National Loans Fund Account 2016-17

HC 186 July 2017

National Loans Fund Account 2016-17

Presented to Parliament pursuant
to Section 21(1) of the National
Loans Act 1968

Ordered by the House of Commons
to be printed on 18 July 2017

HC 186

This publication is available at www.gov.uk/government/publications

Any enquiries regarding this publication should be sent to us at public.enquiries@hmtreasury.gsi.gov.uk

Print ISBN 9781474144797
Web ISBN 9781474144803
PU2085

Printed in the UK by the Williams Lea Group on behalf of the Controller of Her Majesty's Stationery Office

ID 11051711 07/17

Printed on paper containing 75% recycled fibre content minimum

CONTENTS

Performance Report

Overview

Purpose and activities of the National Loans Fund

The National Loans Fund (NLF) was established on 1 April 1968 by the National Loans Act 1968 to account for government borrowing and lending which were until then accounted for as part of the Consolidated Fund (CF). The CF was first set up in 1787 as ‘one fund into which shall flow every stream of public revenue and from which shall come the supply for every service’. The NLF was set up in order to separate government revenue and expenditure on the one hand and government borrowing and lending on the other. The accounts for the CF and NLF are now published separately.

Both the CF and NLF are administered by the Treasury with the bank accounts maintained at the Bank of England. The CF can therefore be regarded as central government’s current account whereas the NLF can be regarded as central government’s main borrowing and lending account. Most of the NLF’s borrowing needs are now met indirectly through borrowing on its behalf by the Debt Management Office (DMO) and National Savings and Investments (NS&I).

The DMO was established as an executive agency of the Treasury on 1 April 1998. Its remit is ‘to carry out the Government’s debt management policy of minimising financing costs over the long term, taking account of risk, and to minimise the cost of offsetting the Government’s net cash flows over time, while operating in a risk appetite approved by Ministers in both cases’. Its operations are managed through the Debt Management Account (DMA) which is a bank account at the Bank of England linked closely with the NLF. As the Government’s debt manager, the DMO has a key role in the issue of gilt-edged securities on behalf of the Treasury. Gilt-edged securities, or gilts, are UK Government sterling-denominated listed bonds. There are two main types: conventional (i.e. fixed rate) gilts and index-linked gilts on which the return is linked to movements in the Retail Prices Index (RPI). They are issued from the NLF and sold into the market by the DMO. In addition, the DMO issues Treasury Bills from the DMA and undertakes other money market operations to meet the Government’s daily cash requirements. Further details on these operations can be found in the Debt Management Report 2017-18[1] published by the Treasury in March 2017.

The Exchange Equalisation Account (EEA) was established in 1932 to provide a fund that could be used when necessary to regulate the exchange value of sterling. It holds the UK’s reserves of gold, foreign currency assets and International Monetary Fund (IMF) Special Drawing Rights. Combined with the UK’s Reserve Tranche Position (RTP) with the IMF, these assets comprise the UK’s official holdings of international reserves. The RTP is an asset of the NLF. The Bank of England acts as the Treasury’s agent in the day-to-day management of the EEA.

The NLF’s main role is to meet the finance needs of the CF to the extent that taxation and other receipts are insufficient to meet the CF’s outgoings. To this end the NLF undertakes borrowing and uses the proceeds to meet any deficits on the CF; conversely, any net surpluses on the CF are passed to the NLF to reduce the latter’s need to borrow or to increase the amount that it can lend. The NLF finishes every day with a nil balance on its bank account because any cash surpluses or deficits are offset by transfers to or from the DMA.

The NLF’s borrowing operations include the temporary borrowing of balances in various government bank accounts that are surplus to immediate requirements. Such borrowing minimises the amount that the NLF needs to borrow from other sources. Where the money borrowed in this way already counts as Exchequer money, interest is not paid. For the rest of its borrowing however the NLF normally has to pay interest. If the NLF’s interest income is less than the interest it pays on its borrowings, which it generally is, the shortfall is met by a transfer from the CF.

The NLF provides finance for both the DMA and EEA so surpluses and deficits of the DMA and EEA are income and expenditure of the NLF and their net assets are assets of the NLF. It also makes loans to various statutory

[1] https://www.gov.uk/government/publications/debt-management-report-2017-to-2018

public sector bodies and provides the finance needed by the Public Works Loan Board (PWLB) for its loans to prescribed bodies, mainly local authorities. The profits of the Issue Department of the Bank of England are also paid to the NLF under section 9(1) of the National Loans Act 1968. The Issue Department is solely concerned with the issue of banknotes and the assets backing them. NS&I's savings products are liabilities of the NLF.

As the vast majority of the assets of the NLF comprise the advances to and net assets of the DMA and EEA and advances to the PWLB, the NLF is not exposed to significant credit risk. Further detail on how credit risk is managed is included in note 15 to the accounts. By virtue of section 19(1) of the National Loans Act 1968, the net liabilities of the NLF are a liability of the CF. The servicing of the NLF's liabilities is expected to be mainly met through future tax revenue receipts. There is no reason to believe that tax revenues will not be forthcoming and therefore, in accordance with the Government Financial Reporting Manual, it has been concluded as appropriate to adopt the going concern basis of preparation for the NLF Accounts.

Key issues and risks

The key issues and risks facing the NLF are considered in the governance statement on pages 9 to 13. In addition, the financial risks related to the NLF are separately disclosed in note 15 on page 33 to 40.

Performance summary

The total comprehensive net expenditure of the NLF decreased by £4.6 billion from £38.3 billion in 2015-16 to £33.7 billion in 2016-17 primarily due to an increase in Other income of £8.0 billion from £6.2 billion in 2015-16 to £14.2 billion in 2016-17 partly offset by an increase in Financing costs of borrowing of £3.2 billion from £48.3 billion in 2015-16 to £51.5 billion in 2016-17.

The NLF's total gross assets increased by £18.7 billion from £325.6 billion in 2015-16 to £344.3 billion in 2016-17. Total gross liabilities increased by £73.6 billion from £1,814.4 billion in 2015-16 to £1,888.0 billion in 2016-17. As a result net liabilities increased by £54.9 billion from £1,488.8 billion in 2015-16 to £1,543.7 billion in 2016-17. Further details can be found in the Performance analysis.

Performance analysis

International Support

The UK has continued to support the International Monetary Fund (IMF) through the NLF in 2016-17 in line with our commitments as an IMF member. The UK has provided such support through its quota subscription and other lending to the Fund. The IMF's 14th General Quota Review, which involved a package of reforms of the Fund's governance and quota, became effective on 26 January 2016. As part of this reform package the UK's quota increased to SDR 20.2bn (£22.0bn). The UK's 2012 bilateral loan agreement (BLA) to the IMF worth SDR 9,178.0 million (£10,000.5 million) also became effective when the UK's quota was increased and the size of the UK's commitment under the New Arrangements to Borrow (NAB) was reduced by the amount of the BLA to SDR 9,479.0 million (£10,328.5 million). The 2012 BLA expired without being used at the end of 2016. The UK agreed to a third bilateral loan facility (2016 bilateral loan) to the IMF again worth SDR 9,178.0 (£10,000.5 million) in October 2016. The NLF's net exposure to the IMF of £5.3 billion at 31 March 2017 (2015-16: £5.2 billion) is described in note 9 and comprises the reserve tranche position of £4.0 billion (2015-16: £3.5 billion) and loans of £1.3 billion (2015-16: £1.7 billion). The IMF maintains precautionary balances of retained earnings to absorb any losses it may incur. As at 31 March 2017, any losses that may be incurred by the IMF on loans to its member countries are not expected to result in losses to the NLF.

The UK's bilateral loan facility to Ireland has been funded by HM Treasury's Vote which is funded through the normal Supply procedures. Details can be found on the GOV.UK website[2]. The UK has a contingent liability in respect of European Union (EU) mechanisms that provide financial assistance to EU Member States and Third Countries including loans from the European Financial Stabilisation Mechanism, European Balance of Payments Facility, Macro Financial Assistance and the European Investment Bank. The CF is responsible for this contingent liability and details can be found in the Consolidated Fund Account 2016-17. The NLF is not party to either the bilateral loan to Ireland or the EU financial assistance arrangements.

Asset Purchase Facility

The Asset Purchase Facility was set up in 2008-09 at the Bank of England and is authorised to purchase assets financed by the issuance of central bank reserves (a process known as 'quantitative easing'). In August 2016, the limit on purchases that may be undertaken by the APF was increased by £70 billion from £375 billion to £445 billion of which £10 billion could be eligible private sector assets and £60 billion is additional gilts. As at 31 March 2017, on an amortised cost basis, £387.8 billion (2015-16: £338.8 billion) of gilts from the NLF were held by the Bank of England for quantitative easing. Excess cash held in the facility, which arises largely from coupons on these gilts, is transferred to the Exchequer via HM Treasury from where it is paid to the CF as Extra Receipts. More information on the scheme can be found on the Bank of England's website[3].

Funding for Lending Scheme (FLS)

The FLS is designed to incentivise banks and building societies to boost their lending to the UK real economy. It was launched in July 2012 and subsequently extended, most recently to allow participants to borrow from the FLS until January 2018. The NLF issues Treasury Bills for sale to the DMA which makes them available to be borrowed by the Bank of England. Banks and building societies participating in the FLS can then borrow Treasury Bills from the Bank of England in exchange for eligible collateral. As at 31 March 2017, on an amortised cost basis, £75.1 billion (2015-16: £86.4 billion) of Treasury Bills issued to the DMA by the NLF for the FLS are outstanding. More information can be found on the Bank of England's website[4].

Outturn for 2016-17

The total comprehensive net expenditure of the NLF decreased by £4.6 billion from £38.3 billion in 2015-16 to £33.7 billion in 2016-17 primarily due to an increase in Other income of £8.0 billion from £6.2 billion in 2015-16 to £14.2 billion in 2016-17 partly offset by an increase in Financing costs of borrowing of £3.2 billion from £48.3 billion in 2015-16 to £51.5 billion in 2016-17.

[2] https://www.gov.uk/government/publications/bilateral-loan-to-ireland
[3] http://www.bankofengland.co.uk/markets/Pages/apf/default.aspx
[4] http://www.bankofengland.co.uk/markets/pages/fls/default.aspx

The increase in Other income was mainly due to a higher gain by the DMA of £6.3 billion and higher gain by EEA of £1.7 billion while the increase in Financing costs of borrowing was mainly as a result of £3.1 billion higher financing costs of gilts.

The total comprehensive net income from the DMA was £10.1 billion in 2016-17 and is reported against Other income in the Statement of Comprehensive Net Expenditure; this compares to net income of £3.8 billion in 2015-16 (reported against Other income). The £6.3 billion difference is primarily due to £5.8 billion gain on the fair value of DMA gilt holdings compared to a loss of £0.5 billion in 2015-16. The total comprehensive net income from the EEA was £3.6 billion in 2016-17 (reported against Other income) compared to net income of £1.9 billion in 2015-16 (reported against Other income). The £1.7 billion difference was largely due to a £1.0 billion increase in net trading income and £0.8 billion increased fair value gain on gold as a result of an increase in the price of gold during 2016-17. Further information on the DMA and EEA can be found in their respective accounts which are published separately.

Excluding the profits and total comprehensive net income/expenditure of other entities, the NLF's total comprehensive net expenditure was £3.2 billion higher at £47.7 billion in 2016-17 compared to £44.5 billion in 2015-16, primarily as a result of higher financing costs of gilts:

	Note	**2016-17 £m**	2015-16 £m
Total comprehensive net expenditure		**33,674**	38,327
EEA total comprehensive net income	5	**3,649**	1,939
DMA total comprehensive net income	5	**10,154**	3,805
Profits of the Bank of England Issue Department	5	**241**	407
		47,718	44,478

Assets

The NLF's total gross assets increased by £18.7 billion from £325.6 billion in 2015-16 to £344.3 billion in 2016-17. This was primarily due to increases in advances of £3.3 billion (consisting of a decrease in advance to the DMA of £5.0 billion, an increase in advance to the EEA of £6.5 billion and an increase in advance to the PWLB of £1.8 billion), an increase in the IMF Quota Subscription & Lending of £1.8 billion (consisting of a £2.2 billion exchange rate gains relating to the Quota subscription and a decrease of £0.4 billion on loans repaid and exchange rate gains relating to IMF Lending) and an increase in Other assets of £13.5 billion. The increase in Other assets was primarily an increase in the net assets of the DMA of £10.1 billion and an increase in the net assets of the EEA of £3.6 billion.

Liabilities

Total gross liabilities increased by £73.6 billion from £1,814.4 billion in 2015-16 to £1,888.0 billion in 2016-17. This is largely a result of gilt-edged stock increasing by £77.6 billion from £1,525.2 billion to £1,602.8 billion, NS&I liabilities increasing by £11.8 billion from £135.1 billion in 2015-16 to £146.9 billion in 2016-17 (reflecting significant inflows from Premium bonds, Index Linked Savings Certificates and Income Bonds) and liabilities to the IMF increasing by £1.7 billion from £16.2 billion to £17.9 billion partly offset by Treasury Bill issuance for the Funding for Lending scheme decreasing by £11.3 billion from £86.4 billion to £75.1 billion.

Public Sector Net Debt

As a result of these changes, the net liabilities of the Fund increased by £54.9 billion from £1,488.8 billion to £1,543.7 billion. This is matched by a corresponding claim on the CF. The NLF lends to and borrows from other parts of the public sector. For example it makes advances to the PWLB and borrows directly from a range of public sector bodies (as described in note 12). In addition, some of the gilts it has issued are held in the public sector, including by the DMA which retains a portfolio of gilts for use as collateral for its money market activities and by the Bank of England under the Asset Purchase Facility. The DMA also has large advances to and from the NLF. Therefore, the NLF's net liabilities do not equate to the Public Sector Net Debt ("PSND"), which is a calculation of the net debt of the whole of the public sector after eliminating intra-public sector balances. Figures for PSND are published jointly by HM Treasury and the Office for National Statistics in the monthly *Public Sector Finances Statistical Bulletin* which can be found on the Office for National Statistics and GOV.UK websites.

Forward Look

Net financing requirement

The Debt Management Remit for 2017-18 was published by the Treasury with the Budget in March 2017 and subsequently revised following publication of the 2016-17 Central Government Net Cash Requirement (CGNCR) Outturn: Update to the DMO Financing Remit 2017-18[5]. On the basis of a CGNCR forecast for 2017-18 of £47.4 billion (excluding NRAM plc, Bradford and Bingley and Network Rail), the revised Net Financing Requirement to be met by the DMO is £104.7 billion (following upward adjustments including £79.5 billion for gilt redemptions and planned financing for the reserves of £6 billion and downward adjustments including £13 billion for the net contribution from National Savings & Investments). The DMO will meet this requirement by gross gilt sales of £114.2 billion (gilts issued by the NLF) partly offset by a total net contribution of Treasury bills for debt financing (through the DMA) of -£9.5 billion.

PWLB

Following a review of the role of the Public Works Loan Commissioners, the Infrastructure Act 2015 introduced a provision to enable HM Government to abolish the PWLB using the Public Bodies Act 2011. In May 2016 a consultation was launched on the transfer of functions from the PWLB to another entity. The results of this consultation were published in November 2016, concluding that the PWLB should be abolished and its powers transferred to HM Treasury. The reforms only affect the governance arrangements and do not change any of the policy or operational aspects of lending to local authorities, the existing lending or loan repayment arrangements for borrowers or the arrangements with the NLF.

Section 4 (1) of the National Loans Act 1968 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 billion to £70 billion. Section 300 of the Finance Act 2014 (which requires authorisation by HM Treasury to come into force), allows a further increase of the limit up to £95 billion (principal) on the total of loans outstanding to the PWLB at any one time.

Notification to leave the EU – Article 50

On 29 March 2017, the UK Government submitted its notification to leave the EU in accordance with Article 50. The triggering of Article 50 starts a two-year negotiation process between the UK and the EU. Any subsequent changes in legislation, regulation and funding arrangements are subject to the outcome of the negotiations. During this two year period, which includes the full duration of the next accounting period, the UK remains a full member of the EU with all the rights and obligations arising from membership. There are no significant impacts on the financial statements in the short term from making the formal notification.

Long-term expenditure trends

Since the function of the NLF is to account for government borrowing and lending, it has no long-term expenditure trends.

Tom Scholar
Accounting Officer
HM Treasury

11 July 2017

[5] http://www.dmo.gov.uk/documentview.aspx?docname=remit/sa250417.pdf&page=Remit/full_details

Accountability report

The accountability report contains a Corporate governance report and a Parliamentary accountability and audit report. The purpose of the corporate governance report is to explain the composition and organisation of the National Loans Fund's governance structures and how they support the achievement of the National Loans Fund's objectives. It includes the Statement of Accounting Officer's responsibilities and the Governance statement. The Parliamentary accountability and audit report includes key Parliamentary accountability information on regularity of expenditure and remote contingent liabilities as well as the Certificate and Report of the Comptroller and Auditor General to the House of Commons.

Corporate governance report

Directors' report

Operationally, the NLF is part of HM Treasury and its staff are employees of HM Treasury. The NLF itself therefore has no employees of its own.

Directors' conflicts of interest

In 2016-2017, no material conflicts of interest have been noted by the senior management overseeing the NLF.

Personal data related incidents

The NLF does not hold any protected personal data.

Statement of Accounting Officer's responsibilities

Under section 21(1) of the National Loans Act 1968 HM Treasury is required to prepare an account relating to the National Loans Fund for each financial year in the form and on the basis considered appropriate by the Treasury. The Account is prepared on an accruals basis and must give a true and fair view of the state of affairs of the Fund and of its Comprehensive Net Expenditure and cash flows for the financial year.

In preparing the Account the Accounting Officer is required to:

- observe the relevant accounting and disclosure requirements of the Government Financial Reporting Manual in so far as they are relevant to the Account and apply suitable accounting policies on a consistent basis;
- make judgements and estimates on a reasonable basis; and
- prepare the accounts on a going concern basis as defined in the Government Financial Reporting Manual.

The Treasury has appointed its Permanent Secretary, Tom Scholar, as Accounting Officer of the National Loans Fund.

The responsibilities of an Accounting Officer, including responsibility for the propriety and regularity of the public finances for which the Accounting Officer is answerable and for keeping proper records, are set out in Managing Public Money published by the Treasury.

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

The Accounting Officer confirms that the annual report and accounts as a whole is fair, balanced and understandable and that he takes personal responsibility for the annual report and accounts and the judgments required for determining that it is fair, balanced and understandable.

Audit arrangements

The NLF accounts are audited by the Comptroller and Auditor General (C&AG) under the requirements of the National Loans Act 1968. The National Audit Office (NAO) bears the cost of all external audit work performed on the NLF. No non-audit work was undertaken by the NAO in relation to the NLF in 2016-17.

Governance Statement

1. Governance Framework

1.1 The NLF is managed within the Treasury's overall risk and governance framework as set out in the Treasury's Annual Report and Accounts 2016-17. This includes the Treasury Board's assessment of its compliance with the Corporate Governance Code.

1.2 The Chancellor of the Exchequer, as Minister in charge of the Treasury, is responsible and answerable to Parliament on all the policies, decisions and actions of the Treasury, and ultimately of the NLF.

1.3 The previous acting Permanent Secretary, John Kingman, was Accounting Officer for the NLF from 1 April 2016 to 30 June 2016. I have been Permanent Secretary to the Treasury and Accounting Officer for the NLF since 1 July 2016. As Accounting Officer for the NLF, I am personally responsible and accountable to Parliament for the organisation and quality of management of the NLF, including its use of public money and the stewardship of its assets, in line with those responsibilities assigned to me in Managing Public Money.

(a) Audit Committee

1.4 The Treasury Group Audit Committee is a subcommittee of the Treasury Board, and is tasked with supporting me in my role as Principal Accounting Officer, and the Treasury's Additional Accounting Officers in their responsibilities for managing risk, internal control and governance related to the Treasury Group's Annual Report and Accounts, the Central Funds (Consolidated Fund, National Loans Fund, Contingencies Fund and Exchange Equalisation Account) and the Whole of Government Accounts. Details on the overall risk and governance structure of HM Treasury can be found in the Governance Statement in the Treasury's Annual Report and Accounts.

1.5 I appoint members of the Committee for periods up to three years, extendable by one additional three-year period. The Chair of the Committee (Richard Meddings) reports directly to me and is also a non-executive Member of the Treasury Board. The membership of the Audit Committee at the close of 2016-17 was:

- Richard Meddings – Member of the Supervisory Board at Deutsche Bank and Deutsche Bank Audit committee chair and member of Risk Committee; Non-executive director, Legal & General PLC (2014 to 2017) and Risk Committee chair; Main Board Director (2002-2014) and Group Finance Director (2006-2014) Standard Chartered PLC; Non-executive director and Senior Independent Director of 3i Group PLC (2008-2014) and chair of Audit and Risk Committee; Financial Reporting Review Panel in FRC; Board member of International Chambers of Commerce UK (2007 to current); and Trustee on Teach First Board.

- Tim Score - Non-executive director and Chair of Audit Committee at Pearson PLC; Non-executive director and Chair of Audit Committee at the British Land Company PLC; Chief Financial Officer of ARM Holdings PLC (2002-2015); Senior independent director, Chair of Audit and Interim Chairman at National Express Group (2005-2014); CFO of Rebus Group and William Baird PLC; Group Financial Controller at BTR Plc and LucasVarity PLC.

- Peter Estlin - Alderman & Sheriff of the City of London; Senior Advisor, Barclays PLC., (previously Group Financial Controller and acting Group CFO); Governor, Bridewell Royal Hospital; Board Member, Trust for London; Trustee, Morden College; Commissioner, Royal Borough of Greenwich Fairness Commission.

- Zarin Patel (from 1 March 2017) – Non-executive Director of John Lewis Partnership and member of its Audit and Risk Committee; formerly Chief Operating Officer of The Grass Roots Group PLC; previously Chief Financial Officer at the BBC and a member of its Executive Board.

- Jacinda Humphry (from 1 March 2017) - Finance Director, Department for Communities and Local Government; previously Director of Planning, Portfolio and Performance Management at the Department for Work and Pensions (DWP).

1.6 The Audit Committee met six times during 2016-17, taking the opportunity for pre-committee discussions with the NAO on each occasion. Attendance is outlined in the table below:

	Eligible to attend	Attended
Richard Meddings (Chair)	6	6
Tim Score	5	5
Mary Hardy (up to 31 December 2016)	5	4
Peter Estlin	6	5
Abhai Rajguru (up to 31 October 2016)	4	3
Zarin Patel	1	1
Jacinda Humphry	1	1

1.7 The Audit Committee has a robust Conflicts of Interest Policy, which requires members to excuse themselves from discussions where potential conflicts may occur. Members are required to inform me about any potential conflicts and highlight these at the start of each meeting as appropriate.

1.8 In addition to the independent members, the appropriate Accounting Officers, HM Treasury's Group Director of Finance and the Treasury Accountant (or, in her absence, the Exchequer Accounts Manager) also attend Committee meetings. Members have the opportunity for a pre-committee discussion with the NAO, Group Head of Internal Audit for HM Treasury and Head of Exchequer Funds Internal Audit (EFIA).

1.9 Over the course of the year, as well as scrutinising the Treasury's financial management and balance sheet risks, the Audit Committee considered a wide range of issues relating to the department's framework of governance, risk management and control. The Audit Committee challenged and approved the Internal Audit work programme throughout the year and followed up on management action to address audit recommendations.

1.10 Outside the planned committee meetings individual members have shared their commercial and professional expertise with key officials across the Treasury.

1.11 The external auditor is the Comptroller and Auditor General and the NAO attend all Audit Committee meetings on his behalf.

1.12 The Audit Committee receives all NAO reports and a summary of EFIA reports relating to the NLF plus underlying reports on internal audits where issues are identified leading to Red or Amber assessments (one such report in 2016-17 and no such report in 2015-16).

(b) Exchequer Funds Internal Audit (EFIA)

1.13 Internal Audit for the NLF is provided by EFIA which reports directly to both me and the Audit Committee on audit reporting matters.

1.14 For the NLF, an annual risk-based internal audit programme is agreed with the Treasury Accountant (or, in her absence, one of her managers) in advance of the Audit Committee's approval. The work programme always includes a review of the receipts and payments process, due to the very high value of payments made by the NLF. The Audit Committee reviews the work programme and is kept informed of progress and amendments.

(c) Management of the National Loans Fund

1.15 The NLF is managed by the Treasury Accountant and her managers within the Exchequer Funds and Accounts (EFA) Team of HM Treasury. The EFA team reports any matters concerning the NLF directly to me.

(d) Reporting to the Treasury's Boards

1.16 The Economic, Fiscal and Operational Risk Groups, each chaired by a member of the Executive Management Board, give evidence to the Treasury Board and its Sub-committee. EFA's risks are regularly reported to the Operational Risk Group.

1.17 The Chair of the Audit Committee is invited to report concerns or issues to the Treasury Board (Sub-committee), and is a Non-Executive member of the Treasury Board.

2. Risk management

2.1 EFA is managed within the Treasury's risk management framework as set out in the Treasury's Annual Report and Accounts. The Treasury Accountant and her managers have overall responsibility on a day-to-day basis for risk management of those Funds managed by EFA, and for ensuring that my financial, regularity and propriety responsibilities as Accounting Officer of the NLF are discharged appropriately. She is supported by members of EFA management who are responsible for ensuring that the tasks in their areas are compliant with operational policies and procedures, and legislation. EFA management provide me with a quarterly update report on changes to the control environment and changes in risk exposure.

2.2 Risk management is key to all processes within EFA, including business continuity resilience planning for those public funds for which EFA is responsible. Business continuity resilience is regularly tested locally and with business partners, and lessons learned feed into improved business continuity processes. The risk management strategy includes periodic horizon scanning to identify any changes in risk exposure, to evaluate the change and to identify appropriate mitigating actions. Significant risk issues are recorded in a risk register and are assessed by likelihood and impact. A risk owner, who is responsible for managing the risk, is assigned to each risk. The risk register is reviewed quarterly by EFA management, and is circulated to me alongside the quarterly risks and controls report.

2.3 There are sufficient experienced staff in the EFA team with an appropriate range and breadth of knowledge to manage the NLF, covering absences as necessary and maintaining resilience. EFA management ensures that staff members working on the NLF are trained and equipped to manage risk in a way appropriate to their authority and duties. Training on risk awareness and management is provided as required, either by management or by attending appropriate courses. Training is also provided to staff to build the team's capability and to increase its resilience. EFA team members are encouraged to obtain professional qualifications in areas that are relevant to their roles.

3. The system of internal control

3.1 As Accounting Officer, I am responsible for maintaining a sound system of internal control that supports the achievement of the NLF's policies, aims and objectives, whilst safeguarding the public funds and assets, for which I am personally responsible, in accordance with the responsibilities assigned to me in Managing Public Money.

3.2 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, rather than eliminate all risk. It can therefore only provide reasonable and not absolute assurance of effectiveness. The system of internal control is based on an ongoing process designed to identify and prioritise the risks to the achievement of the NLF's policies, aims, and objectives; to evaluate the likelihood of those risks being realised and the impact should they be realised; and to manage them efficiently, effectively and economically.

3.3 The system of internal control has been in place throughout the year ended 31 March 2017 and up to the date of approval of the financial statements, and accords with Treasury guidance. During the year, there were no significant changes to the control environment.

4. Risk profile

4.1 The NLF is managed generally within the framework of the Treasury's system of internal control. This framework includes resourcing the administration of the NLF, security and the management of risks across the Treasury's business.

4.2 The key risks in managing the NLF and their associated controls are:

- **Irregularity of transactions, including fraudulent or erroneous payments:** Clear separation of duties is enforced by appropriate user permissions within the accounting system and payment approval panels. Up-to-date policy and procedures manuals including job instructions are readily accessible to all operational staff. Payment instructions are computer-generated and are derived from underlying transaction records. This minimises the risk of keying errors. Separately, the Comptroller and Auditor General, through the NAO Exchequer Section approves NLF payments in advance and reconciles NLF transactions on a daily basis. There is also a clear and comprehensive audit trail in the IT system, to which the NAO Exchequer Section has real-time access.

- **Incorrect accounting:** Application controls exist within the IT system used to manage financial transactions and account for receipts and payments on the NLF. Interest and amortisation are generated automatically by the accounting system at month end using pre-defined rules. New general ledger accounts are authorised by the Treasury Accountant or one of her managers before being set up. Gilts issuances are reported to senior management and key operational staff. EFA reconciles the dividend claims received from the gilts registrar with its own records prior to each interest payment. The Debt Management Office reconciles principal amounts twice a year. Monthly management accounts for the NLF are also produced and reviewed by the Treasury Accountant or the Exchequer Accounts Manager, and are provided to me. The accounting for any unusual transactions is suitably considered.

- **Failure of IT systems:** The Nippon Telegraph and Telephone Corporation (NTT) data centre offers high levels of resilience with the data centre platform availability set to 99.9% and the network connectivity availability set to 99.99%. NTT has dual centres which provides a high level of resilience. As part of disaster recovery measures, there is an Active/Active configuration across the two data centres, which ensures a superior level of availability across both sites with near instant failover. EFA also has its own contingency plans in place.

- **Failure to provide an effective service in adverse circumstances, including disaster situations:** To ensure operational resilience in key areas in the event of a threat to business continuity, staff within EFA are trained to provide cover for times when other staff members are absent. Measures are in place to facilitate the NAO Exchequer Section's normal payments approval process in the event of disruption to enable the essential payments business to continue. The risks that impact upon EFA's key stakeholders are managed by their involvement in business continuity planning and testing. Business continuity arrangements are regularly reviewed and tested within the framework of the Treasury's corporate Business Continuity Plan facilities.

- **Failure of principal counterparties to provide agreed services:** Well-developed Service Level Agreements (SLAs) for the provision of services from all principal counterparties are in place. They cover details of the monitoring and control arrangements that both parties are expected to observe. Bi-annual meetings are held with managers at the Bank of England where service levels are discussed. A monthly report of any failure to meet the service requirements is also sent to the Bank of England by EFA. A monthly meeting is held with Government Banking management where service levels are discussed.

- **Information risk:** Data and information risk are managed in accordance with the Treasury's policies, which involve a range of controls to prevent unauthorised disclosures. These include encryption and physical and IT security. HM Treasury adheres to Cabinet Office guidelines available at https://www.gov.uk/government/publications/security-policy-framework. Further guidance on information security and assurance is available to all Treasury staff on the intranet. EFA's own Data Handling Policy identifies risks specific to EFA. This policy is reviewed as required.

- **Financial risk:** Adverse results of the Debt Management Account and the Exchange Equalisation Account will affect the NLF's results; therefore all financial risks inherent in these accounts are also inherent in the NLF. Responsibility for risk management and the system of internal control is clearly delegated to the Accounting Officers of those accounts, which have their own control frameworks in place.

5. Review of effectiveness

5.1 During the financial year there was an incident involving control failures at a third party supplier resulting in duplicate and delayed payments. The incident was identified and resolved in a timely manner with no loss to the Exchequer. During the incident, controls worked as expected in EFA which helped limit the extent of the initial incident. Following the incident, the supplier's Internal Audit team completed a review of the end-to-end payment process. This Post Incident Review identified the cause of the incident and raised a number of recommendations to strengthen existing controls. These recommendations have since been implemented. In addition, EFIA carried out a separate independent review of the incident and raised a number of actions to strengthen business continuity resilience. These actions have since been closed.

5.2 In line with HM Government guidance, set out within the Corporate Governance Code of Good Practice for central government departments, I have reviewed the effectiveness of the system of internal control. My review is informed by the work of EFIA who provided positive assurance as to the management and control of the NLF in 2016-17, and the executive managers within EFA who have responsibility for the development and maintenance of the internal control framework, as well as comments made by external auditors in their management letter and other reports. I have been supported by the Treasury Group Audit Committee, and risk owners in addressing weaknesses and ensuring continuous improvement of the system is in place. Information about the effectiveness of the Treasury's overall system of governance including board effectiveness, attendance, compliance with the Corporate Governance Code and quality of management information reviewed, is reported in the Treasury's Annual Report and Accounts.

5.3 The Audit Committee considered the 2016-17 accounts in draft and provided me with its views before I formally signed the accounts.

5.4 Other than the incident in paragraph 5.1 above, no significant internal control issues, including data related incidents, have been identified in 2016-17, and no significant new risks have been identified in the year. No ministerial directions have been given in 2016-17.

5.5 In my opinion, the system of internal control was effective throughout the financial year and remains so on the date I sign this report.

Parliamentary accountability and audit report

Regularity of expenditure

The expenditure and income of the NLF were applied to the purposes intended by Parliament.

The borrowings, investments and lending of the NLF were applied to the purposes intended by Parliament.

The above statements have been audited.

Fees and charges

The NLF does not have any fees or charges.

The above statement has been audited.

Remote contingent liabilities

The NLF has two contingent liabilities which fall outside the scope of IAS 37 as the possibility of an outflow of resources is remote. Disclosure of these liabilities is necessary however under Parliamentary reporting requirements.

i) Under the National Loans Act 1968 section 9(3), the NLF has a contingent liability to the Bank of England Issue Department in respect of that part of the assets backing the note issue that is not represented by government securities. This liability would only crystallise if government securities were insufficient to meet demand from holders of notes to exchange them for another instrument. The contingent liability was £70,851 million at 31 March 2017 (£66,172 million at 31 March 2016). No obligations crystallised or expired in 2016-17 (2015-16: none).

ii) The NLF has a contingent liability to the Commissioners for the Reduction of the National Debt (CRND) in respect of unclaimed dividends received in previous years. This represents old uncleared amounts surrendered by the gilts registrar to CRND and then onto the NLF and stood at £29.9 million at 31 March 2017 (£29.3 million at 31 March 2016). This contingent liability would crystallise if holders of gilts requested amounts owed to them in excess of an amount for settlement retained by CRND. No obligations crystallised or expired in 2016-17 (2015-16: none).

The above statements have been audited.

Tom Scholar
Accounting Officer
HM Treasury

11 July 2017

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 National Loans Fund for the year ended 31 March 2017 under the National Loans Act 1968. The financial statements comprise: the Statements of Comprehensive Net Expenditure, Financial Position, Cash Flows, Changes in the Liability of the Consolidated Fund to the National Loans Fund; and the related notes. These financial statements have been prepared under the accounting policies set out within them. I have also audited the information in the Parliamentary Accountability Disclosures that is described as having been audited.

Respective responsibilities of the Treasury, Accounting Officer and Auditor

As explained more fully in the Statement of Accounting Officer's Responsibilities, the Treasury and the Accounting Officer are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. My responsibility is to audit, 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 National Loans Fund's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the National Loans Fund; and the overall presentation of the financial statements. In addition I read all the financial and non-financial information in the Performance Report and Accountability Report, to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by me in the course of performing the audit. 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 National Loans Fund's affairs as at 31 March 2017 and of the total comprehensive net expenditure for the year then ended; and

- the financial statements have been properly prepared in accordance with the National Loans Act 1968 and in the form prescribed by HM Treasury.

Opinion on other matters

In my opinion:

- the Parliamentary Accountability Disclosures to be audited have been properly prepared in accordance with applicable law; and

- the information given in the Performance Report and Accountability Report 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 returns adequate for my audit have not been received from branches not visited by my staff; or

- the financial statements and the Parliamentary Accountability Disclosures to be audited are not in agreement with the accounting records and 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.

Sir Amyas C E Morse
Comptroller and Auditor General

11 July 2017

National Audit Office
157-197 Buckingham Palace Road
Victoria
London SW1W 9SP

Statement of Comprehensive Net Expenditure for the year ended 31 March 2017

	Note	**2016-17 £m**	2015-16 £m
Finance costs of borrowing	2	**51,525**	48,262
Income from lending operations	3	**(3,293)**	(3,667)
Gains on foreign exchange transactions	4	**(548)**	(175)
Other expenditure	5	**174**	107
Other income	5	**(14,184)**	(6,200)
Total comprehensive net expenditure		**33,674**	38,327

The notes on pages 21 to 40 form part of this Account.

Statement of Financial Position as at 31 March 2017

	Note	**At 31 March 2017 £m**	At 31 March 2016 £m
Assets			
Advances	6	**209,843**	206,574
Loans	7	**2,858**	2,822
Other assets	8	**108,353**	94,806
IMF Quota Subscription & Lending	9	**23,223**	21,385
Total assets		**344,277**	325,587
Liabilities			
Gilt-edged stock	10	**1,602,816**	1,525,159
National Savings and Investments products	11	**146,942**	135,149
Other debt:			
FLS Treasury Bills	12	**75,069**	86,387
Other	12	**45,217**	51,477
Liabilities to the IMF	9	**17,946**	16,229
Total liabilities		**1,887,990**	1,814,401
Net liabilities		**1,543,713**	1,488,814
Liability of the Consolidated Fund to the National Loans Fund		**1,543,713**	1,488,814

The notes on pages 21 to 40 form part of this Account.

Tom Scholar
Accounting Officer
HM Treasury

11 July 2017

Statement of Cash Flows for the year ended 31 March 2017

	2016-17	2015-16
	£m	£m
Cash flows from operating activities		
Interest received	**3,323**	3,670
Other receipts	**207**	350
Interest paid	**(45,788)**	(46,870)
Other (outflows) / inflows	**(605)**	100
Transfer from the Consolidated Fund for the cost of debt servicing	**42,863**	42,750
Net cash flow from investing activities	**-**	-
Cash flows from investing activities		
Net decrease in advance to the Debt Management Account	**5,000**	30,000
Net increase in advance to the Public Works Loan Board	**(1,773)**	(810)
Net increase in subscription to the IMF	**-**	(9,063)
Net decrease in loans	**557**	4
Net increase in advance to the Exchange Equalisation Account	**(6,525)**	(2,867)
Net cash (outflow) / inflow from investing activities	**(2,741)**	17,264
Cash flows from financing activities		
Net issuance of government stock	**73,327**	45,943
Net (redemption) / issuance of Treasury Bills for Funding for Lending	**(11,204)**	8,445
Net receipt of cash from National Savings	**10,524**	10,123
Net (decrease) / increase in other sterling borrowing	**(6,276)**	216
Net transfers of IMF non-interest bearing securities	**458**	6,716
Net transfers to the Consolidated Fund	**(64,088)**	(88,707)
Net cash inflow / (outflow) from financing activities	**2,741**	(17,264)
Net change in cash and cash equivalents	**-**	-
Cash and cash equivalents at beginning and end of year	**-**	-

The notes on pages 21 to 40 form part of this Account.

Statement of Changes in the Liability of the Consolidated Fund to the National Loans Fund for the year ended 31 March 2017

	2016-17	2015-16
	£m	£m
Liability of the Consolidated Fund to the National Loans Fund at 1 April	**1,488,814**	1,404,530
Net cash paid to the Consolidated Fund	**64,088**	88,707
Payment from the Consolidated Fund for the cost of debt servicing during the year	**(42,863)**	(42,750)
Total comprehensive net expenditure	**33,674**	38,327
Liability of the Consolidated Fund to the National Loans Fund at 31 March	**1,543,713**	1,488,814

The notes on pages 21 to 40 form part of this Account.

Notes to the Account

1 Accounting Policies

i Accounting convention

The National Loans Fund (NLF) was established on 1 April 1968 by the National Loans Act 1968 to account for government borrowing and lending which were until then accounted for as part of the Consolidated Fund (CF). The NLF Account has been prepared under the historical cost convention and in accordance with International Financial Reporting Standards (IFRSs) as adapted or interpreted for the public sector context in so far as they are relevant to transactions and balances within the NLF.

ii Applicable accounting standards and interpretations issued but not yet adopted

IFRS 9 ‘Financial Instruments’, was issued in July 2014 and is set to replace IAS 39 ‘Financial Instruments: Recognition and Measurement’. It sets out requirements for recognition, measurement, impairment and de-recognition of financial instruments as a single IFRS framework for all financial instruments required or permitted by IFRS. IFRS 9 is effective for reporting periods beginning on or after 1 January 2018. It is expected that the application of IFRS 9 should not have a material impact upon the financial statements of the NLF.

iii Basis of presentation

The NLF Account is stated in millions of pounds sterling (£m). This Account presents the results and transactions of the NLF. The Statement of Financial Position is presented in order of liquidity. The NLF is the government’s main borrowing and lending account. By the nature of government financing, it is expected that the NLF will show a net liability. By virtue of section 19(1) of the National Loans Act 1968, the net liabilities of the NLF are a liability of the CF. The servicing of the NLF’s liabilities is expected to be mainly met through future tax revenue receipts. There is no reason to believe that tax revenues will not be forthcoming and therefore, in accordance with the Government Financial Reporting Manual, it has been concluded as appropriate to adopt the going concern basis of preparation for the NLF Accounts.

iv Recognition of finance income and costs

Premium Bond prizes are recognised in the period to which they relate. Other interest income and costs of financing are determined using the effective interest rate method. The effective interest rate method is a method of calculating the amortised cost of a financial asset or financial liability and of allocating the interest income or interest expense over the expected life of the asset or liability. The effective interest rate is the rate that exactly discounts estimated future cash flows to the instrument’s initial carrying amount. The calculation takes into account premiums or discounts on acquisition or issue of financial assets and liabilities and all the contractual terms of the financial instrument.

The majority of the NLF’s financial assets and liabilities have a fixed return. For those products that have a variable return, the current rate applicable to that product is used in the calculation of the finance income or cost. Gilts with the same maturity and coupon rate are sometimes issued in separate tranches. Because of market conditions each tranche may be issued with a different premium or discount and therefore a different effective interest rate. However, once issued, gilts with the same maturity and coupon rate are indistinguishable from each other and so are accounted for as one issue using a weighted average effective interest rate.

v Recognition of finance income – Special Drawing Rights (SDR)

The IMF remunerates the UK in SDRs on its Reserve Tranche Position (RTP) for balances in excess of SDR 700 million and on its bilateral loans. Under section 3(2) of the Exchange Equalisation Act 1979 any SDRs received by the Government must be treated as assets of the EEA, therefore all SDR income is accounted for in the EEA and not the NLF.

vi Financial assets and liabilities

The assets and liabilities of the NLF are all accounted for as financial assets and liabilities except for those arising from the net assets of the EEA and the DMA which are accounted for as explained in accounting policy ix. The NLF’s financial assets are all designated as loans and receivables. In accordance with IAS 39, financial assets and liabilities are initially recognised at fair value. They are subsequently measured at amortised cost using the effective interest rate method. If gilts are issued by a syndication process, the syndication fees are borne by the NLF and are netted off from gross issuance proceeds as part of the calculation of amortised cost. Other directly related issue costs for assets and liabilities are negligible and are written off as incurred.

The distinction between loans and advances derives from the legislation that governs the operation of the NLF. On loans, interest must be charged at a rate that at least covers the cost that the Fund would have to bear if it were to borrow the same sum for the period of the loan, plus the Treasury's own administration costs. There is no such requirement for advances, although interest is charged at Bank Rate on advances to the DMA. No interest is charged on advances to the EEA. The NLF does not charge interest on its advances to PWLB but interest on loans by the PWLB to local authorities financed by NLF advances is paid to the NLF under section 3(3) of the National Loans Act 1968.

The fair values of the financial assets and liabilities are disclosed in note 13. They are calculated by reference to market prices where instruments are traded on an active quoted market or, where this is not the case, as the net present value of future cash flows.

Impairment of financial assets

Exchequer Funds and Accounts (EFA) assesses at the end of each reporting period whether there is any objective evidence that a financial asset measured at amortised cost is impaired. An asset is impaired if there is objective evidence of impairment as a result of one or more events that occurred after the recognition of the asset (a 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset that can be reliably estimated. Objective evidence used in assessing whether a financial asset is impaired includes financial difficulties experienced by the borrower and breach of loan conditions such as a default or delinquency in interest or principal payments. No impairment losses have been recognised during the year.

vii Foreign currencies

The financial statements of the NLF are presented in sterling which is the Fund's functional currency, being the currency of the primary economic environment in which it operates. Transactions denominated in foreign currencies are recorded at the rate of exchange applicable to the transaction. Monetary assets and liabilities denominated in foreign currencies at the end of the reporting period are reported at the rates of exchange prevailing at that date. Liabilities to the IMF are denominated in sterling but are subject to a revaluation adjustment reflecting movement in the SDR to sterling exchange rate.

viii Administration expenditure

These financial statements reflect activity through, and the financial position of, the NLF. The costs of gilts registration, listing fees and foreign currency debt issuance are met by the NLF. Administration costs such as departmental staff costs and bank charges are borne by the appropriate body and accounted for through their respective accounts.

ix Exchange Equalisation Account and Debt Management Account

Under section 11 of Schedule 5A to the National Loans Act 1968, any excess of the assets of the DMA over its liabilities shall be a liability of the DMA to the NLF. Over time, the NLF has advanced sterling to the EEA in order to finance the UK's reserves of gold, foreign currency assets and IMF Special Drawing Rights. As a result, having been derived from initial NLF financing, the EEA's net assets are ultimately due to the NLF. Annual financial statements are prepared for both the DMA and the EEA. The net assets of the DMA and EEA are reported in Other Assets (note 8) and the total comprehensive net expenditure or income recognised in the Statement of Comprehensive Net Expenditure as Other Expenditure or Other Income (note 5). These NLF assets and net income or expenditure are the result of activity in the EEA and DMA during the year and the various accounting policies applied by them to that activity.

x Critical accounting judgements and key sources of estimation uncertainty

The NLF's accounting policy for impairment losses arising on financial assets is described in vi above. No impairment losses have been recognised in the year. There are no other areas of the financial statements which are reliant on management's judgement in the process of applying the Fund's accounting policies. Fair values are included for disclosure purposes only. Their calculation is described in note 13. As mentioned in accounting policy iv, the majority of the NLF's financial assets have a fixed return. For those products that have a variable return, the current rate applicable to that product is used in the calculation of the finance income or cost. Note 15 applies various assumptions to demonstrate the sensitivity of NLF's assets and liabilities to changes in interest rates, inflation and foreign currency exchange rates.

2 Finance costs of borrowing

	2016-17 £m	2015-16 £m
Gilt-edged stock	**48,631**	45,518
National Savings and Investments products	**2,334**	2,068
Treasury Bills (Funding for Lending)	**429**	507
Other finance costs	**131**	169
Total finance costs of borrowing	**51,525**	48,262

3 Income from lending operations

	2016-17 £m	2015-16 £m
Interest on loans advanced by the National Loans Fund to:		
Public corporations	**45**	46
Central government bodies	**76**	79
	121	125
Interest on loans by the Public Works Loan Board financed by National Loans Fund advances	**2,837**	2,931
Interest on funding advanced to the Debt Management Account	**335**	611
Total income from lending operations	**3,293**	3,667

4 Gains and losses on foreign exchange transactions

	Note	**2016-17 £m**	2015-16 £m
Loss / (gain) on foreign currency borrowing		**26**	(2)
Gain on Reserve Tranche Position at the IMF	9	**(389)**	(93)
Gain on lending to the IMF	9	**(185)**	(80)
Net gain on foreign currency transactions		**(548)**	(175)

5 Other income and expenditure

	2016-17 £m	2015-16 £m
Other expenditure		
Expenditure in respect of depreciation of Issue Department Assets [2]	**171**	104
Miscellaneous expenditure	**3**	3
Total: Other expenditure	**174**	107
Other income		
EEA total comprehensive net income [1]	**(3,649)**	(1,939)
DMA total comprehensive net income	**(10,154)**	(3,805)
Profits of the Bank of England Issue Department [2]	**(241)**	(407)
Income in respect of appreciation of Issue Department Assets [2]	**(137)**	(47)
Written off gilt-edged stock	**-**	-
Miscellaneous receipts	**(3)**	(2)
Total: Other income	**(14,184)**	(6,200)
Net total	**(14,010)**	(6,093)

[1] Of the £3,649m net income received by the EEA, £7 million (2015-16: £1 million) relates to interest income from the IMF Reserve Tranche Position and bilateral loans to the IMF in line with accounting policy v.

[2] Under section 9 of the National Loans Act 1968, the profits of the Issue Department are paid into the NLF. In addition, the Bank of England Issue Department is required by the Currency and Bank Notes Act 1928 to hold investments equal to the value of bank notes in issue. These investments are revalued to market value quarterly. If the market value is less than the value of notes in issue, legislation requires the NLF to pay an amount equal to the deficiency to the Issue Department to finance the purchase of additional investments. Conversely, if the market value of the assets exceeds the value of notes in issue, the Issue Department sells investments to the value of the surplus and pays the proceeds to the NLF.

6 Advances

	Public Works Loan Board		Debt Management Account		Exchange Equalisation Account		Total	
	£m 2016-17	£m 2015-16	**£m 2016-17**	£m 2015-16	**£m 2016-17**	£m 2015-16	**£m 2016-17**	£m 2015-16
Principal outstanding at 1 April	**64,829**	64,019	**98,000**	128,000	**43,172**	40,305	**206,001**	232,324
Advances	**3,634**	3,021	**30,000**	30,000	**9,875**	9,850	**43,509**	42,871
Advances repaid	**(1,861)**	(2,211)	**(35,000)**	(60,000)	**(3,350)**	(6,983)	**(40,211)**	(69,194)
Principal outstanding at 31 March	**66,602**	64,829	**93,000**	98,000	**49,697**	43,172	**209,299**	206,001
Accrued interest	**524**	527	**20**	46	**-**	-	**544**	573
Total advances outstanding	**67,126**	65,356	**93,020**	98,046	**49,697**	43,172	**209,843**	206,574

7 Loans and commitments to lend

Loans			**2016-17**			2015-16
	Public Corporations £m	**Central Government £m**	**Total £m**	Public Corporations £m	Central Government £m	Total £m
Principal outstanding at 1 April	**711**	**2,089**	**2,800**	696	1,933	2,629
Loans advanced	**319**	**214**	**533**	232	294	526
Loans repaid	**(346)**	**(150)**	**(496)**	(217)	(138)	(355)
Principal outstanding at 31 March	**684**	**2,153**	**2,837**	711	2,089	2,800
Accrued interest	**9**	**12**	**21**	10	12	22
Total loans outstanding	**693**	**2,165**	**2,858**	721	2,101	2,822

Commitments to lend			**At 31 March 2017**			At 31 March 2016
	Public Corporations £m	**Central Government £m**	**Total £m**	Public Corporations £m	Central Government £m	Total £m
Undrawn commitments to lend	**8**	**-**	**8**	6	-	6

Commitments to lend are agreements to lend to a customer in the future subject to certain conditions. Such commitments are made either for a fixed period or have no specific maturity but are cancellable by the lender. The NLF does not have any loans or commitments to lend to financial institutions classified as 'Public Financial

Corporations' following the banking crisis. In addition to the above, the NLF has loans and a loan commitment to the IMF which is explained in note 9.

8 Other assets

	At 31 March 2017 £m	At 31 March 2016 £m
Exchange Equalisation Account net assets	**33,057**	29,408
Debt Management Account net assets	**74,344**	64,190
Cash held by National Savings and Investments	**897**	1,159
Sterling balances at Bank of England advanced to IMF	**55**	49
Total other assets	**108,353**	94,806

9 IMF Reserve Tranche Position and Lending to the IMF

The United Kingdom's relationship with the International Monetary Fund (IMF) is accounted for in the NLF and the EEA. The UK's quota subscription to the IMF, 20,155 million Special Drawing Rights (SDRs) - equivalent to £21,961 million[6] at 31 March 2017 (£19,714 million at 31 March 2016) - was paid from the NLF and is recognised as an NLF asset. Part of the subscription is deposited by the IMF in the NLF in return for sterling non-interest-bearing securities (NIBS) which totalled £15,895 million at 31 March 2017 (£15,437 million at 31 March 2016). NIBS represent a liability of the NLF to the IMF. There is a remaining small liability of £55 million (£49 million at 31 March 2016) against which an equal amount of sterling cash is made available in an account at the Bank of England for drawdown by the IMF.

The difference between the gross quota subscription and the NLF's sterling liability to the IMF is the UK's reserve tranche position (RTP). Under the arrangements for membership of the Fund, valuation adjustments are made between the IMF and NLF annually to reflect any changes in value in SDR terms of the NLF's sterling liability to the IMF. An annual settlement payment is made between the NLF and the IMF, normally in May. The cumulative valuation adjustment at 31 March 2017 was £1,996 million loss (£743 million loss at 31 March 2016). The table below sets out the composition of the RTP and the make-up of changes over the year.

[6] The GBP/SDR exchange rate at 31 March 2017 was 0.917752 (31 March 2016: 1.02235)

NLF Assets and Liabilities: Composition of the Reserve Tranche Position and Lending[7] to the IMF

	Asset	Liabilities				Reserve Tranche Position
	IMF Quota Subscription	**Non-interest-bearing securities**	**Other quota liability**	**Valuation adjustment**	**Total liabilities**	
	£m	**£m**	**£m**	**£m**	**£m**	**£m**
Balances at 31 March 2016	19,714	(15,437)	(49)	(743)	(16,229)	3,485
Exchange rate gains for the year on the Quota subscription	2,247				-	2,247
Change in year-end valuation adjustment				(1,253)	(1,253)	(1,253)
Change in loan notes as a result of the valuation settlement		(605)			(605)	(605)
Change in cash on No 1 account			(6)		(6)	(6)
Net decrease in loan notes		147			147	147
Balances at 31 March 2017	**21,961**	**(15,895)**	**(55)**	**(1,996)**	**(17,946)**	**4,015**

Lending to the IMF	**£m**
Lending as at 31 March 2016	1,671
Loans advanced in 2016-17	-
Loans repaid in 2016-17	(594)
Gain on foreign exchange	185
Lending as at 31 March 2017	**1,262**
IMF Quota Subscription and Lending	**23,223**

The RTP is a net asset of the NLF. It represents an SDR asset that can be drawn on by the UK if needed and is considered part of the UK's foreign exchange reserves. Sterling transactions by the IMF impact on the level of non-interest-bearing securities (NIBS) and hence on the RTP. Under current policy, changes in the RTP lead to adjustments in the composition of other reserve assets (held in the EEA) in order to keep the portfolio composition of the reserves in line with plan. Interest is payable by the IMF on the RTP balance in excess of SDR 700 million. This interest is retained in the EEA.

Separately, the EEA also holds the UK's allocation of SDRs (SDR 10,134 million at 31 March 2017) as a liability to the IMF and retains an asset in the form of the UK's holdings of SDRs (SDR 8,251 million at 31 March 2017).

[7] Lending includes both loans made under the New Arrangements to Borrow (NAB) and the bilateral loan facility

During 2016-17 a net payment was made from quota of £147 million to the IMF in support of funding programmes (a net deposit from the IMF of £6,817 million in 2015-16).

During 2009-10 the UK agreed to provide a bilateral loan facility (2009 bilateral loans) to the IMF for an amount up to the equivalent of SDR 9,920 million (£10,809 million at the 31 March 2017 exchange rate). In March 2011, all outstanding claims under the 2009 bilateral loan agreement were folded into the New Arrangements to Borrow (NAB) (see below). The total drawn loans represent a claim on the IMF and are therefore an asset of the NLF and the undrawn loans are a commitment of the NLF. Interest is payable by the IMF on the loan balance and is retained in the EEA in line with accounting policy v.

In April 2012, a G20-led agreement to a temporary increase in IMF resources was reached. As part of this, the UK agreed to provide a new bilateral loan facility (2012 bilateral loans) worth SDR 9,178 million (£10,001 million). This loan facility expired without being used at the end of 2016.

The UK agreed to a third bilateral loan to the IMF, again worth SDR 9,178 million (£10,001 million), in October 2016 (2016 bilateral loans). The 2016 bilateral loan facility has not been used yet.

On 1 April 2011 IMF members agreed to the first activation of the expanded New Arrangements to Borrow (NAB), the IMF's main backstop over and above quota resources. The UK's commitment to the expanded NAB is SDR 18,657 million (£20,329 million at the 31 March 2017 exchange rate). The new NAB however can only be used to finance programmes agreed after its activation. Most recently, the NAB was re-activated during 2015-16 for further six month periods on 1 April and 1 October 2015. The expanded NAB was reduced and deactivated in early February 2016 when the Fourteenth General Quota Review (GRQ – see below) was implemented. Accordingly, the UK's NAB commitment was reduced to SDR 9,479 million (£10,328 million).

On 26 January 2016, the IMF's Fourteenth GRQ, agreed in November 2010, took effect. As a result, the UK's quota subscription increased from SDR 10,739 million to SDR 20,155 million, an increase of SDR 9,416 million. Related transactions were completed on 23 February 2016, as approved by Parliament in July 2011.

UK's total commitment to the IMF

		At 31 March 2017				At 31 March 2016
	Total commitment	**Total drawn**	**Total undrawn**	Total commitment	Total drawn	Total undrawn
Quota (SDRm)	**20,155**	**3,685**	**16,470**	20,155	3,563	16,592
Loans (SDRm)	**18,657**	**1,158**	**17,499**	18,657	1,708	16,949
Total (SDRm)	**38,812**	**4,843**	**33,969**	38,812	5,271	33,541
Quota (£m)	**21,961**	**4,015**	**17,946**	19,714	3,485	16,229
Loans (£m)	**20,329**	**1,262**	**19,067**	18,249	1,671	16,578
Total (£m)	**42,290**	**5,277**	**37,013**	37,963	5,156	32,807

All anticipated changes to the UK's quota subscription and loans to the IMF are reflected within current limits approved by Parliament.

10 Gilt-edged stock

	Conventional	Index-Linked	Total
	£m	£m	£m
At 31 March 2016	1,114,805	410,354	1,525,159
Receipts from gilt issuance	111,455	36,150	147,605
Payments for gilt redemption	(57,110)	(22,205)	(79,315)
Net issuance / (redemption) of DMA gilts	7,975	(2,938)	5,037
Amortisation of premiums and discounts	(3,653)	(1,312)	(4,965)
Change in accrued interest	160	9,135	9,295
At 31 March 2017	**1,173,632**	**429,184**	**1,602,816**

The NLF issues gilts directly to the DMA for use by the Debt Management Office in its money market activities managing the Exchequer's daily cash requirement. These gilts do not contribute directly to Exchequer financing. All other gilts are sold into the primary gilt market to meet government financing needs.

The analysis below shows two large holdings of the gilt liability by UK public sector entities, the DMA and Bank of England.

	At 31 March 2017	At 31 March 2016
	£m	£m
Debt Management Account (DMA)	**123,814**	121,356
Bank of England (for quantitative easing)	**387,756**	338,847
Other investors	**1,091,246**	1,064,956
Total gilt-edged stock	**1,602,816**	1,525,159

Syndication fees are borne by the NLF and are netted off from gross issuance proceeds as part of the calculation of amortised cost. Other directly related issue costs for assets and liabilities are negligible and are written off as incurred. Total syndication fees for the year were £48 million (2015-16: £42 million).

11 National Savings and Investments (NS&I) products

	2016-17 £m	2015-16 £m
Principal outstanding at 1 April	**134,597**	123,435
Cash repayments from the National Loans Fund	**(23,658)**	(20,983)
Principal cash received in the National Loans Fund	**34,182**	31,106
Capitalised interest and other returns to savers	**1,373**	1,207
Change in cash holdings for principal	**(265)**	(168)
Principal outstanding at 31 March	**146,229**	134,597
Accrued interest and other returns to savers	**713**	552
Total principal and accrued interest outstanding	**146,942**	135,149

NS&I provides more detail on this liability in a set of Product Accounts which are published with the NS&I resource accounts on the NS&I website[8].

12 Other debt

	At 31 March 2017 £m	At 31 March 2016 £m
FLS Treasury Bills	**75,069**	86,387
Other:		
Debt Management Account	**13,061**	18,679
Bank of England Issue Department	**370**	370
Balances from government accounts at the Government Banking Service	**21,490**	22,388
Deposits from public sector bodies	**8,587**	8,734
Foreign currency debt	**353**	327
Other	**1,356**	979
	45,217	51,477
Total other debt payable	**120,286**	137,864

Treasury Bills have been issued by the NLF to the DMA in connection with the Bank of England's Funding for Lending Scheme (FLS). Further information on the scheme is provided in the Performance report.

The next two items reflect deficit funding from the DMA and the Issue Department of the Bank of England. The fourth item reflects the transfer to the NLF of any temporary cash surpluses on other government accounts held

8 http://nsandi-corporate.com/about-nsi/our-performance/our-annual-report-and-accounts/

at Government Banking. Deposits from public sector bodies represents deposits by public sector bodies which are directly held with the NLF. Foreign currency debt represents a 3 billion Renminbi bond principal plus accrued interest at 31 March 2017, converted to sterling at the GBP/CNY (offshore) rate of 8.5962. "Other" comprises mostly certificates of tax deposit held by the NLF.

13 Fair Values

Carrying Value and Fair Value of NLF assets and liabilities

	At 31 March 2017		At 31 March 2016	
	Carrying Value	**Fair Value**	Carrying Value	Fair Value
Assets	**£m**	**£m**	£m	£m
Advances:				
Public Works Loan Board	**66,602**	**99,669**	64,829	90,642
Debt Management Account	**93,000**	**93,000**	98,000	98,000
Exchange Equalisation Account	**49,697**	**49,697**	43,172	43,172
Accrued interest	**544**	**544**	573	573
Loans:				
Principal	**2,837**	**3,456**	2,800	3,389
Accrued interest	**21**	**21**	22	22
Other assets	**108,353**	**108,353**	94,806	94,806
IMF quota subscription & lending	**23,223**	**23,223**	21,385	21,385
Total assets	**344,277**	**377,963**	325,587	351,989
Liabilities				
Gilts	**1,602,816**	**2,090,128**	1,525,159	1,863,397
National Savings & Investments:				
Principal	**146,229**	**146,858**	134,597	135,490
Accrued interest	**713**	**719**	552	563
IMF liabilities	**17,946**	**17,946**	16,229	16,229
Other debt:				
Treasury Bills (Funding for Lending)	**75,069**	**75,088**	86,387	86,430
Debt Management Account	**13,061**	**13,061**	18,679	18,679
Issue Department of Bank of England	**370**	**370**	370	370
Government balances	**21,490**	**21,490**	22,388	22,388
Deposits from public sector bodies	**8,587**	**8,587**	8,734	8,734
Foreign currency debt	**353**	**353**	327	327
Other	**1,356**	**1,356**	979	979
Total liabilities	**1,887,990**	**2,375,956**	1,814,401	2,153,586

The NLF's assets are classified as financial assets except for the net assets of the EEA (£33,057 million, 2015-16: £29,408 million) and DMA (£74,344 million, 2015-16: £64,190 million), reported in Other Assets (note 8). The carrying value of financial assets (all of which are designated as loans and receivables) is £236,876 million (2015-16: £231,989 million) and their fair value is £270,562 million (2015-16: £258,391 million). All the NLF's liabilities are financial liabilities. In instances where the fair value differs from the carrying value, the fair value has been calculated by reference to market prices where instruments are traded on an active quoted market or, where this is not the case, as the net present value of future cash flows.

The fair value of advances to the PWLB is calculated as the net present value of future cash flows. Loans by the PWLB are usually at a fixed rate of interest and so their fair value increases or decreases according to changes in the difference between the fixed rate of interest earned on the loan and current market values. Differences between the fair and book value will not be realised as the PWLB loans are not traded by the NLF.

The fair value of gilts and Treasury Bills are calculated by reference to their market prices. Foreign currency debt relates to a Renminbi bond. Its fair value is taken to be equal to its carrying value because of its small size and materiality. Gilts, Treasury Bills and the Renminbi bond will generally be redeemed at their book values so any difference between their fair value and book value will not normally be realised in the NLF accounts.

14 Maturity of assets and liabilities

The following table shows the split between current and non-current assets and liabilities based on contract date of maturity or expected maturity if there is no contract date.

	At 31 March 2017			At 31 March 2016		
	Current	**Non-current**	**Total**	Current	Non-current	Total
	£m	**£m**	**£m**	£m	£m	£m
Assets						
Advances	**2,261**	**207,582**	**209,843**	2,293	204,281	206,574
Loans	**236**	**2,622**	**2,858**	226	2,596	2,822
Other assets	**952**	**107,401**	**108,353**	1,208	93,598	94,806
IMF quota subscription (SDR) & lending	**-**	**23,223**	**23,223**	-	21,385	21,385
Total assets	**3,449**	**340,828**	**344,277**	3,727	321,860	325,587
Liabilities						
Gilts						
Conventional	**86,108**	**1,087,524**	**1,173,632**	71,171	1,043,634	1,114,805
Index-linked	**17,298**	**411,886**	**429,184**	26,172	384,182	410,354
Gilt-edged stock	**103,406**	**1,499,410**	**1,602,816**	97,343	1,427,816	1,525,159
National Savings and Investments	**146,942**	**-**	**146,942**	135,149	-	135,149
IMF liabilities	**-**	**17,946**	**17,946**	-	16,229	16,229
Treasury Bills for FLS	**75,069**	**-**	**75,069**	86,387	-	86,387
Other debt payable	**45,017**	**200**	**45,217**	50,954	523	51,477
Total liabilities	**370,434**	**1,517,556**	**1,887,990**	369,833	1,444,568	1,814,401

All National Savings and Investments products are payable on demand and therefore classified as current liabilities.

The following table shows an analysis of current and non-current assets and liabilities by type of counterparty.

	At 31 March 2017			At 31 March 2016		
	Current	**Non-current**	**Total**	Current	Non-current	Total
	£m	**£m**	**£m**	£m	£m	£m
Assets						
Balances with:						
Other central government bodies	**3,325**	**316,980**	**320,305**	3,613	299,819	303,432
Public corporations and trading funds	**124**	**625**	**749**	114	656	770
Total intra government balances	**3,449**	**317,605**	**321,054**	3,727	300,475	304,202
Balances with bodies external to government	**-**	**23,223**	**23,223**	-	21,385	21,385
Total assets	**3,449**	**340,828**	**344,277**	3,727	321,860	325,587
Liabilities						
Balances with:						
Other central government bodies	**125,707**	**111,264**	**236,971**	141,780	110,584	252,364
NHS Trusts	**4,077**	**-**	**4,077**	4,153	-	4,153
Public corporations and trading funds	**32,837**	**364,701**	**397,538**	27,017	321,799	348,816
Total intra government balances	**162,621**	**475,965**	**638,586**	172,950	432,383	605,333
Balances with bodies external to government	**207,813**	**1,041,591**	**1,249,404**	196,883	1,012,185	1,209,068
Total liabilities	**370,434**	**1,517,556**	**1,887,990**	369,833	1,444,568	1,814,401

15 Financial risks related to the NLF

The Government's debt management objective is set out in the annual Debt and Reserves Management Report:

> *to minimise, over the long term, the costs of meeting the Government's financing needs, taking into account risk, whilst ensuring that debt management policy is consistent with the aims of monetary policy.*

This is achieved by:

- meeting the principles of openness, transparency and predictability;
- developing a liquid and efficient gilt market;
- issuing gilts that achieve a benchmark premium;
- adjusting the maturity and nature of the Government's debt portfolio, primarily by means of the maturity and composition of debt issuance and potentially by other market operations including switch auctions, conversion offers and buy-backs; and
- offering cost-effective savings instruments to the retail sector through National Savings & Investments.

For cash management, the aggregate balance on government accounts is swept daily to the National Loans Fund and then to the DMA. The Debt Management Office deals with the financial markets to manage the daily cash surplus or deficit on the DMA relative to its target overnight balance, lending when there is a surplus and borrowing when there is a deficit.

The NLF's liabilities include conventional and index-linked gilt-edged securities, NS&I product liabilities, certificates of tax deposit, Treasury Bills issued to the DMA for the Funding for Lending scheme, deposits from other public sector accounts; liabilities to the IMF; and foreign currency debt denominated in Renminbi. There is a wide spread of maturities.

NLF assets include advances to the DMA, PWLB and EEA, loans to UK public bodies, net assets of the DMA and EEA, NS&I product-related cash holdings and the UK's gross Quota Subscription and lending to the IMF, denominated in SDRs.

Set out below are certain risk factors that could affect the NLF's operations.

Interest rate and inflation risk

The NLF is exposed to cash flow interest rate risk on its floating rate borrowing and lending due to the risk that future interest rates will fluctuate. It is not exposed to fair value interest rate risk as its financial assets and liabilities are measured at amortised cost and not fair value. Some of the NLF's assets and liabilities have no associated interest income or expense (are "zero-rated") and are therefore not exposed to changes in interest rates.

Inflation risk arises because interest and redemption amounts paid on index-linked gilts vary monthly in line with changes in the UK Retail Prices Index (RPI) since the initial issue of each stock.

The table below analyses the NLF's interest rate and inflation risk. Assets and liabilities are included at carrying amount and are shown at the earlier of contractual re-pricing or maturity dates.

Interest rate and inflation risk analysis as at 31 March 2017

	Up to 1 month/ repayable on demand £m	1-12 months £m	1-5 years £m	Over 5 years £m	Zero-rated £m	Total carrying value £m	Fixed rate £m	Floating rate £m
Assets								
Advances	93,216	2,098	6,990	57,288	50,251	**209,843**	65,976	93,616
Loans	28	187	724	1,898	21	**2,858**	2,837	-
Other assets	-	-	-	-	108,353	**108,353**	-	-
IMF quota subscription	-	-	-	-	21,961	**21,961**	-	-
IMF loans	-	-	-	-	1,262	**1,262**	-	-
Total	**93,244**	**2,285**	**7,714**	**59,186**	**181,848**	**344,277**	**68,813**	**93,616**
Liabilities								
Gilts								
Conventional	-	78,969	353,200	734,325	7,138	**1,173,632**	1,166,494	-
Index-linked	428,137				1,047	**429,184**		428,137
Gilt-edged stock	428,137	78,969	353,200	734,325	8,185	**1,602,816**	1,166,494	428,137
National Savings and Investments	126,756	12,554	6,851	-	781	**146,942**	19,798	126,363
IMF liabilities					17,946	**17,946**		
Treasury Bills for FLS	9,730	65,339	-	-	-	**75,069**	75,069	-
Other debt payable	28,159	784	200	-	16,074	**45,217**	8,935	20,208
Total	**592,782**	**157,646**	**360,251**	**734,325**	**42,986**	**1,887,990**	**1,270,296**	**574,708**
Period gap	**499,538**	**155,361**	**352,537**	**675,139**	**(138,862)**	**1,543,713**		
Cumulative gap	**499,538**	**654,899**	**1,007,436**	**1,682,575**	**1,543,713**			

Interest rate and inflation risk analysis as at 31 March 2016

	Up to 1 month/ repayable on demand £m	1-12 months £m	1-5 years £m	Over 5 years £m	Zero-rated £m	**Total carrying value £m**	Fixed rate £m	Floating rate £m
Assets								
Advances	98,263	2,103	6,625	55,827	43,756	**206,574**	64,143	98,675
Loans	30	174	680	1,916	22	**2,822**	2,800	-
Other assets	-	-	-	-	94,806	**94,806**	-	-
IMF quota subscription	-	-	-	-	19,714	**19,714**	-	-
IMF loans	-	-	-	-	1,671	**1,671**	-	-
Total	**98,293**	**2,277**	**7,305**	**57,743**	**159,969**	**325,587**	**66,943**	**98,675**
Liabilities								
Gilts								
Conventional	-	64,193	319,954	723,679	6,979	**1,114,805**	1,107,826	-
Index-linked	409,219	-	-	-	1,135	**410,354**	-	409,219
Gilt-edged stock	409,219	64,193	319,954	723,679	8,114	**1,525,159**	1,107,826	409,219
National Savings and Investments	114,589	5,023	14,927	-	610	**135,149**	20,574	113,965
IMF liabilities	-	-	-	-	16,229	**16,229**	-	-
Treasury Bills for FLS	9,335	77,052	-	-	-	**86,387**	86,387	-
Other debt payable	35,083	499	523	-	15,372	**51,477**	9,055	27,050
Total	**568,226**	**146,767**	**335,404**	**723,679**	**40,325**	**1,814,401**	**1,223,842**	**550,234**
Period gap	**469,933**	**144,490**	**328,099**	**665,936**	**(119,644)**	**1,488,814**		
Cumulative gap	**469,933**	**614,423**	**942,522**	**1,608,458**	**1,488,814**			

Foreign currency risk

The NLF is exposed to foreign exchange risk through transactions with the IMF as the reserve tranche position (quota subscription less UK liability) and lending to the IMF are denominated in SDRs (note 9). In addition to the risk of unrealised revaluations of the assets and liability, foreign exchange gains and losses are realised as the NLF transacts with the IMF on the UK liability and loans. As it is not possible to predict the size and timing of these transactions with any certainty it has not been deemed cost-effective to attempt to mitigate this risk through hedging arrangements.

There is a small exposure to exchange rate risk relating to a Renminbi bond (note 12). As explained under *Derivatives and hedging* below, this risk is not hedged within the NLF but is hedged when the activities of the EEA and NLF are taken together.

Sensitivity analysis

The following analysis, required by IFRS 7, is intended to illustrate the sensitivity of the NLF's financial assets and liabilities to changes in UK interest rates, the UK Retail Prices Index and the SDR to sterling and Renminbi to sterling exchange rates. The sensitivity analysis has been calculated on the basis that the components of financial assets and liabilities, the amount of instruments held at fixed, floating and zero interest rates and the amount of instruments held in SDRs are all constant and are as at the end of the reporting period.

The following assumptions have been made in calculating sensitivity:

- All sensitivities impact the Statement of Comprehensive Net Expenditure and thereby the net liability of the CF to the NLF.
- Finance income and costs and the net liability of the CF to the NLF will be affected by changes in interest rates on floating rate instruments.
- All instruments are held at amortised cost and are therefore not subject to changes in fair value as a result of interest rate changes.
- No sensitivity is provided for interest accruals where these are based on pre-agreed interest rates and are therefore not susceptible to further rate changes.
- 100 basis points and 10 percent are management's assessment of the reasonably possible change in interest, RPI and FX rates at the end of the reporting period. This is not a forecast.

Using the above assumptions, the following table shows the illustrative impact on the Statement of Comprehensive Net Expenditure that would result from an increase in UK interest rates and the UK Retail Prices Index and if the SDR and Renminbi to sterling exchange rates were to strengthen.

	2016-17 Statement of Comprehensive Net Expenditure £m	2015-16 Statement of Comprehensive Net Expenditure £m
UK interest rates + 100bp expense	**530**	423
UK Retail Prices Index + 100bp expense	**4,281**	4,092
SDR exchange rate + 10% income	**(528)**	(516)
Renminbi exchange rate + 10% expense	**35**	33

An equal, but opposite effect would result if there were a decrease in UK interest rates and the UK Retail Prices Index, and if the SDR and Renminbi to sterling exchange rates were to weaken.

Liquidity risk

Liquidity risk is the risk that the NLF will encounter difficulty in meeting obligations associated with financial liabilities. Its exposure to liquidity risk arises because of its fundamental purpose of being the Government's main borrowing account. NLF liabilities carry a wide range of maturities, spreading funding requirements for redemption payments, and thus liquidity risk, across a wide time period into the future. The longest stock in existence at 31 March 2017 matures in 2068. Deposits in the NLF have a shorter maturity profile since they can change on demand. However, in practice, balances change only slowly due to re-investment. By virtue of section 19(1) of the National Loans Act 1968, the net liabilities of the NLF are a liability of the Consolidated Fund. The servicing of the NLF's liabilities is expected to be mainly met through future tax revenue receipts. There is no reason to believe that tax revenues will not be forthcoming and therefore, in accordance with the Government Financial Reporting Manual, it has been concluded as appropriate to adopt the going concern basis of preparation for the NLF Accounts. Most of the NLF's borrowing needs are met through borrowing on its behalf by the DMO and NS&I.

Contractual undiscounted cash flows of financial liabilities

The following table shows the contractual undiscounted cash flows of the NLF's liabilities. The amounts shown are the cash flows arising from the NLF's financial liabilities during the period up to and including maturity. This is in contrast to the basis on which the Statement of Financial Position amounts are calculated. As described in note 1, items on the Statement of Financial Position are valued at fair value upon initial recognition and subsequently held at amortised cost. Therefore totals in the following table will not agree to the Statement of Financial Position.

The treatment of coupon payments is of particular significance. The table includes contractual coupon payments for the period to maturity based on coupon rates and, in the case of index-linked gilts, the Retail Prices Index at 31 March 2017. Because of the many coupon payments to be made for longer dated gilts the table below reports coupon cash flows of £647,116 million (£645,801 million at 31 March 2016) whereas the gilts liability in the Statement of Financial Position contains coupon accruals to the end of the reporting period of £8,200 million (£8,126 million at 31 March 2016).

The cash flows reported in the table will be funded by replacement debt issues, the proceeds of assets or by finance from the Consolidated Fund.

At 31 March 2017

Liabilities	**0-12 months £m**	**1-2 years £m**	**2-5 years £m**	**Over 5 years £m**	**Undated £m**	**Total £m**
Conventional Gilts:						
Principal	**78,412**	**71,194**	**275,187**	**703,664**	**-**	**1,128,457**
Coupons	**39,653**	**37,026**	**93,862**	**421,443**	**-**	**591,984**
Index-Linked Gilts:						
Principal	**16,237**	**-**	**29,586**	**348,087**	**-**	**393,910**
Coupons	**3,800**	**3,597**	**9,986**	**37,749**	**-**	**55,132**
Total Gilts	**138,102**	**111,817**	**408,621**	**1,510,943**	**-**	**2,169,483**
National Savings and Investments	**146,871**	**-**	**-**	**-**	**69**	**146,940**
IMF	**17,946**	**-**	**-**	**-**	**-**	**17,946**
Treasury Bills For FLS	**75,186**	**-**	**-**	**-**	**-**	**75,186**
Temporary Deposits	**8,388**	**-**	**-**	**-**	**-**	**8,388**
Other debt payable	**36,638**	**4**	**202**	**-**	**-**	**36,844**
	423,131	**111,821**	**408,823**	**1,510,943**	**69**	**2,454,787**

The cash flow analysis after five years is:

	5-10 years £m	**10-20 years £m**	**20-30 years £m**	**30-40 years £m**	**Over 40 years £m**	**Total £m**
Conventional Gilts:						
Principal	**195,679**	**183,217**	**182,564**	**81,408**	**60,796**	**703,664**
Coupons	**115,478**	**164,250**	**90,445**	**37,712**	**13,558**	**421,443**
Index-Linked Gilts:						
Principal	**65,145**	**97,158**	**79,555**	**60,017**	**46,212**	**348,087**
Coupons	**12,571**	**15,280**	**6,306**	**3,048**	**544**	**37,749**
	388,873	**459,905**	**358,870**	**182,185**	**121,110**	**1,510,943**

At 31 March 2016

Liabilities	0-12 months £m	1-2 years £m	2-5 years £m	Over 5 years £m	Undated £m	Total £m
Conventional Gilts:						
Principal	64,011	77,575	237,912	696,150	-	1,075,648
Coupons	39,392	37,544	96,434	415,463	-	588,833
Index-Linked Gilts:						
Principal	25,027	15,828	28,986	316,744	-	386,585
Coupons	3,997	3,684	10,193	39,094	-	56,968
Total Gilts	132,427	134,631	373,525	1,467,451	-	2,108,034
National Savings and Investments	135,092				57	135,149
IMF	16,229	-	-	-	-	16,229
Treasury Bills For FLS	86,603	-	-	-	-	86,603
Temporary Deposits	8,536	-	-	-	-	8,536
Other debt payable	42,429	336	206		-	42,971
	421,316	134,967	373,731	1,467,451	57	2,397,522

The cash flow analysis after five years is:

	5-10 years £m	10-20 years £m	20-30 years £m	30-40 years £m	Over 40 years £m	Total £m
Conventional Gilts:						
Principal	231,867	179,982	149,271	88,536	46,494	696,150
Coupons	114,836	161,635	88,597	37,239	13,156	415,463
Index-Linked Gilts:						
Principal	58,595	89,501	72,961	55,878	39,809	316,744
Coupons	12,984	15,899	6,389	3,259	563	39,094
	418,282	447,017	317,218	184,912	100,022	1,467,451

Credit risk

The NLF makes loans to UK public corporations and central government entities, advances to other UK central Exchequer Funds and subscribes to the IMF. The NLF also lends to the IMF. As a result the NLF is not exposed to significant credit risk. Details of this can be found in notes 6, 7 and 9. Total loans and advances stand at £212,701 million (2015-16: £209,396 million) and gross IMF exposure stands at £23,223 million (2015-16: £21,385 million).

In respect of loans financed by the NLF, the financial relationship with the borrower is managed by the department responsible for the relevant public corporation. The sponsoring department performs due diligence on the borrower and proposes the loan. The Treasury reviews the proposal and, if the proposal is approved, the NLF will make the loan. The NLF is not allowed to accept losses on its loans. Any such losses can only be written off by primary legislation; however, in 1990 the Treasury gave an undertaking to the Public Accounts Committee that it would not seek Parliament's approval to such a course except as part of a reconstruction of the borrower's finances prior to privatisation. In other cases the Treasury would look to the borrower's sponsor department to cover any losses from its resource account.

In the case of advances to the PWLB for loans to Local Authorities, the PWLB manages the financial relationship with the borrower though the credit risk is borne by the NLF.

In the context of NLF loans issued to trading organisations at market rates, under the Treasury's Commercial Lending policy, the terms and interest rates are designed to reflect the terms on which a private sector lender, such as a commercial bank would lend to the borrower if the borrower were a wholly private sector body rather than a government body.

Ceilings on total lending from the NLF to specific bodies are prescribed in the statutes governing each loan. The PWLB is allowed to lend up to an aggregate amount of £70 billion (2015-16: £70 billion). For short-term lending to public bodies, the maximum exposure of the NLF is determined by prescribed credit ceilings appropriate for the circumstances of the body.

The IMF maintains precautionary balances (comprising retained earnings) as prudential cover in order to ensure the continued security and liquidity of its members' claims. Other factors that help safeguard the Fund's resources include the conditionality associated with lending by the IMF and the IMF's status as a creditor with preferential right to receive payment.

None of the NLF's financial assets are past due or impaired.

Derivatives and hedging

The NLF itself does not use derivatives or undertake hedging. However some of the risks on the NLF are offset by the activities of the EEA. The Exchange Equalisation Account Act 1979 constrains how the EEA may borrow from outside government. Where the EEA's foreign currency reserves are financed by foreign currency borrowing, the debt is issued by and is an obligation of the NLF. The foreign currency raised is sold by the NLF to the EEA for sterling. While the NLF remains exposed to the interest and exchange rate risks from the foreign currency debt it has issued, in practice these risks are offset through the EEA's programme of asset management and swaps. The only foreign currency debt outstanding in the NLF at 31 March 2017 is the 3 billion Renminbi bond (£349.0 million principal amount outstanding excluding accrued interest as at 31 March 2017. See note 12 for total outstanding including accrued interest at 31 March 2017).

16 Related Parties

The Treasury is the ultimate controlling party of the NLF. There have been no direct transactions between the Treasury and the NLF in 2016-17. As at 31 March 2017 £200 million proceeds of debt issuance from Treasury Group is deposited with the NLF.

The main related parties of the NLF are the CF, DMA, EEA, PWLB, Bank of England and NS&I. The relationship between the NLF and CF is explained in the Overview within the Performance report. The NLF has provided finance in the year to the DMA, EEA, PWLB and to various statutory public sector bodies. The NLF has also transacted with the Bank of England and NS&I. Transactions with these bodies are all disclosed in these accounts. The NLF has also had a significant number of transactions with other government bodies via its temporary borrowing of balances in various Government Banking bank accounts.

During the year there have been no transactions between key management personnel at the Treasury and the NLF.

17 Events after the Reporting Period

There are no events after the reporting period to report.

18 Date of Authorisation for Issue of Account

The Accounting Officer authorised these financial statements for issue on 11 July 2017.

HM Treasury contacts

This document can be downloaded from
www.gov.uk

If you require this information in an alternative format or have general enquiries about HM Treasury and its work, contact:

Correspondence Team
HM Treasury
1 Horse Guards Road
London
SW1A 2HQ

Tel: 020 7270 5000

Email: public.enquiries@hmtreasury.gsi.gov.uk

ISBN 978-1-4741-4479-7