



United Kingdom
**Debt
Management
Office**

Public Works Loan Board Report & Accounts 2011-2012

**Public Works Loan Board
Report and Accounts 2011 – 2012**

Presented to Parliament pursuant to
Section 3(6) of the National Loans Act 1968

Ordered by the House of Commons
to be printed on 21 June 2012

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http://www.dmo.gov.uk/index.aspx?page=publications/Annual_Reports

ISBN: 9780102978001

Printed in the UK for The Stationery Office Limited
on behalf of the Controller of Her Majesty's Stationery Office

ID 2490927 06/12

Printed on paper containing 75% recycled fibre content minimum.

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Foreword

The Public Works Loan Board (PWLB) is an independent and unpaid statutory body, which originated in 1793 and became established on a permanent basis in 1817. Since 1946 it has consisted of up to twelve Commissioners appointed by the Crown. The functions of the Commissioners are to consider loan applications from local authorities and other prescribed bodies and, where loans are made, to collect the repayments. The PWLB has operated within the United Kingdom Debt Management Office since July 2002.



Introduction

This publication presents the annual Report and Accounts of the Public Works Loan Board for the year ended 31 March 2012. The accounts have been prepared by the Public Works Loan Board (PWLB) under a direction issued by HM Treasury in accordance with Section 3 (6) of the National Loans Act 1968 ('the 1968 Act'). In addition, the publication meets the duty of the Public Works Loan Commissioners, under section 5 (3) of the Public Works Loans Act 1875 ('the 1875 Act'), to report annually to Parliament.

The Report and Accounts show amounts advanced by the PWLB and the repayments received from borrowers. The accounts do not show the resources that have been used to deliver the PWLB's objectives, which are reported in the United Kingdom Debt Management Office Report and Accounts 2011-2012.

by the Crown to hold office for four years. Retiring Commissioners are eligible for re-appointment.

Monies are provided by Act of Parliament and drawn from the National Loans Fund. The National Loans Fund is HM Government's main borrowing account and is administered by HM Treasury.

Background of the Public Works Loan Board

The PWLB is an independent statutory body that originated in 1793 and became permanently established in 1817. It dates in its present form from the 1875 Act. Since 1946 it has consisted of a maximum of twelve Commissioners appointed

The administration of the PWLB is the responsibility of the United Kingdom Debt Management Office (DMO).

Commissioners in post

The Commissioners holding office during the year were as shown below.

Original appointment began		Current appointment ends
1996	Chairman - John Parkes CBE DL Former Treasurer and Pro-Chancellor, University of Hull Director, EMIH Ltd Former Chief Executive, Humberside County Council	2013
1997	Deputy Chair - Rachel Terry Independent consultant, housing finance Former Associate, Tribal Treasury Services Limited Former Partner, Touche Ross & Company	2013

2000	<p>Sarah Wood OBE Former Director of Economic and Environmental Policy, Local Government Association</p>	2012
2001	<p>Mei Sim Lai OBE DL Principal, Lai Peters & Co. Chartered Accountants</p>	2013
2003	<p>Tony Caplin Former Chairman, Panmure Gordon plc Former Chairman, Urban Wimax Chairman, North West London Hospitals NHS Trust</p>	2015
2009	<p>Richard Gibson Former member, Senior Civil Service, Office of the Deputy Prime Minister</p>	2013
2009	<p>John Campbell Former Director of Corporate Resources, Scottish Borders Council</p>	2013
2010	<p>Anna Forge Consultant, Pinsent Masons LLP</p>	2014
2010	<p>Keith Starkey Former Chief Executive, Chesham Building Society</p>	2014
2010	<p>Maureen Wellen Former Assistant Director, Chartered Institute of Public Finance and Accountancy</p>	2014
2011	<p>Hugh O'Sullivan Former Director of Finance and Economic Development, Merthyr Tydfil County Borough Council</p>	2015

Officials of the PWLB were:

Secretary and Accounting Officer
Assistant Secretary

Mr Mark Frankel
Mr Tony Dinnage

The function of the Commissioners

The function of the Commissioners, derived chiefly from the Acts of 1875 and 1968, is to consider loan applications from local authorities and other prescribed bodies and, where loans are made, to collect the repayments. Nearly all borrowers are local authorities requiring loans for capital purposes. The security for money borrowed by a local authority, together with interest, is charged indifferently on all its revenues; all securities created rank equally without any priority. The Commissioners are legally required before making a loan to satisfy themselves that there is sufficient security for its repayment. The management of credit risk is described in Note 10 to the accounts.

The Commissioners are unpaid and act collectively to discharge their duties. The Commissioners have delegated to the Secretary day-to-day responsibilities for authorising loans and collecting due payments. The Secretary acts as the Accounting Officer of the PWLB and attends meetings of the Commissioners, which take place quarterly.

Governance and membership of the Public Works Loan Board

Operationally, the PWLB is a unit of the United Kingdom Debt Management Office (DMO), an executive agency of HM Treasury, and its staff are employees of the DMO. The Commissioners retain their statutory role while expecting the Secretary to supervise the operations of the PWLB subject to the same controls as apply to the DMO's operations as a whole. In so far as the Secretary relies on the effectiveness of the DMO's internal control framework, he looks to its Chief Executive, as Accounting Officer, to manage the DMO to the required standards.

By virtue of a Royal Warrant dated 28 February 2012, Hugh O'Sullivan was appointed as Commissioner, and Tony Caplin re-appointed, for the period 2011-2015.

Statutory provisions for loans

Section 3 (11) and Schedule 4 of the 1968 Act authorise the Commissioners to make loans to any local authority in Great Britain for any purpose for which the authority has power to borrow and to certain other authorities and persons for limited purposes. The Commissioners also have the powers to lend to certain harbours but as a matter of policy do not do so.

The amount which the Commissioners may lend, or undertake to lend, is provided by Section 4 of the 1968 Act, which permits the Commissioners to make loans up to a limit of the aggregate of:

- any commitments of the Commissioners outstanding in respect of undertakings entered into by them to grant local loans; and
- any amount outstanding in respect of the principal of any loans.

Section 4(1) of the 1968 Act limits the aggregate amount that may be outstanding in respect of commitments entered into by the Public Works Loan Commissioners. The Local Loans (Increase of Limit) Order 2008 increased that limit from £55,000 million to £70,000 million.

The PWLB borrows from the National Loans Fund in order to fund its loans. All loan repayments to the PWLB are paid over to the National Loans Fund to reduce this borrowing. All interest and premiums on early redemption paid to the PWLB are paid to the National Loans Fund. The PWLB borrows from the National Loans Fund in order to fund any discounts payable on early redemptions.

In accordance with Sections 3(2) and 5 of the 1968 Act, interest on loans made by the Commissioners is payable at rates set by the DMO using methodologies agreed with HM Treasury. There are regular twice-daily redetermination of rates, published at 9.30a.m. and 12.30p.m. Determinations include a separate set of rates to apply to early repayments.

The two types of loan available from the PWLB are:

- Fixed rate loans, for which the maximum repayment period is 50 years and on which the rate of interest is fixed for the duration of the loan. Repayments for fixed rate loans are due at half-yearly intervals; and
- Variable rate loans, for which the maximum repayment period is 10 years, and on which the rate of interest may be varied at one, three or six month intervals. Repayments are made at intervals corresponding to that selected for the variation of the rate. Once an interval is chosen, it remains unchanged throughout the life of the loan.

Policy and lending arrangements

The Commissioners are normally prepared to lend to an authority up to the available capacity in its legal borrowing limit as determined under Part 1, Chapter 1 of the Local Government Act 2003. The Commissioners require a verbal statement of confirmation from the borrowing authority, on taking out debt, that it is complying with the appropriate requirements of the

PWLB's Circulars and the relevant legislation with regard to the authority's borrowing powers.

Borrowers can request to repay loans before their due date. The PWLB has discretion to accept early repayments, but only on terms which do not favour the borrower over the National Loans Fund. The PWLB's lending policy and operational arrangements are publicised in Circulars issued with the Commissioners' approval and displayed on the website at www.pwlb.gov.uk.

Audit arrangements

The accounts are audited by the Comptroller and Auditor General in accordance with Section 3 (6) of the 1968 Act.

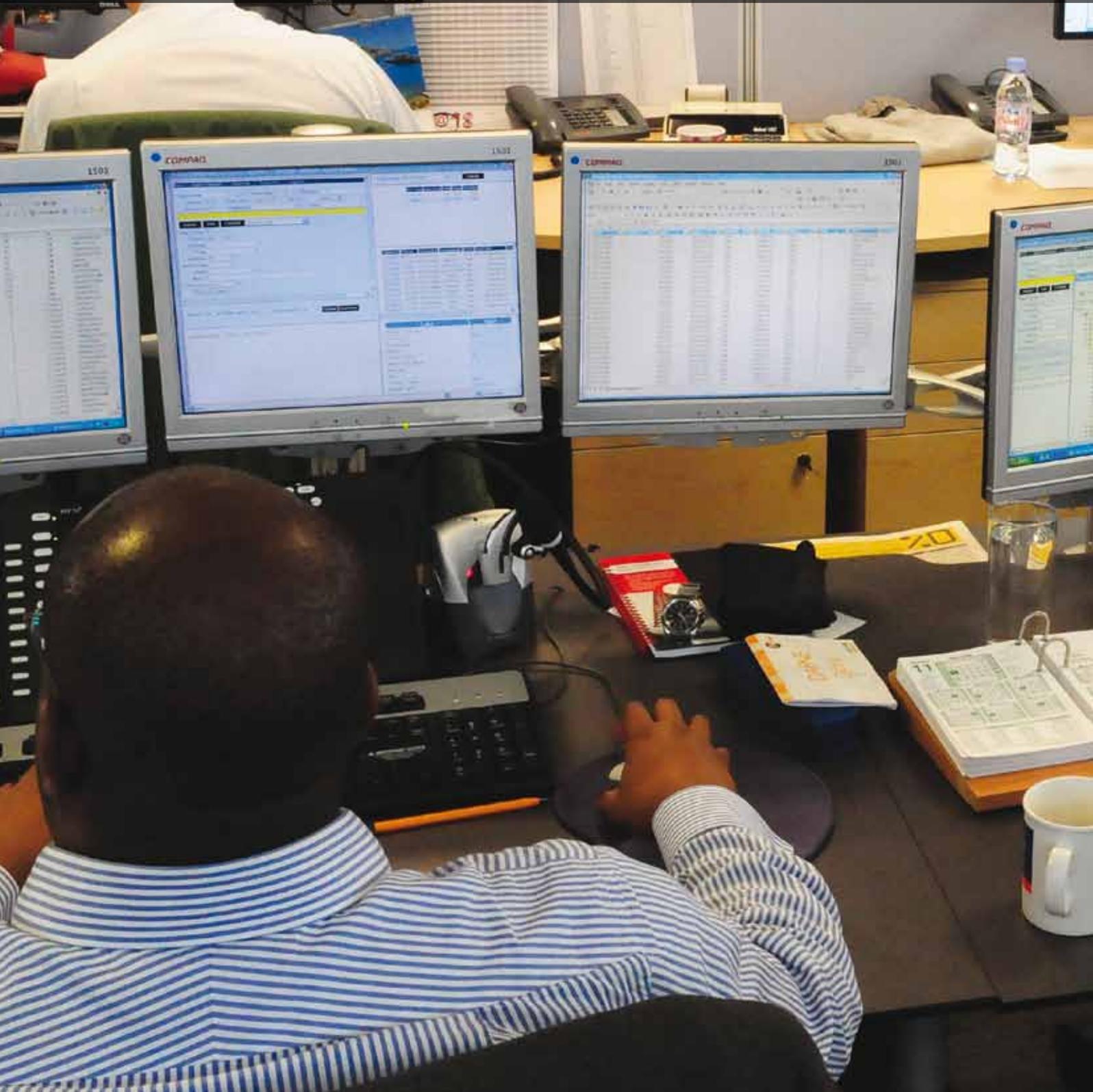
The Secretary has taken all the steps that he ought to have taken to make himself aware of any relevant audit information and to establish that the PWLB's auditors are aware of that information. So far as he knows, there is no relevant audit information of which the PWLB's auditors are unaware.

United Kingdom

Debt Management Office

Management commentary

The Public Works Loan Board received interest income of £4,503 million during 2011-2012. In the year, the Public Works Loan Board agreed new loans to borrowers of £16,111 million. The total of loan principal outstanding at 31 March 2012 was £61,917 million.



Summary of results in 2011-2012

The PWLB received interest income in the year of £4,503 million (2010-2011: £2,978 million). This comprised £2,781 million of contractual interest income (2010-2011: £2,809 million), £1,722 million of premiums received due to the early redemption of loans (2010-2011: £179 million) and less than £1 million of discounts paid due to the early redemption of loans (2010-2011: £10 million).

Year on year, the PWLB's interest income increased by £1,525 million. This was principally the result of a £1,543 million increase in premiums received from early redemptions. This increase was largely due to the PWLB's involvement in the Housing Self-financing operation, as described on page 16. Otherwise, contractual interest income decreased by £28 million and discounts paid reduced by £10 million.

The PWLB agreed new loans to borrowers with a principal value of £16,111 million (2010-2011: £5,255 million).

The PWLB's borrowers redeemed early loans with a principal value of £5,610 million in 2011-2012 (2010-2011: £1,730 million).

At 31 March 2012, the PWLB held loan assets of £62,625 million (31 March 2011: £53,693 million), inclusive of accrued income receivable of £708 million (31 March 2011: £557 million). The PWLB also held a cash balance of £49 million (31 March 2011: £51 million) comprising monies in transition between the National Loans Fund and the PWLB's borrowers.

Figure 1 sets out the advances made, the repayments received and the loan amounts outstanding according to types of borrower in England, Wales and Scotland. It includes the fair value of the PWLB's

loan portfolio, which is equivalent to the net present value of all future contractual cash flows for each loan.

At 31 March 2012, the average period to maturity of fixed rate loans had risen to 24.6 years (31 March 2011: 24.5 years). There had also been a reduction in the weighted average interest rate of the PWLB's loans outstanding at the balance sheet date to 4.62% (31 March 2011: 5.20%).

The assets of the PWLB are funded by borrowing from the National Loans Fund. Therefore all the PWLB's assets are matched by a corresponding liability to the National Loans Fund.

The PWLB's fee income and administrative expenditure are accounted for within the DMO's overall budget, as agreed with HM Treasury. In 2011-2012, the DMO received fees and charges of £6 million from the PWLB's borrowers in respect of new loans issued (2010-2011: £2 million).

Factors influencing financial performance

Movements in the PWLB's statement of financial position and its corresponding pattern of income are driven by the demand for new loans and the repayment (early or otherwise) of existing loans. The demand for new loans is influenced by local authorities' need for capital finance, changes in market borrowing rates and borrowers' expectation of future interest rate changes. These factors, considered alongside any premium or discount payable for early redemption and the rates available for money on deposit, also influence the pattern of demand for early redemption of existing loans and for refinancing.

Figure 1: Summary of transactions and balances outstanding

	In the year 2011-2012			Balances outstanding as at 31 March 2012		
	Advances £m	Repayments of principal £m	Repayments of interest £m	Principal due but not yet paid £m	Principal outstanding £m	Interest due but not yet paid £m
Loans on local revenues to:						
Local authorities in England						
County Councils	728	218	411	12	9,882	41
GLA and London Borough Councils	1,849	3,772	1,736	-	7,577	13
Metropolitan District Councils	1,635	1,970	1,050	1	10,417	30
Non-Metropolitan District Councils	10,626	479	331	17	16,972	25
Parish and Town Councils	16	6	5	-	120	-
Others	426	505	265	7	5,775	63
	15,280	6,950	3,798	37	50,743	172
Local authorities in Wales						
Principal Councils	46	45	135	1	2,637	15
Community Councils	1	-	-	-	4	-
Others	9	10	4	-	92	-
	56	55	139	1	2,733	15
Local authorities in Scotland						
Principal Councils	775	309	394	4	8,171	26
Others	-	16	21	-	226	-
	775	325	415	4	8,397	26
Total loans on local revenues	16,111	7,330	4,352	42	61,873	213

	In the year 2011-2012			Balances outstanding as at 31 March 2012		
	Advances £m	Repayments of principal £m	Repayments of interest £m	Principal due but not yet paid £m	Principal outstanding £m	Interest due but not yet paid £m
Loans on property to harbour authorities						
England	-	-	-	-	-	-
Wales	-	-	-	-	-	-
Scotland	-	-	-	-	2	-
Total loans on property	-	-	-	-	2	-
Total loans on local revenues and property	16,111	7,330	4,352	(a)42	61,875	(a)213
Add Totals from 1817 to 31 March 2011*	215,129	161,994	114,881			
Principal remitted or extinguished To 31 March 2011	n/a	(b)58	n/a			
In the year 2011-2012	n/a	-	n/a			
Total at 31 March 2012	231,240	169,266	119,233			

* This shows the total advances, repayments of principal and repayments of interest since the PWLB was permanently established in 1817 till 31 March 2011.

(a) Repayments in arrear at 31 March 2012, arose for reasons of timing: see page 23.

(b) The principal remitted or extinguished up to 31 March 2011 includes £55 million extinguished on privatisation of water authorities.

The net present value of future cash flows of this portfolio of loans at 31 March 2012 was £76,855 million.

Applications for loans

The PWLB agreed 477 applications for loans (2010-2011: 489 applications), totalling £16 billion (2010-2011: £5 billion). 310 authorities applied for advances (2010-2011: 301 authorities), including 90 non-principal authorities (2010-2011: 134 non-principal authorities). Of the 539 principal authorities, 220 applied to the PWLB during the year. 122 principal authorities had no debt outstanding to the PWLB as at 31 March 2012.

Housing Self-financing

During the year, PWLB worked with the Department for Communities and Local Government (DCLG) on a plan to replace council housing subsidy with self-financing housing revenue accounts. The plan involved re-allocating the debt of local housing authorities, which required PWLB to process a large number of repayments and new loans for settlement on 28 March 2012:

	£bn
New loans	13.0
Loan principal repaid	(5.0)
Net increase in loan principal	8.0

The PWLB advanced £13.0 billion of new loans to authorities required to take on debt. The Department for Communities and Local Government repaid £5.0 billion of principal to the PWLB, on behalf of authorities for whom debt was to be repaid, and paid £1.6 billion of net premiums for the early repayment of these loans.

The Housing Self-financing operation resulted in a net increase in loan principal outstanding to the PWLB of £8.0 billion.

Circular 150

From October 2010 PWLB rates had been set at a margin over gilts of 100 bps, to suppress local authority borrowing and promote a market-facing approach by large borrowers. The need for local

authorities to borrow heavily to buy their way out of negative housing subsidy prompted HM Treasury to announce, on 21 September 2011, a reduction in the margin over gilts to its previous level for Housing Self-financing only. Circular 150 of 21 November 2011 restricted to a single day the availability of the special rate. The decision reflected a need for fiscal certainty around a significant one-off transaction and, given uncertainty in the global financial markets, to reduce the risks associated with local authorities holding large sums in advance of the transaction. It also took into account local authorities' expressed preference for the timing of borrowing.

Review by type of borrower

Figure 2 shows loan advances made by the PWLB in 2011-2012 by type of borrower.

There were 2 advances to drainage boards in the year, totalling less than £1 million (2010-2011: £2 million). As in 2010-2011, there were no advances to harbours.

Figure 2: Amounts advanced by type of borrower

	Fixed rate (£m)	Variable rate (£m)	Total (£m)
Local Authorities in England			
County Councils	728	-	728
GLA and London Borough Councils	1,809	40	1,849
Metropolitan District Councils	1,622	13	1,635
Non-Metropolitan District Councils	10,424	202	10,626
Parish and Town Councils	16	-	16
Others	424	2	426
	15,023	257	15,280
Local Authorities in Wales			
Principal Councils	46	-	46
Community Councils	1	-	1
Others	9	-	9
	56	-	56
Local Authorities in Scotland			
Principal Councils	775	-	775
Others	-	-	-
	775	-	775
	15,854	257	16,111

Types of loans, periods, rates and incidence of drawings

The monthly totals of loan advances, and the effect on the PWLB's loan portfolio, can be seen in Figure 3. The principal balance outstanding to the PWLB at 31 March 2012 was £61.9 billion (31 March 2011: £53.1 billion). The high level of advances in March was due to the PWLB's involvement in the Housing Self-financing operation, as described on page 16.

The relationship between rates of interest and the term till maturity of advances for fixed rate loans can be seen in Figure 4. Figure 5 shows amounts advanced monthly for fixed rate loans and their interest rates. Figure 6 provides a monthly profile of advances and their term till maturity.

The appetite for variable rate loans in 2011-2012

is demonstrated in Figure 7. The PWLB advanced £257 million of variable rate loans (2010-2011: £370 million).

Figure 8 shows the pattern of rates and the term till maturity of advances in the last five years.

The continuing popularity of maturity loans is shown in Figure 9.

The average repayment period for new loans was 24.7 years (2010-2011: 17.6 years). Loans with a value of £1,074 million (2010-2011: £446 million), or 7% of the total (2010-2011: 8%), were taken for the maximum period of 50 years. Loans amounting to £27 million (2010-2011: £200 million), less than 1% of the total (2010-2011: 4%), were taken for the minimum period of one year.

Figure 3: Principal outstanding and advanced, month by month

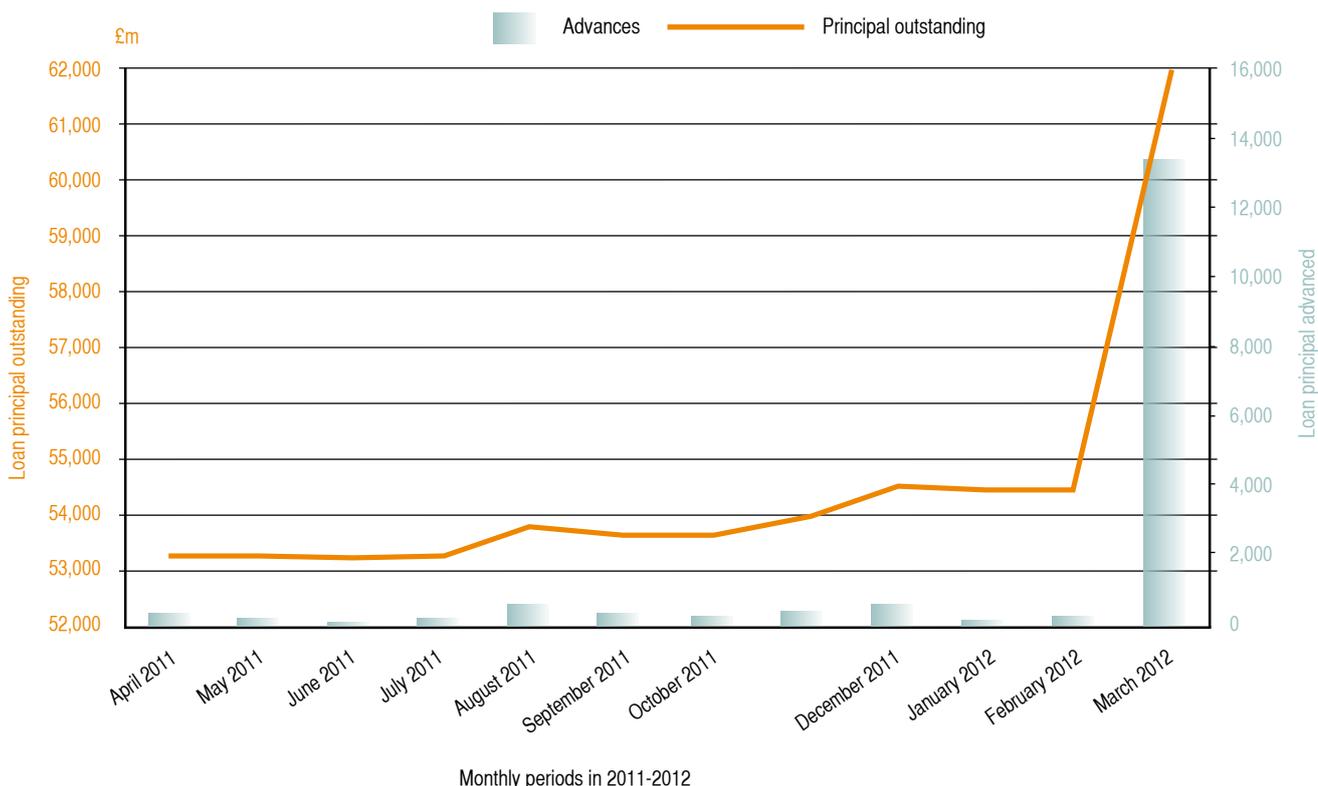


Figure 4: Term till maturity of fixed rate advances and their interest rates

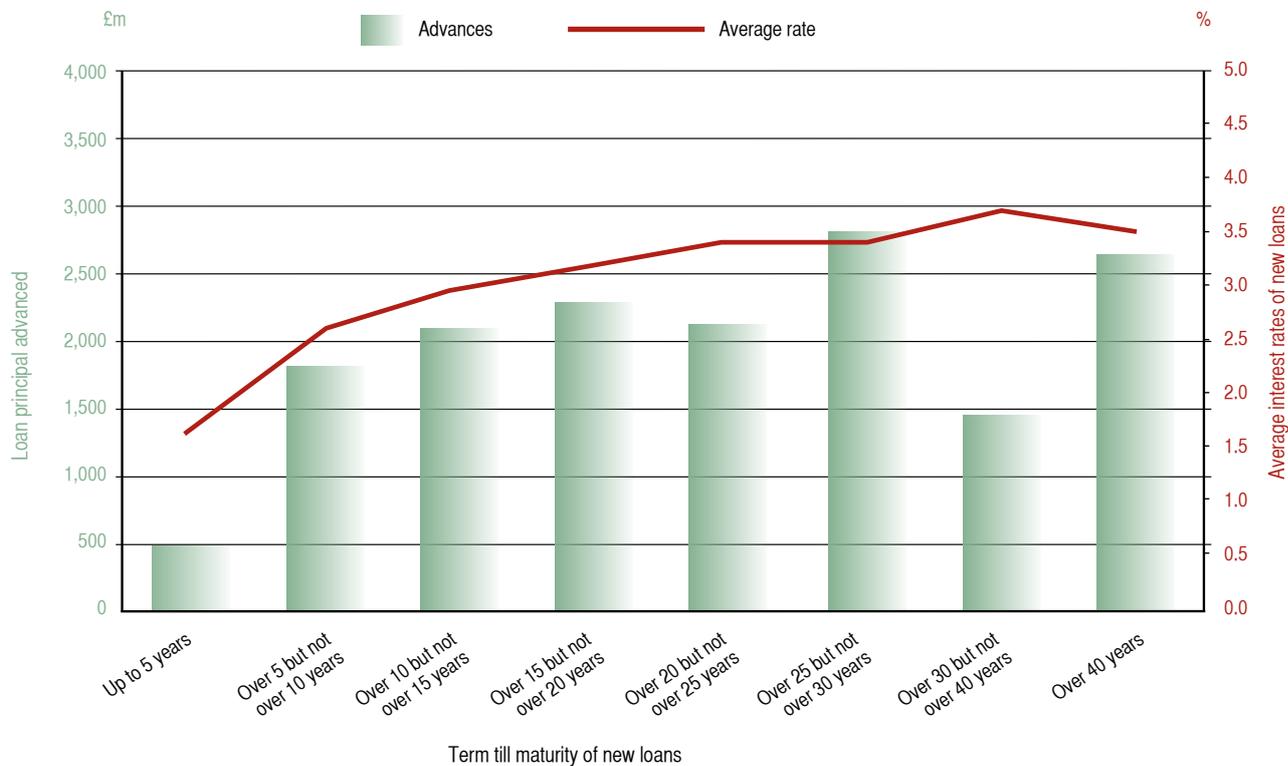


Figure 5: Amounts advanced for fixed rate loans and their interest rates, month by month

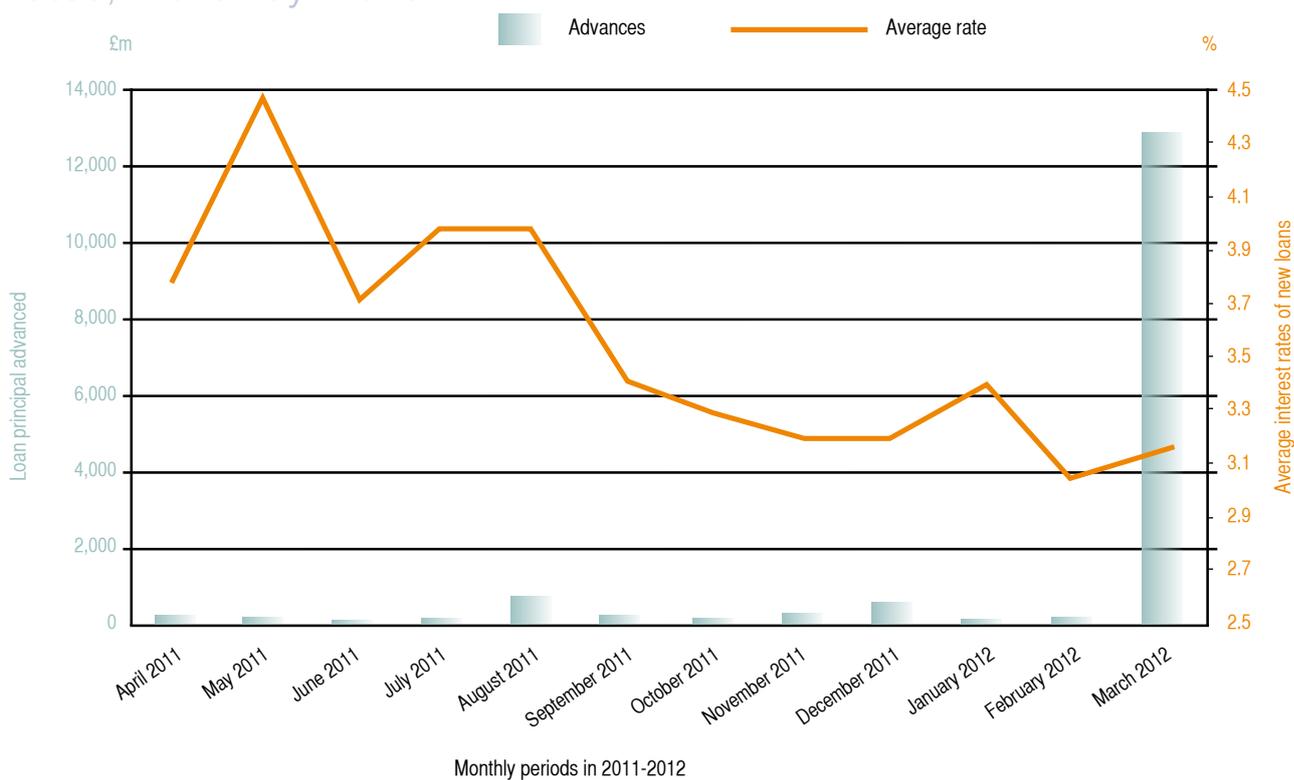


Figure 6: Amounts advanced and their term till maturity, month by month

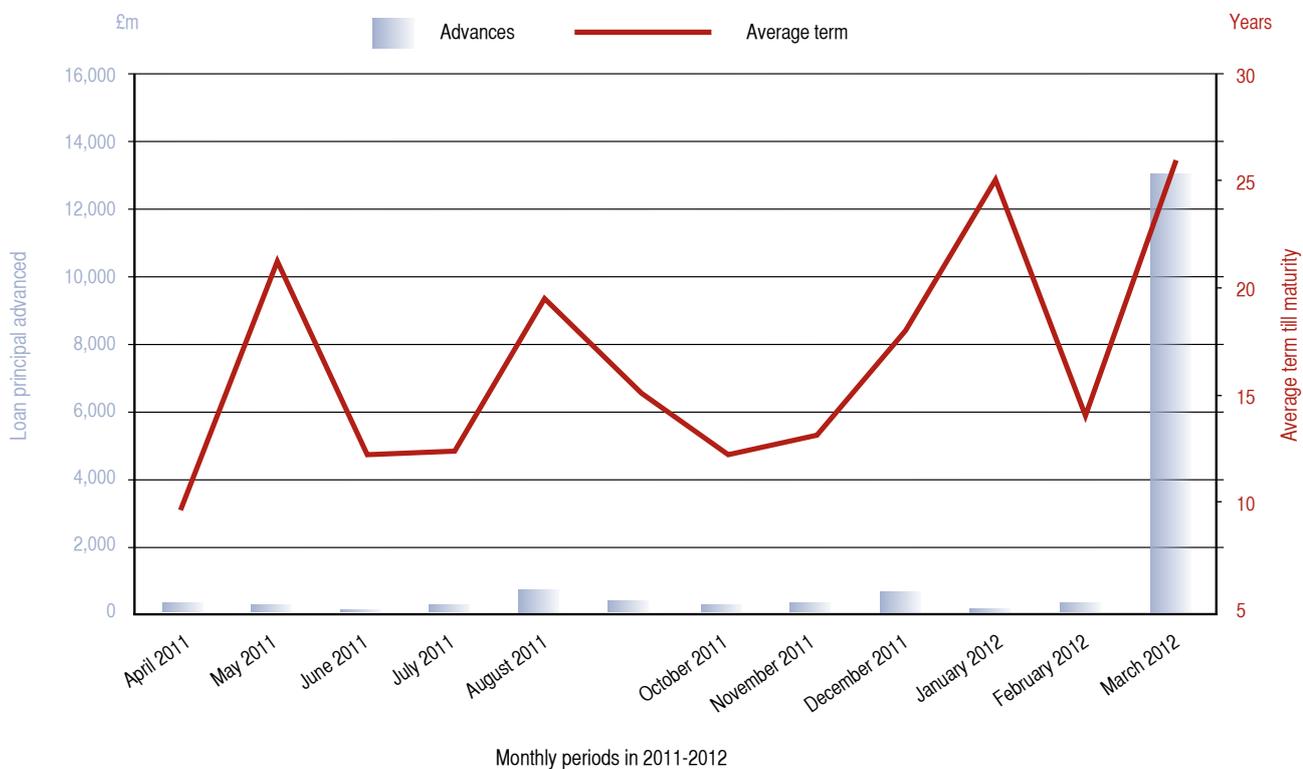


Figure 7: Amounts of fixed and variable rate loans advanced, month by month

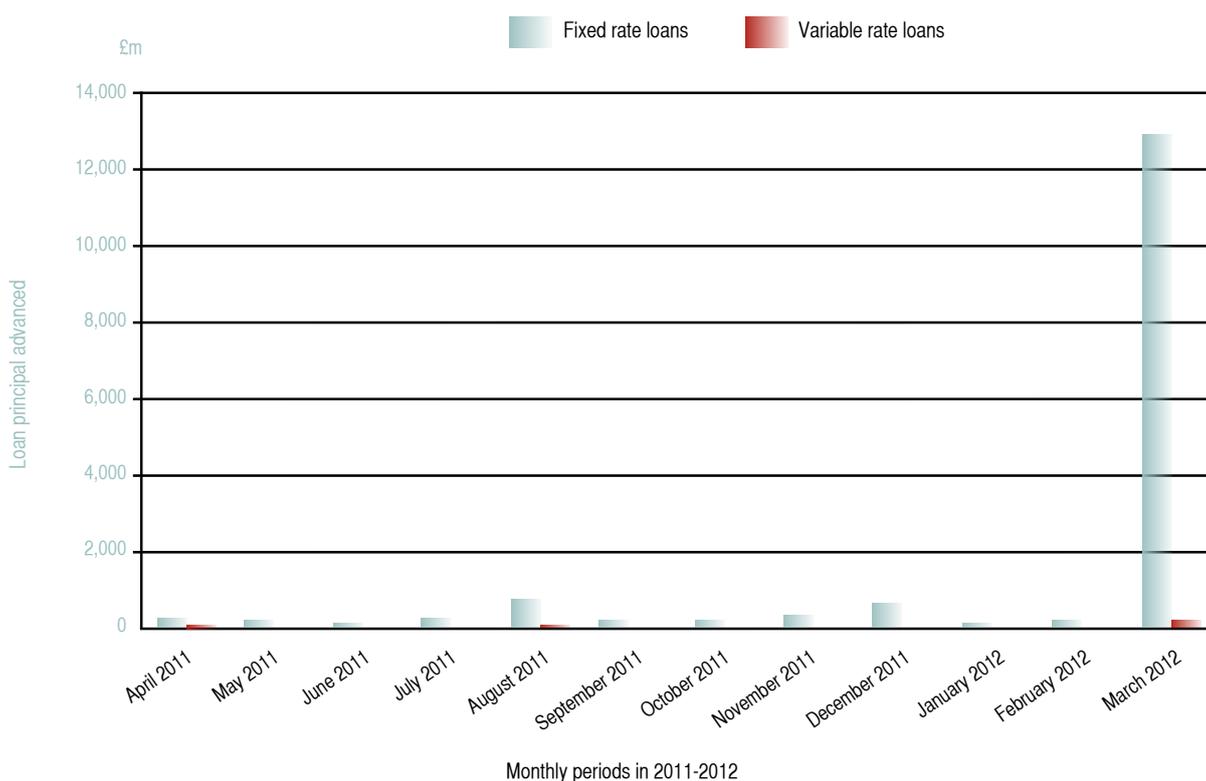


Figure 8: Average rate and term till maturity of advances, year by year

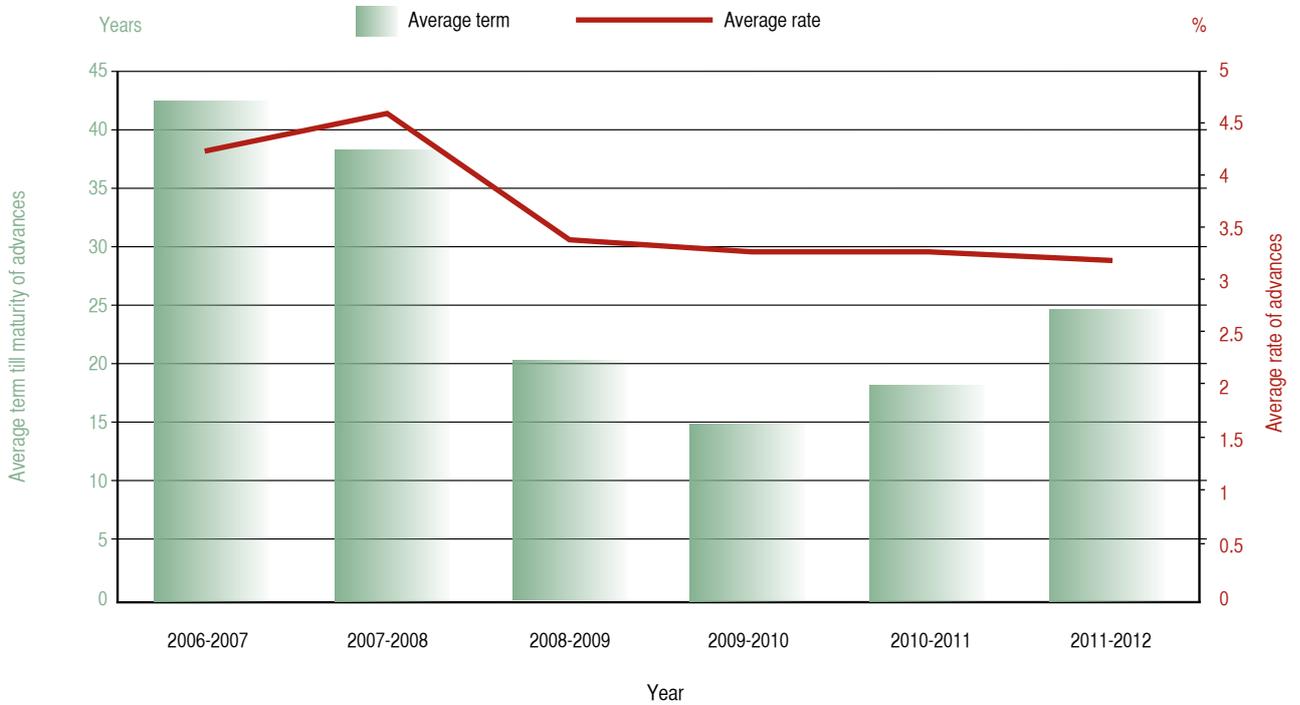


Figure 9: New loans by type and by term till maturity

Method of repayment	Period of repayment (£m)							Total
	Up to 5 Years	Over 5 but not over 10 years	Over 10 but not over 15 years	Over 15 but not over 25 years	Over 25 but not over 30 years	Over 30 but not over 40 years	Over 40 years	
Fixed rate loans								
Maturity	476	1,334	1,797	3,744	2,215	1,440	2,624	13,630
Annuity	1	33	12	510	169	30	8	763
Equal instalments of principal	15	490	311	216	409	20	-	1,461
	492	1,857	2,120	4,470	2,793	1,490	2,632	15,854
Variable rate loans								
Maturity	-	257	-	-	-	-	-	257
	-	257	-	-	-	-	-	257
All loans								
Maturity	476	1,591	1,797	3,744	2,215	1,440	2,624	13,887
Annuity	1	33	12	510	169	30	8	763
Equal instalments of principal	15	490	311	216	409	20	-	1,461
Total	492	2,114	2,120	4,470	2,793	1,490	2,632	16,111

Scheduled repayments and early repayments

When an authority redeems a loan, it is a decision for the authority, subject to the PWLB's lending arrangements, whether to replace the loan with a new loan. The PWLB will treat the replacement loan as a new transaction.

Authorities may, at the PWLB's discretion, redeem a loan early.

In the case of an early redemption, the authority will repay the net present value of the remaining payments of principal and interest, resulting in a discount or premium according to whether the lending rate at the time is higher or lower than the loan rate.

Figure 10 summarises early repayments in 2011-2012.

Figure 10: Early repayments

	Number of loans repaid	Principal repaid	Premium received	Discount paid	Net premiums/ discounts
		£m	£m	£m	£m
Fixed rate loans	1,404	5,556	1,722	-	1,722
Variable rate loans	14	54	-	-	-
Totals	1,418	5,610	1,722	-	1,722

Early repayments of £5.6 billion were made during the year (2010-2011: £1.7 billion), compared to new advances of £16.1 billion (2010-2011: £5.3 billion).

The value of loan principal outstanding to borrowers rose by 16.5% year-on-year (2010-2011: 3.7% rise), to £61.9 billion from £53.1 billion at 31 March 2011.

Repayments in arrears

There were £255 million overdue loan repayments at 31 March 2012 (31 March 2011: less than £1 million). These arose because the payment fell on a weekend and so were duly paid the next working day. All overdue loan repayments at 31 March 2012 have since been paid.

Rates of interest

The PWLB's interest rates are determined by the DMO in accordance with the National Loans Act 1968 and methodologies agreed with HM Treasury. Variable rates are determined by reference to gilt collateral repo rates. Fixed rates are determined from prevailing gilt yields because the funding for the PWLB comes from the National Loans Fund,

which raises funds by issuing gilts. The PWLB's rates include a margin to ensure that the PWLB does not lend at rates lower than those at which HM Government could notionally borrow by issuing gilts. The margin also mitigates the risk of timing and maturity mismatches between the liabilities of the National Loans Fund (i.e. gilts) and its assets (i.e. loans from the PWLB).

Two sets of fixed rates are offered by the PWLB, the 'new loan' rates and the 'early repayment' rates. A negative margin is applied to the 'early repayment' rates to ensure that the PWLB does not accept repayment of loans at below prevailing market rates.

The DMO and HM Treasury reserve the right to change rates at any time intra-daily or to alter the margins and formulas for rates as deemed necessary.

Current and past rates of interest are displayed on the website, www.pwlb.gov.uk.

Fixed rates for four maturities are shown in Figure 11 and variable rates are shown in Figure 12, which also shows the Bank of England rate.

Figure 11: Fixed interest rates by term till maturity of loan

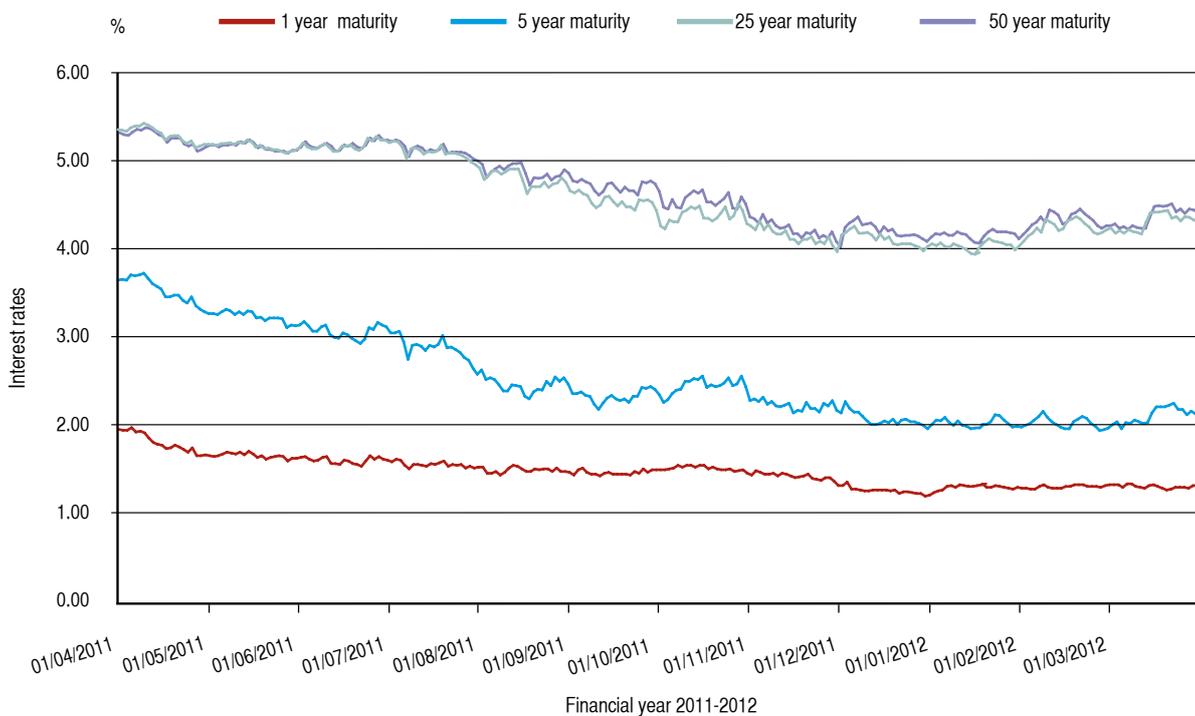
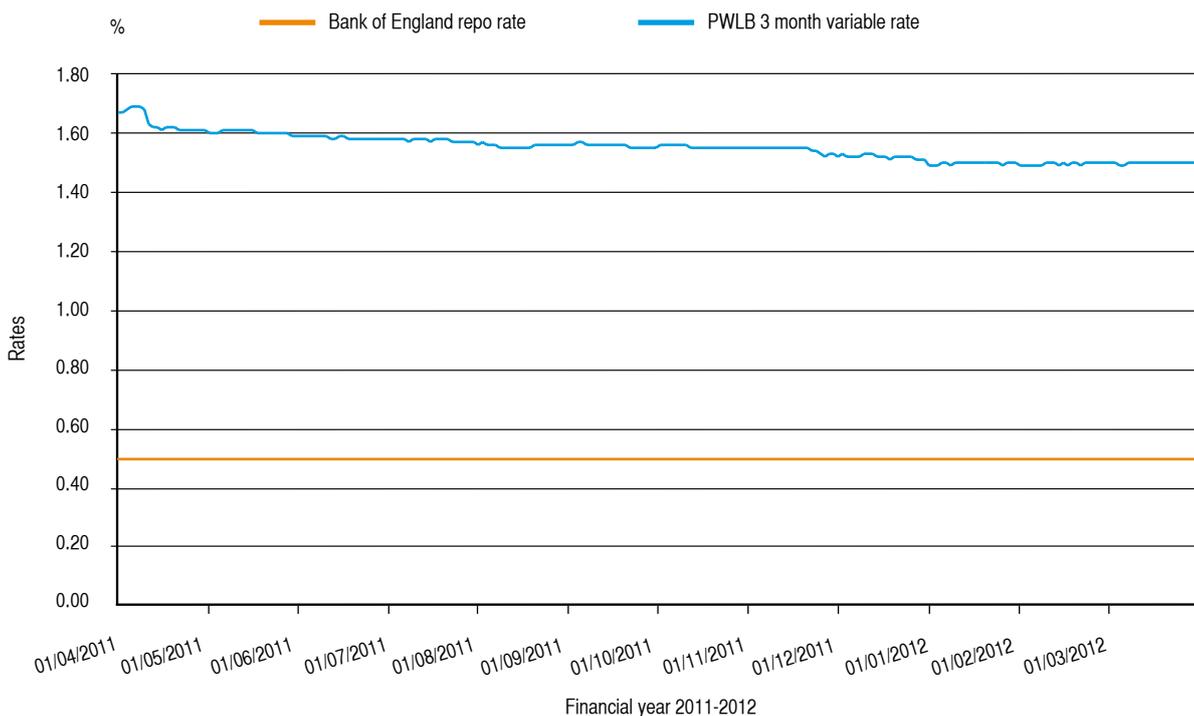


Figure 12: Bank of England rate and the 3 month variable rate



Transfers of debt

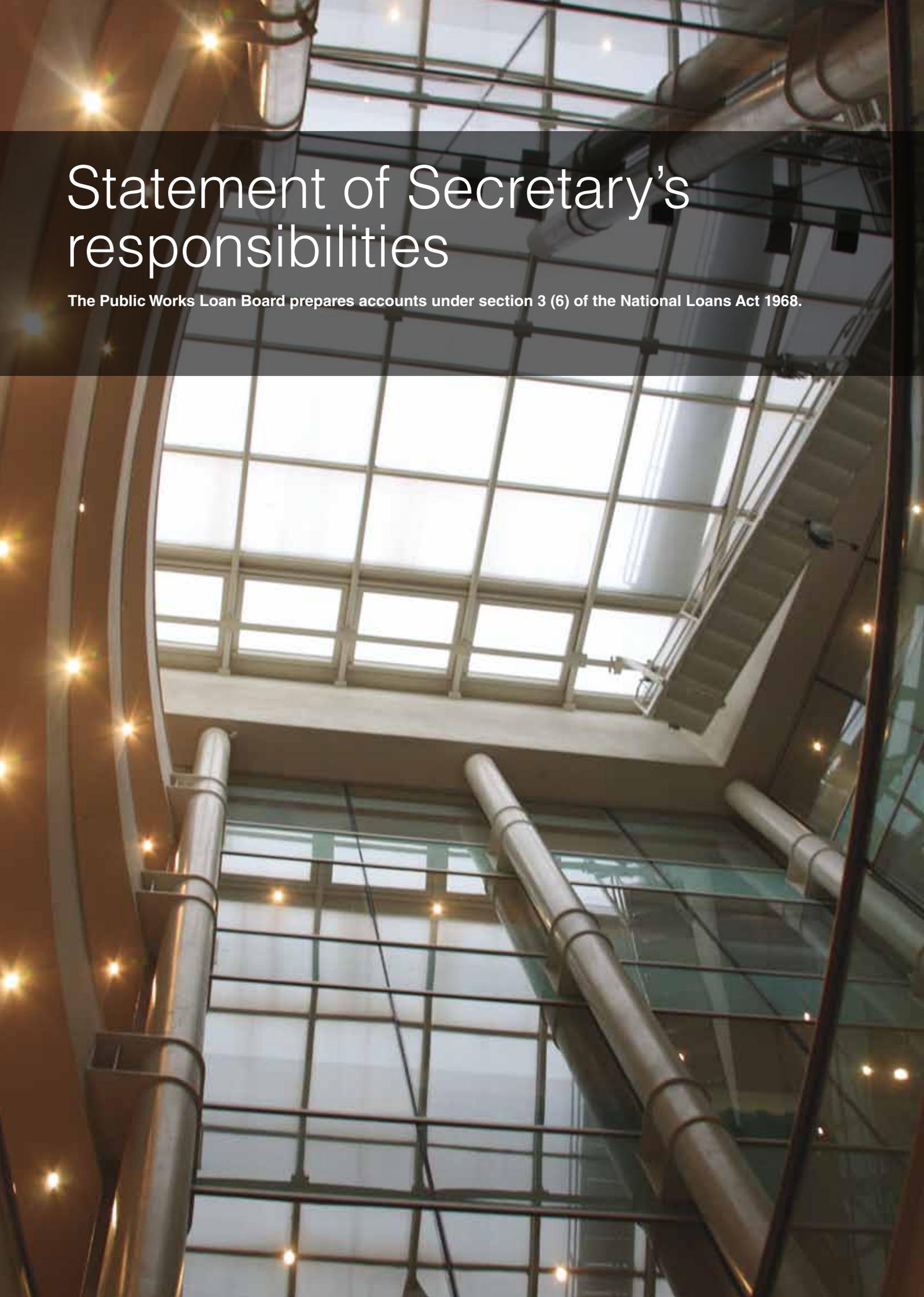
The PWLB is prepared to accommodate borrowers by transferring debt if appropriate, for example following local government reorganisation.

Transfers in the year included the following:
Sandwell to West Midlands Fire and Rescue Authority
Newcastle to Tyne & Wear ITA
Cheshire East to Cheshire West & Chester

Service performance

The PWLB sets itself target timetables for advancing loans and arranging premature repayments. Applications are processed according to the timetables set out in the PWLB's circulars. There was no occasion during the year when the PWLB failed to meet these timetables.

Mark Frankel
Secretary, Public Works Loan Board
8 June 2012



Statement of Secretary's responsibilities

The Public Works Loan Board prepares accounts under section 3 (6) of the National Loans Act 1968.

Statement of Secretary's responsibilities

Under Section 3 (6) of the National Loans Act 1968 the Commissioners are required to prepare for each financial year a statement of accounts in the form and on the basis set out in the Accounts Direction. The accounts are prepared on an accruals basis and must give a true and fair view of the state of affairs of the Public Works Loan Board and its income and expenditure and cash flows for the financial year.

In preparing the accounts, the Secretary is required to comply with the requirements of the Government Financial Reporting Manual and in particular to:

- observe the Accounts Direction issued by HM Treasury, including the relevant accounting and disclosure requirements, and apply suitable accounting policies on a consistent basis;
- make judgements and estimates on a reasonable basis;

- state whether applicable accounting standards as set out in the Government Financial Reporting Manual have been followed, and disclose and explain any material departures in the accounts; and

- prepare the accounts on a going concern basis.

The Commissioners have appointed the Secretary to discharge their residual statutory responsibilities, a role that is analogous to acting as an Accounting Officer. The responsibilities of the Secretary, including responsibility for the propriety and regularity of the public finances for which the Secretary is answerable, for keeping proper records and for safeguarding the Public Works Loan Board's assets, are set out in Managing Public Money published by HM Treasury.

Governance statement

The system of internal control is designed to manage risk to an acceptable level, balancing the impact of potential risks with the resources required to manage them.



Governance statement

Scope of responsibility

The statutory role of the Public Works Loan Board Commissioners is to consider loan applications from local authorities and other prescribed bodies and, where loans are made, to collect the repayments. The Commissioners have delegated to the Secretary day-to-day responsibility for authorising loans and collecting due payments. The Secretary submits reports to the Commissioners on a monthly basis and attends the quarterly meetings of the PWLB Commissioners. At these meetings the Secretary will typically report on a number of standing agenda items including loans advanced and due payments, as well as ad hoc matters. These regular meetings, as well as the annual Report and Accounts, are the primary mechanisms through which the Commissioners inform themselves of the PWLB's operations. A fuller description of the roles and responsibilities of the Commissioners can be found in the foreword to this Report and Accounts.

As Secretary to the Board I am responsible for ensuring that appropriate advice is given to the Commissioners on all matters relating to financial propriety and regularity, for keeping accounts and submitting them for external audit by the Comptroller and Auditor General and for the efficient and effective use of resources and ensuring that the business is managed within the appropriate control framework.

The PWLB is a separate statutory entity managed within the control framework of the United Kingdom Debt Management Office (DMO). While I am responsible for the PWLB's system of internal control, the Accounting Officer of the DMO is responsible for the wider control framework within which the PWLB is managed. In discharging my own control responsibilities I take assurance on the continued sound maintenance of the wider control framework from the Governance Statement for the DMO, although I understand that only reasonable and not absolute assurance can be given that risks have been controlled.

The PWLB is committed to the highest standards

of corporate governance and is guided by the Corporate Governance Code for central government departments (the Code) and the following principles laid down in that Code:

- Parliamentary accountability;
- The role of the board;
- Board composition;
- Board effectiveness; and
- Risk management.

The PWLB does not conduct any part of its business with or through arm's length bodies (ALBs) and therefore has not applied principle six which covers departmental governance arrangements with ALBs.

Managing Board

The Secretary was supported during 2011-2012 by the DMO Managing Board (the board), which comprised:

- Robert Stheeman
DMO Chief Executive and Accounting Officer;
- Jo Whelan
Deputy Chief Executive and Joint Head of Policy and Markets;
- Jim Juffs
Chief Operating Officer;
- Joanne Perez
Joint Head of Policy and Markets;
- Sam Beckett
Non-executive HM Treasury representative;
- Brian Larkman
Non-executive director - Brian Larkman was Global Head of Money Markets at the Royal Bank of Scotland PLC from 2000 to 2001 and Managing Director, Global Money Markets at National Westminster Bank PLC from 1991 to 2000. He was a member of the Regulatory Decisions Committee of the Financial Services Authority until 2006; and
- Brian Duffin
Non-executive director - Brian Duffin was Chief Executive of Scottish Life from 1999 to 2007 and Executive Director of Royal London Mutual from 2001 to 2007.

All of the current directors have been board members throughout the year under review and both non-executive directors have fixed terms defined in their contracts of service. Non-executive board members are appointed following a formal process, receive an induction on joining and have access to additional information and training where they consider it necessary in the discharge of their duties.

One of the roles of the board is to advise the Secretary on any key decisions affecting the PWLB.

An executive sub-committee of the board generally meets weekly and supports the Secretary on operational decisions.

The board has undertaken a formal self evaluation of its performance covering 2011-2012. The board concluded that, during the period under review, it has operated effectively in delivering the objectives set out in its terms of reference. Suggestions for minor improvement are being considered and will be implemented where appropriate.

2011-2012 Board activities

Board meetings were held regularly throughout 2011-2012. In addition to regular agenda items, including risk management, staffing and progress against the operational business plan, the board paid particular attention to the design and progress of the Housing Revenue Account self financing project which was delivered during the period under review.

Board attendance is outlined in the table below:

	Possible	Actual
Robert Stheeman	8	8
Jo Whelan	8	8
Jim Juffs	8	8
Joanne Perez	8	8
Sam Beckett	8	5
Brian Larkman	8	7
Brian Duffin	8	8

Audit Committee

The Secretary was supported during 2011-2012

by the Audit Committee on matters relating to risk, internal control and governance. The Audit Committee covers the activities of the DMO, DMA, CRND and PWLB. The members of the Audit Committee during 2011-2012 were:

- Brian Larkman (Chair);
- Brian Duffin;
- Caroline Mawhood - Caroline Mawhood was Assistant Auditor General at the National Audit Office until 2009 and President of the Chartered Institute of Public Finance and Accountancy for 2008-09. She is a non executive member of the Audit Committees of the Department of Energy and Climate Change and the Corporation of London and an independent member of the Audit Progress Committee of the European Commission. She is also the Honorary Treasurer of Breakthrough Breast Cancer charity.

Audit Committee meetings are typically attended by the DMO Accounting Officer, either or both of the Joint Heads of Policy & Markets/Deputy Chief Executive, the Chief Operating Officer and the Head of Internal Audit. The Secretary of the PWLB also attends meetings when items relevant to the PWLB are due to be discussed by the Committee.

One of the Audit Committee's objectives is to give assurance to the Secretary of the PWLB that:

- High quality processes are in place to manage and control risk for the DMO's financial and non-financial activities;
- Overall governance arrangements are appropriate and operating effectively;
- The financial control framework is effective and supported by an appropriate compliance culture;
- External financial reporting is prudent, accurate, timely, appropriate and consistent with relevant guidance;
- Internal financial and management reporting is timely, prudent, appropriate and consistent with external financial reports;
- Whistle blowing arrangements for confidentially raising and investigating concerns over possible improprieties in the conduct of the PWLB's business are adequate; and
- Relationships with the National Audit Office (NAO) are effective.

During the period under review the Audit Committee paid particular attention to the following areas:

- Business continuity planning;
- Anti-money laundering controls;
- Anti-fraud controls;
- Staff resourcing;
- Risk management and financial control; and
- External and internal financial reporting.

The Audit Committee covers a regular programme of agenda items, together with other current topics, through an annual schedule of four meetings. All scheduled meetings were held and no additional meetings were deemed necessary.

The Secretary has been informed by the following operational committees throughout the period under review:

■ Business Delivery Committee

The Business Delivery Committee reviews the status of the delivery of DMO's business and work plan as a collective cross functional body, resolving emerging issues in a timely way, and agreeing priorities, to ensure the plan stays on track.

The Business Delivery Committee met regularly (typically weekly) throughout 2011-2012.

■ Risk Committees

The Secretary receives advice from three risk committees covering credit and market risk, operational risk and material change programmes. More detail on the roles, responsibilities and activities of these committees can be found in the sections below.

Risk management and internal control

The Secretary is responsible for maintaining a sound system of internal control that supports the achievement of the PWLB's policies, objectives and targets, whilst safeguarding the public funds for which he is accountable, in accordance with the responsibilities assigned to him.

PWLB is managed within the wider DMO system of internal control which is based upon what the DMO

Accounting Officer, with the support of the board, considers to be appropriate taking account of the DMO's activities, the materiality of risks inherent in those activities and the relative costs and benefits of implementing specific controls to mitigate those risks. The DMO's position differs to that of a commercial organisation in that it must always be in a position to transact the underlying business required to meet its remit. As a result the risks associated with this activity cannot be avoided and the system of internal control can only provide reasonable assurance against failure to achieve aims and objectives.

The Risk and Control Framework

The board has designed and put in place a formal risk management framework covering all the activities conducted and overseen by the DMO. This Framework helps ensure that the DMO Accounting Officer is appropriately informed and advised of any identified risks and also allows the management of risks to be monitored. The risk management framework covers both regular operations and new business initiatives, and evolves as the range and nature of the DMO's activities change. The Framework is supported by a clear 'three lines of defence' model:

First line of defence:

Day-to-day management of risk is the responsibility of management staff within business areas. The DMO fosters a risk aware culture and encourages all members of staff, including board members to identify new aspects of risk and changes in previously identified risks, so that these may be assessed and so that appropriate mitigating actions may be put in place.

Mitigating actions typically include segregation of duties, staff training, clear lines of management delegation and robust business continuity arrangements.

Second line of defence:

Oversight of risk is provided by the board and risk committees, whose role is to provide regular and systematic scrutiny of risk issues which lie within their remit and to support the DMO Accounting

Officer in exercising his overall responsibility for risk management.

The DMO considers that the principal risks it faces arise in three broad areas: credit and market risk, operational risk, and risk controls, so it has established committees to meet regularly to review the changing risk pattern for each of these areas and to set up appropriate responses. The work of these committees is described in more detail below.

Credit and Market Risk Committee

The Credit and Market Risk Committee (CMRC) meets on a regular basis, with more frequent meetings held when required, for example during times of market stress. CMRC monitors and reviews the management of market, credit, and liquidity risk. It sets limits across a range of exposures including counterparties, countries, instruments held as collateral as well as setting absolute limits on net daily flows across the DMA.

The CMRC has advised the DMO Accounting Officer and the board, during the year, on significant current and emerging risk issues and actions to mitigate such risks and in particular this year on the impacts of ongoing volatility in the Eurozone on DMO activities. CMRC met twelve times during the year.

Operational Risk Committee

The Operational Risk Committee (ORC) meets regularly to monitor operational risks and to review significant risk issues. The ORC is responsible for reviewing risk incidents identified through the DMO's risk incident reporting process, and considering whether planned mitigating action is appropriate. The Committee also reviews and tracks the progress of actions identified by Internal Audit. The Committee's scope includes issues relating to information risk, IT security, business continuity, anti fraud and key supplier risks.

The ORC has advised the DMO Accounting Officer and the board, during the year, on significant operational risk concerns, significant risk issues and trends as well as actions to mitigate such risks. The Committee has focused this year on further developing business continuity planning, including operational planning for the Olympic period, reviewing trading controls and improving the data quality and reliability of the DMO website. ORC met

eight times during the year.

Controls Group

The Controls Group meets periodically to review issues affecting the DMO's system of internal control and to analyse material changes to the control environment. The Group recommends actions to management to implement changes where appropriate. The Controls Group consists of representatives from Finance, Risk, Compliance and Internal Audit.

The Controls Group has advised the DMO Accounting Officer, the board and senior management on any significant risk concerns stemming from the introduction of new business activities as well as risks relating to other change management activities. The Group has also advised the DMO Accounting Officer on suitable mitigating action where appropriate.

During the year, the Controls Group review work has included improvements in cash forecasting, internal reorganisation of certain control functions for PWLB, the Housing Revenue Account self financing project and trade settlement processing.

Risk Management Unit (RMU)

The risk committees are supported by the DMO's Risk Management Unit (RMU) which ensures key risk issues arising from these committees are communicated to the DMO Accounting Officer and senior management on a regular basis, with additional ad hoc reporting if an emerging issue requires it. The RMU also supports the formal risk reporting processes with defined outputs, including regular detailed risk reports which are reviewed by the board and senior management.

As well as supporting the risk committee structure, the RMU provides control advice on risks. As part of the second line of defence the RMU is separate from and independent of the DMO's trading operations. The RMU conducts risk analysis and provides regular market, credit and operational risk capability for the DMO.

The identification, monitoring and mitigation of operational risk is facilitated by the RMU, via quarterly consultation with heads of business units and functional teams. Significant risk issues are assessed for materiality and probability of occurrence. New

risks, and risks to which exposure is increasing are highlighted and actions are taken to ensure effective management of all risks. The DMO has Senior Risk Owners (SROs) who undertake a cross-functional moderation process to promote better prioritisation of operational risks across the organisation. The RMU maintains a central exception log to record all risk incidents raised, in order to identify control weaknesses and assign actions to improve controls. Progress against treatment actions is obtained on a regular basis to ensure issues highlighted by internal and external audit, and other identified actions to improve the control environment, are managed and progressed within agreed deadlines.

Third line of defence:

The DMO's Internal Audit function provides the DMO Accounting Officer with independent and objective assurance on the overall effectiveness of the Agency's system of internal control. It does this through a risk based work programme which is approved by the Audit Committee at the start of each year. All audits make a series of recommendations which, once agreed by management, are monitored for implementation. The function is independent of the DMO's trading activities and operations and has a direct reporting line to the DMO Accounting Officer. The work of Internal Audit includes assessing the effectiveness of both control design and control performance. With its independence and overall remit, Internal Audit provides a third line of defence

Risk profile

The Secretary and board believe that the principal risks and uncertainties facing the PWLB are outlined in the table below together with the key actions taken to manage and mitigate them:

Principal risks and uncertainties	Mitigation and management
<p>IT systems and infrastructure</p> <p>The PWLB relies on a number of IT systems to conduct its operations. In particular, certain systems are central to the PWLB being able to advance loans and manage repayments in an effective and timely way.</p> <p>A number of the operational systems and services on which the PWLB relies are provided or supported by third party suppliers.</p>	<p>In line with good practice the DMO has put in place comprehensive business continuity arrangements to ensure it is able to continue market operations in the event of an internal or external incident that threatens business as usual activity. These arrangements extend to cover the PWLB.</p> <p>The DMO's Business Continuity Plan (BCP) including Disaster Recovery (DR) and other arrangements is subject to continual review and update. The DMO ensured a programme of DR testing was carried out in 2011, and that BCP arrangements to support key PWLB activities were observed during the year with</p>

against the risks that might prevent the DMO delivering its objectives.

Risk policies and procedures

The DMO's risk policies reflect the high level standards and requirements which determine the way in which risks are managed and controlled. The DMO Accounting Officer, with the support of the board, ensures that policies are regularly reviewed to reflect any changes in the DMO's operations and/or best practice. In 2011 this included broadening the scope of certain DMO policies to cover requirements introduced by the Bribery Act.

Staff are required to confirm that they have read and accepted the DMO's rules on personal dealing and the DMO's policy on the use of information systems and technology, and that they are aware of, and will continue to keep up to date with, the DMO's policies on whistle blowing, fraud and anti-money laundering. The DMO ensures that this exercise is undertaken on an annual basis allowing staff to maintain a good level of awareness of the DMO's policies in these areas. All members of staff have job descriptions which include reference to the specific key risks they are expected to manage.

Managers in each business function are responsible for ensuring that the operations within their area are compliant with plans, policies, procedures and legislation.

Principal risks and uncertainties	Mitigation and management
<p>Transaction processing</p> <p>The PWLB relies on its operational processes to successfully advance loans and manage repayments on a daily basis. Reliance on the accurate execution of processes exposes the PWLB to operational risk arising from process breakdown and human error.</p>	<p>PWLB staff working from the DR site. Assessment of business continuity requirements is a specific requirement for new projects and major business initiatives.</p> <p>The DMO recruited a dedicated business continuity specialist in 2011 to help enhance and promote planning across the organisation.</p> <p>The DMO is represented on the Public Finance Business Continuity Management Group and took part in a market wide business continuity exercise conducted in November 2011.</p> <p>To mitigate the risk of failure of a key third party, where appropriate, the DMO undertakes a corporate risk assessment of the potential supplier in order to assess financial strength and operational capacity. Additionally the DMO has dedicated relationship managers who conduct regular meeting with key suppliers and monitor performance against agreed SLAs.</p> <p>A key component of the PWLB's control framework is the segregation of duties to ensure independent checking and reconciliation, and to avoid concentration of key activities or related controls in individuals or small groups of staff. In particular, segregation of duties takes place between front and back office activities.</p> <p>All teams, including PWLB, have documented procedures for their main activities and there are clearly defined authorisation levels for committing the DMO externally. In 2011-12 system enhancements were made to improve management information on trade activity and regular accounting reports.</p> <p>The RMU conducts regular control and compliance testing, providing the executive sub-committee of the board with assurance on the effectiveness of operational controls.</p> <p>The DMO also maintains a strong audit and control environment which includes a well embedded incident reporting procedure which extends to cover PWLB. This promotes early identification and resolution of risk incidents.</p> <p>DMO recruitment policies help ensure that individuals with the appropriate level of skill and experience are appointed at all levels within the organisation. This helps mitigate the level of human error resulting in process failures.</p>

Principal risks and uncertainties	Mitigation and management
<p>People risk</p> <p>The DMO, including PWLB, relies on maintaining a sufficiently skilled workforce at all levels of the organisation in order to operate effectively and efficiently, and to deliver its strategic objectives. The DMO is exposed to an increased risk of operational failure if it is unable to compete for, and retain, sufficiently skilled staff over time.</p>	<p>The DMO's Training and Development policy aims to ensure that its staff have the right skills to meet its objectives.</p> <p>The DMO has a formal recruitment and selection process to help ensure vacancies are filled quickly by appropriately skilled candidates.</p> <p>The DMO has put in place a formal performance appraisal process and all staff are given clear and achievable objectives. Where appropriate staff are encouraged to engage in activities which promote development, and the DMO provides regular training opportunities and support for professional studies to enhance the skills base of its employees.</p> <p>A Staff Council has met regularly throughout the year and enabled an open exchange of ideas and views between management and staff representatives and has been an effective conduit for wider communication and consultation with all staff.</p> <p>On an annual basis DMO staff take part in the Civil Service employee engagement survey and any issues raised, including mitigating action if required, will be considered by the DMO Accounting Officer and board.</p> <p>The DMO was reaccredited as an Investor in People in 2011.</p>
<p>IT and data security</p> <p>Through its activities the DMO gathers, disseminates and maintains sensitive information including market sensitive information and personal data about staff. The DMO seeks to ensure the highest standards of data protection and information management. The DMO is exposed to risk of an external attack on its IT systems and infrastructure.</p>	<p>The DMO continues to work to maintain the required level of protective security covering physical, personnel and information security.</p> <p>Risks to data and information held by the DMO are owned and managed by designated Information Asset Owners. The DMO has a Senior Information Risk Owner (SIRO) who is responsible for the information risk policy and the assessment of information risks. The SIRO also provides assurance to the Managing Board that information risks are being managed effectively.</p> <p>The DMO has put in place several layers to defend against external attack and its infrastructure undergoes an annual penetration test to ensure the control environment is robust. These tests are undertaken by specialists and form part of the assessment against the CESG requirements. This is a condition for continuing connection to the Government Secure Internet (GSI).</p>

Review of effectiveness

I have reviewed the effectiveness of the system of internal control and confirm that an ongoing process designed to identify, evaluate and prioritise risks to the achievement of the PWLB's aims and objectives has been in place throughout 2011-2012. This review included an assessment of any material risk and control issues identified and reported during the relevant period.

My review has been informed by the advice of the risk committees and by the work of the internal auditors and executive managers within the DMO who have been delegated responsibility for the development and maintenance of the internal control framework, and comments made by the external auditors in their management letter and other reports.

In my role as Secretary I have been advised on the implications of the result of my review of the effectiveness of the system of internal control by the board and the Audit Committee.

Plans to address weaknesses and ensure continuous improvement of the system are in place.

No significant internal control issues, including data security incidents, have been identified in 2011-2012, and no ministerial directions were given.

In my opinion, the PWLB's system of internal control was effective throughout the financial year and remains so on the date I sign this statement.

Mark Frankel
Secretary, Public Works Loan Board
8 June 2012



Certificate and report of the Comptroller and Auditor General



The Certificate and report of the Comptroller and Auditor General to the Houses of Parliament

I certify that I have audited the financial statements of the Public Works Loan Board for the year ended 31 March 2012 under the National Loans Act 1968. These comprise the Statement of Comprehensive Income, the Statement of Financial Position, the Statement of Cash Flows and the related notes. These financial statements have been prepared under the accounting policies set out within them.

Respective responsibilities of the Commissioners, the Secretary of the Public Works Loan Board and auditor

As explained more fully in the Statement of Secretary's Responsibilities, under Section 3 (6) of the National Loans Act 1968 the Commissioners are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. They appoint the Secretary to discharge these responsibilities on their behalf. My responsibility is to certify and report on the financial statements in accordance with the National Loans Act 1968. I conducted my audit in accordance with International Standards on Auditing (UK and Ireland). Those standards require me and my staff to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Public Works Loan Board's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Public Works Loan Board; and the overall presentation of the financial statements. In addition I read all the financial and non-financial information in the Foreword, Management Commentary, Statement of Secretary's responsibilities and Governance statement, to identify material inconsistencies

with the audited financial statements. If I become aware of any apparent material misstatements or inconsistencies I consider the implications for my certificate.

I am required to obtain evidence sufficient to give reasonable assurance that the expenditure and income recorded in the financial statements have been applied to the purposes intended by Parliament and the financial transactions recorded in the financial statements conform to the authorities which govern them.

Opinion on Regularity

In my opinion, in all material respects, the expenditure and income recorded in the financial statements have been applied to the purposes intended by Parliament and the financial transactions recorded in the financial statements conform to the authorities which govern them.

Opinion on financial statements

In my opinion:

- the financial statements give a true and fair view of the state of the Public Works Loan Board's affairs as at 31 March 2012 and of its operating surplus retained for the year then ended; and
- the financial statements have been properly prepared in accordance with the National Loans Act 1968 and HM Treasury directions issued thereunder.

Opinion on other matters

In my opinion, the information given in the Foreword and Management Commentary for the financial year for which the financial statements are prepared is consistent with the financial statements.

Matters on which I report by exception

I have nothing to report in respect of the following matters which I report to you if, in my opinion:

- adequate accounting records have not been kept; or

- the financial statements are not in agreement with the accounting records or returns; or
- I have not received all of the information and explanations I require for my audit; or
- the Governance Statement does not reflect compliance with HM Treasury's guidance.

Report

I have no observations to make on these financial statements.

Amyas C E Morse

Comptroller and Auditor General
National Audit Office
157-197 Buckingham Palace Road
Victoria
London
SW1W 9SP

13 June 2012



Financial statements and notes to the accounts

EXCHEQUER

In use



Statement of comprehensive income

For the year ended 31 March 2012

	Note	2012 £m	2011 £m
Interest income	3, 4	4,503	2,978
Operating income		4,503	2,978
Interest payable to National Loans Fund		(4,503)	(2,978)
Operating surplus retained		-	-

The notes on pages 46 to 55 form part of these accounts.

Statement of financial position

As at 31 March 2012

	Note	2012 £m	2011 £m
Assets			
Cash and balances at bank		49	51
Loans and advances	5	62,625	53,693
Total assets		62,674	53,744
Liabilities			
Amounts owed to National Loans Fund	8	62,674	53,744
Total liabilities		62,674	53,744

The notes on pages 46 to 55 form part of these accounts.

Mark Frankel
Secretary, Public Works Loan Board
8 June 2012

Statement of cash flows

For the year ended 31 March 2012

	Note	2012 £m	2011 £m
Net cash (used in) / from operating activities	9	(4,429)	1,061
Financing activities			
Interest paid to National Loans Fund		(4,364)	(2,983)
Increase in loan principal outstanding to National Loans Fund		8,791	1,918
Net cash from / (used in) financing activities		4,427	(1,065)
Decrease in cash		(2)	(4)

The notes on pages 46 to 55 form part of these accounts.

Notes to the accounts for the year ended 31 March 2012

1 Accounting policies

(i) Basis of preparation

The accounts have been prepared in accordance with a direction given by HM Treasury and International Financial Reporting Standards (IFRS) in so far as they are appropriate to the PWLB, under the historical cost convention. In particular, the following standards have been applied:

- IFRS 7 Financial Instruments: Disclosures
- IAS 1 Presentation of Financial Statements
- IAS 7 Cash Flow Statements
- IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors
- IAS 10 Events After the Balance Sheet Date
- IAS 18 Revenue
- IAS 24 Related Party Disclosures
- IAS 32 Financial Instruments: Presentation
- IAS 36 Impairment of Assets
- IAS 37 Provisions, Contingent Liabilities and Contingent Assets
- IAS 39 Financial Instruments: Recognition and Measurement

Certain IFRS have been issued or revised, but are not yet effective, which will impact on the PWLB in subsequent reporting periods.

These are:

- IFRS 9 Financial Instruments, which will replace IAS 39.

IFRS 9 is expected to improve and simplify the reporting of financial instruments.

Application of IFRS 9 is required for any reporting period beginning on or after 1 January 2015. Earlier application is permitted.

The PWLB expects to apply IFRS 9 in its 2015-2016 Report and Accounts.

The application of IFRS 9 is not expected to impact

on the disclosure of financial instruments reported by the PWLB.

(ii) Financial assets and income recognition

The PWLB classifies its financial assets as loans and receivables under IAS 39 (Financial Instruments: Recognition and Measurement), which are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. The PWLB does not sell financial assets and so does not designate any loans and receivables as available-for-sale or held for trading.

Loans and receivables are recognised when cash is advanced to borrowers and are derecognised when borrowers settle their obligations.

All loans are recognised initially at fair value, normally the amount advanced to the borrower. Loans and receivables are subsequently measured at amortised cost using the effective interest rate method.

The effective interest rate is the rate that exactly discounts estimated future cash receipts or payments through the expected life of the financial instrument or, where appropriate, a shorter period, to the net carrying amount of the instrument. When calculating the effective interest rate, cash flows are based on the contractual terms of the loan. Owing principally to the long maturities of most loans and the volatile pattern of early repayments, the actual cash flows and the expected lives of the loans cannot be estimated reliably. Thus premiums and discounts on early repayments are recognised when received and paid.

The fair value of loans outstanding, disclosed in Note 6 to the accounts, is calculated as the aggregate net present value of future cash flows on each individual loan. These future cash flows are discounted at the PWLB's premature repayment rates at 31 March 2012.

(iii) Financial liabilities

All the PWLB's liabilities relate to monies drawn from the National Loans Fund for the purpose of issuing loans to the PWLB's borrowers. All principal and interest payments receivable by the PWLB, along with any premiums for early redemption, are repayable to the National Loans Fund. Therefore all the PWLB's assets are also liabilities payable to the National Loans Fund. For this reason, the PWLB's liabilities are valued in the same way as the corresponding assets.

Liabilities are recognised when cash is advanced to the PWLB from the National Loans Fund and derecognised when cash is paid back to the National Loans Fund.

(iv) Statement of changes in equity

These accounts do not present a statement of changes in equity, since all the funding of the PWLB is provided by the National Loans Fund, and matches the amount loaned by the PWLB to borrowers. The change in net funding is therefore already disclosed

in the statement of financial position, which demonstrates the change in amounts owed to the National Loans Fund due to changes in the PWLB's loan portfolio.

2 Accounting policy change

In 2011-2012, the PWLB changed its accounting policy relating to the disclosure of related parties. This was done in accordance with revisions to IAS 24 and the interpretation of these revisions for the public sector context from the 2011-2012 FReM. Application of the revised IAS 24 is required for reporting periods beginning on or after 1 January 2011.

Previously, the PWLB disclosed information about the details of its transactions with entities within government. The revisions to IAS 24 and the 2011-2012 FReM state that this information no longer needs to be disclosed.

This change in accounting policy has no retrospective impact and no comparative figures have been restated.

3 Interest income

	2012 £m	2011 £m
Contractual interest income for fixed rate loans	2,773	2,804
Contractual interest income for variable rate loans	8	5
Premiums received	1,722	179
Discounts paid	-	(10)
	4,503	2,978

4 Segmental analysis of interest income by country

	2012 England £m	2012 Wales £m	2012 Scotland £m	2012 Total £m
Fixed rate loans	3,896	154	445	4,495
Variable rate loans	7	-	1	8
	3,903	154	446	4,503

	2011 England £m	2011 Wales £m	2011 Scotland £m	2011 Total £m
Fixed rate loans	2,376	171	426	2,973
Variable rate loans	4	-	1	5
	2,380	171	427	2,978

5 Loans and advances

	2012 £m	2011 £m
Fixed rate loans principal	60,904	52,287
Variable rate loans principal	1,013	849
Loan principal outstanding	61,917	53,136
Accrued income on fixed rate loans	707	556
Accrued income on variable rate loans	1	1
Accrued income	708	557
Value of loans outstanding	62,625	53,693

6 Loan principal

6a Loan principal outstanding - fair value and weighted average interest rate

	2012 Principal £m	2012 Fair value £m	2012 Weighted average interest rate* %
Fixed rate loans	60,904	75,841	4.68
Variable rate loans	1,013	1,014	0.72
	61,917	76,855	4.62
	2011 Principal £m	2011 Fair value £m	2011 Weighted average interest rate* %
Fixed rate loans	52,287	60,212	5.27
Variable rate loans	849	850	0.88
	53,136	61,062	5.20

* This excludes overdue payments.

The fair value is the net present value of all future contractual cash flows for each loan. These cash flows are discounted at the PWLB's premature repayment rates at 31 March 2012.

The weighted average period for which rates are fixed is 24.6 years (2011: 24.5 years) for fixed rate loans.

At 31 March 2012, no loans (31 March 2011: £4 million) had been confirmed, but not yet advanced. Such loans are not included in the statement of financial position.

At 31 March 2012, borrowers had confirmed their intention to repay £45 million of loans, which were not yet due (31 March 2011: £nil). Such repayments are not reflected in the statement of financial position.

6b Loan principal outstanding – maturity analysis

	2012 Principal outstanding £m	2011 Principal outstanding £m
Up to 1 month / repayable on demand	125	96
In more than 1 month but not more than 3 months	155	266
In more than 3 months but not more than 1 year	1,067	1,334
In more than 1 year but not more than 5 years	7,032	7,044
In more than 5 years but not more than 10 years	7,923	7,242
In more than 10 years but not more than 20 years	12,584	9,039
In more than 20 years but not more than 30 years	10,185	6,920
In more than 30 years but not more than 40 years	6,350	4,476
More than 40 years	16,496	16,719
	61,917	53,136

6c Loan principal outstanding – interest rate profile

	2012 Principal outstanding £m	2011 Principal outstanding £m
Up to 1 month / repayable on demand	397	384
In more than 1 month but not more than 3 months	362	492
In more than 3 months but not more than 1 year	1,530	1,629
In more than 1 year but not more than 5 years	6,843	6,799
In more than 5 years but not more than 10 years	7,170	6,678
In more than 10 years but not more than 20 years	12,584	9,039
In more than 20 years but not more than 30 years	10,184	6,920
In more than 30 years but not more than 40 years	6,351	4,476
More than 40 years	16,496	16,719
	61,917	53,136

This note indicates the period of the next re-pricing date for variable rate loans and the maturity date for fixed rate loans.

6d Loan principal outstanding - analysis by country

	2012 Principal outstanding £m	2011 Principal outstanding £m
England	50,780	42,450
Wales	2,734	2,733
Scotland	8,403	7,953
	61,917	53,136

7 New issue, maturity and early redemption of loan principal

	2012 £m	2011 £m
New loans	16,111	5,255
Loans maturing	(1,720)	(1,607)
Loans redeemed early	(5,610)	(1,730)
Net increase in loan principal	8,781	1,918

8 Amounts owed to National Loans Fund

	2012 £m	2011 £m
Loan principal outstanding to borrowers	61,917	53,136
Accrued income on loans to borrowers	708	557
	62,625	53,693
Loan repayments not yet surrendered to National Loans Fund	49	51
	62,674	53,744

9 Reconciliation of operating income to net cash
(used in) / from operating activities

	Note	2012 £m	2011 £m
Operating income		4,503	2,978
Increase in loan principal outstanding to customers (Increase) / decrease in accrued income	7	(8,781) (151)	(1,918) 1
Net cash (used in) / from operating activities		(4,429)	1,061

10 Risk management

The PWLB's management of its risk exposure is described below.

Credit risk

Credit risk is the risk that a counterparty will fail to discharge a contractual obligation, resulting in financial loss to the PWLB. Any such loss would be borne by the National Loans Fund.

Risk measurement

The credit risk exposures of the PWLB are shown below:

	Cash held at bank*	Major local authorities	Parish councils and drainage boards	Harbour boards	Total
	£m	£m	£m	£m	£m
2012					
Cash and balances at bank	49	-	-	-	49
Loans outstanding to borrowers	-	62,296	327	2	62,625
Total	49	62,296	327	2	62,674
Loans confirmed but not advanced	-	-	-	-	-
2011					
Cash and balances at bank	51	-	-	-	51
Loans outstanding to borrowers	-	53,361	330	2	53,693
Total	51	53,361	330	2	53,744
Loans confirmed but not advanced	-	4	-	-	4

* The PWLB's banking services are provided by the Government Banking Service.

The value of the loans above are based on carrying amounts as reported in the statement of financial position.

There were £255 million overdue loan repayments at 31 March 2012 (31 March 2011: less than £1 million). The majority of these arose because the payment fell on a weekend and so were duly paid the next working day. All overdue loan repayments at 31 March 2012 have since been paid.

There were no renegotiated loans or assets considered impaired at 31 March 2012 (31 March 2011: no renegotiated loans or impaired assets).

Loans for which payment schedules had been amended in order to facilitate more efficient administration by local authorities are not considered to constitute renegotiated loans in credit risk terms.

The risk of default is not perceived to have increased materially during the year.

The PWLB does not issue any financial guarantees.

Risk management

As stated on page 9, the PWLB Commissioners are legally required before making a loan to satisfy themselves that there is sufficient security for its repayment.

The PWLB obtains all necessary information from borrowers to gain assurance that the authority is acting appropriately and within the framework set out in the PWLB's circulars.

The PWLB lends only to local authorities and other prescribed bodies.

Loans to local authorities, together with related interest, are automatically secured by statute on all revenue streams of the borrower.

Parish, town and community council applicants for loans need borrowing approval from the Department for Communities and Local Government, or, in the case of Welsh councils, the Welsh Assembly Government. Drainage board applicants for loans need a loan sanction from the Department for Environment, Food and Rural Affairs.

Loans to harbour boards are secured on property and are made only with the provision of a guarantee from the local authority. In addition, the business

plan is reviewed. No new loans were made to harbour boards in the year ended 31 March 2012 (31 March 2011: no loans).

The PWLB does not differentiate borrowers by credit rating.

The PWLB continuously monitors its total lending against a limit set by statute.

Market risk

Market risk is the risk that the fair value of a financial instrument will fluctuate because of changes in market prices.

Market risk comprises interest rate risk, currency risk and other price risk. The PWLB's activities do not give rise to interest rate risk for the PWLB itself, but form part of the interest rate risk profile of the National Loans Fund.

There is no exposure to currency risk or other price risk.

Liquidity risk

Liquidity risk is the risk that the PWLB will encounter difficulty in meeting obligations associated with financial liabilities.

The PWLB's activities are not considered to give rise to liquidity risk for the PWLB itself, but rather form part of the liquidity risk profile of the National Loans Fund. The PWLB's cash flow requirements are forecast and monitored daily.

11 Related party transactions

The PWLB is a statutory body operating within the United Kingdom Debt Management Office, an executive agency of HM Treasury. During the year, the PWLB had a significant number of material transactions with the National Loans Fund, a fund which is administered by HM Treasury. The National Loans Fund lends cash to the PWLB so that it can subsequently lend the cash to its borrowers. In turn the PWLB will return cash to the National Loans Fund

as its loans to borrowers are redeemed.

The total amount owed by the PWLB to the National Loans fund at 31 March 2012 was £62,674 million.

The key management personnel of the PWLB, the Secretary and Assistant Secretary of the PWLB, had no transactions with the PWLB during the year and were remunerated by the United Kingdom Debt Management Office.

12 Date of authorisation for issue

The Secretary of the PWLB has authorised these accounts for issue on 13 June 2012.

Accounts Direction



Accounts Direction given by HM Treasury in accordance with section 3 (6) of the National Loans Act 1968

1. This direction applies to the Public Works Loan Board.
2. The Public Works Loan Board shall prepare accounts for the year ending 31 March 2012 and each subsequent financial year, which give a true and fair view of its state of affairs at the reporting date, and of its income and expense and cash flows for the year then ended.
3. The accounts shall be prepared in accordance with applicable accounting standards, and shall be consistent with relevant requirements of the extant Government Financial Reporting Manual.
4. The accounts shall present a statement of comprehensive income, a statement of financial position and a statement of cash flows. The statement of financial position shall present assets and liabilities in order of liquidity.
5. The notes to the accounts shall include disclosure of assets and liabilities, and of income and expense, relating to other central government funds including the National Loans Fund.
6. The report shall include:
 - (i) a foreword
 - (ii) a management commentary, including information on financial performance and financial position; and
 - (iii) a governance statement.
7. This accounts direction shall be reproduced as an appendix to the accounts.
8. This accounts direction supersedes all previous Directions issued by HM Treasury.

Chris Wobschall

Deputy Director, Assurance and Financial Reporting Policy, HM Treasury

23 March 2012



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Published by TSO (The Stationery Office) and available from:

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www.tsoshop.co.uk

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