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United Kingdom Debt Management Office

Report and Accounts 2005-2006

Presented to Parliament in pursuance of Section 7 of the Government Resources and Accounts Act 2000.

Ordered by the House of Commons to be printed 17 July 2006.

The United Kingdom
Debt Management Office
is an Executive Agency of
HM Treasury

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This publication is available in electronic form on the DMO website www.dmo.gov.uk.

All the DMO's publications are available on its website including:

- annual review covering the main developments for the financial year in which the DMO has been in operation;
- quarterly review highlighting more recent developments in the DMO's gilts and cash market activities;
- guides for potential investors in gilts – both wholesale and retail;
- the DMO's annual Report and Accounts for its administrative expenditure and also for the operation of the Debt Management Account;
- Operational Notices covering the DMO's market activities in the gilts and cash markets;
- the DMO's annual business plan;
- the DMO's framework document (which sets out the DMO's relationship with HM Treasury).

Alternatively, hard copies of these publications are available from the DMO by telephoning 020 7862 6501.

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Contents

Chief Executive's Report

Foreword

Innovation in UK Government financing

In 2005-06 the UK Debt Management Office (DMO) again successfully delivered its Debt and Cash Management Remits and also introduced significant innovations in gilt issuance.

A significant feature of 2005-06 was the continued interest by pension fund and insurance companies in long-dated gilts. In response to this particular area of investor interest, the DMO issued on behalf of the UK Government a new 50-year conventional bond in May 2005, thereby becoming one of only two G 10 countries to issue a bond of such maturity during the financial year.

This event was followed in September 2005 by the launch of the first ever syndicated offering of a gilt. The 1 1/4% Index-linked Gilt 2055, which is the longest-dated sovereign index-linked bond in the world, also incorporated a shortened indexation lag. This design, which is consistent with international best practice, has been adopted for all new index-linked gilts issued with effect from September 2005. These innovations are described in more detail on page 10.

Since the DMO was established as the UK Government's debt manager in 1998, the Government's borrowing requirement has risen six fold to £52.3 billion in 2005-06. This requirement was successfully financed in terms of gilt sales through the conduct of 25 auctions and one syndicated offer.

The rising trend of gilt issuance was an operational challenge to those DMO staff involved in implementing the debt issuance programme. The effective way in which the programme was conducted is testament to their high standards of expertise and skill.

The DMO was also instrumental in providing advice on and implementing the UK Government's daily cash management requirements and the operational management of the Government's balance sheet. The DMO's fund management operation also continued to provide a cost-effective service to clients and the facility to provide loans to local authorities experienced increased demand as the maximum maturity of loans increased. The achievements against these and other organisational objectives and targets can be reviewed on pages 12 to 17.

Looking forward, our financing Remit for 2006-07 is again challenging but is supported by a robust and transparent policy framework combined with a pragmatic approach to implementation. Modifications to the Remit, approved by Ministers, have been introduced and designed both to enhance the predictability and transparency of the current framework and to increase the Government's ability to respond to any substantial changes in market conditions that may occur during the course of the financial year. These temporary changes form part of our Remit for 2006-07 which includes plans for a record level of gilt supply (£63.0 billion) including record amounts of long-dated and index-linked gilt issuance. In addition to a record amount of supply, the DMO is also aiming to increase the amount of certainty surrounding the core part of our issuance programme (of £53.0 billion) by providing long dated index-linked issuance each month and at least two long dated conventional auctions per quarter. During the year, we have also committed to issuance of at least £10.0 billion in each of the short and medium maturity bands. Alongside the core programme, £10.0 billion of gilt sales are to be allocated on a quarterly basis in a way designed to respond to any changes in market conditions or patterns of demand.

2005-06 has proved to be a year of innovation and the DMO has responded to the change in market conditions in the delivery of its objectives. It has continued to ensure that UK Government debt management not only continues to conform to international best practice, but also sets its own standards of excellence. As always the continued success of the DMO depends on the efforts of its staff and I remain very grateful for their outstanding contribution throughout the year.

Background on the DMO

The DMO was established on 1 April 1998, with the aim '…to carry out the Government's debt management policy of minimising financing costs over the longer term, taking account of risk, and to manage the aggregate cash needs of the Exchequer in the most cost effective way'.

In institutional terms, the DMO is legally and constitutionally part of HM Treasury, but as an executive agency, it operates at arm's length from Ministers. The Chancellor of the Exchequer determines the policy and operational framework within which the DMO operates, but delegates to the Chief Executive operational decisions on debt and cash management, and day-to-day management of the office.

The separate responsibilities of the Chancellor and other Treasury Ministers, the Permanent Secretary to the Treasury and the DMO's Chief Executive are set out in a published Framework Document, (available on the DMO website at www.dmo.gov.uk), which also sets out the DMO's objectives and its Chief Executive's lines of accountability. The Chief Executive is accountable to Parliament for the DMO's performance and operations, both in respect of its administrative expenditure and the Debt Management Account.

On 1 July 2002, the operations of the Public Works Loan Board (PWLB), and the Commissioners for the Reduction of the National Debt (CRND)[1] (two constituent parts of the National Investment and Loans Office (NILO)) were integrated with the DMO, and the relevant PWLB and CRND staff relocated to the DMO's premises. The PWLB lends principally to local authorities for capital purposes and collects the repayments. Its responsibilities include ensuring these loans are made correctly and that there is no loss to the Exchequer. The CRND's principal function is managing the investment portfolios of certain public funds. PWLB and CRND continue to carry out their longstanding statutory functions within the DMO.

On 20 December 2004, the DMO introduced a Gilt Purchase & Sale Service for retail investors that replaced the Bank of England's Brokerage Service. This service is only available to those registered on the Approved Group of Investors database, which members of the public are able to apply to join and is operated by Computershare Investors Services PLC, as an agent of the DMO. This service enables members of the public to undertake secondary market transactions in gilts on an execution only basis, cheaply and quickly within the framework provided by the Approved Group process, which was introduced as an anti-money laundering measure. This additional service provided by the DMO coincided with the administration of the gilt register being transferred from the Bank of England to Computershare. The contract with Computershare is managed by DMO on behalf of HM Treasury.

1 The National Debt Office (NDO) previously administered the activities of the CRND.

Principal Activities

- DMO – the DMO's aim is to carry out the Government's debt management policy of minimising financing costs over the longer term, taking account of risk, and to manage the aggregate cash needs of the Exchequer in the most cost-effective way.
- PWLB – the PWLB issues loans from central government funds, primarily to local authorities and collects the repayments. Its responsibilities include ensuring the loans are made correctly and that there is no loss to the Exchequer.
- CRND – the CRND invests and manages certain public funds such as the United Kingdom National Insurance Fund and monies generated by the National Lottery for good causes pending drawdown by the Distribution Bodies.

Management of the DMO

At the start of 2005-06, ministerial responsibility for the DMO was vested in the Financial Secretary to the Treasury, which was held by Stephen Timms MP. Following an announcement in May, this responsibility was transferred to the post of Economic Secretary to the Treasury, which has been held by Ivan Lewis MP.

Robert Stheeman, the Agency's Chief Executive, is the Accounting Officer for the Agency and is responsible to HM Treasury Ministers for the overall operation of the Agency in accordance with its Framework Document.

The Chief Executive's appointment was through open competition by HM Treasury and he commenced his role as head of the DMO on 6 January 2003. His appointment was for an initial 3-year fixed term period and has since been extended for a further fixed term period until 31 December 2007. The contract is subject to a 3-month notice requirement. Compensation for early termination would be paid in accordance with the relevant provisions of the Civil Service Compensation Scheme.

A corporate governance infrastructure has been established to assist the Chief Executive, comprising of a high level Managing Board that at the 31 March 2006, in addition to the Chief Executive, comprised:

Jo Whelan	– Deputy Chief Executive
Jim Juffs	– Chief Operating Officer
Sue Owen	– non-Executive HM Treasury representative
Colin Price	– non-Executive Director
Brian Larkman	– non-Executive Director

Corporate Governance

A number of committees and other groups support the Chief Executive in carrying out his responsibilities. The Managing Board is the DMO's senior committee and supports the Chief Executive in delivering the DMO's objectives. This in turn is supported by the following operational committees:

- Debt Management Committee
- Cash Management Committee
- Fund Management Committee
- Risk Committee
- Audit Committee

During 2005-06, the DMO employed the services of two external non-Executive Directors, Colin Price and Brian Larkman, as members of the high level Managing Board. In addition to these appointments, Sue Owen who is an employee of HM Treasury also sits on the Board.

Colin Price, who was appointed by the Chief Executive, was Finance Director of Shell Pensions Management Services Ltd between 1991 and 2001, and a member of the Board of IMRO from 1996 to 2000. This position is subject to regular review. Brian Larkman was Global Head of Money Markets at the Royal Bank of Scotland PLC from 2000 to 2001 and previously Managing Director, Global Money Markets at National Westminster Bank PLC from 1991 to 2000. He is currently a member of the Regulatory Decisions Committee of the FSA. His appointment was made on the basis of open competition.

The DMO established an Audit Committee in 1999 as part of its development of internal risk management and control arrangements in line with best private sector practice. During the year, the Committee met quarterly and was chaired by Colin Price.

Other Organisational Arrangements

Preparation of accounts

The financial accounts have been prepared in accordance with a direction given by HM Treasury in pursuance of section 7 (2) of the Government Resources and Accounts Act 2000. The text of the direction is reproduced on page 51.

As far as I am aware, as Accounting Officer, there is no relevant audit information of which the Agency's auditors are unaware. I have taken all the steps that I ought to have taken to make myself aware of any audit information and to establish that the Agency's auditors are aware of that information.

Civil Service Pensions

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 the 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 based arrangement with a significant employer contribution (partnership pension account).

Employee contributions are set at the rate of 1.5 per cent of pensionable earnings for classic and 3.5 per cent 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.

The partnership pension account is a stakeholder pension arrangement. The employer makes 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 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 per cent of pensionable salary (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 centrally-provided risk benefit cover (death in service and ill-health retirement).

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

Pension liabilities

Past and present employees are covered by the provisions of the Principal Civil Service Pension Schemes (PCSPS) which are described above. The defined benefit schemes are unfunded and are non-contributory except in respect of dependants' benefits. The Agency 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, the Agency recognises the contributions payable for the year.

Equal opportunities

The DMO is an equal opportunities employer. Policies are in place to ensure that no job applicant or member of staff receives less favourable treatment on grounds of gender, gender re-assignment, marital or family status, colour, racial origin, sexual orientation, age, background, religion, disability, Trade Union membership or by any other condition or requirement which cannot be shown to be justifiable. The DMO attaches great importance to its equal opportunities policy, which it believes to be of benefit to itself and its employees.

Disability

The DMO is committed to the promotion of opportunity in all fields and the above policy statement affirms its commitment to equality of opportunities in employment and to the development of management and staff who demonstrate clear awareness of equality issues. The DMO has a culture of inclusiveness and is working towards removing barriers to achieve full diversity.

Employee relations

The DMO continues to maintain effective employee relations and to involve staff in decision-making.

A Staff Council has met regularly throughout the year and enabled an open exchange of thoughts, ideas, views and feelings between management and staff representatives and has been effective as a conduit for wider communication and consultation with all staff.

Union arrangements also continue for staff transferred to the DMO in 2002 under TUPE principles. Staff may also choose to join a Trade Union of their choice on an individual basis.

Improving good practice and investment in people

The DMO was re-accredited as an Investor in People in September 2005 and continues to work towards maintaining this status with the next formal review due by September 2008. The DMO's training and development policy is central to ensuring that the right people with the right skills are in the right job at the right time. The DMO's comprehensive corporate training programme, complemented by additional specialist and individual training as well as support for ongoing professional studies, continues to enhance the skills base of its employees.

ROBERT STHEEMAN
Chief Executive and Agency Accounting Officer
26 June 2006

Management Commentary

Review of Activities

2005-06 was a successful year for the DMO in managing its daily operations. It successfully met both its Debt and Cash Management Remits as directed by HM Treasury, as well as meeting the majority of its objectives and published targets in full. A full account of these is given on pages 12 to 17.

Debt Management

During 2004-05, the DMO conducted a wide-ranging, but informal consultation exercise with investors (fund managers), pension fund trustees, consultants, actuaries and academics to fully understand the market interest in the issuance of a potential ultra-long gilt instrument. The feedback, together with our own view of the potential benefits for the Government in such an issuance, saw HM Treasury Ministers instruct the DMO to launch a formal consultation exercise that was consistent with Government practice to widely consult stakeholders. The Chancellor of the Exchequer launched this exercise alongside the Pre-Budget Report on 2 December 2004.

This formal consultation confirmed the earlier assessment that it would be possible to issue ultra-long gilts at a favourable cost to the Government. Consequently, in his 2005 Budget speech, the Chancellor announced to Parliament that the DMO would issue ultra-long gilts as part of our financing Remit for 2005-06.

The gilt auction held on 26 May 2005 saw the DMO issue a new 50-year conventional bond, 4 1/4% Treasury Gilt 2055, the first gilt of such maturity to be issued since October 1960. During 2005-06, this gilt was auctioned on four occasions and resulted in £9.5 billion (nominal) being issued.

As part of its strategy to efficiently manage the Government's debt portfolio, the DMO also issued a 50-year index-linked gilt by syndication during September. This transaction was innovative in several respects: it marked a 20-year extension of the index-linked gilt curve as well as the global index-linked bond market (the gilt was – and remains – the longest-dated sovereign index-linked bond globally); it marked the introduction of a new design for index-linked gilts, with the adoption of a 3-month indexation lag, also used by most other sovereign issuers, to replace the 8-month indexation lag that had been used beforehand in the gilt market; and it was the first time a syndicated offering had been used by HM Government as the method of issuance.

The decision to open this gilt by syndication rather than by the usual auction method reflected the significant uncertainty that existed prior to issuance as regards the pricing of the bond, given its innovative character. A syndicated offering was deemed to provide a transparent and iterative price formation process that would be more conducive to an accurate pricing of the bond in the primary market than might have taken place through an auction. This decision therefore reflected the unusual circumstances of the initial opening of the bond. Auctions remain the preferred issuance method of the DMO and have been used for subsequent openings of this gilt as well as for (re-) openings of all other gilts.

On 13 September 2005, the DMO announced that it would issue the gilt through a syndicate of banks, composed of all fourteen index-linked Gilt-edged Market Makers, four of which were selected to be joint bookrunners. An amount of £1.25 billion nominal of the gilt was issued on 23 September 2005.

The outcome of the transaction (pricing at the high end of the initial price guidance range) and the stability of the gilt price in relation to the rest of the yield curve in the days following the transaction suggest that the objectives have been achieved, in particular as regards the efficiency and cost-effectiveness of pricing in the primary market.

Cash Management

In June 2005, following recommendations of the 2004-05 Cash Management Review, the DMO began to assess Government active cash management against a single, quantified measure of performance, and within the context of a quantified definition of risk – risk appetite - approved by Ministers. The approach that has been adopted compares the cost and risk of Government active cash management, including contributions from both forecasting and market operations, against the cost and risk of a simple passive default strategy. It is intended that this method of assessment be introduced formally over the course of 2006-07, following further calibration in the light of any changes to the Sterling money markets, including following the Bank of England's reforms.

Other developments in DMO cash management activities introduced in 2005-06 included the widening of the range of cash management counterparts, including via electronic platforms and making more consistent use of interbank, Certificate of Deposit and Commercial Paper markets.

PWLB

PWLB had another year of successful operation that saw it increase its maximum lending maturity from 30-years to 50-years. Interest rates for new loans from the Board continued on a declining trend over 2005-06 and resulted in a marked increase in customer activity. This in turn generated an unusually high amount of fee income.

CRND

2005-06 was a year of consistency for CRND, who continued to provide an efficient, value for money investment service to various Government clients, with the material objectives of all investments being to maintain sufficient liquid funds to meet withdrawals by the clients and to protect the capital value of the funds.

CRND continues to investigate the scope for providing a more active style of fund management from within the private sector in addition to the existing cash management and gilt index-tracking options on offer.

During the year CRND assumed responsibility for investing the new Olympic Lottery Distribution Fund, increasing the number of investment accounts managed to ten.

Financial Performance

The Agency is financed through HM Treasury and operated under net administration cost arrangements, meaning that the control total for the DMO's annual expenditure agreed by Parliament comprises an aggregate of target expenditure and income.

The DMO's net operating cost for 2005-06 was £7.5 million. This represents an increase of £0.6 million from the previous year, and remained within the DMO's voted expenditure limit.

During the reporting period, the DMO's gross administrative expenditure increased by £1.7 million compared to the previous year, as the DMO continued to develop and improve its capability to deliver its core objectives.

Programme expenditure increased in the year to £3.8 million (2005-06: £1.3 million), driven largely by the cost of the UK Government's first syndicated issuance of a gilt in September 2005. Given the absence of suitable market reference prices, syndication was judged to be the most effective method of issuance to achieve best value for the Exchequer, by ensuring a transparent and efficient price formation process. The cost incurred by the DMO for this operation was off-set by income in the form of a recovery from the National Loans Fund.

In total, the DMO received operating income of £7.8 million (2004-05: £4.2 million), an increase of £3.6 million. In addition to the recovery of syndication costs, increased PWLB lending also contributed to the increase in income as local authority borrowers responded to the generally falling pattern of lending rates over the course of 2005-06, and to the extension on 7 December 2005 from 30 to 50 years of the maximum maturity period for PWLB loans.

Achievements against Objectives

HM Treasury Ministers set the DMO's strategic objectives, which are published in the DMO's Business Plan and its Framework Document. The objectives for 2005-06 and the DMO's performance against them are summarised below.

1. **To develop, provide advice on and implement the Government's debt management strategy.**

   The DMO provided analysis and advice to HM Treasury in connection with the preparation of its Remit for 2005-06 and, in particular, recommendations about the prospects for ultra-long gilt issuance.

   Following consultation with the public and stakeholders the DMO launched ultra-long-dated gilts with original maturities of approximately 50 years. This represented the first issue of 50-year conventional gilts by the UK government for over 40-years, and the longest-ever issue of index-linked gilts. The DMO also introduced a new design of index-linked gilts, with a 3-month indexation lag, in line with international best practice. The 50-year index-linked gilt is the longest-dated indexed sovereign bond in the world.

   The gilt Remit for 2005-06 was successfully delivered, with outturn gilt sales of £52.3 billion (cash) through the conduct of 25 gilt auctions and, for the first time ever, one syndicated offer – for the inaugural issue of the 50-year index-linked gilt – reflecting the unique characteristics of that first issue.

2. **To develop, provide advice on and implement the Government's cash management requirement.**

   The DMO prepared the strategic and operational capability to deliver a new cash management objective introduced as part of the 2005-06 cash management Remit in April 2005.

   Following work on the strategic and operational capability of DMO systems, Phase 1 of the Cash Management Review was successfully implemented on 27 June 2005. Relative performance measurement of the active cashbook against the default benchmark strategy in terms of risk and P&L measures has been in place since then. Work is on going for the outstanding transitional issues necessary for the implementation of Phase 2.

3. To advise on the development and implementation of HM Treasury's strategy for managing the Government's balance sheet to secure sound public finances.

The DMO has continued to provide analysis and advice to HM Treasury on the broader implications for HM Government's balance sheet of the management of the Government liabilities and assets entrusted to the DMO, with a view in particular to avoiding unwanted mismatches in the nature of assets and liabilities.

This analysis has contributed to the decision to extend the maximum maturity of PWLB loans, responding to the similar extension of the maximum maturities of gilts issued by the DMO.

At an operational level, the DMO has also continued to hedge HM Government's exposure to the equity market through the sale of National Savings and Investments' (NS&I) Guaranteed Equity Bond (GEB) product by implementing swap transactions with market counterparties.

4. To develop and deliver its fund management responsibilities and, in particular, to provide a cost-effective service for stakeholders.

The DMO, through its Fund Management operation, continued to provide a cost-effective service to client funds that are the responsibility of the Commissioners for the Reduction of the National Debt (CRND).

The DMO continued to manage the gilt registration contract with Computershare Investor Services PLC ("Computershare") on behalf of HM Treasury following the transfer of the registration function from the Bank of England in December 2004. It also continued to offer the gilt purchase and sale service for retail investors, which is carried out in association with Computershare as the DMO's agent.

5. To provide a cost-effective lending service to local authorities through the Public Works Loan Board.

The Public Works Loan Board continued to provide loans for capital purposes to local authorities and other prescribed borrowers. In December 2005 the Board, after consultation with HM Treasury, increased the maximum maturity of its loans from 30 to 50-years. This followed the successful issuance of 50-year gilts in accordance with the DMO's debt management Remit. With rates on a declining trend for most of 2005-06 there was increased demand for loans and at end March 2006 loans outstanding to the Board totalled £47.1 billion compared with £42.1 billion at end March 2005.

6. To resource, staff and manage the DMO efficiently and cost-effectively to ensure key responsibilities are achieved.

The DMO was reaccredited as an "Investor in People" in September 2005 and continues to work towards maintaining this status with the next formal review due by September 2008. The DMO's training and development policy is central to ensuring that the right people with the right skills are in the right job at the right time. The DMO's corporate training programme, complemented by additional specialist and individual training as well as support for ongoing professional studies, continues to enhance the skills base of its employees.

7. To manage, operate and develop an appropriate risk and control framework.

The DMO continued to operate an effective risk and control framework throughout the year and has made some significant enhancements to the framework. An independent review of the risk reporting processes were carried out during the year and a number of recommendations have been implemented to improve the focus on key risks and controls and the usefulness of the information produced. In addition a range of new risk and performance measures were introduced governing the cash management operation.

Performance against Targets

1. To ensure full compliance with the Government's Remit for the DMO as set out in the Debt and Reserves Management Report 2005-06, and to ensure consistency with the objectives of monetary policy.

The gilt sales target has been met through the conduct of 25 outright auctions (fifteen conventional and ten index-linked), and one syndicated offer. Outright sales of £53.5 billion were planned in the remit for 2005-06, published on 16 March 2005. The sales target was decreased to £52.3 billion in the PBR on 5 December 2005, but this was still the highest level for over 10 years. The gilt sales outturn for 2005-06 was £52.3 billion (therefore within agreed operational tolerances). The composition of issuance was £41.5 billion conventional gilts and £10.8 billion index-linked gilts. There was no uncovered gilt auctions.

	2005-06 £m	2004-05 £m
Nominal value of gilts issued on behalf of the National Loans Fund	47,925	46,748
Proceeds paid to the National Loans Fund	52,361	50,101

25 outright auctions were held as follows:

- 12 April: £800 million (nominal) of 2% IL 2035
- 14 April: £2,500 million (nominal) of 5% 2025
- 28 April: £3,000 million (nominal) of 4¾% 2010
- 24 May: £425 million (nominal) of 2½% IL 2016
- 26 May: £2,500 million (nominal) of 4¼% 2055
- 7 June: £2,750 million (nominal) of 4¾% 2020
- 23 June: £450 million (nominal) of 4⅛% IL 2030
- 14 July: £2,250 million (nominal) of 4¼% 2055
- 26 July: £400 million (nominal) of 2½% IL 2020
- 2 August: £3,000 million (nominal) of 4% 2009
- 6 September: £2,750 million (nominal) of 4¼% 2036
- 27 September: £2,750 million (nominal) of 4¾% 2020
- 13 October: £2,750 million (nominal) of 4¼% 2032
- 25 October: £675 million (nominal) of 1¼% IL 2055
- 8 November: £3,250 million (nominal) of 4¼% 2011
- 24 November: £525 million (nominal) of 2½% IL 2013
- 7 December: £2,250 million (nominal) of 4¼% 2055
- 14 December: £375 million (nominal) of 4⅛% IL 2030
- 10 January: £2,500 million (nominal) of 4¾% 2020
- 24 January: £650 million (nominal) of 1¼% IL 2055
- 26 January: £3,000 million (nominal) of 4¼% 2011
- 7 February: £1,000 million (nominal) of 1¼% IL 2017
- 16 February: £2,500 million (nominal) of 4¼% 2055
- 1 March: £3,000 million (nominal) of 4% 2016
- 7 March: £625 million (nominal) of 2% IL 2035

In addition to the outright auctions mentioned above, the following stock was issued by means of a syndicated offer:

- 22 September: £1,250 million (nominal) of 1 1/4% IL 2055

The stock of Treasury bills in market hands fell from £20.3 billion at end-March 2005 to the Remit target of £19.1 billion at end-March 2006.

2. **To ensure that the maximum time taken to issue the results of gilt auctions does not exceed 40 minutes, that for weekly Treasury bill tenders does not exceed 30 minutes, and that for ad hoc Treasury bill or other tenders does not exceed 15 minutes, whilst achieving complete accuracy.**

Achieved. The gilt auction result release times during the year were all within the 40 minutes target:

■ 12 April: 2% IL 2035	16 minutes
■ 14 April: 5% 2025	17 minutes
■ 28 April: 4¾% 2010	16 minutes
■ 24 May: 2½% IL 2016	18 minutes
■ 26 May: 4¼% 2055	23 minutes
■ 7 June: 4¾% 2020	20 minutes
■ 23 June: 4⅛% IL 2030	17 minutes
■ 14 July: 4¼% 2055	21 minutes
■ 26 July: 2½% IL 2020	16 minutes
■ 2 August: 4% 2009	15 minutes
■ 6 September: 4¼% 2036	20 minutes
■ 27 September: 4¾% 2020	21 minutes
■ 13 October: 4¼% 2032	21 minutes
■ 25 October: 1¼% IL 2055	19 minutes
■ 8 November: 4¼% 2011	19 minutes
■ 24 November: 2½% IL 2013	15 minutes
■ 7 December: 4¼% 2055	34 minutes
■ 14 December: 4⅛% IL 2030	17 minutes
■ 10 January: 4¾% 2020	15 minutes
■ 24 January: 1¼% IL 2055	22 minutes
■ 26 January: 4¼% 2011	15 minutes
■ 7 February: 1¼% IL 2017	15 minutes
■ 16 February: 4¼% 2055	26 minutes
■ 1 March: 4% 2016	21 minutes
■ 7 March: 2% IL 2035	17 minutes

The average release time for gilt auctions was 19 minutes.

- 22 September: the DMO launched 1 1/4% Index-linked Treasury Gilt 2055 via a syndicated offering. The gilt was issued on 23 September 2005.

The target release time for the Treasury bill tenders was also met. The release times for the results of the 51 weekly tender bills held during the financial year ranged from 6 to 26 minutes and averaged 11 minutes. There were no ad hoc or other tenders.

3. **To achieve complete accuracy, within agreed accounting tolerances, in the recording and reporting of transactions through the Debt Management Account (DMA), and in delivering money (and reconciling payments) to the National Loans Fund (NLF) and to meet the required deadlines for the publication or submission for audit of the annual reports of the DMO agency and DMA.**

   The National Audit Office has certified that:

   The 2004-05 Debt Management Office financial statements give a true and fair view of the state of affairs of the UK Debt Management Office as at 31 March 2005 and of the net operating cost, total recognised gains and losses and cash flows for the year then ended and have been properly prepared in accordance with the Government Resources and Accounts Act 2000 and directions made there under by HM Treasury; and 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.

   The 2004-05 Debt Management Account financial statements give a true and fair view of the state of affairs of the Debt Management Account as at 31 March 2005 and of the surplus, total recognised gains and losses and cash flows for the year then ended and have been properly prepared in accordance with Schedule 5A of the National Loans Act 1968 and directions made there under by HM Treasury; and 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.

   The 2004-05 DMO Report and Accounts were laid before Parliament on 18 July 2005 and the DMA Account was laid on 20 July 2005.

4. **To acknowledge all letters and e-mail enquiries from the public within 4 working days and for at least 95 per cent to be sent a substantive reply within 2 weeks. Furthermore, the DMO will respond to enquiries under the Freedom of Information Act within the statutory timeframe.**

   Achieved. Over the financial year 282 queries were received (of which 251 were e-mails). The average response time was 2 working days.

5. **To achieve fewer than 5 breaches of Operational market notices (excluding any breaches which HM Treasury accept were beyond the control of the DMO).**

   Achieved. There were no breaches of the Operational market notices in the financial year.

6. **To ensure that, where there is a late change in the cash management forecast, any necessary use of end of day borrowing or lending facilities is notified by the due time.**

   Achieved. Deadlines for late lending and borrowing were met. In addition, in the event of a late shut-down the actual due time is moved, but the target remains the same. On one occasion in the financial year there was an unexpectedly large surplus balance following an incorrect adjustment of a repo trade that had failed the previous day (caused by the Bank's CREST settlement connection going down).

7. To ensure that instructions to counterparties, agents and external systems are complete, accurate and timely, and that monitoring of the progress of transactions through settlement is effective, so that the DMO achieves at least 99% (by value) successful settlement of agreed trades on the due date.

Achieved. Total turnover in 2005-06 was £1,083.2 billion. During the year, trades with a value of £833 million failed, as a result of circumstances outside the DMO's control. No trades failed within the DMO's control. Failed trades represented 0.08% of turnover.

8. To release all market sensitive data and announcements in a timely manner and to aim to achieve no factual errors in material published by the DMO on its wire service pages, its websites or its printed documents (insofar as the material is under the control of the DMO and not third parties).

Achieved on timeliness. All releases were announced in a timely manner.

Not achieved on accuracy. There were 18 factual errors discovered (and quickly corrected) on the DMO website in the financial year.

9. To process all loans or early settlement applications from local authorities within two working days (between the date of agreement and completion of transaction).

All loans or early settlement applications were agreed and advanced within two working days of the dates of agreement within the quarter and indeed the financial year apart from one occasion. On one loan the funds were advanced to the wrong account and as this could not be corrected until the next day, there was a charge of one night's interest of approx £600.

10. To ensure that the Gilts Purchase and Sales Service is operated according to its published terms and conditions.

The gilt sale and purchase scheme was conducted fully in line with its terms and conditions in the financial year as a whole. The pattern of sales and purchases through the financial year is shown in the table below.

	Sales (transactions)	Purchases (transactions)	Aggregate retail sales £m	Aggregate retail purchases £m
April – June 2005	1,674	915	10	15
July – September 2005	1,680	700	12	10
October – December 2005	1,400	1,144	11	18
January – March 2006	1,712	613	16	8
Total	**6,466**	**3,372**	**49**	**51**

Forward Look

The DMO's strategic objectives for 2006-07

1. To develop, provide advice on and implement the Government's debt management strategy.

2. To develop, provide advice on and implement the Government's cash management requirements.

3. To advise HM Treasury on the development and implementation of strategies for managing the Government's balance sheet, to secure sound public finances.

4. To develop and deliver its fund management responsibilities and, in particular, to provide a cost-effective service for stakeholders.

5. To provide a cost-effective lending service to local authorities through the Public Works Loan Board.

6. To resource, staff and manage the DMO efficiently and cost-effectively to ensure key responsibilities are achieved.

7. To manage, operate and develop an appropriate risk and control framework.

In the delivery of these objectives, the DMO seeks to primarily support HM Treasury's Objective I: "Maintain a stable macroeconomic environment with low inflation and sound public finances in accordance with the Code for Fiscal Stability". It also seeks to support Objective III "Promote efficient, stable and fair financial markets, for their users and the economy"; Objective VI: "Improve the quality and the cost-effectiveness of public services"; and Objective VII: "Achieve world-class standards of financial management in government".

The DMO's targets for 2006-07

1. To ensure full compliance with the Government's Remit for the DMO (which is primarily set out in the Debt and Reserves Management Report 2006-07 but, in some areas, is subject to confidential parameters notified separately to the DMO).

2. To ensure that the maximum time taken to issue the results of gilt auctions does not exceed 40 minutes, that for weekly Treasury bill tenders does not exceed 30 minutes, and that for ad hoc Treasury bill or other tenders does not exceed 15 minutes, whilst achieving complete accuracy.

3. To achieve complete accuracy, within agreed accounting tolerances, in the recording and reporting of transactions through the DMA, and in delivering money (and reconciling payments) to the NLF and to meet the required deadlines for the publication or submission for audit of the annual reports of the DMO and DMA.

4. To acknowledge all letters and e-mail enquiries from the public within 4 working days and for at least 95 per cent to be sent a substantive reply within 2 weeks. Furthermore, the DMO will respond to enquiries under the Freedom of Information Act within the statutory timeframe.

5. To achieve fewer than 5 breaches of operational market notices (excluding any breaches which HM Treasury accept are beyond the control of the DMO).

6. To ensure that, where there is a late change in the cash management forecast, any necessary use of end of day borrowing or lending facilities is notified by the due time, where applicable; and to ensure that target weekly balances and expected daily variations are notified according to the agreed schedule. This target is only applicable until 17 May.

7. To ensure that instructions to counterparties, agents and external systems are complete, accurate and timely, and that monitoring of the progress of transactions through settlement is effective, so that the DMO achieves at least 99% (by value) successful settlement of agreed trades on the due date.

8. To release all market sensitive data and announcements in a timely manner and to aim to achieve no factual errors in material published by the DMO on its wire service pages, its websites or its printed documents (insofar as the material is under the control of the DMO and not third parties).

9. To process all loan or early settlement applications from local authorities within two working days (between date of agreement and completion of transaction).

10. To ensure that the gilts purchase and sales service is operated according to its published terms and conditions.

The DMO's 3-year plan

To continue to deliver the DMO's core operations and activities to the excellent standard required.

This will include the following:

- Managing the debt and cash management operations successfully to deliver the financing programmes incorporated within the 2006-07 Remit.
- Developing in due course the debt and cash management Remit for 2007-08.
- Delivering the PWLB lending objectives for local authorities and developing, where appropriate and feasible, enhancements to the service.
- Managing the CRND funds in accordance with their respective mandates from clients.
- Delivering the gilt purchase and sale service for retail investors efficiently and effectively.
- Managing the registration contract with Computershare, on behalf of HM Treasury, in an effective and efficient way.
- Continuing to manage hedging transactions as required and to meet NS&I's requirements in respect of its issuance of Guaranteed Equity Bonds.
- Ensuring that the DMO's website, publications and information are managed effectively and are available to stakeholders when required.

To further the development of debt and cash management strategy, in particular where we identify initiatives that may provide cost and risk minimisation benefits for the Government.

This will include the following:

- Developing further our understanding of the composition of, drivers for and issues relating to the investor base for gilts and Treasury bills.
- Developing further analytical tools and techniques – in consultation with HM Treasury as necessary – that help inform debt and cash management strategy.
- Assisting HM Treasury with the development of a consolidated profile of public finances and considering any associated asset / liability-related issues.
- Continuing to work with the National Audit Office on their study on debt management.
- Developing enhancements to the delivery and measurement of the effectiveness of cash management operations.

To improve efficiency and to reduce operational risk where possible.

This will include the following:

- Taking forward the preparations for the introduction of electronic bidding at gilt auctions and Treasury bill tenders.
- Reviewing further the DMO's banking and settlement arrangements with the intention of identifying efficiencies and where possible advances in operational effectiveness.
- Developing and enhancing the DMO's business delivery capability to improve the operational efficiency of the agency.
- Enhancing the DMO's risk management analytical and reporting framework and capability.
- Continuing to enhance business continuity arrangements to develop further the DMO's operational resilience.
- Implementing a programme of strategic IT work to enhance the DMO's core infrastructure and applications.
- Developing further the management information produced to support the DMO's business and agency functions.
- Implementing efficiencies in the management of information taking due account of the Freedom of Information Act requirements.
- Continuing to deliver the programme of savings identified as part of the Efficiency Review.
- To continue to contribute to the workstreams underpinning the ongoing Comprehensive Spending Review.

To ensure the core values of the DMO continue to make it an excellent place to work.

This will include the following:

- Continuing to integrate and embed the DMO's core values into all aspects of the DMO's operations ensuring these activities are consistent with and build upon its "Investor in People" status.
- Identifying and implementing where appropriate more effective ways of working.

Resources

Sustainable development

As an executive agency of HM Treasury, the DMO is a party to the Joint Sustainable Development Statement, signed by the 'Green Minister' for the Chancellor of the Exchequer's Departments and Agencies, John Healey MP and published on the DMO website.

The DMO is committed to contributing to the Government's objectives on Sustainable Development as contained in the Framework for Sustainable Development in the Government Estate.

Service quality

The DMO does not provide services direct to the public, and so is not covered by existing arrangements for reporting service quality. However, the DMO has strong partnerships with parts of the public sector and provides advice and expertise to other Government departments (and other governments), in developing solutions for financial cost-effectiveness and risk reduction when managing the Government's balance sheet. The DMO has launched a consultation paper outlining its plans to introduce electronic bidding for gilt auctions and Treasury bill tenders, is frequently required to present to or host groups and individual officials from overseas countries, and promotes the gilts market when speaking at bond conferences both domestically and internationally. The DMO has also continued to upgrade and expand the content of its website (www.dmo.gov.uk) on which all its publications appear and which acts as a means of communication for all those with an interest in the DMO's activities.

HM Treasury services

In view of the DMO's executive agency status and the diseconomies of scale inherent in setting up a wide range of internal support systems given its small size, several key support services have in the past year been provided by HM Treasury, for example, purchase order processing, invoice processing and payment, payroll, and library.

Supplier payment policy

All the DMO's invoices are processed for payment by HM Treasury, which is committed to the CBI code on prompt payment and aims to pay all valid invoices within 30 days or less after acceptance of the relevant goods and services, or the receipt of a legitimate invoice if that is later. For 2005-06, HM Treasury achieved this payment target for 95% of invoices across the department.

Auditors' detail

As specified by the Government Resources and Accounts Act 2000, the Comptroller and Auditor General is responsible for auditing the DMO's annual accounts.

Remuneration Report

The DMO has a Pay Committee, which during 2005-06 comprised of:

Robert Stheeman	– Chief Executive (Chair)
Jo Whelan	– Deputy Chief Executive
Jim Juffs	– Chief Operating Officer
Colin Price	– non-Executive Director
Brian Larkman	– non-Executive Director

The Pay Committee is responsible for overseeing the DMO's delegated pay arrangements and ratifying the DMO's Pay Remit submission to HM Treasury and its subsequent implementation, taking account of individual performance (as assessed through the DMO's appraisal arrangements), job size (as assessed by job evaluation) and, where appropriate, external market comparators as well as public pay policy and affordability.

Remuneration Policy

Senior DMO staff

The Chief Executive is a member of the Senior Civil Service, employed by HM Treasury and included in HM Treasury's appraisal arrangements. Increases in salary are made by HM Treasury in accordance with the Senior Salaries Review Body's Report.

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

Salaries of the Deputy Chief Executive and Chief Operating Officer are set internally in accordance with DMO's delegated pay arrangements and ratified by the non-Executive Directors.

In accordance with these pay arrangements, all material pay increases are determined by performance as assessed through the internal annual appraisal process. The term 'performance' relates to the 'total contribution' of individuals in carrying out their core role, achievement of delivery objectives, and a demonstration of competencies as determined through a robust performance management and assessment process.

Non-Executive Directors

The Chief Executive, in discussion with the Deputy Chief Executive and Chief Operating Officer, determines the remuneration of the non-Executive Directors. Remuneration is reviewed annually taking account of external market comparators as well as public sector pay policy and affordability, but the DMO reserves the right not to make adjustments at that time.

The non-Executives are appointed as "office holders".

Contracts

Senior DMO staff

The Chief Executive's appointment was for an initial 3-year fixed term period from 6 January 2003 to 5 January 2006 and has since been extended for a further fixed term period until 31 December 2007. The contract is subject to a 3-month notice requirement. Compensation for early termination would be paid in accordance with the relevant provisions of the Civil Service Compensation Scheme.

The appointments of the Deputy Chief Executive and Chief Operating Officer have been made in accordance with the provisions of the Civil Service Commissioners' Recruitment Code.

Further information about the work of the Civil Service Commissioners can be found at www.civilservicecommissioners.gov.uk

Non-Executive Directors

Colin Price's contract was originally for an initial 2-year period from 21 February 2002 until 20 February 2004 and has been extended for a further period of 3 years to 20 February 2007.

Brian Larkman's contract is for a period of 3 years from 1 January 2005 until 31 December 2007.

Both contracts are subject to a one-month notice requirement. Contracts will automatically terminate on the date stated unless a further extension has been agreed. As office holders there is no provision for compensation for early termination.

Remuneration Received

	2005-06 Salary £000	**2004-05 Salary £000**
Robert Stheeman – Chief Executive	120 – 125	120 – 125
Jo Whelan – Deputy Chief Executive*	100 – 105	90 – 95
Jim Juffs – Chief Operating Officer	120 – 125	110 – 115

* The salary disclosed reflects part time hours and is calculated on a pro rata basis from full time equivalent (FTE) of 0.78 in 2005-06 (0.78 in 2004-05).

'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 allowances to the extent that it is subject to UK taxation.

This report is based on payments made by the Agency and thus recorded in these accounts.

Salaries and allowances payable to both Colin Price and Brian Larkman as non-Executive Directors in the reporting period were £15,000 each.

The DMO is not responsible for the remuneration of any Ministers and Sue Owen, who is an employee of HM Treasury, is similarly not remunerated by the Agency.

Pension Benefits

	Accrued pension at age 60 at 31 March 2006 and related lump sum £000	Real increase in pension and related lump sum at age 60 £000	CETV at 31 March 2005 Restated £000	CETV at 31 March 2006 £000	Real increase in CETV £000
Robert Stheeman – Chief Executive	5 – 10	0 – 2.5	41	79	21
Jo Whelan – Deputy Chief Executive	0 – 5	0 – 2.5	15	38	14
Jim Juffs – Chief Operating Officer	30 – 35	5 – 7.5	77	124	20

Civil Service Pensions

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 based arrangement with a significant employer contribution (partnership pension account).

Employee contributions are set at a 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 in the same way as in classic.

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 from a selection of approved products. 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).

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

The cash equivalent transfer value (CETV)

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 CS 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.

The factors used to calculate the CETV were revised on 1 April 2005 on the advice of the Scheme Actuary. The CETV figure for 31 March 2005 has been restated using the new factors so that it is calculated on the same basis as the CETV figure for 31 March 2006.

Real increase in CETV

This reflects the increase in CETV effectively funded by the employer. It takes account of 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.

ROBERT STHEEMAN
Chief Executive and Agency Accounting Officer
26 June 2006

UK Debt Management Office Annual Accounts

Year ended 31 March 2006
Presented to Parliament 17 July 2006

Contents

Statement of Accounting Officer's Responsibilities

Under the Government Resources and Accounts Act 2000, the DMO is required to prepare resource accounts for each financial year, in conformity with an HM Treasury direction, detailing the resources acquired, held, or disposed of during the year and the use of resources by the DMO during the year.

The resource accounts are prepared on an accruals basis and must give a true and fair view of the state of affairs of the DMO, the net resource outturn, resources applied to objectives, recognised gains and losses, and cash flows for the financial year.

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 HM Treasury, including the relevant accounting and disclosure requirements, and apply suitable accounting policies on a consistent basis;
- make judgements and estimates on a reasonable basis;
- state whether applicable accounting standards, as set out in the *Government Financial Reporting Manual* have been followed, and disclose and explain any material departures in the accounts;
- prepare the accounts on a going-concern basis.

HM Treasury has appointed the Chief Executive as Accounting Officer for the DMO.

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 the DMO's assets, are set out in the Accounting Officers' Memorandum issued by HM Treasury and published in *Government Accounting*.

Statement on Internal Control

Scope of responsibility

As Accounting Officer, I have responsibility for maintaining a sound system of internal control that supports the achievement of the Debt Management Office's policies, aims and objectives, whilst safeguarding the public funds and departmental assets for which I am personally responsible, in accordance with the responsibilities assigned to me in *Government Accounting*.

I am Accounting Officer for both the Debt Management Account (DMA) and the Debt Management Office (DMO), an executive agency of HM Treasury. My accountability is subject to the overall responsibility of the Permanent Secretary of HM Treasury (in his capacity as Accounting Officer) for the organisation and management of the Department. In exercising my responsibilities for the DMA, I pay regard to the consequences for the National Loans Fund (NLF) and consult the Permanent Secretary if I consider that my actions could have implications for him in his role as NLF Accounting Officer.

CRND and PWLB are separate business entities within the DMO. Each has its own accounting officer who is responsible for maintaining a sound system of internal control that supports the delivery of the entity's agreed policies, objectives and targets. However, I am responsible for the wider DMO control framework within which both CRND and PWLB are managed, and both accounting officers take assurance from me for the continued sound maintenance of this in relation to their own control responsibilities.

In exercising my specific responsibilities for debt and cash management I take regard of the objectives set by Treasury Ministers for the Government's debt and cash management. It is my responsibility to ensure that all activities brought to account on the DMA are conducted with due regard to value for money. I have put arrangements in place to ensure that there is a proper evaluation of the balance of cost and risk in our operations, taking account where appropriate of any cost, risk or other strategic objectives, parameters or guidelines agreed with HM Treasury.

As Agency Accounting Officer I am responsible to the Chancellor and accountable to Parliament for the Agency's use of resources in carrying out its functions as set out in the Framework Document.

The purpose of the system of internal control

The system of internal control is designed to manage risk to an acceptable level, balancing the impact of potential risks with the resources required to manage them, rather than to eliminate all risk. It can therefore only provide reasonable and not absolute assurance of effectiveness. The system of internal control is based on a process designed to identify and prioritise the risks to the achievement of policies, aims and objectives, to evaluate the likelihood of those risks being realised and the impact should they be realised, and to manage them efficiently, effectively and economically.

The system of internal control has been in place in the Debt Management Office for the year ended 31 March 2006 and up to the date of approval of the annual report and accounts, and accords with HM Treasury guidance. The DMO has made additions to the system of internal control over the course of the year.

Capacilty to handle risk

The DMO has a formal risk management strategy and policy set by Managing Board. This includes an outline of the DMO's capacity to handle risk. The DMO has produced a Risk Management Assurance Strategy comprehensively documenting its risk management processes.

The DMO Managing Board is responsible for setting strategic direction and considering high-level operational issues. An executive sub-committee of the Managing Board meets weekly. The terms of reference of these management committees and those of the Cash Management, Debt Management, Fund Management and Risk Committees clearly set out their roles and responsibilities providing the organisational capability to consider issues and make relevant decisions at the appropriate level. A Programme Board met regularly during the year to review progress for all DMO projects agreed as part of the business planning process. It reported on resourcing, prioritisation and delivery issues to the Managing Board's executive sub-committee.

Staff have attended presentations on relevant elements of the DMO's risk management framework. These have covered specific issues such as anti-money laundering, whistleblowing, fraud and personal dealing in order to ensure a good level of awareness of DMO's risk policies and controls. All members of staff have job descriptions, including specific key risks they are expected to manage.

Management in each business function is responsible for ensuring that the operations within their area are compliant with plans, policies, procedures and legislation. Functional managers are responsible for maintaining compliance arrangements across the DMO in their area of specialism. Risk Management Unit has issued guidance on those sections of the Financial Services Authority handbook that are most pertinent to the DMO's business to all relevant business areas to support managers in meeting this responsibility.

The risk and control framework

The DMO has various formal mechanisms for managing the DMO's risks but it is recognised that the most important aspect is that a strong risk management culture pervades the organisation at all levels. This is embedded in both regular operations and the approach taken to new business initiatives. The DMO includes risk management considerations as part of normal business management. The DMO is making on-going efforts to embed a strong risk management culture in every part of the organisation.

The DMO's risk management strategy seeks to achieve a strong risk management culture by linking organisational objectives to the business planning process. Organisational objectives cascade down to individual objectives and job descriptions. This is intended to promote a clear understanding of the ownership of each risk within the organisation. There has been substantial progress in development of performance measures in the year, in particular for cash management operations.

Heads of business units and functional teams assess regularly whether risks to their operations are being managed effectively. New risks, and risks with an increased likelihood of occurrence, are highlighted and actions identified to ensure all risks will be effectively managed. The DMO has introduced Senior Risk Owners who undertake a cross-functional moderation process to promote better prioritisation of risks across the organisation. Project teams use risk registers to monitor and manage identified risks for each DMO project. Managing Board have reviewed during the year the high level risks that the organisation faces, and the adequacy of the relevant controls. This process is supported by the maintenance of exception logs, which identify control weaknesses and resultant actions to improve controls. Key risks and exceptions are documented in a regular report produced by the Risk Management Unit for the Risk Committee and the Managing Board.

A key component of the DMO's control framework is the segregation of duties to promote independent checking and avoid concentration of key activities or related controls in individuals or small groups of staff. In particular segregation of duties takes place between front and back office activities.

All teams have documented procedures for their main activities. The DMO has policies on anti-fraud measures and whistle blowing. In establishing controls to deter money laundering the DMO has followed best practice guidance in the Financial Services Authority's handbook and from the joint money laundering steering group. The DMO has its own anti-money laundering handbook. DMO staff provide an annual report of anti-money laundering developments and processes to the Managing Board.

The DMO's Business Continuity Plan (BCP), including disaster recovery site and other arrangements, is subject to continual review and update. The DMO tested the main elements of the BCP during the year. Assessment of business continuity requirements is a specific requirement for new projects and major business initiatives.

An independent review of the DMO's risk reporting framework was undertaken during 2005-06. Improvements to the DMO's risk reporting have been made in response to the report's recommendations, primarily a revised and more focused risk map linking detailed risks to high level risks and a more effective reporting process.

The DMO's business planning and project management processes, specifically around budgeting, approval, cost monitoring and delivery, have been strengthened in 2005-06 in response to recommendations made following an independent review. Further strengthening of controls in these areas will be implemented in 2006-07.

Improvements to financial controls and reporting were made in 2005-06 in response to recommendations made following an independent review. Further improvements and adoption of best practice will be implemented in 2006-07.

The DMO has established effective communication channels with its main stakeholders to help highlight issues that may affect either party's risks. In addition to maintaining bilateral contacts with market counterparties, the DMO also holds quarterly consultation meetings with market makers in gilts (GEMMs) and issues ad hoc public consultation documents on specific issues.

Review of effectiveness

As Accounting Officer, I have responsibility for reviewing the effectiveness of the system of internal control. My review of the effectiveness of the system of internal control is a continuous process. It is informed by the work of the executive managers within the department who have responsibility for the development and maintenance of the internal control framework, work of the internal auditors and comments made by the external auditors in their management letter and other reports. There are a number of activities that form the basis of my review. Annually I formally review the key outcomes and findings of each activity in order to make my assessment.

An Internal Controls team meets regularly to review the DMO's system of internal control, recommend actions to management and to implement changes where appropriate. The controls team comprises the Head of the DMO's Risk Management Unit, the Controls and Compliance Manager, the Head of Internal Audit and the Finance Manager. A non-Executive Director attends meetings of the team periodically. The controls team reports regularly to the Audit Committee on progress to improve the internal control system during the year.

The Managing Board met approximately every six weeks and considered risk management and operational control issues throughout the year. Additionally it received quarterly reports based on the outputs of DMO teams' risk registers on actions required as a result of changes in DMO's risk profile. The executive sub-committee of the Managing Board met weekly and considered risk and control issues on a regular basis.

The DMO's Audit Committee, comprising two non-Executive Directors, met quarterly. The Audit Committee reviews the adequacy and effectiveness of the DMO's management of risk and internal controls, and makes recommendations for improvement as appropriate.

The DMO's Internal Audit team evaluates the effectiveness of the DMO's processes for risk management, control and governance in order to provide me with an independent and objective opinion. To inform this opinion an Internal Audit strategy is produced which enables a systematic and prioritised review of the systems and controls established by management. This involves production and delivery of an annual audit plan including operational audit, project audit and provision of controls consultancy. The audit strategy is subject to review and approval by the Managing Board sub-committee and Audit Committee.

The DMO's Risk Management Unit conducts monthly controls and compliance testing, providing the executive sub-committee of Managing Board with independent assurance on the effectiveness of operational controls and compliance with relevant FSA rules in the dealing and settlements areas. Compliance testing is also a component of each operational review undertaken by Internal Audit.

In my opinion, the DMO's system of internal control was effective throughout the financial year 2005-06 and remains so on the date I sign this statement.

ROBERT STHEEMAN
Chief Executive and Agency Accounting Officer
26 June 2006

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 the UK Debt Management Office for the year ended 31 March 2006 under the Government Resources and Accounts Act 2000. These comprise the Operating Cost Statement and Statement of Recognised Gains and Losses, the Balance Sheet, the Cash Flow Statement and the related notes. These financial statements have been prepared under the accounting policies set out within them.

Respective responsibilities of the Agency, Chief Executive and Auditor

The Agency and Chief Executive are responsible for preparing the Annual 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 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 part of the Financial Statements and 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 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. I also report to you if, in my opinion, the Annual Report is not consistent with the financial statements, if the Agency 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 relevant authorities regarding remuneration and other transactions is not disclosed.

I review whether the statement on pages 28 to 31 reflects the Agency's compliance with HM Treasury's guidance on the Statement on Internal Control, and I report if it does not. I am not required to consider whether the Accounting Officer's statements on internal control cover all risks and controls, or to form an opinion on the effectiveness of the Agency'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. This other information comprises the Chief Executive's Report, the unaudited part of the Remuneration Report, and the Management Commentary. I consider the implications for my report 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 opinion

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 Agency and Chief Executive in the preparation of the financial statements, and of whether the accounting policies are most appropriate to the Agency'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.

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 Agency's affairs as at 31 March 2006 and of the surplus, 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
- 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.

I have no observations to make on these financial statements.

The maintenance and integrity of the UK Debt Management Office's website is the responsibility of the Accounting Officer; the work carried out by the auditors does not involve consideration of these matters and accordingly the auditors accept no responsibility for any changes that may have occurred to the financial statements since they were initially presented on the website.

JOHN BOURN
Comptroller and Auditor General
28 June 2006

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

Operating Cost Statement for the year ended 31 March 2006

	Note	2005-2006 £000	2005-2006 £000	2004-2005 £000
Administration costs				
Staff costs	2	5,854		4,418
Other administration costs	3	5,652		5,435
Gross administration costs		**11,506**		**9,853**
Administration income	5	(4,336)		(3,334)
Net administration costs			**7,170**	**6,519**
Gross programme costs	4	3,822		1,276
Programme income	5	(3,460)		(851)
Net programme costs			**362**	**425**
Net Operating Cost			**7,532**	**6,944**

All income and expenditure are derived from continuing operations.

Statement of Recognised Gains and Losses for the year ended 31 March 2006

	2005-2006 £000	2004-2005 £000
Net gain on revaluation of tangible fixed assets	80	7
Total recognised gains and (losses) for the financial year	**80**	**7**

The notes on pages 37 to 50 form part of these accounts.

Balance Sheet as at 31 March 2006

		2005-2006		2004-2005
	Note	£000	£000	£000
Fixed assets				
Tangible assets	6.1	737		702
Intangible assets	6.2	861		858
			1,598	1,560
Current assets				
Debtors	7	1,122		4,334
Cash at bank and in hand	8	310		371
		1,432		4,705
Creditors (amounts falling due within one year)	9	(4,447)		(4,441)
Net current (liabilities) / assets			**(3,015)**	**264**
Total assets less current liabilities			**(1,417)**	**1,824**
Creditors (amounts falling due after more than one year)	9		-	(268)
Provisions for liabilities and charges	10		(249)	(284)
			(1,666)	**1,272**
Represented by:				
Taxpayers' equity				
General Fund	11		1,753	(1,265)
Revaluation Reserve	12		(87)	(7)
			1,666	**(1,272)**

ROBERT STHEEMAN
Chief Executive and Agency Accounting Officer
26 June 2006

The notes on pages 37 to 50 form part of these accounts.

Cash Flow Statement for the year ended 31 March 2006

	Note	2005-2006 £000	2004-2005 £000
Net cash outflow from operating activities	13.1	(6,134)	(6,053)
Capital expenditure and financial investment	13.2	(500)	(841)
Net cash outflow before financing		**(6,634)**	**(6,894)**
Payment of amounts due to the Consolidated Fund		(3,466)	-
Financing	13.3	10,039	6,906
(Decrease) / increase in cash in the period		**(61)**	**12**

The notes on pages 37 to 50 form part of these accounts.

Notes to the Accounts

1 STATEMENT OF ACCOUNTING POLICIES

1.1 Basis of preparation

These financial statements have been prepared in accordance with the 2005–06 *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 that it is meaningful and appropriate to the public sector.

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

1.2 Accounting convention

These accounts have been prepared under the historical cost convention modified to account for the revaluation of fixed assets.

1.3 Administration and Programme Expenditure

The Operating Cost Statement is analysed between administration and programme income and expenditure. Administration costs reflect the cost of running the Agency. These include both administrative costs and associated operating income. Income is analysed in the notes between that which, under the administrative cost-control regime, is allowed to be offset against gross administrative costs in determining the outturn against the administration cost limit, and that operating income which is not. Programme costs reflect non-administration costs, including external settlement charges and gilt issuance costs.

1.4 Operating income

Operating income for the DMO relates to cost recoveries on a full cost basis for services provided to external clients and the direct costs when acting as an agent for the National Loans Fund. Fees received from PWLB customers and the management of the Gilt Purchase and Sale Service are set by statute.

As the Agency is subject to net administration cost control provisions, for funding purposes, HM Treasury treats operating income amounts as Appropriations-in-Aid. The operating income is principally:

- Recoveries of costs associated with the DMO acting as an agent for the National Loans Fund regarding stock listing, settlement and gilt auction advertising.
- Charges, where statute permits, for the investment management and administration of public funds by the Commissioners for the Reduction of the National Debt.
- Fees for loans advanced to local authorities from the Public Works Loan Board.
- Fees for secondary market purchase and sale transactions in gilts conducted by members of the public, under a DMO managed contract with Computershare.

1.5 Fixed Assets

Assets acquired for on-going use with a purchase cost in excess of £5,000 are capitalised. All assets acquired on an individual basis for on-going use falling above this threshold will be shown as fixed assets.

Fixed assets are revalued each year to the net current replacement cost by reference to appropriate indices issued by HM Treasury and prepared by the Valuation Office. Revaluation surpluses arising from temporary changes in value are credited to the revaluation reserve. Permanent diminutions in value are charged to the Operating Cost Statement, except to the extent that a revaluation surplus exists in respect of the same asset.

Profits or losses arising on the disposal of fixed assets are calculated by reference to the carrying value of the asset.

Internal staff costs for IT development work are capitalised as tangible assets when a distinct asset for on-going use is created or significantly developed.

Software purchases that meet the capitalisation criteria are classified as intangible assets.

1.6 Depreciation

Depreciation is provided on a straight-line basis, calculated on revalued amounts to write off assets over their estimated useful lives. The useful lives of fixed assets have been estimated as follows:

- IT equipment and software — 3 years
- Development costs — 3 years
- Office and other non IT equipment — 5 years
- Furniture, fixtures and fittings — 10 years
- Licence software — license duration up to 10 years
- Leasehold improvements — lesser of 10 years or outstanding lease term

1.7 Operating leases

Amounts paid and received under the terms of operating leases are charged to the Operating Cost Statement on a straight-line basis over the term of the lease. Operating leases are accounted for in accordance with SSAP 21. The DMO's commitments and receivables are disclosed in Note 14.

1.8 Notional charges

Central HM Treasury costs and other overheads are charged on a notional basis and included in the accounts. These charges include auditors' remuneration and centrally provided support services for payroll, procurement, finance, security, health and safety and legal services. Notional costs are charged to the Operating Cost Statement and credited as a movement on the general fund.

1.9 Value added tax

Value added tax (VAT) on purchases, to the extent that it is irrecoverable, is charged to the Operating Cost Statement included under the heading relevant to the type of expenditure. Where VAT is recoverable in respect of DMO expenditure, it is recovered by HM Treasury and is not refunded to the DMO. Where output tax is charged or input tax is recoverable, the amounts are stated net of VAT.

1.10 Capital charge

A charge reflecting the cost of capital utilised by the Agency is included within the Operating Cost Statement. The charge is calculated at the real rate set by HM Treasury, currently 3.5 per cent on the average carrying amount of all assets less liabilities.

1.11 Pensions

Past and present employees are covered by the provisions of the Principal Civil Service Pension Schemes (PCSPS) which are described in Note 2. The defined benefit schemes are unfunded and are non-contributory except in respect of dependants' benefits. The Agency 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, the Agency recognises the contributions payable for the year.

1.12 Provisions

The Agency provides for legal or constructive obligations, which are of uncertain timing or amount at the balance sheet date on the basis of the best estimate of the expenditure required to settle the obligation. Where the effect of the time value of money is significant the estimated risk-adjusted cash flows are discounted using the HM Treasury discount rate of 2.2 per cent in real terms.

2 STAFF NUMBERS AND RELATED COSTS

2.1 Aggregate staff costs comprise:

	2005-2006			2004-2005
	TOTAL	Permanent Staff	Others	
	£000	£000	£000	£000
Wages and salaries	4,768	3,989	779	4,272
Social security costs	375	375	-	351
Other pension costs	771	771	-	549
Sub Total	**5,914**	**5,135**	**779**	**5,172**
Inward secondees	24	24	-	12
Total Net Costs *	**5,938**	**5,159**	**779**	**5,184**

* Of the total, £84,437 (2004-05: £766,281) has been charged to capital.

The Principal Civil Service Pension Schemes (PCSPS) to which all of the Agency's employees are members is an unfunded multi-employer defined benefit scheme, but the DMO is unable to identify its share of the underlying assets and liabilities. The scheme Actuary (Hewitt Bacon Woodrow) valued the scheme as at 31 March 2003 and details can be found in the resource accounts of the Cabinet Office: Civil Superannuation (www.civilservice-pensions.gov.uk).

For 2005–06, normal employer contributions of £737,913 were payable to the PCSPS (2004–05 £500,891) at one of four rates in the range 16.2 to 24.6 per cent (2004-05: 12 to 18.5 per cent) of pensionable pay, based on salary bands. The scheme's Actuary reviews employer contributions every four years following a full scheme valuation. From 2006-07, the salary bands will be revised and the rates will be in a range between 17.1% and 25.5%.

The contribution rates are set to meet the costs of the benefits accruing during 2005-06 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. Employer's contributions of £33,110 (2004-05: £20,411) were paid to one or more of the panel of four appointed **stakeholder** pension providers. Employer contributions are age-related and range from 8 to 11.5 per cent (2004-05: 8 to 10 per cent) of pensionable pay. Employers also match employee contributions up to 3 per cent of pensionable pay. In addition, employer contributions of £1,803, 0.8 per cent of pensionable pay (2004-05: £1,370, 0.8 per cent), 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 £4,784 (2004-05 restated: £4,721). Contributions prepaid at that date were nil.

2.2 The average number of whole-time equivalent persons employed by the DMO during the year was as follows:

		2005-2006			2004-2005
	TOTAL £000	Senior Management £000	Officials £000	Agency, temporary, and contract staff £000	Total £000
Maintaining sound public finances in accordance with the Code for Fiscal Stability	**79**	3	70	6	75
Staff engaged on capital projects	**1**	-	-	1	9
TOTAL	**80**	**3**	**70**	**7**	**84**

3 OTHER ADMINISTRATION COSTS

	2005-2006 £000	2004-2005 £000
Rentals under operating leases:		
Other operating leases	1,164	1,131
Non-cash items (Note a):		
Depreciation and amortisation of fixed assets	594	765
Deficit on revaluation	344	121
Cost of capital charge	25	48
Auditor's fee	21	21
Loss on disposal	-	7
Provision for early-departure costs:		
Provided in year	8	(18)
Unwinding of discount on provisions	15	9
Other expenditure (Note b)	3,481	3,351
	5,652	**5,435**

Notes:

a

Other administration costs – non-cash items (as above)	1,007	953

b

Accommodation related costs	580	482
Consultants & professionals	576	768
IT & telecommunications	1,697	1,415
Travel, subsistence & hospitality	88	85
Legal services	78	64
Training	104	139
Printing & stationery	56	79
Other costs	302	319
	3,481	**3,351**

Rentals under operating leases include £1,129,541.60 for rent on building.

The auditor's fee relates entirely to audit work.

4 PROGRAMME RELATED COSTS

	2005-2006 £000	2004-2005 £000
Settlement and custodial charges	580	465
Stock Exchange listing fees	598	593
Auction advertising costs	178	169
Gilt Syndication fees	2,187	-
DMO Gilt Purchase & Sale Service costs	188	36
Other trading costs	91	13
	3,822	**1,276**

Programme related costs are costs that the DMO must incur as a result of trading and other dealing activities and are not directly controllable. They relate primarily to stock listing, settlement, auction advertising and other trading fees. Where the DMO is acting as agent for the NLF regarding these transactions, these costs are reimbursable.

5 OPERATING INCOME

	2005-2006		2004-2005
	£000	£000	£000
Administration income			
Recharges to GEMMS	91		96
Rentals receivable in respect of operating leases	226		226
Other accommodation related income	47		43
Fees and charges to CRND clients	852		1,008
Fees and charges to PWLB customers	3,087		1,891
Other income	33		70
		4,336	**3,334**
Programme related income			
Recharges to the National Loans Fund	2,963		762
DMO Gilt Purchase & Sale Service commission	495		86
Bank interest	2		3
		3,460	**851**
Total income		**7,796**	**4,185**

Recharges to GEMMS relate to trading system costs.

All rentals receivable in respect of operating leases are from external clients.

Recharges to the National Loans Fund relate to gilt issuance charges.

Income that is surrenderable to the Consolidated Fund in the period comprises Bank of England interest received in the year amounting to £2,173.04 (2004-05 £2,512.95) and excess Appropriations-in-Aid made up from Administration and Programme related income amounting to £2,485,809.15 (2004-05 £3,334,367.93).

Analysis of Fees and Charges Income for the year ended 31 March 2006

This analysis is provided for the purposes of those services that attract fees and charges and not for the disclosure requirements under SSAP 25.

Financial objective:

- **CRND**: To invest and manage certain public funds and charge, where statute permits, an administrative cost calculated on a full-cost recovery basis. CRND also carries out other miscellaneous statutory functions for which there is no provision for recovering costs.
- **PWLB**: To advance loans, primarily to local authorities, at a fee rate that is set by statute and designed to cover the cost of examining applications for loans, making advances and maintaining accounts.
- **DMO Gilt Purchase & Sale Service**: To operate a gilt purchase and sale service for retail investors in the secondary market and charge the appropriate transactional cost as defined by statute.

Analysis of Net Operating Cost

	CRND £000	PWLB £000	DMO Gilt Purchase & Sale Service £000
Full cost	1,014	1,097	702
Income	(852)	(3,087)	(495)
(Surplus) / deficit	**162**	**(1,990)**	**207**

Performance against the financial objective:

- **CRND**: Achieved in full, by continuing to provide a cost-effective service.
- **PWLB**: Achieved in full.
- **DMO Gilt Purchase & Sale Service**: Achieved in full.

6 FIXED ASSETS

6.1 Tangible Fixed Assets

	Leasehold Improvements £000	IT £000	Telecoms £000	Office Equipment £000	Total £000
Cost or valuation					
At 1 April 2005	765	2,398	154	23	3,340
Additions	-	323	-	-	323
Disposals	-	(40)	-	-	(40)
Revaluation	80	(120)	(8)	-	(48)
At 31 March 2006	**845**	**2,561**	**146**	**23**	**3,575**
Depreciation					
At 1 April 2005	(301)	(2,186)	(141)	(10)	(2,638)
Charged in year	(76)	(224)	(13)	(4)	(317)
Disposals	-	40	-	-	40
Revaluation	(40)	109	8	-	77
At 31 March 2006	**(417)**	**(2,261)**	**(146)**	**(14)**	**(2,838)**
Net Book Value					
At 31 March 2006	**428**	**300**	**-**	**9**	**737**
At 31 March 2005	**464**	**212**	**13**	**13**	**702**

Capitalised staff development costs of £NIL (2004-05 £217,038) are included in the tangible assets figure.

6.2 Intangible Fixed Assets

	Software £000
Cost or valuation	
At 1 April 2005	2,254
Additions	573
Disposals	(5)
Revaluation	(217)
At 31 March 2006	**2,605**
Amortisation	
At 1 April 2005	(1,396)
Charged in year	(499)
Disposals	5
Revaluation	146
At 31 March 2006	**(1,744)**
Net Book Value	
At 31 March 2006	**861**
At 31 March 2005	**858**

7 DEBTORS

7.1 Analysis by Type

	2005-2006 £000	2004-2005 £000
Amounts falling due within one year:		
Prepayments and accrued income	782	596
Amounts receivable from the NLF	222	351
Other trade debtors	109	284
Receivable from the Consolidated Fund		
Supply not yet drawn	-	3,084
	1,113	**4,315**
Amounts falling due after more than one year:		
Prepayments and accrued income	9	19
	1,122	**4,334**

7.2 Intra-Government Balances.

	Amounts falling due within one year		Amounts falling due after more than one year	
	31 March 2006 £000	31 March 2005 £000	31 March 2006 £000	31 March 2005 £000
Intra-government balances: Balances with other central government bodies	237	3,518	-	-
Balances with bodies external to government	876	797	9	19
Total debtors at 31 March	**1,113**	**4,315**	**9**	**19**

8 CASH AT BANK AND IN HAND

	2005-2006 £000	2004-2005 £000
Balance at 1 April	371	359
Net change in cash balances	(61)	12
Balance at 31 March	**310**	**371**

9 CREDITORS

9.1 Analysis by Type

	2005-2006 £000	2004-2005 £000
Amounts falling due within one year:		
Trade creditors	657	215
Taxation and Social Security creditors	195	172
Accruals and deferred income	926	687
Deposit advance held as a creditor bond	268	-
Creditor bond interest	41	30
Payable to the Consolidated Fund:		
Excess appropriations-in-aid	2,358	3,334
Other payments due to be paid to the Consolidated Fund	2	3
	4,447	**4,441**
Amounts falling due after more than one year:		
Deposit advance held as a creditor bond	-	268
	4,447	**4,709**

9.2 Intra-Government Balances

	Amounts falling due within one year		Amounts falling due after more than one year	
	31 March 2006 £000	31 March 2005 £000	31 March 2006 £000	31 March 2005 £000
Intra-government balances: Balances with other central government bodies	2,584	3,559	-	-
Balances with bodies external to government	1,863	882	-	268
Total creditors at 31 March	**4,447**	**4,441**	**-**	**268**

10 PROVISIONS FOR LIABILITIES AND CHARGES

	2005-2006 Early departure costs £000	2004-2005 Early departure costs £000
Balance at 1 April 2005	284	466
Provided in the year	8	(18)
Provisions utilised in the year	(58)	(173)
Unwinding of discount	15	9
Balance at 31 March 2006	**249**	**284**

Early departure costs

The Agency meets the additional costs of benefits beyond the normal PCSPS benefits in respect of employees who retire early by paying the required amounts annually to the PCSPS over the period between early departure and normal retirement date. The Agency provides for this in full when the early retirement programme becomes binding by establishing a provision for the estimated payments discounted by the HM Treasury discount rate of 2.2 per cent in real terms.

11 GENERAL FUND

Reconciliation of Net Operating Cost to changes in General Fund

	2005-2006 £000	2004-2005 £000
Balance at 1 April	(1,265)	(1,485)
Net Parliamentary Funding		
Drawn Down	(6,955)	(9,992)
Net transfer from Operating Activities		
Net operating cost	7,532	6,944
CFERs repayable to the Consolidated Fund	2,487	3,337
Non-cash charges		
Cost of Capital	(25)	(48)
Auditors' Remuneration	(21)	(21)
Balance at 31 March	**1,753**	**(1,265)**

12 REVALUATION RESERVE

	£000
Balance at 1 April 2005	(7)
Movement on revaluation during the year	(80)
Balance at 31 March 2006	(87)

13 ANALYSIS OF CASH FLOW

13.1 Reconciliation of Operating Costs to Operating Cash Flows:

	2005-2006		2004-2005
	£000	£000	£000
Net operating cost		(7,532)	(6,944)
Adjust for non-cash transactions:			
Depreciation	594		765
Notional interest on capital	25		48
Auditor's fee	21		21
Other	344		128
Provision for early-departure costs	23		(9)
		1,007	953
Adjust for movement in working capital other than cash:			
Decrease / (increase) in debtors	128		53
Increase / (decrease) in current creditors	715		166
Less items not passing through the Operating Cost Statement	(394)		(108)
Use of provisions	(58)		(173)
		391	(62)
Net cash outflow from operating activities		**(6,134)**	**(6,053)**

13.2 Analysis of capital expenditure:

	2005-2006	2004-2005
	£000	£000
Tangible fixed asset additions	(46)	(298)
Intangible fixed asset additions	(454)	(543)
Net cash outflow from investing activities	**(500)**	**(841)**

13.3 Analysis of financing:

	2005-2006	2004-2005
	£000	£000
From Consolidated Fund (Supply) – current year	6,955	6,908
From Consolidated Fund (Supply) – prior year	3,084	(2)
Net financing	**10,039**	**6,906**

14 OPERATING LEASES

14.1 At 31 March 2006 the commitments under operating leases to pay rentals during the year following the year of these accounts are shown below, analysed according to the period in which the lease expires:

	2005-2006			2004-2005
	Land and Buildings £000	Other £000	Total £000	Total £000
Operating leases which expire beyond one year but not more that five years	-	37	37	12
Operating leases which expire beyond five years:				
premises lease	1,130	-	1,130	1,116
	1,130	**37**	**1,167**	**1,128**

14.2 At 31 March 2006 receivables under operating leases were as follows:

	2005-2006	2004-2005
	Land and Buildings £000	Total £000
Operating leases which expire within one year:		
premises lease	114	-
Operating leases which expire beyond one year but not more that five years:		
premises lease	-	226
	114	**226**

15 CAPITAL COMMITMENTS

The DMO has no capital commitments at 31 March 2006.

16 CONTINGENT LIABILITIES DISCLOSED UNDER FRS 12

The DMO has no contingent liabilities at 31 March 2006.

17 RELATED PARTY TRANSACTIONS

The DMO is an executive agency of HM Treasury. During the year HM Treasury has provided various business services to the DMO as listed in the Resources section of the Annual Report.

The Consolidated Fund and the National Loans Fund are central government borrowing and expenditure accounts under the control of HM Treasury. The DMO has had transactions with both accounts and they are regarded as related parties because they are under common control of HM Treasury.

The DMO also has undertaken various transactions with the Bank of England and National Savings and Investments. They are regarded as related parties because HM Treasury has significant influence over all entities.

CRND is managed as part of the DMO but is a separate legal entity. CRND is a related party of DMO because Jo Whelan is the Deputy Chief Executive of the DMO and also the Comptroller of CRND.

PWLB is also operated within the DMO and subjected to the same operational controls as applied to the DMO's operations as a whole, but charges to PWLB clients are set by statute and the Public Works Loan Commissioners retain their statutory role. Therefore, PWLB is not considered a related party to the DMO.

None of the DMO Managing Board members, senior managers or other related parties has undertaken any material transactions with the DMO during the year.

18 FRS13 DISCLOSURES

Excluding the Debt Management Account, the PWLB lending facility and the CRND Investment Accounts (which are reported separately from its administrative expenditure) the DMO agency account has no material exposure to liquidity risk, interest rate risk or currency risk. The DMO agency account does not have any borrowings, deposits or foreign currency positions. All material assets and liabilities are denominated in sterling.

Accounts Direction given by HM Treasury in accordance with section 7(2) of the Government Resources and Accounts Act 2000

1. This direction applies to the United Kingdom Debt Management Office.

2. This executive agency shall prepare accounts for the year ended 31 March 2006 in compliance with the accounting principles and disclosure requirements of the edition of the *Government Financial Reporting Manual (FReM)* issued by HM Treasury which is in force for 2005-06.

3. The accounts shall be prepared so as to:

   3.1 give a true and fair view of the state of affairs as at 31 March 2006 and of the income and expenditure (or as appropriate, net resource outturn), total recognised gains and losses (or, as appropriate, recognised gains and losses), and cash flows of the agency for the financial year then ended; and

   3.2 provide disclosure of any material expenditure or income that has not been applied to the purposes intended by Parliament or material transactions that have not conformed to the authorities which govern them.

4. Compliance with the requirements of the *FReM* will, in all but exceptional circumstances, be necessary for the accounts to give a true and fair view. If, in these exceptional circumstances, compliance with the requirements of the *FReM* is inconsistent with the requirement to give a true and fair view the requirements of the *FReM* should be departed from only to the extent necessary to give a true and fair view. In such cases, informed and unbiased judgement should be used to devise an appropriate alternative treatment, which should be consistent with both the economic characteristics of the circumstances concerned and the spirit of the *FReM*. Any material departure from the *FReM* should be discussed in the first instance with HM Treasury.

DAVID CRUDEN FCA
Head of the Central Accountancy Team, Her Majesty's Treasury
13 January 2005

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