Export Credits Guarantee Department

The UK's Official Export Credit Agency

Annual Review and Resource Accounts

2006-07

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Export Credits Guarantee Department
The UK's Official Export Credit Agency

Annual Review and Resource Accounts
2006-07

This Annual Review, which covers the functions of the Secretary of State for Business, Enterprise and Regulatory Reform exercised through the Export Credits Guarantee Department, is published in accordance with the requirements of the Export and Investment Guarantees Act, 1991.

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Message from the Secretary of State for Business, Enterprise and Regulatory Reform

I am pleased to be able to present ECGD's Annual Review for 2006-07, including the Resource Accounts laid before Parliament.

It has been an eventful year for ECGD. In July 2004, it had been announced that ECGD would take steps to test the merits of a Trading Fund. Since then, the prevailing trend of reduced volumes of new business underwritten by ECGD has continued. This served to cast doubt on whether an ECGD Trading Fund would be appropriate into the longer term. The Government concluded that an ECGD Trading Fund should not be established. On 26 June Ian McCartney accordingly announced to Parliament that Ministers had agreed a new financial framework for the Department.

With the agreement of the Chief Secretary of HM Treasury, this new financial framework will run from 1 April 2008. It takes account of ECGD's changed circumstances and the experience gained from running a Pilot Trading Fund. The framework will be consistent with the principles of the July 2004 Announcement by Ministers to Parliament about the basis on which ECGD's future governance would be set, including the maintenance of its prevailing risk reward balance.

ECGD has spent considerable time since 2000 in devising an appropriate financial regime, which balances support for exporters with the need to protect the interests of taxpayers. I am pleased that this exercise has now been completed and that ECGD can now focus its resources on its role of supporting exporters within the policy objectives set by Ministers.

Following a lengthy Public Consultation, ECGD strengthened its anti-bribery and corruption rules. These came into force on 1 July 2006 for new applications for support. These changes are in line with the Government's commitment to combat bribery and corruption in business. Among other matters, exporters must declare the names of Agents involved in transactions; Special Handling Arrangements have been introduced to minimise the risk of an inadvertent disclosure in the light of concerns on confidentiality where this is requested by exporters. The Trade and Industry Committee of the House of Commons looked at the new rules in June 2006. The Committee went on to comment that the Public Consultation had been thorough, comprehensive and responsive, and that the new procedures should be workable.

During the year, a Public Consultation was launched to seek views on possible changes to the rules that govern the amount of foreign content that is eligible for ECGD cover. Historically, ECGD has always been willing to provide cover for an element of foreign content, but the nature of UK manufacturing and trade has changed markedly in recent years, with the onset of globalisation, and the existing arrangements had become too rigid and unnecessarily complicated. Having taken into account the responses made to the Consultation, and in recognition of the way UK exporters have oriented more towards the provision of goods procured in overseas markets than the export of goods manufactured in the UK, as well as the provision of services from the UK, the Government has decided to simplify and liberalise ECGD's foreign content rules. In future, foreign content, up to a maximum of 80% of a contract value, will be eligible for ECGD support on credit contracts where its risk capacity is available and its risk standards have been met. This matches ECGD's longstanding policy on cash contracts.

The Rt Hon John Hutton MP
Secretary of State for Business,
Enterprise and Regulatory Reform

Chairman's Foreword

This year the Management Board spent substantial time on two important issues in addition to its usual work of overseeing ECGD's finances, risk management and business policies. The first concerned the advice to give DTI Ministers to inform their decision on whether to establish an ECGD Statutory Trading Fund in the light of the experience of piloting such a structure since April 2005. The second related to the application of ECGD's Business Principles.

On the first of these, the decision not to establish a Statutory Trading Fund has ended a resource intensive programme, which began in 2000 with consideration of the use of capital as a risk measure. The disciplines that this programme has brought to ECGD, in both risk management and pricing its products, have been of great value and will be continued under its new financial framework. This decision ends uncertainty about ECGD's operating status and should provide a stable and lasting platform going forward. This will be a welcome result for staff and exporters.

The second issue related to ECGD's Business Principles. This involved work on the application of new rules to combat bribery and corruption in any business supported by ECGD, which included responding to an inquiry by the Trade and Industry Committee into this matter. The Board has also focused on sustainable development issues. This included deliberation over the issues raised by the consideration of possible support for the Sakhalin II Energy project, the formulation of ECGD's first full Sustainable Development Action Plan, and the potential impacts of climate change issues on ECGD's business. In regard to climate change, the two principal areas of pressure have been in respect of ECGD support for oil and gas projects and for aircraft sales. ECGD takes due account of the policies set by Government on such issues as climate change.

The Management Board has benefited from three new appointments and has sadly had to recognise two retirements. Peter Haslehurst, currently Chairman of Luxfer Holdings PLC, was appointed to the Board in September 2006. Peter has over 40 years' experience of exporting all over the world and has in the past been a user of ECGD's services. He has already brought a businessman's view to the deliberations of the Management Board and of the Export Guarantees Advisory Council which he attends as an observer. Katherine Letsinger was Group Finance Director of Wellington Underwriting plc until recently, having previously held a finance post with a re-insurer and been a partner in Price Waterhouse. Katherine was appointed in January 2007 and chairs the Audit Committee.

John Wright retired from the Management Board in March. He had completed two three-year terms as a Non-Executive Director and as Chairman of our Audit Committee.

A former Chief Executive of Clydesdale Bank, John brought great wisdom in the area of operational risk as well as experience of banking in the Middle East and Asia. His counsel has been invaluable and we shall miss him.

Victor Lunn-Rockliffe retired as head of the Business Group on 30 June 2006 after a career with ECGD of over 30 years. The Board valued his long experience of the business in their deliberations. Following an open competition, he was succeeded by Steve Dodgson, formerly a member of the Board serving as ECGD's Human Resources Director.

Finally, I would like to compliment Patrick Crawford and his team for their hard work and careful management in a difficult climate of falling volumes of new business for ECGD and for maintaining high risk standards.

Graham Pimlott
ECGD Chairman

Chief Executive's Foreword

The 2006-07 financial year has been one of continued progress in the increased efficiency and effectiveness of ECGD in the interests of exporters and taxpayers.

The value of guarantees and insurance policies issued by ECGD was £1.8 billion, a 19 per cent fall on last year but broadly in line with 2004-05. This is hardly surprising, given the changing nature of UK manufacturing and the continuing benign global risk environment. The total number of guarantees and policies issued was 91, a fall from 151 in 2005-06. The value of guarantees represented by Airbus deliveries fell to 27 per cent of business issued due mainly to high levels of liquidity in the capital markets. Given the importance of Airbus to ECGD's business, we have this year continued to work closely with our French and German counterparts to develop our working practices to improve our service to it; we will be pursuing this further in the forthcoming year.

For a second year, good progress has been made in the recovery of claims paid in relation to aircraft, against the background of a buoyant civil aviation sector. With the removal of 18 aircraft from the repossessed fleet and successful conclusion of a restructuring involving 3 aircraft, the portfolio of distressed aircraft has reduced from 105 last year to 84 this year, 66 of which remain with the original airline on restructured leases. Other than a limited number of aircraft nearing the end of the sale process, all repossessed aircraft remaining to be sold are due to be placed with a single Aircraft Management and Remarketing Manager, who will also be a source of expert technical advice should a downturn in the aviation sector occur leading to airline failures.

Following last year's closure of our main office in Cardiff, the new finance team in London has become fully integrated with the organisation, and we are now seeing the benefits of all key functions being performed on one site. The building in Cardiff and two floors of our Docklands headquarters, which were vacated following a reorganisation of our office space and a move to more open-plan working, have now been sub-let, thus leading to a reduction in our annual running costs of £1.25 million.

During the course of this year, we bade farewell to 15 colleagues as part of a voluntary early retirement exercise. Between them they had 518 years experience in ECGD; my colleagues and I wish them well for the future.

No organisation can meet the demands of the future by standing still. This is particularly true of ECGD, which over the coming years can expect to face volatility in its levels of business, reflecting changing conditions in global investment activity and capital availability. As the results of our Public

Consultation on foreign content have shown, ECGD is able to adapt to the needs of UK exporters and of their customers within the international marketplace. I am confident that we can continue to make the changes needed to deliver our services to exporters in a cost effective way.

J.P.S. Crawford

Patrick Crawford
ECGD Chief Executive

Mission Statement

Aim

To benefit the UK economy by helping exporters of UK goods and services win business, and UK firms to invest overseas, by providing guarantees, insurance and reinsurance against loss, taking into account the Government's international policies.

Objectives

Consistent with the above aim, ECGD seeks:

- To achieve Financial Objectives set by Ministers.
- To operate in accordance with its Business Principles.
- To ensure its activities accord with other Government objectives, including those on sustainable development, human rights, good governance and trade.
- To promote an international framework that allows UK exporters to compete fairly by limiting or eliminating all subsidies and the adoption of consistent practices for assessing projects and countries on a multilateral basis.
- To recover the maximum amount of debt in respect of claims paid by ECGD in a manner consistent with the Government's policy on debt forgiveness.
- To ensure ECGD's facilities are, in broad terms, complementary to those in the private sector.
- To provide an efficient, professional and proactive service for customers which focuses on solutions and innovation.
- To employ good management practice to recruit, develop and retain the people needed to achieve ECGD's business goals and objectives.

Financial Overview – five year summary

Operating Statement	2006-07 £m	2005-06 £m	2004-05 £m	2003-04 £m	2002-03 £m
Overall Value of Guarantees and Insurance Policies Issued	**1,798**	2,230	1,995	2,991	3,532
Of which Overseas Investment Insurance	**152**	239	351	706	905
Premium Income	**55**	88	45	102	77
Of which Overseas Investment Insurance	**1**	2	3	7	7
Claims Authorised	**61**	79	87	211	261
Net Operating Income	**404**	1,699	1,108	613	201

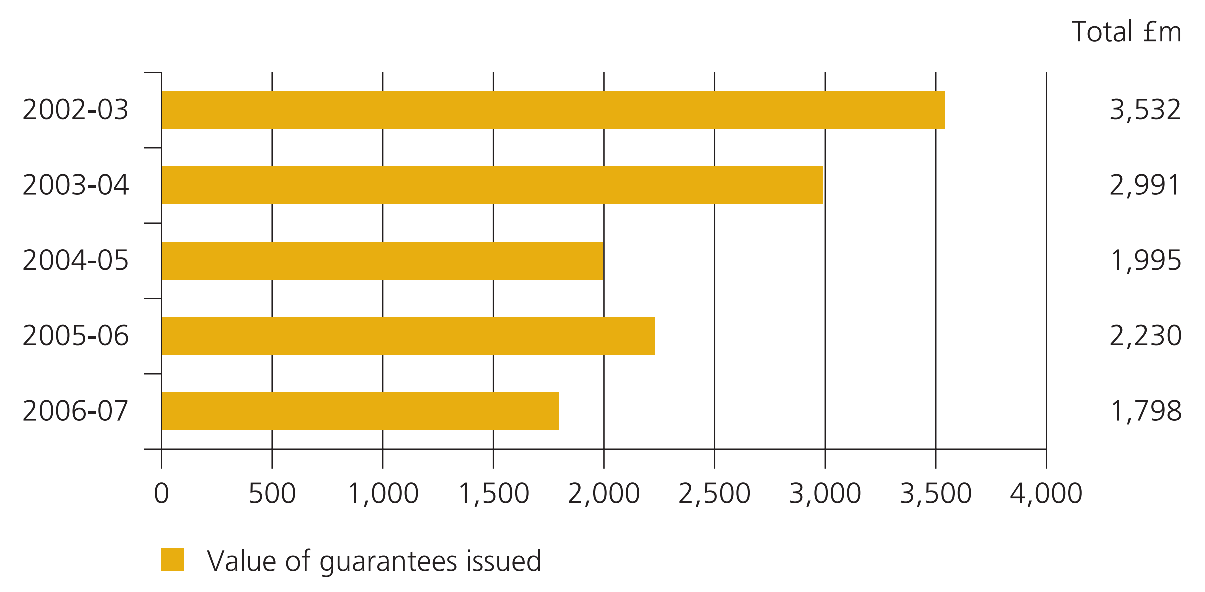
Financial Objectives

ECGD met its key financial objectives in 2006-07, particularly in respect of:

- **Account 2 In-Year Reserve Coverage Ratio**, that measures the adequacy of premium income in 2006-07 relative to risks on new business supported and costs incurred in the year. The ratio for 2006-07 was 1.82, against a target of 1.4.
- **Account 2 Reserves Index**, that measures the adequacy of reserves against the risks across the whole portfolio. The ratio for 2006-07 was 2.72, against a target of 1.

Business Overview

ECGD Supported Business (£m)



New Business

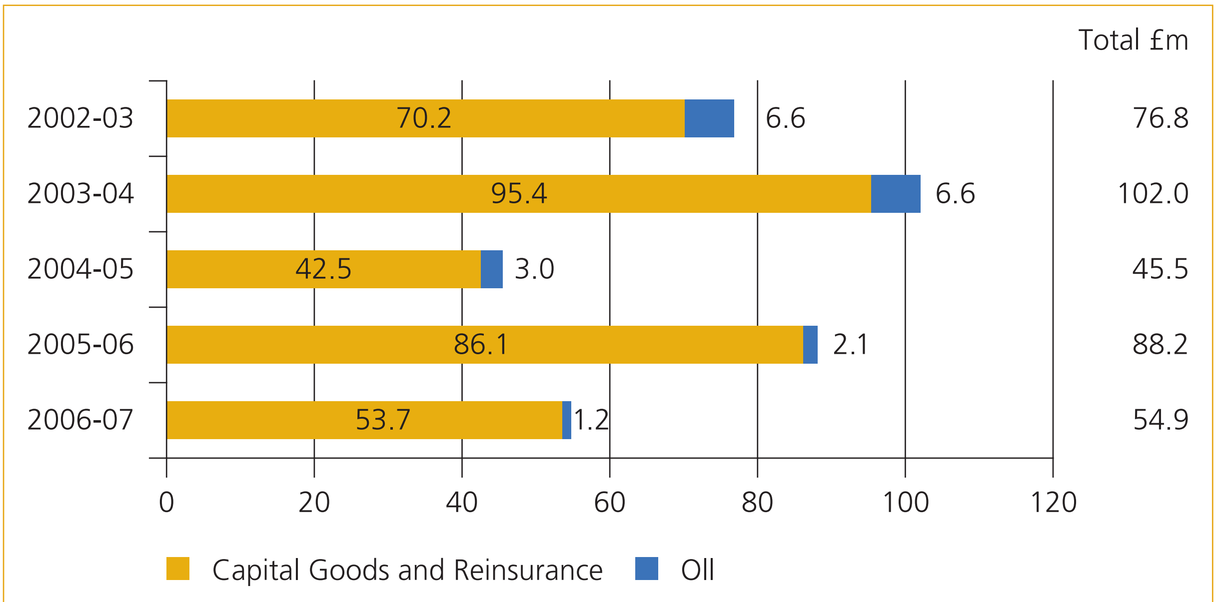
During 2006-07, ECGD supported a wide range of exports and investments and issued guarantees and insurance policies with an aggregate value of £1,798 million. This represented a 19 per cent decrease from the level of business supported in 2005-06.

Buyer Credit and Supplier Credit financing accounted for £799 million of support, Supplier Credit Insurance and Indemnities for £847 million and Overseas Investment Insurance ('OII') business for £152 million.

The business supported related to 20 overseas countries, compared with 25 the previous year, and the total number of guarantees issued fell from 151 to 91 (including 8 OII renewals, 5 fewer than last year).

Premium earned was £55 million, down by 38 per cent from 2005-06 levels, and there was a continued decline in the premium earned from OII as the size of this portfolio decreased.

Premium Earned (£m)



List of Guarantees and Insurance Policies Issued

Market/Exporter	Buyer/Airline/ Operating Lessor	Project	Case Impact[1]	ECGD Maximum Liability, £s or Equivalent
Azerbaijan				
Airbus S.A.S.	Azerbaijan Airlines	Airbus aircraft	-	4,623,163
Chile				
Airbus S.A.S.	LAN Airlines S.A.	Airbus aircraft	-	45,765,069
China				
Siemens VAI Metals Technologies Ltd	China Zhejiang International	Vantage Control System	Low	870,485
Siemens VAI Metals Technologies Ltd	Lanzhou Aluminium Company Limited	Vantage Control System	Low	447,173
Czech Republic				
Airbus S.A.S.	CSA Czech Airlines	Airbus aircraft	-	22,213,434
El Salvador				
Airbus S.A.S.	TACA International Airlines	Airbus aircraft	-	21,492,699
Kenya				
Rolls-Royce plc	Kenya Airways Limited	Trent engine	-	6,016,752
Malaysia				
Airbus S.A.S.	Airasia Berhad	Airbus aircraft	-	4,210,038
Mexico				
SLP Engineering Limited	Pemex Exploracion y Produccion.	KMZ Oil Field Offshore Accommodation Platform	Medium	13,275,285
Morocco				
Airbus S.A.S.	Royal Air Maroc	Airbus aircraft	-	5,256,022
Netherlands				
Airbus S.A.S.	Koninklijke Luchtvaart Maatschappij NV (KLM)	Airbus aircraft	-	12,122,704
Airbus S.A.S.	Aercap BV	Airbus aircraft	-	11,871,757
Pakistan				
Motorola Ltd	Pakistan Mobile Communications (PVT) Limited	Supply of GSM equipment for expansion	Medium	65,493,127
Philippines				
Airbus S.A.S.	CEBU Air, Inc.	Airbus aircraft	-	20,243,965
Mabey & Johnson Ltd	Dept of Finance, Philippines	Rural Bridges Programme	Medium	50,800,373
Qatar				
Airbus S.A.S.	Qatar Airways (Q.C.S.C.)	Airbus aircraft	-	91,396,727
Russian Federation				
Airbus S.A.S.	Aeroflot Russian Airlines JSC	Airbus aircraft	-	19,608,716
Thales Training & Simulation Limited	JSC Sukhoi Civil Aircraft	Superjet 100 full flight simulators	Low	23,955,611
Saudi Arabia				
Foster Wheeler Energy Limited	Yanbu National Petrochemical Company	Yansab Petrochemical Project	High	44,851,381
Fluor Limited	Yanbu National Petrochemical Company	Yansab Petrochemical Project	High	76,920,504
Taiwan				
Siemens VAI Metals Technologies Ltd	Dragon Steel Corporation	Taichung Steel Works upgrade	Medium	86,317,786
Thailand				
Rolls-Royce Power Engineering plc	Thai Airways International Public Company Limited	Trent engines for Boeing 777	-	34,532,055
Turkey				
Airbus S.A.S.	Turkish Airlines (THY)	Airbus aircraft	-	75,402,081
United States of America				
Airbus S.A.S.	Aviation Capital Group Holding Corp	Airbus aircraft	-	37,926,842
Airbus S.A.S.	International Lease Finance Corporation	Airbus aircraft	-	67,471,635
Vietnam				
Airbus S.A.S.	Vietnam Airlines Corporation	Airbus aircraft	-	43,861,999
		Sub-Total		**886,947,383**
		Other business not listed[2]		911,270,787
		Grand Total		**1,798,218,170**

1 The level of environmental and/or social impacts that could potentially occur without the intervention of the impact elimination systems. See the ECGD website for more information on ECGD's case impact analysis process at: http://www.ecgd.gov.uk/index/pi_home/case_impact_analysis_process.htm

2 Details of some further cases are commercially confidential and not disclosed.

Aerospace

ECGD continued to provide support to the UK's civil aerospace industry, although demand was reduced from last year due to the buoyancy of the commercial markets in arranging financing for aircraft without Export Credit Agency backing, particularly in major growth markets such as China.

ECGD, along with its French and German counterparts, provided support in respect of 58 deliveries of Airbus aircraft. This involved ECGD issuing guarantees amounting to some £483 million. The aircraft were delivered to 15 different airlines and operating lessors in Azerbaijan, Chile, Czech Republic, El Salvador, Malaysia, Morocco, Netherlands, Philippines, Qatar, Russian Federation, Turkey, USA and Vietnam.

ECGD also provided support for Rolls-Royce Trent engines installed on Boeing aircraft under its cooperation agreement with US Eximbank. Guarantees amounting to some £41 million were issued in respect of Boeing aircraft delivered to Kenya Airways and Thai Airways.

Support of some £24 million was also provided in respect of a Thales contract to supply full flight simulators to Sukhoi Civil Aircraft in Russia for the Sukhoi Superjet 100 regional airliner.

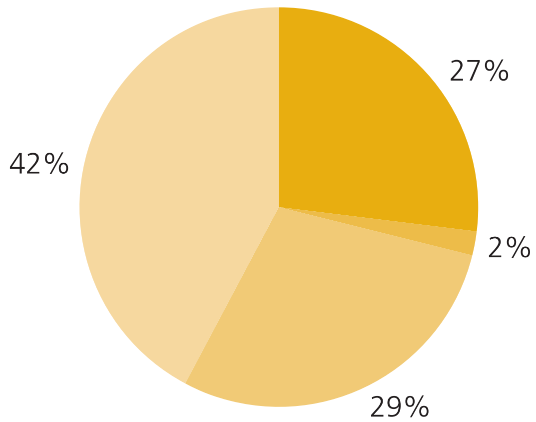
Defence

The UK applies strict controls to defence equipment exports through a licensing system administered by the Department for Business, Enterprise and Regulatory Reform and also involving the Department for International Development, the Foreign and Commonwealth Office and the Ministry of Defence. The provision of ECGD support for export sales that are subject to an export licence is conditional upon that licence being obtained.

During the year, ECGD support amounted to some £750 million for UK defence exports, representing some 42% of ECGD's total business for the year.

ECGD will support a major contract secured by VT Ships in Trinidad and Tobago in 2007-08.

Value of Business Supported by Sector (%)



		2006-07	2005-06	2004-05	2003-04	2002-03
Airbus		**27%**	44%	31%	17%	14%
Other Aerospace		**2%**	3%	1%	6%	1%
Civil		**29%**	30%	30%	38%	35%
Defence		**42%**	23%	38%	39%	50%

Civil

Infrastructure

ECGD supported a further contract for Mabey & Johnson to provide steel bridging in the Philippines. The 2006 contract involved the supply of 458 modular panel bridges to rural areas around the country. In order to finance this deal, ECGD agreed to guarantee a loan of ¥19.1 billion, with reinsurance being given by EKN of Sweden for goods sourced outside the UK. Mabey & Johnson has now installed in excess of 1,500 bridges in the Philippines under the on-going President's Bridge Programme.

Metals, Mining and Process Plant

The recent trend for refurbishment of existing steel plants continued, and ECGD supported plant upgrades in China and Taiwan with a total insured value of £88 million. In addition, ECGD provided support for a number of similar contracts in India during the year.

Oil, Gas and Petrochemicals

ECGD provided a re-imbursement Supplier Credit Facility to HSBC to support a US$18 million loan to Pemex, the Mexican state oil company, to help finance SLP Engineering Limited's share of a US$164 million joint venture with Keppel O & M and Keppel Amfels (USA) for the design and construction of two accommodation platforms in the Bay of Campeche.

The largest financing concluded was the Yansab Petrochemical Project in Saudi Arabia, which will contain the world's biggest ethane 'cracker' and be one of the world's largest petrochemical complexes. It is the largest ever 'greenfield' project financing in Saudi Arabia, and the first that ECGD has supported in the Kingdom. ECGD is guaranteeing a loan of US$150 million alongside SACE (the Italian Export Credit Agency), which is providing some US$550 million of support. ECGD's support will facilitate exports from Foster Wheeler, based in Reading, and Fluor, based in Camberley. Foster Wheeler will provide project management services, while Fluor will design, engineer and plan the construction of the utilities and offsite facilities.

The innovative financing, which was awarded the Middle East Petrochemicals Project Finance Deal of the Year 2006 by Project Finance Magazine, contains the largest Islamic financing tranche (US$850 million) in any multi-sourced project financing to date. The Public Investment Fund of the Kingdom of Saudi Arabia is also providing some US$1 billion of finance, with total debt amounting to US$3.5 billion.

ECGD continued to consider the provision of support for the US$21 billion Sakhalin II gas and oil project in Russia. In December 2006, Royal Dutch Shell, Mitsui & Co and Mitsubishi Corporation, who were the shareholders of the project company, Sakhalin Energy Investment Company Limited (SEIC), reached an agreement with OAO Gazprom of Russia to bring them into SEIC as a majority shareholder. As at the date of publication of this review, a decision had yet to be taken as to whether ECGD support would be given to the project.

Telecommunications

Building on earlier successes, Motorola secured further orders with Pakistan's leading mobile phone operator, Pakistan Mobile Telecommunications Limited ('PMCL'). An ECGD-backed Buyer Credit was signed with PMCL to help finance the supply of Motorola GSM base transceiver stations. These will be deployed across Pakistan to extend PMCL's existing GSM network and provide additional network capacity.

Transport

Buyer Credit facilities totalling US$18.4 million in respect of contracts secured by Brecknell Willis & Co. Limited and Westinghouse Rail Systems Limited became effective. The contracts, for conductor rail, system components and automatic train control and protection equipment, are part of the ongoing development of the Beijing Metro system in preparation for the 2008 Olympic Games.

Overseas Investment Insurance

Overseas Investment Insurance ('OII') provides political risk insurance for up to 15 years. With the growth of private market alternatives, demand for this cover from ECGD has continued to reduce since its peak in 2001-02. The maximum liability in respect of OII stands at a total of £152 million as at 31 March 2007, a reduction from the £239 million total of 2005-06. This trend is expected to continue.

Renewable Energy

ECGD and the Department for Business, Enterprise and Regulatory Reform continue to promote the Government's Renewables Initiative. This offers to make a minimum of £50 million of ECGD cover available each year to support any UK renewable energy exports and investments that meet ECGD's minimum risk standards.

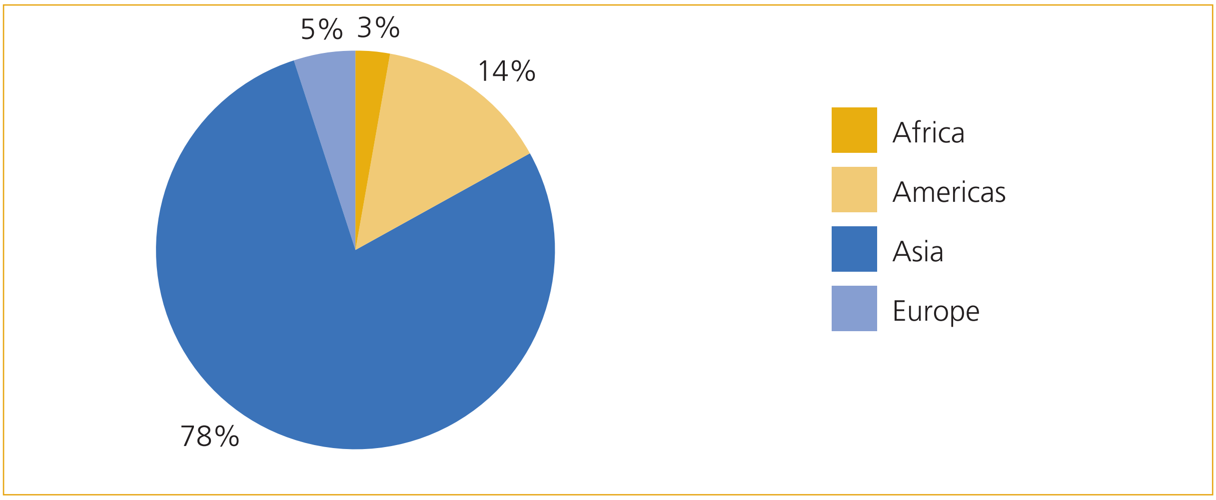
ECGD provides advice on export finance and insurance issues to the inter-departmental Sustainable Energy Exports Committee and a range of trade advisory groups, which bring together government and industry representatives from three key sectors:

- airports
- power
- water.

SME Support

During 2006, the Sovereign Star Trade Finance facility targeted at SME exporters was re-launched. The facility is run by Sovereign Star, a UK financial institution. It can provide overseas buyers with medium term finance for up to 5 years for their capital goods purchases. Loans will usually be for a maximum of £2 million and finance up to 85% of eligible goods and services.

Business Supported by Region (%)



Scott Shepherd, President and Chief Executive Officer of Northstar Trade Finance and Patrick Crawford signing the Sovereign Star agreement

Claims and Recoveries

ECGD pays claims once it is satisfied that a liability exists and, as appropriate, a claims waiting period has expired.

ECGD seeks to recover claims which it has paid:

- through the Paris Club, the informal group of official creditors which seeks to establish co-ordinated and sustainable solutions for debtor nations facing payment difficulties. ECGD implements debt rescheduling and debt write-off agreed by the Paris Club in respect of its exposure to some of the world's poorest countries, reflecting the UK Government's commitment to addressing debt sustainability; or
- directly, on a case-by-case basis (non-Paris Club recoveries).

Claims

The benign global risk environment has led to a reduction in the level of paid claims. Payments authorised on capital goods and project business decreased from £79 million in 2005-06 to £61 million, the lowest annual level of claims since 1976-77. As was the case in 2005-06, no new claims were authorised in the course of the year.

Recoveries

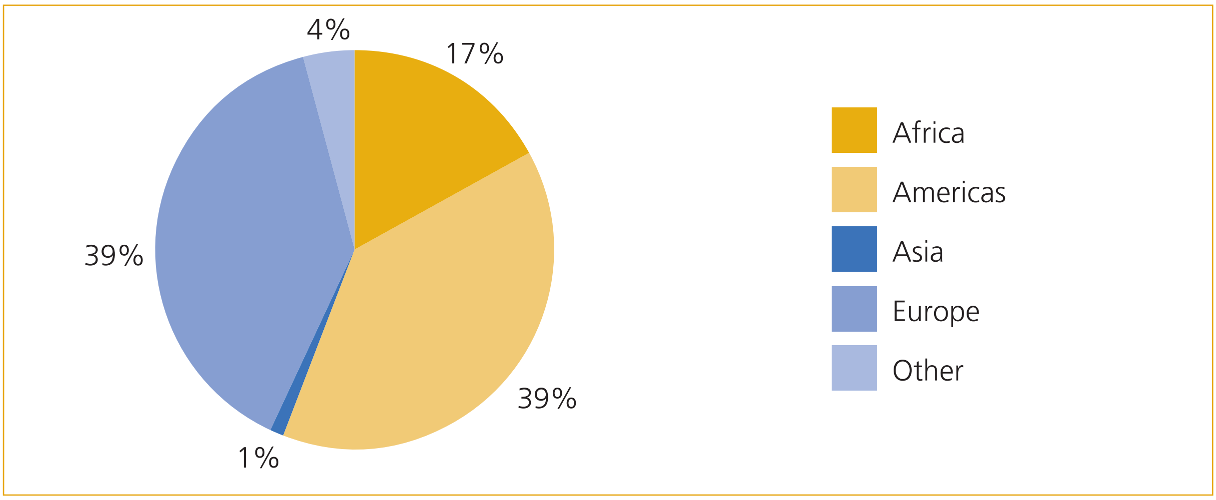
Recoveries of principal amounts increased from £720 million in 2005-06 to £872 million in 2006-07. The main sources of recoveries were Algeria, Nigeria and the Russian Federation.

Paris Club Activity

ECGD received a total of £1,396 million in rescheduled debt and interest payments under bilateral debt rescheduling agreements, compared to £1,691 million in 2005-06. Through the Paris Club, ECGD participated in a new rescheduling with Grenada (£2 million) and final debt treatments for Cameroon, Malawi and Sierra Leone under the Heavily Indebted Poor Countries Initiative. All debt owed by Malawi and Sierra Leone, amounting to £300,000 and £3 million respectively, was forgiven. Cameroon received a final write-off of approximately £37 million.

Following the agreement reached between Nigeria and its Paris Club creditors in October 2005, the final element of the payment due from Nigeria was received by ECGD when £661 million was paid on 25 April 2006.

Claim Payments by Region (%)



Pre-payment agreements in respect of Paris Club debt owed to ECGD were signed with Algeria (£110 million), Macedonia (£1.5 million) and Russia (£382 million). This cleared all outstanding debt with these countries.

Angola began to reduce its arrears to Paris Club creditors. ECGD received £90 million to clear arrears, other than late interest. This was the first payment to be made by Angola since 1989.

As a result of high receipts and debt reductions, the amount owed to ECGD under Paris Club restructurings has continued to fall and is now £3.3 billion.

Non-Paris Club Recoveries

Recoveries of £69.3 million were made during the year, of which £0.8 million related to recoveries of claims paid under Short and Extended Terms Guarantees underwritten by the Insurance Services Group, which was privatised in 1991. The figures were, respectively, £61 million and £1.3 million in 2005-06.

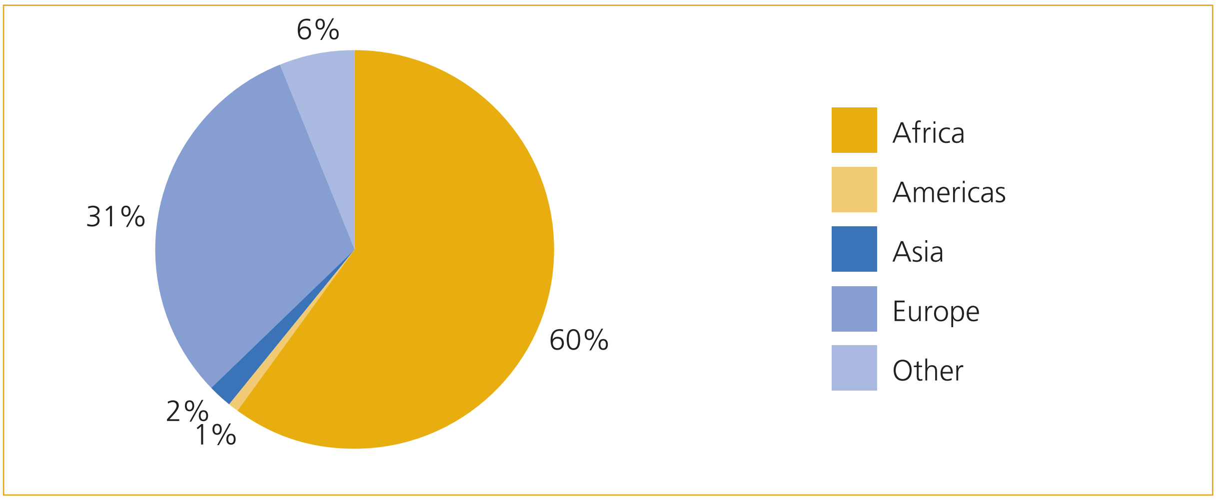
For yet another year, recovery work was dominated by the aircraft sector. Taking advantage of a buoyant market for second hand aircraft, 16 aircraft, which had been repossessed by agent banks from failed airlines, were sold. In addition, one airline recovered from financial difficulties, enabling it to prepay amounts owing under restructured leases in respect of 3 aircraft. Recoveries were also made in respect of 2 aircraft, which were the subject of a total loss for insurance purposes.

As a result, at 31 March 2007, ECGD's distressed airline portfolio accounted for 84 aircraft involving 9 airlines, where aircraft have been repossessed or where the lease repayments have been restructured. This compares to figures of 105 aircraft involving 12 airlines as at 31 March 2006. ECGD's distressed aircraft exposure as at 31 March 2007 was £444 million, a reduction from £639 million as at 31 March 2006.

66 aircraft with an exposure of £321 million remain in operation with their original airlines on restructured leases.

Of the remaining 18 repossessed aircraft in the distressed portfolio, there are firm prospects for sale in respect of 16 aircraft and some possibility of the disposal of the remaining 2.

Recoveries by Region (%)




CSA
CZECH AIRLINES

Operations

Pilot Trading Fund

By the end of the financial year, ECGD had completed the second of three years operating as a Pilot Trading Fund. The pilot was set up to test whether it would be appropriate for ECGD to establish a Statutory Trading Fund, and, if so, under what conditions. The Pilot Trading Fund systems and processes have proved successful, leading to improved reporting and risk management.

However, there have been changes in the external environment since the proposal to establish an ECGD Trading Fund was first mooted, and Ministers have decided that it is not appropriate to proceed further on this basis. Instead, the best features of the risk management structure will be retained, within a new financial framework which will also incorporate certain arrangements common to other government departments.

Risk Management

Last year, ECGD reported on enhancements being made in risk management in the areas of portfolio modelling, stress testing and scenario analysis, and country limit setting methodology.

Under the new Exposure Management Framework, exposure limits have now been re-defined on a more transparent and consistent basis across all markets. This has increased risk capacity for some countries.

Additional refinements have been made during the year to improve further the quality of reporting, in comprehensive risk reports which are produced on a regular basis. This has strengthened the risk management of the portfolio and case decision-making at Risk Committee.

Given ECGD's experience over many years in dealing with distressed airline cases, the opportunity has been taken to revisit airline risk modelling and underlying assumptions so as to improve risk and pricing decisions.

More recently, policy has been under review in a number of other areas, for example in the instance of the minimum risk standards for corporate risk so that they are expressed on a basis more consistent with how risk is measured elsewhere. This will have the effect of enabling lower rated risks to be considered where a transaction is appropriately structured.

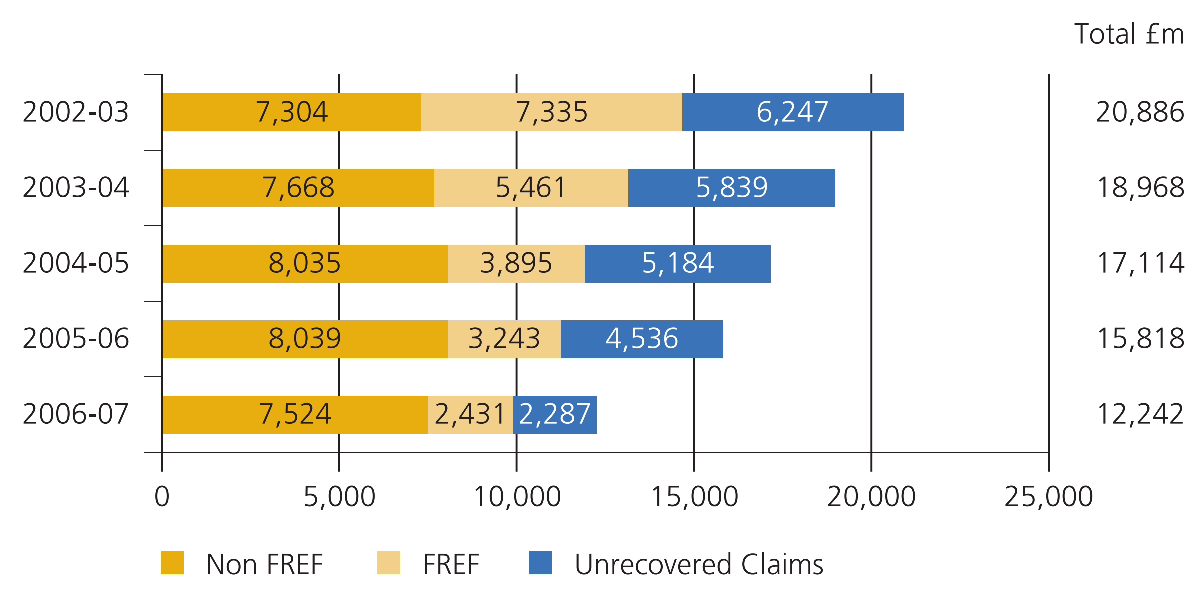
Also, new risk rating tools have been introduced to support risk analysis and inform risk decisions on exposure to small corporate buyers in a wide range of markets including, as has been mentioned elsewhere in this review, risks under the Sovereign Star Trade Finance facility.

Fixed Rate Export Finance

ECGD's Fixed Rate Export Finance ('FREF') scheme enables importers to obtain financing at OECD Commercial Interest Reference Rates (CIRRs). The current scheme was introduced in 2005. It will be reviewed in 2008 in the light of experience and of progress internationally in eliminating interest rate subsidies within the OECD régime.

FREF financing is available for US Dollars, Sterling, Euro and Japanese Yen loans. In 2006-07, ECGD supported two new guarantees that were arranged using FREF. ECGD uses a mix of interest rate hedging and loan refinancing techniques to limit the cost to it of offering FREF support. In 2006-07, interest rate hedges of US$38 million (six swaps), £14.8 million (nine swaps), €6.5 million (four swaps) and ¥9,330 million (ten swaps) respectively were entered into as part of ECGD's interest rate risk management activities.

Total Credit Risk Exposure on ECGD's Books (£m)



Debt Sales

Under Paris Club arrangements, Export Credit Agencies are permitted to sell a portion of debt to third parties, provided that the debts are redeemed in local currency and reinvested in the debtor's country. ECGD undertook such a transaction in Jordan, involving debt amounting to £12.5 million. This debt sale assisted in the privatisation and development of the former Royal Jordanian Airline Training and Simulation Centre.

Bribery and Corruption Procedures

Following a Public Consultation on proposals to strengthen ECGD's rules to assist the deterrence of bribery and corruption in contracts which it supports, the Government issued its Concluding Response in March 2006. Amongst a number of measures, two key changes were introduced; first, that names of agents involved in helping to secure the relevant contract must be disclosed to ECGD; and second, the introduction of internal Special Handling Arrangements for those exporters who wish to limit the number of ECGD staff who have knowledge of an agent's name, so as to minimise the risk of inadvertent disclosure in order to protect commercial confidentiality.

The new rules were implemented from 1 July 2006 alongside the introduction of new application forms with revised disclosure and warranty requirements. The new rules are consistent with the revised OECD Recommendation on Bribery and Officially Supported Export Credits, which was issued in December 2006.

The Trade and Industry Committee of the House of Commons published reports in July 2006 and in October 2006 on ECGD's new anti-bribery rules. The Committee commented that ECGD's procedures are in the vanguard of those countries tackling bribery and corruption, and that they should be workable and go some considerable way to reducing the risk of ECGD supporting contracts tainted by corruption. The Committee is due to review ECGD's experience in implementing these procedures in 2009.

Foreign Content review

In 2006-07 ECGD undertook a Public Consultation on its foreign content rules that govern the eligibility and amounts of foreign content that ECGD can support. The consultation proposed simplification and liberalisation of the current rules. The Government's Response was published in June 2007. In future, ECGD can support up to 80% foreign content of an eligible contract. This will be applied to contracts paid for on cash terms of payment and insured by ECGD or financed through credit and supported by ECGD under one of its guarantee products.

Information Technology

A new Head of IT was appointed in July 2006. An IT strategy has since been developed that takes account of the decision taken by ECGD three years ago to replace its suite of bespoke systems with new commercial systems. This subsequently led to the implementation of an industry standard loans administration system. The strategy will be used as the basis for the procurement of a new IT service contract when the existing contract expires in November 2009. It will also impose greater discipline in the development of new programs and, where appropriate, make better use of IT to support business processes to improve effectiveness and efficiency. The strategy envisages the early introduction of software to improve collaborative working through its workflow and document-management capabilities.

Data Management

During the year, considerable efforts have been made, under the auspices of a formal programme of projects, to improve data management. The programme is on track to deliver material improvements to the integrity, definition and control of data. This will in turn improve corporate and financial reporting.

Sovereign Debt Management

During the year, delays occurred in allocating and paying sovereign debt recoveries under bilateral debt rescheduling agreements involving a number of debtor countries, but principally Nigeria where a large volume of recoveries was received. These delays arose as a result of challenges that were encountered in using the new IT systems. ECGD creditors were kept informed of progress, with payments being resumed in December 2006. Some payments remain outstanding, for example, where the documentary evidence supporting the allocation of the payment is unclear or where creditors have become insolvent since the original debt was contracted. It is expected that these will be resolved during 2007-08.

Human Resources

A new Head of Human Resources was appointed in December 2006.

In 2006-07, a key challenge was to complete the final stages of a Cost and Efficiency Review that had begun in the previous financial year. A major aim was to reduce staffing levels from 315 to 268, by March 2007. This was achieved, assisted by the closure of the main Cardiff office as at 31 March 2006 and through an early retirement programme in London. This has delivered significant savings in ongoing staff costs of some £2 million per annum.

The loss of experienced staff has been challenging for ECGD. A key goal is to strengthen succession planning and career management. During the year, a successful recruitment campaign was launched to attract new staff at middle management levels. Priority is being given to ensuring staff are equipped through training and work experience, so that they are appropriately skilled.

A programme of work is being developed to update, improve and simplify a number of HR systems, including performance management and related arrangements, and pay and reward systems.

ECGD retained its status as an organisation committed to employing people with disabilities, including its right to continue using the Double Tick symbol. A draft Joint Equality Scheme has been published; once finalised, this will underpin ECGD's commitment to Equal Opportunities irrespective of age, disability, gender, race, religious belief, or sexual orientation.

Facilities Management

Following the closure of its main office in Cardiff, all ECGD's core business operations are now conducted from a single location in Harbour Exchange in London. Office space in Harbour Exchange was also rationalised during the year. This has resulted in reducing the use of floor space. Two floors of Harbour Exchange have been sub-let to the Legal Services Commission and ECGD's lease on its main Cardiff Office has been assigned to FirstRand Bank. As a result, there will be a reduction in ongoing accommodation costs of some £1.25 million per annum.

Freedom of Information

The Freedom of Information Act, 2000 (FOI) gave the public new rights of access to information held by public authorities, and came into force on 1 January 2005. Since then, ECGD has received a steady flow of requests covering a range of issues, such as ECGD's environmental impact assessments on projects which it has supported, particular sectors or business receiving its support, international debt and ECGD's organisational structure.

In 2006-07, ECGD received 65 requests for information, either under the Freedom of Information Act or the Environmental Information Regulations régime. These are broken down as follows:

Issue	No. of requests
Environmental information	27
ECGD's structure/contracts	9
Defence business	8
General ECGD business	8
International debt	5
Sakhalin II Project	5
Baku-Tbilisi-Ceyhan Pipeline Project	2
Anti-bribery and corruption procedures	1

This compares with the first full financial year of requests for information, in 2005-06, when ECGD received 54 requests. These were broken down as follows:

Issue	No. of requests
Defence business	14
ECGD's structure/contracts	11
International debt	8
Environmental information	6
Baku-Tbilisi-Ceyhan Pipeline	6
General ECGD business	4
FOI processes	3
Anti-bribery and corruption procedures	2

International Developments

ECGD has continued to take an active role within the EU and OECD in support of moves to strengthen the international regulation of export credits.

Aircraft Sector Understanding

One of the main areas of activity has been the negotiations at the OECD to establish new rules for export credit support for civil aircraft. ECGD's aim has been to establish new risk-related minimum premium rates as part of a comprehensive Aircraft Sector Understanding (ASU) that covers both large and regional commercial aircraft. The negotiations have involved existing OECD Participants, including the European Community, the USA and Canada, and also Brazil. This is consistent with the OECD's efforts more widely to expand the level playing field, so as to encompass non-OECD countries and encourage them to adopt the disciplines and common approaches of OECD providers.

Buyer Risk Assessment and Pricing

In support of the mandate given by the OECD Participants Group to the Premium Experts Group, ECGD is continuing to press for a common approach to buyer risk assessment and risk-reflective pricing for corporate risk.

Bribery and Corruption

ECGD attended OECD discussions on strengthening its rules on bribery and corruption. The OECD upgraded the resulting revised OECD Action Statement on Bribery and Officially Supported Export Credits to Recommendation status in December 2006. This served to enhance the formal status of its contents.

Responsible Lending

Responsible lending to low-income countries is a key concern for the UK Government following the Multilateral Debt Relief Initiative. ECGD, in close coordination with HM Treasury and the Department for International Development, has been working with OECD members, the International Monetary Fund (IMF) and the World Bank to develop proposals to ensure that new lending does not lead to unsustainable debt burdens for former Heavily Indebted Poor Countries (HIPCs) and countries that the World Bank classifies as eligible only for highly concessional loans and grants from the International Development Association (IDA-only).

Positive steps were made at the OECD Export Credits Group ('ECG') meeting in April 2007. The ECG agreed to improve information sharing with the IMF and World Bank and to extend the scope of the current OECD Statement of Principles on Unproductive Expenditure[3] beyond just HIPCs to also cover all IDA-only countries. This means that over 25 additional countries will be covered by the agreement.

ECGD is now working with international partners and the IMF and World Bank to present to the ECG in November 2007 proposals to strengthen the OECD Statement of Principles on Unproductive Expenditure.

3 http://www.oecd.org/document/27/0,2340,en _2649_34179_2675739_1_1_1_1,00.html

Sustainable Development

ECGD contributes to Sustainable Development mainly through its analysis of the impacts of overseas projects related to the exports or investments that it is asked to support.

ECGD's Business Principles Unit ('BPU') reviews applications in accordance with ECGD's policies on social and environmental impacts. The policies provide that projects that comply with these relevant international standards will normally be considered acceptable on environmental and social grounds, although due consideration is given to the specific requirements of each project's actual site and location.

In 2006-07, the largest part of the BPU's resource was focused on the continuing review of the Sakhalin II Phase 2 oil and gas project in Russia. A number of site visits were made during 2006-07.

The BPU also monitored performance of projects for which support had been issued in previous years. These included the Baku-Tbilisi-Ceyhan pipeline project, the Nigeria LNG plant, and phases 9 & 10 of the South Pars gas production and refinery project in Iran.

In the international arena, ECGD contributes to Sustainable Development through the influence it is able to exert in various international fora.

ECGD welcomed the agreement in April 2006 on a strengthened OECD Action Statement on Bribery and Officially Supported Export Credits. This represented a positive step forward by tightening existing arrangements and improving transparency. In December 2006, the revised Action Statement was upgraded by the OECD Council to an OECD Recommendation, representing a higher degree of commitment to compliance. ECGD's revised rules which were introduced in July 2006, as noted earlier, were compliant with the OECD Action Statement.

Also during 2006-07, a review of the OECD Recommendation on Common Approaches on the Environment and Officially Supported Export Credits (the Common Approaches) was in progress. ECGD's main objectives were to seek greater consistency in the process for identifying and categorising projects, to obtain a clear definition of the minimum international standards that should normally be met, and to clarify the extent to which social impact issues might be addressed. As part of this, ECGD hosted an ECAs' Environment Practitioners workshop to facilitate the identification of the options and implications relating to the possible adoption of Performance Standards of the International Finance Corporation. Agreement on a revised text was reached in May 2007; this was adopted by the OECD Council and published on 12 June 2007.

ECGD also contributes to Sustainable Development through improvement of its own environmental and social performance. To this end, ECGD developed a comprehensive Sustainable Development Action Plan during 2006-07 in fulfilment of the commitment it made in 2005. This was published on 30 April 2007. It identifies specific actions that ECGD will implement to reduce its direct environmental footprint, offset some of its emissions and encourage good practice by its staff including undertaking voluntary work in the community. ECGD will also be taking action in order to demonstrate its adherence to the objectives set out in the Sustainable Development Commission's report of February 2007 on Sustainable Development in Government. ECGD's Sustainable Development Action Plan 2007 can be found on ECGD's website.

The Management Board

1. Nicholas Ridley
(General Counsel)

2. John Wright
(Non-Executive Director, retired March 2007)

3. Steve Dodgson
(Director, Business Group)

4. David Godfrey
(Non-Executive Director)

5. Graham Pimlott
(Chairman)

6. David Harrison
(Non-Executive Director)

7. Katherine Letsinger
(Non-Executive Director)

8. David Havelock
(Director, Credit Risk Group)

9. Patrick Crawford
(Chief Executive)

10. Peter Haslehurst
(Non-Executive Director)

11. Nigel Addison Smith
(Finance Director)

The Board

The Management Board (the 'Board') of ECGD, which is responsible for advising and supporting the Accounting Officer in respect of the governance of ECGD, consists of four independent Non-Executive Directors and a Non-Executive Chairman, together with members of the Executive Committee of ECGD. There were three new appointments to the Board during the year. Peter Haslehurst, Chairman of Luxfer Holdings PLC and Katherine Letsinger, former Group Finance Director of Wellington Underwriting plc, were appointed as Non-Executive Directors. Steve Dodgson was appointed Director, Business Group (having previously been a member of the Board as Head of Human Resources), succeeding Victor Lunn-Rockliffe who retired in June 2006. After six years as a member of the Board and as Chair of the Audit Committee, John Wright retired in March 2007, and has been succeeded by Katherine Letsinger as Chair of the Audit Committee.

The Board is accountable to Ministers for the governance and performance of ECGD within the policy framework set by Ministers. The Board has responsibility for, amongst other things, the Annual Review and Resource Accounts, strategy, annual business plan and certain significant policies (such as those on risk appetite). The Board has a regular schedule of meetings, and holds ad hoc meetings as required by the ongoing business of ECGD. Senior managers meet weekly as the Executive Committee, chaired by the Chief Executive, to deal with the ongoing management of ECGD.

Statement on Compliance with the Code of Good Practice

In 2005-06, the Board conducted a review of ECGD's compliance with the Code of Good Practice for Corporate Governance in Central Government Departments and found ECGD's governance arrangements to be fully compliant with the Principles of the Code. The conclusions continued to be relevant this year.

Officers of the Shareholder Executive meet Non-Executive Directors annually to review governance in the absence of the Chairman and of ECGD members of staff.

Committees

The most senior committees of the Board are the Audit Committee and the Remuneration Committee. These Committees are entirely composed of independent Non-Executive Directors.

In support of the Accounting Officer in the ongoing management of ECGD are the Executive Committee, the Risk Committee, and the Business Systems and Infrastructure Committee, whose memberships comprise ECGD officials.

The Export Guarantees Advisory Council advises Ministers on matters upon which they request advice. It focuses its advice to ECGD upon the application of its Business Principles. The membership comprises individuals appointed by Ministers.

Audit Committee

The Audit Committee meets regularly with ECGD's senior financial management and internal audit staff to consider ECGD's arrangements for financial reporting, governance, risk, internal control and assurance. The External Auditors, the Accounting Officer and other senior members of staff attend meetings as required. The Chair formally reports to the Board after each meeting of the Audit Committee. At least once a year, the Chair meets separately with the Non-Executive Directors, the Head of Internal Audit and the External Auditors outside formal Committee meetings and in the absence of other members of ECGD staff in order to review the Committee's activities.

Remuneration Committee

The Committee reviews recommendations from the Chief Executive for the setting of remuneration for staff members who belong to the Senior Civil Service. It further decides on the remuneration of the Chief Executive following consultation by the Chairman with the Shareholder Executive.

Details of ECGD's remuneration policy and practice are set out in the Remuneration Report.

Non-Executive Directors

The Board considers that its Non-Executive Directors are independent. In making this determination, the Board has considered whether each such director is independent in character and judgement and whether there are relationships or circumstances which are likely to affect, or could affect the director's judgement.

Board Performance Evaluation

In 2006, a thorough Board performance evaluation was carried out with advice from both Executive and Non-Executive Directors, as a result of which the Chairman made some changes to Board procedures. A more informal review was undertaken in 2007 and its findings were reviewed by the Board in June.

The Chief Executive and Shareholder Executive officials assess the performance of the Chairman annually.

Internal Audit and Assurance

ECGD's internal audit strategy and plan are important elements of its control framework and corporate governance procedures. These include an integrated approach to audit and risk management, which links risk-based audits with ECGD's risk and assurance framework.

Internal Audit advises senior managers on the completion of their annual Letters of Assurance to the Chief Executive and on associated risk management and control procedures, in support of the Statement on Internal Control in the associated Resource Accounts by the Chief Executive as the Accounting Officer. In these letters, managers identify their objectives and responsibilities, and provide a summary of the risk management, control and review processes in operation throughout the accounting period. They also describe any significant internal control issues.

Internal Audit also undertakes an annual programme of visits to banks and exporters to check for compliance with certain terms and conditions of the issued guarantees. Where appropriate, this may include a site visit to gain a better understanding of the contract under review.

Findings arising from all audit work are discussed with the relevant staff and any action required to improve control is agreed with the relevant manager. Follow-up of these agreed actions is monitored by Internal Audit and reported to the Executive Committee and to the Audit Committee.

Operational Risk

Annually, the Board approves objectives and plans, and considers the main risks to the achievement of objectives; mitigating actions are determined and the success of these actions monitored. An overarching strategic risk register is maintained and formally reviewed every six months by the Board.

Quarterly risk reports are provided by senior managers to the Executive Committee on the steps they are taking to manage risks in their areas of responsibility as part of the maintenance of Department-wide risk registers. Policy submissions to the Board and/or Ministers include an assessment of risk. Projects are governed by formal project management disciplines, including the regular review of project risks, overseen by either the Executive Committee or the Business Systems and Infrastructure Committee.

Export Guarantees Advisory Council Annual Report 2006-07

1. Andrew Wiseman (Partner, Blake Lapthorn Tarlo Lyons)

2. Anthony Shepherd (Chairman, The Alderley Group)

3. Professor Jonathan Kydd (Dean of the External System, University of London)

4. John Elkington Chair (Founder & Chief Entrepreneur, SustainAbility Ltd)

5. Paul Talbot (Assistant General Secretary, Unite-Amicus Section)

6. Peter Haslehurst – observer (Non-Executive Director)

7. Dr Robert Barrington (Director of Governance & Socially Responsible Investment, F&C Asset Management Plc)

8. Professor Glen Plant (Barrister)

9. Dr Raj Thamotheram (Director, Responsible Management, AXA Investment Managers Ltd)

10. Not pictured – Martin Roberts (Senior Consultant, Beachcroft Wansbroughs Regulatory Consulting)

We aim to advise Ministers on how ECGD can support UK industry, whilst at the same time contributing to sustainable development in emerging markets, and complying with Government policies on transparency and on combatting bribery and corruption, as set out in ECGD's Business Principles. We noted in last year's report our aim of focusing during 2006-07 on the latter aspects of our Terms of Reference (particularly items 5.5 and 5.6), an intention which we fulfilled.

The remit of the Council is defined by the Export and Investment Guarantees Act, 1991. Its Terms of Reference, along with the minutes of each EGAC meeting, and a Register of Member's interests, are available on the ECGD website.

During the year, we welcomed three new members to the Council: Dr Robert Barrington, Professor Glen Plant, and Andrew Wiseman, all of whom began their terms towards the end of 2006, and who each bring with them considerable expertise in areas related to ECGD's Business Principles. We also welcomed Peter Haslehurst, ECGD Non-Executive Director, acting as an observer. His role is to provide a link and closer understanding between the Council and ECGD's Management Board. Both new and existing members benefited from an informative induction session, covering ECGD's background, products, and Business Principles.

According to a pre-agreed schedule of fewer, longer meetings, the Council met four times in 2006-07 and considered a range of issues, providing advice to Ministers as appropriate. We met once with the then Minister for Trade, Investment and Foreign Affairs during the year, having the opportunity to discuss a number of topics. The Council considers that during this period ECGD operated in accordance with its existing Mission Statement and Business Principles.

The year saw the Council focus more particularly on policies stemming from ECGD's Business Principles, and their application to ECGD's activities. In October 2006, a highly informative meeting was held between the Council and representatives of NGO groups, at which ECGD-related issues of particular interest to the NGO community were discussed, with a view to helping inform the Council in the planning of its own forward agenda. The meeting was well attended, with a significant number of NGO groups represented, and it was agreed that a similar meeting would be held in 2007-08. The Council would like to express its appreciation for the NGO inputs.

During the year, the Council reviewed ECGD's policies relating to post-issue project monitoring and its case impact assessment procedures, and concluded that ECGD's policies in each area were both robust and appropriate. The Council also confirmed the extent to which its remit should cover exports in the defence sector, provoking useful debate. It is expected that the issue will form part of the Council's agenda for the forthcoming year.

At each meeting, the Council receives information from ECGD on the guarantees and insurance support issued in the course of the financial year, and how these comply with ECGD's Business Principles. The Council asked to review one case in detail during the year, and, in May 2007, it reviewed the activities of the Business Principles Unit of ECGD over the past twelve months.

The Council also examined the results of ECGD's public consultation on its rules for supporting Foreign Content, and was involved with the development of ECGD's Sustainable Development Action Plan. This latter relates both to ECGD's external policies on sustainable development and to internal issues, such as recycling. The Council continues to receive regular updates on ECGD's experience since the implementation of the Freedom of Information Act in January 2005. The Council noted the Sustainable Development Commission's assessment of ECGD's sustainable development performance and, while there are complexities that make some of the Commission's recommendations hard to implement, we will monitor this closely.

Patrick Crawford, ECGD Chief Executive, provides a briefing at each of our meetings on ECGD's financial position and risk management policies and processes, as well as the current issues facing ECGD. This year, a specific focus was ECGD's work internationally, particularly in areas relating to the Berne Union of Credit and Investment Insurers, the Aircraft Sector Understanding under the OECD Arrangement, and the OECD Common Approaches on the Environment.

Over the coming year, the Council aims to continue its focus on how the Business Principles relate to the day-to-day work of ECGD, as well as continuing what it is now expected to be an annual meeting with NGOs to hear their views – and to report back on progress. As a result, the Council will be able to provide better-informed advice to ECGD and its Ministers, as they consider the UK's response to current issues.

John Elkington
Chair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Annual Report

OVERALL RESULTS

1 The Export Credits Guarantee Department (ECGD) issues guarantees against loss for exporters of UK goods and services and overseas investors from the UK, and provides Fixed Rate Export Finance ("FREF") on behalf of exporters. ECGD achieved an operating surplus in 2006–07 of £403.8 million, down from £1,698.9 million in 2005-06, even though the recoveries of Principal and Interest for the year were £1,536 million for 2006-07 compared to £1,678 million for 2005-06. The majority of the recoveries during the year were consistent with those expected and accounted for in the prior year. A summary analysis of the results is set out in the Management Commentary below.

STATUTORY POWERS

2 ECGD is a Department of the Secretary of State for Business, Enterprise and Regulatory Reform. It derives its statutory authority from the Export and Investment Guarantees Act, 1991 (the Act), and its primary function is to facilitate exports of goods and services by the provision of guarantees and insurance pursuant to Section 1 of the Act. Section 2 enables ECGD to provide Overseas Investment Insurance.

3 ECGD is able to make any arrangements considered to be in the interests of the proper management of the ECGD portfolio. Such arrangements may comprise any form of transactions, including lending, and providing or taking out insurance and guarantees (Section 3). Section 4 permits transactions under these sections to be on such terms and conditions as ECGD considers appropriate and states that its powers are exercisable only with the consent of HM Treasury. Section 13 requires ECGD to consult the Export Guarantees Advisory Council (EGAC) when determining whether there is a national interest case for providing reinsurance support.

4 The financial statements which follow are prepared in accordance with the Accounts Direction issued under Section 5(2) of the Government Resources and Accounts Act, 2000.

MINISTERS

5 The Ministers who had responsibility for ECGD during the year ended 31 March 2007 and up to the date of these accounts were:

The Rt Hon Alan Johnson MP, Secretary of State for Trade and Industry (to 5 May, 2006)
The Rt Hon Alistair Darling MP, Secretary of State for Trade and Industry (from 5 May, 2006 to 28 June 2007)
The Rt Hon John Hutton MP, Secretary of State for Business, Enterprise and Regulatory Reform (from 28 June 2007)
Mr Ian Pearson MP, Minister of State for Trade and Investment (to 5 May 2006)
The Rt Hon Ian McCartney MP, Minister of State for Trade, Investment and Foreign Affairs (from 5 May, 2006 to 28 June 2007)
Malcolm Wicks MP, Minister of State (from 28 June 2007)

PERMANENT HEAD OF ECGD AND THE MANAGEMENT BOARD

6 ECGD's Accounting Officer is Mr Patrick Crawford.

7 The Management Board advises the Accounting Officer in his management and direction of ECGD and its staff so that it achieves its business and financial objectives within agreed resources and budgets. The Management Board consisted of the Accounting Officer and the following:

Executive Members:

Mr David Havelock, Credit Risk Group Director
Mr Nicholas Ridley, General Counsel
Mr Nigel Addison Smith, Finance Director
Mr Steve Dodgson, Human Resources Director (to 30 June 2006), Business Group Director (from 1 July 2006)
Mr Victor Lunn-Rockliffe, Business Group Director (to 30 June 2006)

Non-Executive Members:

Mr Graham Pimlott, (ECGD Chairman), Non-Executive Chairman, Metronet Group Holdings Ltd
Mr David Godfrey, Head of Credit & Financial Market Risk, Swiss Re
Mr David Harrison, former Group Advisor, Lloyds TSB Group plc
Mr John Wright, former CEO of Clydesdale Bank plc and of Yorkshire Bank plc, (to 31 March 2007)
Mr Peter Haslehurst, Chairman, Luxfer Holdings plc, (from September 2006)
Ms Katherine Letsinger, former Group Finance Director, Wellington Underwriting plc, (from January 2007)

The remuneration of the Executive Members is determined in accordance with the rules for the Senior Civil Service (SCS). Non-Executive Members are paid a fee determined by ECGD.

ACTIVITIES OF ECGD

8 These financial statements present the results of ECGD's activities in issuing guarantees against loss for UK exporters, Reinsurance (Supplemental Reinsurance and Transitional Reinsurance), administration of discontinued credit insurance short-term facilities and Overseas Investment Insurance. These activities are referred to in the Resource Accounts as Underwriting Activities.

9 ECGD also performs other functions which are included in these statements. They consist of the provision of Fixed Rate Export Finance ("FREF") on behalf of UK exporters, together with arrangements for capital market funding of fixed rate export finance loans, and for certain interest rate swap arrangements. These activities are referred to in the Resource Accounts as Export Finance Activities.

10 There are no other entities included within the Resource Accounting boundary. Guaranteed Export Finance Corporation PLC ("GEFCO"), the special purpose vehicle through which ECGD conducts some of its Export Finance Activities, is not consolidated. This is in accordance with the Government Financial Reporting Manual ("FReM").

ACCOUNTS 1, 2, 3, AND 4

11 A number of the disclosures in the financial statements are disaggregated into four Accounts. Accounts 1, 2, and 3 cover ECGD's Underwriting Activities, while Account 4 covers Export Finance Activities.

Account 1 – guarantees issued for project business prior to April 1991 and guarantees issued by the Insurance Services Group of ECGD (the main part of which was privatised on 1 December 1991) for which ECGD retains all contingent liabilities ('Insurance Services Business').

Account 2 – guarantees issued for project business since April 1991, Overseas Investment Insurance (all years), and Reinsurance (Supplemental Reinsurance and Transitional Reinsurance) since the privatisation of the main part of the then Insurance Services Group on 1 December 1991.

Account 3 – guarantees issued, on the written instruction of Ministers, for project business since April 1991, which ECGD's Accounting Officer had advised did not meet normal underwriting criteria.

Account 4 – the provision of FREF to UK exporters, together with arrangements for capital market funding of FREF loans and for certain interest rate swap arrangements. FREF is only available to exporters doing business under Account 2.

SEGMENTAL INFORMATION

12 The Annual Review and Resource Accounts contains information regarding the regional spread of ECGD's guarantees and policies issued and its exposure as at 31 March 2007. Note 9 of ECGD's accounts outlines the results by Account while Note 11 analyses premium geographically and by business type.

FOREIGN CONTENT

13 Of the £1,031.0 million total support provided to UK exporters during the year, £91.3 million (8.9%) was in respect of goods and services sourced from outside the UK. For this purpose total support does not include Aerospace or OII.

PAYMENT POLICY

14 ECGD's payment policy is that all invoices should be paid on contractual due date or, where there is no contractual provision, within 30 days of receipt. This policy is in accordance with the requirements laid down in Government Accounting and follows the Confederation of British Industry (CBI) code on prompt payment of commercial debt. During 2006–07, ECGD paid 98.8 per cent of invoices within the policy requirement.

ECGD'S RECRUITMENT POLICY

15 ECGD is committed to the core principles of fair and open competition for recruitment and of selection on merit, as laid down in the guidance from the Civil Service Commissioners.

ECGD's systems and processes are subject to scrutiny by ECGD's Internal Audit and Assurance Division on a regular basis. A member of Human Resources Division (independent of the relevant recruitment exercise) undertakes an annual review on a sample basis of the recruitment exercises based on Internal Audit methodology. Any corrective action required is then taken to ensure that the required standard is delivered. These systems are also subject to annual audit by the Civil Service Commissioners.

The following recruitment schemes resulted in the appointment of a number of staff from outside the Civil Service:

- One candidate as Business Group Director (SCS2), recruited in conjunction with Michael Page International and the Civil Service Commissioners. One candidate as Head of IT (SCS1) recruited in conjunction with JM People. Both were male and not from an ethnic minority group.
- One candidate as Legal Advisor (Pay Band 11), recruited in conjunction with Lipson Lloyd Jones. One candidate as Service Delivery Manager (Pay Band 10), recruited in conjunction with JM People. Of the successful candidates, one was female, one was male, and neither was were from an ethnic minority group.
- Five candidates at Pay Band 6 (middle management), recruited in conjunction with Capita. Of the successful candidates, three were female, two were male, and none was from an ethnic minority group.
- Five candidates as Operational Research Analysts (Pay Band 5), recruited through the Government Operational Research Service. Of the successful candidates, two were female, three were male, and none was from an ethnic minority group.
- Two candidates (twelve successful at recruitment) at Pay Band 3, recruited in conjunction with Capita. Of the successful candidates, four were female, eight were male, and four were from an ethnic minority group.
- One candidate as Legal Secretary (Pay Band 2), recruited in conjunction with Reed. The successful candidate was a female, who was not from an ethnic minority group.
- Three candidates were appointed on a fixed term contract of 12 months or less. Of these, one was female, two were male, and none was from an ethnic minority group.

None of the above have declared a disability.

AUDIT

16 ECGD's accounts are audited by the Comptroller and Auditor General.

Management Commentary – Five Year Summary

	£m 2006-07	£m 2005-06	£m 2004-05	£m 2003-04	£m 2002-03
Operating Statement					
Overall Value of Guarantees and Insurance Policies Issued	**1,798**	**2,230**	**1,995**	**2,991**	**1,427**
Premium Income	**55**	**88**	**45**	**102**	**77**
Net Operating Income – total	**404**	**1,699**	**1,108**	**562**	**201**
– Account 1	211	1,464	892	424	161
– Account 2	159	143	89	115	132
– Account 3	23	54	51	22	0
– Account 4	10	38	76	0	(92)
Cashflow					
Recoveries in the year – total	**872**	**720**	**590**	**329**	**279**
– Account 1	735	682	530	285	229
– Account 2	137	38	60	44	50
Interest on Unrecovered Claims in the year – total	**593**	**958**	**595**	**231**	**201**
– Account 1	573	948	563	211	147
– Account 2	20	10	32	23	54
Claims Paid – total	**61**	**83**	**89**	**217**	**205**
– Account 1	-	4	-	12	36
– Account 2	61	79	89	205	225
Net Cash Flows – total	**1,557**	**1,815**	**1,427**	**246**	**258**
– Account 1	1,306	1608	914	433	350
– Account 2	168	103	66	(49)	(300)
– Account 4	83	103	447	(138)	208
Balance Sheet					
Amounts at Risk	**9,955**	**11,282**	**10,958**	**13,129**	**14,639**
Non-FREF	7,524	8,039	8,035	7,668	7,304
FREF	2,431	3,243	2,923	5,461	7,335
Recoverable Claims – Gross	**2,287**	**4,536**	**5,184**	**5,839**	**6,243**
– Account 1	1,444	3,574	4,289	4,902	5,412
– Account 2	843	962	895	937	831
Recoverable Claims – Net	**1,127**	**1,909**	**2,322**	**2,692**	**2,577**
– Account 1	540	1,233	1,694	2,046	2,028
– Account 2	587	676	628	646	549
Interest on Unrecovered Claims – Net	**184**	**601**	**212**	**-**	**-**
– Account 1	127	565	212	-	-
– Account 2	57	36	-	-	-
Underwriting Funds	**642**	**723**	**763**	**882**	**974**
– Account 1	5	6	21	29	39
– Account 2	624	687	660	725	787
– Account 3	13	32	82	129	148
Direct Funding balance	**998**	**1,475**	**1,878**	**2,416**	**3,166**
FREF Loans balance	**1,737**	**2,570**	**2,923**	**3,737**	**5,138**

Management Commentary

ACCOUNT 1

As Account 1 relates to guarantees issued before 1991, the main activity relating to this account is the administration and collection of the claims paid out against these guarantees. The key measurements are:

- Claims Recoveries in the year continued strongly at £735 million (£682 million 2005-06). The main recoveries in the year were Nigeria (£226 million), and the Russian Federation (£299 million). For both countries these payments are the final recoveries to be made.
- Recoveries of Interest on claims at £573 million were lower than 2005-06 (£948 million) but continued at a high level. Again, the main markets were Nigeria (£379 million), and Russia (£102 million) which both made their final payments.
- Gross and Net Recoverable Claims, which are the main asset within Account 1, have reduced significantly over the last few years. The balances for gross claims reduced markedly from £3,574 million (2005-06) to £1,444 million during the year, while net claims reduced from £1,233 million (2005-06) to £536 million during the same period. As Recoverable Claims have reduced to a relatively low level, the expected value of recoveries in the future will not reach the levels achieved in recent years.
- Interest on Unrecovered Claims has reduced from £564 million (2005-06) to £127 million as a result of the receipts from Nigeria and Russia during the year (see above). The reduced level of claims will also mean reduced levels of recoverable income in the future.
- Operating Income for Account 1 is generated when unrecovered claims or interest, which were not previously expected to be recoverable, become recoverable or recovered. During 2006-07, the reduction in Operating Income to £211 million from £1,464 million (2005-06) was due to the majority of the amounts recovered being treated as recoverable in the prior year.

ACCOUNT 2

Account 2 represents the current guarantee activity of ECGD and the key measurements are:

- Value of Guarantees Issued and Premium Income Generated. Both measures have decreased compared to 2005-06 with Guarantees Issued reducing from £2,230 million (2005-06) to £1,798 million and Premium Income from £88 million (2005-06) to £55 million. The reductions were caused by a significant reduction in airline sector business.
- Claims Authorised and Paid during the year reduced from £79 million to £61 million. There were no new claims authorised in the year, the amount representing further payments against claims previously authorised.
- Net Operating Income at £159 million shows an increase over £143 million recorded in the previous year. As ECGD operates through Underwriting Funds, the net insurance income for the year is dependent on the results of the funds closing in the current year. The net insurance income for the year was £91 million (2005-06, £52 million) relating to funds from 1997 £20 million and 2003 £71 million. In addition, Interest Receivable on Claims of £41 million (2005-06 £47 million) and Capital Income of £34 million (2005-06, £47 million) make up the balance of the Net Operating Income.
- Recoveries, Net Cash Flow, Gross and Net Recoverable Claims. Recoveries for the year were £68 million from political Claims of and £69 million from buyer claims; these were a significant increase over 2005-06 (£4 million for political claims, £34 million for buyer claims). As a result, the Gross and Net Recoverable Claims reduced during the year. Gross Claims reduced from £962 million to £843 million, while Net Claims reduced from £676 million to £587 million.

ACCOUNT 3

There were no new guarantees issued or claims made on this Account during the year. The income for the year of £23 million compares with £54 million for 2005-06, reflecting the release of the Underwriting Fund set up 10 years earlier.

ACCOUNT 4

This Account involves the provision of Fixed Rate Export Finance to export customers with the following key measures:

- FREF loan balances continued to run off during the year with the balance reducing from £2,570 million (2005-06) to £1,737 million due to loan instalments and early repayments.
- The Direct Funding balance represents the funds loaned by HM Treasury to reduce the cost of FREF. The balance reduced substantially during the year from £1,475 million (2005-06) to £998 million as both regular instalments and early repayments were made.
- Net Operating Income reduced from £38 million in 2005-06 to £10 million in 2006-07. The reduction was caused by increased cost of financing and lower gains on derivatives held to protect ECGD from adverse changes in interest rates.

ALL ACCOUNTS

- Operating expenses reduced by £2.8 million to £25.7 million, mainly as a result of the cost reduction programme. ECGD's staffing level decreased from an average full time equivalent of 304 for the year ended 31 March 2006 to 245 for the year ended 31 March 2007.
- For the reasons set out above, the major asset of ECGD, being Net Recoverable Claims reduced by 41% from £1,909 million (2005-06) to £1,127 million during the year. (Gross claims reduced from £4.5 billion to £2.3 billion).
- Within Financial Instruments held for Portfolio Management Purposes are the committed premia in respect of market-traded sovereign Credit Default Swaps shown in the balance sheet at £23.3 million on an amortised basis of the lives of the contracts. This is after including further premia committed in the year of £9.9 million and amortisation of £2.4 million. These derivatives have been purchased in order to manage the concentration of risk in certain markets.

DETAILED EXPLANATION OF VARIANCES BETWEEN ESTIMATE AND OUTTURN

It should be noted that ECGD is unusual as a department, having net income from various sources some of which can be offset against its costs; and in the case of one Request for Resources (RfR), the net request is reduced to a token sum of £1,000.

RfR 1 – Provision of export finance assistance

Overall, the estimated net cost after appropriations in aid was £71.6 million compared to an estimate of £102.8 million. The Other Current Expenditure totalled £42.6 million, while Estimate was £67.7 million, due in the main to the Estimate including £23.8 million for expected unwinding of derivative contracts whereas the actual cost was £1.5 million. In addition the Capital Charge, estimated at £66.2 million, was £60.2 million due to early repayments of loans during the year. Appropriations in Aid were restricted to the number included in the Estimate.

RfR 2 Provision of export credit guarantees and insurance

This RfR includes the administration costs of ECGD which are offset by Appropriations in Aid to give a requirement of zero (£1,000 for the Estimate). The total expenses at £26 million compares with the Estimate of £27.2 million. The costs for the year are significantly lower than the Estimate due to the larger than estimated reduction in headcount and related costs. Estimated costs were reduced by a £5 million contribution towards restructuring costs, which was accounted for in the previous year. The levels of Appropriation in Aid remain sufficient to reduce the net requirement to zero.

JPS Crawford
Accounting Officer
6 July 2007

Statement of Accounting Officer Responsibilities

1 Under the Government Resources and Accounts Act, 2000, HM Treasury has directed ECGD to prepare for each financial year resource accounts detailing the resources acquired, held or disposed of during the year and the use of resources by the department during the year. The accounts are prepared on an accruals basis and must give a true and fair view of ECGD income and expenditure, recognised gains and losses and cash flows for the financial year.

2 In preparing the accounts the Accounting Officer is required to comply with the requirements of the Government Financial Reporting Manual and in particular to:

- Observe the Accounts Direction issued by the Treasury, including the relevant accounting and disclosure requirements, and apply suitable accounting policies on a consistent basis;
- Make judgements and estimates on a reasonable basis;
- State whether applicable accounting standards as set out In the Government Financial Reporting Manual have been followed, and disclose and explain any material departures in the accounts; and
- Prepare the accounts on the going concern basis.

3 HM Treasury has appointed the Chief Executive as the Accounting Officer of ECGD. The responsibilities of an Accounting Officer, including responsibility for the propriety and regularity of the public finances for which the Accounting Officer is answerable, for keeping proper records, and for safeguarding ECGD's assets, are set out in the Accounting Officers' Memorandum issued by HM Treasury and published in Government Accounting.

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Remuneration Report

1 The following section provides details of the remuneration and pension interests of the members of ECGD's Management Board.

REMUNERATION

Remuneration Policy

Executive Directors

2 The executive members of the Management Board are members of the Senior Civil Service (SCS). The Cabinet Office determines the Senior Civil Service pay system. The remuneration of Senior Civil Servants is set by the Prime Minister following independent advice from the Senior Salaries Review Body (SSRB). In reaching its recommendations, the SSRB has regard to the following considerations:

- The need to recruit, retain and motivate suitably able and qualified people to exercise their different responsibilities;
- Regional/local variations in labour markets and their effects on the recruitment and retention of staff;
- Government policies for improving the public services including the requirement on departments to meet the output targets for the delivery of departmental services;
- The funds available to departments as set out in the Government's departmental expenditure limits;
- The Government's inflation target; and
- Evidence it receives about wider economic considerations and the affordability of its recommendations.

3 Recommendations made by the SSRB take account of the Government's overall approach to public sector pay. SSRB recommendations cover the level of uplift to the SCS pay bands in the light of economic evidence and movements in the private and wider public sector markets for senior executives. The SSRB also gives a view on performance awards for base salary and the minimum bonus payment.

4 Further information about the work of the Review Body can be found at www.ome.uk.com.

5 The SCS pay structure currently comprises four broad pay bands – Pay Bands 1,1A, 2 and 3. The pay band structure is underpinned by a tailored job evaluation scheme (JESP – Job Evaluation for Senior Posts), which provides a consistent basis for comparing the relative value of jobs within and across Departments.

6 The applicable base pay ranges from 1 April 2006.

Pay Band	Minimum £	Progression Target Rate (PTR) £	Recruitment & Performance Ceiling (RPC) £
1	55,000	77,000	116,000
1A	64,000	86,000	127,000
2	80,000	n/a	160,000
3	98,000	n/a	205,000

7 There are two components of SCS pay: base salary and bonus. Departments administer their own SCS reward arrangements, setting out how the overall SCS reward strategy is applied in their Department within the framework of the SCS pay system and the funding available. Departments also decide base pay and bonus awards for all their SCS staff. In practice, base pay salary increases are intended to reflect:

- The individual's overall growth in competence;
- The challenge associated with their job; and
- Confidence in the individual's future performance based on sustained past performance.

8 Within a range that is recommended by the SSRB as accepted by the Government, there is no centrally prescribed formula for deciding on individual awards. Departments are able to apply judgement to salary decisions and are permitted to vary awards to differentiate between levels of performance. Broadly, higher performers are paid a more significant award than those who have performed at a lower level.

9 The payment of bonuses is intended to reward in-year performance in relation to an individual's agreed objectives, or short-term personal contribution to wider organisational objectives. Bonuses are paid in addition to base pay increases and do not count towards pension. Bonuses are allocated from a 'pot', expressed as a percentage of the SCS salary bill, which is agreed centrally each year following the SSRB recommendations. The Cabinet Office issues guidance about how many of the SCS should receive a bonus. The intention is that bonus decisions are differentiated in order to recognise the most significant deliverers of in-year performance.

Non-Executive Directors

10 Non-Executive Directors are paid a flat fee for their attendance at Management Board, Audit and Remuneration Committee meetings, or to attend other ad hoc meetings and, from time to time, perform other duties. They are also paid travel and subsistence expenses.

11 The level of fees paid to the Non-Executive Directors is decided by the Shareholder Executive[1], on the advice of the Chairman of the Management Board. The Shareholder Executive, in consultation with the Chief Executive, decides the remuneration of the Chairman of the Management Board. The fees payable take account of:

- The going rate amongst other public bodies;
- The need to give a fair reflection of the time, including preparation for meetings, required to undertake the role; and
- Their advisory role; that they do not carry the same legal responsibilities as Non-Executive Directors in the private sector.

1 The Shareholder Executive is an operational body within the Department for Business, Enterprise and Regulatory Reform and is responsible for the oversight of Government-owned businesses and other organisations that operate on business-like principles including the provision, for a number of activities, of advice to the Secretary of State on the exercise by Ministers of responsibility for ECGD.

Remuneration Committee

12 The Remuneration Committee is responsible for overseeing the pay of SCS including the Executive Directors of the Management Board. The membership of the Remuneration Committee for 2006-07 was:

- Graham Pimlott – Chairman
- David Godfrey – Non-Executive Director
- John Wright – Non-Executive Director

13 The Chief Executive attends meetings. The Head of Human Resources Division acts as Secretary.

14 The role of the Committee is to ensure that Cabinet Office rules and guidance are properly applied in the operation of the Senior Civil Service pay. The Committee's terms of reference are to oversee the operation of the SCS pay system in ECGD. Specifically, the Committee:

- Issues an annual Pay Strategy;
- Reviews recommendations made by the Chief Executive on annual pay and bonus awards consistent with the SCS Pay System as promulgated by the Cabinet Office and, in the case of appeals, decide awards;
- Issues a report on the outcome of the annual SCS pay round to the Cabinet Office.

15 The Chairman of the Remuneration Committee makes recommendations to the Shareholder Executive in respect of the Chief Executive's pay, on the advice of other Non-Executive Directors.

Service Contracts

Executive Directors

16 Civil Service appointments are made in accordance with the Civil Service Commissioners' Recruitment Code, which requires these to be made on merit on the basis of fair and open competition but also includes the circumstances when appointments may otherwise be made.

17 The Executive Directors of the Board hold appointments that are open-ended. Early termination, other than for misconduct, would result in the individual receiving compensation as set out in the Civil Service Compensation Scheme.

Non-Executive Directors

18 Non-Executive Directors are appointed in keeping with the rules of the Office of the Commissioner for Public Appointments (OCPA). Non–Executive Directors are appointed on three year contracts, which may be extended. There is no contractual provision for the payment of compensation in the event of termination of contracts.

Remuneration (the following information has been subject to audit)

	2006-07 Salary £'000	2006-07 Benefits in kind (to nearest £100)	2005-06 Salary £'000	2005-06 Benefits in kind (to nearest £100)
Executive Directors				
Patrick Crawford *Chief Executive* *(Appointed July 2004)*	240-245	7,200	225-230	13,300
Nigel Addison Smith *Finance Director* *(Appointed June 2005)*	110-115	-	80-85 (100-105 full year equivalent)	-
Victor Lunn-Rockcliffe[2] *Director, Business Group* *(Appointed December 1991)*	25-30 (90-95 full year equivalent)	-	90-95	-
Steve Dodgson[3] *Director, Business Group* *(Appointed July 2006)*	100-105	-	80-85	-
David Havelock *Director, Credit Risk Group* *(Appointed October 2005)*	95-100	-	45-50 (100-105 full year equivalent)	-
Nicholas Ridley *General Counsel* *(Appointed June 1999)*	130-135	-	120-125	-
Non-Executive Directors				
Graham Pimlott *Non-Executive Chairman* *(Appointed December 2003)*	55-60	-	45-50	-
John Wright[4] *(Appointed April 2001)*	10-15	-	5-10	-
David Harrison (Appointed February 2002)	15-20	-	5-10	-
David Godfrey *(Appointed March 2005)*	5-10	-	5-10	-
Peter Haslehurst *(Appointed September 2006)*	5-10	-	-	-
Katherine Letsinger *(Appointed January 2007)*	0-5	-	-	-

Salary

19 'Salary' includes gross salary and bonuses. This report is based on payments made by ECGD and thus recorded in the Resource Accounts.

Benefits in kind

20 The monetary value of benefits in kind covers any benefits provided by ECGD and treated by HM Revenue and Customs as a taxable emolument. The Chief Executive had the private use of an allocated car in the circumstances permitted by the Civil Service Management Code.

2 Retired from the Management Board 30 June 2006
3 Head of Human Resources Division until 30 June 2006
4 Retired from the Management Board 31 March 2007

Pension Benefits

21 The pension provision is as follows (the following information has been subject to audit)

	Accrued pension at age 60 as at 31/3/07 and related lump sum £'000	Real increase in pension and related lump sum at age 60 £'000	CETV at 31/3/07 £'000	CETV at 31/3/06 £'000	Real increase in CETV £'000
Executive Directors					
Patrick Crawford *Chief Executive*	0-5	0-2.5	68	41	27
Nigel Addison Smith *Finance Director*	0-5	2.5-5	35	16	19
Victor Lunn-Rockliffe *Director, Business Group*	40-45 Plus lump sum of 120-125	0-2.5 Plus lump sum of 0-2.5	930	887	1
Steve Dodgson *Director, Business Group*	35-40 Plus lump sum of 105-110	2.5-5 Plus lump sum of 10-12.5	625	539	72
David Havelock *Director, Credit Risk Group*	0-5	0-2.5	44	14	26
Nicholas Ridley *General Counsel*	5-10 Plus lump sum of 25-30	0-2.5 Plus lump sum of 2.5-5	167	141	17
Non-Executive Directors	Nil	Nil	Nil	Nil	Nil

Civil Service Pensions

22 Pension benefits are provided through the Civil Service Pension arrangements. From 1 October 2002, civil servants may be in one of three statutory based 'final salary' defined benefit schemes (Classic, Premium, and Classic Plus). The schemes are unfunded with the cost of benefits met by monies voted by Parliament each year. Pensions payable under Classic, Premium, and Classic Plus are increased annually in line with changes in the Retail Prices Index. New entrants after 1 October 2002 may choose between membership of Premium or joining a good quality 'money purchase' stakeholder arrangement with a significant employer contribution (Partnership Pension Account).

23 Employee contributions are set at the rate of 1.5% of pensionable earnings for Classic and 3.5% for Premium and Classic plus. Benefits in Classic accrue at the rate of 1/80th of pensionable salary for each year of service. In addition, a lump sum equivalent to three years' pension is payable on retirement. For Premium, benefits accrue at the rate of 1/60th of final pensionable earnings for each year of service. Unlike Classic, there is no automatic lump sum (but members may give up (commute) some of their pension to provide a lump sum). Classic Plus is essentially a variation of Premium, but with benefits in respect of service before 1 October 2002 calculated broadly as per Classic.

24 The Partnership Pension Account is a stakeholder pension arrangement. The employer makes a basic contribution of between 3% and 12.5% (depending on the age of the member) into a stakeholder pension product chosen by the employee. The employee does not have to contribute but where they do make contributions, the employer will match these up to a limit of 3% of pensionable salary (in addition to the employer's basic contribution). Employers also contribute a further 0.8% of pensionable salary to cover the cost of centrally-provided risk benefit cover (death in service and ill health retirement).

25 The accrued pension quoted is the pension the member is entitled to receive when they reach 60, or immediately on ceasing to be an active member of the scheme if they are already 60.

26 Further details about the Civil Service Pension arrangements can be found at the website www.civilservice-pensions.gov.uk

Cash Equivalent Transfer Values

27 A Cash Equivalent Transfer Value (CETV) is the actuarially assessed capitalised value of the pension scheme benefits accrued by a member at a particular point in time. The benefits valued are the member's accrued benefits and any contingent spouse's pension payable from the scheme. A CETV is a payment made by a pension scheme or arrangement to secure pension benefits in another pension scheme or arrangement when the member leaves a scheme and chooses to transfer the benefits accrued in their former scheme. The pension figures shown relate to the benefits that the individual has accrued as a consequence of their total membership of the pension scheme, not just their service in a senior capacity to which disclosure applies. The CETV figures, and from 2003-04 the other pension details, include the value of any pension benefit in another scheme or arrangement which the individual has transferred to the Civil Service Pension arrangements and for which the Cabinet Office's Civil Superannuation Vote has received a transfer payment commensurate to the additional pension liabilities being assumed. They also include any additional pension benefit accrued to the member as a result of their purchasing additional years of pension service in the scheme at their own cost. CETVs are calculated within the guidelines and framework prescribed by the Institute and Faculty of Actuaries.

Real increase in CETV

28 This reflects the increase in CETV effectively funded by the employer. It does not include the increase in accrued pension due to inflation, contributions paid by the employee (including the value of any benefits transferred from another pension scheme or arrangement) and uses common market valuation factors for the start and end of the period.

JPS Crawford
Accounting Officer
6 July 2007

Statement on Internal Control

1. Scope of responsibility

1.1 ECGD is a Department of the Secretary of State for Business, Enterprise and Regulatory Reform. In fulfilling ECGD's statutory obligations under the Export and Investment Guarantees Act 1991 and in accordance with the connected HM Treasury Standing Consent and the duties assigned to me in Government Accounting, I have responsibility as Accounting Officer for maintaining a sound system of internal control that supports the achievement of ECGD's aims, objectives and policies, while safeguarding public funds and Departmental assets, for which I am personally responsible.

1.2 In discharging my responsibilities as Accounting Officer, I am advised by ECGD's Management Board and its Executive Committee.

1.3 I report to the Secretary of State for Business, Enterprise and Regulatory Reform and the Minister for Trade, Investment and Foreign Affairs. The Shareholder Executive (within the Department of Business, Enterprise and Regulatory Reform) is responsible for advising the Secretary of State on the Government's 'ownership interest' in ECGD. I have regular meetings with the Minister for Trade, Investment and Foreign Affairs, HM Treasury and the Shareholder Executive on a range of matters, including actual and potential risks to which the organisation is or may be exposed.

2. The purpose of the system of internal control

2.1 ECGD's primary business purpose is the assumption of financial risk through issuing guarantees or insurance contracts in furtherance of its statutory powers to facilitate exports and overseas investments. Separate arrangements exist to manage *financial risks*, i.e. credit and treasury risk exposures (that represent contingent public expenditure liabilities on the Exchequer until the risks expire), and the *operational risks* associated with the delivery of ECGD's objectives.

2.2 In regard to operational risks, the system of internal control is designed to manage risk to a reasonable level rather than to eliminate all risk of failure to achieve aims, objectives and policies; it can therefore provide only a 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 ECGD's aims, objectives and policies; to evaluate the likelihood of those risks being realised and the impact should they transpire; and to manage them efficiently, effectively and economically. The system of internal control has been in place in ECGD for the year ended 31 March 2007 and up to the date of approval of the Annual Review and Resource Accounts, and accords with HM Treasury guidance.

3. Capacity to handle risk

3.1 ECGD's Management Board and Executive Committee have the primary responsibility for identifying and monitoring the key financial and operational risks facing ECGD. Annually, the Management Board approves a Budget and Operational Plan, and considers the main risks to the achievement of objectives; mitigating actions are determined and the outcome of these actions monitored.

3.2 The Audit Committee, a sub-committee of the Management Board, examines and reviews, in conjunction with Internal Audit, the adequacy of the arrangements for accounting, risk management, internal control and governance. To avoid any perceived or actual conflicts of interest, the membership of the Audit Committee comprises solely of non-executive members. I am not a member of the Committee but attend its meetings, as does the Finance Director, the Head of Internal Audit and an official of the National Audit Office. The Chair formally reports to the Management Board after each meeting of the Audit Committee.

3.3 The Finance Director is responsible for the ongoing development and improvement of ECGD's operational risk management policies and procedures. Guidance has been provided for completing and reviewing risk registers which includes direction on risk escalation.

3.4 The Director of Credit Risk Group is responsible for the key credit risk management systems and processes in ECGD.

3.5 The Head of Human Resources is responsible for ensuring that ECGD employs good personnel management systems and practices, so that staff possess the right level of knowledge, skill and competence to run the business efficiently and effectively. The Staff Handbook sets out the principles and rules of conduct, including duty of care, standards of propriety and for avoidance of conflicts of interest, to which staff members are expected to adhere.

3.6 The General Counsel manages legal risk.

4. The risk and control framework

4.1 During the year, ECGD continued to improve and adapt its organisational and management arrangements in order to embed a culture of risk management and to provide a platform for ECGD to become more effective in the management of its financial and operational risks. These changes include:

- The successful completion of a plan to achieve necessary cost reductions and increases in efficiency, while retaining the necessary knowledge, skill and experience to continue to manage the business effectively;
- Learning from the experience of the Pilot Trading Fund to inform risk management policies and procedures and the components for the future financial management framework for ECGD;
- The introduction of industry and insurance expertise to the Management Board. Peter Haslehurst and Katherine Letsinger were appointed as Non-Executive members of the Board. Katherine Letsinger was also appointed as Chair of the Audit Committee with effect from 22 March 2007 in succession to John Wright following his retirement from the Management Board.
- The introduction of a revised exposure management framework, focusing on capital at a portfolio level and on exposure at a country level;
- The strengthening of ECGD's ability to meet OECD and Government policy by the introduction of revised anti-bribery and corruption procedures with effect from 1 July 2006;
- The instigation of a review of credit risk policy and procedures, including the consideration of options for an alternative approach to capital measurement having regard to ECGD's long-term and highly concentrated portfolio in higher risk markets;
- The review and updating of the policies and procedures for Active Portfolio Management;
- The development of a revised IT Strategy;
- The establishment of an Information Security Management Forum to oversee all aspects of Information Security work in support of the Departmental Security Officer; and
- The continuous improvement of the policies, structures and procedures concerned with managing financial and operational risks.
- The policies, structures and procedures for managing financial and operational risks are set out in separate Policy Statements. The structures and processes include:

Financial Risk

- The Risk Committee is responsible for the effective management of all aspects of ECGD's financial risk exposures, including case-related legal and reputational risks, in accordance with the policies set by the Management Board, implemented by the Executive Committee and contained in a Risk Policy Statement. Responsibilities are delegated by me to named individuals within a framework agreed by the Risk Committee and set out in the Risk Policy Statement.
- With the exception of entering into cross-currency swaps for the GEFCO refinancing operation, ECGD is not permitted to protect itself from any adverse impact on its financial performance as a result of exposure to foreign exchange risk. The issue of the future management of such exposures will be re-examined as part of the review of the Pilot Trading Fund period.

Operational Risk

- A strategic risk register is maintained; it is reviewed every six months by the Management Board. Policy submissions to the Management Board and to Ministers include an assessment of risk. Projects are governed by formal project management disciplines, including the regular review of project risks and issues, overseen by the Executive Committee or by the Business Systems and Infrastructure Committee on its behalf. Operational risk registers are maintained to allocate ownership for the management of operational risks. The risk registers are regularly reviewed by senior managers.

5. Review of effectiveness

5.1 As Accounting Officer, I have reviewed the effectiveness of the system of internal control. The main processes that have been applied in reviewing the effectiveness of the system of internal control include:

- Regular reports by Internal Audit, including the Head of Internal Audit's independent opinion on the adequacy and effectiveness of ECGD's risk management, control and governance systems, together with his recommendations for improvement;
- A formal year-end sign-off process by senior management in order to ensure that, as far as is possible, the controls and safeguards are being operated in line with established procedures, policies and standards;
- A process to monitor progress towards the key strategic goals and to ensure that the management of underlying risks, both at a strategic and operational level, is satisfactory;
- Periodic reports from the Chair of the Business Systems and Infrastructure Committee and the Head of the Business Change Unit;
- An annual review of legal risks by the General Counsel; and
- Comments made by the external auditors in their management letter and reports.

5.2 ECGD continues to be fully compliant with the Code of Good Practice for Corporate Governance in Central Government Departments.

5.3 The Management Board and its Audit Committee have advised me on the implications of the result of my review of the effectiveness of the system of internal control. A plan to address weaknesses and to promote continuous improvement of the system is in place. Significant issues for internal control include:

- Efficiency: The effective management of costs continues to be a key objective due to a decline in business levels and dependence on a small number of large contracts. Following the successful conclusion of a two year cost and efficiency plan, ECGD will continue to take steps to manage costs and increase efficiency. The emphasis will be on simplifying systems and processes, creating greater flexibility and maintaining the necessary knowledge and skills, against the requirement to contain costs taking account of current and expected future business levels.
- Data Management: Following the implementation of major commercial off-the shelf IT systems in August 2005, replacing outdated bespoke legacy systems, ECGD is making further improvements to processes and controls in order to achieve the full benefits of improved data quality and efficiency. A data quality programme has been set up to deliver these further improvements. Good progress has been made and the full benefits should be delivered by 31 March 2008.

JPS Crawford
Accounting Officer
6 July 2007

The Certificate and Report of the Comptroller and Auditor General to the House of Commons

I certify that I have audited the financial statements of Export Credits Guarantee Department for the year ended 31 March 2007 under the Government Resources and Accounts Act 2000. These comprise the Statement of Parliamentary Supply, the Operating Cost Statement and Statement of Recognised Gains and Losses, the Balance Sheet, the Cashflow Statement and the Statement of Operating Costs by Departmental Aim and Objectives 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 Remuneration Report that is described in that report as having been audited.

Respective responsibilities of the Accounting Officer and auditor

The Accounting Officer is responsible for preparing the Annual Report, which includes the Remuneration Report, and the financial statements in accordance with the Government Resources and Accounts Act 2000 and HM Treasury directions made thereunder and for ensuring the regularity of financial transactions. These responsibilities are set out in the Statement of Accounting Officer's Responsibilities.

My responsibility is to audit the financial statements and the part of the remuneration report to be audited in accordance with relevant legal and regulatory requirements, and with International Standards on Auditing (UK and Ireland).

I report to you my opinion as to whether the financial statements give a true and fair view and whether the financial statements and the part of the Remuneration Report to be audited have been properly prepared in accordance with HM Treasury directions issued under the Government Resources and Accounts Act 2000. I report to you whether, in my opinion, certain information given in the Annual Report from page 42-54 is consistent with the financial statements. I also report whether in all material respects the expenditure and income have been applied to the purposes intended by Parliament and the financial transactions conform to the authorities which govern them.

In addition, I report to you if the Department has not kept proper accounting records, if I have not received all the information and explanations I require for my audit, or if information specified by HM Treasury regarding remuneration and other transactions is not disclosed.

I review whether the Statement on Internal Control reflects the Department's compliance with HM Treasury's guidance, and I report if it does not. I am not required to consider whether this statement covers all risks and controls, or to form an opinion on the effectiveness of the Department's corporate governance procedures or its risk and control procedures.

I read the other information contained in the Annual Report and consider whether it is consistent with the audited financial statements. I consider the implications for my certificate if I become aware of any apparent misstatements or material inconsistencies with the financial statements. My responsibilities do not extend to any other information.

Basis of audit opinions

I conducted my audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. My audit includes examination, on a test basis, of evidence relevant to the amounts, disclosures and regularity of financial transactions included in the financial statements and the part of the Remuneration Report to be audited. It also includes an assessment of the significant estimates and judgments made by the Accounting Officer in the preparation of the financial statements, and of whether the accounting policies are most appropriate to the Department's circumstances, consistently applied and adequately disclosed.

I planned and performed my audit so as to obtain all the information and explanations which I considered necessary in order to provide me with sufficient evidence to give reasonable assurance that the financial statements and the part of the Remuneration Report to be audited are free from material misstatement, whether caused by fraud or error, and that in all material respects the expenditure and income have been applied to the purposes intended by Parliament and the financial transactions conform to the authorities which govern them. In forming my opinion I also evaluated the overall adequacy of the presentation of information in the financial statements and the part of the Remuneration Report to be audited.

Opinions

Audit Opinion

In my opinion:

- the financial statements give a true and fair view, in accordance with the Government Resources and Accounts Act 2000 and directions made thereunder by HM Treasury, of the state of the Department's affairs as at 31 March 2007, and the net cash requirement, net resource outturn, net operating cost, operating costs applied to objectives, recognised gains and losses and cashflows for the year then ended;
- the financial statements and the part of the Remuneration Report to be audited have been properly prepared in accordance with HM Treasury directions issued under the Government Resources and Accounts Act 2000; and
- information given within the Annual Report from page 42-54 is consistent with the financial statements.

Emphasis of Matter – Significant Uncertainty

In forming my opinion, I have also considered the adequacy of the disclosures made in Note 1 to the financial statements concerning the considerable uncertainty attaching to the final outcome of the underwriting activities. As explained in Note 1, the nature of these activities mean that the ultimate liability for claims and losses will vary as a result of subsequent information and events and may result in significant adjustments to the amounts included in the accounts. My opinion is not qualified in this respect.

Audit Opinion on Regularity

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

Report

I have no observations to make on these financial statements.

John Bourn
Comptroller and Auditor General
10 July 2007

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

Statement of Parliamentary Supply

Summary of Resource Outturn 2006-07

The Parliamentary control schedule compares outturn with estimate for both resource expenditure and the overall cash requirement.

			2006-07 Estimate			Outturn	2006-07	2005-06 Outturn
	Gross Expenditure	A. in A.	NET TOTAL	Gross Expenditure	A. in A.	NET TOTAL	Net Outturn Compared with Estimate Savings/ (Excess)	NET TOTAL
Request for Resources	**£'000**	**£'000**	**£'000**	**£'000**	**£'000**	**£'000**	**£'000**	**£'000**
1 Export Finance Assistance	133,977	31,170	102,807	102,812	31,170	71,642	31,165	72,445
2 Trading Operations	32,926	32,925	1	28,496	28,496	0	1	0
Total Resources	**166,903**	**64,095**	**102,808**	**131,308**	**59,666**	**71,642**	**31,166**	**72,445**
Non-Operating Cost A in A			338,282			0	338,282	0

Net Cash Requirement 2006-07

				2006-07	2005-06
		Estimate	Outturn	Net Outturn Compared with Estimate Savings/ (Excess)	Outturn
	Note	**£'000**	**£'000**	**£'000**	**£'000**
Net Cash Requirement	4	(1)	0	0	0

Summary of Income payable to the Consolidated Fund

In addition to appropriations in aid, the following income relates to ECGD and is payable to the Consolidated Fund (cash receipts being shown in italics):

			Forecast 2006-07		Outturn 2006-07
		Income	Receipts	Income	Receipts
	Note	**£'000**	**£'000**	**£'000**	**£'000**
Total	5	83,878	*512,168*	475,454	*2,024,126*

Explanations and variances between Estimate and Outturn (net total resources) are given in Note 2 and in the Management Commentary.

OPERATING STATEMENT

– for year ended 31 March 2007

	Note	2006-07 £'000	2005-06 £'000
Underwriting			
Gross Premium Income		63,229	91,386
Less ceded to other insurers		(8,377)	(3,179)
Net Premium Income	11	54,852	88,207
Amortisation of Instruments held for Portfolio Management		(2,389)	(2,175)
Interest Receivable	12	177,372	1,343,263
Claims Credit for the Year	13	89,144	177,721
Changes in Provisions for Losses on Future Claims	26	80,638	39,977
Staff Costs	14	(11,110)	(12,314)
Other Administration and Operating Costs	15	(9,513)	(11,716)
Foreign Exchange Gain/(Loss)	16	(47,517)	51,386
Capital Income/(Charge)		61,963	(12,990)
Net Income arising from Underwriting Activities		**393,441**	**1,661,359**
Export Finance			
Interest Make-up Scheme:			
Interest Support Costs		718	14,467
Net Movement in Fair Value of Derivatives		3,441	6,104
Directly Funded Export Finance Loans:			
Interest Income		70,243	111,803
Capital Charge		(60,235)	(89,171)
Provision for Counterparty Risk		1,254	841
Staff Costs	14	(3,157)	(2,275)
Other Administrative and Operating Costs	15	(1,893)	(2,165)
Foreign Exchange Loss	16	0	(2,014)
Net Income on Export Finance Activities		**10,371**	**37,590**
Net Operating Income for the year		**403,812**	**1,698,949**

There are no other recognised gains or losses for the current or preceding year.
All income and expenditure is derived from continuing operations.

The notes on pages 65 to 94 form part of these accounts.

Balance Sheet

As at 31 March 2007

	Note	2006-07 £'000	2005-06 £'000
Tangible Fixed Assets	19	1,505	2,251
Financial Instruments held for Portfolio Management Activities		23,266	15,740
Debtors due after one year	20 (i)	1,725,070	2,380,842
		1,749,841	**2,398,833**
Debtors due within one year	20 (ii)	638,352	1,692,964
Cash at Bank and in Hand	24	1,763,164	2,105,781
Other Financial Assets held at Fair Value	30	30,653	53,665
Total Current Assets		**2,432,169**	**3,852,410**
Creditors due within one year	25 (ii)	(1,828,159)	(2,171,807)
Total Net Current Assets		**604,010**	**1,680,603**
Total Assets less Current Liabilities		**2,353,851**	**4,079,436**
Creditors due after one year	25 (i)	(442,457)	(797,284)
Provisions for Losses on Future Claims	26	(642,009)	(722,646)
Other Financial Liabilities held at Fair Value	30	(38,376)	(65,548)
Total Net Assets		**1,231,009**	**2,493,958**
TAXPAYERS' EQUITY			
Exchequer Financing	27 (i)	(332,936)	(871,182)
Cumulative Trading Surplus	27 (ii)	1,557,833	3,348,636
General Fund	27 (iii)	6,112	16,504
Total		**1,231,009**	2,493,958

The notes on pages 65 to 94 form part of these accounts.

JPS Crawford
Accounting Officer
6 July 2007

Cashflow Statement

For year ended 31 March 2007

	Note	2006-07 £'000	2005-06 £'000
Net Cash Inflow from Operating Activities	29 (a)	1,556,821	1,815,533
Capital Expenditure and Financial Investment	29 (b)	467,305	395,996
Payment of Amounts due to Consolidated Fund	29 (d)	(2,105,781)	(1,745,590)
Financing	29 (c)	0	0
Amounts due to Consolidated Fund received in current year and paid over		(260,961)	(105,747)
(Decrease)/Increase in Cash in period	29 (d)	**(342,616)**	**360,192**

The notes on pages 65 to 94 form part of these accounts.

Statement of Operating Costs by Departmental Aim and Objectives

	2006-07 Gross Expenditure	Gross Income	Net	2005-06 Gross Expenditure	Gross Income	Net
	£'000	£'000	£'000	£'000	£'000	£'000
Departmental Aim						
To benefit the UK economy by helping exporters of UK goods and services to win business, and UK firms to invest overseas, by providing guarantees, insurance and reinsurance against loss taking into account the Government's international policies.						
Objective 1						
To provide UK exporters with guarantees and insurance to help them to win business: in accordance with its Business Principles, in accord with Government objectives, complementary to the private sector, and employing good management practice	(113,868)	307,090	193,221	(157,671)	393,293	235,622
Objective 2						
To secure an efficient market by ensuring as much as practicable a "level playing field" internationally in relation to government-supported Export Credit Agencies	(778)	0	(778)	(939)	0	(939)
Objective 3						
To recover as much as possible of the debt in respect of claims paid in a manner consistent with the Government's policy on debt forgiveness	(17,727)	229,095	211,369	(68,543)	1,532,809	1,464,266
Total	**(132,373)**	**536,185**	**403,812**	**(227,153)**	**1,926,102**	**1,698,949**

Note 9.2 analyses capital employed by account. For the most part Costs are allocated to Objectives by Account. Account 2, 3 and 4 support Objective 1 while Account 1 supports Objective 3. Objective 2 is supported by a number of staff within divisions and an appointment of Cost is used for this purpose.

The notes on pages 65 to 94 form part of these accounts.

Notes to Resource Accounts

For the year ended 31 March 2007

1 STATEMENT OF ACCOUNTING POLICIES

The financial statements have been prepared in accordance with the 2006-07 Government Financial Reporting Manual ("FReM") issued by HM Treasury. The accounting policies contained in the FReM follow UK generally accepted accounting practice for companies ("UK GAAP") to the extent it is meaningful and appropriate to the public sector.

In addition to the primary statements prepared under UK GAAP, the FReM also requires ECGD to prepare two additional primary statements. The Statement of Parliamentary Supply and supporting notes show outturn against Estimate in terms of the net cash requirement. The Statement of Operating Costs by Departmental Aim and Objectives and supporting notes analyse ECGD's income and expenditure by the objectives agreed with its Ministers.

Where the FReM permits a choice of accounting policy, the accounting policy which has been judged to be the most appropriate to the particular circumstances of ECGD for the purpose of giving a true and fair view has been selected. ECGD's accounting policies have been applied consistently in dealing with items considered material in relation to the accounts.

ECGD has agreed with HM Treasury that it is necessary to make disclosures in the operating cost statement and balance sheet, which vary from the standard disclosures in the FReM. The disclosures reflect the specialised and long-term nature of insurance activity, and a requirement that ECGD should measure performance over more than one financial year, particularly where deficits are funded by the Exchequer.

The capital charging regime has also been varied to reflect the cost of Exchequer funding in past years. Details of the particular accounting policies adopted by ECGD are described below.

Accounts 1, 2, 3, and 4
In certain of the notes to the Resource Accounts, the financial statements are disaggregated into four Accounts – 1, 2 and 3 cover ECGD's underwriting activities, while Account 4 covers export finance activities.

Account 1 – guarantees issued for project business prior to April 1991, and guarantees issued by the Insurance Services Group of ECGD (the main part of which was privatised on 1 December 1991) for which ECGD retains all contingent liabilities ('Insurance Services Business').

Account 2 – guarantees issued for project business since April 1991, Overseas Investment Insurance guarantees (all years), and Reinsurance (Supplemental Reinsurance and Transitional Reinsurance) since the privatisation of the main part of Insurance Services Group on 1 December 1991.

Account 3 – guarantees issued, on the written instruction of Ministers, for project business since April 1991, which ECGD's Accounting Officer had advised did not meet normal underwriting criteria.

Account 4 – the provision of Fixed Rate Export Finance ("FREF") to foreign importers of UK goods and services, together with arrangements for capital market funding of FREF loans and for certain interest rate swap arrangements.

Nature of ECGD's Underwriting Activity (Accounts 1 – 3)

Due to the nature of ECGD's activities, the outcome is subject to considerable uncertainty primarily as a result of:

- **Unpredictability** – losses arising from political risks are very difficult to assess and calculate with any degree of confidence, particularly over the longer term;
- **The long term nature of the risks underwritten** – the underwriting cycle, up to 30 years if a Paris Club recovery is involved, means that the outcome may not be known with certainty for many years; and
- **The narrow base of risk** – ECGD has a far narrower risk base than would normally obtain in commercial insurance, and its risk base is also subject to an uncertain degree of systemic risks which narrows the base even further. This makes the underwriting outcome extremely volatile.

Many claims and subsequent recoveries take several years to materialise. Although the financial results cannot be established with certainty, ECGD sets provisions for irrecoverable claims based upon current perceptions of risk employing a substantial degree of experience and judgement. The level of such provisions has been set on the basis of information which is currently available. Whilst ECGD considers that claims provisions and related recoveries are fairly stated on the basis of the information currently available to it, the ultimate liability will vary as a result of subsequent information and events. This may result in significant adjustments to the amounts provided. These estimates and methods of estimation are reviewed annually and, if adjustments prove necessary, they will be reflected in future accounts.

Fund Basis of Accounting for Underwriting Activities

The Fund Basis of Accounting has been applied because the nature of the business is such that the Annual Basis (whereby the profit/loss is struck on the first anniversary of establishment of each Annual Fund) would not be appropriate. Insufficient information is available on expected future claims and recoveries for reliable estimates to be made at the end of each financial year.

Under the Fund Basis of accounting, premium, net of provisions for any unrecovered claims and expenses, is carried forward as a fund, and profit recognition is deferred until the end of four years (for business written in respect of cash-based risk where no credit after delivery has been extended to the customer), or ten years (for business written in respect of extended credit risks) from the start of an underwriting year. However, as Account 1 is in run-off and in surplus, this Account is considered as a whole.

Where the fund for any underwriting year is considered insufficient to meet estimated future net claims or losses, a transfer is made from the cumulative surplus/deficit to cover the potential shortfall.

(a) Premium Income

Premium income for the underwriting year is recognised as detailed below:

- **Project Business:** the income on all guarantees becoming effective during the year (including income for which deferred payment terms have been agreed);
- **Overseas Investment Insurance:** the amount due in the financial year in which the annual cover commences; and
- **Reinsurance:** premiums due based on notifications received in the year from export credit insurers.

(b) Interest Receivable – Underwriting Activities

Balances in relation to performing markets, where payments of both principal and interest are being made in line with agreed Paris Club rescheduling, are provided for in line with the market provision rate applied to the principal outstanding (see note 22). Interest accruing on non-performing markets is provided for at 100 per cent.

(c) Claims and Recoveries

- **Claims** are recognised when authorised;
- **Recoveries**, where a realistic prospect of full or partial recovery exists, the estimated recovery proceeds, net of estimated expenses in achieving the recovery, are included as assets in the Balance Sheet, as "Recoverable Claims". When ECGD considers that it is no longer practicable or cost effective to pursue recovery, recoverable claims are formally abandoned and the amounts are deducted from recoverable assets and written off to the surplus/deficit for the year to the extent that existing provisions are not adequate to cover such amounts;
- **Recovered Assets**, beneficial interests in assets including aircraft are obtained in satisfaction of a recoverable claim or as a result of a claim on a guaranteed loan. The interests in these assets have been acquired with a view to achieving an orderly realisation of the recoverable claim and consequently the value of these assets is considered when calculating the provision against recoverable claims in the balance sheet.

(d) Provisions for Losses on Future Claims

In assessing the adequacy of a Fund, account is taken of future investment income and, based on information available at the balance sheet date, provisions are estimated according to the categories of risk, as follows:

- **Political:** risks associated with a country which could potentially affect every insured transaction in that country, e.g. currency transfer difficulties or other events of a political nature such as war, government interference, etc.
- **Buyer:** risks directly associated with transactions, e.g. buyer or borrower insolvency. A discount rate of 3.5 per cent per annum is applied to reflect present values.

(e) Financial Instruments Held at Fair Value

Derivatives held for the purpose of customer facilitation are recorded at trade date and stated at fair value. Fair value is the amount at which an instrument could be exchanged in an arms length transaction between informed and willing parties other than on a forced or liquidation sale. Fair value is calculated using current and observable market information utilising valuation models and techniques that are consistent with those used by the financial services industry (see Note 30). Changes in fair value are recognised in the Operating Statement.

(f) Operating Expenses

All operating expenses are charged in the year they are incurred. Costs are allocated or apportioned on an activity basis. Operating expenses include the cost of early retirement (see Note 14).

(g) Foreign Exchange

Transactions denominated in foreign currencies are translated into Sterling at the rates of exchange ruling at the dates of transactions. Monetary assets and liabilities are translated into Sterling at the rates of exchange ruling at the balance sheet date, and resulting differences are charged or credited to the operating statement.

(h) Capital Charge

A charge reflecting the cost of the capital utilised by ECGD is included in operating costs. The cost is charged or credited on the balance with the Consolidated Fund. A floating interest rate applies to Account 1 – 3 and a range of fixed interest rates is applied to Account 4. The interest rates are agreed with HM Treasury.

(i) Tangible Fixed Assets
Tangible fixed assets consist of leasehold improvements and computer and telecommunication equipment. Depreciation is provided at rates calculated to write off the cost, less estimated residual value, over the estimated useful economic lives, as follows:

Leasehold improvements	Period of lease
Computer and telecommunication equipment	3 – 5 years

(j) Leases
Rentals under operating leases are charged to the resource accounts in equal annual instalments over the period of the lease.

(k) Exchequer Financing
To reflect the long term nature of ECGD's activities, and recognising that operating and investment cashflows in a particular year will not always be sufficient to service operating commitments, a cumulative balance with the Exchequer is maintained and disclosed on the face of the balance sheet. The balance moves from year to year in response to the cashflows and accrued income arising from ECGD's operating and investment activities, and attracts capital charges where voted monies have been used to fund underwriting activities and directly funded export loans.

(l) Cumulative Surplus
ECGD seeks to measure its performance on an ongoing basis for underwriting activities by maintaining a cumulative surplus. This is changed each year by the net operating cost/income for underwriting activities.

(m) Pension costs
Past and present employees are covered by the provisions of the Principal Civil Service Pension Scheme (PCSPS). The defined benefit schemes are unfunded and are non-contributory except in respect of dependants' benefits. ECGD recognises the expected cost of these elements on a systematic and rational basis over the period during which it benefits from employees' services by payment to the PCSPS of amounts calculated on an accruing basis. Liability for payment of future benefits is a charge on the PCSPS. In respect of the defined contribution schemes, ECGD recognises the contributions payable for the year. Early retirement costs are accrued in the year of retirement.

(n) Financial Instruments
(i) Portfolio Management Activities (Credit Default Swaps)
Derivatives have been purchased in order to manage the concentration of risk in certain markets. The cost thereof has been amortised over their respective periods of risk.
(ii) Derivatives held for customer facilitation
Derivatives held for the purpose of customer facilitation are recorded at trade date and stated at fair value. Changes in fair value are recognised in the Operating Statement.

(o) Contingent Liabilities
In addition to contingent liabilities disclosed in accordance with FRS 12, ECGD discloses for Parliamentary reporting and accountability purposes certain statutory and non-statutory contingent liabilities where the likelihood of a transfer of economic benefit is remote, but which have been reported to Parliament in accordance with the requirements of Government Accounting.

Where the time value of money is material, contingent liabilities, which are required to be disclosed under FRS 12, are stated at discounted amounts and the amount reported to Parliament separately noted. Contingent liabilities, that are not required to be disclosed by FRS 12, are stated as the amounts reported to Parliament.

2 Analysis of net resource outturn by section

								2006-07	2005-06
						Outturn	**Estimate**		
	Admin £000	**Other Current £000**	**Grants £000**	**Gross Resource Expenditure £000**	**A. in A. £000**	**Net Total £000**	**Net Total £000**	**Net Total outturn compared with Estimate £000**	**Prior-year outturn £000**
Request for Resources 1: To provide export finance assistance through interest support to benefit the UK economy by facilitating exports									
Central Government spending									
Section A – Fixed Rate Export Finance		20,686		20,686	14,725	5,961	26,348	20,387	19,109
Section B – GEFCO loans and interest equalisation		21,891	60,235	82,126	16,445	65,681	76,459	10,778	53,336
Total	0	42,577	60,235	102,812	31,170	71,642	102,807	31,165	72,445
Request for Resources 2: To provide export credit guarantees to benefit the UK economy by facilitating exports and to provide investment insurance									
Central Government spending									
Section A – Administration		435		435		435	472	37	562
Section B – Administration – running costs		25,672		25,672	5,428	20,244	26,699	6,455	28,470
Section C – Export credits					21,837	(21,837)	(26,165)	(4,328)	(29,379)
Section D – Overseas Investment Insurance					1,231	(1,231)	(1,005)	226	(1,828)
Section E – Active portfolio management		2,389		2,389		2,389	0	(2,389)	2,175
Total		28,496	0	28,496	28,496	0	1	1	0
Resource Outturn	0	71,073	60,235	131,308	59,666	71,642	102,808	31,166	72,445

Brief explanation of variances between estimate and outturn

RfR1
Actual gross expenditure was less than the Estimate as a result of lower capital charges, and lower interest make up costs.

RfR2
Gross expenditure of £28 million was offset by reductions in provisions on unrecovered claims sufficient to reduce the net expenditure under the Request for Resource to zero.

Detailed explanation of the variances is given in the Management Commentary.

3(a) Reconciliation of net resource outturn to net operating income

	Note	2006-07 Income £'000	2005-06 Income £'000
Net Resource Outturn	2	(71,642)	(72,445)
Income from Export Finance Activities Classified as CFER (Accrual CFER)	5	87,062	116,489
Income from Underwriting Activities Classified as Surplus A. in A. (Accrual A. in A.)	5	388,392	1,654,905
Total A. in A.* and CFER		475,454	1,771,394
Net Operating Income (Operating Statement)		403,812	1,698,949

* See Glossary for definitions of A. in A. and CFER

3(b) Outturn against final Administration Budget

ECGD has no administration budget.

4 Reconciliation of resources to cash requirement

	Note	Estimate £'000	Outturn £'000	Net Total Outturn Compared with Estimate Savings/(Excess) £'000
Net Total Resources	**2**	**(102,808)**	**(71,642)**	**31,166**
Capital				
Acquisition of Fixed Assets		(380)	(123)	257
Non-Operating A. in A.				
Repayment of Export Finance Loans		338,282	0	(338,282)
Accruals Adjustments				
Non-cash items		66,700	48,977	(17,723)
Movements in provisions		0	246,089	246,089
Movement in Working Capital Other than Cash		126,495	825,114	698,619
Changes in Creditors Due after more than one year		0	(4,266)	(4,266)
Excess Cash receipts surrenderable to the Consolidated Fund		(428,290)	(1,044,149)	(615,859)
Net Cash Requirement		**(1)**	**0**	**1**

5 Analysis of Income Payable to the Consolidated Fund

In addition to Appropriations in Aid, the following income relates to ECGD and is payable to the Consolidated Fund (cash receipts being shown in italics):

	Note	Income	2006-07 Forecast Receipts	Income	2006-07 Outturn Receipts
		£'000	£'000	£'000	£'000
Operating Income and Receipts – Excess A. in A.		0	*0*	388,392	*400,496*
Other operating income and receipts not classified as A. in A.		83,878	*83,878*	87,062	*102,138*
Subtotal		**83,878**	***83,878***	**475,454**	***502,633***
Non–Operating income and receipts	7	0	*0*	0	*477,343*
Excess Cash receipts surrenderable to the Consolidated Fund		0	*428,290*	0	*1,044,149*
Total		**83,878**	***512,168***	**475,454**	***2,024,126***

6 Reconciliation of income recorded within the Operating Statement to operating income payable to the Consolidated Fund

	Note	2006-07 £'000	2005-06 £'000
Income	10	535,120	1,803,384
Adjustment for transactions between RfRs		0	0
Gross income		**535,120**	**1,803,384**
Income authorised to be Appropriated in Aid		(59,666)	(31,990)
Operating income payable to the Consolidated Fund	5	**475,454**	**1,771,394**

7 Non-operating income – Excess A. in A.

	2006-07 £'000	2005-06 £'000
Principal repayments of voted loans	477,343	397,585
Proceeds on disposal of fixed assets	0	0
Other	0	0
Non-operating income – excess A. in A.	**477,343**	**397,585**

8 Non-operating income not classified as A. in A.

ECGD does not have income of this classification.

9.1 Operating Statement

For the year ended 31 March 2007

2006-07	Account 1	Account 2	Account 3	Account 4	Total
	£'000	£'000	£'000	£'000	£'000
UNDERWRITING					
Gross Premium Income	0	63,229	0	0	63,229
Less ceded to other insurers		(8,377)			(8,377)
Subtotal	0	54,852	0	0	54,852
Amortisation of Instruments held for Portfolio Management	0	(2,389)	0	0	(2,389)
Interest Receivable	136,595	40,777	0	0	177,372
Claims Credit/(Charge) for the Year	68,163	20,980	0	0	89,143
Changes in provisions for losses on future claims	1,085	60,998	18,555	0	80,638
Staff Costs	(1,685)	(9,425)	0	0	(11,110)
Non-staff Administration and Operating costs	(1,039)	(8,444)	(28)	0	(9,511)
Foreign Exchange Gain/(Loss)	(15,002)	(32,515)	0	0	(47,517)
Capital (Charge)/Income	23,252	33,884	4,827	0	61,963
Net Income arising from Trading Operations	**211,369**	**158,718**	**23,354**	**0**	**393,441**
EXPORT FINANCE					
Interest Make-Up Scheme					
Interest Support Costs	0	0	0	718	718
Movement in Fair Value of Derivatives	0	0	0	3,441	3,441
Directly Funded Export Finance Loans					
Interest Income	0	0	0	70,243	70,243
Capital Charge	0	0	0	(60,235)	(60,235)
Provision for Counterparty Risk	0	0	0	1,254	1,254
Staff Costs	0	0	0	(3,157)	(3,157)
Other Administrative and Operating costs	0	0	0	(1,893)	(1,893)
Foreign Exchange Gain	0	0	0	0	0
Net Income on Export Finance	**0**	**0**	**0**	**10,371**	**10,371**
Net Operating Income for the year	**211,369**	**158,718**	**23,354**	**10,371**	**403,812**

Comparatives for the totals are given on the summary Operating Statement.

9.2 Balance Sheet

As at 31 March 2007

2006-07	Account 1	Account 2	Account 3	Account 4	Total
	£'000	£'000	£'000	£'000	£'000
Tangible Fixed Assets	0	1,505	0	0	1,505
Financial Instruments held for Portfolio Management Activities	0	23,266	0	0	23,266
Debtors due after one year	474,026	518,328	0	732,716	1,725,070
	474,026	**543,099**	**0**	**732,716**	**1,749,841**
Debtors due within one year	193,001	153,627	0	291,724	638,352
Cash at Bank and in Hand	1,326,693	139,119	(28)	297,380	1,763,164
Other Financial Assets held at Fair Value				30,653	30,653
Total Current Assets	**1,519,694**	**292,746**	**(28)**	**619,757**	**2,432,169**
Creditors due within one year	(1,363,694)	(154,369)	28	(310,124)	(1,828,159)
Total Net Current Assets	**156,000**	**138,377**	**0**	**309,633**	**604,010**
Total Assets less Current Liabilities	**630,026**	**681,476**	**0**	**1,042,349**	**2,353,851**
Creditors due after one year	(414,038)	(28,419)	0	(0)	(442,457)
Provisions for Losses on Future Claims	(4,839)	(624,368)	(12,802)	0	(642,009)
Other Financial Liabilities held at Fair value				(38,376)	(38,376)
Total Net Assets	**211,149**	**28,689**	**(12,802)**	**1,003,973**	**1,231,009**
TAXPAYERS' EQUITY					
Exchequer Financing	(459,293)	(775,283)	(96,221)	997,861	(332,936)
Cumulative Trading Surplus	670,442	803,972	83,419		1,557,833
General Fund				6,112	6,112
Total	**211,149**	**28,689**	**(12,802)**	**1,003,973**	**1,231,009**

Comparatives for the totals are given on the summary Balance Sheet.

9.3 Cashflow Statement

For the year ended 31 March 2007

2006-07	Account 1	Account 2	Account 3	Account 4	Total
	£'000	£'000	£'000	£'000	£'000
Net Cash Inflow from Operating Activities	1,306,112	168,133	(28)	82,604	1,556,821
Capital Expenditure and Financial Investment	0	(10,038)	0	477,343	467,305
Payment of Outstanding Amounts due to the Consolidated Fund	(2,002,983)	292,918	(22)	(395,694)	(2,105,781)
Amounts due to the Consolidated Fund received in current year and paid over	0	0	0	(260,961)	(260,961)
Increase/(Decrease) in Cash in Period	(696,871)	451,013	(50)	(96,708)	(342,616)

Comparatives for totals are given on the Cashflow Statement.

10 Income

This represents all income generated during the period and includes non-cash items such as changes in provisions.

			2006-07	2005-06
	RfR 1	RfR 2	Total	Total
	£'000	£'000	£'000	£'000
Net Premium Income	0	54,852	54,852	88,207
Interest Receivable	0	177,372	177,372	1,343,263
Claims Credit for the Year	0	41,789	41,789	177,721
Changes in Provisions for Losses on Future Claims	0	80,638	80,638	0
Administration	0	274	274	333
Foreign Exchange Gain	0	0	0	45,380
Interest Support Costs	46,735	0	46,735	35,835
Interest Income – Directly Funded Export Loans	70,243	0	70,243	111,803
Notional Interest	0	61,963	61,963	0
Provision for Counterparty Risk	1,254	0	1,254	841
Total Income in Year	**118,232**	**416,888**	**535,120**	**1,803,384**

11 Premium Income

	Buyer Credit		Overseas Investment Insurance		Supplier Credit Financing Facility		Other		Total	
	2006-07	2005-06	2006-07	2005-06	2006-07	2005-06	2006-07	2005-06	2006-07	2005-06
	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000
Africa	256	12,965	326	304	0	0	3	193	585	13,462
Americas	5,321	9,421	481	533	0	3,015	370	0	6,172	12,969
Asia	16,196	30,344	424	991	0	8,470	29,887	14,380	46,507	54,185
Europe	1,169	6,360	0	0	0	340	422	286	1,591	6,986
Other	(3)	594	0	0	0	3	0	8	(3)	605
Total	**22,939**	**59,684**	**1,231**	**1,828**	**0**	**11,828**	**30,682**	**14,867**	**54,852**	**88,207**

12 Interest Receivable

				2006-07				2005-06
	Account 1	Account 2	Account 3	Total	Account 1	Account 2	Account 3	Total
	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000
Moratorium Interest	132,030	39,598	0	171,628	1,296,704	37,906	0	1,334,610
Other Interest	4,565	1,179	0	5,744	962	7,691	0	8,653
Credited to Trading Account	**136,595**	**40,777**	**0**	**177,372**	**1,297,666**	**45,597**	**0**	**1,343,263**

Other interest includes delay interest (i.e. interest which is payable on late payment of Moratorium Interest) and also arises from late receipt of premium income.

13 Claims Credit/(Charge) for the Year

			2006-07			2005-06
	Account 1	Account 2	Total	Account 1	Account 2	Total
	£'000	£'000	£'000	£'000	£'000	£'000
Claims Authorised in Year	(9)	(60,692)	(60,701)	(4,676)	(78,573)	(83,249)
Anticipated Recoveries on those Claims	0	37,713	37,713	4,676	31,966	36,642
Movement in Provisions on Previous Claims	68,173	43,959	112,132	190,280	34,048	224,328
Credit from/(Charge) to Account	**68,164**	**20,980**	**89,144**	**190,280**	**(12,559)**	**177,721**

14 Staff Numbers and Costs

A. Staff costs consist of:

	2006-07	2005-06
	£'000	£'000
Salaries and Wages	10,130	11,508
Social Security Costs	917	1,052
Early Retirement Costs	4,019	3,060
Other Pension Costs	2,019	2,231
Total	**17,085**	**17,851**
Less Restructuring Cost	2,818	3,262
Staff Cost after Restructuring	**14,267**	**14,589**
Of which:		
Trading Operations (Underwriting)	11,110	12,314
Export Finance	3,157	2,275

The Principal Civil Service Pension Scheme (PCSPS) is an unfunded multi-employer defined benefit scheme but ECGD is unable to identify its share of the underlying assets and liabilities. The scheme's Actuary valued the scheme as at 31 March 2003. Details can be found in the resource accounts of the Cabinet Office: Civil Superannuation (www.civilservice-pensions.gov.uk).

For 2006-07, employers' contributions of £2,006,156 were payable to the PCSPS (2005-06 £2,230,600) at one of four rates in the range of 17.1% to 25.5% of pensionable pay, based on salary bands (the rates in 2005-06 were between 16.2% and 24.6%). The scheme's Actuary reviews employer contributions every four years following a full scheme valuation. From 2007-08, the salary bands will be revised, but the rates will remain the same.

The contribution rates are set to meet the costs of the benefits accruing during 2006-07 to be paid when the member retires, and not the benefits paid during this period to existing pensioners.

Employees can opt to open a partnership pension account, a stakeholder pension with an employer contribution. Employers' contributions of £1,006 were paid to one or more of a panel of three appointed stakeholder pension providers. Employer contributions are age-related and range from 3 to 12.5 per cent of pensionable pay. Employers also match employee contributions up to 3 per cent of pensionable pay, this includes employer contributions of 0.8 per cent of pensionable pay, which were payable to the PCSPS to cover the cost of the future provision of lump sum benefits on death in service and ill health retirement of these employees.

Contributions due to the partnership pension providers at the balance sheet date were £95. Contributions prepaid at that date were £Nil.

B. The average number of full-time equivalent persons employed (including senior management) and full time equivalent of temporary workers during the year was as follows:

	2006-07		2005-06	
	Employed	Temporary	Employed	Temporary
Objective				
1 To provide UK exporters with guarantees and insurance to help win business: in accordance with its Business Principles, in accord with Government objectives, complementary to the private sector, and employing good management practice	207	10	245	15
2 To secure an efficient market by ensuring as much as practicable a "level playing field" internationally in relation to government-supported Export Credit Agencies	9	1	10	1
3 To recover as much as possible of the debt in respect of claims paid in a manner consistent with the Government's policy on debt forgiveness	29	1	49	2
Total	**245**	**12**	**304**	**18**

Salary

'Salary' includes gross salary; performance pay or bonuses; overtime; reserved rights to London weighting or London allowances; recruitment and retention allowances; private office allowances and any other allowance to the extent that it is subject to UK taxation.

Pension

Pension benefits are provided through the Civil Service pension arrangements. From 1 October 2002, civil servants may be in one of three statutory based "final salary" defined benefit schemes (classic, premium, and classic plus). New entrants after 1 October 2002 may choose between membership of premium or joining a good quality "money purchase" stakeholder based arrangement with a significant employer contribution (partnership pension account).

(a) Classic Scheme

Benefits accrue at the rate of 1/80th of pensionable salary for each year of service. In addition, a lump sum equivalent to three years' pension is payable on retirement. Members pay contributions of 1.5 per cent of pensionable earnings. On death, pensions are payable to the surviving spouse at a rate of half the member's pension. On death in service, the scheme pays a lump sum benefit of twice pensionable pay and also provides a service enhancement on computing the spouse's pension. The enhancement depends on length of service and cannot exceed 10 years. Medical retirement is possible in the event of serious ill health. In this case, pensions are brought into payment immediately without actuarial reduction and with service enhanced as for widow(er) pensions.

(b) Premium Scheme

Benefits accrue at the rate of 1/60th of final pensionable earnings for each year of service. Unlike the Classic Scheme, there is no automatic lump sum, but members may commute some of their pension to provide a lump sum up to a maximum of 3/80ths of final pensionable earnings for each year of service or 2.25 times pension if greater (the commutation rate is £12 of lump sum for each £1 of pension given up). For the purposes of pension disclosure, the tables assume maximum commutation. Members pay contributions of 3.5 per cent of pensionable earnings. On death, pensions are payable to the surviving spouse or eligible partner at a rate of 3/8ths the member's pension (before any commutation). On death in service, the scheme pays a lump-sum benefit of three times pensionable earnings and also provides a service enhancement on computing the spouse's pension. The enhancement depends on length of service and cannot exceed 10 years. Medical retirement is possible in the event of serious ill health. In this case, pensions are brought into payment immediately without actuarial reduction. Where the member's ill health is such that it permanently prevents them undertaking any gainful employment, service is enhanced to what they would have accrued at age 60.

(c) Classic Plus Scheme

This is essentially a variation of the Premium Scheme, but with benefits in respect of service before 1 October 2002 calculated broadly as per the Classic Scheme.

Pensions payable under the Classic, Premium, and Classic Plus Schemes are increased in line with the Retail Prices Index.

(d) Partnership Pension Account

This is a stakeholder-type arrangement where the employer pays a basic contribution of between 3 per cent and 12.5 per cent (depending on the age of the member) into a stakeholder pension product. The employee does not have to contribute but where they do make contributions, these will be matched by the employer up to a limit of 3 per cent (in addition to the employer's basic contribution). Employers also contribute a further 0.8 per cent of pensionable salary to cover the cost of risk benefit cover (death in service and ill health retirement). The member may retire at any time between the ages of 50 and 75 and use the accumulated fund to purchase a pension. The member may choose to take up 25 per cent of the fund as a lump sum. As at 31 March 2007, five employees had joined this scheme

15 Other Administrative and Operating Costs

	2006-07	2005-06
	£'000	£'000
IT	4,811	5,104
Indirect Staff and Personnel Expenses	761	1,044
Business Promotion	28	54
Rent	2,184	3,266
Other Establishment Costs	977	1,112
Underwriting Expenses	229	203
Claims and Recovery Expenses	(412)	310
Non-Refundable Premium Administration Income	(247)	(182)
Other Administration Costs	737	796
Depreciation Charges	369	472
Travel, Subsistence and Hospitality	444	494
Restructuring Cost (net of DTI contribution £10 million accounted for in 2005-06)	1,523	1,208
Expenditure	**11,404**	**13,881**
Of which:		
Trading Operations	9,511	11,716
Export Finance	1,893	2,165

Auditor's remuneration included in the above figures:

	2006-07	2005-06
	£'000	£'000
Audit Fees	200	185

16 Foreign Exchange Gain/(Loss)

					2006-07					2005-06
	Account 1	Account 2	Account 3	Account 4	Total	Account 1	Account 2	Account 3	Account 4	Total
	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000
Exchange gain/(loss) on recoverable claims and interest before provisions	(138,799)	(44,484)	0	0	(183,283)	120,088	27,384	0	0	147,472
Exchange gain/(loss) on provisions against recoverable claims and interest	110,868	11,128	0	0	121,996	(90,860)	(6,783)	0	0	(97,643)
Exchange gain/(loss) on premium debtors	0	(235)	0	0	(235)	0	2,927	0	0	2,927
Exchange gain/(loss) on other working capital	0	1,606	0	0	1,606	254	(1,607)	0	0	(1,353)
Realised gain/(loss)	12,929	(530)	0	0	12,399	2	3	(22)	(2,014)	(2,031)
Exchange (loss)/gain for year	**(15,002)**	**(32,515)**	**0**	**0**	**(47,517)**	**29,484**	**21,924**	**(22)**	**(2,014)**	**49,372**

17 Guaranteed Export Finance Corporation PLC

Guaranteed Export Finance Corporation PLC (GEFCO), Registered No 1980873, is not legally owned by ECGD and is excluded from the consolidation boundary as defined in the FReM. In order to provide a fuller picture of GEFCO operations in relation to ECGD, extracts from GEFCO's Annual Financial Statements for the year ended 31 March 2007 are shown below. For any further information, please refer to the full audited accounts of GEFCO which can be obtained from Companies House. GEFCO prepares its financial statements in accordance with IFRS.

	2006-07	2005-06
	£'000	£'000
Extracts from the profit and loss account		
Interest receivable and similar income		
Transacted with ECGD	1,112	5,430
Transacted with third parties	172,815	230,137
	173,927	235,567
Interest payable and similar charges		
Transacted with ECGD	(80,686)	(109,519)
Transacted with third parties	(93,235)	(126,042)
	(173,921)	(235,561)
Net Interest Income	**6**	**6**
Net Trading Income (Fair value movements)	**(4,423)**	**4,279**
Other Operating Income		
Transacted with ECGD	5,791	(2,787)
Transacted with third parties	639	(476)
	6,430	(3,263)
Other Operating Charges transacted with third parties	**695**	**422**
Net operating income	**1,312**	**1,444**
Transacted with third parties	(2,007)	(1,438)
Profit before taxation and retained profit for the year	**6**	**6**

17 Guaranteed Export Finance Corporation PLC – continued

	2006-07	2005-06
	£'000	£'000
Extracts from the balance sheet		
Assets		
Long term advances (Note i)	927,038	1,487,271
Derivative financial instruments	752,450	1,241,253
Trade and other receivables	289,983	242,111
Other debtors	65	2,535
	1,969,536	2,973,170
Liabilities		
Term lending from ECGD	1,032,289	1,562,593
Debt securities in issue (Note ii)	383,504	404,953
Derivative financial instruments	542,260	987,274
Overdraft	55	20
Other creditors	11,289	18,142
	1,969,397	2,973,037
Capital and reserves	**139**	**133**
	1,969,536	**2,973,170**

i) The counterparties of the long term advances are UK banks who have financed overseas customers of UK exporters. In all cases, the credit risk in relation to the overseas customer is borne by ECGD under guarantees issued by its underwriting business. The maturity profile of the long-term advances is as follows:

	2006-07	2005-06
	£'000	£'000
Amounts falling due within one year	254,162	31,612
Amounts falling due between one and two years	195,738	107,234
Amounts falling due between two and five years	291,520	661,470
Amounts falling due after more than five years	185,618	686,955
	927,038	**1,487,271**

ii) Loan stock and bonds comprise £250 million 9.75% Guaranteed Loan Stock redeemable at par in 2010, and £100 million 9.25% Guaranteed Bonds redeemable at par in 2008. ECGD is the guarantor of both issues.

18 Movements in Working Capital Other Than Cash

	2006–07	2005–06
	£'000	£'000
The movements in working capital used in the reconciliation of resources to cash requirement comprise:		
Decrease in Claims	811,418	637,174
Increase/(Decrease) in Debtors	6,195	(5,379)
Increase in Creditors falling due within one year	7,501	34,189
Net Decrease in Working Capital Other Than Cash	**825,114**	**665,984**
The movements in working capital other than cash used in the cashflow statement comprise:		
Decrease in Claims	811,418	637,174
Increase/(Decrease) in Debtors	33,374	9,405
Increase/(Decrease) in Creditors falling due within one year	7,501	34,189
Net Decrease in Working Capital Other Than Cash	**852,293**	**680,768**

19 Tangible Fixed Assets

	IT Equipment	Leasehold Improvements	Total
	£'000	£'000	£'000
Cost			
Balance at 1 April 2006	**3,717**	**4,535**	**8,252**
Disposals	0	(1,500)	(1,500)
Additions	20	103	123
Balance at 31 March 2007	**3,737**	**3,138**	**6,875**
Accumulated Depreciation			
Balance at 1 April 2006	**3,235**	**2,766**	**6,001**
On Disposals	0	(1,000)	(1,000)
Charge for the Year	183	186	369
Balance at 31 March 2007	**3,418**	**1,952**	**5,370**
Net book value			
At 31 March 2007	**319**	**1,186**	**1,505**
At 31 March 2006	**482**	**1,769**	**2,251**

20 Debtors

	Note	31 March 2007 £'000	31 March 2006 £'000
(i) Amounts falling due after one year:			
Premium Debtors	21	9,942	15,703
Recoverable Claims – Rescheduled	22	982,412	1,256,228
Export Finance Loans		732,716	1,108,911
Total		**1,725,070**	**2,380,842**
(ii) Amounts falling due within one year:			
Premium Debtors	21	15,885	23,423
Recoverable Claims	22	144,883	653,247
Recoverable Interest	23	183,575	600,825
Export Finance Loans		265,144	366,292
Other Debtors – Policyholders		190	239
Other Debtors – Export Finance		27,401	45,829
Prepayments and Accrued Income		1,274	3,109
Total		**638,352**	**1,692,964**

Included within debtors is £41.5 million (2005-06 £68.7 million) that will be due to the Consolidated Fund once the debts have been collected.

Included within Other Debtors – Export Finance are balances with other central Government bodies at 31 March 2007 of £7.8 million.

21 Analysis of Premium Debtors

The movement on balances of premium due was:

	Account 1 £'000	Account 2 £'000	Account 3 £'000	Total £'000
Premium Debtors at 1 April 2006	0	39,126	0	39,126
Premiums arising on Guarantees Issued	0	54,852	0	54,852
Cash Received In Year	0	(68,681)	0	(68,681)
Foreign Exchange Loss	0	530	0	530
Premium Debtors at 31 March 2007	**0**	**25,827**	**0**	**25,827**
Due				
Within one year	0	15,885	0	15,885
After one year	0	9,942	0	9,942

Premium debtors represent premiums on certain major overseas contracts with long contract completion periods where ECGD accepts payment on deferred terms, and premium receivable in respect of guarantees not yet effective at the balance sheet date.

22 Recoverable Claims

			Account 1			Account 2	
	Political	Buyer	Total	Political	Buyer	Total	Total
	£'000	£'000	£'000	£'000	£'000	£'000	£'000
Unrecovered Claims – Gross							
Balance as at 1 April 2006	3,558,986	15,174	3,574,160	811,049	151,162	962,211	4,536,371
Reclassifications	0	0	0	0	0	0	0
Claims in the Year	9	0	9	11,371	49,321	60,692	60,701
Recoveries in the Year	(734,955)	(151)	(735,106)	(68,442)	(68,570)	(137,012)	(872,118)
Recoveries Abandoned in the Year	(1,325,363)	0	(1,325,363)	0	0	0	(1,325,363)
Foreign Exchange (Loss)/Gain	(69,581)	(3)	(69,584)	(26,692)	(15,920)	(42,612)	(112,196)
Balance as at 31 March 2007	**1,429,096**	**15,020**	**1,444,116**	**727,286**	**115,993**	**843,279**	**2,287,395**
Provisions							
Balance as at 1 April 2006	2,327,508	13,239	2,340,747	231,056	55,093	286,149	2,626,896
Reclassifications	0	0	0	0	0	0	0
Additional Provisions during the Year	(65,990)	(2,173)	(68,163)	(16,626)	(4,354)	(20,980)	(89,143)
Provision on Recoveries Abandoned	(1,325,363)	0	(1,325,363)	0	0	0	(1,325,363)
Foreign Exchange Gain (Note 16)	(43,032)	(0)	(43,032)	(5,158)	(4,099)	(9,257)	(52,289)
Balance as at 31 March 2007	**893,123**	**11,066**	**904,189**	**209,272**	**46,640**	**255,912**	**1,160,101**
Net Unrecovered Claims as at 31 March 2007	**535,973**	**3,954**	**539,927**	**518,014**	**69,354**	**587,367**	**1,127,294**
Net Unrecovered Claims as at 31 March 2006	1,231,478	1,935	1,233,413	579,993	96,069	676,062	1,909,475
Provision as a % of Unrecovered Claims as at 31 March 2007	**62.5%**	**73.7%**	**62.6%**	**28.8%**	**40.2%**	**30.3%**	**50.7%**
Provision as a % of Unrecovered Claims as at 31 March 2006	65.4%	87.2%	65.5%	28.5%	36.4%	29.7%	57.9%

There are no recoverable claims on Accounts 3 and 4.

As at 31 March 2007, the total of unrecovered political claims was £2,156,382,000 (2005-06 £4,370,035,000).

23 Interest on Unrecovered Claims

	Account 1	Account 2	Total
	£'000	**£'000**	**£'000**
Unrecovered Interest			
Balance at 1 April 2006	3,335,974	44,225	3,380,199
Interest Charged in the year	441,690	45,773	487,463
Interest Received in the Year	(573,046)	(20,198)	(593,244)
Recoveries Abandoned in the Year	(1,709,123)	0	(1,709,123)
Foreign Exchange Adjustment	(69,215)	(1,873)	(71,088)
Balance at 31 March 2007	**1,426,280**	**67,927**	**1,494,207**
Provisions			
Balance at 1 April 2006	2,771,144	8,229	2,779,373
Release of Provisions During the Year	305,096	4,995	310,091
Recoveries Abandoned in the Year	(1,709,123)	0	(1,709,123)
Foreign Exchange Adjustment	(67,836)	(1,873)	(69,709)
Balance at 31 March 2007	**1,299,281**	**11,351**	**1,310,632**
Net Unrecovered Interest as at 31 March 2007	**126,999**	**56,576**	**183,575**
Net Unrecovered Interest as at 31 March 2006	564,830	35,996	600,826
Provision as a % of Unrecovered Interest at 31 March 2007	**91.1%**	**16.7%**	**87.7%**

24 Cash at Bank and In Hand

	£'000
Balance at 1 April 2006	**2,105,780**
Net Cash Inflow to ECGD	2,024,126
Paid to the Consolidated Fund	(2,366,742)
Balance at 31 March 2007	**1,763,164**
The following balances at 31 March 2007 are held at:	
The Office of Paymaster General	1,749,228
Commercial Banks and Cash in Hand	13,936
Balance at 31 March 2007	**1,763,164**

25 Creditors

(i) Amounts falling due after one year

	31 March 2007	31 March 2006
	£'000	£'000
Policyholders	6,358	7,947
Payable to the Consolidated Fund	414,038	773,131
Other Creditors	22,061	16,206
Total	**442,457**	**797,284**

(ii) Amounts falling due within one year

	31 March 2007	31 March 2006
	£'000	£'000
Policyholders	1,156	14,852
Balance payable to the Consolidated Fund (CFER)	1,763,164	2,105,781
Export Finance	5,707	6,077
Accruals and Deferred Income	12,333	11,365
Other Creditors	45,800	33,732
Total	**1,828,160**	**2,171,807**

26 Provisions

		2006–07		2005–06
	£'000	£'000	£'000	£'000
Balance at 1 April 2006		**722,646**		762,623
Release of Provision				
Account 1	(1,085)		(15,379)	
Account 2	(109,593)		(69,457)	
Account 3	(20,258)	(130,936)	(51,827)	(136,663)
Increase in Provision				
Account 1	0		0	
Account 2	48,596		95,121	
Account 3	1,703	50,299	1,565	96,686
Balance at 31 March 2007		**642,009**		**722,646**

Each Underwriting Fund is set at the higher of (i) the current expected loss on amounts at risk on unexpired guarantees, or (ii) accumulated premiums plus interest earned, less both administration costs and provisions made for the unrecoverable proportion of paid claims. In the case of the latter, the premium income credited to a Provision is net of any reinsurance premium ceded to re-insurers where ECGD, as lead insurer, has reinsured a proportion of the total contract risk.

As at 31 March 2007, the gross expected loss value in respect of Account 2 was £202.5 million.

(ii) Counterparty Risk

A provision of £2.4 million has been made on the Account 4 Export Finance business to reflect the £1.6 billion amounts at risk with banking counterparties. This provision has been included in other creditors.

27 Taxpayers' Equity

				2006-07	2005-06
	(i) Movement on Exchequer Financing £'000	(ii) Movement in Cumulative Trading Surplus £'000	(iii) Movement on General Fund (Export Finance) £'000	Total £'000	Total £'000
Balance at 1 April 2006	**(871,182)**	**3,348,636**	**16,504**	**2,493,958**	**3,319,689**
Transfers					
Adjustment for Debt Forgiveness & Abandonments (see note 28)	2,184,244	(2,184,244)		**0**	**0**
Funding non-breakeven Activities	80,998		(80,998)	**0**	**0**
Other movements					
CFER arising in year transferred to current liabilities	(2,024,126)			**(2,024,126)**	**(2,211,527)**
Long term Consolidated Fund Creditor	359,093			**359,093**	**(415,312)**
Non Cash adjustments					
Capital Charge/(Income)	(61,963)		60,235	**(1,728)**	**102,161**
Transfer from Operating Statement					
Surplus for year		393,441	10,371	**403,812**	**1,698,949**
Balance at 31 March 2007	**(332,936)**	**1,557,833**	**6,112**	**1,231,009**	**2,493,960**

28 Movement in Exchequer Financing

The resources consumed by ECGD in respect of its export finance activities and trading operations are supplied annually by Parliament through the "Supply procedure" of the House of Commons. The Estimate voted on in the "Supply procedure" also sets an annual ceiling on ECGD's voted net cash requirement. By the provisions of Section 14(2) of the Export and Investment Guarantees Act, 1991 (the "Act"), ECGD is able to pay claims direct from the Consolidated Fund in the event that sufficient funds have not been voted for the purpose by Parliament.

The Exchequer balances also include notional amounts for interest in respect of the year of £66,983,000 (2005-06 £12,990,000). The average floating interest rate for the year as agreed with HM Treasury was 5.1537 per cent as compared with 4.88 per cent in 2005-06. The average annual fixed rate on export finance was 4.85 per cent.

In prior years a portion of the Exchequer Financing in respect of Account 1 was written off each year. This write off was calculated by reference to the amounts forgiven, including Moratorium Interest, or amounts abandoned from Unrecovered Claims and Interest. It has been agreed with HM Treasury that the process should be reversed this year together with any Notional Interest applicable to balances written off from Account 2. As a result, the sum of £2,184,244,000 has been added back to Exchequer Financing and Cumulative Trading Surplus (Note 27(i) and (ii)).

During 2006-07 a bilateral agreement was signed with Grenada while final debt treatments for Cameroon, Malawi and Sierra Leone were processed under the Heavily Indebted Poor Countries Initiative. Nigeria paid £661 million being the final payment of a prepayment agreement signed in October 2005. Prepayment agreements were signed with and payments were from Algeria (£110 million), Macedonia (£1.5 million) and Russia (£382 million). These payments cleared all outstanding debt with the countries. During the year Claims balances for Iraq were written down by £28 million – the claim was previously at 95%.

29 Notes to the Cashflow Statement

29(a) Reconciliation of Operating Income to Operating Cashflow

	2006-07 £'000	2005-06 £'000
Net Operating Income	403,812	1,698,949
Adjust for Non-Cash Transactions:		
Capital Charges	(1,728)	102,161
Depreciation	369	472
Claims Credit for Year	(89,144)	(177,721)
Interest Credit for Year	415,871	(385,452)
Changes in Provisions for Future Claims	(80,638)	(39,977)
Unrealised Foreign Exchange Gain/(Loss)	59,915	(51,402)
Amortisation of Financial Instruments held for Portfolio Management	2,389	2,175
Other Non-Cash Items:		
Movements in Working Capital Other than Cash	852,793	680,768
Changes in Creditors due after more than one year	(4,266)	2,455
Financial Instruments – Change in Fair Value	(2,552)	(16,895)
Net Cash Inflow from Operating Activities	**1,556,821**	**1,815,533**

29(b) Analysis of Capital Expenditure and Financial Investment (RfR 2)

	2006-07	2005-06
	£'000	£'000
Purchase of Fixed Assets	(123)	(110)
Purchase of Financial Instruments	(9,915)	(1,479)
Advance of Export Finance Loans	0	0
Repayment of Export Finance Loans	477,343	397,585
Net Cash Inflow from Investing Activities	**467,305**	**395,996**

29(c) Analysis of Financing

From Consolidated Fund – current year	0	0
From Consolidated Fund – prior year	0	0
Exchequer Financing – prior periods undrawn grant adjustment	0	0
Net Financing	**0**	**0**

29(d) Reconciliation of Net Cash Requirement to increase in cash

Net Cash Requirement	0	0
From Consolidated Fund - current year	0	0
Prior Periods Undrawn Grant Adjustment	0	0
From Consolidated fund - prior year	0	0
Amounts due to Consolidated Fund received in prior year and paid over	(2,105,780)	(1,745,590)
Amounts due to the Consolidated Fund received and not paid over		
Excess A. in A. and CFERs	1,285,821	1,708,195
Excess Non-Operating A. in A.	477,343	397,585
Increase/(Decrease) in Cash	**(342,616)**	**360,190**

30 Financial Assets and Liabilities

These disclosures do not cover provisions for losses on future claims. Short term debtors and creditors are excluded from the disclosures except for recoverable claims due in less than one year, which are included in order to reflect fully the currency risk to ECGD, as they are the only material balances denominated in foreign currency.

Financial Liabilities and Available Facilities

ECGD is funded by supply approved by Parliament – see Note 28. In transacting its normal business, ECGD is exposed to the following risks: credit risk, interest rate risk, foreign currency risk and liquidity risk.

Guaranteed Export Finance Corporation PLC (GEFCO)

ECGD uses Guaranteed Export Finance Corporation PLC (GEFCO) for its refinancing programme. This refinancing programme uses public funds and thereby makes greater savings than would be achieved by GEFCO borrowing in the commercial market (see Note 17).

Interest Make-up Scheme

In support of its main trading activities, ECGD provides an interest rate support programme. This enables banks to offer overseas buyers fixed rate loans at rates in accordance with The Arrangement, while the banks receive a floating rate based on their cost of funds plus an agreed margin. This is a form of interest rate swap in that, if the rate payable to the bank is higher than the fixed rate, ECGD pays the difference to the banks; if the rate is lower, ECGD receives the difference.

Credit Risk

Credit risk arises where the possibility exists of a counter-party defaulting on its obligations. This risk is recognised by the creation of a provision for losses on future claims as described in Note 26 to the accounts.

Interest Rate Risk

Since transactions under the interest make-up scheme create a risk arising from taking on the fixed rate, a part of the FREF portfolio is hedged by entering into interest rate swaps which provide ECGD with floating rate exposure in exchange for a fixed rate. FREF firm business is hedged using the sensitivity method in line with standard market practice. In total, 29 interest rate swaps were transacted following a competitive bidding process and involving counter-parties with a minimum AA – long term credit rating at the time. The total nominal values in each currency were US$38 million (six swaps), £14.8 million (nine swaps), ¥9,330 million (ten swaps) and €6.5million (four swaps). The exposures created by Interest Make-up ("IMU") swaps are generated with reference to the original underlying loan agreement, while the hedge swap exposures are generated with reference to the terms agreed between ECGD and the market at inception.

Foreign Currency Risk

All operations are UK-based and ECGD's functional currency is Sterling. Funding for claims denominated in foreign currencies is provided by the Exchequer in Sterling. ECGD is not permitted by HM Treasury to hedge foreign currency exposure.

Liquidity Risk

As a Government Department, ECGD does not face liquidity risk, since funds are drawn from the Exchequer as required. All cash balances are in Sterling and deposited at either the Bank of England or with the Paymaster General and earn variable rates of interest.

Financial Instruments on Account 4

Fair Values

Fair values are based on quoted market prices where available or determined using appropriate models based on market price information. The fair values of the IMU swaps are based on the full potential liability of ECGD and therefore are based on the loan profile of the underlying loan agreement and not necessarily the actual loan drawn to date, as the actual drawdown is not deemed to reflect properly uncertainties in the future cashflow and therefore the fair value of the swap. The fair values shown do not include IMU swaps where a commitment to provide interest rate support exists, but the drawdown has not been agreed due to the uncertainties in future commitments.

Interest Rate Risk – Account 4

2006-07	Fixed Rate £'000	Interest Free £'000	Total £'000	Weighted Average Fixed Interest Rate %	Weighted Average Period to Maturity (Years)
Financial Assets					
GEFCO Loans	997,860		997,860	6.40	2.9
Cash		297,380	297,380		
Other Debtors		57,233	57,233		
Total Financial Assets	**997,860**	**354,613**	**1,352,473**		
Financial Liabilities					
Treasury Creditor		297,380	297,380		
Other Creditors		51,120	51,120		
Consolidated Fund	997,860		997,860	4.85	2.9
Total Financial Liabilities	**997,860**	**348,500**	**1,346,360**		

The Government Financing balance of £997,860 has no set date for repayment, but is assumed to match GEFCO loans and bears interest on a fixed rate based on the National Loan Fund Rate.

Currency Risk – Account 4

The functional currency of all Account 4 operations is Sterling.

Net Foreign Currency Monetary Assets/(Liabilities) – Account 4	**£'000**	**£'000**	**£'000**	**£'000**
at 31 March 2007	**Sterling**	**US Dollar**	**Japanese Yen**	**Euro**
Functional Currency: Sterling	5,059	3,784	(1,778)	3,936

Liquidity Disclosures – Account 4	**Assets**	**Liabilities**
	at 31 March 2007	**at 31 March 2007**
	£'000	**£'000**
Less than 1 year	619,796	1,346,360
Over 1 year and under 2 years	222,774	
Over 2 years and under 5 years	330,537	
Over 5 years	179,366	
	1,352,473	**1,346,360**

Fair Values	**Fair value 31 March 2007**	**Fair value 31 March 2006**
	£'000	**£'000**
Primary Financial Instruments – Account 4		
GEFCO Loans	1,032,289	1,504,014
Cash	297,380	395,694
Other financial assets & liabilities	13,836	28,387
Derivative Financial Instruments – Account 4		
Assets	30,653	53,666
Liabilities	(38,376)	(65,548)
	1,335,781	**1,916,211**

Claims

Claims of £1,127,294,000 (2005-06 £1,909,475,000) are shown at fair value in the balance sheet and in Note 22. The following table provides a broad guide to the timescale during which ECGD is due to receive the proceeds:

	31 March 2007	**31 March 2006**
	£'000	**£'000**
Over five years	669,276	813,757
Two – five years	222,934	348,932
One – two years	90,202	93,536
Less than one year	79,099	586,993
In arrears	65,783	66,255
	1,127,294	**1,909,473**

The following table provides an analysis of the currency breakdown:

	31 March 2007	31 March 2006
	£'000	£'000
UK Sterling	780,804	1,343,752
US Dollars	341,722	556,558
Euro	4,768	9,163
Other	0	0
	1,127,294	**1,909,473**

The majority of the agreements have floating rates which vary according to a margin based on the London InterBank Offer Rate ("LIBOR").

31 Related Party Transactions

ECGD is a Department of the Secretary of State for Business, Enterprise and Regulatory Reform and as such it has a number of transactions with other Government Departments and other central government bodies. None of the Management Board members has undertaken any material transactions with ECGD during the year. Transactions between ECGD and GEFCO (see note 17) in 2006-07 were net recoveries of Export Finance Loans £477,343,000 (2005-06 £397,585,000) and Other Transactions £86,066,000 (2005-06 £111,803,000). In addition, GEFCO's long-term advances, guaranteed loan stock, guaranteed bonds, currency swaps and the short-term borrowings of the company are guaranteed unconditionally and irrecoverable by the Secretary of State for Business, Enterprise and Regulatory Reform of Her Britannic Majesty's Government acting by ECGD.

32 Contingent Liabilities

(i) Amounts at Risk and other contingent liabilities

	Account 1	Account 2	Account 3	Account 4	Total
	£'000	£'000	£'000	£'000	£'000
As at 1 April 2006	**146,469**	**11,056,236**	**79,387**	**0**	**11,282,092**
Guarantees and Insurance Policies Issued and Renewed	0	1,798,218	0	0	1,798,218
Run Off	(34,539)	(2,269,713)	(23,480)	0	(2,327,732)
Foreign Exchange Adjustments	(1,596)	(795,039)	(2,467)	0	(799,102)
As at 31 March 2007	**110,334**	**9,789,702**	**53,440**	**0**	**9,953,476**

Amounts at Risk in respect of guaranteed bank loans (Account 1 only) are not shown separately as they are included in the above figures for the underlying credit insurance guarantees. In the event of a default on a guaranteed bank loan, ECGD would normally offset against any basic credit insurance claim for which it is liable or seek direct recourse from the exporter or guarantor. The Amounts at Risk in respect of Performance Bonds are reflected in the risks shown above under the basic guarantees. The amounts at risk in respect of Overseas Investment Insurance agreements comprise the current value of insured investments.

(ii) Statutory Limits

The Export and Investment Guarantees Act 1991 sets limits on the maximum liabilities that ECGD may incur in both sterling and foreign currency. The latter is expressed in Special Drawing Rights (SDR). The following table shows the Statutory Limits at 31 March 2007 and the cumulative outstanding commitments set against them:

	31 March 2007				31 March 2006			
	Sterling	Foreign Currency	Sterling Equivalent	Sterling Total	Sterling	Foreign Currency	Sterling Equivalent	Sterling Total
	£'000	SDR'000	£'000	£'000	£'000	SDR'000	£'000	£'000
Section 6(1) amounts								
Statutory Limit	35,000,000	30,000,000	23,137,440	58,137,440	35,000,000	30,000,000	24,915,300	59,915,300
Commitments	3,266,423	10,458,631	8,066,198	11,332,621	4,026,206	10,908,629	9,059,726	13,085,932
Section 6(3) amounts								
Statutory Limit	15,000,000	10,000,000	7,712,480	22,712,480	15,000,000	10,000,000	8,305,100	23,305,100
Commitments	125,883	706,118	544,592	670,475	135,133	1,195,446	992,830	1,127,962
Totals								
Statutory Limit	**50,000,000**	**40,000,000**	**30,849,920**	**80,849,920**	**50,000,000**	**40,000,000**	**33,220,400**	**83,220,400**
Commitments	**3,392,305**	**11,164,749**	**8,610,790**	**12,003,096**	**4,161,339**	**12,104,075**	**10,052,556**	**14,213,894**

At 31 March 2007, 1 SDR = £0.77125

At 31 March 2006, 1 SDR = £0.83051

Section 6(1) of the Act sets limits on the amounts relating to exports and insurance. Section 6(3) of the Act relates to arrangements in the interests of the proper financial management of the ECGD portfolio.

The commitment figures shown above are greater than the Amounts at Risk due to the inclusion of:

- Non-trading activities;
- Commitments contingent upon the full utilisation of credit insurance facilities made available to exporters; and
- Guarantees issued but not yet effective.

34 Leasehold Obligations

Annual commitments of ECGD in 2006-07 under non-cancellable operating leases are:

	31 March 2007	31 March 2006
	Land and Buildings	Land and Buildings
	£'000	£'000
Leases which expire after five years	2,677	2,677

35 Losses

	31 March 2007	31 March 2006
	£'000	£'000
Total value	581	nil

During the year, ECGD identified and corrected an administrative error, in the previous year, which resulted in an additional interest rate hedging cost of £581,000. Corrective action has been taken to ensure similar errors will not occur in the future.

2007 Departmental Expenditure Report

Departmental Expenditure Report

A Departmental Expenditure Report (DER) is the primary document through which a department sets out its accountability to Parliament and the public. This DER is presented alongside ECGD's Annual Review and Resource Accounts 2006-07 to provide a comprehensive review of ECGD's performance and expenditure during the financial year.

1 ECGD'S AIM AND OBJECTIVES

The aim of ECGD is "to benefit the UK economy by helping exporters of UK goods and services win business, and UK firms to invest overseas, by providing guarantees, insurance and reinsurance against loss, taking into account the Government's international policies".

ECGD's full Mission Statement can be found on page 10. This sets out the Department's aim and high-level objectives.

2 2006–07 SERVICE DELIVERY AGREEMENT (SDA) TARGETS – RESULTS

Key Target 1

To achieve the Financial Objectives set by Ministers.

Measures of Delivery

(i) For its business relating to the provision of guarantees and insurance since April 1991 ("Account 2 business"), ECGD is required to maintain a Reserves Index of at least 1. The Reserves Index compares the cumulative adjusted[1] reserves and claims provisions to those estimated as required to ensure, with a 77.5% confidence, that the value of cumulative reserves, when added to the value of claims provisions, will be sufficient to cover eventual losses on contingent liabilities and claims paid.

$$\text{Reserves Index} = \frac{\text{Claims Provisions} + \text{Adjusted}^{1}\ \text{Cumulative Account 2 Reserves}}{\text{Claims Provisions} + \text{Required Account 2 Reserves}}$$

Result: As at 31 March 2007, the Reserves Index was 2.72, above the required target.

(ii) For Account 2 business over the period 2005–2007, ECGD is required to maintain a Two-Year Reserve Coverage Ratio (Two-Year RCR) of at least 1.4. The Two-Year RCR is defined as the ratio of Account 2 premium earned (net of Account 2 administration costs) to expected losses on amounts at risk in respect of guarantees and insurance issued in the two financial years.

Result: As at 31 March 2007, the Two-Year RCR was 1.80, above the required target.

(iii) For Fixed Rate Export Finance (FREF) support, ECGD must maintain a Mark-to-Market (MTM) value on its Old FREF[2] portfolio at a value no lower than minus £204 million. The MTM value must be calculated inclusive of the cumulative cash outturn[3] of the Old FREF portfolio since 1 April 2002 less the cumulative value of Administration Expenses incurred by ECGD in respect of the Old FREF portfolio since 1 April 2001.

If the MTM value of the Old FREF portfolio is negative, then ECGD must notionally transfer from its cumulative Account 2 Reserves to Account 4[4]:

(a) the first £15 million of any negative MTM value equal to or less than £102 million; and

(b) 14.7 per cent of each £1 of such negative MTM value between £102 million and £204 million.

1 That is, after the notional transfer of reserves to cover FREF costs as described under items (iii) to (v) below.
2 The Old FREF – that business deriving from FREF commitments entered into by ECGD prior to 1st April 2001, including business deriving from such commitments which had not expired by that date.
3 This measure shall include no more than 7.5 per cent of the value of any cash savings derived from refinancing undertaken by ECGD on the Old FREF portfolio since 1 April 2002 and no more than 7.5 per cent of the value of any future savings derived from such refinancing.
4 Account 4 comprises the Old FREF, New FREF and 2005 FREF portfolios.

Result: The net MTM valuation of the Old FREF portfolio at 31 March 2007 was £29.6 million. The target was therefore met. In accordance with the agreed formulae, £15 million was transferred from the cumulative Account 2 reserves to Account 4.

(iv) ECGD must maintain a non-negative MTM value on its New FREF portfolio. Such non-negative MTM value must be calculated inclusive of the cumulative cash outturn[5] in respect of the New FREF portfolio, less the cumulative value of Administration Expenses incurred by ECGD in respect of the New FREF portfolio[6].

If the MTM value of the New FREF portfolio is negative, then ECGD must notionally transfer cumulative Account 2 reserves to Account 4 in order to restore the MTM value of the New FREF portfolio to a non-negative position.

Result: The net MTM value of the New FREF[7] portfolio was £6.3 million at 31 March 2007. Total transfer from cumulative Account 2 reserves at 31 March 2007 in respect of the New FREF portfolio was £11.9 million, comprising £6.3 million for New FREF and £5.6 million for Interim LASU[8] in accordance with the agreed formulae.

(v) ECGD must maintain an MTM value on its 2005 FREF[9] portfolio at a value no lower than minus £30 million. Such MTM value must be calculated inclusive of the cumulative cash outturn in respect of the 2005 FREF portfolio, less the cumulative value of administration expenses incurred by ECGD in respect of the 2005 FREF portfolio.[10]

If the MTM value of the 2005 FREF portfolio is negative, ECGD must notionally transfer cumulative Account 2 reserves to Account 4 in order to restore the MTM value of the 2005 FREF portfolio to a non-negative position.

Result: The net MTM value of the 2005 FREF portfolio was minus £646,000 at 31 March 2007. £646,000 was transferred from cumulative Account 2 reserves so as to restore the MTM value of the 2005 FREF portfolio to a non-negative value.

Key Target 2

To promote an international framework that allows UK exporters to compete fairly by multilaterally limiting or eliminating all subsidies, and by promoting the adoption of consistent practices for assessing projects and buyers.

Measures of Delivery

(i) To continue the process of updating the OECD Arrangement[11].

Result: Non-OECD members are being encouraged to support the terms of the OECD Arrangement under the OECD's Outreach Programme.

The Aircraft Sector Understanding is under re-negotiation; it is expected that this will result in the introduction in 2007 of a new regime of risk-related premium rates.

5 The footnote above applies here also to the New FREF portfolio.

6 This obligation is subject to the following exception: when calculating the MTM value of the New FREF portfolio, ECGD is not required to include business deriving from commitments entered into by ECGD between 1 April 2001 and 31 March 2002 (inclusive) in respect of support for Airbus sales under the terms and conditions set out in the Large Aircraft Sector Understanding contained within the OECD Arrangement on Officially Supported Export Credits ("LASU"). This exception is subject to the condition that ECGD must transfer, from its Account 2 Reserves, the first US$10 million worth of any costs (defined for the purposes of this condition to mean those costs to the Exchequer that arise from ECGD providing FREF for LASU business committed between 1 April 2001 and 31 March 2002 (inclusive) on terms not consistent with the FREF financial objective), and thereafter 50 per cent of any further costs that may arise, subject to an overall ceiling of US$15 million.

7 The New FREF portfolio – that business deriving from FREF commitments entered into by ECGD between 1st April 2001 and 31st March 2005 (inclusive), including business deriving from (i) renewals of FREF commitments originally given prior to 1st April 2001, and (ii) FREF commitments which had not expired by 31st March 2005.

8 Interim LASU refers to the portfolio of commitments entered into by ECGD between 1 April 2001 and 31 March 2002 (inclusive) in respect of support for Airbus sales under the terms and conditions set out in the Large Aircraft Sector Understanding contained within the OECD Arrangement on Officially Supported Export Credits ("LASU").

9 The 2005 FREF portfolio – that business deriving from FREF commitments entered into by ECGD between 1st April 2005 and 31st March 2008 (inclusive), including business deriving from FREF commitments originally given prior to 1st April 2008 which had not expired by that date

10 This measure shall include no more than 7.5 per cent of the value of any cash savings derived from refinancing undertaken by ECGD on the 2005 FREF portfolio and no more than 7.5 per cent of the value of any future savings derived from such financing.

11 The OECD Arrangement on Officially Supported Export Credits seeks to foster a level playing field for official export credit support in order to encourage competition among exporters based on the quality and price of goods and services exported, rather than on the degree to which officially supported financial terms and conditions are more favourable

(ii) To reduce any subsidies inherent within Commercial Interest Reference Rates (CIRRs).

Result: Despite a positive reception to technical work undertaken by ECGD, progress has been limited due to the different views on this issue within EU Member States. Further work towards CIRR reform continues.

(iii) To strengthen the existing Recommendation on Common Approaches to the Environment.

Result: The review by OECD members of the OECD Recommendation on Common Approaches on the Environment and Export Credits concluded in April 2007. Progress was made in all three of the UK's priority areas: achieving greater consistency in the identification and categorisation of project impacts; increasing the extent to which social impacts are included in the agreement; and defining more clearly the minimum international standards that must be met.

(iv) To strengthen the anti-bribery and corruption procedures of ECAs.

Result: A strengthened OECD Action Statement on Bribery and Officially Supported Export Credits was agreed in April 2006, introducing enhancements to existing anti-bribery and corruption measures. This was upgraded to a Recommendation of the OECD Council in December 2006.

(v) To build a consensus towards the incorporation into the OECD Arrangement of risk-reflective pricing for non-governmental buyer risk.

Result: Following a UK-inspired mandate, technical discussions continue within the OECD with the aim of developing guiding principles for common buyer risk assessment and pricing practices to facilitate risk premium convergence. Less progress has been made than the UK had hoped, but it continues to pursue this aim.

(vi) To introduce international guidelines to ensure responsible lending to low-income countries.

Result: ECGD has worked with OECD members, the International Monetary Fund and the World Bank to develop proposals to ensure that new lending does not lead to unsustainable debt burdens for former Heavily Indebted Poor Countries (HIPCs) and countries that the World Bank classifies as eligible for highly concessional loans and grants for the International Development Association. In April 2007, OECD Export Credit Agencies agreed that new lending to the latter group of countries should be subject to the same tests as are currently applied to HIPC markets under the OECD Statement of Principles on official Export Credit Support to heavily indebted poor countries.

Key Target 3

To provide an efficient, professional and proactive service for exporters of UK goods and services which focuses on solutions and innovation.

Measures of Delivery

(i) Compliance with service delivery targets set out in ECGD's Customer Charter, performance against which is reported in *ECGD News* publication.

Result: Service delivery targets as set out in ECGD's Customer Charter, and reported in *ECGD News*, were met, with two exceptions:

a. ECGD was unable to meet the target relating to the allocation to insured parties of certain (Paris Club) recoveries due to technical difficulties with its IT system. Most of these allocations have been paid and work to clear the remaining payments is underway. During 2007-08 ECGD, once again, expects to meet the service delivery targets for allocation of Paris Club recoveries

b. The target relating to the 'Provision of Preliminary Response Letters within four working days' was achieved for 53% of cases in 2006-07. Although ECGD was taking corrective steps with respect to providing responses on straightforward cases, the target would not be met on complex cases where rigorous underwriting procedures were required. Customers have accepted that the target is inappropriate for such cases, and have been able to make use of ECGD's enhanced Website Calculator to determine approximate premium rates for the majority – about 80% - of enquiries. ECGD therefore stated its intention to review this (and all other) Charter targets during 2006-07 to seek to develop more suitable measures of service delivery.

As noted as its intent last year, ECGD duly undertook a review of its Customer Charter in the course of the year in order to reflect the current business environment and recent improvements made to its internal processing systems. An amended Charter came into effect on 2 April 2007 and can be found on ECGD's website.

Key Target 4

To reduce the concentration of risk prevalent in the ECGD portfolio of business by working with the private sector.

Measures of Delivery
Subject to market potential and satisfaction of value for money criteria:

(i) To have transferred risk of contingent liabilities to the private sector via Active Portfolio Management (APM).

Result: ECGD has continued to purchase further protection from private sector counterparties in respect of certain contingent liabilities. In the year to 31 March 2007, protection with a notional value of JP¥ 19,200m (£83 million equivalent) was purchased.

3 CORE TABLES

Please see ECGD's Resource Accounts – pages 42 to 94 of this document. This includes details of resources, spending and investment. Staff numbers and costs are included on pages 76 to 77, in addition to the section on personnel in the Annual Report on page 26.

4 DEPARTMENTAL INVESTMENT STRATEGIES

In the autumn of 2005, ECGD completed a major programme of work which involved the replacement of bespoke, separate systems with an integrated solution using commercial software packages.

As ECGD began to develop a deeper understanding of the new systems, it became apparent during the course of 2006 that, if full advantage was to be taken of their functionality and data-handling capabilities, further work involving significant resource would be needed. A Data Improvement Programme was started in the summer of 2006, with the key aims of developing appropriate processes and procedures together with robust systems and data. The Programme is expected to be largely complete by 31 March 2008. Work will continue thereafter in order to realise the longer-term benefits for ECGD from the new systems.

5 OTHER INFORMATION IN THE PUBLIC INTEREST

The main body of this Annual Review describes ECGD policies on a wide range of topics. Information on recruitment, training and development, public appointments; and policies related to the environment and to sustainable development can be found in the relevant sections.

Glossary

ACTIVE PORTFOLIO MANAGEMENT (APM)
The mitigation of ECGD's risks through arrangements with the private and/or international public sectors, resulting in a reduction in the Trading Fund's capital consumption and associated cost of capital.

AMOUNTS AT RISK (AAR)
AAR is equivalent to the accounting term Contingent Liability. This represents the unexpired portion of the total risks guaranteed by ECGD, thus AAR would normally be less than Maximum Liability by the amount of expired risk i.e. payment received or the unutilised amount of a loan.

APPROPRIATIONS IN AID (A. IN A.)
Comprise income received by ECGD, which it is authorised to retain (rather than surrender to the Consolidated Fund) to offset related expenditure. Such income is voted by Parliament and accounted for in the Department's resource accounts. Any receipts in excess of the approved amounts form Excess A. in A. and are payable directly to the Consolidated Fund as a CFERs.

BUYER CREDIT
A medium to long-term finance facility in which, normally, a 100 per cent unconditional guarantee is given by ECGD to a UK bank. This is in respect of a loan made available to an overseas borrower to finance a contract relating to the supply of Capital Goods and Services by a UK-based supplier to a buyer in an overseas market.

CONSOLIDATED FUND EXCESS RECEIPTS (CFERs)
Comprise receipts realised or recovered by ECGD in the process of conducting services charged on public funds which are not authorised to be appropriated in aid of expenditure, but which must be paid directly to the Consolidated Fund.

CREDIT DEFAULT SWAPS (CDS)
A market instrument included in the APM programme to transfer credit risk.

EXPORT CREDIT AGENCIES (ECA)
These are institutions providing government-backed guarantees, insurance and sometimes loans, covering commercial and political risk. Most industrialised nations have an ECA, which is usually a national, public or publicly-mandated agency supporting companies from their home country.

FINANCIAL OBJECTIVES
The Department's financial aim, which is the subject of agreement with HM Treasury.

FIXED RATE EXPORT FINANCE (FREF)
Finance for export contracts involving credit of two years or more provided by lending banks at fixed interest rates determined under The Arrangement, and which is guaranteed by ECGD and is the subject of interest equalisation. The finance can be offered in sterling and a range of standard currencies. Non-standard currencies need to be cleared by HM Treasury and the Bank of England.

HEAVILY INDEBTED POOR COUNTRIES (HIPC)
Heavily Indebted Poor Countries as classified by the World Bank/IMF.
See http://www.imf.org/external/np/exr/facts/hipc.htm for more information.

OVERSEAS INVESTMENT INSURANCE (OII)
ECGD facility which provides UK investors with insurance for up to 15 years against political risks in respect of new investment overseas. Also available to UK banks in respect of overseas lending, whether or not it is in connection with an UK investment or export.

PREMIUM EARNED / PREMIUM INCOME
Consideration receivable for guarantees and insurance contracts that become effective during the financial year. Premium Income is stated both gross and net of amounts ceded to other ECAs.

PROJECT FINANCE
Transactions which are dependent on generating sufficient revenue from a project to service debt, once commissioned e.g., a power station or toll road.

PROVISIONS
Amounts which are set aside within ECGD's Trading Accounts to allow for non-recovery of claims already paid and of claims to be paid in the future.

SUPPLIER CREDIT
Credit given by a UK exporter to an overseas buyer. In such cases, the normal method of financing the contract is for the bank to lend the exporter money and for the exporter to repay, usually when it receives payment from the buyer after the agreed credit period. ECGD can provide insurance for this finance under the SCF facility.

SUPPLIER CREDIT FINANCE FACILITY (SCF)
An ECGD facility for the sale of semi-capital or capital goods on two or more years of credit, providing finance to the supplier in the majority of cases without recourse.

THE ARRANGEMENT
The OECD Arrangement on Guidelines for Officially Supported Export Credits, sometimes referred to as "The Consensus". This limits self-defeating competition on export credits among members of the OECD who have undertaken that they will operate within these guidelines when providing official support for export credits of two years or more. The Arrangement covers all officially supported export credits except those for agricultural produce and military equipment. Aircraft, ships, nuclear power plants, water and renewable energy projects are subject to separate sector understandings.

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