

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

**NATO UNCLASSIFIED**

21 December 2020

**DOCUMENT**  
C-M(2020)0053-AS1

**IBAN AUDITOR'S REPORT ON THE 2019 FINANCIAL YEAR STATEMENTS OF NATO  
AIRBORNE EARLY WARNING AND CONTROL PROGRAMME MANAGEMENT  
AGENCY (NAPMA)**

**ACTION SHEET**

On 18 December 2020, under the silence procedure, the Council noted the RPPB report attached to C-M(2020)0053, agreed its conclusions and recommendations, and agreed to the public disclosure of the report, the IBAN Auditor's Report, and the restated NAPMA 2019 financial statements.

(Signed) Jens Stoltenberg  
Secretary General

NOTE: This Action Sheet is part of, and shall be attached to C-M(2020)0053.

**NATO UNCLASSIFIED**



**NATO UNCLASSIFIED**

11 December 2020

**DOCUMENT**  
C-M(2020)0053  
**Silence Procedure ends:**  
**18 Dec 2020 15:30**

**IBAN AUDITOR'S REPORT ON THE 2019 FINANCIAL YEAR STATEMENTS OF NATO  
AIRBORNE EARLY WARNING AND CONTROL PROGRAMME MANAGEMENT  
AGENCY (NAPMA)**

**Note by the Secretary General**

1. I attach the International Board of Auditors for NATO (IBAN) Auditor's Report on the 2019 restated financial statements of NATO Airborne Early Warning and Control Programme Management Agency (NAPMA). The IBAN Auditor's Report set out a qualified opinion on the 2019 financial statements and an unqualified opinion on compliance for NAPMA.
2. The IBAN report has been reviewed by the Resource Policy and Planning Board (RPPB) (see Annex 1).
3. I do not believe this issue requires further discussion. Therefore, **unless I hear to the contrary by 15:30 hours on Friday, 18 December 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 Report, and the restated NAPMA 2019 financial statements.

(Signed) Jens Stoltenberg

1 Annex  
1 Enclosure

Original: English

**NATO UNCLASSIFIED**

-1-



**IBAN AUDITOR'S REPORT ON THE 2019 FINANCIAL YEAR STATEMENTS OF NATO  
AIRBORNE EARLY WARNING AND CONTROL PROGRAMME MANAGEMENT  
AGENCY (NAPMA)**

**Report by the Resource Policy and Planning Board**

References:

- |    |                     |   |
|----|---------------------|---|
| A. | IBA-A(2020)0079     | IBAN's Auditor's Report on the audit of 2019 restated financial statements of the NATO Airborne Early Warning and Control Programme Management Agency (NAPMA) |
| B. | C-M(2015)0025       | NATO Financial Regulations (NFR)  |
| C. | BC-D(2015)0260-REV1 | Financial rules and procedures (FRP)  |
| D. | C-M(2016)0023       | NATO Accounting Framework   |
| E. | PO(2015)0052        | Wales Summit tasker on transparency and accountability  |

**INTRODUCTION**

1. This report by the Resource Policy and Planning Board (RPPB) addresses the International Board of Auditors for NATO (IBAN) Auditor's Report on the 2019 Restated Financial Statements and compliance of NATO Airborne Early Warning and Control Programme Management Agency (NAPMA). The IBAN Auditor's Report produced a qualified opinion on the Restated Financial Statements and unqualified opinion on compliance for NAPMA (reference A).

**AIM**

2. This report highlights key issues in the IBAN Auditor's Report (reference A) to enable the Board to reflect on strategic challenges 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 Report that have been discussed and dealt with by the participating Nations, represented on the NAPMO Agency Supervisory Board, which is the appropriate governing body. The RPPB is mandated under Article 15 of the NFRs (reference B) to examine the Auditor's Report and to provide comments and recommendations as required.

**DISCUSSION**

4. During the audit, IBAN issued two observations and recommendations: recognition of Contractor Acquired Property (CAP Assets) as Property, Plant and Equipment (PP&E) and understatement of revenue related to a grant received which both impacted the audit opinion. Due to these two new observation the IBAN issued a qualified opinion on the

Restated Financial Statements and an unqualified opinion on compliance for the year 2019. Additionally, the IBAN followed up on the status of observations and recommendations from the previous years' audits and noted that two remain in progress.

5. Observation 1: The IBAN found that an adjustment is needed related to the Final Lifetime Extension Programme (FLEP) in the recognition of Contractor Acquired Property (CAP Assets) as Property, Plant and Equipment (PP&E) to adhere to the NATO Accounting Framework. This is because NAPMA incorrectly reported material CAP Assets owned by NATO and controlled by NAPMA, such as liaison offices, laboratories, facilities, test equipment and tools as WIP (Work in Progress) and not as PP&E. However, these assets should not be accounted for as WIP as they are not physically transferrable to the NATO Airborne Early Warning & Control (NAEW&C) Force. According to the IBAN, CAP Assets should have been reported in a separate category as PP&E and recognised in the Financial Statements over the period of the FLEP contract. Therefore the PP&E, which should have been capitalised, is understated.

5.1. NAPMA agreed to perform a systematic analysis of the possibility to change its accounting policy to address this observation. NAPMA also agreed to disclose any information regarding disposed or sold CAP Assets in the future. NAPMA pointed out that CAP Assets may also include intangible assets and confirmed its willingness to solve all pending issues in coordination with the IBAN. To reduce the likelihood of these errors occurring again, the Board supports the IBAN recommendation for NAPMA to correctly reclassify, account and disclose all upcoming CAP Assets in the Financial Statements in accordance with the NATO Accounting Framework (reference D) and NAPMO Financial Regulations. The Board stresses the need for the financial statements to disclose a reasonable estimated value of CAP assets that should lead to the closure of this observation for the 2020 Financial Statements. In addition the Board supports the proposal to include findings from NAPMA analysis of its accounting policy into the upcoming review of the NATO Accounting Framework.

6. Observation 2: The IBAN found that NAPMA's accounting policy did not cover the recognition of grant revenue when there are no performance obligations. As a result of this weakness, Deferred Revenue included USD 7 million related to a grant from the Single European Sky Air Traffic Management Research (SESAR), which should have been recognised as revenue, given that the activity was certified as completed, and funds received in 2019. As a result, Deferred Revenue was overstated and Revenue understated by USD 7 million.

6.1. NAPMA concurred with the recommendation and agreed to correct its 2020 Financial Statements. The Board supports the IBAN recommendations for NAPMA to revise its accounting policy in order to ensure that it covers the special case regarding the recognition of grant revenue and to apply the correction in its 2020 Financial Statements.

7. Prior year observations in-progress: In the audit of the 2017 NAPMA Financial Statements, IBAN recommended that NAPMA enhances the financial reporting review

process, especially in relation to inaccuracies and non-material errors identified in the financial statements and to improve its risk management, internal control and internal audit. Although significant actions have been taken by NAPMA in recent years, it still has to ensure that its review process identifies material disclosure errors in order to avoid restating the financial statements and to continue working towards full compliance with the approved internal control framework, COSO<sup>1</sup>.

7.1. NAPMA concurred with the recommendation and pledged to ensure consistency between the face of the statements, notes and annexes. Additionally, NAPMA will carry on with its activities to accomplish full compliance with COSO. IBAN reiterated that financial reporting review process should be improved, especially the Budget Execution Statements. The Board concluded that the progress on 2019 observations and prior-year observations will be reviewed in the context of 2020 IBAN audit of Financial Statements.

8. The discussion was welcomed by the Board as an important and transparent exercise of the RPPB's oversight role. The Board confirmed its reliance on IBAN's observations, stressed the importance of an accurate financial estimates and called for all measures to be taken to ensure a clean audit with unqualified opinions for 2020 Financial Statements.

## **CONCLUSIONS**

9. Two new IBAN observations were raised for NAPMA which impacted the qualification of audit opinion on the restated financial statements for NAPMA in 2019. As of the date of the respective IBAN Auditor's Report a total of two prior year observations for NAPMA were in-progress.

10. In 2019, IBAN found that CAP Assets were incorrectly recognised in Work in Progress and grant-related revenue was incorrectly documented in accounting records. The Board supports the IBAN recommendation for NAPMA to reclassify CAP Assets from WIP to a PP&E asset category and to account and disclose all CAP Assets in the Financial Statements. Furthermore, the Board notes that CAP Assets may also include intangible assets and supports the recognition of a reasonable estimated value of these assets in the Financial Statements. To mitigate the likelihood of understating revenue again, the Board supports the IBAN recommendation for NAPMA to correct the grant-related figures in its accounting records and revise its accounting policies.

11. In respect of prior year observations, the Board notes the progress made by NAPMA and reiterates its request to NAPMA to address the IBAN prior year findings related to the improvement of financial reporting as well as risk management, internal control and internal audit.

---

<sup>1</sup> Committee of Sponsoring Organizations of the Treadway Commission

12. The Board confirmed its reliance on IBAN's observations, stressed the importance of an accurate financial estimates and called for all measures to be taken to ensure a clean audit with unqualified opinions for 2020 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 reference A;

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

13.3. agree to the public disclosure of the 2019 restated financial statements for NAPMA, its associated IBAN Auditor's Reports and this report in line with agreed policy at reference E.



NORTH ATLANTIC TREATY ORGANIZATION  
ORGANISATION DU TRAITÉ DE L'ATLANTIQUE NORD  
INTERNATIONAL BOARD OF AUDITORS  
COLLÈGE INTERNATIONAL DES AUDITEURS EXTERNES DE L'OTAN

Enclosure to  
C-M(2020)0053

**NATO UNCLASSIFIED**

IBA-A(2020)0079  
26 August 2020

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

Cc: NATO Permanent Representatives  
Chairman, NATO Airborne Early Warning & Control Programme Management Organisation (NAPMO) Board of Directors  
General Manager, NATO Airborne Early Warning & Control Programme Management Agency (NAPMA)  
Financial Controller, NAPMA  
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 Airborne Early Warning & Control Programme Management Agency's (NAPMA) Restated Financial Statements for the year ended 31 December 2019 – IBA-AR(2020)0018***

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

IBAN's report sets out a qualified opinion on the Financial Statements of the NATO Airborne Early Warning & Control Programme Management Agency and an unqualified opinion on compliance for financial year 2019.

Yours sincerely,

Daniela Morgante  
Chairman

Attachments: As stated above.

**NATO UNCLASSIFIED**

-1-

**Summary Note for Council  
by the International Board of Auditors for NATO (IBAN)  
on the audit of the Restated Financial Statements of the  
NATO Airborne Early Warning and Control  
Programme Management Agency (NAPMA)  
for the year ended 31 December 2019**

The NATO Airborne Early Warning & Control Programme Management Organisation (NAPMO), including the NATO Airborne Early Warning & Control Programme Management Agency (NAPMA) was established to assume the direction, the co-ordination, and the execution of the NATO Airborne Early Warning and Control (NAEW&C) system. The management of the program consists of overseeing the acquisition of the operating assets needed to establish NAEW&C capability and subsequent acquisitions of enhancements thereof. NAPMA expenditure in 2019 – including additions to modernisation assets – was approximately USD 120 million.

IBAN issued a qualified opinion on the financial statements and an unqualified opinion on compliance for the year ended 31 December 2019.

During the audit, IBAN made two observations and recommendations. These findings are in the Letter of Observations and Recommendations (Annex 3).

The main findings are listed below and impact the audit opinion on the financial statements but not on compliance:

1. Recognition of Contractor Acquired Property (CAP Assets) as Property, Plant & Equipment.
2. Understatement of revenue related to a grant received.

IBAN followed up on the status of observations and recommendations from the previous years' audits and found that two remain in progress.

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

The observations and recommendations raised during the audit as well as the follow-up of the previous years' observations, which have not been included in the IBAN's Letter of Observations and Recommendations are included in a Management Letter addressed to NAPMA management. This is because IBAN considers that these matters are to be addressed by Management and therefore fall under NAPMA executive responsibility



**NATO UNCLASSIFIED**

ANNEX 2  
IBA-AR(2020)0018

26 August 2020

**INTERNATIONAL BOARD OF AUDITORS FOR NATO**

**AUDITOR'S REPORT ON THE RESTATED FINANCIAL STATEMENTS OF THE  
NATO AIRBORNE EARLY WARNING AND CONTROL  
PROGRAMME MANAGEMENT AGENCY**

**(NAPMA)**

**FOR THE YEAR ENDED 31 DECEMBER 2019**

**NATO UNCLASSIFIED**

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

**Report on the Audit of the Restated Financial Statements**

**Qualified Opinion on the Restated Financial Statements**

The International Board of Auditors for NATO (IBAN) has audited the Restated Financial Statements of NATO Airborne Early Warning and Control Programme Management Agency (NAPMA), for the 12 month period ended 31 December 2019, issued under document reference NAPMA/NFC(20)50-00/031, and submitted to IBAN on 6 July 2020, according to IBAN's letter of 9 January 2020. These Restated Financial Statements comprise the Statement of Financial Position as at 31 December 2019, 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 2019, including a summary of significant accounting policies and other explanatory notes. In addition, the Restated Financial Statements include a budget execution report for the 12 month period ended 31 December 2019.

In our opinion, except for the effects of the matter described in the Basis for Qualified Opinion section of our report, the Restated Financial Statements give a true and fair view of the financial position of NAPMA as at 31 December 2019, and of its financial performance, its cash flows and budget execution for the 12 month period ended 31 December 2019, in accordance with accounting requirements and reporting standards consistent with the NATO Accounting Framework.

**Basis for Qualified Opinion on the Restated Financial Statements**

Other Non-Current Assets - Work in Progress (WIP) amounting to USD 26 million include material Contractor Acquired Property (CAP Assets) related to the Final Lifetime Extension Programme (FLEP), such as liaison offices, laboratories, facilities, test equipment and tools. In addition, Projects Expenses include at least USD 2 million related to CAP Assets. These assets, which are owned by NATO and controlled by NAPMA, are not physically transferrable to the NATO Airborne Early Warning & Control (NAEW&C) Force. CAP Assets should have been reported in Property, Plant and Equipment (PP&E) in accordance with IPSAS 17, *Property, Plant and Equipment*, and the respective annual depreciation charge allocated to WIP in accordance with IPSAS 11, *Construction Contracts*.

Deferred Revenue include USD 7 million related to a grant from the Single European Sky Air Traffic Management Research (SESAR), for which the activity was certified as completed, and funds received in 2019. In accordance with IPSAS 23, *Revenue from Non-Exchange Transactions*, this grant revenue should have been recorded as Revenue. As a result, Deferred Revenue was overstated and Revenue understated by USD 7 million.

Overall, the overstatement of Project Expenses by at least USD 2 million and the understatement of Revenue by USD 7 million lead to an understatement of Surplus/(Deficit) for 2019 and Net Assets/Equity at 31 December 2019 by at least USD 9 million.

In accordance with the NAPMO Financial Regulations (NFRs), external audit of the NATO bodies and reporting entities 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 NAPMA 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 31<sup>st</sup> March following the end of the financial year.

The Financial Statements are signed by the Head of the NATO reporting entity and the Financial Controller. In signing the Financial Statements, the Head of the NATO reporting entity and the Financial Controller 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 NAPMO 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 NAPMA staff, military and civilian, are obligated to comply with the NAPMO Financial Regulations, associated Financial Rules and Procedures and internal implementing directives. These include the NATO Civilian Personnel Regulations.

General Manager is responsible and accountable for sound financial management. The financial administration of NATO bodies and reporting entities 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, 26 August 2020



Daniela Morgante  
Chairman

**NATO UNCLASSIFIED**

ANNEX 3  
IBA-AR(2020)0018

26 August 2020

**INTERNATIONAL BOARD OF AUDITORS FOR NATO**

**LETTER OF OBSERVATIONS AND RECOMMENDATIONS**

**NATO AIRBORNE EARLY WARNING AND CONTROL  
PROGRAMME MANAGEMENT AGENCY**

**(NAPMA)**

**FOR THE YEAR ENDED 31 DECEMBER 2019**

**NATO UNCLASSIFIED**

## **Introduction**

The International Board of Auditors for NATO (IBAN) audited the NAPMA Restated Financial Statements for the year ended 31 December 2019, and issued a qualified opinion on the Restated Financial Statements and an unqualified opinion on compliance.

## **Observations and Recommendations:**

During the audit, IBAN made two observations and recommendations.

These observations impact the audit opinion on the Restated Financial Statements, not on compliance:

1. Recognition of Contractor Acquired Property (CAP Assets) as Property, Plant & Equipment.
2. Understatement of revenue related to a grant received.

IBAN followed up on the status of observations and recommendations from the previous years' audits and found that two remain in progress.

The observations and recommendations raised during the audit as well as the follow-up of the previous years' observations, which have not been included in the IBAN's Letter of Observations and Recommendations are included in a Management Letter addressed to NAPMA management. This is because IBAN considers that these matters are to be addressed by Management and therefore fall under NAPMA executive responsibility.



## OBSERVATIONS AND RECOMMENDATIONS

### 1. RECOGNITION OF CONTRACTOR ACQUIRED PROPERTY (CAP ASSETS) AS PROPERTY, PLANT AND EQUIPMENT

#### Reasoning

1.1 The NATO Airborne Early Warning & Control (NAEW&C) Programme covers the development and modernisation of a fleet of aircrafts owned by North Atlantic Treaty Organisation (NATO) and operated by the NAEW&C Force part of Allied Command Operations (ACO).

1.2 NAPMA, as the Executive Agent for NAPMO, operates under the juridical personality possessed by NATO by virtue of the Ottawa Agreement. Allied Command Operations (ACO) operates under the juridical personality possessed by the Supreme Headquarters Allied Powers Europe (SHAPE), which is a different juridical personality established by virtue of the Paris Protocol. Therefore, from a legal perspective, NAPMA and ACO are two separate juridical personalities.

1.3 In accordance with the NATO Accounting Framework, ACO controls the fleet of aircraft including the engines and engine components/accessories. Accordingly, NAPMA accounts for the cost of the development of the aircraft as a Work in Progress Non-Current Asset in the Statement of Financial Position. This Work in Progress represent payments made to the prime contractor and its subcontractors related to milestone payments plus advances for work to be performed. Work in Progress is transferred to ACO once completed to reflect the transfer of control over the physical assets.

1.4 As per Article 13 section V of the NAPMO Charter related to the ownership of assets: *“All assets acquired by NAPMO shall be acquired in the name of and as the property of NATO. However, NAPMO shall exercise all rights thus enjoyed by NATO”*. This article means that all assets acquired or developed by NAPMO are owned by the NATO legal entity established under the Ottawa Agreement.

1.5 Furthermore, as per Article 3.4 NAPMO Financial Regulations: *“NAPMA shall be responsible, within the limits laid down in the NAPMO Charter and in compliance with the purposes therein defined, for the correct administration of funds and assets placed at NAPMA's disposal for the execution of the NAEW&C Modernisation Programme.”* This article means that as NAPMO's Executive Agent, NAPMA is responsible for the administration of assets owned by NAPMO. In addition, as per Article 17 of NAPMO Financial Regulations: *“a global statement of amounts written-off shall be reported in the annual financial statements”*.

1.6 As at 31 December 2019, two NAPMA programmes are still active. The first programme is the NATO AWACS Follow on Upgrade Programme (FUP), which started in 2010 and was planned for closure in 2019. The second programme is the Final

Lifetime Extension Programme (FLEP), which started in 2019 and is planned to end in 2027. As part of these programmes NAPMA has signed, on behalf of NAPMO, two successive contracts to develop and modernise the fleet of aircraft, with an industrial consortium formed of a prime contractor and subcontractors.

1.7 The FUP and FLEP Programmes contracts both include two separate sets of contract provisions that cover clearly distinguishable activities. The main construction contract provisions relate to the development and modernisation of the main aircraft assets. In addition, these two contracts include special provisions that include the acquisition or development of Property, Plant and Equipment (PP&E), such as liaison offices, laboratories, facilities, special test equipment and tools by the prime contractor or its subcontractors.

1.8 As per Article 6 of the Special Provisions of the NATO AWACS Final Lifetime Extension Programme (FLEP) and Follow on Upgrade Programme (FUP) related to the NATO Furnished Property/Data/Services/Classified Equipment:

“6.3. Title

*Article 6.3.1 In order to define the obligations of the parties under this Special Provision, title to each item of facilities, special test equipment, and special tooling acquired by the Contractor for NATO pursuant to this contract shall pass to and vest in NATO when it has been fully paid for by NATO either through amortization under this Contract or otherwise.*

6.4. Property/Data Administration

*6.4.1 The Contractor shall administer NATO property/data, in accordance with sound industrial practice, and in accordance with any other applicable provision as may be specified in this Contract. In addition, the Contractor shall create and maintain property records in support of their stewardship responsibilities, which shall be made available to NAPMA upon request.*

6.8. Final Accounting and Disposition of NATO Property

*6.8.1 Upon the completion of this contract, or at such earlier dates as may be fixed by the Purchaser, the Contractor shall submit, in an electronic format acceptable to the Purchaser, inventory schedules covering all items of NATO property not consumed in the performance of this contract and shall prepare for shipment, deliver f.o.b. origin, or dispose of the NATO property, as may be directed or authorized by the Purchaser.”*

1.9 Article 6 above means that all CAP Assets procured or developed on behalf of NAPMO that were used for the development and modernisation of the aircraft, such as liaison offices, laboratories, facilities, special test equipment and tools, are owned by NATO and controlled by NAPMA. These assets therefore need to be accounted for

by NAPMA in accordance with Article 3.4 of the NAPMO Financial Regulations.

1.10 According to the NATO Accounting Framework for Property, Plant and Equipment (PP&E), all NATO Reporting Entities should maintain a fixed asset register that identifies and groups all fixed assets into PP&E classes or categories. It serves as a tool for the safeguarding of assets. A review of fixed assets needs to be conducted to ensure that assets remain fit for use and to ensure accuracy and completeness of the fixed asset register and the property accounting records.

1.11 As per IPSAS 17 *Property, plant and equipment, paragraph 14: The cost of an item of property, plant and equipment shall be recognized as an asset if, and only if: (a) It is probable that future economic benefits or service potential associated with the item will flow to the entity; and (b) The cost or fair value of the item can be measured reliably.*

1.12 As per IPSAS 11 *Construction contracts, paragraph 24: "Cost that relate directly to a specific contract includes depreciation of plant and equipment used on the contract"*. Therefore, applying IPSAS 17 for the recognition of CAP Assets controlled by NAPMA does not prevent NAPMA from applying the provisions of IPSAS 11 for allocating the annual depreciation charge to the value of WIP related to aircraft assets that are transferable to ACO.

1.13 Changes to accounting policies are implemented in accordance with IPSAS 3. According to IPSAS 3: *"When it is impracticable to determine the cumulative effect, at the beginning of the current period, of applying a new accounting policy to all prior periods, the entity shall adjust the comparative information to apply the new accounting policy prospectively from the earliest date practicable."*

## Observation

1.14 NAPMA applies the provisions of *IPSAS 11 Construction Contracts* to account for operational costs related to the FLEP and FUP programmes. Accordingly, until the physical aircraft assets are transferred to NAEW&C Force, all operational costs for the two programmes are recorded as Work in Progress (WIP) in Other Non-Current Assets in the Statement of Financial Position. The same amount is recognised in Other Non-Current Liabilities - Deliverable to NAEW&C Force.

1.15 When the physical aircraft assets are modernised and transferred to NAEW&C Force, NAPMA reduces the value of the Other Non-Current Assets and Other Non-Current Liabilities by the contract value of the aircraft assets transferred.

1.16 As at 31 December 2019, NAPMA recognised Other Non-Current Assets Work in Progress (WIP) and Other Non-Current Liabilities - Deliverable to NAEW&C Force amounting to USD 37 million. Of this amount, USD 26 million related to the FLEP Programme and USD 11 million related to the FUP Programme.

1.17 During the course of the audit, IBAN reviewed WIP for both programmes and found that not all assets were physically transferable to NAEW&C Force as they will not be used to operate the fleet of aircraft.

#### FLEP Programme

1.18 For the FLEP Programme, according to the first Payment Milestone Confirmation of Completion, the closure criteria for the USD 26 million recorded as WIP relate to the reimbursement made to the Prime Contractor for the construction and acquisition of CAP Assets on behalf of NAPMA in 2019. None of these assets are physically transferable to NAEW&C Force. These CAP Assets are composed of the construction of laboratories, NAPMA liaison offices, and the acquisition of tools, and testing equipment, that occurred before the end of December 2019. These CAP Assets are legally owned by NATO and controlled by NAPMA. NAPMA accounted for these CAP Assets as part of WIP in its financial statements, when they should have been reported in a separate asset category as PP&E to reflect the Special Provisions of the FLEP Programme contract in accordance with IPSAS 17, *Property, Plant and Equipment*.

1.19 The FLEP Programme started in 2019 after the adoption of the NATO Accounting Framework and contract terms were therefore updated to incorporate the relevant financial reporting requirements regarding non-current assets. The first Payment Milestone amounting to USD 26 million uses CAP assets as a basis for the closure criteria, which is a clear indication that CAP assets are material. This amount does not represent the exact total value of CAP assets of the FLEP Programme, which still needs to be estimated. According to the FLEP Programme contract, contractors are now required to perform, record and report physical inventories throughout the FLEP Engineering Manufacturing and Development (EMD) Phase, at least every six months. This report will be reviewed by NAPMA and its contractors on a regular basis. NAPMA will therefore be able to ensure the completeness and accuracy of CAP Assets recognised as PP&E and corresponding liabilities to be recognised in the Financial Statements.

1.20 In accordance with IPSAS 11, *Construction Contracts*, the depreciation of PP&E acquired or used specifically for the purpose of a construction contract may be allocated to Work in Progress. This means that at the end of a contract the total WIP transferred to NAEW&C Force includes the cost of CAP Assets, to reflect the full cost recovery nature of the development and modernisation contracts. There is therefore no net impact caused by the depreciation charge to the Statement of Financial Performance. However, over the period of the contract, a tangible depreciable PP&E asset needs to be recognised on the face of the Statement of Financial Position, to reflect NAPMA's control and NATO's ownership over these CAP Assets.

1.21 NAPMA is authorised to use and if necessary dispose or transfer CAP Assets, following the delegation of authority provided by the NAPMO Board of Directors (BoD) to NAPMA and the NAPMO Financial Regulations. NAPMA therefore decides on the

final use of CAP Assets, once they are no longer needed for the Programmes.

1.22 IBAN also found that some CAP Assets related to the FLEP Programme were delivered in 2019 and expensed in the Statement of Financial Performance for at least USD 2 million. Therefore, PP&E shown in the 2019 NAPMA Statement of Financial Position are also understated by the value of these CAP Assets, which should have been capitalised, rather than recognised as expenses.

1.23 The total cost of CAP Assets acquired, transferred, disposed or written off are important information for the users of the financial statements, however the material cost of these assets are not currently disclosed in the NAPMA Financial Statements.

#### FUP Programme

1.24 For the FUP Programme, we found during the course of the audit that WIP included CAP Assets amounting to approximately USD 4 million, which were held at the premises of one of NAPMA's smaller sub-contractors based on contract value. Following this review, as these assets had not been physically transferred to ACO, NAPMA decided for the first time not to transfer the value of these specific CAP Assets, as it was done in the past for all other CAP Assets before 2019. NAPMA presented these assets in WIP and did not reclassify this amount to PP&E.

1.25 Since the start of the EMD phase related to the FUP modernisation Programme, NAPMA did not disclose in its Financial Statements the accumulated value of CAP Assets held at contractors' premises as PP&E. This is because NAPMA could not reliably distinguish the value of the fleet of aircraft from the value of CAP Assets. As the FUP Programme started in 2010, the contractual terms were set before the adoption of the NATO accounting Framework. Since the contract terms were not designed to provide IPSAS-compliant information regarding PP&E, the Prime Contractor did not make this information available to NAPMA in a comprehensive and timely manner. Furthermore, as NAPMA used the Foreign Military Sales (FMS) General Agent for a significant part of its contracting, this led to additional challenges in obtaining IPSAS-compliant supporting documentation, as described in the NATO Accounting Framework.

1.26 Given that it was impracticable to account for the value of CAP Assets in a reliable manner, NAPMA therefore recorded CAP Assets directly as WIP and then transferred to ACO the entire value of the assets developed and acquired under the programme, including the value of CAP Assets. The accumulated value of CAP Assets was therefore not presented as a separate PP&E asset class in the Financial Statements since the beginning of the Programme.

1.27 Had it not been impracticable to account for the value of CAP Assets related to FUP in a reliable manner, NAPMA would have been required to show total CAP Assets as PP&E in accordance with IPSAS 17. The related annual depreciation charge would have been allocated to WIP over the period of the Programme and transferred

to ACO in accordance with IPSAS 11.

1.28 As a result of NAPMA's accounting policy, information regarding the value of CAP Assets sold, disposed, written off, or transferred to the FLEP Programme was not disclosed in the Financial Statements.

1.29 Due to the impracticability of obtaining reliable and timely information for the FUP Programme, IBAN considers that the accounting treatment for this Programme was reasonable and fair, given the particular circumstances applying to the FUP Programme at the time the contractual terms were drawn.

### **Recommendations**

1.30 IBAN recommends that NAPMA:

- a) Reclassify FLEP Contractor Acquired Property (CAP Assets) from Work in Progress amounting to USD 26 million, and CAP Assets amounting to approximately USD 2 million from expenses to a newly created Property, Plant and Equipment (PP&E) asset category,
- b) Account and disclose in the Financial Statements all future CAP Assets as PP&E in accordance with the NATO Accounting Framework and NAPMO Financial Regulations,
- c) Allocate the annual depreciation charge for CAP Assets to the Work in Progress account, which is transferable to Allied Command Operations,
- d) Disclose the information regarding CAP Assets disposed, sold, or transferred in the Financial Statements;
- e) Change its accounting policy for the FLEP programme, taking into account the above changes.

## **2. UNDERSTATEMENT OF REVENUE RELATED TO A GRANT RECEIVED**

### **Reasoning**

2.1 In 2016, NAPMA received funding from the Single European Sky Air Traffic Management Research (SESAR) for the efforts in defining, developing and delivering new or improved technologies and procedures to increase the performance of Europe's Air Traffic Management (ATM) system. NAPMA received one grant represented by the following two activities (1) Production and Retrofit (PAR), and (2) Flight Simulator Training Device upgrade and Air Crew Training (FSTD). The maximum grant allowance amounted to USD 19 million.

2.2 SESAR certified that the activity related to FSTD amounting to USD 7 million was completed in 2018. The activity relating to PAR amounting to USD 12 million was 90% completed by the end of 2019. To complete the PAR activity, NAPMA needs to provide to SESAR evidence of project completion such as:

- A confirmation of project completion signed by a relevant Aviation Authority (could be a NAPMA Board signature); and/or
- Updated E3-A airworthiness Military Type Certificate (MTC); and/or
- Whatever other official document demonstrating the project is completed.

2.3 As per IPSAS 23 Revenue from non-exchange transactions, paragraph 22: *“The definition of a condition imposes on the recipient entity a performance obligation – that is, the recipient is required to consume the future economic benefits or service potential embedded in the transferred asset as specified, or return the asset or other future economic benefits or service potential to the transferor. To satisfy the definition of a condition, the performance obligation will be one of substance not merely form and is required as a consequence of the condition itself. A term in a transfer agreement that requires the entity to perform an action that it has no alternative but to perform, may lead the entity to conclude that the term is in substance neither a condition nor a restriction. This is because in these cases, the terms of the transfer itself do not impose on the recipient entity a performance obligation.”*

2.4 The purpose of the grant was to subsidise NAPMA for the FUP modernisation programme that provides the AWACS with an integrated Communication, Navigation, and Surveillance system that fully complies with the evolving concepts in civil ATM and meets all Single European Sky (SES) mandates. This means that NAPMA performs an action that it has no alternative but to perform. Therefore, the grant gives rise to obligations, but not performance obligations, because there is a lack of transfer of goods or services to the grantor or a third-party beneficiary.

2.5 As per the SESAR’s Framework Partnership Agreement, Article II.25.4 related to Reduction for poor, partial or late implementation, or breach of contractual obligations: *“If the action is not implemented properly in accordance with Annex I of the Specific agreement, or if any partner fails to comply with any other obligations under the Framework agreement or Specific agreement, the Commission may reduce the grant amount set out in the Article 3 of the Specific agreement in proportion to the improper implementation of the action or to the seriousness of the breach of obligations”.*

2.6 The terms of the grant does not specify the return of the funds, but a reduction of resources in proportion if the grant recipient does not fully complete the construction of the asset. The liability related to the return of the funds occurs only after the terms of the arrangement are breached and SESAR requests the return of funds. This grant term must not be considered as a condition or restriction since it is similar to a contingent liability under IPSAS 19, *Provisions, Contingent Liabilities and Contingent Assets*, as a future event (breaching the terms of the grant) has not yet occurred to

give rise to a present obligation. Therefore, rather than recognition, the contingency should be disclosed in the notes to the financial statements.

2.7 As per the grant agreement: *“Upon entry into force of the Specific Agreement, the Agency shall make a first pre-financing payment equivalent to 40% of the amount of the first annual instalment of the maximum contribution. At the end of each reporting period, except the last reporting period, the coordinator may submit a request for further pre-financing payment. The further pre-financing payment shall be calculated on the basis of 40% of the cumulated financing needs. At the end of at least every two reporting periods, the coordinator shall submit a request for interim payment”.*

2.8 In July 2018, NAPMA submitted the interim grant financial statements that cover eligible costs incurred in 2016 and 2017 for USD 9 million. The NAPMA internal auditor audited these interim financial statements in accordance with SESAR’s delegation of authority and guidance. The payment request of the final balance for approximately USD 4 million will be submitted to SESAR in July 2020.

## Observations

2.9 As at 31 December 2019, NAPMA accounted for the grant payments as deferred revenue amounting to USD 16 million, of which USD 7 million related to pre-finance payment received in 2016, and USD 9 million to interim payments received in 2019 and covering the costs incurred in 2016 and 2017.

2.10 Under a prudent approach, NAPMA intended to recognise the total deferred revenue as revenue after the issuance of the MTC, which should occur before the end of 2020, at the end of the FUP Programme. This accounting treatment of the grant does not reflect a fair view of the project activities advancement given the fact that the FSTD activity was completed in 2018 and that NAPMA has no alternative but to complete the PAR activity, which relates to the ongoing FUP Programme.

2.11 IBAN found that the interim payments of USD 9 million received in 2019 include costs related to the FSTD activity for approximately USD 7 million. These costs were approved as eligible costs by SESAR and the FSTD activity was reported to and certified by SESAR as achieved in 2018. Therefore, NAPMA should have recognised the revenue related to the achievement of the FSTD activity for USD 7 million. This led to an understatement of revenue in the Financial Statement of Performance and the Statement of Changes in Net Assets/Equity of USD 7 million as at 31 December 2019.

## Recommendations

2.12 IBAN recommends that NAPMA:

- a) Revise its accounting policy in order to ensure that it covers the recognition of grant revenue when there are no performance obligations,



- b) Recognise a revenue for USD 7 million in the Statement of Financial Performance and in the Statement of Changes in Net Assets/Equity, to reflect completion of the Flight Simulator Training Device upgrade and Air Crew Training (FSTD) activity funded by SESAR.

**FOLLOW-UP OF PREVIOUS YEARS' 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.

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 Reporting Entity 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. In the case where there are sub-recommendations, the status related to each sub-recommendation is indicated in the Action Taken column.

OBSERVATION / RECOMMENDATION	ACTION TAKEN BY AUDITEE	STATUS
<p><b>(1) NAPMA FY 2017</b> <b>IBA-AR(2018)0013, paragraph 1</b></p> <p><b>INNACURACIES AND NON-MATERIAL ERRORS IDENTIFIED IN THE FINANCIAL STATEMENTS</b></p> <p><b>IBAN's Recommendation</b> The Board recommends NAPMA to improve the financial reporting review process. Specifically, the Board recommends NAPMA to:</p> <ul style="list-style-type: none"> <li>• Present current and non-current liabilities as separate classifications in the face of the Statement of Financial Position.</li> <li>• Ensure consistency between the face of the Statements and the Notes.</li> <li>• Explain, in a more complete and clear manner, the explanatory note about "Risk Mitigation Fund Nations".</li> </ul>	<p>Current and non-current liabilities were presented as separate classifications in the face of the 2019 Statement of Financial Position. <b>Observation Closed</b></p> <p>IBAN identified a disclosure error in the 2019 Budget Execution Statements which led to a request for restatement of the Financial Statements. The amount related to Projects Expenses disclosed for 2019 was 66,316,522.62 USD instead of 117,746,596 USD. The financial reporting review process still requires further improvements. <b>Observation Open</b></p> <p>Explanation provided in the note sufficiently enhanced. <b>Observation Closed</b></p>	<p>Observation <b>In-Progress</b></p>

OBSERVATION / RECOMMENDATION	ACTION TAKEN BY AUDITEE	STATUS
<ul style="list-style-type: none"> <li>Start depreciation of assets when they are placed in service and are in the location and condition necessary to be capable of operating in the manner intended by management, as established by NATO Accounting Framework and IPSAS 17.</li> <li>Ensure that the historical value of write-offs approved during the year is correctly disclosed in the Financial Statements.</li> </ul>	<p>Depreciation of assets start when they are placed in service and are in the location and condition necessary to be capable of operating as established by IPSAS 17. <b>Observation Closed</b></p> <p>No disposals in 2019 for the Administrative Budget. Disposals in 2019 for the Operational budget are not disclosed in the Financial Statements. See Observation 1 related to CAP Assets. <b>Superseded so closed.</b></p>	
<p><b>(2) NAPMA FY 2017</b> <b>IBA-AR(2018)0013, paragraph 2</b></p> <p><b>IMPROVEMENTS REQUIRED IN THE AREA OF RISK MANAGEMENT, INTERNAL CONTROL AND INTERNAL AUDIT</b></p> <p><b>IBAN's Recommendation</b> The Board recommends that NAPMA:</p> <ul style="list-style-type: none"> <li>Prepare an updated entity-wide risk management plan in line with the "COSO Implementation Plan" put in place by the Agency.</li> <li>Determine the risk appetite taking three steps: 1) Define and set the risk appetite, 2) Communicate the risk appetite, 3) Monitor and update the risk appetite on an on-going basis. In doing so, NAPMA should ensure the NAPMO Governing Body's review and concurrence.</li> <li>Continue working on a systematic and detailed assessment and documentation of its internal control and risk management procedures to support compliance with its approved internal control framework, COSO.</li> </ul>	<p>The entity-wide risk management plan was implemented through the NAPMA operating instruction OI-A-18 (1 March 2019). Please, refer to the point below. No further action required. <b>Observation Closed</b></p> <p>The risk appetite was formalised at governance level. NAPMA operating instruction OI-A-18 (1 March 2019) describes the concept of risk appetite and prescribes who is determining it and how it is set. No further action required. <b>Observation Closed</b></p> <p>In December 2018, a NAPMA Risk Management and Internal Control Policy document was released as the basis for subsequent Enterprise Risk Management and Internal Control operating instructions development. These two Operating Instructions have since been released and are in</p>	<p>Observation <b>In-Progress</b></p>

OBSERVATION / RECOMMENDATION	ACTION TAKEN BY AUDITEE	STATUS
<ul style="list-style-type: none"> <li>Internal Audit to fully evaluate internal control and risk management throughout NAPMA, and that this work be clearly documented so as to be able to conclude as to NAPMA's compliance against COSO.</li> </ul>	<p>use by NAPMA (OI.A-18 ERM and OI.A-19 Internal Control).</p> <p>In addition, a revised NAPMO Corporate Governance Policy (NCGP) was drafted to incorporate the requirement to apply Enterprise Risk Management and Internal Controls at NAPMA. The revised NCGP is expected to be endorsed by the NAPMO Finance Committee (PFC) for NAPMO BOD approval at the BOD-104 session (before December 2020).</p> <p><b>Observation In-Progress</b></p> <p>In 2018, the Internal Auditor performed an evaluation of the Risk Management. Overall assessment - some improvements needed - pending NAPMO's revised Corporate Governance Policy, requiring implementation of Enterprise Risk Management and Internal Control.</p> <p>An update to the 23 March 2017 NAPMA Memo NAPMA/COS(17)11-00/002 <i>COSO Enterprise Risk management and Internal Control Integrated Framework – Initial Mapping</i> to support an evaluation of NAPMA incorporation of COSO principles is still in-progress.</p> <p>The formal evaluation of the system of internal controls was initiated in January 2020 by the Internal Auditor and will be presented to the NAPMO Audit Committee/PFC in September 2020.</p> <p><b>Observation In-Progress</b></p>	

**NATO AIRBORNE EARLY WARNING AND CONTROL  
PROGRAMME MANAGEMENT AGENCY (NAPMA) FORMAL COMMENTS  
ON THE LETTER OF OBSERVATIONS AND RECOMMENDATIONS AND  
THE INTERNATIONAL BOARD OF AUDITORS (IBAN) POSITIONS**

**OBSERVATION 1:  
RECOGNITION OF CONTRACTOR ACQUIRED PROPERTY (CAP ASSETS) AS  
PROPERTY, PLANT AND EQUIPMENT**

***NAPMA's Formal Comments***

***Recommendation a)***

*Further to the item above, NAPMA objects to the classification of the full value of the milestone payment for FLEP (25.7 million) in 2019 as CAP due to the following:*

*The milestone payment includes far more than simply the purchase of CAP. The applicable Contract Line Item (CLIN) encompasses all of the Engineering Manufacturing and Development (EMD) phase of the contract - a value in excess of approximately 515M USD which includes labour hours associated with the design activity, as well as the hardware and software purchased and developed, training, and even the associated travel activity. The total CLIN negotiated covers a period of approximately six years. The payment milestones to the Contractor have been time-phased across all six years based upon an estimated expenditure profile negotiated with the contractor and approved by the NAPMO BOD. As such, these milestones target key points during the period of performance that demonstrate measurable outcomes of progress. Furthermore, NAPMA has attempted to prudently balance cash flow requirements of the contractor while incentivizing ultimate delivery of a compliant EMD design and retrofitted aircraft while striving for cash flow neutrality in the overall payment plan as much as possible.*

*In summary, because the payment milestones are reflective of commingling of the full scope of the Statement of Work for the period in question as explained above NAPMA cannot agree with the full value of the initial payment invoice as accountable to CAP.*

**IBAN's Position**

**IBAN takes note of the explanation provided by NAPMA and the fact that payment milestones may not exactly match the value of the assets used as a basis for the milestone completion criteria. The Basis of Opinion section and Observation has been reworded to reflect this point.**

**Recommendation b)**

*NAPMO notes the recommendation. NAPMA will perform a thorough analysis of the possibility to change its accounting policy for contractor acquired property.*

**Recommendation c)**

*NAPMO notes the recommendation. If NAPMA can change its accounting policy on CAP, NAPMA will allocate the annual depreciation charge for CAP assets to the Work in Progress account.*

**Recommendation d)**

*NAPMO concurs with the recommendation. NAPMA will disclose any information regarding disposed or sold CAP assets in the future.*

**Recommendation e)**

*NAPMA has historically reported such Contractor Acquired Property as Work In Progress to include the most recent modernization Projects (NATO Mid Term, LAIRCM, and FUP).*

*NAPMA notes the IBAN's recommendation and will perform a thorough analysis of the possibility to change its accounting policy with the approval of the NAPMO Board of Directors. This will require the development and application of an estimation methodology capable of obtaining NAPMO approval. Upon receiving BOD approval of this new estimation methodology, NAPMA will return to the IBAN and request its confirmation that this new methodology meets the intent of the IBAN's recommendation.*

**OBSERVATION 2:  
UNDERSTATEMENT OF REVENUE RELATED TO A GRANT RECEIVED**

**NAPMA's Formal Comments**

**Recommendation a)**

*NAPMO accepts the IBAN's recommendation, but does not agree with the observation. NAPMA will correct the statement of financial performance and the statement of changes in net assets/equity in its 2020 Financial Statements comparative figures.*

*NAPMA's accounting policy for other revenue (revenue is recognized when*

*economic benefits that can be measured reliably will flow to NAPMA) encompasses both revenue from exchange (IPSAS 9, Objective) and non-exchange transactions (IPSAS 23, par 45). NAPMA therefore believes that its accounting policy is adequate for the recognition of revenues from grants.*

**IBAN's Position**

**IBAN acknowledges that NAPMA's accounting policy for the recognition of revenues from grants may be adequate in general. However, IBAN recommends NAPMA to revise its accounting policy in order to ensure that it covers the special case regarding the recognition of grant revenue when there are no performance obligations. The recommendation is reworded to reflect this point.**

***Recommendation b)***

*NAPMO concurs with the recommendation. NAPMA will correct the statement of financial performance and the statement of changes in net assets/equity in its 2020 Financial Statements comparative figures.*

**FOLLOW-UP ON PREVIOUS YEARS OBSERVATIONS**

**(1) NAPMA FY 2017**

**IBA-AR(2018)0013, paragraph 1**

**INNACURACIES AND NON-MATERIAL ERRORS IDENTIFIED IN THE FINANCIAL STATEMENTS**

*NAPMO concurs with the recommendation. NAPMA will ensure consistency between the face of the statements and the notes and annexes.*

**(2) NAPMA FY 2017**

**IBA-AR(2018)0013, paragraph 2**

**IMPROVEMENTS REQUIRED IN THE AREA OF RISK MANAGEMENT, INTERNAL CONTROL AND INTERNAL AUDIT**

*NAPMO concurs with the recommendation. NAPMA will continue working towards full compliance with the approved internal control framework, COSO.*

## **GLOSSARY OF TERMS**

In accordance with auditing standards, audit opinions on financial statements and on compliance can be unqualified, qualified, a disclaimer, or adverse:

- An unqualified opinion is when IBAN issues an opinion that the financial statements and budget execution report are stated fairly and that nothing has come to our attention 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 rules and regulations.
- A qualified opinion means that IBAN was generally satisfied with the presentation of the financial statements, but that some key elements of the statements were not fairly stated or affected by a scope limitation, or specific issues have come to our attention 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 rules and regulations.
- A disclaimer is issued when the audit scope is severely limited and IBAN cannot express an opinion, or when there are material uncertainties affecting the financial statements or the use of funds.
- An adverse opinion is issued when the effect of an error or disagreement is so pervasive and material to the financial statements that IBAN concludes that a qualification of the report is not adequate to disclose the misleading or incomplete nature of the financial statements.



NATO UNCLASSIFIED



# **NAPMA**

## **FINANCIAL STATEMENTS 2019**

NATO UNCLASSIFIED

**Contents NAPMA Financial Statements**

	<b>Page</b>
Overview	Page 2 - 4
Statement of Financial Position	Page 5
Statement of Financial Performance	Page 6
Statement of Changes in Net Assets/Equity	Page 7
Cash Flow Statement	Page 8
Accounting Policies	Page 9 - 15
Notes to the Financial Statements	Page 16 - 30
Annex A - Budget Execution Statement	Page A1
Annex B - Statement of Internal Control	Page B1 - B4

## **OVERVIEW**

### **Overview of the NAEW&C Programme Management Organisation's Operations and Environment (NAPMO)**

In 1975, the NATO Military Authorities established a "priority one" requirement for an Airborne Early Warning and Control (AEW&C) system to operate over both land and sea. The system was designed to provide an airborne warning and detection capability and to improve the Alliance's maritime surface surveillance capability. It would also contribute to the direction and control of tactical air forces and to the gathering of information on hostile ship and aircraft movements.

In December 1978, a number of NATO Nations joined together to establish and implement the NATO AEW&C Programme. As a result of the international agreements formally ratified at that time, the NAEW&C Force Programme Management Organisation (NAPMO) was created as a NATO Production and Logistics Organisation and established as a NATO civil organisation under the provisions of the 1951 Ottawa Agreement i.a.w. its charter.

Nations agreed at the time to operate and support the NAEW&C Force under a single Force Commander subordinate to the Strategic Commanders (SCs). The Supreme Allied Commander Europe (SACEUR) acts as the executive agent for the SC's in NAEW&C Force matters. However with regard to the maintenance and supply concept the NAPMO retained responsibility to represent the NAPMO Nations' interest, in particular the NAPMO Board of Directors (BOD) is responsible for the Depot Level Maintenance (DLM) policy and its implementation, while NAPMO at the same time is responsible for the achievement of industrial benefits.

Currently, the NATO AEW&C Programme is comprised of 16 Nations participating as full members – Belgium, Czech Republic, Denmark, Germany, Greece, Hungary, Italy, Luxembourg, The Netherlands, Norway, Poland, Portugal, Romania, Spain, Turkey, and the United States.

The United Kingdom exercises limited participation as a NAPMO member; but its fleet of E-3D aircraft is an integral part of the NAEW&C Force.

France has an observer role and maintains continual coordination to ensure its four E-3F aircraft remain interoperable with the other E-3 fleets. France also often assists in coordinated operations with the NAEW&C Force.

### **Role of the NAEW&C Programme Management Agency (NAPMA)**

As NAPMO executive agent, the NAEW&C Programme Management Agency (NAPMA) is accountable to the Board of Directors (BOD) for planning and coordinating the acquisition strategy, managing projects associated with modernisation of the E-3A fleet, providing sustainment support services, and overseeing the technical aspects of the NAEW&C airworthiness programme.

NAPMA is a programme management organisation mainly funded through contributions made by the Member Nations.

## **NATO UNCLASSIFIED**

NAPMA's 2019 implemented Final Lifetime Extension Programme (FLEP) Peacetime Establishment (PE) is 113 posts plus a few remaining posts closing the FUP projects; manned by seconded military officers and civilian personnel, drawn from all of the Nations participating in the Programme (A-Grades) and from all NATO Nations (B-Grades). While most are located in Brunssum, The Netherlands, a small number perform their duties in Manching (until August 2019) and in Geilenkirchen, Germany. The legal status of NAPMA, as an integral part of the North Atlantic Treaty Organisation, is laid down in the Ottawa Agreement as of 20 September 1951. Based on this agreement, NAPMA is, inter alia, exempt from all taxes and customs duties. The NAPMA General Manager (GM) is responsible for the Technical Airworthiness of the NAEW&C Force Fleet.

### **How NAPMA's operating environment affects its Financial Statements**

NAPMA's overall activities are funded by Member Nations through projects and related Administrative Budgets; "separate and distinct from the International Staff, other NPLSOs or other NATO Organs" and through other generated income. The budgets are approved annually by the NAPMO BOD. The Nations' Contributions are to remain within the overall Programme ceiling as agreed in the respective MMoU addendum amendment. The Administrative Budget covers all expenditures for the internal functioning of the Agency. The Project Budgets contain the appropriations for the modification of the NAEW&C Force fleet. Aside from its own budgeted activities, NAPMA also supports other NATO entities such as NAEW&C Force Command, and relies on the support of NATO Support Procurement Agency (NSPA) and NATO Communication and Information Agency (NCIA).

NAPMO has an agreement with the US Government (USG) that they can act as an exclusive general agent which has responsibility and authority to procure and manage aircraft modernisation efforts. This gives NAPMO a special arrangement in the Foreign Military Sales (FMS) process but more specifically the USG can act as the Agent for NAPMO resulting in Agent Contracts between NAPMO and US industry. The System Programme Office (SPO) at Hanscom Air Force Base, Massachusetts performs the day-to-day support functions for the US Agent. Since 2017 NAPMO also uses regular agreements under the FMS with the United States.

### **Compliance with Financial Regulations**

The NAPMA Financial Statements have been prepared on the accrual basis of accounting in accordance with the NATO Accounting Framework (NAF) as adopted by the North Atlantic Council (NAC). The NAF is based upon the International Public Sector Accounting Standards (IPSAS) issued by the IPSAS Board (IPSASB) and relevant to NAPMA as decided by the NAC in 2002 and revised again in 2013 and 2016 to adapt IPSAS 12 – Inventories, IPSAS 17 – Property Plant and Equipment, IPSAS 31 – Intangible Assets, and IPSAS 1 – Presentation of Financial Statements.

NAPMA Financial Statements have been prepared in accordance with the accounting requirements of the NAPMO Financial Regulations (NFRs), Version 2.0, approved by the NAC on 07 December 2017 and the NAPMO Financial Rules and Procedures (FRPs).

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

NAPMA's mission is to plan, acquire and deliver improvements to the NATO AEW&C capabilities following the guidance of the NAPMO Nations taking into account life cycle

## **NATO UNCLASSIFIED**

considerations.

In relation to the financial position NAPMA has several separate multi-year projects, both direct and indirect (administered by the US agent and US FMS), which require maintaining substantial annual cash levels to satisfy requirements which may be required in support of the procurement efforts towards the end of the current modernisation programme.

### **Analysis of NAPMA's Financial Statements**

Key points to note in respect of the Financial Statements are:

- NAPMA's functional and reporting currency used throughout these Financial Statements is stated in USD (\$) equivalent. Therefore realised and unrealised gains and losses resulting from the translation into USD equivalent and from the revaluation at the reporting dates of monetary assets and liabilities in currencies other than USD are recognized in the Statement of Financial Performance.
- Existing funds (revenue recognized in previous years) are used to cover dedicated project expenditures which are recognized in the Statement of Financial Performance.

### **Risks and Uncertainties that affect NAPMA's Financial Position and Performance**

COVID-19 pandemic may impact NAPMA Programme of Work and may have financial implications.

### **Final Lifetime Extension Programme (FLEP)**

At the Wales Summit in 2014, the NATO Council stated: "NATO's Airborne Early Warning and Control Force will continue to be modernized to maintain its full operational capability."

Accordingly, at the Warsaw summit it was stated that "NATO's Airborne Early Warning and Control Force (AWACS) continues to prove itself instrumental not only to monitor our airspace, but also as a critical part of NATO's command and control capabilities and that NATO AWACS will continue to be modernised and extended in service until 2035. By 2035, the Alliance needs to have a follow-on capability to the E-3 AWACS".

Upon receipt of the last signature of a financially contributing NAPMO Nation the 6th Amendment to the Addendum to the Multilateral Memorandum of Understanding (MMOU) entered into effect 23 September 2019, committing the Nations to the US \$ 1,000 Million at Base-Year 2016 ceiling amount for the FLEP. This allowed for the necessary Contract Authority to enter into the main contract for this Modernization Programme and secured the related Administrative budgets for the Agency.

The main contract with Boeing was formally awarded on 27 November 2019.

# NATO UNCLASSIFIED

## NAPMA Statement of Financial Position

as at 31 December 2019

(in USD equivalent)

			Restated	Original
	Note	2019	2018	2018
<b>ASSETS</b>				
<b>Current assets</b>				
Cash and cash equivalents	1	91,638,942	94,141,900	289,141,900
Receivables	2	12,748,298	1,542,445	1,542,445
Prepayments	3	3,346,136	4,484,294	4,484,294
Investments**	4	290,000,000	195,000,000	0
		<u>397,733,375</u>	<u>295,168,639</u>	<u>295,168,639</u>
<b>Non-current assets</b>				
Prepayments >12 Months	5	80,481	10,519	10,519
Property, Plant & Equipment	6	958,886	1,348,460	1,348,460
Other non-current assets*	7	<u>37,037,349</u>	<u>119,145,364</u>	<u>119,145,364</u>
		<u>38,076,716</u>	<u>120,504,343</u>	<u>120,504,343</u>
<b>TOTAL ASSETS</b>		<b><u>435,810,091</u></b>	<b><u>415,672,982</u></b>	<b><u>415,672,982</u></b>
<b>LIABILITIES</b>				
<b>Current liabilities</b>				
Payables	8	1,686,283	1,056,766	1,056,766
Accruals	8	13,759,466	25,573,770	25,573,770
Deferred Revenue	9	271,077,337	169,790,525	169,790,525
Advances	10	<u>14,396,150</u>	<u>0</u>	<u>0</u>
		<u>300,919,236</u>	<u>196,421,061</u>	<u>196,421,061</u>
<b>Non-current liabilities</b>				
Advances > 12 Months	11	72,540,862	79,653,471	79,653,471
Risk Mitigation Fund Nations	11	19,720,364	12,691,124	12,691,124
Reimbursables NATO Entities	11	976,584	1,168,775	1,168,775
Other non-current liabilities	12	<u>37,037,349</u>	<u>119,145,364</u>	<u>119,145,364</u>
		<u>130,275,159</u>	<u>212,658,734</u>	<u>212,658,734</u>
<b>TOTAL LIABILITIES</b>		<b><u>431,194,396</u></b>	<b><u>409,079,795</u></b>	<b><u>409,079,795</u></b>
<b>Net assets/equity</b>	13	<b><u>4,615,696</u></b>	<b><u>6,593,188</u></b>	<b><u>6,593,188</u></b>
<b>TOTAL LIABILITIES AND NET ASSETS</b>		<b><u>435,810,091</u></b>	<b><u>415,672,982</u></b>	<b><u>415,672,982</u></b>

\* The figures given in respect of indirect contracting via the U.S. System Program Office (SPO) are presented on a modified cash and not on an accrual basis; more information can be found in the Accounting Policies (see page 9).

\*\*Following IBAN recommendation to re-classify part of the cash and cash equivalent into financial assets (current) in order to fully comply with the NAF.

We hereby certify that to the best of our knowledge the attached financial statements and notes present a true and fair view of the financial performance and position of NAPMA as at 31 December 2019.

*Guerrero E Ruiz*  
on behalf of

BrigGen Michael Gschossmann  
General Manager NAPMA

*Kees Schutten*

Col Kees Schutten  
Financial Controller NAPMA

06 July 2020

# NATO UNCLASSIFIED

## NAPMA Statement of Financial Performance

for the year ended 31 December 2019

(in USD equivalent)

	<u>Note</u>	<u>2019</u>	<u>2018</u>
<b>Revenue</b>			
Revenue from Contributions	14	47,953,309	37,417,233
Financial Revenue	14	262,112	0
Other Revenue	14	18,527,383	15,070,848
<b>Total Revenue</b>		<b><u>66,742,805</u></b>	<b><u>52,488,081</u></b>
<b>Expenses</b>			
Projects - direct	15	50,275,725	31,740,927
Projects - indirect via SPO*	15	0	642,671
Administrative	15	18,054,505	19,130,180
Depreciation	15	389,574	184,289
Finance Expenses	15	0	31,793
<b>Total expenses</b>		<b><u>68,719,804</u></b>	<b><u>51,729,859</u></b>
<b>Surplus/(Deficit) for the period</b>	16	<b><u>(1,976,999)</u></b>	<b><u>758,222</u></b>

\* The figures given in respect of indirect contracting via SPO are presented on a modified cash basis

NATO UNCLASSIFIED

**NAPMA Statement of Changes in Net Assets/Equity**

for the year ended 31 December 2019

(in USD equivalent)

	Capital assets	Cash Reserves	Accumulated surplus/deficit	Total
<b>Balance at the beginning of the period 2018</b>	<b>552,990</b>	<b>5,646,521</b>	<b>(238,974)</b>	<b>5,960,538</b>
Changes in accounting policy/prior period errors				
<b>Restated balance</b>	552,990	5,646,521	(238,974)	5,960,538
Net gains/(losses) recognised directly in net assets/equity	0	0	0	0
Use of cash reserves	0	(5,455)	5,455	0
Net increase-decrease capital assets	795,469	0	(795,469)	0
Exchange difference on translating foreign operations	0	(162,322)	0	(162,322)
Net unrealised foreign exchange gains and losses	0	36,750	0	36,750
Surplus/(Defecit) for the period	0	0	758,222	758,222
<b>Change in net assets/equity for the year ended 2018</b>	<b>795,469</b>	<b>(131,027)</b>	<b>(31,793)</b>	<b>632,650</b>
<b>Balance at the end of the period 2018</b>	<b>1,348,459</b>	<b>5,515,494</b>	<b>(270,767)</b>	<b>6,593,188</b>
Changes in accounting policy/correction prior period errors				0
<b>Restated balance</b>	1,348,459	5,515,494	(270,767)	6,593,188
Net gains/(losses) recognised directly in net assets/equity	0	(52,347)		(52,347)
Use of cash reserves	0	(1,849,536)	1,849,536	0
Net increase-decrease capital assets	(389,574)	0	389,574	0
Exchange difference on translating foreign operations	0	(290,177)	0	(290,177)
Net unrealised foreign exchange gains and losses	0	342,032	0	342,032
Surplus/(Defecit) for the period	0	0	(1,976,999)	(1,976,999)
<b>Change in net assets/equity for the year ended 2019</b>	<b>(389,574)</b>	<b>(1,850,028)</b>	<b>262,112</b>	<b>(1,977,490)</b>
<b>Balance at the end of the period 2019</b>	<b>958,885</b>	<b>3,665,466</b>	<b>(8,654)</b>	<b>4,615,696</b>

NATO UNCLASSIFIED



# NATO UNCLASSIFIED

## NAPMA Statement of Cash Flow

for the year ended 31 December 2019

(in USD equivalent)

		Restated	Original
	2019	2018	2018
<b>Cash Flow from Operating Activities</b>			
Surplus/(Deficit) from Operating Activities	(1,976,999)	758,222	758,222
Change in net assets/correction	(52,347)		
<b>Add: Non-Cash Movements</b>			
Depreciation	389,574	184,289	184,289
(Increase)/Decrease in Accounts Receivable	(11,205,852)	17,187,817	17,187,817
(Increase)/Decrease in Prepayments	1,068,196	693,527	693,527
Increase/(Decrease) in Accrued Bank Charges	0	0	0
Increase/(Decrease) in Accounts Payables	629,517	(13,724,553)	(13,724,553)
Increase/(Decrease) in Unearned Contributions	101,286,812	(80,508,993)	(80,508,993)
Increase/(Decrease) in Advances and Reimbursables NATO Entities	14,120,590	(48,004,149)	(48,004,149)
Change of Value in Deliverable to NAEW&C Force*	51,247,056	115,771,262	355,698,617
Increase/(Decrease) in Goods Receipt	(11,814,304)	4,942,854	4,942,854
<b>Net Cash Flow from Operating Activities</b>	<b>143,692,242</b>	<b>(2,699,725)</b>	<b>237,227,630</b>
<b>Cash Flow from Investing Activities</b>			
Additions to Other investments not included in cash and cash equivalent**	(95,000,000)	(195,000,000)	0
(Purchase)/Disposal of Assets	0	(979,758)	(979,758)
Additions to Work in Progress (WIP)*	(51,247,056)	(115,771,262)	(355,698,617)
<b>Net Cash Flow from Investing Activities</b>	<b>(146,247,056)</b>	<b>(311,751,020)</b>	<b>(356,678,375)</b>
<b>Cash Flow from Financing Activities</b>			
Fund Transfer from Net Assets	(290,177)	(162,322)	(162,322)
<b>Effect of Currency Valuations</b>			
Currency Valuation Operating Activities	0	0	0
Currency Valuation Financing Activities	342,032	36,750	36,750
<b>Total Currency Valuations</b>	<b>342,032</b>	<b>36,750</b>	<b>36,750</b>
<b>Net Increase (Decrease) in Cash/Cash Equival.</b>	<b>(2,502,958)</b>	<b>(314,576,317)</b>	<b>(119,576,317)</b>
Cash and Cash Equiv. Beginning of Period	94,141,900	408,718,217	408,718,217
<b>Cash and Cash Equiv. End of Period</b>	<b>91,638,942</b>	<b>94,141,900</b>	<b>289,141,900</b>

\* Restated figures adjust the amounts for the correction of prior period presentation error, as per IBAN report IBA-A(2019)0108. Further details see page 11.

\*\*Following IBAN recommendation to re-classify part of the cash and cash equivalent into financial assets (current) in order to fully comply with the NAF.

# NATO UNCLASSIFIED

## **GENERAL INFORMATION**

The NAPMA Financial Statements for the year ending 31 December 2019 were authorized for issuance in accordance with NAPMO Financial Rules and Procedures by the General Manager and the Financial Controller on 30 April 2020. Due to exceptional circumstances caused by the global COVID-19 crisis, IBAN authorized a delay from the standard 31 March reporting date. Additionally, with approval from IBAN, the General Manager and the Financial Controller, on an exceptional basis and with the intent to correct a material misstatement or disclosure, can restate financial statements until 17 July 2020.

## **ACCOUNTING POLICIES**

### **Basis of Preparation**

NAPMA Financial Statements have been prepared on the accrual basis of accounting in accordance with the NAF, which is based on the IPSAS issued by the IPSAS Board. NAPMA Financial Statements are prepared in accordance with the accounting requirements of the NAPMO FRs and FRPs and uses an Enterprise Resource Planning System based in SAP to record and report financial information.

The accounting principles accepted as appropriate for the recognition, measurement and reporting of the financial position, performance, and cash flows are based on accrual accounting using historical costs, unless the NAF requires otherwise. The accounting principles have been applied consistently throughout the reporting period. This ensures that the Financial Statements provide information that is relevant to decision-making and that is reliable, comparable, and understandable in light of the qualitative characteristics of financial reporting.

For the accounting of the expenditures related to indirect contracts and FMS, in accordance with the NAF's adaptation of IPSAS 1 – Presentation of Financial Statements, NAPMA reports data on a cash basis where the agency is unable to satisfy that the data is presented on a reliable accrual basis. The modified cash basis reflects that FMS/indirect contracts goods and services delivered according to DD645 billing statements as provided by the US government and for which the US government has received cash payments.

Slight differences in summation may occur due to the fact that all the figures have been rounded to the nearest dollar.

The Financial Statements have been prepared on a going-concern basis which assumes that NAPMA will continue in operation for at least a year from the date the financial statements are Issued.

In accordance with the NAF, the Financial Statements necessarily include amounts based on estimates and assumptions made by the management and based on historical knowledge as well as on the most reliable information available. In exercising the judgement to formulate 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 on-going basis. These estimates and assumptions affect the amounts of assets, liabilities, revenues and expenses reported. The estimates are subject to a measure of uncertainty. The effect of changes to such estimates and assumptions in future periods could be significant to the Financial Statements.

## NATO UNCLASSIFIED

The most significant estimate used in these Financial Statements is the estimation of goods/services received that are not yet supported by an invoice at year-end.

### Accounting Period

The 2019 Financial Statements are based on the accounting records of NAPMA as of 31 December 2019. In accordance with the NAPMO FRs, the financial year at NAPMA begins on 1 January and ends on 31 December.

### Functional and reporting Currency

The functional and reporting currency used throughout these Financial Statements is the USD (\$) equivalent. The Financial Statements are prepared using data based on the actual multi-currency execution of the approved budget appropriations.

### Cash Flow Statement

IPSAS 2 – Cash Flow Statement allows the choice between presenting the cash flow based on the direct method or indirect method. NAPMA has selected the indirect method of presentation for these Financial Statements.

### Revenue and Expense Recognition

According to its charter NAPMA has an administrative budget and an operational budget for the annual programme objectives and operating plans of NAPMO. The operational (program) budget covers the disbursements which are directly related to the modernization of the NE-3A aircraft. The administrative budget covers the expenses for the administration, acquisition, execution, support and other management activities related to the modernization programmes. The administrative and operational budget are mainly funded through contributions made by the Member Nations.

NAPMA recognizes revenue when the administrative budget is used (e.g. expenses incurred) for its intended purpose as authorized by the BOD. NAPMA recognizes revenue when the operational budget is used (e.g. expenses incurred) for its intended purpose as authorized by the BOD except when in respect of the same outflow a liability to deliver assets to the NAEW&C Force is also recognized. In that case the operational expenses will be capitalized as work in progress. NAPMA also recognizes revenue when other economic benefits that can be measured reliably will flow to NAPMA.

Revenues and expenses are accrued when goods and services are received or when economic benefits or expenses are incurred.

Expenditures from the administrative budget for the acquisition of Property, Plant and Equipment (PP&E) are capitalized and recognized as revenue at the moment of acquisition. Depreciation is recognized in surplus or deficit for each period of the useful live of the PP&E. All other gains or losses will be returned to the Nations unless otherwise instructed by the NAPMO BOD. These gains/losses are since 2014 held in the Risk Mitigation Fund.

### Foreign Currency Transactions

Non USD expenditures are accounted for at the weekly posted NATO exchange rates for conversion to USD equivalents that apply on the date of the transaction.

## NATO UNCLASSIFIED

### **Reporting Foreign Currency items**

Foreign currency monetary items, like cash, trade creditors or debtors, will for reporting purposes be translated into US Dollar equivalents using the closing rate. Exchange differences are accounted for in the Risk Mitigation Fund. All unrealised exchange differences due to reporting purposes are included in surplus or deficit in the period in which they arise.

Non-monetary items that are measured in terms of historical cost in a foreign currency (e.g. PP&E), are translated using the exchange rate at the date of the transaction.

### **Changes in Accounting Policies and Corrections**

The same accounting policies are applied within each period and from one period to the next, unless a change in accounting policy is required by a standard, or if the change results in the financial statements providing more reliable and relevant information.

For the 2019 Financial Statements, held-to-maturity fixed term deposits with original maturities between three and six months are re-classified from cash and cash equivalents to current assets investments.

### **Changes in Accounting Standards**

NAPMA discloses when initial application of an IPSAS has or would have an effect on the current period of any prior period of the Financial Statements. For 2019 no new relevant standards had or would have had an effect on the Financial Statements.

### **Prior year adjustments**

1. Correction of 2018 comparative figures for cash and cash equivalents and current assets investments because of the reclassification of held-to-maturity fixed term deposits with original maturities between three and six months.
2. A presentation error was discovered during the audit of the Financial Statements 2018 and therefore retroactively corrected (restated) in the comparative figures in the Cash Flow Statement.

### **Assets – Current Assets**

The current assets of NAPMA are cash and cash equivalents, accounts receivables prepayments and short term investments. They are measured at fair value. Changes in fair value. are recognized in the Statement of Financial Performance.

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

Cash and cash equivalents comprise cash at current and saving bankaccounts and fixed-term deposits with an original maturity of three months or less.

#### **Receivables**

Receivables are reported at fair value in the Statement of Financial Position. No provisions are made against national debts as they are deemed to be collectable.

## NATO UNCLASSIFIED

In accordance with IPSAS, receivables are disaggregated into amounts non-exchange recoverables from Member Nations and receivables from NATO and Non-NATO Entities, Staff Members, bank interest and other receivables.

### Prepayments

Prepayments made to suppliers and to other NATO entities are reflected in the Statement of Financial Position.

### Investments

NAPMA's current investments are held-to-maturity fixed term deposits with original maturities between three and six months. After initial measurement, held-to-maturity investments are measured at amortized cost using the effective interest method.

### Assets – Non-Current Assets

In this category, NAPMA is reporting all assets which are not expected to realise within twelve months after the reporting period.

### Property, Plant and Equipment

Property, plant, and equipment (PP&E) includes tangible items that support programme management activities and are expected to be used in more than one reporting cycle. PP&E is recognized and capitalized in accordance with the criteria relating to control outlined in the NAF. Where an asset is acquired in a non-exchange transaction the asset is initially measured at its fair value.

After recognition as an asset, an item of PP&E is carried at its historical cost less any accumulated depreciation and impairment losses. Cost includes all expenditure that is directly attributable to the acquisition of the items.

The building and the land that NAPMA occupies are provided by the Host Nation as a "right of use".

All expenditures from the operational budget for modernising the NE-3A aircraft are capitalized as work in progress and transferred to the NAEW&C Force after the NAEW&C Force has taken over control of the related assets. No PP&E from the operational budget is capitalized in NAPMA's financial statements.

Depreciation of an asset begins the first month after it is available for use. PP&E categorizations for purposes of determining the appropriate depreciable life of the assets is listed in the table below as well as the associated capitalization thresholds per item. Straight-line depreciation method is used for all categories. However the depreciable life of an asset depends upon the particular category it is in.

## NATO UNCLASSIFIED

## NATO UNCLASSIFIED

The table for purchases in 2019 were as follows:

PP&E Category	Description	Threshold per item	Useful life
Buildings	Building	200,000	40
Installed Equipment	Equipment/building improvements as part of the building such as heating & cooling systems, security systems, renovation, replacements and fixtures	30,000	10
Vehicles	Transportation equipment	10,000	5
Furniture	Desks, Chairs, Cabinets, Safes, etc.	30,000	10
Automated Information Systems	NIMS, major Hardware and Software	50,000	3
Communication and IT Equipment	Equipment/Tools required for daily office operations such as PC's, Laptops, Software, etc.	50,000	3
Government Furnished Equipment	Miscellaneous Equipment provided to Contractors	50,000	10

### Leases

Leases are classified as finance leases whenever the terms of the lease transfers substantially all the risks and benefits incidental to ownership to the lessee.

All other leases are classified as operating leases. NAPMA does not have any finance leases.

### Work in Progress (other non-current assets)

Work in progress is the aggregate amount of expenses for the modernization of the NE-3A aircraft, accumulated during the executing of the modernization programmes. Work in progress that is ready for its intended use and controlled by the NAEW&C Force, will be transferred to the NAEW&C Force and subsequently derecognized in NAPMA's financial statements. Work in progress is valued at its historical acquisition value at the exchange rate in effect on the date of the expenditure transactions. The expenditures for US FMS contracts and indirect agent contracts are recorded corresponding financial data on a cash basis provided by the US Government under the US Government Acquisition Agreement. Work in Progress is presented on a modified cash basis in the financial statements.

Acquisition programmes have a full cost recovery basis for NAPMA, so no surpluses or deficits are recognized in relation to the work in progress with the provision that the budget is used for its intended purpose. Impairment or depreciation of the accumulated costs only starts after the operational capability has been transferred to the NAEW&C Force and put into service.

## NATO UNCLASSIFIED

## NATO UNCLASSIFIED

### Liabilities – Current Liabilities

#### Payables and Accruals

Payables are reported at fair value in the Statement of Financial Position. They represent amounts for which goods and services, supported by an invoice, have been received due to NATO and Non-NATO entities, commercial vendors and NAPMA Staff for goods received or services provided that remain unpaid as of the reporting date. Accruals are estimates of the cost for goods and services received but not yet supported by an invoice at year-end.

#### Deferred Revenue

Deferred revenue represents contributions from Nations and payments from third parties that are subject to specific conditions which have not been met during the reporting year. The recognition of revenue is deferred until those conditions have been satisfied.

#### Employee Benefits

NAPMA employees participate in one of the two NATO pensions funds: the Coordinated Pension Scheme (CPS) which is a benefit plan, and the Defined Contribution Pension Scheme (DCPS) which is a contribution plan. NATO IS operates the CPS for all NATO staff. NATO appointed Previnet SPA as the pension scheme administrator for the DCPS. The assets and liabilities for these pension schemes are accounted for centrally at NATO Headquarters and therefore are not recognized in these Financial Statements. NAPMA only accounts for the contributions paid during the year.

### Liabilities – Non-Current Liabilities

#### Advance Contributions

Advances on contributions represent the amounts of funds held on behalf of the Contributing Nations, which arise from a variety of sources including advances from some Nations on calls for the following fiscal year, sales of residual assets and Research and Development (R&D) recoupment.

#### Risk Mitigation Funds (RMF)

During BOD96, the NAPMO BOD approved the creation of a fund comprised of revenue generated from gross interest earned and investments to mitigate currency and exchange risks. Upon dissolution of the fund, the fund will be redistributed to the Nations according to the then current MoU cost shares.

The RMF is comprised of income generated from interest earned on bank accounts, investments in term/time deposits or money market accounts and gains or losses from foreign currency exchanges. The liquidity held in the fund will have no denomination or link to a particular programme rate or inflation factor.

#### Reimbursables NATO Entities

Advances received from NATO Entities to support Third Party Projects. Funds are received and expended on behalf of other NATO entities, predominantly the NAEW&C Force, for execution of projects and activities for Operations and Support.

## NATO UNCLASSIFIED

### **Deliverables to NAEW&C Force (other non-current liabilities)**

Deliverables to NAEW&C Force represent the obligation to transfer work in progress that is ready for its intended use after the NAEW&C Force has taken over control of the related assets.

Because work in progress is presented in the financial statements on a modified cash basis, deliverables to NAEW&C Force – being a derivative – is also presented on a modified cash basis.

### **Provisions and Contingent Liabilities**

Provisions are recognized when the NAPMA has a present obligation as a result of a past event, it is probable that an outflow of resources embodying economic benefits or service potential will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation.

NAPMA does not recognize a contingent liability, but discloses details of any contingencies in the notes to the financial statements, unless the possibility of an outflow of resources embodying economic benefits or service potential is remote.

### **Net Assets**

Net assets represent the net result of revenues and expenditures, and the accumulation of inventory, capital and retained earnings over the life-time of the NAPMA Programme.

Net assets are subdivided into capital asset reserves, cash reserves and accumulated gains/losses.

### **Nature and purpose of reserves**

A capital assets reserve has been established for the depreciation and impairment of capitalized PP&E from the administrative budget. The capital assets reserve is increased with the expenditures for acquired PP&E and decreased with the depreciation and impairment of the PP&E. The capital assets reserve equals the carrying amount of the PP&E. The capital assets reserve is not available for redistribution to nations, programmes or budgets.

Cash reserves are the accumulated surpluses and deficits generated until 2009 and additional contributions subsequently received from new joiners to the programme.

### **Surplus or Deficit for the Period**

Accounting surpluses or deficits can occur when funds from the cash reserve in net assets are used to cover non-contribution project expenditures.

Surpluses and deficits can also result from the currency translation adjustments at year-end in accordance with IPSAS 4 and purchases of administrative assets minus the depreciation expenses.



# NATO UNCLASSIFIED

## NOTES TO THE STATEMENT OF FINANCIAL POSITION

### Assets – Current Assets

#### 1. Cash and Cash Equivalents

<u>Cash and cash equivalents</u>	<u>2019</u>	<u>Restated</u> <u>2018</u>	<u>Original</u> <u>2018</u>
Current Accounts	192,966	191,057	191,057
Saving Accounts	91,445,976	93,950,842	93,950,842
Fixed-Term Deposits	0	0	195,000,000
<b>Total</b>	<b>91,638,942</b>	<b>94,141,900</b>	<b>289,141,900</b>

Cash balances are held in current and deposit accounts spread between various reliable financial institutions. Multiple currencies are held in separate accounts. As of the 31st of December 2019 NAPMA invested a part of the cash holding in high rated short fixed-term deposits. As per recommendation from the IBAN during the interim audit fieldwork the amount for the fixed-term deposits was re-classified into financial assets investments to be in compliance with the NAF.

#### Saving accounts held:

<b>Bank</b>	<b>Currency</b>	<b>USD equivalent</b>
DNB	EUR	16,696,335
	NOK	15,379,609
	USD	33,915,011
WELLS FARGO	USD	37,537,074
<b>Grand Total</b>		<b>91,445,976</b>

Savings are converted using NATO weekly posted exchange rates applicable on 31 December 2019.

The Calls for Contributions to participating Nations are issued according to the 2019 approved budget based on the Medium Term Financial Plan (MTFP) approved by the BOD and according to Art. 29 of the NAPMO FRs and Financial Rules and Procedures (FRPs).

## NATO UNCLASSIFIED

### 2. Accounts Receivable

<b><u>Accounts receivable</u></b>	<b><u>2019</u></b>	<b><u>2018</u></b>
Receivables from Nations	11,884,218	0
Receivables from NATO Entities	161,310	613
Receivables from Staff Members	0	0
Other Receivables/Recoverable	5,905	0
Receivables from Bank interest	696,864	1,128,881
Long outstanding Receivables	0	412,952
<b>Total</b>	<b>12,748,298</b>	<b>1,542,445</b>

Most receivables are due from Member Nations. It is deemed that all accounts receivable activities will be closed within 12 months from the end of the reporting period. No provisions are made against debts as they are deemed to be collectible.

The increase in the Receivables is primarily due to payments of contributions not received prior to the year-end.

Receivables from NATO Entities include a compensatory payment from the NATO Group insurance as per reference action memo EM(2019)0080-REV1 dated 25 November 2019 which was received on 07 April 2020.

### 3. Prepayments

<b><u>Prepayments</u></b>	<b><u>2019</u></b>	<b><u>2018</u></b>
NATO Entities	283,950	849,631
DFAS	2,903,258	3,449,054
ADMIN NON-NATO Entities	158,928	185,609
<b>Total</b>	<b>3,346,136</b>	<b>4,484,294</b>

Advance payments were made to NSPA (NATO Entities) and DFAS against Taskings and Case Directive Amendments (CDAs).

Advance payments to Non-NATO entities cover prepayments executed in 2019 related to administrative and operational transactions.

NATO UNCLASSIFIED

## NATO UNCLASSIFIED

### 4. Investments

<u>Investments</u>	<u>2019</u>	<u>Restated 2018</u>	<u>Original 2018</u>
Investments	290,000,000	195,000,000	0
<b>Total</b>	<b>290,000,000</b>	<b>195,000,000</b>	<b>0</b>

NAPMA's current investments are held-to-maturity fixed term deposits with original maturities between three and six months. The carrying amounts for these deposits are a reasonable approximation of their fair value due to their short term maturities.

The majority of the increase in investments is due to the payments of contributions received prior to year end which were invested in fixed term deposits.

<b>Bank</b>	<b>Duration</b>	<b>Currency</b>	<b>Total amount</b>
WELLS FARGO	Up to 6 Months	USD	90,000,000
JP MORGAN	Up to 6 Months	USD	30,000,000
DNB Bank	Up to 6 Months	USD	170,000,000
	<b>Grand Total</b>	<b>USD</b>	<b>290,000,000</b>

### Assets – Non-Current Assets

#### 5. Prepayments > 12 Months

<u>Prepayments</u>	<u>2019</u>	<u>2018</u>
ADMIN NON-NATO Entities > 12Months	80,481	10,519
<b>Total</b>	<b>80,481</b>	<b>10,519</b>

Prepayments executed in 2019 related to licences with validity through 2020.

NATO UNCLASSIFIED

## NATO UNCLASSIFIED

### 6. Property, Plant and Equipment (PP&E)

During 2019, there were no additions to PP&E.

Changes in Property, Plant and Equipment and related depreciation for the year were as follows:

	Automated Inf. System (NIMS)	Communication and IT Equipment	Furniture	Vehicles	Buildings	Installed Equipment	Totals
Opening Balance (01 January 2019)	28,439	794,797	29,241	105,161	387,804	3,018	1,348,460
Additions	0	0	0	0	0	0	0
Disposals/Corrections	0	0	0	0	0	0	0
Depreciation	28,439	309,919	11,813	23,144	15,097	1,161	389,574
<b>Closing Balance (31 December 2019)</b>	<b>0</b>	<b>484,878</b>	<b>17,428</b>	<b>82,017</b>	<b>372,706</b>	<b>1,857</b>	<b>958,886</b>
Gross Carrying Amount	7,500,612	929,758	668,851	115,722	603,899	12,149	9,830,991
Accumulated Depreciation	7,500,612	444,880	651,423	33,705	231,192	10,292	8,872,105
<b>Net Carrying Amount</b>	<b>0</b>	<b>484,878</b>	<b>17,428</b>	<b>82,017</b>	<b>372,706</b>	<b>1,857</b>	<b>958,886</b>

### 7. Work in Progress (WIP) (other non-current assets)

<u>Work in Progress</u>	<u>2019</u>	<u>2018</u>
Work in Progress (WIP)	37,037,349	119,145,364
<b>Total</b>	<b>37,037,349</b>	<b>119,145,364</b>

WIP – The value of work in progress for the acquisition projects will be transferred to the NAEW&C Force when the modernisation of the aircraft has been completed and is in use by NAEW&C Force.

The amount of 133,355,071 USD equivalent was transferred to the NAEW&C Force in 2019 in compliance with the control criteria of assets as outlined in the NAF.

Work in progress transferred to the NAEW&C Force may contain property that is paid by NAPMA, acquired by contractors and not expensed as incurred while modifying the NE-3A aircraft. This concerns NATO-owned property. Contractual terms oblige contractors to administer NATO property, in accordance with sound industrial practice and create and maintain property records in support of their stewardship responsibilities. These property records must be made available to NAPMA at least upon request. NAPMA has made timely requests to its contractors to submit property records of NATO property under their control. NAPMA has not received sufficient information to recognize these assets in accordance with the NATO Accounting Framework. Because the modernization programmes are full cost recovery programmes for NAPMA, the expenditures for the unrecognized assets have been transferred to the NAEW&C Force. NAPMA will continue to gather information on NATO property that is acquired by contractors in order to achieve the transfer of these assets to the NAEW&C Force.

## NATO UNCLASSIFIED

## NATO UNCLASSIFIED

In accordance with the NAF, NAPMA records the amounts of the expenditures related to indirect contracts in the Financial Statements based on data/billing reports as provided by the US Government. The amount of 37,608,939 USD equivalent is presented on a modified cash basis.

The below summary table shows additions and transfers occurred during the fiscal year as well as the accumulated amounts.

	Work in Progress (WIP)
Opening Balance (01 January 2019)	119,145,364
Additions	51,247,056
Transferred to NAEW&C	(133,355,071)
Disposals/Corrections	0
<b>Closing Balance (31 December 2019)</b>	<b>37,037,349</b>
Gross Carrying Amount	2,382,295,753
Accumulated Transfers	(2,345,258,404)
<b>Net Carrying Amount</b>	<b>37,037,349</b>

### Liabilities – Current Liabilities

#### 8. Accounts Payable and Accruals

<u>Accounts Payable</u>	<u>2019</u>	<u>2018</u>
Payables to NATO Entities	17,915	2,946
Payables to Non-NATO Entities	275,898	332,661
Payables to Suppliers	1,368,237	720,940
Payables to Staff	24,233	219
<b>Total</b>	<b>1,686,283</b>	<b>1,056,766</b>

NATO UNCLASSIFIED

## NATO UNCLASSIFIED

### Payables to NATO Entities

Payables to NATO Entities include an invoice from NSPA for shipment task that was not settled at year-end.

### Payables to Non-NATO Entities

Payables to Non-NATO Entities include the DFAS US-Reimbursables that were not settled at year-end.

### Payables to Suppliers

Payables to suppliers include invoices received from commercial vendors not settled at year-end. There is an increase in payables to suppliers because the majority of the invoices were not paid before year-end.

### Payables to staff members

Amounts due to staff members such as travel expenses. There is an increase in the payable to staff members due to travels performed late in the year and therefore not settled before the cut-off-date.

<b><u>Accruals</u></b>	<b><u>2019</u></b>	<b><u>2018</u></b>
Goods receipt – Invoices to be received	13,759,466	25,573,770
<b>Total</b>	<b>13,759,466</b>	<b>25,573,770</b>

Goods Receipt – Invoices to be received are the amounts based on estimates and assumptions made for goods/services that were delivered/performed during fiscal year 2019 and prior but not invoiced by the 31 December 2019.

The variance between the comparative figures is explained by the receipt in invoicing from the prime contractor before the cut-off date.

## 9. Deferred Revenue

<b><u>Unearned Contributions</u></b>	<b><u>2019</u></b>	<b><u>2018</u></b>
Unearned Contribution - Current	255,503,650	163,284,252
Unearned Contribution - SESAR	15,573,687	6,506,273
<b>Total</b>	<b>271,077,337</b>	<b>169,790,525</b>

Unearned Contributions - Currently represent the balance of Nations' Contributions associated to the various programmes, inclusive of administrative support, that have not yet been recognized as revenue. The BOD approved budgets and associated Call for Contributions are based on the Medium Term Financial Plan (MTFP). NAPMA issued only one 2019 call in September, as the first FLEP call to all nations, except for Norway and Denmark per their request.

## NATO UNCLASSIFIED

## NATO UNCLASSIFIED

The NAPMO-USAF cooperatively developed CNS/ATM received funding from the Single European Sky Air Traffic Management Research (SESAR), for the efforts in defining, developing and delivering new or improved technologies and procedures (SESAR Solutions). The evaluation performed by SESAR awarded the funding to NAPMO in one grant represented by two clusters paid in three instalments per cluster: Prefinancing, interim payment and balance payment. An interim payment on cluster 1 and 3 were received in 2019.

For the retention of the existing funds and the payment of the balance, NAPMA must submit a certified final technical report, a certified final financial statement and a certified summary financial statement (aggregation of previously submitted financial statements and received interim payments).

### 10. Advances

<u>Advances</u>	<u>2019</u>	<u>2018</u>
Advance Nation accounts	14,396,150	0
<b>Total</b>	<b>14,396,150</b>	<b>0</b>

Advances are funds held on behalf of the Participating Nations which arise from calls for next year's budget as stated in the NAPMO FR art. 29.5. NAPMA issued the first call for contribution for 2020 for the 6<sup>th</sup> amendment in November 2019. The call went to all nations and only requested 70% of the total Administrative Budget for 2020 as there was sufficient project funds on hand to cover any expenditures before the second 2020 call would be issued.

Advance nation accounts also include a compensatory payment received from the NATO Group Insurance provider following the recommendation option 1 to return the funds to nations as per reference EM(2019)0080-REV1.

### Liabilities – Non-Current Liabilities

#### 11. Advances > 12 Months and Reimbursables NATO Entities

<u>Advance Nation Accounts</u>	<u>2019</u>	<u>2018</u>
Advance Nation accounts	72,540,862	79,653,471
<b>Total</b>	<b>72,540,862</b>	<b>79,653,471</b>

Advances Nation accounts are funds held on behalf of the Participating Nations which arise from a variety of funding sources, sales of residual assets, R&D recoupment for the Radar System Improvement Project (RSIP). As per 2019 Administrative Budget Book, approximately 7 million USD equivalent were used to cover administrative expenditures.

NATO UNCLASSIFIED

## NATO UNCLASSIFIED

	<u>2019</u>	<u>2018</u>
<b><u>Risk Mitigation Fund Nations</u></b>		
Risk Mitigation Fund Nations	19,720,364	12,691,124
<b>Total</b>	<b>19,720,364</b>	<b>12,691,124</b>

During BOD96, the NAPMO BOD approved the creation of a Risk Mitigation Fund (RMF) to mitigate currency and exchange risks.

The RMF is comprised of income generated from interest earned on bank accounts, investments in term/time deposits or money market accounts and gains from foreign currency exchanges since 2014. The liquidity held in the fund will have no denomination or link to a particular programme rate or inflation factor.

Risk management procedures are implemented specifically pertaining to measuring and managing liquidity risk in both normal and adverse conditions.

The RMF balance on the 31 December 2019 is mainly made of interest generated in bank accounts held in USD.

In 2019, the RMF covered bank charges and negative interest in the amount of 102,902 USD equivalent.

	<u>2019</u>	<u>2018</u>
<b><u>Reimbursables</u></b>		
Reimbursables NATO Entities	976,584	1,168,775
<b>Total</b>	<b>976,584</b>	<b>1,168,775</b>

This account tracks the financial activities to support Third Party NATO Entities. Funds are received and expended on behalf of other NATO entities predominantly the NAEW&C Force for execution of projects and activities for Operations and Support.

### 12. Other non-current liabilities (Deliverables)

	<u>2019</u>	<u>2018</u>
<b><u>Deliverable to NAEW&amp;C Force</u></b>		
Deliverables	37,037,349	119,145,364
<b>Total</b>	<b>37,037,349</b>	<b>119,145,364</b>

Deliverables to NAEW&C Force represent the cumulative amount that is still to be transferred to NAEW&C Force when the modernisation of the aircraft has been completed and is in use by NAEW&C Force.

NATO UNCLASSIFIED



## NATO UNCLASSIFIED

Changes in Deliverables for the year were as follows:

	<b>Deliverables</b>
Opening Balance (01 January 2019)	119,145,364
Additions	51,247,056
Transferred to NAEW&C	(133,355,071)
Disposals/Corrections	0
<b>Closing Balance (31 December 2019)</b>	<b>37,037,349</b>
Gross Carrying Amount	2,382,295,753
Accumulated Transfers	(2,345,258,404)
<b>Net Carrying Amount</b>	<b>37,037,349</b>

### 13. Net Assets

Net assets represent the net result of revenues and expenditures, and the accumulation of inventory, capital and retained earnings over the life-time of the NAPMA Programme.

Net assets are subdivided into capital asset reserves, cash reserves and accumulated gains/losses. Further details can be found in the Statement of Changes in Net Assets/Equity (page 7).

During the reconciliation of cash balances, a difference was discovered in the amount of 52,347 USD equivalent. This difference is recognized directly in the net assets.

## NATO UNCLASSIFIED

### NOTES TO THE STATEMENT OF FINANCIAL PERFORMANCE

#### 14. Revenue

Revenue recognition is matched with the recognition of expenses against NAPMA budgets. Contributions when called are booked as unearned revenue and recognized when earned. The table below shows the breakdown of the operating revenue.

<b><u>Revenue</u></b>	<b><u>2019</u></b>	<b><u>2018</u></b>
Revenue from Contributions	47,953,309	37,417,233
Financial Revenue	262,112	0
Other Revenue	18,527,383	15,070,848
<b>Total</b>	<b>66,742,805</b>	<b>52,488,081</b>

Revenue from Contributions has been recognized for project and administrative activities.

Financial revenue represents the accumulated exchange rate gains and losses due to transactions recorded in foreign currencies during the year, which reflect an unrealised gain required for reporting purposes.

#### 15. Expenses

Expenses are recognized by nature within the following groups.

<b><u>Project Expenses</u></b>	<b><u>2019</u></b>	<b><u>2018</u></b>
Projects direct	50,275,725	31,740,927
Projects indirect (via SPO)	0	642,671
<b>Total</b>	<b>50,275,725</b>	<b>32,383,598</b>

Project expenses are divided into direct and indirect and are not capitalized under WIP. Indirect expenses are incurred under the US agreement and are presented on a "modified cash" basis.

No indirect expenses which have not been capitalized under WIP occurred in 2019.

## NATO UNCLASSIFIED

<b><u>Administrative Expenses</u></b>	<b><u>2019</u></b>	<b><u>2018</u></b>
Personnel	15,698,258	16,588,733
Operational	2,356,247	2,541,446
<b>Total</b>	<b>18,054,505</b>	<b>19,130,180</b>

The amounts for Personnel include expenses for salaries and emoluments for NATO civilian positions and temporary personnel, for other salary related and non-related allowances including overtime, medical examinations, recruitment, installation, removal and training.

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

	<b>2019</b>	<b>2018</b>
Salaries	10,627,876	11,280,940
Allowances	2,377,038	2,590,412
Pension contributions	1,100,552	1,108,718
Health care contributions	1,294,443	1,345,665
Loss-of-Job Indemnities	0	0
Other	298,349	262,997
<b>Total</b>	<b>15,698,258</b>	<b>16,588,733</b>

### **Employee Disclosure**

NAPMA personnel is enrolled in two NATO pension schemes. NAPMA contributes to the schemes for existing employees at amounts laid out in the NATO Civilian Personnel Regulations (NCPR's).

NAPMA does not control or manage any of the schemes or scheme assets and is not exposed to the risks and rewards of the schemes and hence does not record any assets or liabilities of the schemes on its statements of financial position. In 2019 NAPMA contributed 1,100,552 USD equivalent to the NATO pension schemes.

The remaining part of the administrative expenses relate to operational activities such as maintenance costs, travel expenses, communication and information systems. These expenses are needed to meet NAPMA's operational requirements.

The lease for three staff cars and photocopiers have been qualified as operating leases and are therefore also included in the administrative costs.

## NATO UNCLASSIFIED

<b><u>Depreciation Expenses</u></b>	<b><u>2019</u></b>	<b><u>2018</u></b>
Depreciation and amortization	389,574	184,289
<b>Total</b>	<b>389,574</b>	<b>184,289</b>

Assets of PP&E are depreciated over their useful life (see also Note 6 on page 19).

<b><u>Finance Expenses</u></b>	<b><u>2019</u></b>	<b><u>2018</u></b>
Finance Expenses	0	31,793
<b>Total</b>	<b>0</b>	<b>31,793</b>

Finance Expenses represent the accumulated exchange rate gains and losses due to transactions recorded in foreign currencies during the year which reflect an unrealised loss required for reporting purposes.

### 16. Deficit for the Period

The 2019 deficit in the amount of (1,976,999) USD equivalent results from:

- The currency translation adjustments at the end of the year in accordance with IPSAS 4 presented under Financial revenue in the amount of (262,112) USD equivalent;
- Non-contribution project expenses in the amount of 1,849,536 USD equivalent
- The depreciation expenses in the amount of 389,574 USD equivalent

## NATO UNCLASSIFIED

### EVENTS AFTER THE REPORTING DATE

NAPMA's reporting date is 31 December 2019 and the Financial Statements were authorized for issue by the General Manager on 30 April 2020.

In response to the current COVID-19 pandemic, NAPMA senior management has directed the NAPMA staff to work from home to the maximum extent practical from 17 March 2020 until further notice. Due to this arrangement, the preparation of NAPMA 2019 Financial statements are delayed by one month to 30 April 2020 (Reference NAPMA/GM(20)11-00/010).

No material events, favorable or unfavorable, which would have an impact on the statements have occurred between the reporting date and the date on which the Financial Statements were authorized for issue.

### RELATED PARTY DISCLOSURE

Under IPSAS 20 parties are considered to be related if one party has the ability to control or exercise significant influence over the other party in making financial and operating decisions. IPSAS 20 requires the disclosure of the existence of related party relationships, where control exists, and the disclosure of information about transactions between the entity and its related parties. This information is required for accountability purposes and to facilitate a better understanding of the Financial Position and Performance of the reporting entity.

The BOD members receive no remuneration and do not receive loans from the entity. Based on the BOD annual declarations for 2019, received from all the BOD Members, no significant related party relationships could be identified which could affect the operation of NAPMA.

Based on the annual declaration for 2019 received from the key management personnel of NAPMA, there were no significant related party relationships identified which could affect the operation of NAPMA.

Senior management is remunerated in accordance with the published NATO pay scales. They do not receive loans that are not available to all staff members.

The aggregate remuneration of key management personnel during the year was as follows:

#### Number of individuals at year end on a full time equivalent basis

Grade	2019	2018
A7	1	1
A6	3	3
A5	8	4
A4	7	8
A3	2	1
<b>Total</b>	<b>21</b>	<b>17</b>

NATO UNCLASSIFIED

## NATO UNCLASSIFIED

### Salaries and benefits paid to key management personnel

Remuneration type	2019	2018
Basic salaries	2,786,145	2,406,268
Allowances	531,340	619,253
Employer's contribution to insurance	336,129	289,401
Employer's contribution to pension	328,763	264,129
Other	3,922	5,001
<b>Total</b>	<b>3,986,299</b>	<b>3,584,053</b>

The General Manager is entitled to receive a representation allowance as per DC(2016)0100 and PO(2013) 0154. The amount spent in 2019 was 9,106 USD equivalent. Expenditures made against this allowance are supported by invoices.

### BUDGET EXECUTION STATEMENT

The execution of the budget during fiscal year 2019 is shown in annex A.

The budget and accounting bases differ for NAPMA. The Financial Statements for NAPMA are prepared on an accrual basis, based on the nature of expenses in the Financial Statements whereas the Budgets are prepared on a commitment basis. Budgets are approved annually by programme/project, but cover multi-year requirements. All budgets are approved in US Dollar equivalent at an established rate at the beginning of each project. Execution of the approved budgets is in multi-currencies and is expressed in USD equivalent at the established programme rate.

The BOD approves the budgets based on programme/projects including administrative costs. Budgets may be subsequently amended by the Board. On 28 January 2019 and 9 August 2019 the PFC approved a supplemental transfer of appropriation between projects. On 12 July 2019 the BOD approved supplemental budget for Risk Reduction.

In the Clearing House process, actual expenditures are recognized when USD equivalent payments are made through DFAS or via a Direct USD contract with Boeing, while the Budgeted Expenditures are recognized when payments are made to subcontractors, in multi-currencies, by NAPMA.

In the Budget Execution Statement, actual expenditures are recorded on an accrual basis. Budgeted expenditures are recognized when the Service Entry (Good Receipt) is posted and the budget is consumed by an individual project.

The following table reconciles the differences between budget expenses (commitment basis) and actual expenses (accrual accounting basis) which are driven primarily by timing differences in Clearing House, accruals and capitalization. Exchange rate differences are generated because the BES expenditures are calculated at programme rate while the Financial Statement expenditures are calculated at market rate (NATO Parity Rate).

## NATO UNCLASSIFIED

## NATO UNCLASSIFIED

2019 Expenditure Reconciliation								
	Expenditure Comparison		Difference		Explanation			
Fund Center	BES Expense at Program Rate (\$EQ)	Financial Stmt Expense at Market Rate (LC) (Incl WIP)	BES Expense @ Program Rate less Fin Stmt Expense @ Mkt Rate	Financial Stmt Expense at Program Rate (\$EQ)	Exchange Difference Program Rate to Mkt Rate	Currency Clearing House Difference	Accrual Difference	Delta
PROJECTS	117,746,595.52	101,522,779.35	16,223,816.17	101,962,351.06	(439,571.71)	(3,955,281.64)	(11,828,963.67)	(0.85)
ADMIN	18,704,690.11	18,054,505.21	650,184.90	18,626,361.94	(571,856.73)		(78,328.17)	(0.00)
<b>TOTAL</b>	<b>136,451,285.63</b>	<b>119,577,284.56</b>	<b>16,874,001.07</b>	<b>120,588,713.00</b>	<b>(1,011,428.44)</b>	<b>(3,955,281.64)</b>	<b>(11,907,291.84)</b>	<b>(0.85)</b>

### WRITE OFF

Assets which are currently providing operational service potential are deemed to be the reporting responsibility of NAEW&C Force, NAPMA only reports write-offs of NAPMA fixed admin assets and inventory. This results from the implementation of the NAF.

### FINANCIAL INSTRUMENTS DISCLOSURE

NAPMA's financial requirements are set by its Member Nations. NAPMA does not borrow money to meet any financial obligation. Other than financial assets and liabilities which are generated by day-to-day operational activities, no long term financial instruments are held. The Risk Mitigation Fund's purpose is to mitigate currency and exchange risks.

#### Liquidity risk

NAPMA's financial requirements and capital expenditures are met by its Member Nations and are typically funded in advance. NAPMA is therefore not exposed to material liquidity risks.

#### Credit risk

NAPMA Nations are member and partner Nations of NATO, hence NAPMA is not exposed to material credit risks. Credit risk of financial institutions is mitigated by the Risk Mitigation Fund.

#### Foreign currency risk

NAPMA has limited exposure to foreign currency because some of its work is denominated in currencies other than the USD. However, risk related to foreign currency transactions is ultimately borne by NAPMA Nations.

### CONTINGENCIES

There is a claim by Mrs. C. Niessen, dated 5 April 2018, represented by DAS, Onderwijsboulevard 2015, 5223 DJ Den Bosch, claiming materiel and immateriel damages resulting from a fall at NAPMA premises while working for the cleaning company Hectas.

NATO UNCLASSIFIED

Annex A to the Financial Statements  
Budget Execution Statement

2019 Budget Execution Statement											
Funds Center	Appropriations current Budget Year(\$EQ)	Total Changes to Previous Appropriations (\$EQ)	Uncommitted Appropriations Carried Forward from Previous FY(\$EQ)	(TOTAL) Commitments Carried Forward from Previous FY(\$EQ)	Lapse in current FY (\$EQ)	Total Appropriations Available FY (\$EQ)	Expense Program Rate (\$EQ)	Uncommitted Appropriations Carried Forward (\$EQ)	(TOTAL) Commitments Carried Forw. into Following FY(\$EQ)	Total Appropriations Used FY (\$EQ)	Total Appropriations Available -Total Appropriations Used(\$EQ)
	\$	\$	\$	\$	\$	\$	\$	\$	\$	\$	\$
PROJECTS	267,774,352.15	(50,864,273.08)	90,698,461.17	90,687,940.84	(1,761,114.63)	396,535,366.45	(117,746,595.52)	(19,349,932.41)	(259,481,442.03)	(396,577,969.96)	(42,603.51)
ADMIN	22,108,232.46	-	-	420,517.25	(3,458,347.06)	19,070,402.65	(18,704,690.11)	-	(382,426.29)	(19,087,116.40)	(16,713.75)
<b>GRAND TOTAL</b>	<b>289,882,584.61</b>	<b>(50,864,273.08)</b>	<b>90,698,461.17</b>	<b>91,108,458.09</b>	<b>(5,219,461.69)</b>	<b>415,605,769.10</b>	<b>(136,451,285.63)</b>	<b>(19,349,932.41)</b>	<b>(259,863,868.32)</b>	<b>(415,665,086.36)</b>	<b>(59,317.26)</b>

(3)

Note 1: Technical discrepancy due to ERP settings.

Note 2: Due to the requirement for manual Carry Forwards in NIMS, errors in document processing across fiscal years occur.

Note 3: Appropriation transfer between projects per BOD/100 approval

NATO UNCLASSIFIED



## **STATEMENT OF INTERNAL CONTROL**

### **Scope of Responsibility**

1. As General Manager of NAPMA, I am responsible and accountable to the agency's Board of Directors (BOD) for designing, implementing and maintaining an efficient, effective and economical system of Internal Control that supports the achievement of NAPMA's objectives. To this end, I have established an effective, efficient and economical Internal Control System in accordance with NAPMO Financial Regulations (NFR) and NAPMO Financial Rules and Procedures (FRP) based on the principles of COSO Enterprise Risk Management (ERM) and Internal Control System as described below.
2. As the NAPMA Financial Controller I am responsible to the General Manager and accountable to the NAPMO Policy and Finance Committee (PFC) for establishing a system of internal financial and budgetary control, delegate authority to officials who may disburse and receive funds on my behalf, maintaining comprehensive accounting records of all assets and liabilities and the correct use of funds made available to the agency in accordance with the NFR and FRP.

### **Purpose and Limitation of the System of Internal Control**

3. The Internal Control System defines a process carried out by NAPMA's management and staff designed to provide reasonable assurance that the Agency will achieve its objectives while using the agency's resources in an efficient and effective manner.
4. NAPMA's system of internal control specifically addresses the efficiency and effectiveness of operations, accuracy and reliability of financial reporting and compliance with its legal framework and applicable laws and regulations.
5. Common limitations for an internal control system are collusion, human error and management override.
6. The cost of the internal controls should not outweigh the risks they are mitigating.

### **Oversight over NAPMA's Internal Control**

7. Oversight on NAPMA's internal control is exercised by the NAPMO BOD and the PFC pursuant to Articles 28 and 30 of the NAPMO Charter and paragraph 39 of the NAPMO Corporate Governance Policy (NCGP). The PFC's oversight role as the Agency's Audit Advisory Panel are pursuant to Article 16 of the NFR and paragraph 40 of the NCGP.
8. In June 2018, the BOD tasked NAPMA to update the NCGP. In Oct 2018, NAPMA presented a draft NCGP to the PFC with proposed changes in the areas of internal audit, audit committee roles and application of the COSO Enterprise Risk Management framework. While this revised NCGP awaits formal PFC endorsement and BOD approval, NAPMA has already began implementing parts of the revised NCGP with the NAPMO Nations' agreement.

## **Risk Management**

9. NAPMA manages risks at two distinct levels: the enterprise and the functional levels. NAPMA has established an Enterprise Risk Manager and an enterprise risk management plan to manage risks that can jeopardize NAPMA's abilities to successfully execute the modernisation of the NE-3A aircraft and other missions assigned by the NAPMO BOD to include its Technical Airworthiness responsibilities.
10. Division Heads and Office Chiefs are responsible for managing risks within their functional areas and complying with the internal controls in place.

## **Internal Control System**

11. Other key elements of the Agency's Internal Control System include, but are not limited to:
  - Commitment of NAPMA's senior leadership to integrity and ethical values;
  - Standards of Behaviour in line with the NATO Code of Conduct with an annual signed declaration of adherence by each staff member;
  - Annual confirmation of the responsibility and accountability for NAPMA's system of internal control by the General Manager and the Financial Controller by signature of the Statement of Internal Control;
  - Annual signature by NAPMA key personnel of a statement on related party disclosure;
  - NAPMA Program Office Estimate (POE) for the financial planning and management of modernization programmes;
  - Presentation of an annual Mid Term Financial Plan to the PFC and approval of administrative and project budgets by the BOD;
  - Signature on an annual basis by the General Manager and the Financial Controller of a NAPMA Management Representation Letter that provides assurance regarding the integrity, reliability, accuracy, completeness and consistency of information contained in the Financial Statements;
  - The NFR and FRP;
  - NAPMA Management Directives and Operating Instructions;
  - The use of the NAPMA Integrated Management System (NIMS) which incorporates the standard SAP Enterprise Resource Planning system with a budgeting module especially designed to manage, monitor and safeguard the funds appropriated to NAPMA;
  - A Treasury Policy Group that periodically reviews cash management and issues regarding the financial institutions which are responsible for cash deposits;
  - Signature on an annual basis by designated responsible managers within the NAPMA organization of a statement of assurance declaring their assessment of the execution of their internal controls.

**Internal Audit**

12. NAPMA has a permanently staffed internal audit function that independently evaluates the adequacy and effectiveness of the organization's governance, risk management, and internal controls to help the GM to protect assets, reputation and sustainability of the organization.

**Important Developments that Influenced NAPMA's Internal Control in 2020**

13. NAPMA concluded the Boeing contract for the Final Lifetime Extension Programme (FLEP) of the NAEW&C E-3A Fleet on 21 November 2019. The FLEP is valued at \$1 Billion (Base Year 2016) with \$750 Million allocated to the main contract with Boeing and its European subcontractors. The execution of the FLEP-contract requires extra controls especially with regard to non-expendable NATO property held at the contractors' locations.

**Review of the Effectiveness of the System of Internal Control**

14. The Financial Controller is responsible for evaluating the system of financial control.
15. The main basis for the assessment of the effectiveness of the system of internal control by the Financial Controller is direct observation. Other sources include, but are not limited to, reporting by internal and external auditors, signed statements of assurance by designated responsible managers within NAPMA and identifying risks and mitigation controls as described in Guideline FC #1 Financial and Budgetary Control.
16. It is the Financial Controller's assessment that strong controls exist over accounting, budgeting, treasury and the non-expendable items controlled by NAPMA. Some items controlled by NAPMA are held at contractors' locations. The Financial Controller found that strong controls exist for the accounting and safeguarding of NAPMA furnished property but that the accounting for the completeness of Contractor Acquired Property to which NATO has title is challenging.

**General Manager's Internal Control Priorities for the Year 2020**

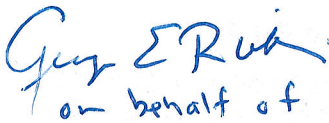
17. The General Manager's Internal Control Priorities for the Year 2020 are:
  - Continue the implementation of a tailored NAPMA ERM and Internal Control System in compliance with the principles of the COSO framework;
  - Implement specific internal control measures for FLEP, notably asset control.

NATO UNCLASSIFIED

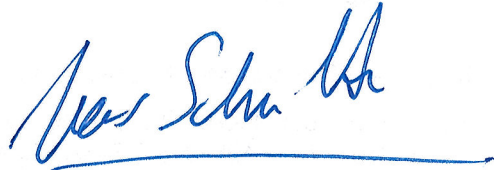
Annex B to the Financial Statements  
Statement of Internal Control

**Conclusion**

18. Based on the above, we consider, to the best of our knowledge and information available and within the scope of our respective responsibilities, that the agency operated satisfactory systems of internal control for the year ended 31 December 2019 and up to the date of approval of the Financial Statements.

  
on behalf of

BrigGen Michael Gschossmann  
General Manager NAPMA



Col Kees Schulten  
Financial Controller NAPMA

06 July 2020