritten signature in blue ink, appearing to read 'Hans Leijtens', is written over a faint, light blue rectangular background.

Dr. Hans Leijtens
Chairman

NATO UNCLASSIFIED

ANNEX 3
IBA-AR(2019)0013

28 August 2019

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)

NATO UNCLASSIFIED

Introduction

The International Board of Auditors for NATO (IBAN) audited the NAMMO Restated Financial Statements for the year ended 31 December 2018, and issued an unqualified opinion on the financial statements and on compliance.

Observations and Recommendations

During the audit, IBAN made three observations, which do not impact the audit opinion:

1. Improvements needed in the presentation of the Statement of Budget Execution for the Operational budget.
2. Weaknesses and errors in the accounting of NAMMO receivables.
3. Improvements needed in the determination of NAMMO accrued expenses.

There were no observations from previous years' audits to follow up on.

IBAN also issued a Management Letter (reference IBA-AML(2019)0009) to the NETMA General Manager with observations for management's attention.

OBSERVATIONS, CONCLUSIONS AND RECOMMENDATIONS**1. IMPROVEMENTS NEEDED IN THE PRESENTATION OF THE STATEMENT OF BUDGET EXECUTION FOR THE OPERATIONAL BUDGET****Reasoning**

1.1 The objective of financial reporting by public sector entities is to provide information about the entity that is useful to users for accountability purposes and for decision-making purposes.

1.2 As per International Public Sector Accounting Standards (IPSAS) 1, the objective of general purpose financial statements is also to provide information to meet the needs of those users of financial statements who are not in a position to demand reporting adapted to their needs. NAMMO financial statements are made publicly available and therefore need to meet the needs of these external users.

1.3 As per NETMA financial regulations, the annual financial statements of NAMMO shall include a budget execution report. In addition, as stated in article 44.2 of the NETMA financial regulations, the financial controller must provide to Nations *“a statement presented on a cash basis, which shows the position at the end of the financial year of these items¹ : (a) the total budget credits, (b) credits carry forward (...), (c) commitments undertaken, payments made and balance of credits available, (d) contributions requested of Nations, together with the contributions received and the resultant balances (...).”*

1.4 A statement of budget execution shall present a clear comparison of the budget authorised, budget amendments, funds committed, actual expenditures and lapses. IPSAS 24 states that *“the comparison of budget and actual amounts shall present separately: (a) The original and final budget amounts; (b) The actual amounts on a comparable basis (...). In addition, budgets may focus on, or include information about, commitments to expend funds in the future and changes in those commitments”*.

Observation

1.5 The Statement of Budget Execution is prepared on a cash basis for the Tornado Operational budget according to NETMA financial regulations. IBAN found that important information is missing in order to understand how the operational budget has been executed during the year.

¹ These items are listed in Articles 43.1.1 to 43.1.9.

1.6 As NAMMO is a programme with multi-year contracts that create a legal obligation for the entire duration of the contract, the operational budget is based on forecasts of planned expenditures provided by industries for several years. Therefore, the information disclosed in the Statement of Budget Execution should be in line with these multi-year requirements and show the budget executed during a larger time frame than just the single year shown. In the current presentation of the budget execution, only information about the budget ceiling approved for the year, expenditure, open commitments and unused budget are provided.

1.7 According to NETMA Financial Regulations, the uncommitted balance of credits will be cancelled at the end of each financial year, but the unexpended balance of committed credits may be carried forward if a legal liability to pay exists or if the carry-forward is specifically approved by the finance and administration committee. The Statements of Budget Execution for NAMMO did not disclosed information about these unexpended balances of committed credit.

1.8 IBAN has also noted that the word “expenses” has been used in the Statement of Budget Execution instead of “expenditure”, which is more appropriate. The word “expenses” refers to the cost of goods and services delivered, while the word “expenditure” relates to “payments or disbursements”. It is therefore incorrect to use the word “expenses” in the Statements of budget execution, as these amounts in fact relate to payments or disbursements and should therefore be called “expenditure”.

1.9 In addition, the comments and figures disclosed in the Notes on the Statement of Budget Execution are more focused on comparative figures with the previous budget and do not provide supporting explanations regarding the budget executed in the year.

Recommendations

1.10 In order to facilitate the understanding of the readers and users of financial statements, IBAN recommends to:

- Improve the presentation of Statement of Budget Execution for NAMMO financial statements to ensure that the information is in line with the needs of the users on the operational budget.
- Implement documented controls on information produced for the Statements of Budget Execution.

2. WEAKNESSES AND ERRORS IN THE ACCOUNTING OF NAMMO RECEIVABLES

Reasoning

2.1 According to IPSAS 1, the financial statements shall present fairly the financial position, financial performance, and cash flows of an entity. Fair presentation requires the faithful representation of the effects of transactions, other events, and conditions in accordance with the definitions and recognition criteria for assets, liabilities, and revenues set out in IPSAS. NAMMO financial statements are prepared in accordance with the NATO Accounting Framework on an accrual basis and transactions and events are recorded and recognised in the financial statements of the periods to which they relate.

2.2 At year end, each entity recognised as revenues contributions from member nations to fund annual operational budgets. As per NETMA financial regulations, contributions receivable are recognised when a call for contribution has been issued to the member nations.

Observation

2.3 We found that an adjustment of one nation's call for contributions for the year 2017 was booked wrongly in the financial statements for the year 2018. The NAMMO receivables for the year 2017 is therefore understated by EUR 2.45 million.

Recommendations

2.4 In order to ensure the completeness of contributions presented in the annual financial statements, IBAN recommends that NETMA improves the methodology of accruals for contributions by:

- Taking into account the year end adjustment and cash contributions received in the following year but related to the operational budget of the current year.
- Developing controls and reconciliation of the revenues and receivables with annual confirmations of contributions received from Nations.

3. IMPROVEMENTS NEEDED IN THE DETERMINATION OF NAMMO ACCRUED EXPENSES

Reasoning

3.1 According to IPSAS 1, the financial statements shall present fairly the financial position, financial performance, and cash flows of an entity. Fair presentation requires the faithful representation of the effects of transactions, other events, and conditions in accordance with the definitions and recognition criteria for assets, liabilities, revenue, and expenses set out in IPSAS. NAMMO's financial statements are prepared in accordance with the NATO Accounting Framework on an accrual basis and transactions and events are recorded and recognized in the financial statements of the periods to which they relate. At year end, each entity estimates the value of goods and services rendered during the year but not yet invoiced.

Observation

3.2 NAMMO's accrual for goods and services as at 31 December 2018 is EUR 29.6 million (EUR 15.3 million related to spares purchased from industry and EUR 14.3 million related to services rendered from suppliers). The accrued amount is posted manually into the accounting system and has been assessed by analysing invoices in the PARMIS accounting system dated in 2018 or earlier and paid until mid-February 2019 (NAMMO cut-off date).

3.3 Since PARMIS does not provide information related to delivery dates, the following manual analyses were performed to capture invoices of goods and services rendered during the year :

- For spares purchased from industry: analysis of the Central Automatic Data Processing System (CADPS) report, which includes all invoices paid in January to mid-February 2019 with a 2018 delivery date.
- For services rendered from suppliers: analysis of material hard copy invoices received until mid-February 2019, from which the achievement dates are checked manually in AIMS (Tornado project management system).

3.4 The process is mainly manual, time consuming and relies on the knowledge of staff in a context of a high turnover.

3.5 Moreover, the current NAMMO accrual estimate methodology does not take into account the goods and services rendered but not yet invoiced.

3.6 IBAN found that the above mentioned CADPS report for the period between mid-February and mid-June 2019 shows that EUR 5.5 million (VAT included) of goods were delivered in 2018 and paid in 2019 but not accrued as at 31 December 2018. This demonstrates the limit of the CADPS accrual estimate exercise since the report extracted mid-February 2019 for the accrual estimate purpose does not fully capture all goods delivered in 2018 but not yet invoiced.

3.7 More generally, IBAN found that the AIMS report does not provide sufficiently reliable and complete information on the services rendered milestone achievement dates. Consequently, the accrual estimate exercise can only be performed on the basis of hard copy invoices received until mid-February 2019, and therefore cannot capture all the services rendered during the year but not yet invoiced. The current NAMMO accrual estimate methodology therefore does not take into accounts the goods and services rendered but not yet invoiced.

3.8 It is important to ensure a fair presentation of accruals, taking into account the most reliable information available related to goods and services rendered during the year but not yet invoiced.

Recommendations

3.9 In order to ensure a fair presentation of accruals in a context of a high staff turnover, taking into account the most reliable and complete information available, IBAN recommends NETMA for NAMMO to :

- Improve the IT systems (CADPS and AIMS) in order to obtain or develop reliable reports, which fully capture all goods and services rendered during the year but not yet invoiced.
- Determine accrued expenses based on these reports, which fully capture all goods and services rendered during the year but not yet invoiced.

NAMMO ANNUAL FINANCIAL STATEMENTS

PERIOD ENDED 31 DECEMBER 2018



NETMA

NATO EF2000 AND TORNADO DEVELOPMENT, PRODUCTION
AND LOGISTICS MANAGEMENT AGENCY

Contents



INTRODUCTION	3
STATEMENT OF INTERNAL CONTROL	5
<i>FINANCIAL STATEMENTS</i>	
- STATEMENT OF FINANCIAL POSITION	7
- STATEMENT OF FINANCIAL PERFORMANCE	8
- STATEMENT OF CASH FLOW	9
- STATEMENT OF CHANGES IN NET ASSETS/EQUITY	10
- STATEMENT OF BUDGET EXECUTION	11
SIGNIFICANT ACCOUNTING POLICIES	13
NOTES TO STATEMENT OF FINANCIAL POSITION	18
NOTES TO STATEMENT OF FINANCIAL PERFORMANCE	20
NOTES TO STATEMENT OF CASH FLOW	21
NOTES TO STATEMENT OF BUDGET EXECUTION	22
CONTINGENT LIABILITIES / PROVISIONS	23
RELATED PARTY DISCLOSURE	23
WRITE OFF AND DONATIONS	23

These statements are produced in Thousands of Euros. For example 34,632 = Thirty Four Million Six Hundred and Thirty Two Thousand Euros; 132 = One Hundred and Thirty Two Thousand Euros

Introduction to the 2018 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 continued to be deployed in coalition operations against Daesh in Iraq and Syria and was involved in a number of national and joint exercises in 2018.

Key points from the Annual Financial Statements

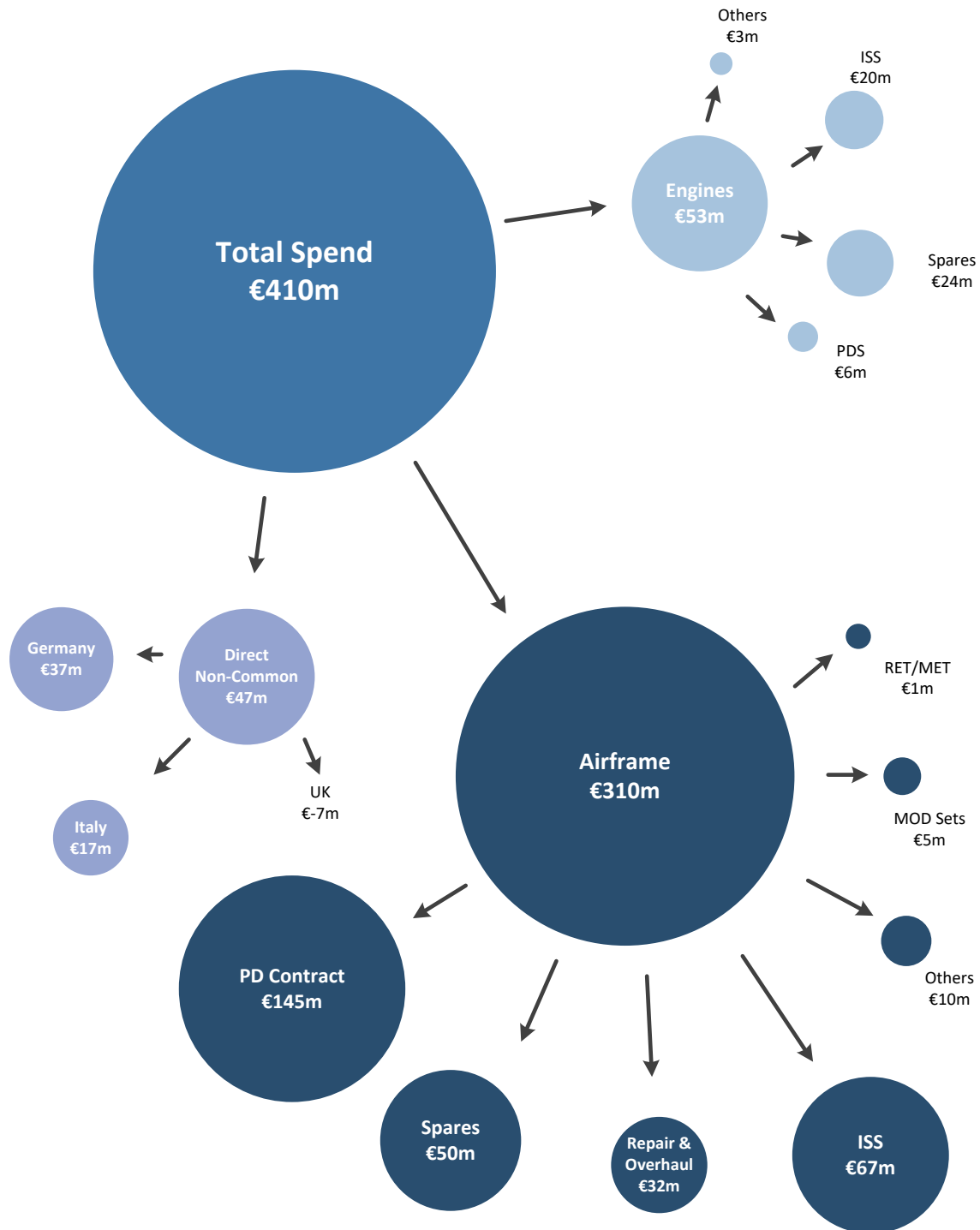
In 2018 the three Nations have continued to work together to support Tornado as the UK nears the withdrawal of its Tornado fleet from service in March 2019.

Agreement between the Nations that the UK will remain within the partnership has been finalised and has meant that the programme has continued to move forward with no adverse effects.

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 2018

The total spend on the Tornado programme through NETMA in 2018 was €410m, a €14m increase from 2017. Spend on Tornado is dominated by the airframe totalling 75% of costs, with 13% 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 an 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 process 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 2018.

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 2018.

MR GABRIELE SALVESTRONI
General Manager

MR MARK GANFIELD
Financial Controller

PAGE INTENTIONALLY BLANK

STATEMENT OF FINANCIAL POSITION

AS AT 31 DECEMBER 2018

(in thousands of Euros)

	Notes	2018	2017
Assets			
Current assets			
Cash and cash equivalents	B1	192,277	159,005
Short term investments		0	0
Receivables		217	2,058
Prepayments		0	0
Inventories		0	0
		<u>192,494</u>	<u>161,063</u>
Non-current assets			
Property, plant & equipment		0	0
Intangible assets		0	0
		<u>0</u>	<u>0</u>
Total assets		<u>192,494</u>	<u>161,063</u>
Liabilities			
Current liabilities			
Payables	B2	37,028	33,239
Deferred revenue		0	0
Advances	B3	155,466	127,824
		<u>192,494</u>	<u>161,063</u>
Non-current liabilities			
Provisions		0	0
		<u>0</u>	<u>0</u>
Total liabilities		<u>192,494</u>	<u>161,063</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 2019.



MR GABRIELE SALVESTRONI
General Manager



MR MARK GANFIELD
Financial Controller

STATEMENT OF FINANCIAL PERFORMANCE

FOR THE YEAR ENDED 31 DECEMBER 2018

(in thousands of Euros)

	Notes	2018	2017
Revenue			
Revenue	C1	413,195	397,136
Financial revenue		0	0
Other revenue		0	0
Total revenue		413,195	397,136
Expenses			
Personnel		0	0
Contractual supplies and services	C2	(412,800)	(396,436)
Depreciation and amortisation		0	0
Impairment		0	0
Provisions		0	0
Other expenses		0	0
Finance costs	C3	(395)	(700)
Total expenses		(413,195)	(397,136)
Surplus/(deficit) for the period		0	0

STATEMENT OF CASH FLOW

FOR THE YEAR ENDED 31 DECEMBER 2018

(in thousands of Euros)

	Notes	2018	2017
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	3,789	5,468
Increase/ (decrease) in advances	D3	27,642	(37,878)
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	1,841	(2,027)
Net cash flow from operating activities		33,272	(34,437)
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		33,272	(34,437)
Cash and cash equivalents at the beginning of the period		159,005	193,442
Cash and cash equivalents at the end of the period		192,277	159,005

STATEMENT OF CHANGE IN NET ASSETS/EQUITY

FOR THE YEAR ENDED 31 DECEMBER 2018

(in thousands of Euros)

	PP&E Asset Reserve	Revaluation Reserves	Accumulated surplus/deficit	Total
Balance at the beginning of the period 2017	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 2017	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 2018	0	0	0	0

NATO UNCLASSIFIED

STATEMENT OF BUDGET EXECUTION

FOR THE YEAR ENDED 31 DECEMBER 2018

(in thousands of Euros)

Budget 2018

		Initial budget	Transfers	Bud Adj 1	Bud Adj 2	Bud Adj 2	Final budget	Commitments	Expenses	Unused Budget
All nations	E1	459,132	0	23,916	0	0	483,048	382,294	410,255	72,793
Total FY 2018		459,132	0	23,916	0	0	483,048	382,294	410,255	72,793

PAGE INTENTIONALLY BLANK

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 2018 financial statements, the accounting policies have been applied consistently throughout the reporting period. There have been no changes to NAMMO accounting policy in 2018.

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 NAMMO Financial Statements 2018: 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 NEFMO Financial Statements. IPSAS 39 (Employer benefits) became effective January 1st 2018 and will replace IPSAS 25. IPSAS 40 (Public Sector Combinations) will become effective January 1st 2019.

Restatements

NAMMO has not restated any balances in the 2017 financial statements.

After the 2018 Annual Financial Statement audit review, NAMMO has restated the total Commitments reported at 31st December 2018 in the Statement of Budget Execution.

Changes in financial rules and regulations

During 2015 NATO adopted new financial rules and regulations. During 2018 there were no additional changes. These financial statements have been produced in line with these financial rules and regulations. NETMA intends to conduct a review of these financial rules and regulations during 2019.

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 2018, resulting realised and unrealised gains and losses are recognised in the Statement of Financial Performance.

NAMMO used the following exchange rates as at 31st Dec 2018:

EUR – GBP = 1: 0.9034

EUR – USD = 1: 1.1538

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 PANAVIA an assessment has been made on information available. The asset base of PANAVIA 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 2018 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.

Disclosure of Assets purchased prior to 2013 and still in use:

<i>Asset Type</i>	<i>Number of Locations Held</i>	<i>Number of Assets</i>
Avionic Equipment	2	31
Outdoor Test Facility	1	1
Mechanical System Test Facility	1	1

NATO UNCLASSIFIED

These assets are held at a total of 3 different locations across 2 countries affiliated to the Tornado Programme. The future values are likely to change due to potential disposal action in place.

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 2018 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.

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 for 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 2018, 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 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

	2018	2017
Cash accounts	0	0
Clearing cash accounts	0	0
Petty cash and advances	0	0
Current bank accounts	192,277	159,005
Receivables	217	2,058
Clearing-bank accounts	0	0
Total	192,494	161,063

Current bank accounts

The Tornado Programme 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 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 has increased in 2018 due to Nations transferring more money into the agency.

Receivables show the value of the credit notes sent into the agency restated as receivables previously included within payables.

2. Payables

	2018	2017
Payables to suppliers	31,184	27,584
Payables to non-consolidated entities	0	0
Payables to staff members	0	0
Payables to governments	0	0
Other payables	5,844	5,656
Total	37,028	33,239

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 2018 is €1.5M compared with the 2017 amount of €0.9M.

A manual accrual has been assessed by analysing PARMIS invoices paid in January and the first 2 weeks of February 2019 with 2018 (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 2018 is €29.631M compared with the 2017 accrual of €26.7M.

Other payables

NATO UNCLASSIFIED

Other payables include bank interest payable to National Treasuries (€0.767M) and income generated from levies (€5.077M). Income generated from levies has increased by €0.188M since 2017.

3. Advances

	2018	2017
Other advances	155,466	127,824
Total	155,466	127,824

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:

	2018	2017
Unearned revenue b/f	127,824	165,702
National contributions	444,247	359,258
Miscellaneous revenue (excl bank interest)	9,922	19,174
Bank interest	15	2
<i>Less:</i>		
Operational expenditure	420,034	407,462
Other operational revenue	6,097	8,148
Bank interest returned to nations	8	1
<i>Add:</i>		
Miscellaneous financial income / (charges)	(1)	(1)
Foreign exchange gains / (losses)	(400)	(700)
Unearned revenue c/f	155,466	127,824

C. Notes to Statement of Financial Performance

1. Revenue

	2018	2017
National contributions	444,247	359,258
National contributions to be called for	0	0
Other reimbursements	(31,052)	37,878
Total	413,195	397,136

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 and a transfer of funds back to the UK treasury in 2018. 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

	2018	2017
Operating expenses	(412,800)	(396,436)
PP&E movement	0	0
Total	(412,800)	(396,436)

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

	2018	2017
Foreign exchange gain / (loss)	(400)	(700)
Other financial income / (charges)	5	0
Total	(395)	(700)

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 programme. Where income has not been refunded to National Treasuries the remaining balance is treated as unearned revenue.

D. Notes to Statement of Cash Flow

1. Surplus / (Deficit) from operating activities

	2018	2017
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

	2018	2017
Payables to suppliers	3,601	4,657
Other payables	188	811
Total	3,789	5,468

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

Other payables include bank interest and levies generated from defence programmes.

3. Increase / (decrease) in advances

	2018	2017
Advance contributions	0	0
Unearned revenue	27,642	(37,878)
Total	27,642	(37,878)

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

	2018	2017
National contributions	0	0
Other receivables	1,841	(2,027)
Total	1,841	(2,027)

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 2018.

E. Notes to Statement of Budget Execution

1. Budget analysis - 2018

	2018	2017
All nations initial approved budget	459,132	431,449
In year budget adjustments	23,916	19,200
Total	483,048	450,649

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. During 2018 one Nation chose to uplift their budget from the original values by €23,916M to reflect additional Air Force Operational requirements.

NETMA does not formally lapse budget called for but unspent in the following year. The excess of funds is viewed as an "unused budget", this is then taken into consideration the following year when Calls for Funds are issued to nations to cover expenditure.

Previously within the budget execution table NETMA has shown commitments being the same as expenditure. For true transparency this has been removed for 2018 as it could create a misleading picture to the reader where a number of commitments span a larger time frame than just the single year shown in the Budget Execution Statement.

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

	2018	2017
NET CASH INFLOW FROM OPERATING ACTIVITIES	33,272	(34,437)
- Cash contributions received in year	(444,247)	(359,258)
- Bank interest in year	(15)	(2)
- Other reimbursements	(9,721)	(22,643)
GROSS CASH OUTFLOW FROM OPERATING ACTIVITIES	(420,712)	(416,339)
- Bank interest returned to Italy in year	8	7
- Other disbursements	6,314	20,432
EXPENSES PRE EXCHANGE RATE VARIATIONS	(414,389)	(395,900)
- Foreign exchange gains and losses	33	(77)
- Operational budget vs actual exchange gains and losses	4,460	(9,832)
PREDICTED BUDGET CASH PAYMENTS	(409,896)	(405,809)
SCHEDULE 5: EXPENSES	(410,255)	(395,743)

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 2018. 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

	2018	2017
SCHEDULE 2: OPERATING EXPENSES	413,195	397,136
Add: opening payables and accruals	27,584	22,926
Less: closing payables and accruals	(31,184)	(27,584)
Exchange rate difference (OB v corporate)	(4,460)	9,832
Foreign exchange gains and losses	(33)	77
PREDICTED BUDGET CASH PAYMENTS	405,102	402,386
SCHEDULE 5: EXPENSES	410,255	395,743

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 2018. 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. 1.26% (€5.15M) and results from timing differences in payments.

F. Contingent Liabilities / Provisions

NAMMO has no contingent liabilities or provisions.

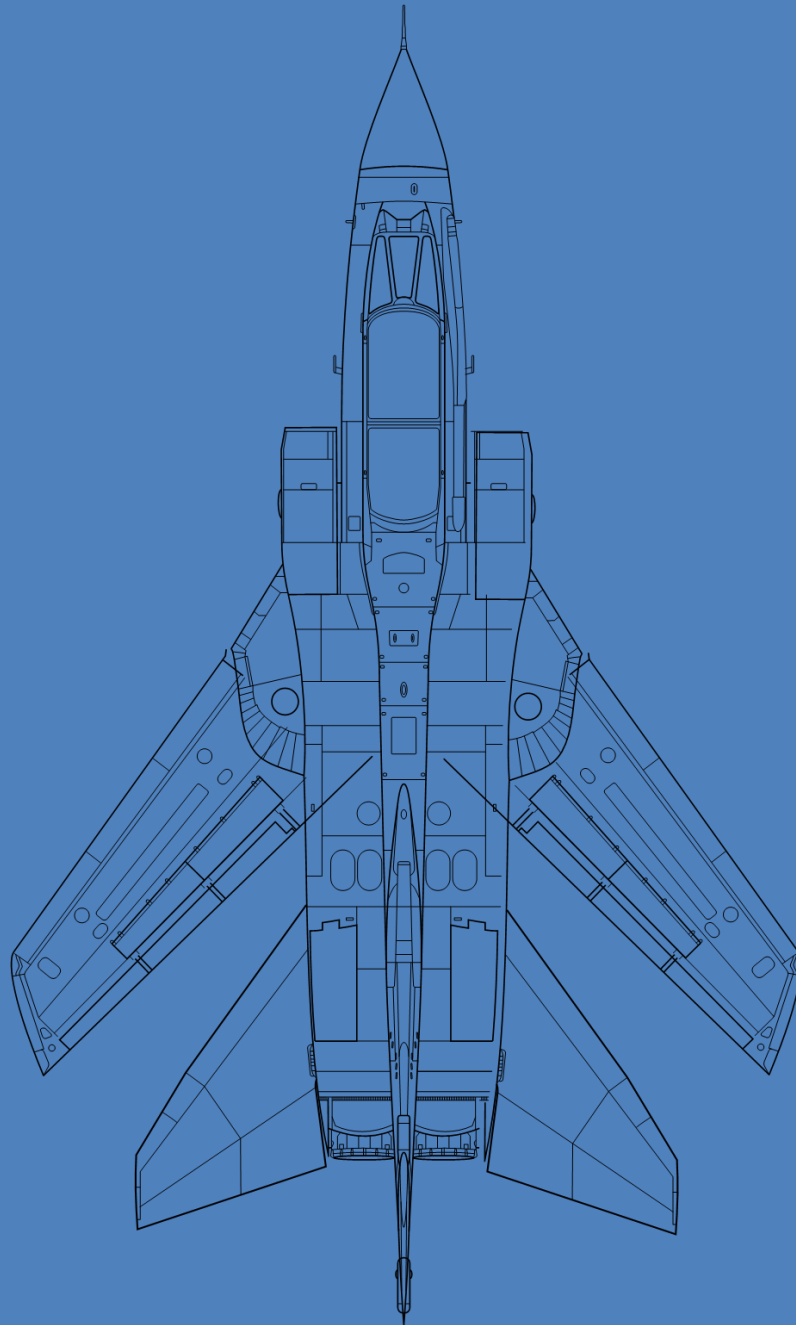
G. Related Parties Disclosure

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 2,032 items were submitted and approved for write off through the NETMA Internal Audit section in 2018 in accordance with NETMA delegated authorities. These write-offs cover items that are obsolete, damaged beyond economic repair or lost.

NATO UNCLASSIFIED



NATO UNCLASSIFIED



NORTH ATLANTIC TREATY ORGANIZATION
ORGANISATION DU TRAITÉ DE L'ATLANTIQUE NORD

INTERNATIONAL BOARD OF AUDITORS FOR NATO
COLLÈGE INTERNATIONAL DES AUDITEURS EXTERNES DE L'OTAN

NATO UNCLASSIFIED



IBA-A(2019)0099
28 August 2019

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

Cc: Chairman NEFMO Board of Directors
Chairman NAMMO Board of Directors
General Manager, NETMA
Division Leader, Finance Division, NETMA
Chairman, Resource Policy & Planning Board
Branch Head, Secretariat and Finance Branch, NATO Office of Resources
Private Office Registry

Subject: ***International Board of Auditors for NATO (IBAN) Auditor's Report and Letter of Observations and Recommendations on the audit of the NATO EF2000 and Tornado Development, Production and Logistics Management Agency (NETMA) Financial Statements for the year ended 31 December 2018 – IBA-AR(2019)0012***

IBAN herewith submits its approved Auditor's Report (Annex 2) and a Letter of Observations and Recommendations (Annex 3) with a Summary Note for distribution to the NATO Council (Annex 1).

IBAN's report sets out an unqualified opinion on the Financial Statements of the NETMA and on compliance for the financial year 2018.

Yours sincerely,

Dr. Hans Leijtens
Chairman

Attachments: As stated above.



**Summary Note for Council
by the International Board of Auditors for NATO (IBAN)
on the audit of the Financial Statements of the
NATO EF2000 and Tornado Development,
Production and Logistics Management Agency (NETMA)
for the year ended 31 December 2018**

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

IBAN audited the Financial Statements of the Administrative Budget of NETMA for the year ended 31 December 2018. The total expenditure in 2018 for the Administrative Budget amounted to EUR 44 million.

IBAN issued an unqualified opinion on the NETMA Financial Statements and on compliance for the year ended 31 December 2018.

During the audit, IBAN made no observations.

IBAN also followed up on the status of the observations from the previous year's audit and noted that one recommendation remained opened and one recommendation was in-progress.

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 IBAN's position on those comments where necessary, see Appendix to Annex 3.

NATO UNCLASSIFIED

ANNEX 2
IBA-AR(2019)0012

28 August 2019

INTERNATIONAL BOARD OF AUDITORS FOR NATO

AUDITOR'S REPORT ON THE FINANCIAL STATEMENTS OF

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

(NETMA)

FOR THE YEAR ENDED 31 DECEMBER 2018

NATO UNCLASSIFIED

**INDEPENDENT AUDITOR'S REPORT
TO THE NORTH ATLANTIC COUNCIL**

Report on the Audit of the Financial Statements

Unqualified Opinion on the Financial Statements

The International Board of Auditors for NATO (IBAN) has audited the Financial Statements of NETMA for the 12 month period ended 31 December 2018, issued and submitted to IBAN on 31 March 2019. These Financial Statements comprise the Statement of Financial Position as at 31 December 2018, the Statement of Financial Performance, the Statement of Changes in Net Assets/Equity and the Statement of Cash Flow, for the 12 month period ended 31 December 2018, including a summary of significant accounting policies and other explanatory notes. In addition, the Financial Statements include a budget execution report for the 12 month period ended 31 December 2018.

In our opinion, the Financial Statements give a true and fair view of the financial position of NETMA as at 31 December 2018, and of its financial performance, its cash flows and budget execution for the 12 month period ended 31 December 2018, in accordance with accounting requirements and reporting standards consistent with the NATO Accounting Framework.

Basis for Opinion on the Financial Statements

In accordance with the NATO Financial Regulations (NFRs), external audit of the NATO bodies pursuant to the North Atlantic Treaty shall be performed by IBAN.

We have conducted our audit in accordance with the International Standards of Supreme Audit Institutions (ISSAIs 1000-1810) developed by the International Organisation of Supreme Audit Institutions (INTOSAI) and in accordance with the additional terms of reference defined in our Charter.

We are independent in accordance with the INTOSAI Code of Ethics and we have fulfilled our other ethical responsibilities in accordance with these requirements. The responsibilities of the members of IBAN are more extensively described in the section «Auditor's Responsibilities for the Audit of the Financial Statements» and in our Charter. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Management's Responsibility for the Financial Statements

Management's responsibility for the financial statements is laid down in the NFRs. The Financial Statements of NETMA are drawn up in accordance with accounting requirements and reporting standards consistent with the NATO Accounting Framework as approved by the Council. The Financial Controller is responsible for submitting the Financial Statements for audit to IBAN not later than 31st March following the end of the financial year.

The Financial Statements are signed by the Head of the NATO body and the Financial Controller. In signing the Financial Statements, the Head of NATO body and the Financial Control confirm the establishment and maintenance of financial governance, resource management practices, internal controls and financial information systems to achieve the efficient and effective use of resources.

This confirmation covers the design, implementation and maintenance of internal controls relevant to the preparation and presentation of financial statements that are auditable and free from material misstatement, whether due to fraud or error. This also covers reporting on the entity's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless there are plans to liquidate the entity or to cease its operations, or there is no realistic alternative but to do so.

Auditor's Responsibilities for the Audit of the Financial Statements

The objectives of the audit are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes an opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISSAIs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with ISSAIs, we exercise professional judgement and maintain professional scepticism throughout the planning and performance of the audit. This involves taking into account Considerations Specific to Public Sector Entities. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and

appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit 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 the entity's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of the use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the entity's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the entity to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We are required to communicate with the bodies charged with governance, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

Our Independent External Auditor's Report is prepared to assist North Atlantic Council in carrying out its role. We are therefore responsible solely to the North Atlantic Council for our work and the opinion we have formed.

Report on Compliance

Opinion on Compliance

Based on the procedures we performed, nothing has come to our attention, as part of our audit of the Financial Statements that causes us to believe that funds have not been properly used for the settlement of authorised expenditure or are not in compliance with the NATO Financial Regulations and the NATO Civilian Personnel Regulations.

Basis for Opinion

We have conducted our compliance audit in accordance with the International Standards of Supreme Audit Institutions (ISSAI 4000) developed by the International Organisation of Supreme Audit Institutions (INTOSAI) and in accordance with the additional terms of reference defined in our Charter.

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

Management's Responsibility for Compliance

All NATO staff, military and civilian, are obligated to comply with the NATO Financial Regulations, associated Financial Rules and Procedures and internal implementing directives. These include the NATO Civilian Personnel Regulations.

The General Manager of NETMA is responsible and accountable for sound financial management. The financial administration of NATO bodies must incorporate the principles of propriety, sound governance, accountability, transparency, risk management and internal control, internal audit, external audit, and fraud prevention and detection.

Auditor's Responsibilities for Compliance

In addition to the responsibility to provide reasonable assurance about whether the financial statements as a whole are free from material misstatement, the IBAN Charter requires IBAN to provide independent assurance and report annually to the North Atlantic Council about whether funds have been properly used for the settlement of authorised expenditure (propriety) and are in compliance with the regulations in force (regularity). Propriety relates to the observance of the general principles governing sound financial management and the conduct of public officials. Regularity concerns the adherence to formal criteria such as relevant regulations, rules and procedures.

This responsibility includes performing procedures to obtain independent assurance about whether funds have been properly used for the settlement of authorized expenditure and whether they have been used in compliance with the regulations in force. Such procedures include consideration of the risks of material non-compliance.

Brussels, 28 August 2019

A handwritten signature in blue ink, appearing to read 'Hans Leijtens', is written over a faint, light blue circular stamp or watermark.

Dr. Hans Leijtens
Chairman

NATO UNCLASSIFIED

ANNEX 3
IBA-AR(2019)0012

28 August 2019

INTERNATIONAL BOARD OF AUDITORS FOR NATO

LETTER OF OBSERVATIONS AND RECOMMENDATIONS

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

(NETMA)

FOR THE YEAR ENDED 31 DECEMBER 2018

NATO UNCLASSIFIED

Introduction

The International Board of Auditors for NATO (IBAN) audited the NETMA Financial Statements for the year ended 31 December 2018, and issued an unqualified opinion on the financial statements and an unqualified opinion on compliance.

Observations and Recommendations

During the audit, IBAN made no observations.

IBAN also followed up on the status of the observations from the previous year's audit and found that one recommendation remains open and one was in-progress.

IBAN also issued a Management Letter (reference IBA-AML(2019)0009) to the NETMA General Manager with observations for management's attention.

FOLLOW-UP OF PREVIOUS YEAR'S OBSERVATIONS

IBAN followed up on the status of observations from the previous years' audit. The observations, actions taken by the auditee as reviewed by IBAN, and their status are summarised in the table below.

OBSERVATION / RECOMMENDATION	ACTION TAKEN	STATUS
<p>(1) NETMA FY 2017 IBA-AR(2018)0021-REV1, paragraph 1</p> <p>ROLE AND RESPONSIBILITIES OF THE HEAD OF INTERNAL AUDIT DOES NOT ENSURE SEGREGATION OF DUTIES AND INDEPENDENCE</p> <p>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.</p>	<p>To improve the organisational independence of the internal audit function, NETMA changed the reporting line of the head of internal audit. It is no longer the Section leader of finance division (SLF3) but the team leader of the NETMA audit Team.</p> <p>According to NETMA, even if the Team Leader of the Audit Team reports to SLF3, in his duties as Head of Internal Audit, he reports to Divisional Leader Finance and has direct access to the Deputy General Manager for Internal Audit Functions.</p> <p>Moreover, NETMA set up an audit committee and an audit advisory panel. But there is a mistake in the naming and roles and function of these committees. The NETMA audit advisory panel should be named "Audit Committee" and vice versa. The right NETMA current audit advisory panel, which should be named the Audit Committee, has to approve the future annual audit programmes, the audit reports and subjects and findings related to the internal audit.</p> <p>An internal audit manual has also been issued by NETMA in December 2017. IBAN notes the progress and improvements made to ensure the independence of the internal audit</p>	<p>Observation In-progress.</p>

OBSERVATION / RECOMMENDATION	ACTION TAKEN	STATUS
	function. IBAN acknowledges that NETMA is a small organisation and do not have the resources for a completely separate Internal Audit Function. However, as this organisation is not fully in compliance with international internal auditing standards, NETMA, during next financial audits will tend to demonstrate how the segregation of duties is ensured with the new organisation of the NETMA internal audit function.	
<p>(2) NETMA FY 2017 IBA-AR(2018)0021-REV1, paragraph 2</p> <p>INTERNAL CONTROLS OVER FINANCIAL REPORTING NEED TO BE IMPROVED</p> <p>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 mistakes before the issuance of the Financial Statements.</p>	<p>In 2018, according to the NETMA finance team, different persons have checked numbers and figures disclosed in the 2018 financial statements, but due to staff turnover, it was difficult to perform a thorough review.</p> <p>IBAN still found errors in the 2018 financial statements that could be avoid by performing cross reviews, analyses and comparisons with previous years, and by performing an active reading of the financial statements.</p>	<p>Observation Open.</p>

The Open status is used for recommendations that are open and for which no notable progress has been achieved to date. The In-progress status is used for open recommendations when the NATO Body has started to implement the recommendation or when some (but not all) sub-recommendations are closed. The Closed status is used for recommendations that are closed because they have been implemented, are superseded, or have lapsed.

**THE 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 (IBAN) POSITIONS**

FOLLOW-UP OF PREVIOUS YEARS' OBSERVATIONS

(1) NETMA FY 2017

IBA-AR(2018)0021-REV1, paragraph 1

**ROLE AND RESPONSIBILITIES OF THE HEAD OF INTERNAL AUDIT DOES NOT
ENSURE SEGREGATION OF DUTIES AND INDEPENDENCE**

In a continued effort to improve our Internal Audit Function and in direct response to the IBAN audit reports of 2017, which stated that there was not a clear separation of duty between the Head of Internal Audit and the business, NETMA has changed the Head of Internal Audit. This has been discussed and approved by the Audit Advisory Panel (to be renamed the Audit Committee).

We have demonstrated that the IA Function has independence from the business and where a Finance audit is part of the programme a different Section Head is involved in the audit. We see continued monitoring of the separation of duties as part of normal ongoing audit process.

We have reviewed the ISPPA standards for organisational independence, which are as follows:

1110 - Organisational Independence

The chief audit executive must report to a level within the organisation that allows the internal audit activity to fulfil its responsibilities. The chief audit executive must confirm to the board, at least annually, the organisational independence of the internal audit activity.

Interpretation:

Organisational independence is effectively achieved when the chief audit executive reports functionally to the board. Examples of functional reporting to the board involve the board:

- *Approving the internal audit charter - This is written by IA and approved by DGM (a board member).*
- *Approving the risk-based internal audit plan - This is approved by the Audit Committee (to be renamed Audit Advisory Panel), which contains DGM.*
- *Approving the internal audit budget and resource plan - Internal audit budget and resource plan is part of the Administration plan which is approved by the Nations.*
- *Receiving communications from the chief audit executive on the internal audit activity's performance relative to its plan and other matters - Head of IA presents the audit findings and new audit plan directly to the Audit Committee.*
- *Approving decisions regarding the appointment and removal of the chief audit executive.*
- *Approving the remuneration of the chief audit executive - Not Applicable in NATO/NETMA.*
- *Making appropriate inquiries of management and the chief audit executive to determine whether there are inappropriate scope or resource limitations - Board has direct access to Head of Internal Audit to make any enquiries they wish.*

1110.A1 - The internal audit activity must be free from interference in determining the scope of internal auditing, performing work, and communicating results. The chief audit executive must disclose such interference to the board and discuss the implications.

I am content that the NETMA Internal Audit function is fully in compliance with the ISPPIA standards in respect of Organisational Independence. As a result I believe this observation is closed.

IBAN's Position

IBAN will review as part of the audit of the 2019 financial year how organisational independence of the NETMA Internal Audit Function has been operating in practice, prior to closing this observation.

NETMA ANNUAL FINANCIAL STATEMENTS

PERIOD ENDED 31 DECEMBER 2018



NETMA

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

Contents



INTRODUCTION	3
STATEMENT OF INTERNAL CONTROL	5
FINANCIAL STATEMENTS	
- STATEMENT OF FINANCIAL POSITION	7
- STATEMENT OF FINANCIAL	8
PERFORMANCE	
- STATEMENT OF CASH FLOW	9
- STATEMENT OF CHANGES IN NET	10
ASSETS/EQUITY	
- STATEMENT OF BUDGET EXECUTION	11
SIGNIFICANT ACCOUNTING POLICIES	13
NOTES TO STATEMENT OF FINANCIAL POSITION	17
NOTES TO STATEMENT OF FINANCIAL PERFORMANCE	21
NOTES TO STATEMENT OF CASH FLOW	24
NOTES TO STATEMENT OF BUDGET EXECUTION	26
CONTINGENT LIABILITIES / PROVISIONS	27
WRITE OFF AND DONATIONS	27

These statements, *with the exception of Key management remuneration and Representation Allowance*, are produced in Thousands of Euros. For example 34,632 = Thirty Four Million Six Hundred and Thirty Two Thousand Euros; 132 = One Hundred and Thirty Two Thousand Euros

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 each 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. Therefore, in accordance with IPSAS 13, it 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 2018.

Addressing Previous Audit Observations

The IBAN audit report for the 2017 NETMA Financial Statements included the following observation:

“Roles and Responsibilities of Head of Internal Audit does not ensure segregation of duties and independence”

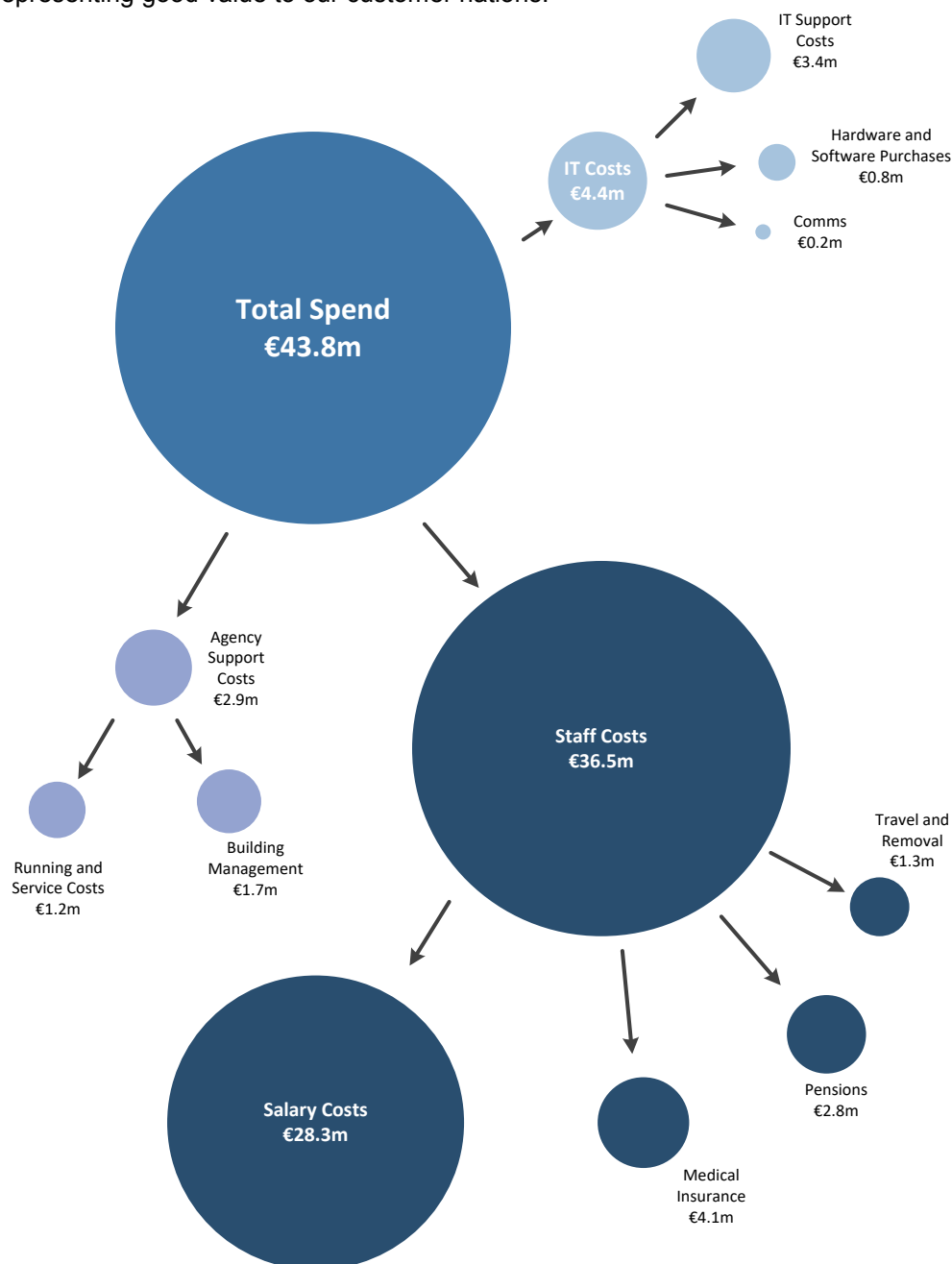
In order to address the specific issues raised by IBAN, the role of Head of Internal Audit has been moved to the Audit Team Leader. Therefore, the Head of Internal Audit is no longer involved or responsible for business operations, the role is now entirely focussed on managing the audit processes for the Agency. This was discussed at the Audit Advisory Panel as a way to mitigate the IBAN's concern without compromising the excellent value that the current process and organisational structure is bringing to the Agency.

NETMA Expenditure Breakdown 2018

The NETMA spend in the Administration Budget, as reported in the NETMA financial statements, was €43.8m in 2018. 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 2018 figures reflect the lower cost of IT consultancy support brought about by a robust negotiation of the existing support contract during 2014, additionally the continued 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 an 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 process 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 and continued in 2018.

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 2018.

MR GABRIELE SALVESTRONI
General Manager

MR MARK GANFIELD
Financial Controller

PAGE INTENTIONALLY BLANK

STATEMENT OF FINANCIAL POSITION

AS AT 31 DECEMBER 2018

(in thousands of Euros)

	Notes	2018	2017
Assets			
Current assets			
Cash and cash equivalents	B1	9,706	7,978
Short term investments			0
Receivables	B2	8,165	12,151
Prepayments	B3	0	0
Inventories		0	0
		<u>17,871</u>	<u>20,129</u>
Non-current assets			
Property, plant & equipment	B4	137	6
Intangible assets			0
		<u>137</u>	<u>6</u>
Total assets		<u>18,008</u>	<u>20,135</u>
Liabilities			
Current liabilities			
Payables	B5	2,787	4,238
Deferred revenue	B6	6,127	9,877
Advances	B7	8,010	4,906
		<u>16,924</u>	<u>19,021</u>
Non-current liabilities			
Provisions		0	0
Other Long Term Liabilities	B8	948	1,108
		<u>948</u>	<u>1,108</u>
Total liabilities		<u>17,872</u>	<u>20,129</u>
Surplus/(Deficit)	B9	130	(70)
Reserves	B10	6	76
Total net assets		<u>136</u>	<u>6</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 2018

(in thousands of Euros)

	Notes	2018	2017
Revenue			
Revenue	C1	44,270	42,982
Financial revenue			0
Other revenue			0
Total revenue		44,270	42,982
Expenses			
Personnel	C2	36,956	36,015
Contractual supplies and services - Buildings & Maintenance	C3	2,805	2,766
Contractual supplies and services - IT Services	C4	4,337	4,415
Depreciation and amortisation	C5	43	70
Impairment		0	0
Provisions		0	0
Other expenses		0	0
Finance costs	C6	(2)	(214)
Total expenses		44,140	43,052
Surplus/(Deficit) for the period		130	(70)

STATEMENT OF CASH FLOW

FOR THE YEAR ENDED 31 DECEMBER 2018

(in thousands of Euros)

	Notes	2018	2017
Cash flow from operating activities			
Surplus/(deficit)	D1	130	(70)
Non-cash movements			
Depreciation/ amortisation	D2	43	70
Impairment		0	0
Increase /(decrease) in payables	D3	(1,451)	(2,478)
Increase/ (decrease) in advances	D4	3,104	(5,261)
Increase/ (decrease) in other liabilities	D5	(160)	(161)
Increase/ (decrease) in provisions		0	160
Increase/ (decrease) in deferred revenue	D6	(3,750)	3,361
Decrease/ (Increase) in receivables	D7	3,986	(11,292)
Net cash flow from operating activities		1,902	(15,671)
Cash flow from investing activities			
Purchase of property plant and equipment / Intangible assets		(174)	0
Proceeds from sale of property plant and equipment		0	0
Net cash flow from investing activities		(174)	0
Cash flow from financing activities		0	0
Net cash flow from financing activities		0	0
Net increase/(decrease) in cash and cash equivalents		1,728	(15,671)
Cash and cash equivalents at the beginning of the period		7,978	23,649
Cash and cash equivalents at the end of the period		9,706	7,978

STATEMENT OF CHANGE IN NET ASSETS/EQUITY

FOR THE YEAR ENDED 31 DECEMBER 2018

(in thousands of Euros)

		PP&E Asset Reserve	Revaluation Reserves	Accumulated Surplus/(Deficit)	Total
Balance at the beginning of the period 2017		215	0	(139)	76
Changes in accounting policy		0	0	0	0
Restated balance		215	0	(139)	76
Transfer from Accumulated Surplus / (Deficit)		(139)	0	139	0
Surplus/(Deficit) for the period		0	0	(70)	(70)
Balance at the end of the period 2017		76	0	(70)	6
Changes in accounting policy		0	0	0	0
Restated balance		76	0	(70)	6
Transfer from Accumulated Surplus / (Deficit)	D1	(70)	0	70	0
Surplus/(Deficit) for the period	D1	0	0	130	130
Balance for the period ended 2018		6	0	130	136

STATEMENT OF BUDGET EXECUTION

FOR THE YEAR ENDED 31 DECEMBER 2018

(in thousands of Euros)

		Initial budget	Transfers	BA1	Transfers	Final budget	Commitments	Expenses	Carry forward	Lapsed
Budget 2018										
Chapter 1										
Personnel costs	E1	37,771	0	0	0	37,771	36,539	36,400	139	1,232
Chapter 2										
Agency support costs	E1	2,923	0	0	0	2,923	2,881	2,749	132	42
Chapter 3										
Process and IT management	E1	4,842	0	0	0	4,842	4,426	3,844	583	415
Total FY 2018		45,535	0	0	0	45,535	43,846	42,994	853	1,689
Chapter 1 c/o from 2017		89	0	0	0	89	51	51	0	38
Chapter 2 c/o from 2017		136	0	0	0	136	126	126	0	10
Chapter 3 c/o from 2017		573	0	0	0	573	507	507	0	67
Historical c/o		84	0	0	0	84	73	73	0	11
Total		46,417	0	0	0	46,417	44,603	43,750	853	1,814

PAGE INTENTIONALLY BLANK

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 judgements

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 2018 Financial Statements the accounting policies have been applied consistently throughout the reporting period. During 2018 NETMA formally reviewed its accruals threshold and adjusted the threshold for accruals from €50,000 down to €20,000 to give a more accurate view on the expenses within the Financial Statement. There were no further adjustments to accounting rules or policies in 2018.

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 2018: 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) became effective January 1st 2018 and replaces IPSAS 25. IPSAS 40 (Public Sector Combinations) will become effective January 1st 2019.

Changes in financial rules and regulations

During 2015 NATO adopted new financial rules and regulations. During 2018 there were no additional changes. These financial statements have been produced in line with the 2015 changes to financial rules and regulations, during 2019 NETMA will be conducting an internal review of their Financial Rules and Regulations to further update them in line with the 2015 NATO adaptation.

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 2018. 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 2018:

EUR – GBP = 1: 0.9034

EUR – USD = 1: 1.1538

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. During the 2017 audit NETMA was asked to record future year Calls for Funds as a receivable in the accounts. This has continued in 2018 with the corresponding double entry against unearned revenue.

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. Therefore, in accordance with IPSAS 13 - Leases, it 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. NETMA has no assets purchased prior to 2013 that would still have an economic life still in active use within the agency.

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, future years call for funds and double entry adjustments for lapsed credits which are now shown as a payable to nations.

Advances

Advances are contributions from member nations called for 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

	2018	2017
Cash accounts	9,704	7,977
Clearing cash accounts	0	0
Petty cash and advances	2	1
Current bank accounts	0	0
Cash equivalents	0	0
Bank accounts interest	0	0
Total	9,706	7,978

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 2018 and 2017 on the main accounts is that one participating nation paid its 1st Quarter Call for Funds for 2019 in 2018, which did not happen in 2018.

2. Receivables

	2018	2017
Contributions receivable from nations current year	0	3
Receivables from non-consolidated entities	431	649
Contributions receivable from nations following year	7,720	11,456
Receivables from staff members	14	43
Other receivables	0	0
Total	8,165	12,151

Receivables from non-consolidated entities

Represent receivables recoverable from MoD Germany with regards to VAT charged in 2018.

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 2018. One nation has paid their element as at 31st December thus the value is lower than the previous year.

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

	2018	2017
Suppliers	0	0
Staff	0	0
Total	0	0

No material prepayments were made to suppliers in 2018 (a value of €489.70 was paid in 2018 relating to 2019).

4. Property, Plant and Equipment

	2018	2017
PP&E	137	6
Total	137	6

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 in the future.

As at 31 December 2018 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. During 2018 4 new Items of IT capability valued at €174K were purchased that met the capitalisation criteria and have been added to the asset register.

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

	2018	2017
Cost		
Opening Balance	6	76
Additions	174	0
Disposals	0	0
Depreciation	(43)	(70)
Closing Balance	137	6
Gross carrying amount	1,414	1,240
Accumulated depreciation	(1,277)	(1,233)
Net Carrying Amount	137	6

5. Payables

	2018	2017
Payables to suppliers	5	8
Payables to non-consolidated entities	0	0
Payables to staff members	0	0
Lapsed Credits to be offset from future CFFs	1,814	3,419
Other payables	969	811
Total	2,787	4,238

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 2018, an estimate is undertaken by reviewing invoices paid in January and the first 2 weeks of February 2019. The estimated accrual for goods and services as at 31 December 2018 is €550K. The other element is the estimated accrual relating to unpaid leave, this is based on

the untaken leave carried forward as at 31 December 2018 multiplied by the average salary costs per day. This results in an accrual of €419K.

6. Deferred Revenue

	2018	2017
Deferred Revenue	6,127	9,877
Total	6,127	9,877

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 decreased for 2018 as per note B2 where we have received one nations Call relating to 2019 in 2018.

	2018	2017
Unearned revenue b/f	9,877	7,316
National Contributions	42,505	33,159
Miscellaneous Revenue (excl Bank Interest)	108	86
Movement in Receivable from nations for following year	39	10,215
Less:		
Operational Expenditure	43,750	43,156
Movement in Lapsed Credits from Budget Execution	(1,605)	(2,082)
Movement in Following years CFF Receivables	3,736	0
Miscellaneous Financial Charges / (Income)	524	600
Foreign Exchange (Gains) / Losses	(4)	(775)
Unearned revenue c/f	6,127	9,877

7. Advances

	2018	2017
Advance contributions	8,010	4,906
Total	8,010	4,906

Advance contributions

Advances include funding received above the budget for that year, relating to 2019 Calls for Funds received in 2018 and nations individual travel requirements.

8. Other long term liabilities

	2018	2017
Operating lease liability	948	1,108
Total	948	1,108

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)

	2018	2017
Surplus / (Deficits)	130	(70)
Total	130	(70)

The accumulated surplus balance represents in year movements relating to PP&E. The surplus for 2018 results from in year depreciation charges totalling €43K against the asset purchases totally €174K. This surplus/(deficit) is transferred to Reserves at the close of each financial year.

NATO UNCLASSIFIED

10. Reserves

	2018	2017
PP&E asset reserve	6	76
Total	6	76

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 2017, the PP&E asset reserve was decreased by the accumulated deficit of €70K resulting in an opening Net Assets balance as at 1st January 2018 of €6K.

NATO UNCLASSIFIED

C. Notes to Statement of Financial Performance

1. Revenue

	2018	2017
National contributions	42,505	41,036
National contributions to be called for	0	0
Other reimbursements	1,765	1,945
Total	44,270	42,982

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

	2018	2017
Pay and overtime	23,435	22,720
Allowance	4,729	4,900
Pension	2,805	2,710
Medical and insurance	4,154	3,883
Travel	1,834	1,801
Total	36,956	36,015

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 252 established posts. A breakdown of wages, salaries and employee benefits is provided below. Costs remained largely consistent in 2018, although there was a pay rise applied to all staff.

	2018	2017
Employee benefits expense	32,318	31,494
Post employee benefits		
- For defined contribution pensions scheme	2,805	2,710
Untaken leave accrued	418	461
Total employee benefits expense	35,541	34,665

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.

NATO UNCLASSIFIED

DCPS Insurance Premium Refund

Further to an analysis covering the last years of the history of death in service risks in relation to premiums paid by the Organisation during 2012-2015, a compensation of EUR 6 million at the NATO-wide level was agreed by the insurance company. End 2018, the NATO Secretary General decided that a fraction of this amount (circa EUR 1.7 million) should be paid to NATO staff who were members of the DCPS during the period 2012-2015 in proportion to the contributions they made to the DCPS. Staff employed by "NATO body" during the period 2012-2015 and affiliated to the DCPS are therefore entitled to a payment to be made from the NATO DCPS accounts. A decision still has to be taken concerning the remaining amount of the compensation, which may result in a proportional payment to "NATO body".

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 are all other NETMA staff.

	2018	2017
Key management remuneration	925	844

The figure for 2018 is higher than 2017 in-line with NATO wide pay increases and the senior management team being in post for a longer period of time resulting in step rises not occurring in the year previous.

Representation allowance

As per PO(2014)0154 dated 27 March 2013, expenditure on the representation allowance by the qualifying officials totalled €5,583 and is broken out below.

	2018	2017
Rent supplement	2,411	3,173
Hospitality expenses	3,173	6,749
Total	5,583	9,922

3. Buildings and maintenance

Contractual supplies and services

	2018	2017
Building rent and maintenance	1,791	1,789
Security	655	607
Other costs	359	369
Total	2,805	2,766

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.

NATO UNCLASSIFIED

In accordance with IPSAS 13 – Leases, the table below details obligations under the Operating Leases as at 31 December 2018: (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.

	2018	2017
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

4. IT services

Contractual supplies and services

	2018	2017
Communication	202	112
Information technology support	4,136	4,304
Total	4,337	4,415

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

5. Depreciation and amortisation

	2018	2017
Depreciation and amortisation	43	70
Total	43	70

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

	2018	2017
Foreign exchange gain /(loss)	(0)	0
Other charges	(2)	(214)
Total	(2)	(214)

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 2018 only immaterial values of €468 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.

D. Notes to Statement of Cash Flow

1. Surplus / (deficit) from operating activities

	2018	2017
Surplus / (deficit)	130	(70)
Total	130	(70)

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

	2018	2017
Depreciation and amortisation	43	70
Total	43	70

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

3. Increase / (decrease) in payables

	2018	2017
Payables to suppliers	(4)	(396)
Other payable	(1,447)	(2,082)
Total	(1,451)	(2,478)

The movement on payables in 2018 represents an decrease in the outstanding liabilities from 2017. The decrease is attributable to a lower lapsed credit value to be returned to nations in 2018 compared to 2017 Budget Execution Statement.

4. Increase / (decrease) in advances

	2018	2017
Advance contributions	3,104	(5,261)
Total	3,104	(5,261)

Movement on advances results from the UK paying the 1st Quarter Call for Funds for 2019 in 2018. There is no longer an advance in the accounts relating to the relocation from Unterhaching to Hallbergmoos and this has been transferred off of the Admin account as per the nations' request.

5. Increase / (decrease) in other liabilities

	2018	2017
Operating lease liability	(160)	(161)
Total	(160)	(161)

This reflects the movement created by the operating lease liability explained at Note B8.

6. Increase / (decrease) in deferred revenue

	2018	2017
Deferred revenue	(3,750)	3,361
Total	(3,750)	3,361

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

7. (Increase) / decrease in receivables

	2018	2017
National contributions	3,739	(11,016)
VAT	218	(247)
Other receivables	29	(29)
Total	3,986	(11,292)

The decrease in National receivables is explained in Note B2, but relates to national contributions received relative to the annual budget in 2018 for future budgets for 2019 called for in 2018. The decrease in VAT receivable relates to monies owed to the Agency from the German VAT office regarding VAT reclaimable spends in 2018. Other receivables relate to monies owed from NETMA Staff members.

E. Notes on Statement of Budget Execution

1. Budget analysis - 2018

	2018	2017
Chapter 1 -2018	37,771	38,066
Total	37,771	38,066

There was an underspend of €1,232M against the budget for 2018 due to lower than budgeted removals expenses, reduced spend on duty travel and lower education allowance expenditure than previously anticipated. The return of the lapsed credits will be agreed with nations in 2019.

	2018	2017
Chapter 2 – 2018	2,923	3,053
Total	2,923	3,053

In 2018 for Chapter 2 NETMA spent 5% less than budget due to lower than expected security cost and lower than expected maintenance and repair costs. The return of the lapsed credits will be agreed with nations in 2019.

	2018	2017
Chapter 3 – 2018	4,842	4,748
Total	4,842	4,748

In 2018 for Chapter 3 NETMA spent 21% (€998K) less than the approved budget. This was caused by lower than budgeted costs for Communications costs, IT Consultancy spend and software purchases. Large elements of this underspend were committed at year end and have been carried forward into 2019 to complete work. Where applicable the return of the lapsed credits will be agreed with nations in 2019.

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

	2018	2017
NET CASH INFLOW FROM OPERATING ACTIVITIES	1,902	(15,671)
- Cash contributions received in year	(42,505)	(34,999)
- Cash Contributions due	(7,720)	0
- VAT reimbursement from Germany MoD	(1,189)	(723)
- Other cash revenue in year	(141)	(11,645)
GROSS CASH OUTFLOW FROM OPERATING ACTIVITIES	(49,653)	(63,038)
- Recoverable VAT paid in year	431	648
- Lapsed credits returned to Nations	3,419	12,819
- Prepayments to Suppliers	0	0
- Other Movements	524	(2,934)
- Other Cash payments in year	1,515	10,806
PREDICTED BUDGET CASH PAYMENTS	(43,763)	(41,699)
SCHEDULE 5: EXPENSES	(43,750)	(42,369)

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

	2018	2017
SCHEDULE 2: EXPENSES	44,140	43,052
Add: opening payables and accruals	4,238	1,215
Less: closing payables and accruals	(2,787)	(4,238)
Property, Plant and Equipment adjustments	130	(70)
Transfer of UK Relocation Advance	1,470	0
Operating lease liability / Movement in VAT Paid	597	(160)
CASH PAYMENTS	47,788	39,799
Closing payables and accruals included in/(excluded from) budget	(0)	(592)
Less: Lapsed Credits to be returned to Nation	(3,419)	3,419
Less: Italian duty travel / Spanish Phone line expenses excluded from budget	(501)	(576)
Less: NETMA relocation costs excluded from budget	0	0
PREDICTED BUDGET CASH PAYMENTS	43,868	42,049
SCHEDULE 5: EXPENSES	43,750	42,369

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 0 items were submitted and approved for write off through the NETMA Internal Audit section in 2018 in accordance with NETMA delegated authorities. Previously these write-offs cover items that are obsolete, damaged beyond economic repair or lost.

