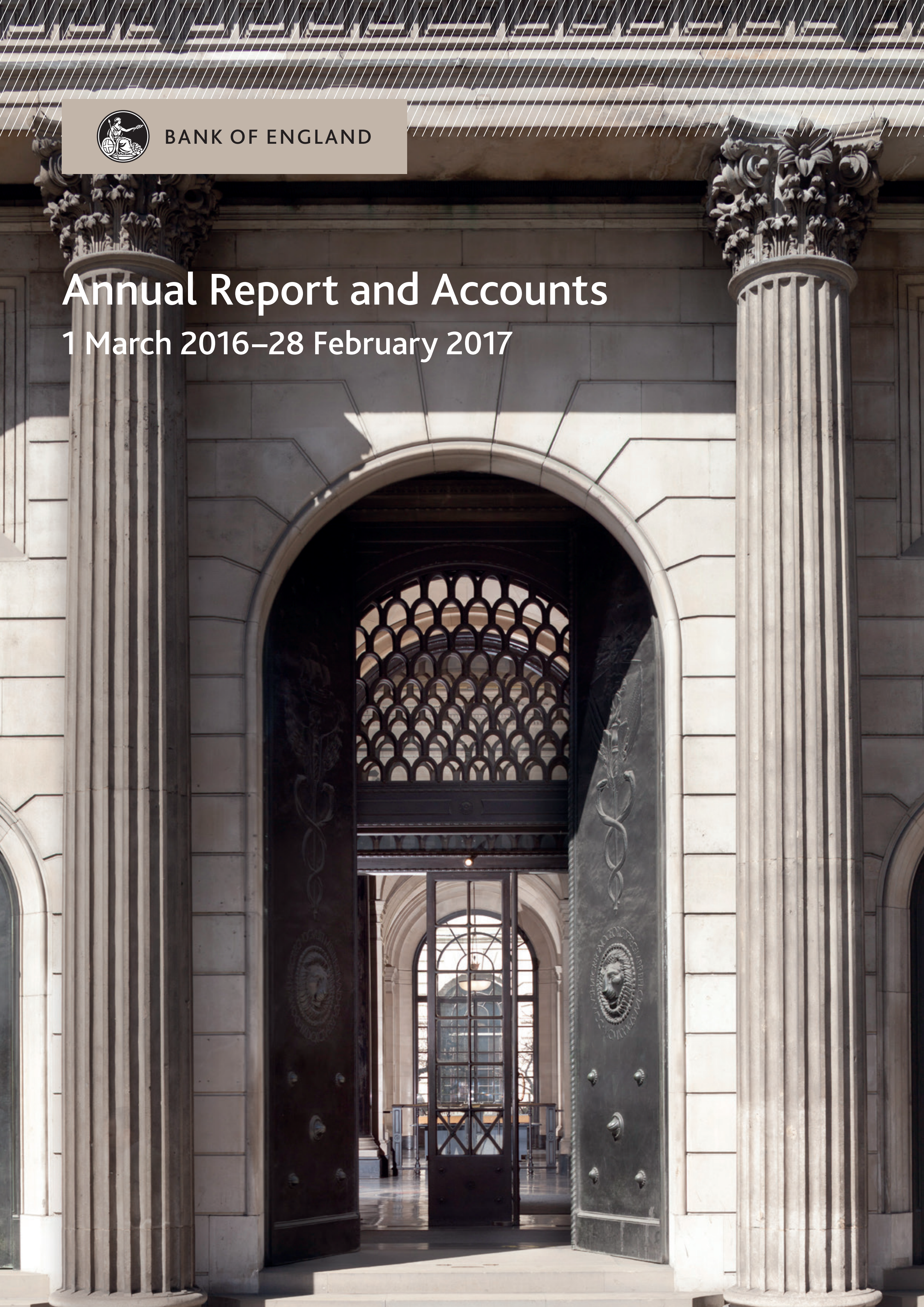
BANK OF ENGLAND

Annual Report and Accounts

1 March 2016–28 February 2017



Bank of England

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1 March 2016 to 28 February 2017

Presented to Parliament by the Chief Secretary to the Treasury
by Command of Her Majesty

The contents of this Report encompass the requirements of Section 4 of the Bank of England Act 1998, and include: (1) a report by the Court of Directors (Court) on the matters which it reviews, monitors or otherwise considers in the performance of its oversight functions (S4(2)(a)); (2) a report by Court on the activities of the Financial Policy Committee of the Bank (S4(2)(aa)); (3) a copy of the statement for the year prepared under section 7(2) and the report of the Bank's auditors on it; (4) a statement of the rates at which Non-executive Directors of the Bank have been remunerated (S4(4)(a)); and (5) a statement of the Bank's objectives and strategy for the next year, as determined by Court (S4(4)(b)).

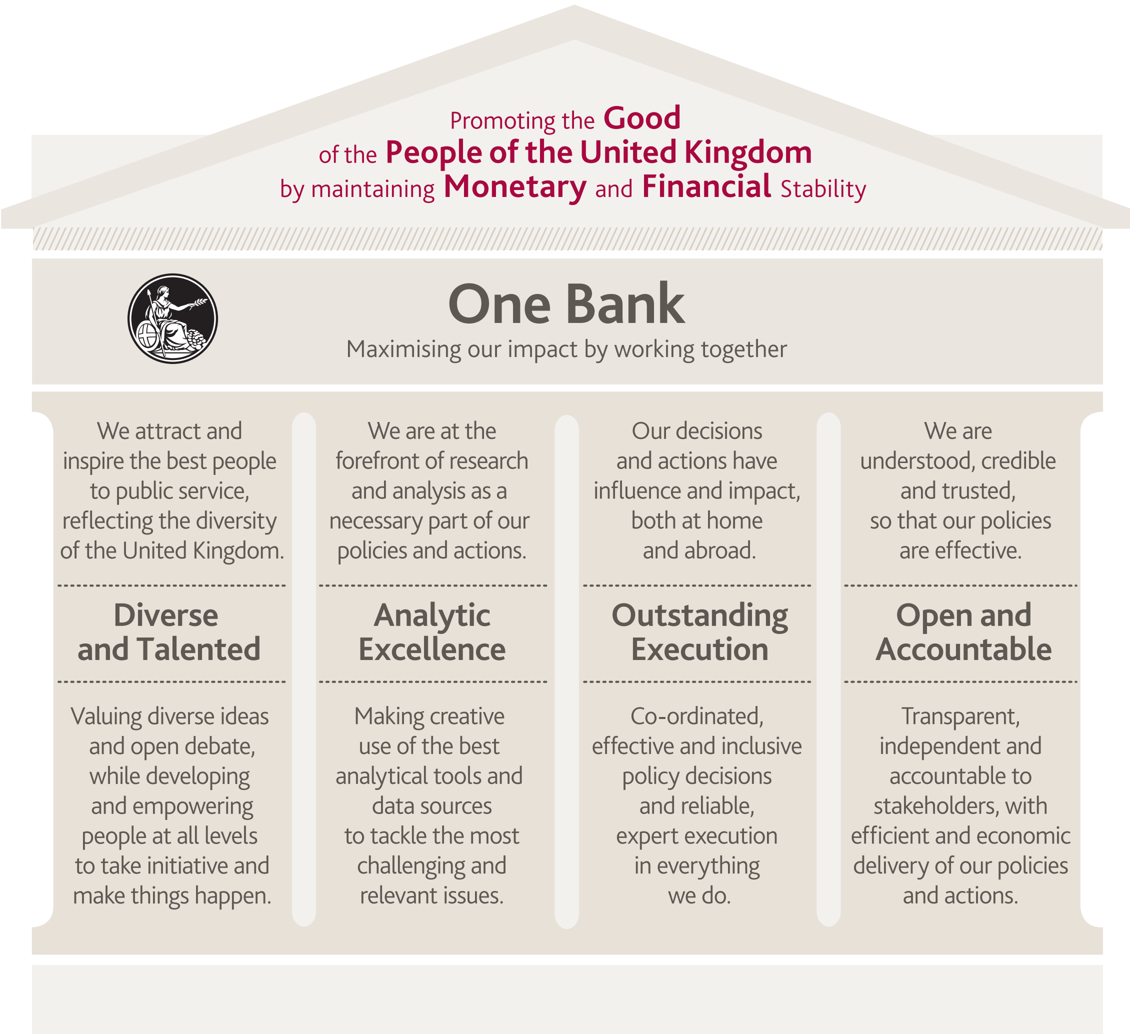
The Prudential Regulation Authority has published a separate report as required by paragraph 19 of Schedule 1ZB of the Financial Services and Markets Act 2000, and in accordance with the requirements of the Companies Act 2006.

The Bank has also published a separate report, as required by section 203B of the Banking Act 2009 and paragraph 33 of Schedule 17A of the Financial Services and Markets Act 2000, on its supervision of financial market infrastructures.

Contents

One Mission, One Bank

The Bank of England's mission is to promote the Good of the People of the United Kingdom by maintaining Monetary and Financial Stability.



Statement by the Chair of Court

Anthony Habgood
Chair of Court

Three years ago, the Bank launched the One Bank strategy to deliver the synergies between monetary policy, macroprudential policy and microprudential supervision. The past twelve months have continued to see that strategy come to fruition.

The implementation of the One Bank strategy was underpinned by the changes brought about by the Bank of England and Financial Services Act 2016. As of 1 March 2017, following the Act's final implementation, the three main committees of the Bank — the MPC, FPC and PRC — now enjoy the same statutory footing. The Act has also streamlined and reinforced the work of the Court as the Bank's unitary Board, with a firm focus on ensuring the professional management of a world-class institution.

The resulting benefits of the One Bank approach have been evident across the organisation. This includes our joint work — led by the policy committees — on priority areas such as stress testing and banking resilience. An example during the year was the work to support monetary and financial stability in the run-up to, and the immediate aftermath of, the United Kingdom's vote to leave the European Union.

The One Bank strategy has rightly prioritised investment in the Bank's most important asset — its people. The institution has seen material improvements in its approach to reward, recruitment and retention, in talent management, in succession planning and in measures taken to encourage diversity in all its forms. But while much has been done, challenges remain. For example, while it is encouraging to see increases in the proportion of female managers and of managers from an ethnic minority background, more needs to be done if the Bank is to succeed in meeting its 2020 diversity targets, particularly at senior levels.

The first phase of the strategy emphasised the need for 'Outstanding Execution' — that is, reliable, world-class execution in all that the institution does. That was exemplified in the comprehensive, highly effective and detailed contingency planning carried out by the Bank in the run-up to the referendum on EU membership, and in the professionalism of the institution's response immediately following the 'leave' vote. The co-ordination between the policy committees of the Bank during this period was unprecedented.

The policy work of the Bank is not the only area that has benefited from reliable, professional execution. In cyber security, for example, the Bank's investments in expertise and in professional standards have considerably strengthened the organisation's defences. But, in a fast-moving environment, no institution can afford to stand still. And the Bank needs to continue to raise its game if it is to keep pace with the evolving nature of the threat.

Much of the Bank's success stems from its deserved reputation for analytical excellence. The Bank has continued to invest in this area over the past three years, not least with the development of the One Bank Research Agenda and the launch of the Research Hub. Those investments have begun to reap rewards, including the notable rise in the Bank's research ranking.

Investment in data capability and expertise has been another analytical priority. While there has been clear progress here, it has not been without its difficulties, not least that the transformation has proved to be more complex, and more time-consuming, than initially envisaged. In this area, as in a number of others at the Bank, it is crucial that the institution continues to equip its managers with the professional skills they need.

Openness and accountability is essential to maintain the public trust that the Bank needs if it is to fulfil successfully its mission. And both Court, and the Bank more widely, continue to seek out opportunities to bolster transparency and trust. They are assisted in this by the Bank's Independent Evaluation Office (IEO), established in 2014 as part of the first phase of the Bank's Strategic Plan. The IEO has published two further reports on the work of the Bank during the year, covering FMI supervision and the PRA's insurance objective.

Sustained success in any organisation begins and ends with its values. The Bank rightly holds itself to the highest standards of ethics and probity, and Court has consistently taken decisive action on the occasions when it has appeared that these standards were not adhered to.

The Bank self-referred to the Serious Fraud Office (SFO) in late 2014 when internal investigations raised questions about the conduct of the emergency liquidity auctions held in 2007–08. I am pleased to report that on 23 June 2017 the SFO closed its subsequent investigations, concluding that 'there is no evidence of criminality in relation to this matter'. Separately, the Bank has assisted ongoing investigations into the Libor interest rate benchmark.

The past year has seen a number of changes in the Bank's leadership. In late 2016, Dame Minouche Shafik resigned her post as Deputy Governor of Markets and Banking to take up the position of Director of the London School of Economics. On behalf of Court, I would like to thank Dame Minouche for her service to the institution as well as to her valuable contribution to cultural change — both within the Bank, and within the financial services industry through her leadership of the Fair and Effective Markets Review. I wish her every success in her new role.

Subsequently, and with regret, we saw the resignation of Charlotte Hogg, the Bank's Chief Operating Officer (COO) who, in early 2017, had been approved as Dame Minouche's successor. During her time as COO, Ms Hogg made an enormous contribution to the Bank and to the One Bank strategy, including by leading much-needed change right across the business's operational areas. The events that led to her resignation turned on incomplete compliance with the Bank's Code of Conduct, and Court is reviewing the lessons.

All successful organisations need to maintain productive relationships with their key stakeholders. And I would like to thank colleagues at Her Majesty's Treasury for their continued support of the Bank's work. I would also like to thank Andrew Tyrie, the former Chair of Parliament's Treasury Committee, for his leadership of the Committee during what has been an extraordinary period for the UK economy and financial system, as well as for his lasting contribution to the reform of banking standards.

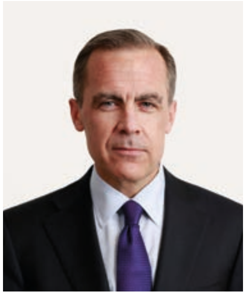
The past few months have not only seen the conclusion of the first phase of the Bank's Strategic Plan; they have seen the commencement of the next phase in the form of Vision 2020. This will focus on a set of important initiatives for change grouped together under the banners of 'How We Work' and 'How We Communicate'. More generally, Vision 2020 will continue the drive for higher professional and managerial standards, essential if the institution is to enhance its reputation as a world-class, modern, central bank.

I look forward to continuing to work alongside the Governor and other Bank colleagues in support of these priorities, and, more broadly, in support of the Bank's continuing mission to promote the public good by maintaining monetary and financial stability.

Anthony Habgood.

26 June 2017

Report by the Governor



Mark Carney
Governor

During an eventful year of great change, the Bank has remained focused on delivering its mission to promote the good of the people of the United Kingdom by maintaining monetary and financial stability.

We have now completed our One Bank Strategic Plan. The dedication, buy-in and hard work of colleagues has ensured that we have met 95% of its targets. Such outstanding execution has meant that the Bank is more open and accountable, diverse and talented, and effective and insightful.

The benefit of working as One Bank was clearly evident in the events surrounding the referendum on the United Kingdom's membership of the European Union (EU). Across all of our policy responsibilities, we worked together to meet our policy objectives. Many colleagues worked tirelessly in the run-up to the vote to prepare for every contingency. They pooled knowledge, resources, and skills from across the organisation. The Bank catalysed contingency planning within the private financial sector and worked with overseas authorities to ensure necessary policy measures could be co-ordinated as needed. Such contingency planning supported orderly market functioning in the immediate aftermath of the referendum despite extraordinary volatility in the prices of many UK assets.

In the weeks that followed the referendum the Bank first assessed economic conditions and risks and then responded with appropriate monetary and macroprudential policy measures. The Financial Policy Committee acted quickly to reduce the countercyclical buffer rate on banks' UK exposures, raising banks' capacity to lend to UK businesses and households by up to £150 billion. The Monetary Policy Committee delivered a timely, coherent and comprehensive package of easing measures that lowered the cost of credit and improved financial conditions for households and businesses during a period of uncertainty. These initiatives provided significant support to the UK economy as it began its transition to a new arrangement with the EU.

While the referendum was a major event, there has been much more to our year.

The New Fiver marked a major milestone. Physical money has been around in one form or another for more than 3,000 years. For over 300 years, the Bank has issued paper banknotes. Polymer marks a new era. The New Fivers are cleaner, safer and stronger than their paper predecessors, as well as more environmentally friendly.

The new banknotes generated intense interest. Over a million people have viewed the New Fiver website; 300,000 people viewed the informational video on YouTube; and we engaged with almost 14,000 people on our regional roadshows. By the time of the launch nine out of ten people were aware of the New Fiver.

As an open and accountable central bank, we strive continually to address the issues that are important to the public we serve. That is why, when we discovered that a trace amount of tallow was used to produce our new £5 pound note, we spoke to a range of groups to understand their concerns more fully. We undertook detailed analysis with our suppliers to consider potential solutions. Weighing all considerations, we concluded that it would be appropriate to keep the new £5 polymer note in circulation and to issue the £10 polymer note as planned. Before making any decisions on future production runs of £5 and £10 and the new £20 note, the Bank will evaluate opinions expressed in our public consultation on relative merits of animal-derived products and plant-based alternatives in our notes.

It is not only the components of, but also the characters on our notes that are now shaped by public input. Three years ago, the Bank committed to making its character selection process more open and transparent. We created the Banknote Character Advisory Committee of external experts who decided the new £20 should feature an eminent contributor from the field of visual arts. The Bank then invited the public to make nominations in this field.

The response was exceptional and demonstrated not only the depth of achievement of British art but also the public's passion for it. We received almost 30,000 individual suggestions, between them nominating 590 different characters from sculptors to filmmakers. The Committee used their expertise, supplemented with views from public focus groups, and whittled down the nominations to a shortlist of five characters who had made an unquestioned, enduring contribution to the visual arts, as well as a wider contribution to British society. In April last year, at the British seaside in Margate, we announced that J.M.W Turner met all these criteria and would feature on the new £20 in a striking design that captures his famous words 'light is therefore colour'.

Our design work extended beyond banknotes to making the financial system safer, simpler and fairer.

The system is safer because banks are now much more resilient. Capital requirements for the largest global banks are ten times higher than before the crisis and a new leverage ratio guards against risks that may seem low but prove not. This year, we completed our third concurrent stress test which showed that the banking system is, in aggregate, capitalised to support the real economy in a severe, broad and synchronised global stress scenario. And the Bank is continuing to develop its stress-testing framework: in 2017, it will examine an 'exploratory scenario' to consider how the UK banking system might evolve if recent headwinds to bank profitability persist or intensify.

The system is also safer because of the G20's efforts to reduce systemic risks by encouraging greater use of central counterparties (CCPs) to clear standardised derivatives transactions. CCPs reduce the risk of contagion to the financial system from the failure of individual institutions, as well as by making derivatives markets themselves more robust. The overall effect on systemic risks depends on the resilience and resolvability of CCPs themselves. Over the past year, therefore, the Bank has played a leading role in international efforts to enhance the resilience, recovery and resolution of CCPs.

The financial system is simpler. As banks have become less complex and more focused, they are lending more to households and businesses and less to each other. We are focused on eliminating toxic and fragile forms of shadow banking while reinforcing the best of resilient market-based finance. In prudential regulation we have focused closely on the implementation of ring-fencing, to ensure banks are structured to limit contagion of risks across entities. This project remains on track to implement changes by 2019 as planned.

The financial system is fairer. A decade ago, large complex banks operated in a 'heads I win, tails you lose' bubble. They privatised profits in the run-up to the crisis before socialising the losses when the music stopped. To bring back the discipline of the market and to end reliance on public funds, standards have now been agreed to ensure that major banks can fail safely in future. In particular, banks will be required to hold sufficient debt in life such that, in the event one fails, its successor can be recapitalised to support the continued operation of its most important activities.

To that end, last year following a public consultation we published our policy on setting the 'Minimum requirement for own funds and eligible liabilities' (MREL). As a result of these measures, estimates of the 'too big to fail' public subsidy for private systemic banks have fallen by around 90% in the United Kingdom.

Prevention is still better than the cure, so we are also addressing the root causes of a torrent of misconduct. In partnership with the Financial Conduct Authority, we have introduced measures to ensure firms and their employees take responsibility — individually and collectively — for their own conduct. These range from securing compliance with minimum standards to a common and dynamic understanding of good practice that is widely understood and collectively enforced through the Senior Managers Regime.

Delivering these considerable projects requires a robust and high-performing organisation.

Three years ago we made Diverse and Talented a central pillar of our One Bank Strategic Plan. It was the right thing to do. Diversity helps to build the trust we need to deliver our remits, and it leads to more creative thinking. We aim to have 35% female staff in our senior roles by 2020, and want to increase the proportion of our employees who are Black, Asian or Minority Ethnic (BAME) to 13% by 2022. Across the remainder of our staff, we have set a target of 50% female, and 20% BAME by 2020.

To increase our diversity, we are seeking to make the Bank a more obvious career destination for a wide range of recruits from young school leavers to experienced professionals.

In our last graduate round, we hired from over 40 UK universities (four times as many as a decade ago). Two fifths of the 2016 intake were female and a quarter came from a BAME background. Only half took economics with the remainder studying for science, business and the humanities degrees.

To recruit a more diverse range of experienced hires, we have committed to creating diverse shortlists and interview panels wherever possible in order to mitigate affinity effects and unconscious biases. This is starting to pay off. Of the 700 experienced professionals we hired last year, almost half were women and a quarter came from a BAME background.

We recognise that career paths can be varied, so for people who want to return to work or to retrain, we are offering more opportunities to learn. Around 200 of our colleagues studied for degrees or professional qualifications in 2016 and 675 re-skilled through internal job moves across directorates.

It is not enough for the Bank to reflect diversity, however, we need also to choose inclusion in order to unlock the true value of a diverse workforce. That is why in February we launched our Inclusion Strategy to build a culture that values diverse ideas, encourages open debate, and empowers people at all levels to take initiative.

Inclusion empowers people to speak up, it helps us to learn and continually improve. It is in this spirit that in 2017 we launched our new Strategic Plan — Vision 2020.

Vision 2020 will reinforce and build on the successes of our One Bank strategy by transforming 'How We Work' and 'How We Communicate' in order to maximise our potential so that together we can deliver the best policies for the good of the people of the United Kingdom.

In shaping Vision 2020, we listened to colleagues through a series of workshops, lunches, informal gatherings and surveys. We heard that colleagues wanted to be more empowered, for the Bank to be even more inclusive, and for our work to focus on what matters most.

We also listened to external stakeholders through a series of company visits. And we spoke to more than 30 leading external organisations to draw on best practice. We learnt that we need to do a better job of explaining our complex, technical work to non-technical audiences, and that there is a broad range of new ways of working that could make us more efficient, engaged and effective.

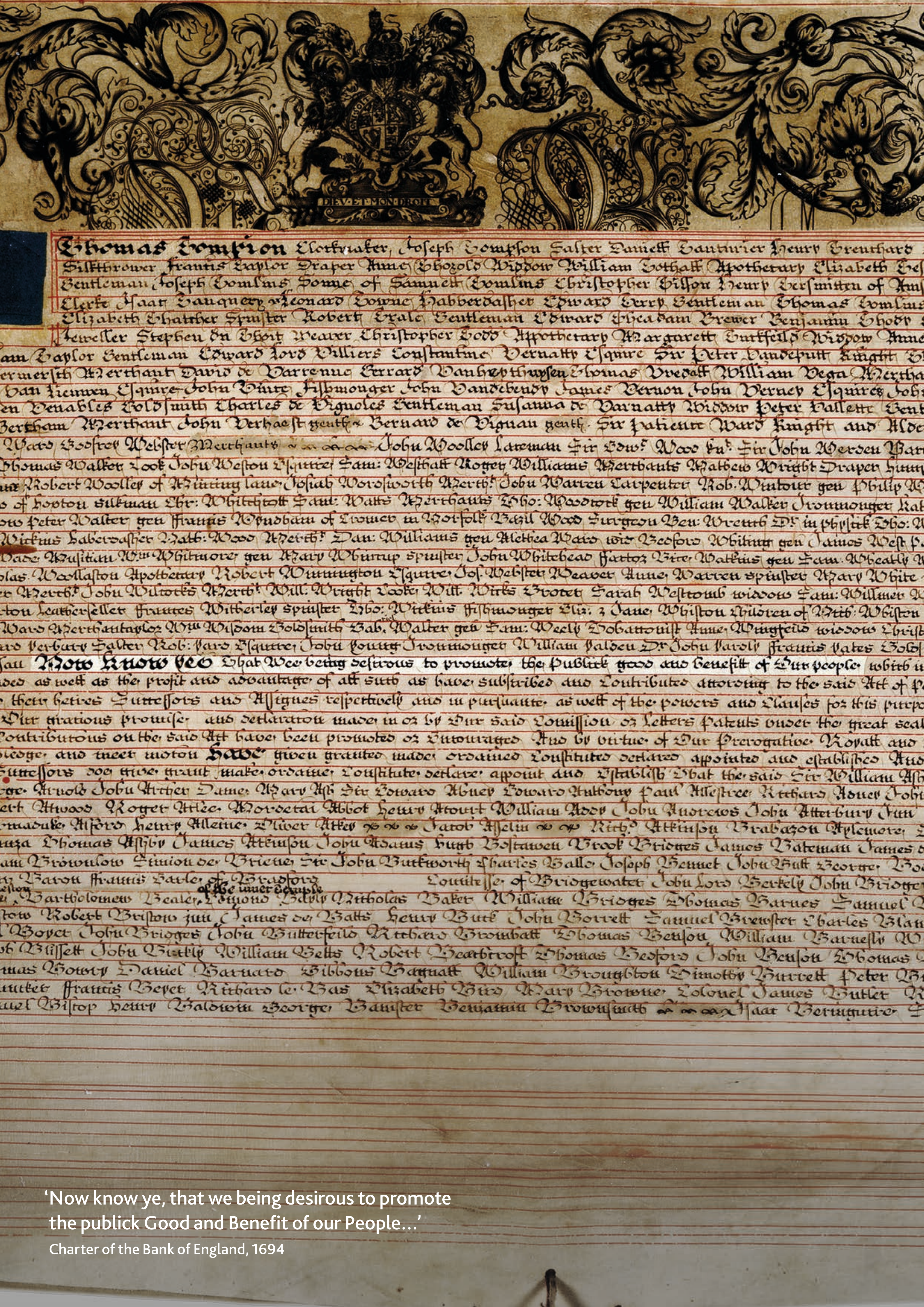
Drawing on these lessons, we will transform the way we communicate. Our messages will be more creative and better targeted to different audiences, so that our policies are better understood and more powerful. We will make the Bank more permeable, so that our internal analysis can more easily and frequently be picked up by traditional and social media. And we will improve our internal communications and decision-making.

We will transform the way we work. Vision 2020 will make our structures more fluid and our prioritisation more effective. Working across internal boundaries will become the norm, bringing together people with different expertise, skills and outlook to solve problems. These initiatives will be supported by new technologies and structures to help colleagues readily share ideas, skills and opportunities.

The years ahead promise to be as eventful as the one which has just passed.

By building on our achievements as One Bank and by transforming how we communicate and work I am confident that the Bank will continue to undertake the necessary analysis and pursue the right policies to promote monetary and financial stability for the good of the people of the United Kingdom.

26 June 2017



'Now know ye, that we being desirous to promote the publick Good and Benefit of our People…'

Charter of the Bank of England, 1694

Court, and the Bank's policy committees

The Bank's framework for governance and accountability is set by the Bank of England Act 1998. The Court of Directors acts as a unitary Board, with executive and non-executive members and an independent non-executive chair.

Court sets the Bank's strategy and budget, takes key decisions on resourcing and appointments, and keeps the Bank's performance and financial management under review. The Court meets at least seven times a year, and its minutes are published.[1]

Members of Court are appointed by the Crown, for periods of eight years in the case of the Governor, five years for the Deputy Governors, and up to four years for the Non-executive Directors. One of the Non-executive Directors is designated by the Chancellor of the Exchequer to chair Court.

Court delegates the day-to-day management of the Bank to the Governor and through him to other members of the executive. But it reserves to itself a number of key decisions, including:

- the Bank's strategy and objectives;
- the Bank's (including the PRA's) expenditure budget;
- major capital projects;
- the Bank's financial framework;
- the Bank's risk tolerance framework;
- approval of the accounts and the appointment of auditors;
- the remit for managing the Bank's balance sheet;
- senior appointments within the Bank;
- major changes in staff remuneration and pension arrangements; and
- the Bank's succession plan.

The major sub-committees of Court are the Audit and Risk Committee, the Remuneration Committee and the Nominations Committee. Terms of reference of these and other Committees are published on the Bank's website.[2]

Members of Court have been indemnified by the Bank against personal civil liability arising from the carrying out or purported carrying out of their functions, provided they have acted honestly and in good faith and have not acted recklessly. These indemnities were first granted in 2000 and approved by HM Treasury in accordance with the practice of the Government in relation to board members of Non-Departmental Public Bodies.

7

Court meetings

Court met seven times during the year.

Attendance at Court and Committee meetings is given on page 74

1 www.bankofengland.co.uk/publications/minutes/Pages/court/default.aspx.

2 www.bankofengland.co.uk/about/Documents/pdfs/courtmatters.pdf.

The Court of Directors
as at 26 June 2017

Anthony Habgood
Chair of Court

Appointed NED
1 July 2014
Term expires on
30 June 2018

– Chairman, RELX Group plc
– Chairman, Preqin Holding Limited
– Visiting Fellow, Oxford University

Mark Carney
Governor

– Chair, Financial Stability Board
– First Vice-Chair, European Systemic Risk Board
– Member, ECB General Council
– Member, Group of Thirty
– Member, Board of Directors, Bank for International Settlements
– Member, Group of Governors and Heads of Supervision, Basel Committee on Banking Supervision
– Member, Board of Trustees, World Economic Forum

Ben Broadbent
Deputy Governor, Monetary Policy

– Alternate, ECB General Council
– Member, OECD Working Party No. 3

Sir Jon Cunliffe
Deputy Governor, Financial Stability

– Member, Financial Stability Board Steering Committee
– Member, European Systemic Risk Board
– Member, Board of Directors, Bank for International Settlements
– Alternate, ECB General Council

Sam Woods
Deputy Governor, Prudential Regulation

– Chief Executive, Prudential Regulation Authority
– Board Member, Financial Conduct Authority
– Member, Board of Supervisors and Management Board, European Banking Authority
– Member, Group of Governors and Heads of Supervision, Basel Committee on Banking Supervision
– Alternate, ECB General Council

Bradley Fried

Appointed NED
1 June 2012
Term expires on
31 May 2019

– Partner, Grovepoint
– Board Member, Financial Conduct Authority
– Fellow of Magdalene College, Cambridge
– Governor, London Business School

Tim Frost

Appointed NED
1 June 2012
Term expires on
31 May 2018

- Chair, Cairn Capital Group Limited

Baroness (Dido) Harding of Winscombe

Appointed NED
1 August 2014
Term expires on
31 July 2018

- Chief Executive, TalkTalk Telecom Group plc (up to 10 May 2017)
- Life Peer taking the Conservative Whip
- Member of the Jockey Club
- Trustee of DotEveryone
- Member of the UK Holocaust Memorial Foundation

Dave Prentis

Appointed NED
1 June 2012
Term expires on
31 May 2019

- General Secretary of UNISON
- Member of the Trades Union Congress Executive Council
- Member of the Labour Party Joint Policy Committee
- Vice-President of the European Public Services Union
- President of Public Services International
- President of Unity Trust Bank

Don Robert

Appointed NED
1 August 2014
Term expires on
31 July 2018

- Chairman, Experian plc
- Senior Independent Director, Compass Group plc
- Chairman, Achilles Group Limited
- Chairman, Validis Holdings Limited
- Visiting Fellow, Oxford University

Dorothy Thompson

Appointed NED
1 August 2014
Term expires on
31 July 2018

- Chief Executive, Drax Group plc
- Director, Haven Power Limited
- Director, Drax Biomass Inc
- Director, Drax Power Limited
- Non-executive Director, Eaton Corporation plc

Find out more online
www.bankofengland.co.uk

Policy committees

Monetary Policy Committee (MPC)

Members as at 26 June 2017
Top row, left to right

Mark Carney
Governor

Ben Broadbent
Deputy Governor,
Monetary Policy

Sir Jon Cunliffe
Deputy Governor,
Financial Stability

Andy Haldane
Executive Director
and Chief Economist

Bottom row, left to right

Kristin Forbes*
External member
Term: 1 July 2014
– 30 June 2017

Ian McCafferty
External member
Term: 1 September 2012
– 31 August 2018

Michael Saunders
External member
Term: 9 August 2016
– 9 August 2019

Gertjan Vlieghe
External member
Term: 1 September 2015
– 31 August 2018

The Bank of England's MPC contributes to the Bank's mission to achieve monetary stability by setting monetary policy to:

- maintain price stability; and, subject to that,
- to support the Government's economic policies, including its objectives for growth and employment.

At least once a year, the Government updates its price stability target and its growth and employment objectives. In March 2017, the Chancellor of the Exchequer re-confirmed the inflation target[1] as '2 per cent as measured by the twelve-month increase in the Consumer Prices Index'. The economic policy objective of the Government is 'to achieve strong, sustainable and balanced growth'.

The MPC has nine members.[†] Five are Bank Governors and officials and four are external members appointed by the Chancellor. An HM Treasury representative also sits with the Committee at its meetings. The Committee meets eight times a year to set policy. The MPC's Minutes are published alongside the Committee's decisions after each meeting. The Bank's quarterly *Inflation Report* includes the MPC's projections for inflation and output.

Since February 2016 members of the MPC have been indemnified by the Bank against personal civil liability on the same terms as members of Court (see page 9).

* Following the end of Kristin Forbes' term of office, Silvana Tenreyro will be appointed as an external member of the MPC on 7 July 2017 for an initial three-year term.

† Following the departure of Charlotte Hogg on 28 April 2017 the MPC had eight members on 26 June as shown here.

1 www.bankofengland.co.uk/monetarypolicy/Documents/pdf/chancellorletter080317.pdf.

Financial Policy Committee (FPC)

Members as at 26 June 2017
Top row, left to right

Mark Carney
Governor

Ben Broadbent
Deputy Governor, Monetary Policy

Sir Jon Cunliffe
Deputy Governor, Financial Stability

Sam Woods
Deputy Governor, Prudential Regulation and Chief Executive of the PRA

Alex Brazier
Executive Director, Financial Stability Strategy and Risk

Bottom row, left to right

Andrew Bailey
Chief Executive, Financial Conduct Authority

Anil Kashyap
External member
Term: 1 October 2016 – 30 September 2019

Donald Kohn
External member
Term: 1 April 2013 – 31 March 2018

Richard Sharp
External member
Term: 1 April 2013 – 31 March 2019

Martin Taylor
External member
Term: 1 April 2013 – 31 March 2018

The Bank of England's FPC contributes to the Bank's mission to achieve financial stability by:

- identifying, monitoring and taking action to reduce risks to the financial system; and, subject to that,
- supporting the Government's economic policies, including its objectives for growth and employment.

The FPC also advises Court on the Bank's Financial Stability Strategy.

At least once a year, the Government must make recommendations about the FPC's responsibilities for financial stability and also about its growth and employment objectives. The FPC must respond formally to these, and provide reasons if it proposes not to follow the recommendations.[1]

The FPC has thirteen members.[2] Six are Bank Governors and officials, and seven are external members — the Chief Executive of the Financial Conduct Authority, five members appointed by the Chancellor and a non-voting member from HM Treasury. The Committee meets at least quarterly. It may give Directions to the PRA and the Financial Conduct Authority in relation to macroprudential measures prescribed by secondary legislation under the Bank of England Act 1998. The FPC also has powers to make Recommendations to any other body. It publishes a record of its formal policy meetings and is responsible for producing the twice-yearly *Financial Stability Report*.

Since February 2016 members of the FPC have been indemnified by the Bank against personal civil liability on the same terms as members of Court (see page 9).

1 The 2017 remit and recommendations is at www.bankofengland.co.uk/financialstability/Documents/fpc/letters/chancellorletter080317.pdf. And the FPC's response is at www.bankofengland.co.uk/financialstability/Pages/fpc/remit.aspx.

2 Following the departure of Charlotte Hogg on 28 April 2017 the FPC had eleven members on 26 June.

Find out online
www.bankofengland.co.uk

Prudential Regulation Committee (PRC)

Members as at 26 June 2017*

Top row, left to right

Mark Carney
Governor, Chair of the PRC

Ben Broadbent**
Deputy Governor,
Monetary Policy

Sir Jon Cunliffe
Deputy Governor,
Financial Stability

Sam Woods
Deputy Governor, Prudential Regulation and Chief Executive of the PRA

Middle row, left to right

Andrew Bailey
Chief Executive of the Financial Conduct Authority
1 March 2017 –

David Belsham
External member
Term: 1 March 2017
– 30 April 2018

Sandy Boss
External member
Term: 1 March 2017
– 31 August 2017

Norval Bryson
External member
Term: 1 March 2017
– 31 August 2018

Bottom row, left to right

Charles Randell
External member
Term: 1 March 2017
– 28 February 2019

David Thorburn
External member
Term: 1 March 2017
– 31 August 2018

Mark Yallop
External member
Term: 1 March 2017
– 30 November 2017

On 1 March 2017, the PRA Board was replaced by the Prudential Regulation Committee (PRC), and the PRA was brought within the single legal entity of the Bank of England. These changes were required by the Bank of England and Financial Services Act 2016 (the Act).

The PRC is the body within the Bank responsible for exercising the Bank's functions as the Prudential Regulation Authority as set out in the Bank of England Act 1998 and the FSMA 2000.[1] The PRC is on the same legal footing as the Monetary Policy Committee (MPC) and the Financial Policy Committee (FPC).

The PRC has twelve members,[2] consisting of five Bank Governors and officials, the Chief Executive of the FCA, and at least six members appointed by the Chancellor of the Exchequer.

Following the commencement of the relevant provisions of the Act:

- The PRC continues to be independent in all its decision-making functions, including making rules and the PRA's most important supervisory and policy decisions.
- The PRA functions continue to be exercised by the Bank and will continue to be funded by the PRA levy, with the PRC responsible for consulting on and setting the level.
- The PRA's legal status as a subsidiary company has been ended.

* For details of date of first appointment and terms on the PRA Board, please refer to Table 3 on page 58 in the PRA *Annual Report* 2016–17.

** The Act provides for one member to be appointed by the Governor with the approval of the Chancellor. The Governor has appointed Ben Broadbent.

1 In this report, references to the 'PRA' should be construed as references to either: (i) the Company, acting via its Board, in the period to 1 March 2017; or (ii) the Bank, acting through the PRC, post-1 March 2017, as the context requires.

2 Following the departure of Charlotte Hogg on 28 April 2017, the PRC had eleven members on 26 June as shown here.

- The PRC will report annually to the Chancellor on the adequacy of the resources allocated to the PRA functions and the extent to which the exercise of those functions is independent of the exercise of the Bank's other functions.

- HM Treasury can make recommendations to the PRC about aspects of the Government's economic policy to which the PRC should have regard when considering how to advance its objectives, and when considering the application of the regulatory principles in FSMA.

These changes will maintain the PRA's operational independence, while at the same time promoting the sharing of knowledge, expertise, and analysis throughout the Bank. The statutory objectives of the PRA, which underpin its forward-looking, judgement-based approach to supervision, remain unchanged:

- a general objective to promote the safety and soundness of the firms it regulates;

- specifically for insurers, to contribute to the securing of an appropriate degree of protection for those who are or may become insurance policyholders; and

- a secondary objective to, so far as is reasonably possible, act in a way which facilitates effective competition in the markets for services provided by PRA-authorised persons in carrying on regulated activities.

Under FSMA, the PRA is required to review, and if necessary revise, and publish annually its strategy in relation to how it will deliver its statutory objectives. The PRA's strategy will be set by the PRC, in consultation with the Bank's Court of Directors (Court). The strategy for 2017/18 can be found in the Strategic Report section on page 19 in the PRA *Annual Report* 2016–17.

Our organisation

The executive and their membership, where relevant, of the MPC, FPC and PRC are indicated below.

Governor

Mark Carney
(MPC, FPC, PRC)

Deputy Governors

Ben Broadbent
Monetary Policy
(MPC, FPC, PRC)

Sir Jon Cunliffe
Financial Stability
(MPC, FPC, PRC)

Joanna Place
Chief Operating
Officer (Acting)

Sam Woods
Prudential Regulation
and Chief Executive
of the PRA (FPC, PRC)

Executive Directors

Sonya Branch
General Counsel

Alex Brazier
Financial
Stability
Strategy and
Risk (FPC)

Sarah Breeden
International
Banks
Supervision

Jonathan Curtiss
Human Resources
(Acting)

Rob Elsey
Technology

John Footman
Secretary of
the Bank

Andrew Gracie
Resolution

Andy Haldane
Monetary
Analysis and
Chief Economist
(MPC)

Andrew Hauser
Banking,
Payments
and Financial
Resilience

Lyndon Nelson
Supervisory Risk
Specialists and
Regulatory
Operations;
Deputy Chief
Executive, PRA

Mike Peacock
Communications
(Acting)

Rommel Pereira
Finance

James Proudman
UK
Deposit-takers
Supervision

David Rule
Insurance
Supervision

Chris Salmon
Markets

Victoria Saporta
Prudential
Policy

Review of 2016/17

In 2014, the Bank of England launched its three-year Strategic Plan to create a single, unified, institution, working as One Bank across all its functions, with a single mission: 'promoting the good of the people of the United Kingdom by maintaining monetary and financial stability'.

Our One Bank strategy has had a huge impact on how we work together to achieve our objectives and has delivered real organisational and cultural change.

We have been able to deliver on complex cross-Bank workstreams: from policy issues such as the housing market and stress testing; to vital core initiatives such as information security.

We have changed our recruitment and talent management to attract and inspire the best people to public service, reflecting the diversity of the United Kingdom, set up a dedicated Research Hub to push us towards the forefront of research and analysis, led the development of new reforms both domestically and internationally, and revamped our monetary policy communications in pursuit of our aim to be understood, credible and trusted.

Overall we have completed 95% of what we planned to deliver as part of our One Bank strategy. That progress is testament to the tremendous efforts of colleagues across the Bank. But there is more work to do. That is why we have launched a new three-year strategic plan, 'Vision 2020', which will consolidate and build on the success of our One Bank strategy.

This Review begins by detailing the specific steps that the Bank has taken over the past twelve months to work as One Bank and to strengthen the four pillars that underpin our Strategic Plan: Diverse and Talented; Analytic Excellence; Outstanding Execution; and Open and Accountable. It then goes on to describe the Bank's work to advance its policy objectives in the areas of monetary policy, financial policy and prudential regulation.

Highlights include the work done across the Bank in: the lead up to, and aftermath of, the EU referendum; the launch and development of our FinTech Accelerator; and in developing the Future Forum which discussed our role in promoting the good of the people of the United Kingdom in times of uncertainty.

The Review ends by looking forward to our new three-year strategic plan, Vision 2020.

Vision 2020

Our new Strategic Plan will maximise our potential

Key successes of the Strategic Plan

One Bank

- Restructure of Bank committees, governance and decision-making lines.
- Increased connectivity across the MPC, FPC and PRC, with principles agreed for streamlined decision-making.
- PRC established on equal footing to MPC and FPC following implementation of the Bank of England and Financial Services Act 2016.
- Enhanced communications and transparency throughout the Bank.
- Increased empowerment and transparency.
- Development and embedding of Our Code.

Diverse and Talented

- Aligned reward for all areas of the Bank to support career mobility via One Bank Your Reward.
- New performance management approach and framework embedded.
- Development and launch of new training offering including the Central Banking Qualification (CBQ).
- Enhanced school leaver, graduate and PhD programmes and the African/Caribbean Scholarship programme.
- Launch of our Inclusion Strategy and progress against our diversity targets.

Open and Accountable

- Stakeholder Relations Group established with strategy agreed and implemented.
- Increased engagement with the public via the Open & Future Forum events.
- Implementation of all Warsh Review actions.
- Establishment of the Independent Evaluation Office, with four evaluations completed.
- Public Understanding Team established with strategy agreed and implemented.
- Development and launch of our KnowledgeBank website.

Outstanding Execution

- Fair and Effective Markets Review undertaken and published.
- Increases and enhancements to our cyber security, making the Bank safer, stronger and more secure.
- Market Intelligence Review completed.
- Successful launch of the new polymer £5 note and development of the £10 note.
- Creation of the Bankwide Risk Division and agreed risk framework.
- Creation of our International Directorate and strategy.

Analytic Excellence

- Creation of the Research Hub and Advanced Analytics and subsequent wider successes in research, as shown by the increase in our RePEc ranking.
- Increased focus on data visualisation and development of new skills.
- Launch and ongoing success of Bank Underground staff blog.
- One Bank Research inventory launched to keep track of all research projects across the Bank.
- Creation of the Central Data Office and our One Bank Data Strategy.

One Bank

At the core of the Bank's Strategic Plan is a commitment to build One Bank. One Bank is about maximising our impact by working together to make full use of the knowledge, resources and skills from across the organisation. It is also about building a strong common culture that will mobilise everyone in the Bank to support our policy and operational decisions. We were therefore pleased to see that our staff survey this year showed increased scores on engagement and enablement from the previous year, and the same levels of engagement and enablement for the Prudential Regulation Authority as for other functions of the Bank.

During this year, a central part of our One Bank plan came into effect: the Bank of England and Financial Services Act 2016 put all of the Bank's policy committees on the same legal basis and helped rationalise the structure of the Bank. This includes the transfer on 1 March 2017 of functions exercised by the Prudential Regulation Authority (PRA) to the Bank of England through the Bank's Prudential Regulation Committee (see pages 14–15). These changes mean we can operate more effectively to promote the monetary and financial stability of the United Kingdom.

This year also saw a number of cross-Bank initiatives that provided clear evidence of the benefits of our One Bank strategy.

EU referendum

The EU referendum provides the most compelling example of the importance, and success, of our One Bank strategy. Over the period many parts of the organisation worked closely together to inform our policy actions. This ensured that the events surrounding the vote did not endanger our mission to maintain monetary and financial stability.

In advance of the referendum, there was extensive cross-Bank contingency planning. Detailed plans were formulated for the financial sector and there was close co-ordination with overseas authorities to ensure we would be able to implement whatever policy responses were required. These contingency plans were informed by a clear, evidence-based assessment of financial stability risks associated with the referendum and underpinned a sequence of carefully designed and calibrated policy responses.

Our contingency plans were built on measures, which had been taken over a number of years, to make the UK financial system much more resilient. The capital requirements of our largest banks are now ten times higher than before the crisis. Through our stress testing we have also ensured that these banks are resilient to a range of severe scenarios. As a result of these actions, UK banks had raised over £130 billion of capital, and had more than £600 billion of high-quality liquid assets which underpinned confidence in the wake of the referendum.

To support the functioning of markets, and to act as a backstop, we put in place measures to provide more than £250 billion of additional funds through our normal facilities if that was required. We also stood ready to provide substantial liquidity in foreign currency.

In the weeks that followed the referendum the Bank assessed economic conditions and responded by putting in place a series of timely and coherent monetary and macroprudential policy responses. All these were aimed at smoothing the adjustment of the UK economy and financial system to a new relationship with the European Union, by maintaining monetary and financial stability.

These actions were transparently and effectively communicated to the public and the markets, including via a statement by the Governor immediately following the referendum result, and subsequently in our

EU referendum

The EU referendum illustrated the importance and success of our One Bank strategy, working together to deliver monetary and financial stability

policy publications and evidence-based judgements to Parliament.

All this work relied on the timely creation of a diverse and talented team who were able to formulate comprehensive plans and execute them quickly in response to events. The response was managed across, and co-ordinated with, all three policy committees, delivering an effective response that was designed to have the maximum impact on the real economy.

Our work on this issue has not stopped with the passing of the referendum. The process of the United Kingdom's withdrawal from the European Union is a large and complex undertaking that will take several years. To ensure our co-ordinated approach continues throughout this process we have established a dedicated unit to draw together work across the Bank on the potential impact of the United Kingdom's exit from the European Union on our policy objectives of monetary and financial stability.

Financial technology

Recent advances in financial technology (FinTech) provide a clear example of how as an organisation we need to continually adapt and change as society itself changes if we are to meet our mission to promote the good of the people of the United Kingdom.

FinTech presents both opportunities and risks for the way we set monetary policy, the safety and soundness of the firms we supervise, the resilience of the financial system as a whole, and the nature of shocks that it might face. For instance, FinTech has already had a significant impact on traditional banking and payment services in ways that could affect financial stability (see the infographic on page 22).

To work through these issues we have embarked on a programme of research and development in collaboration with academic and industry stakeholders. Key to this programme was the launch in June 2016 of our FinTech Accelerator to help us better understand how changes in financial technology might impact the way we work. Through the Accelerator we are working in partnership with technology firms to run a series of targeted, rapid proofs of concepts for solutions to real issues facing us as policymakers. Since launch we have run eight proofs of concepts that cover three areas: data analytics; information security; and distributed ledgers. The firms are carefully chosen through an open process based on published criteria.

Since the launch of the FinTech Accelerator we have met or researched over 230 start-ups, participated in around 45 conferences, and held roundtables with more than 110 organisations. In listening and learning, we have been able to begin to form a judgement about how these technologies might impact the way we meet our mission.

Given the breadth of the potential impact of FinTech on how we work many staff from across the organisation work closely together on these issues including those in Banking, Payments and Financial Resilience; Financial Stability Strategy and Risk; and the PRA.

Information security

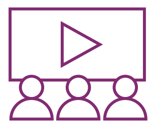
Security is vital to our mission at the Bank of England. Throughout our history, that security has been provided by the physical structure of the Bank. But in a digital age, this is no longer enough to protect us. Today, all our staff work together to support our information security.

The Bank's critical information assets are protected by detecting and mitigating cyber threats, through robust governance of risk and compliance and management of information security policies, and by providing all Bank staff with the knowledge they need to meet their information security responsibilities. This

FinTech Accelerator

Since its launch we have:

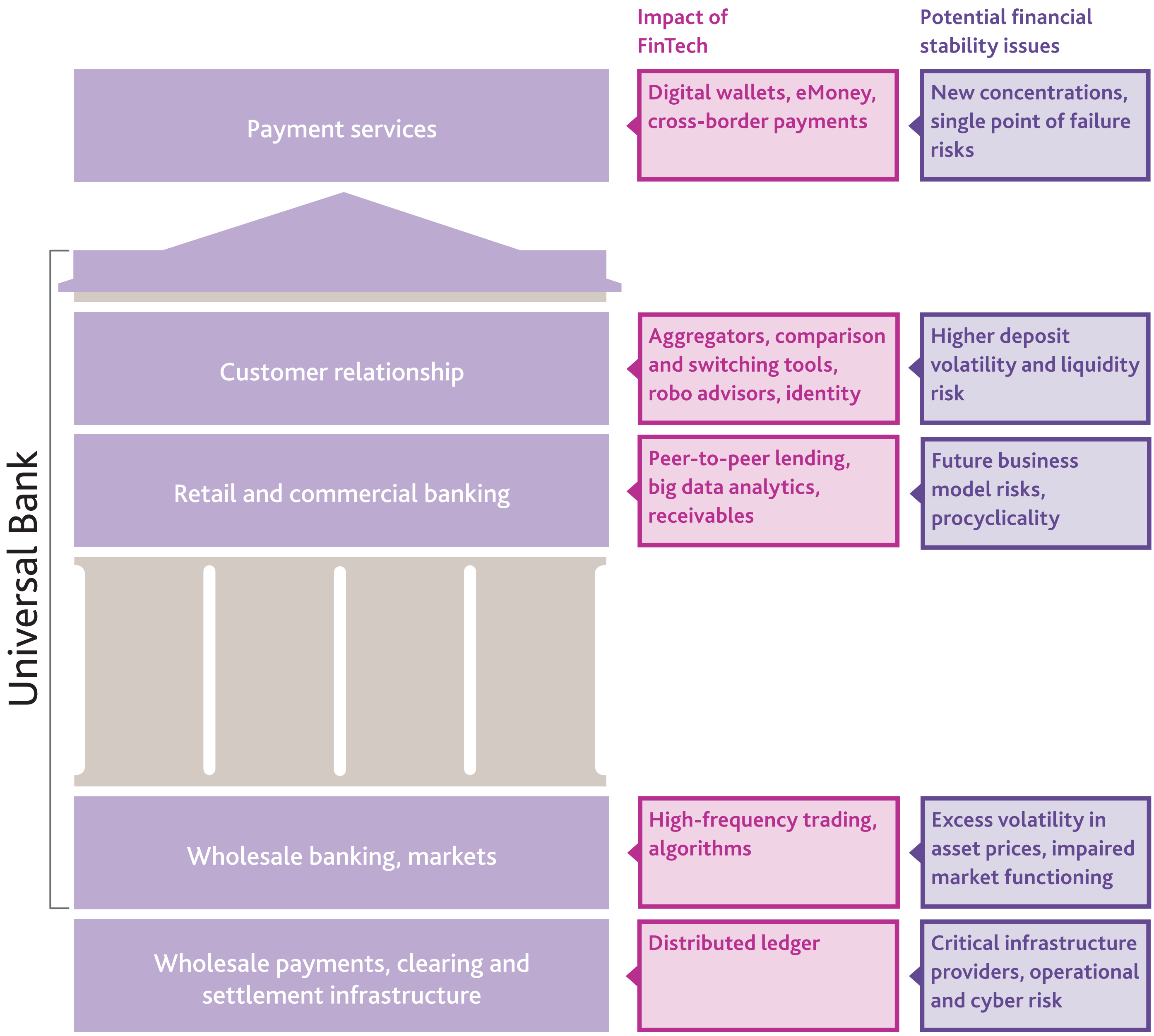
- **Met with over 230 start-ups**



- **Attended 45 conferences**

- **Held roundtables with 110 organisations**

Financial services value chain



includes cultural awareness programmes such as regular phishing campaigns against staff.

We also provide expert advice and support for the CBEST framework — which delivers a controlled, intelligence-led security test. The test mimics behaviours of cyber attackers who are assessed by HM Government and commercial intelligence providers as posing a genuine threat to systemically important financial institutions.

This year we implemented a new multi-level defence strategy for information security. This has reduced the likelihood and potential impact of a cyber-security breach impacting one of the Bank's critical services and ensured the Bank has the right framework in place to keep these defences up to date. It has also improved our ability to be able to respond in the event that our defences are breached. Alongside this we have made great headway towards ensuring our critical systems that support our operations meet the most exacting international standards.

Future Forum

In October 2016, the Bank of England hosted Future Forum. This event brought together people from different sectors of the community to discuss our role in promoting the good of the people of the United Kingdom in times of uncertainty.

The Bank's Governors spent the morning visiting locations across the Midlands, listening to the views and concerns of local business leaders, technology developers, representatives from the voluntary and education sectors, and the wider public.

The Governors then joined together for an afternoon session held at Birmingham Town Hall, where they discussed what they heard and considered actions for the Bank to take forward. The session was attended by over 200 delegates and, via social media, we had 138,000 Twitter impressions, 170 re-tweets and close to 1,400 YouTube views. Feedback was very positive with 80% of attendees reporting that they had a good experience at Future Forum, and close to 70% saying that it had encouraged an open discussion between the Bank and the public.

By listening we formed a clear impression of the needs of our key stakeholders and what we could do to help. For instance, we were told that there are gaps in economics and financial education that we could help to fill, and that we need to do more to connect with the public, so we can listen and engage in a dialogue about the economy and our role in it. In response we have put education and outreach at the heart of our new organisational strategy, Vision 2020.

Overview
Court, and the Bank's policy committees
Our organisation
Review of 2016/17
Financial Stability Strategy
Financial review 2016/17
Risk management and business practices
Corporate social responsibility
Report of the Remuneration Committee
Report on Oversight Functions
Report of the Audit and Risk Committee
Statement of the responsibilities of the Court of Directors in relation to the financial statements
Financial statements
Contacting the Bank of England

Diverse and Talented

The Bank of England is committed to attracting and inspiring the best people to public service. To do that we need to continue valuing diverse ideas and open debate, while developing and empowering people at all levels to take initiative and make things happen.

Investing in our leadership is a key focus within our Diverse and Talented pillar, with the introduction of a number of initiatives including succession planning, 360° feedback, and development reviews for all scales. Following a pilot Bankwide succession planning exercise for all Heads of Division roles, the exercise has now been embedded into our regular processes.

Following the progress made on our diversity aims we launched our new Inclusion Strategy in February 2017 as part of 'Inclusion Fortnight'. Over 20 events were held over ten days, across four sites, and attended by almost 1,700 people. Our Viewpoint survey showed that our work to support inclusion is paying real dividends with almost 80% of staff feeling that the Bank takes diversity seriously, and 90% of people feeling respected. Responses on engagement and enablement have also improved significantly by 3 percentage points each to over 65% and 60% respectively.

We are also encouraged to see that 675 members of staff moved internally across directorates this year. These moves help to spread expertise and make connections across all parts of the Bank, and demonstrate that there are broad career opportunities for individuals working at the Bank, complemented by our successful secondments programme.

Our Central Banking Qualification (CBQ) designed in collaboration with Bank experts and academics from Warwick University also shows how we are making a step change in developing the expertise of our staff. By mixing professional with more academic-style training, the CBQ helps staff develop a more coherent analytical framework to critically assess the issues they will face in their careers, giving them the tools and skills for constructive challenge. Now in its second year, we have more than 160 graduates studying for the CBQ.

Looking forward we have set ourselves stretching diversity targets and aim to have 35% female staff in our senior roles by 2020, and want to increase our Black, Asian and Minority Ethnic (BAME) employees in these roles to 13% by 2022. Across the remainder of our staff, we have set a target of 50% female, and 20% BAME by 2020. In 2016 we hired graduates from over 40 UK universities (four times as many as a decade ago), attracting students from a range of socio-economic backgrounds. Two fifths of the 2016 intake was female and a quarter came from a BAME background. Only half of these students studied economics.

Diversity targets

We have set ourselves some stretching diversity targets

50% **female**

20% **BAME**

by 2020

Analytic Excellence

For the Bank, analytic excellence is about being at the forefront of research and analysis as a necessary part of ensuring we have effective policymaking, operations and tools. And it means making creative use of the best analytical tools and data sources to tackle the most challenging and relevant issues.

During the year we have made important progress on our One Bank Research initiative. This includes the establishment of an Academic Advisory Group to help shape our research, greater integration of our research into the policymaking process, and revamped policy committee research awaydays and novel research showcase events.

These initiatives are already having an impact on the way we analyse such diverse topics as digital currencies, climate change, the housing market and credit unions. They are also reflected in some of our key metrics. The Bank's Research Papers in Economics (RePEc) ranking has risen from 19th at the launch of the Strategic Plan to 11th in February 2017.[1] This brought us within touching distance of achieving our ambitious target of 10th or better by the end of the Strategic Plan. We have also increased the number of top conference presentations and nearly half of the Bank's research projects have external co-authors, demonstrating the extent of our collaboration with the academic community.

This year has also seen an enhancement of our forecasting capabilities. In line with the recommendations of the Independent Evaluation Office (IEO), we have developed an entirely new methodology and process for monitoring and evaluating the accuracy of our macroeconomic forecasts.

Outstanding Execution

The Bank recognises that it is only as effective as its actions. No matter how good our analysis, our decisions and actions need to have influence and impact, both at home and abroad. To achieve our mission, we need co-ordinated and inclusive policy decisions, and reliable, expert execution in everything we do.

In support of our aim of outstanding execution we have continued to lead the development of new reforms both domestically and internationally. That includes being at the forefront of efforts to make the global financial system safer, simpler and fairer.

We have played a leading role in the development of a global code of conduct for the foreign exchange market, and have helped develop a new code that sets out clear, principles-based standards and best practice for participants in UK money markets. We have also set out proposals to deliver a stronger, more resilient, flexible and innovative sterling settlement system for the highest-value payments in the country. And we have worked with the Financial Conduct Authority to increase individual accountability in financial services through new compensation rules.

In September 2016 we issued our new polymer £5 note which is cleaner, safer and stronger than paper banknotes, as well as more environmentally friendly due to their durability. The new note cost around £45 million to print, and the waste from unfit polymer notes will be fully recycled, ensuring the environmental impact is minimised.

The issuance of the new polymer note was widely welcomed. However the Bank experienced an unexpected challenge when it was discovered that trace amounts of animal-derived products were used in the polymer production process. In February 2017 we released a statement that concluded, following careful consideration, it would be

RePEc research ranking

2014 19th

2017 11th

1 The ranking is based on data gathered within the RePEc project that aims to enhance the dissemination of research in Economics and related sciences.

appropriate to keep the £5 polymer note in circulation and to issue the £10 polymer note featuring Jane Austen as planned in September 2017.

Given the public interest in banknotes, and the complex issues involved, the Bank has sought, via a public consultation, opinions on the future composition of polymer notes (including the use of plant-based alternative additives). This will feed into its decisions on the polymer used in future production runs of £5 and £10 polymer notes and the new £20 polymer note featuring J.M.W. Turner which is planned to enter circulation by 2020.

The selection of J.M.W. Turner — celebrating his influence on the visual arts — was announced after almost 30,000 nominations from the public as part of the Bank's new, more open and transparent, character selection process.

Open and Accountable

We recognise that we need to earn the legitimacy to perform the functions given to us by Parliament by becoming more open, more accountable and more transparent. Without doing so, we cannot earn the trust or credibility required for our policies to be effective.

The IEO has continued to support Court in keeping the performance of the Bank under review. Since the previous *Report* the IEO has published two in-depth evaluations on the Bank's approach to financial market infrastructures (FMIs) supervision (February 2017) and the PRA's insurance objective (March 2017). These reports have led to material improvements in the way the Bank discharges its responsibilities in these areas. In the coming year, Court has commissioned two further in-depth reports from the IEO — one into the Bank's framework for resolution, and a second on the provision of liquidity through the Sterling Monetary Framework. The IEO also continues to develop its follow-up framework for previously published reports, such as its November 2015 report into forecast evaluation. The IEO is additionally providing support to the Review by the Non-executive Directors of Court into the Bank's approach to managing conflicts of interest. This was commissioned by Court following the resignation of Charlotte Hogg in March 2017.

Through our One Bank Strategic Plan we have also made strides in improving the transparency, accountability and openness of our communications. Our Bank Underground staff blog, launched in 2015, enables colleagues to share their diverse opinions externally. Over the past year some 350,000 people viewed the blog, and its followers and subscribers increased by 60%.

We also launched in September 2016 a new public understanding website called KnowledgeBank to host simple and visually engaging digital guides on what the Bank does and why. We now have 20 guides covering topics ranging from 'What is the Bank of England doing to support the economy?' to 'How much gold is kept at the Bank of England?' Since launch we have already had over 100,000 page views and our independent survey told us that 90% of respondents thought KnowledgeBank was clearly explained and visually engaging.

This year we also launched a new film competition for secondary schools called Bank, Camera, Action! The topic for 2016 was 'A day in the life of the New Fiver' to celebrate the launch of the new polymer £5 note. The response was fantastic with over 1,000 students taking part from over 100 schools.


TB 267

Monetary policy

The Bank of England's Monetary Policy Committee (MPC) contributes to the Bank's mission to achieve monetary stability by setting monetary policy to meet the 2% inflation target and, subject to that, helps to support growth and employment.

In the wake of the EU referendum the MPC announced an exceptional package of monetary policy measures comprising a 25 basis point reduction in Bank Rate to 0.25%; a new Term Funding Scheme; a new programme of private sector asset purchases with up to £10 billion of UK corporate bonds; and a £60 billion expansion of gilt purchases.[1]

With this response, the MPC delivered a timely, coherent and comprehensive package of easing measures that lowered the cost of credit and improved financial conditions for households and businesses across a wide range of channels.

In line with the MPC's remit, the response was calibrated to balance the speed with which the MPC intends to return inflation to the target and the support that monetary policy provides to jobs and activity.

The analysis supporting the MPC, and the rationale for the MPC's decisions, are set out more fully in the Minutes of the Committee's policy meetings and its *Inflation Reports*.

Financial policy

The Bank of England's Financial Policy Committee (FPC) contributes to the Bank's mission to achieve financial stability by identifying, monitoring and taking action to remove or reduce systemic risks with a view to protecting and enhancing the stability of the United Kingdom's financial system. Subject to that, it supports the economic policy of the Government, including its objectives for growth and employment.

In June 2016 following the EU referendum the FPC acted quickly to reduce the countercyclical buffer rate on banks' UK exposures. This was a response to greater uncertainty around the UK economic outlook and the increased possibility that material domestic risks could crystallise in the near term. The reduction of the buffer rate was intended to reinforce the FPC's expectation that all elements of capital and liquidity buffers are able to be drawn on to support the real economy when necessary. Looking forward, there are a range of possible outcomes arising from the exit negotiations between the United Kingdom and the European Union. The FPC will oversee contingency plans to mitigate risks to financial stability as this process unfolds. It will also assess the financial stability implications of regulated firms' plans to adapt to the United Kingdom's withdrawal from the European Union.

In November 2016 we published the results of our third concurrent stress test of the UK banking system. The scenario was designed under a new approach that ensures the stress is broad, coherent and severe, considering risks across institutions, markets and jurisdictions. We also put in place improvements to the hurdle rate to improve consistency with the capital framework and in line with our continued commitment to improve transparency we disclosed more information around individual banks' capital requirements.

1 For information on the amount and profile of the lending and additional asset purchases see the *Bank of England Asset Purchase Facility Fund Limited Annual Report and Accounts* published in July 2017.

While the test revealed some capital inadequacies for three individual banks, these banks each now have in place the necessary plans to build their resilience further.

The Bank has continued to make a significant contribution to the international debate on financial policy, informed by our commitment to cutting-edge research and analysis. The Bank's work on financial stability is internationally respected and plays an important part in influencing and informing the agendas of the groups in which it regularly participates. These include the G7, G20, International Monetary Fund, Bank for International Settlements, European Systemic Risk Board and the Financial Stability Board.

The work of the FPC is set out more fully in the twice-yearly *Financial Stability Report* and in the records of the FPC's quarterly policy meetings.

Prudential regulation

The Prudential Regulation Authority (PRA) is responsible for the prudential regulation and supervision of over 1,500 banks, building societies, credit unions, insurers and major investment firms. On 1 March 2017 the PRA was brought within the single legal entity of the Bank of England, and the PRA Board was replaced by the Prudential Regulation Committee.

The PRA has three statutory objectives: a general objective to promote the soundness and safety of regulated firms; a specific objective for insurance firms to contribute to the securing of an appropriate degree of protection for those who are or may become insurance policyholders; and a secondary objective to, as far as reasonably possible, facilitate effective competition.

Over the past year a major ongoing priority for the PRA has been to implement ring-fencing in the United Kingdom. This will ensure that banks are structured in a way that supports resolution when they get into difficulty. We also announced in November 2016 new rules that are designed to make it easier to manage the failure of banks and building societies in an orderly way, by ensuring they have sufficient liabilities that can be 'bailed in'.

More detail on these and other activities are provided in the PRA's *Annual Report*, published in July 2017.

To complement these measures, significant progress has been made to ensure there is co-ordination between national authorities should a large international bank fail. This includes running a series of 'war games' to critically test these arrangements with US and EU authorities.

We have also implemented an enhanced supervisory approach for FMIs that includes payments systems and central counterparties. This new approach was developed in light of the increasing systemic importance of FMIs and the complexity of risks they face. The Bank has also made a significant contribution in driving forward international standards on central counterparties' resilience and recovery as well as analysing system-wide interdependencies under the auspices of the Financial Stability Board (FSB) of which Governor Carney is Chair.

The Bank has provided input into the FSB consultation on policy recommendations to address structural vulnerabilities in asset management activities. Taken alongside the work on central counterparties, this marked a significant step forward in building resilient market-based finance, making derivatives markets safer, and market infrastructure more durable. However, more work needs to be done before we complete the journey to a resilient financial system.

Vision 2020

The Bank has a timeless mission: to promote the good of the people of the United Kingdom by maintaining monetary and financial stability. But the way we discharge that responsibility needs to be constantly refreshed if we are to meet the needs of the public we serve.

In May 2017, we launched our new 'Vision 2020' Strategic Plan. Vision 2020 will build on and reinforce the successes of our One Bank Strategic Plan, as well as the values and pillars that support it, as we look ahead to responding to the challenges of the future.

Every member of staff had an opportunity to have their say about how we can best solve these challenges, and as a result has helped shape the development of Vision 2020. We held a series of workshops, open to everyone, to share ideas and proposals, and we visited external organisations to understand how others have dealt with similar challenges.

The core aim of Vision 2020 is to unlock the true potential of all our people by increasing empowerment and maximising our impact. To do that we need to change the way we work to ensure diverse, expert people work together and more often — across disciplines and across areas — to solve the policy challenges we face. And we need to further support our staff by offering varied and interesting careers while providing targeted training and development to equip them with the full set of skills they need.

Vision 2020 is built around two platforms: How We Communicate; and How We Work (see infographic opposite).

How We Communicate

Vision 2020 will transform the way we communicate. Our messages will be more creative and better targeted to different audiences, so that our policies are better understood and more powerful. We will be more permeable, so that our analysis can more easily and frequently be picked up by traditional and social media. And we will improve our internal communications and decision-making. We will empower our staff to form judgements and better equip them to communicate these judgements more effectively.

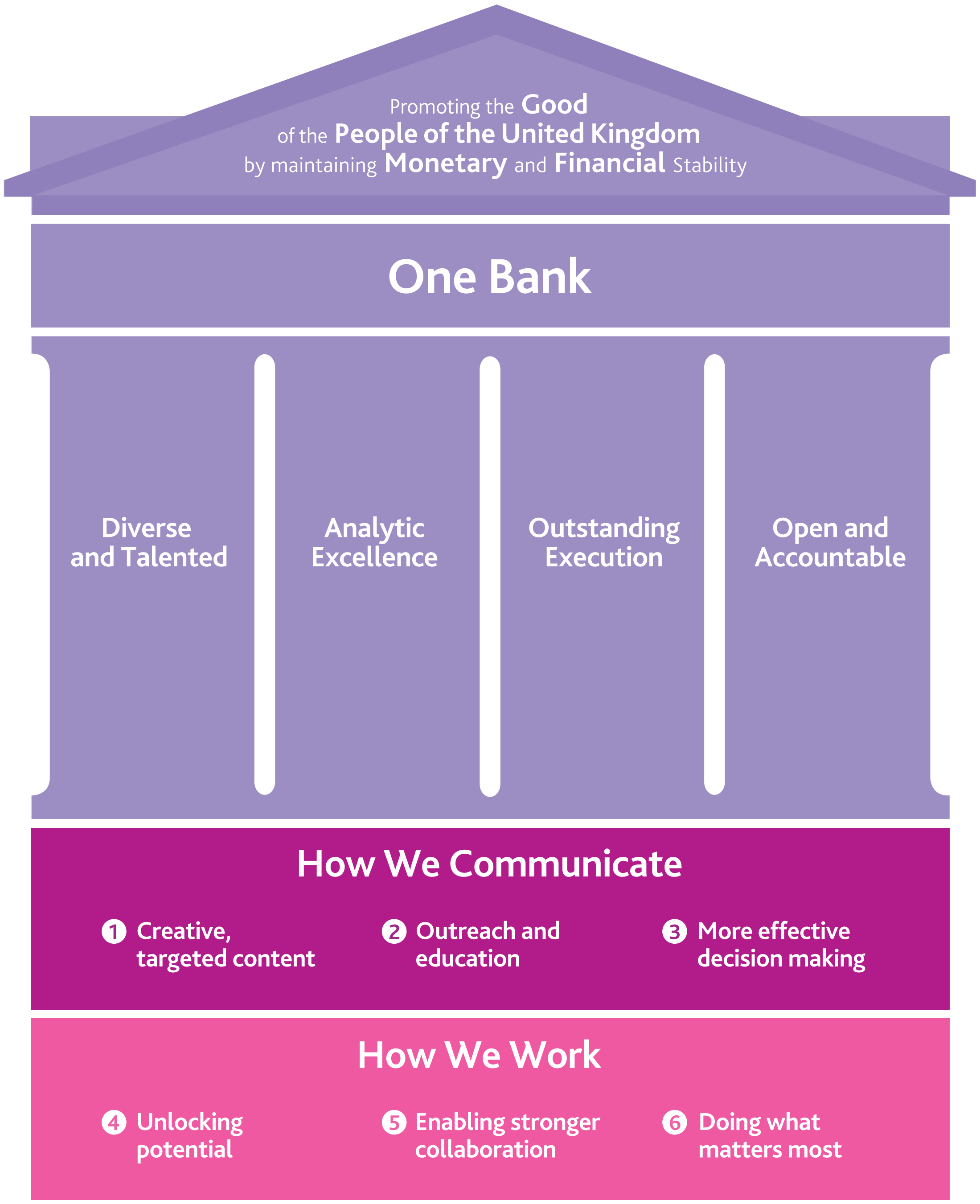
How We Work

We will also transform the way we work. Vision 2020 will make our structures more fluid and our prioritisation more effective. Working across boundaries will become the norm, bringing together people with different expertise, skills and outlook to solve problems. These initiatives will be supported by new technologies and structures to help staff readily share ideas, skills and opportunities.

These changes will build upon our existing intellectual rigour, operational excellence and long history. Success will depend on every single person at the Bank understanding their role in delivering our mission.

Vision 2020

The Bank of England's mission is to promote the Good of the People of the United Kingdom by maintaining Monetary and Financial Stability.



Financial Stability Strategy

The Bank of England's financial stability objective is to 'protect and enhance the stability of the financial system of the United Kingdom'. This is defined by Parliament, through the Bank of England Act 1998.

The Court of Directors of the Bank has a statutory responsibility to determine the Bank's strategy in relation to this objective and to review it at least every three years. Court has delegated the review of the strategy to the Financial Policy Committee (FPC), as permitted by the Act; but Court retains ultimate responsibility for the strategy. The strategy below fulfils this requirement. It was agreed in June 2017, following a review by the Bank's FPC of the strategy that was set by Court in 2014, and following consultation, as required by statute, with HM Treasury (HMT).

Guiding principles for the Bank's Financial Stability Strategy

- **Financial stability is the consistent supply of the vital services that the real economy demands from the financial system (which comprises financial institutions, markets and market infrastructures).** Those services are:

  - providing the main mechanism for paying for goods, services and financial assets;
  - intermediating between savers and borrowers, and channelling savings into investment, via debt and equity instruments; and
  - insuring against and dispersing risk.

- **Left unchecked, the financial system can develop in ways that leave it vulnerable to shocks.** It can take excessive risks; and, where borrowers become highly indebted, shocks to the real economy, and hence the financial system, can be amplified. There is therefore a role for public authorities to ensure that the system is resilient to potential risks: by establishing a rigorous baseline level of resilience to protect the UK real economy; ensuring the level of resilience adapts to the risks the system faces; and enabling the system to absorb shocks, if/when they occur, so it can continue to support the economy.

- **Financial stability is not about the elimination of all risks or minimising volatility in the financial system.** It is about identifying and taking action to remove or reduce systemic risks — those that could severely impair the consistent supply of the financial system's vital services.

- **The necessary resilience must be delivered efficiently** so as not to hamper the ability of the system to serve the real economy.

- **The United Kingdom is the leading internationally active financial centre, with a financial system that is, by asset size, around ten times UK GDP.** It is therefore exposed to shocks from abroad. Standards of UK resilience must reflect these risks to protect the domestic real economy. The global importance of the UK financial system means the actions of the UK authorities contribute to both domestic and international financial stability. The United Kingdom's institutions and markets must be a source of strength for the global system and able to be relied on by others. Standards of resilience must reflect this.

The Bank of England's strategy to deliver financial stability

The strategy has three broad elements:

(a) establishing a rigorous baseline level of resilience to protect the UK real economy;
(b) ensuring the level of resilience adapts to the possible shocks the system might face; and
(c) enabling the system to absorb shocks, if/when they occur, so it can continue to support the economy.

(a) Establishing a rigorous baseline level of resilience to protect the UK real economy

(1) **Implement robust prudential regulation in the UK financial system**, requiring a level of resilience to be maintained that is at least as great as that currently planned, which itself exceeds that required by international baseline standards; and do this consistently, fairly and transparently. This level of resilience protects the UK real economy and ensures the UK financial system is a source of strength for the global system.

(2) **Work with international authorities to develop rigorous common international baseline standards** for the financial system, and assist in the consistent implementation of those standards internationally. Robust, consistently implemented, standards increase the resilience of the global financial system and ensure a level playing field across jurisdictions — this promotes financial stability, financial openness and efficiency. Hosting a global financial centre also means that the United Kingdom depends upon other jurisdictions implementing robust standards.

(3) **Supervise firms to promote their safety and soundness to prudential and operational risks (including cyber risk) and in the case of insurers, also to protect insurance policyholders.** A forward-looking, judgement-based supervisory approach ensures prompt, corrective actions are taken where needed. Effective co-operation and information sharing with other jurisdictions helps supervisors to gauge and manage risks for global financial firms. World-class supervision of UK-based globally important financial market infrastructure, including central counterparties, reduces systemic risks both in the United Kingdom and at the global level.

(4) **Increase individual accountability in financial services.** The United Kingdom has introduced new compensation rules to align better risk and reward. UK authorities have encouraged market participants to develop new codes of conduct domestically and globally. In the United Kingdom, the Senior Managers Regime embeds risk awareness, openness and ethical behaviour. These initiatives will all help to improve conduct and lay the groundwork for better culture in financial services.

(5) **Remove incentives for excessive risk-taking and establish market discipline by ending the problem of financial companies that are 'too big to fail'.** Ensure that banks, building societies, central counterparties and investment firms are set up so that, if they fail, their failure can be managed without severe disruption to the financial system and wider economy and without recourse to the taxpayer. Planned ring-fencing of UK domestic banking services will help to ensure that banking services on which UK households and companies depend can be sustained in the face of external shocks.

(6) **Provide the infrastructure for resilient settlement of the most critical high-value sterling payments in the economy and the most important retail payment systems** by enabling them to be settled across the balance sheet of the Bank of England.

(b) Ensuring the level of resilience adapts to the risks the system faces

(7) **Identify potential risks to financial stability and explain them publicly** so that the financial system can be prepared and resilience can be built up. Transparency about risks is essential to strengthen resilience and for plans to be put in place to manage those risks should they crystallise.[1] Where necessary, action is taken to address these risks.

1 Twice a year, the FPC publishes its *Financial Stability Report* (*FSR*) which sets out the FPC's view of the outlook for UK financial stability, including its assessment of the resilience of the UK financial system and the current main risks to financial stability. It also publishes records of each of its quarterly meetings. For *FSRs* see www.bankofengland.co.uk/publications/Pages/fsr/default.aspx. For FPC meeting Records and Statements see www.bankofengland.co.uk/financialstability/Pages/fpc/meetings/default.aspx.

(8) **Stress test the core banking system regularly to assess its resilience to evolving risks.** The Bank stress tests the resilience of the UK banking system as a whole to potential macroeconomic and other shocks. These tests aim to ensure the system can continue to supply credit and other services even in a very severe stress. The sizes of the shocks to different sectors and economies are adjusted each year to deliver a stressed outcome that reflects the vulnerabilities in those sectors and economies.[1]

(9) **Take action, where necessary, to mitigate financial stability risks from very high levels of private sector debt, which can make the system less resilient and economic growth more fragile.** A large number of highly indebted households and businesses could make the economy more volatile. Although the system could be made more resilient to these threats, it can be difficult to do so robustly and there are broader benefits to avoiding the threats arising in the first place.[2]

(10) **Propose changes to the UK regulatory perimeter where needed to ensure the system is resilient to risks.** The FPC is mandated to assess new and emerging risks to financial stability, including those that may arise beyond the core banking sector.[3] And it has the power to make Recommendations to HMT to change the regulatory perimeter to deal with those risks, if deemed necessary. International co-ordination to identify and manage risks beyond the core banking sector is essential to manage cross-border challenges to financial stability.

(c) Enabling the system to absorb shocks, if/when they occur, so it can continue to support the economy

(11) **Ensure resilience is used effectively in times of stress.** The Bank aims to ensure that banks can draw on their capital and liquidity buffers, as necessary, to allow them to cushion shocks and maintain the provision of financial services to the real economy. Some buffers are intended to be 'countercyclical'; as risks grow, the buffers will increase. If and when risks crystallise, buffers are made available for banks to draw down so they can absorb shocks without disrupting services.

(12) **Provide liquidity to the UK financial system to mitigate disruption**. In some cases, banks' liquidity buffers may not be sufficient to absorb the full impact of a stress. The Bank stands ready to provide liquidity in the event of unexpected developments by offering to swap high-quality but less liquid collateral for liquid assets. In exceptional circumstances, the Bank stands ready to act as a market maker of last resort by buying and/or selling capital market assets against central bank money.[4] The FPC contributes to the Bank's annual review of its liquidity facilities, by giving views on whether the facilities remain fit for purpose from a macroprudential perspective.

(13) **Use resolution powers to manage failures of individual banks, building societies, central counterparties and certain investment firms to mitigate severe disruption to the financial system and wider economy.** The Bank has a number of resolution powers to achieve this, including the ability to bail in creditors and to restructure the firm, with the aim of reducing disruption to the financial system and the wider economic costs of failure.

1 The Bank's stress-testing framework is set out in 'The Bank of England's approach to stress testing the UK banking system'; www.bankofengland.co.uk/financialstability/Documents/stresstesting/2015/approach.pdf.

2 The FPC has set out a description of its powers and the circumstances in which they might use them in a series of Policy Statements. The FPC has taken action on mortgage lending in the United Kingdom. For FPC policy statements see www.bankofengland.co.uk/financialstability/Pages/fpc/policystatements.aspx.

3 The FPC undertakes a regular review of developments beyond the core banking sector, as well as targeted reviews of specific activities. The results of these have been published in *Financial Stability Reports*; see www.bankofengland.co.uk/publications/Pages/fsr/default.aspx.

4 The framework for the Bank's liquidity operations are set out in the Bank's *Red Book*. Annual updates on the Bank's liquidity operations are also included in the annual report on the Sterling Monetary Framework. See 'The Red Book'; www.bankofengland.co.uk/markets/Pages/sterlingoperations/redbook.aspx. See the Sterling Monetary Framework Annual Reports; www.bankofengland.co.uk/markets/Pages/money/default.aspx.

Organisation of responsibilities

- The Bank is responsible for the delivery of its financial stability objective in line with this strategy.

- Within the Bank, two statutory bodies have responsibilities to make specific contributions to UK financial stability:

  – The FPC is responsible for identifying, monitoring, and taking action to remove or reduce systemic risks with a view to protecting and enhancing the resilience of the UK financial system. In meeting this responsibility, the FPC maintains an overview of the UK regulatory and supervisory frameworks and any financial stability issues arising in relation to these. Subject to achieving that, the FPC should act in a way that supports the economic policy of the Government. The FPC has specific powers of Direction over the Prudential Regulation Authority (PRA) and Financial Conduct Authority (FCA) and the ability to make 'comply or explain' Recommendations to both authorities; it has the ability to make Recommendations to any relevant authority on action necessary to conserve financial stability.

  – The PRA must take into account financial stability considerations when advancing its general objective to promote the safety and soundness of the firms it regulates, including banks, building societies, credit unions, designated investment firms and insurers. The PRA also has an objective to protect insurance policyholders and a secondary objective to facilitate effective competition. The PRA's most important decisions are taken by the Prudential Regulation Committee (PRC) of the Bank. The strategy for conducting effective supervision was adopted by the PRC and published in full in the PRA's *Annual Report*.[1]

- The Bank has statutory responsibilities in relation to financial market infrastructure (FMI) and resolution:

  – The FMI Board exercises the Bank's powers in relation to FMIs, and the Bank's strategy with respect to FMI supervision is set out in an approach document,[2] with updates provided in the Bank of England's Annual Report on FMI supervision.[3]

  – The Bank is the resolution authority for the United Kingdom and has published its approach to resolution.[4]

- The Bank also relies on other UK authorities to meet their responsibilities. For example, HMT determines the regulatory framework for the UK financial system and is able to specify which activities should be regulated and which activities should be prudentially regulated by the PRA. The FCA is the conduct regulator for financial companies and financial markets in the United Kingdom and the prudential regulator for some of those firms, including asset managers, consumer credit providers and insurance brokers. A Memorandum of Understanding outlines how HMT, the Bank and the PRA will co-ordinate with each other in the run-up to and during the resolution of a firm. As resolution authority, the Bank decides which resolution tools to use and carries out the resolution, except for temporary public ownership and public equity support, for which HMT is responsible. HMT must also authorise the use of any resolution power which would have implications for public funds.

1 For *PRA Annual Reports* see www.bankofengland.co.uk/pra/Pages/publications/praannualreport/default.aspx. The PRA has also published approach documents on banking and insurance supervision. See *The PRA's approach to banking supervision*; www.bankofengland.co.uk/publications/Documents/praapproach/bankingappr1603.pdf and *The PRA's approach to insurance supervision*; www.bankofengland.co.uk/publications/Documents/praapproach/insuranceappr1603.pdf.

2 See *The Bank of England's approach to the supervision of financial market infrastructures*; www.bankofengland.co.uk/financialstability/Pages/fmis/supervisory_app/supervisoryapproach.aspx.

3 For *FMI Annual Reports* see www.bankofengland.co.uk/publications/Pages/fmi/default.aspx.

4 See *The Bank of England's approach to resolution*; www.bankofengland.co.uk/financialstability/Documents/resolution/apr231014.pdf.

Financial review 2016/17

Financial statements highlights

The table below presents highlights of the combined 2017 financial statements.
Further explanation and commentary is provided below.

Financial statement highlights

	2017 £m	2016 £m
Banking Department total balance sheet size	517,679	405,758
Banking Department profit before tax	222	233
Cash Ratio Deposits	4,424	4,136
Funding for Lending Scheme	52,170	57,645
Funding for Lending Scheme income	146	160
Notes in circulation	73,198	67,818
Net seigniorage income	432	462
Combined cost base	568	549
PRA cost base	254	253
Payment to HM Treasury in lieu of dividend	101	105

Financial framework

The Bank operates as One Bank, a single unified institution, and the financial review is presented in a way that is consistent with this operating principle.

The PRA was a separate legal entity, operating under the Financial Services and Markets Act 2000 (as amended), until the enactment of the Bank of England and Financial Services Act 2016 which transferred the assets and liabilities of the PRA to the Bank of England on 1 March 2017. From this date the PRA has operated as a directorate of the Bank.

The disclosures presented in this review for the PRA are recognised separately in the PRA's *Annual Report*.

Additionally, under the 1844 Bank Charter Act, the Bank was divided for accounting purposes into the Issue Department, covering banknote issuance activity, and the Banking Department, which encompasses all other activities.

Under the Bank of England Act 1998, the financial statements are prepared on a non-consolidated basis. The 'combined' income statement and balance sheet data represents the aggregation of the Banking Department, Issue Department and PRA, and is presented for information purposes only.

The key elements of the financial framework of each component of the Bank are detailed below.

For the Banking Department, the Bank compiles its medium-term spending plans within a financial framework which has four main tenets:

- first, that policy functions of the Bank (monetary policy and financial stability) are financed by the Cash Ratio Deposit (CRD) scheme. Under the CRD regime, banks and building societies are required to place an interest-free deposit at the Bank which is a set percentage of their deposit base. The Bank then invests those deposits in interest-yielding assets, generating income to fund its policy functions. The CRD requirements are set by HM Treasury through a Statutory Instrument every five years;[1]
- second, that the remunerated activities of the Bank — banking and lending operations for the Bank's own account — will be expected to break even over the medium term. In these areas the focus will be on net spending, although the Bank will remain committed to providing value for money, without running undue risks. Any gains or losses from these activities will not flow back to CRD payers, but instead be recognised in the Bank's capital. The Funding for Lending Scheme (FLS) is considered a remunerated activity;
- third, the Bank of England in its capacity as the PRA, operating under the Financial Services and Markets Act 2000, may levy regulated firms to recover all costs incurred in the performance of the PRA's functions under the Act; and
- fourth, that if spending on policy functions is in line with CRD income and other functions break even, the profit of the Bank should be broadly equivalent to the return on the assets in which its capital and reserves are invested — largely gilts. Under the Bank of England Act 1998, the Bank's post-tax profit is shared 50:50 with HM Treasury unless otherwise agreed.

The Issue Department is funded by buying interest-yielding assets to back the notes in circulation. The interest earned on these assets is used to fund the costs of note production and supply. The net profits/losses of the Issue Department are referred to as seigniorage, and paid/claimed directly to/from HM Treasury via the National Loans Fund.

Court considers the operation of the Bank's financial framework in fulfilling its responsibilities under the Bank of England Act 1998.

1 The current requirements were agreed in May 2013; see www.legislation.gov.uk/uksi/2013/1189/pdfs/uksi_20131189_en.pdf for the 2013 Cash Ratio Deposit legislation.

Combined income statement

The combined income statement reflects a profit before tax of £222 million (2016: £233 million). This is effectively equal to the Banking Department profit before tax as the PRA operates a cost recovery model, and Issue Department profits are payable in full to HM Treasury.

Year-on-year fall in profit before tax of £11 million was driven by increased expenditure on remunerated functions, decreases in Funding for Lending Scheme (FLS) fee income and CRD income offset by mark-to-market gains on foreign currency deposits and increased management charges.

Summary combined income statement[1]

	2017 £m	2016 £m
Income	**790**	**782**
Banking Department	634	626
Issue Department	538	542
PRA	254	253
less internal income recoveries and seigniorage income		
Banking Department corporate service management fee to the PRA	(98)	(97)
Issue Department income transferred under seigniorage arrangements	(538)	(542)
Expenses	**(568)**	**(549)**
Banking Department	(412)	(393)
Issue Department	(106)	(80)
PRA	(254)	(253)
less internal cost recoveries and seigniorage expenses		
Issue Department costs under seigniorage arrangements	106	80
PRA corporate services management charge from the Banking Department	98	97
Combined profit before tax	**222**	**233**
Taxation	(20)	(24)
Payment in lieu of dividend	(101)	(105)
Profit after tax and dividend for the year ended 28 February	**101**	**104**

1 The separation of the Banking and Issue Department for accounting purposes is required by statute. A summary 'combined' income statement and balance sheet as at 28 February 2017, aggregating the Banking Department, Issue Department and the PRA, is provided in this financial review. It is provided for information purposes only.

Expenditure by function

Total expenditure for 2017 of £568 million was £14 million below the 2017 budget of £582 million.[1] The variance to budget was predominantly attributable to lower accounting costs on the defined benefit pension scheme, lower-than-expected banknote production and lower investment expenditure throughout the year.

The 2018 cost budget has been set at £659 million (of which the PRA is £288 million). The increase is driven by a combination of increases in banknote production (higher anticipated printing volumes ahead of the £10 polymer launch in September 2017), incremental costs relating to implementation of Structural Reform, higher accounting costs on the defined benefit pension scheme, and the impact of EU withdrawal. Budgeted cost growth excluding these items has been limited to 1.5%.

Combined expenditure by function[2]

	2017 Actual £m	2016 Actual £m
Policy functions		
Monetary policy	77	77
Financial stability	81	75
Expenditure on policy functions	**158**	**152**
Remunerated functions		
Notes issue costs recharged to the Issue Department	105	83
Government agency services	10	9
Payment and settlement	14	13
Banking services	36	35
Other functions	7	5
Expenditure on remunerated functions	**172**	**145**
Net legacy items in relation to pensions and property	(16)	(1)
Corporate service costs recharged to the PRA	98	97
Expenditure on other functions	**82**	**96**
Total Banking Department	**412**	**393**
Issue Department	**106**	**80**
Operational expenditure	243	240
Special project and Solvency II costs	11	13
Prudential Regulation Authority	**254**	**253**
Issue Department costs settled under seigniorage arrangements	(106)	(80)
PRA corporate services management charge from the Banking Department	(98)	(97)
Internal charges and settlements under seigniorage arrangements	**(204)**	**(177)**
Total combined expenditure	**568**	**549**

1 The budget of £582 million presented in the 2016 *Annual Report*.

2 Combined expenditure by function represents the aggregation of the Banking Department, Issue Department and the PRA, adjusted for internal charges and eliminations under seigniorage arrangements.

Policy functions

Expenditure on policy functions was £158 million, a year-on-year increase of £6 million, due to continued investment in the Financial Stability and Resolution functions, the Bank's research and analytical capability, and information security.

Remunerated functions

Expenditure increased by £28 million to £172 million (2016: £144 million), this was primarily driven by the increased cost of notes production for polymer £5 note launch stocks.

The Bank's remunerated functions (operating on a full and fair cost recovery basis) continue to make a surplus as a consequence of FLS income of £146 million (2016: £160 million).

Prudential Regulation Authority

Operating costs for 2017 of £254 million (2016: £253 million) were slightly higher than the budget of £253 million, predominantly due to additional expenditure in relation to EU withdrawal activity and acceleration of system costs for supervisory risk management.

Issue Department

Expenditure of £106 million on the Issue Department increased by £26 million year on year due to spend on the switch to polymer notes in 2016.

Combined balance sheet

The combined balance sheet grew by £105.1 billion in 2017. The largest movement in assets was an increase in 'Loans and advances' of £101.7 billion, primarily attributable to an increase in the Loan to BEAPFF following the resumption of asset purchases.

The upward trend in 'Notes in circulation' (NIC) continued in 2017, bringing the total liability to £73.2 billion (2016: £67.8 billion).

Drawings on the FLS as at 28 February of £52.2 billion have decreased on the prior year balance (£57.6 billion). This followed announcement of the Term Funding Scheme (TFS), operated through the Bank of England Asset Purchase Facility Fund Limited (BEAPFF).

FLS is a fully collateralised scheme, classified as off balance sheet under a collateral swap arrangement, which allows participants to borrow UK Treasury bills in exchange for eligible collateral.

Combined balance sheet

	2017 £m	2016 £m
Assets		
Loans and advances	503,593	401,886
Securities held at fair value through profit or loss	9,157	7,190
Available for sale securities	11,226	11,178
Other assets	3,852	2,448
Total assets	**527,828**	**422,702**
Equity and liabilities		
Deposits	440,846	344,594
Notes in circulation	73,198	67,818
Foreign currency bonds in issue	6,450	4,333
Other liabilities	2,580	1,367
Capital and reserves	4,754	4,590
Total equity and liabilities	**527,828**	**422,702**
Off balance sheet — Funding for Lending Scheme		
Funding for Lending drawdowns	**52,170**	**57,645**

Financial review of Banking and Issue Departments

Banking Department

The Banking Department's financial statements for the year ended 28 February 2017 are shown on pages 82–135 and reflect a profit before tax of £222 million (2016: £233 million) and tax charge of £20 million (2016: £24 million). The Bank and HM Treasury share the Banking Department's post-tax profits equally, with profit transferred to reserves of £101 million (2016: £104 million), and the amount payable to HM Treasury in lieu of dividend accounts for £101 million (2016: £105 million).

The statement of comprehensive income reflects a net increase for the year of £265 million (2016: £1,296 million), comprising post-tax operating profits of £202 million (2016: £209 million) and 'other comprehensive income' totalling £63 million (2016: £1,087 million). 'Other comprehensive income' includes a net increase in the fair value of available for sale assets of £145 million (2016: £758 million), retirement benefit remeasurements decreases of £76 million (2016: £300 million increase) and property revaluation losses of £6 million (2016: £29 million).

The total balance sheet of the Banking Department increased during the year, from £405.8 billion at 29 February 2016 to £517.7 billion as at 28 February 2017.

The main change in Banking Department assets was an increase in 'Loan to BEAPFF' in 'other loans and advances' of £110.0 billion, following the MPC announcement of further asset purchases and the TFS.

'Capital and reserves' increased to £4.8 billion (2016: £4.6 billion), due to changes in market valuations of available for sale assets. The Bank's retained earnings, together with Cash Ratio Deposits, are predominantly invested in gilts and supranational sterling bonds. The Banking Department's holdings of gilt securities and other supranational bonds totalled £7.2 billion at 28 February 2017 (2016: £6.8 billion).

At 28 February 2017, the Banking Department balance sheet contained £6.4 billion of liabilities associated with the management of the Bank's foreign exchange reserves (2016: £4.3 billion).

The main movement in Banking Department liabilities was an increase of £108.4 billion in 'deposits repayable on demand'.

Issue Department

The statements of account for the Issue Department (which are provided on pages 136–40) reflect net profits from note issue of £432 million (2016: £462 million), payable in full to HM Treasury. In 2017, gilt revaluations contributed £137 million to income (2016: £47 million), this increase was offset by a reduction in interest earned and combined with higher note production costs drove the decrease in net profits in 2017.

'Notes in circulation' continued to increase year on year, and totalled £73.2 billion at 28 February 2017 (2016: £67.8 billion). Gilt purchases to back banknote issuance, introduced in January 2008, remained on hold during the year while BEAPFF undertook gilt purchase operations. The market valuation of gilts on Issue Department was £2.8 billion at 28 February 2017 (2016: £3.2 billion). The 'Ways and Means advance' to HM Treasury remained at £370 million as at 28 February 2017.

Taylor's Treasury, the newly refurbished area of the Bank uncovered after almost 45 years hidden.

Risk management and business practices

Court is responsible for the risk management and internal control systems in the Bank and its subsidiaries.

The risk management and internal control systems are based on what Court considers to be appropriate for the Bank's activities, appropriate to the materiality of operational, financial, and other risks inherent in those activities and appropriate to the relative costs and benefits of implementing specific controls. The systems are designed to manage rather than eliminate the risk of failure to achieve the Bank's mission and, as such, provide reasonable, but not absolute, assurance against material misstatement or loss. Risk is assessed and managed in accordance with the risk tolerance agreed by Court.

In accordance with the Financial Reporting Council's guidance on the UK Corporate Governance Code,[1] Court has reviewed the effectiveness of the Bank's risk management and internal control systems. Court confirms that an ongoing process of identifying, evaluating and managing the Bank's risks has operated throughout the year covered in this *Annual Report* and up to the date of its approval. To facilitate Court's review and confirmation, the Governors, Executive Directors and Directors have certified compliance with the Bank's risk management and internal control requirements by the areas for which they are responsible. This attestation included a review of the risk and control issues identified and reported during the year.

Risk governance

The Court of Directors

Court's overall responsibilities include determining the Bank's objectives and strategy, and ensuring the effective discharge of the Bank's functions and the most efficient use of the Bank's resources. Within this, Court takes responsibility for the overall governance framework of the Bank, including the Bank's risk management and internal control systems. Court determines the strategy for managing risk and the Bank's tolerance for risk. It takes the lead in setting a strong risk management culture across the Bank and relies on a sound governance structure to ensure its risk management strategy is implemented through frameworks, policies and risk reporting.

The Audit and Risk Committee (ARCo)

ARCo assists Court in meeting its responsibilities for an effective system of financial reporting, internal control and risk management. It has responsibility for reviewing the findings of internal and external auditors and monitoring outstanding actions for timely completion. The Committee receives reports on the Bank's risk profile, the operation of the risk framework and, the risk management processes and systems in place in the Bank. ARCo reviews accounting policies and the annual financial accounts for approval by Court. The Chair of ARCo is responsible for the performance of the Committee. The Bank voluntarily complies with the core principles of the Senior Managers Regime framework. As part of that framework, the Chair of ARCo has responsibility for ensuring and overseeing the integrity of the independence of the Bank's Audit, Risk and Compliance functions. The Bank's Internal Auditor, Head of Risk and Head of Compliance have reporting lines to the Chair of ARCo.

1 Guidance on Risk Management, Internal Control and Related Financial and Business Reporting, published September 2014.

Executive responsibility

Within the Senior Managers Regime framework, the Governor has overall executive responsibility for risk and ensures that the Bank has a risk profile consistent with ensuring the delivery of its objectives. During the year, the Governor delegated line management responsibility for oversight of the Bank's risk profile and the management of non-financial risk to the Chief Operating Officer.

In March 2017, Senior Management Responsibility for oversight of the Bank's risk profile and the management of non-financial risk moved to the Deputy Governor for Prudential Regulation, reporting to Court's ARCo on risk matters. Compliance and risk governance arrangements, including the extent to which the changes to reporting lines and internal structures are adequate, are subject to a review through the 'Non-Executives' review of Conflicts of Interest at the Bank of England', announced on 14 March 2017 (see page 73).

The Governor delegates management of the Bank's balance sheet and its financial risk through a Balance Sheet Remit to the Deputy Governors (principally the Deputy Governor Markets and Banking), and in part on to Executive Directors and Directors (principally ED Markets, and ED Banking, Payments and Financial Resilience (BPFR)). The Balance Sheet Remit governs the management of the Bank's balance sheet for both routine activities and in the event of contingencies. It sets out the high-level purposes, responsibilities, constraints and associated delegated authorities with respect to those activities.

Three Lines of Defence

The Bank operates a 'Three Lines of Defence' model to distinguish between those areas which:

1. own risk and implement controls. This is delivered by first line management. Executive Directors manage risk on a day-to-day basis within their directorates, identifying, assessing, and mitigating the risks associated with the Bank's functions, processes and systems.

2. provide independent forward-looking assessment and challenge of overall risks across operations and business lines, and define risk management frameworks and tools. This is delivered by second line risk functions, including an independent central Bank-wide risk function, a second line financial risk division and a compliance division; and

3. provide assurance that the risk management framework is robust and internal controls are appropriate and effective by independently and objectively evaluating internal controls, risk management and governance processes. This third line is delivered by the Bank's Internal Audit function as part of its role in helping Court and executive management protect the Bank and its subsidiaries.

The Bank's risk management framework

The Bank's mission is to maintain monetary and financial stability. The Monetary Policy Committee, Financial Policy Committee and Prudential Regulation Committee[1] are responsible for making statutory policy decisions, which the Bank implements. While policy formulation risks are the remit of the Committees, the implementation of policy decisions exposes the Bank to a wide variety of risks which it seeks to manage through its risk framework. It is the responsibility of the Governor/Deputy Governors to brief the relevant committee on material risk issues.

Risks to which the Bank is exposed through policy implementation include *operational* risks (such as weaknesses in processes, failure of systems, resource issues, or third party/external events), *financial risk* (impacting the Bank's capital through exposure to market, credit or liquidity risk); *strategic risk* (associated with decisions on the best way of executing policy and whether or not to pursue certain strategic initiatives) and *conduct risk*. The crystallisation of any of the above risks may also affect the Bank's credibility (or '*reputation*').

The Bank has developed a Risk Management Framework which supports a consistent and holistic approach to identifying, assessing and monitoring the risks to which it is exposed, and the actions required to mitigate them. Risk management processes and systems of internal control are embedded within its operations.

Within the framework, a Risk Tolerance Statement, owned by Court, provides an approach for managing both financial and non-financial risks within agreed tolerance levels. Generally, the Bank seeks to keep its exposure to risk low and aims to have a control environment and risk culture which supports this.

Risk assessment is forward looking and seeks to identify material risks to which the Bank may become exposed in conducting its day-to-day operations, and emerging risks from the changing external environment. For non-financial risk, a likelihood and impact matrix is used to determine a risk rating, which takes into account both the potential reputational and financial impact to the Bank in the event of a risk crystallising. Where risks are assessed as out of tolerance, action plans are developed to bring those risks within the Bank's tolerance threshold. The framework recognises, however, that there may be instances where the Bank chooses to accept a risk in the interests of delivering its policy objectives.

For financial risk, the Bank translates its tolerance into a set of limits and monitoring thresholds in order to facilitate day-to-day control of financial exposures and appropriate senior management involvement. In certain circumstances, informed by robust analysis, a decision may be taken by the Governors, with approval from Court, to exceed the Bank's usual limits and expose the balance sheet to significant risk of material financial loss, if it is determined that the expected benefits to monetary and financial stability outweigh the risk.

Executive Risk Committee (ERC)

The ERC oversees the operation of the Bank's Risk Management Framework, including proactive monitoring of the Bank's risk profile against tolerance and identification of emerging risks; reviewing and challenging those risks before escalation to ARCo. ERC also reviews themes and lessons from material incidents; and oversees prioritisation of mitigating actions. During the year, ERC was chaired jointly by the Bank's Chief Operating Officer and Deputy Governor, Markets and Banking. Since March 2017, ERC has been chaired by the Deputy Governor for Prudential Regulation.

1 During the financial year covered by this *Report*, this role was performed by the PRA Board.

Principal risks

As noted above, delivery of the Bank's mission exposes the Bank to a broad range of risks, of which the principal types are described below.

Operational risks

As explained above, through its policy implementation and day-to-day operations (such as the provision of liquidity to sterling markets; operation of the United Kingdom's Real-Time Gross Settlement system, and the production and distribution of banknotes), the Bank is exposed to a wide variety of operational risks. These include people risks, process and systems risks, as well as those arising from external events that would have an operational impact. In general, the Bank has a very low tolerance for operational risks which impact business-critical functions, although, as noted above, a higher level of tolerance may be agreed in order to meet specific policy objectives. Further detail on the operational risks to which the Bank is exposed is provided in Box 1.

Financial risk

The Bank is exposed to credit, market and liquidity risk in its operations to implement monetary and financial stability policies. Those operations include notes and payments systems operations as well as its operations in financial markets. Other activities, such as budget management and procurement activities, also expose the Bank to financial risk. Financial risks are managed so that the occurrence of any material loss in the Bank's operations resulting from policy decisions is a very rare event. The Bank seeks to maintain a level of its own financial resources that provides it with sufficient resilience to be able to withstand a severe but plausible scenario without its capital falling negative.

Conduct risk

The Bank has a very low tolerance for any conduct which may negatively impact its credibility and reputation. The Bank holds its staff to the highest standards of integrity. The policies and rules that underpin these standards are brought together in 'Our Code'. All employees are required to attest on an annual basis that they have adhered to the requirements of Our Code. Compliance with Our Code is monitored by a Compliance Division.

Strategic risk

An actual or perceived inability to deliver on its strategic initiatives could impact the achievement of the Bank's mission and consequently damage its reputation. The Bank has a low tolerance for threats to the effective delivery of its strategic initiatives.

Exchange Equalisation Account

The Bank acts as agent for HM Treasury in managing the United Kingdom's foreign currency assets and gold reserves, and its foreign currency liabilities. These funds are not held on the Bank's balance sheet, but in HM Government's Exchange Equalisation Account (EEA). The risks incurred in conducting this business are similar to those in relation to the Bank's own business, namely credit, market, liquidity and operational risk and the controls are applied and monitored alongside those applied in respect of Bank business. The management of the EEA is conducted within a framework agreed annually with HM Treasury, which is described in the EEA Report and Accounts published by HM Treasury. The Executive Director for Markets reports quarterly to HM Treasury on major risks, incidents and control issues on the EEA.

Box 1
Examples of types of operational risk to which the Bank is exposed

Information security risks
The Bank seeks to operate within a highly secure environment which protects its people, data, systems and digital assets from cyber threats through robust technology solutions, security policies and processes. The Bank has established processes for data integrity and compliance with legal requirements. Its tolerance for compromise of IT security, data integrity, or core operational systems is low.

Physical security risks
The Bank aims to have high standards of physical security and to operate robust incident management processes to protect its people and physical assets from external or internal threats. Its tolerance for compromise of physical security is very low.

People risk
The Bank is committed to attracting and retaining people of the highest calibre and relevant experience, and aims to be fully and appropriately resourced. It seeks to mitigate the risk of the loss of key skills and experience through talent management, training, and motivating and developing staff to fulfil their potential. The Bank has a low tolerance for resourcing risks which impact the delivery of its mission.

Process risks
The Bank has in place business processes to support development and delivery of policy and to ensure compliance with legal requirements. Processes are managed through control frameworks and independent review. It has a low tolerance for process failures which impact negatively on the outcomes of business-critical functions.

Business continuity risks
The Bank aims to maintain the capability both to respond effectively to, and recover safely from incidents that could affect its people, operations or credibility. It gives priority to providing stable, high-availability systems to support its business-critical activities, in particular the provision of payment and settlement services, and critical banking services. Its tolerance for disruption to transaction-processing capabilities is low. Its tolerance for outages of critical business systems is very low.

Outsourcing and procurement risks
The Bank uses third parties in some areas to assist delivery of its mission; this exposes it to risk from the poor performance or failure of those parties, and risk to its reputation through association should such a third party act in a way that is inconsistent with its standards. Risk management is a key consideration in the Bank's outsourcing and procurement. The Bank has a very low tolerance for poor performance of third parties and breaches of its ethical standards.

Health and safety risks
The Bank aims to create a safe working environment which is fully compliant with legal requirements. It has a very low tolerance for any actions or behaviours which may cause harm to its staff.


SIR JOHN SOANE 1753 183

Corporate social responsibility

'Doing Good Together' is the Bank's commitment to Corporate Social Responsibility (CSR). It is an expression of the values we share, and of how we deliver our mission responsibly and sustainably by embedding a culture where we value our people, support our community and protect our environment.

Over the past year we have increased our focus and energy on CSR by developing our strategic vision and centralising our CSR work so we can actively co-ordinate the varied range of activities across the Bank.

In this review we detail the key initiatives that the Bank has undertaken in support of our CSR aims. Highlights include: the development of a new Inclusion Strategy launched as part of 'Inclusion Fortnight'; working together to raise a record of over £250,000 for our charities of the year The Lily Foundation and Myotubular Trust; the release of a short film 'This is Me in the City' to help end the stigma around mental health; and the creation of our new environmental programme 'Greener Bank'.

Inclusion

The Bank recognises that we need to build a culture that values diverse ideas, encourages open debate, and empowers people at all levels to take initiative if we are to unlock the full potential of all our people.[1]

In support of that aim we continue to develop a culture at the Bank where everyone can contribute their best work. Through this agenda we aim to build greater diversity across the Bank to reflect the society we serve; support a proactive approach to wellbeing to support our staff; and use our influence and experience to create a positive impact in society and inspire colleagues to get involved with the community.

To celebrate and support our inclusive culture the Bank came together for an 'Inclusion Fortnight' with over 20 events held over ten days, across four sites, and attended by almost 1,700 people, including the Governor and Deputy Governors. This was successful in helping us step back and consider what more we can all do to continue to promote our work on community, diversity and wellbeing.

Our people are reaping the benefits of our efforts to be a more inclusive organisation. In our latest Viewpoint staff survey, two thirds feel encouraged to try new ideas, three quarters believe that their manager acts on people's suggestions and ideas, and 60% feel comfortable speaking up on important issues. We have improved on all of these measures over the past year but we know we need to do more.

Diversity

The Bank of England is committed to attracting and inspiring the best people to public service. We view this as our duty to the people of the United Kingdom. We also believe it is necessary if we are to reach the right policy and operational decisions in support of our mission.

In 2016 the Bank ran its second employee survey 'Viewpoint', to receive feedback on how we can make the Bank a more effective and better place to work. We were encouraged to see that close to 80% of staff responded positively to the statement 'The Bank takes diversity seriously' (a rise of 5 percentage points over the previous year), and more than 60% believed that over the past year they 'had seen progress in supporting the Bank's diversity aspirations and goals' (a rise of more than 10 percentage points).

Inclusion Fortnight

80%

of staff believe we take diversity seriously

1 'Reflecting diversity, choosing inclusion', speech by Mark Carney, February 2017, available at www.bankofengland.co.uk/publications/Pages/speeches/2017/958.aspx.

Targets

To meet our diversity aspirations the Bank has set itself some challenging, but achievable, targets to broaden the range of thought, skills and experience within the institution. This is supported by a rigorous approach to monitoring progress including through annual review and challenge by Court. In support of our aspirations to adhere to best practice on transparency and diversity we have also adopted the relevant recommendations for reporting under the Gadhia Review for both gender and BAME.[1]

The targets we have set ourselves are to triple both the proportions of female staff in our senior roles relative to the start of the Strategic Plan, to 35% by 2020, and of BAME employees in these roles to 13% by 2022. Across the remainder of our staff, we have set a target of 50% female, and 20% BAME by 2020.

Setting challenging targets has been instrumental in the progress we have made over the course of the Strategic Plan. Nevertheless our key objective is to see year-on-year progress and to build a culture where over time targets are not necessary. During 2016/17 senior management female representation increased from 28% to 30%, and female representation below senior management rose from 44% to 45%.

BAME representation below senior management has risen from 17% to 18%. The representation of BAME staff at the Bank substantially exceeds that for the UK population (at 12%), though it is below that for London (at 37%).[2] However we still have some way to go to increase the representation of BAME staff in senior management as this remained unchanged over the year at 6%.

Recruitment

To help us meet our diversity targets we are changing the way we recruit new staff and support the careers of existing staff. This year we hired graduates from over 40 UK universities (four times as many as a decade ago), attracting students from a range of socio-economic backgrounds. Two fifths were female and a quarter came from a BAME background. Only half of these students studied economics. Moreover, a fifth of our applicants were from lower socio-economic backgrounds.

We are also continuing our efforts to increase awareness of the Bank in underrepresented communities through our African Caribbean Scholarship programme which offers summer internships to candidates from lower-income households and provides specific feedback on their performance and career mentors. In 2016/17, over 2,000 applicants applied for support from the Bank to cover their tuition fees, with an overall cost to the Bank of £93,000.

We have also continued our work with external recruitment consultants and professional networks such as 'We Are The City' to enhance the diversity of our workforce and to help us harness the talent within minority groups. To support this programme of engagement the majority of our senior management population have taken unconscious bias training and we have committed to ensure that wherever possible, we will create diverse shortlists for jobs and interview people with diverse panels in order to mitigate affinity effects and unconscious biases. In that way we can make sure we recruit the best people to public service from a variety of backgrounds.

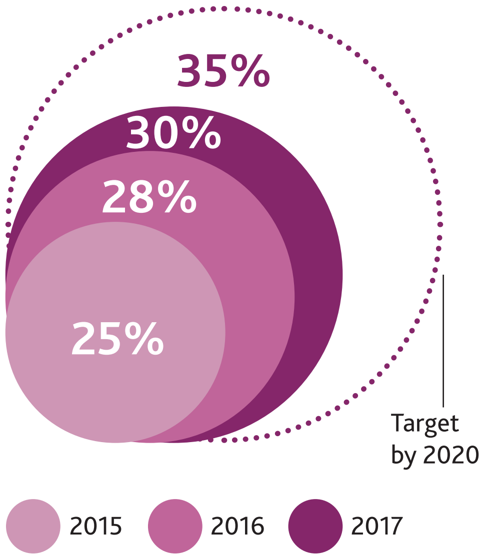
Our African Caribbean Scholarship programme

1 'Empowering productivity: harnessing the talents of women in financial services', https://uk.virginmoney.com/virgin/assets/pdf/Virgin-Money-Empowering-Productivity-Report.pdf.

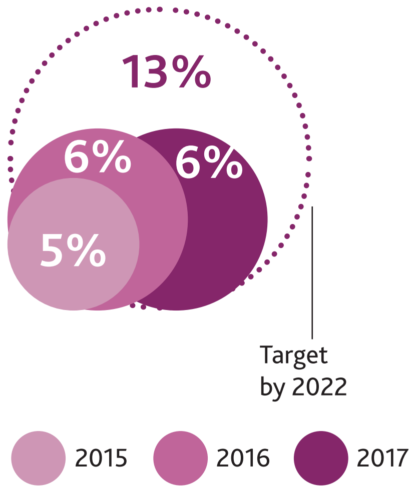
2 Data for the United Kingdom are taken from the February 2017 release of the ONS's Labour Market Status by Ethnic Group. Data for London come from the latest UK Census taken in 2011.

Diversity and inclusion metrics

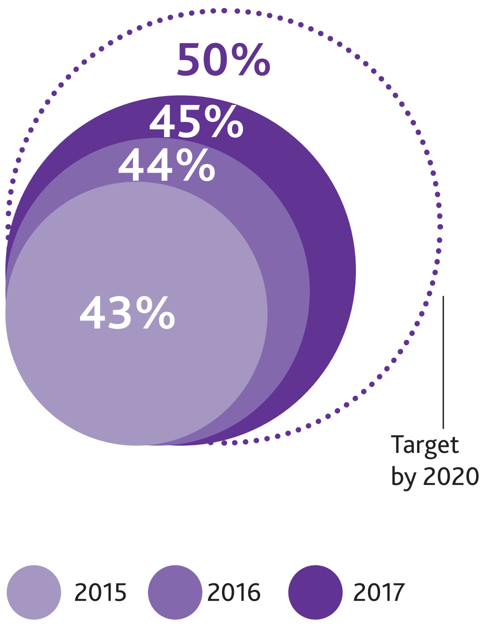
Female representation Senior management



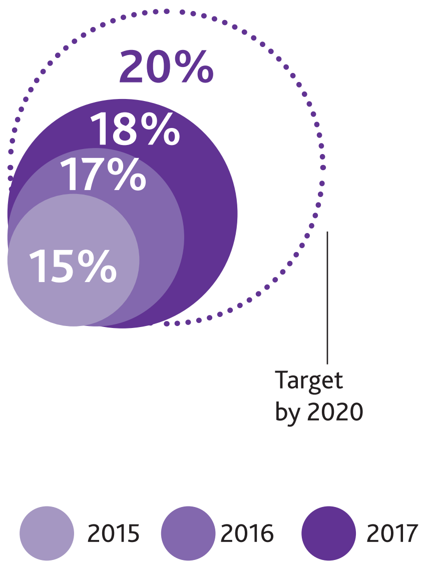
BAME representation Senior management



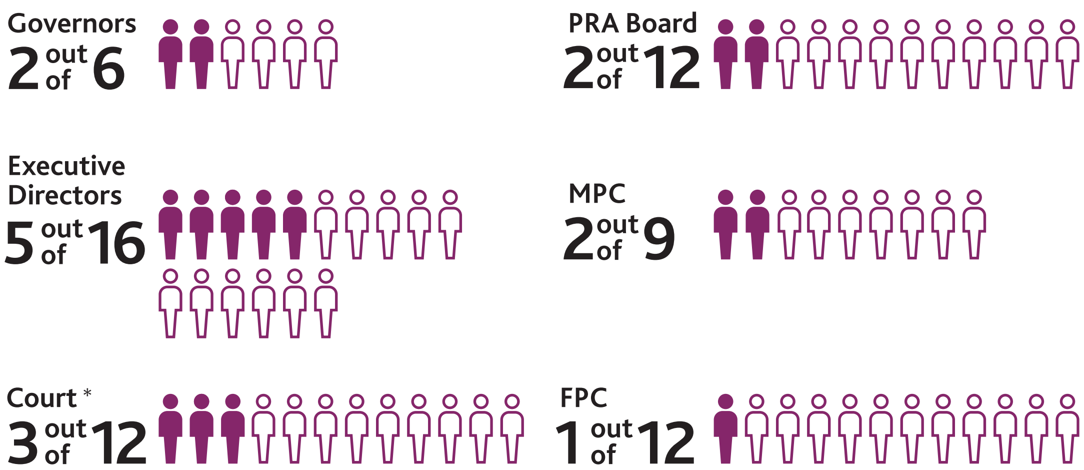
Female representation Below senior management



BAME representation Below senior management



Female representation among the Executive and Committees at 28 February 2017



* On 31 July 2017, Court membership was corrected from '2 out of 11' to '3 out of 12'.

Female representation

Of those newly hired

2015	41%
2016	42%
2017	44%

Of those promoted

2015	44%
2016	43%
2017	43%

Of those working part-time

2015	82%
2016	83%
2017	83%

Of those leaving the Bank

2015	34%
2016	37%
2017	40%

BAME representation

Of those newly hired

2015	21%
2016	23%
2017	25%

Of those promoted

2015	16%
2016	17%
2017	16%

Of those working part-time

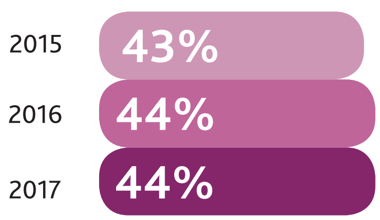
2015	11%
2016	12%
2017	11%

Of those leaving the Bank

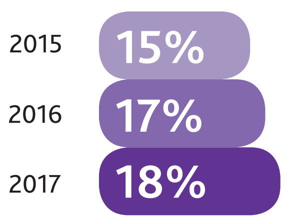
2015	20%
2016	18%
2017	25%

Overall split

Female representation



BAME representation



Female and BAME representation across the functions of the Bank

	Female (per cent)			BAME (per cent)		
	2015	2016	2017	2015	2016	2017
Governor's Office	62	66	**64**	10	14	**19**
Chief Operating Officer's Unit	38	36	**37**	15	18	**16**
Financial Stability	36	39	**42**	15	13	**13**
Markets and Banking	47	49	**50**	13	14	**16**
Monetary Policy	46	48	**48**	10	11	**12**
Prudential Regulation Authority	42	43	**43**	20	20	**20**

Overview
Court, and the Bank's policy committees
Our organisation
Review of 2016/17
Financial Stability Strategy
Financial review 2016/17
Risk management and business practices
Corporate social responsibility
Report of the Remuneration Committee
Report on Oversight Functions
Report of the Audit and Risk Committee
Statement of the responsibilities of the Court of Directors in relation to the financial statements
Financial statements
Contacting the Bank of England

Recruitment (continued)

Of the 700 experienced professionals we hired last year, almost half were women and a quarter came from a BAME background, up from two fifths and one fifth respectively since our Strategic Plan was launched.

In recognition of our efforts the Bank received an award from the Employers Network for Equality and Inclusion for inclusive recruitment and was also highly commended for the representative workforce award.

We also received a Blue Badge Style award for our new wheelchair access at the Bank's front entrance on Threadneedle Street which has greatly improved access for wheelchair users. Currently 3% of our staff have declared they have a disability. This is unchanged from last year.

Declaration and monitoring

Promoting an inclusive working environment is also one of our key values in support of our Diverse and Talented aspirations. We are encouraged that the number of staff that have disclosed themselves as lesbian, gay, bisexual and transgender has continued to rise from 2½% last year to over 3% this year, which is above official estimates for the UK population (at 1.7%). These higher disclosure rates demonstrate we are developing an organisation where staff can be themselves. Flexible working is also encouraged and all Bank colleagues are able to work flexibly within their standard contracts where businesses allow it. Currently 12% of our staff work part-time compared to 11% last year. We ask our staff to tell us if they are a carer or have a requirement for reasonable adjustments to the workplace. In this way we are striving to meet the needs of all our staff.

Employee network groups

The Bank supports inclusion through a number of widely supported diversity and inclusion employee network groups. Membership numbers have continued to increase, as has participation in network speaker and development events. These networks celebrate the diversity of our staff, help to promote awareness and understanding across the institution, as well as provide support to their members.

Key initiatives this year were the introduction of a new Parents Network; our Carers Network's work with 'Employers for Carers' which brought together organisations from across the City of London to discuss how to improve support for carers in the workplace; our Bank of England Ethnic Minorities Network's sponsorship of a second round of the 'Building Bridges' reciprocal mentoring scheme between senior management and BAME staff; and our Mental Health Network launch of the film 'This is Me in the City' where colleagues talked openly about the impact mental health issues have had on their lives. We were also pleased to celebrate the LGBT Network's 10th birthday this year, and this year for the first time we flew the Pride Flag on top of our Threadneedle Street building.

Community

The Bank has a long history of community involvement, and supporting the voluntary sector continues to be an important part of the Bank's culture. The Bank encourages staff to become involved in initiatives that maximise the Bank's positive impact and influence in the community.

To support our community work we have recently rolled out our 'Community Champions': a network of community-minded people across the Bank to help promote the range of community-orientated opportunities that staff can get involved with, and to help the Bank shape its future community activities.

Our award-winning new wheelchair access

Flying the Pride Flag

Volunteering

The Bank offers its employees paid leave to perform voluntary duties in the community, or to undertake public and civic duties in a way that caters for a variety of staff levels and time commitments. Volunteering helps us to build relationships with our communities, support recruitment and retention, and provides real situations in which to develop our skills.

During 2016/17 staff were involved in 785 days of community activity (2015/16: 586 days) either through personal volunteering and civic duties or through participating in the Bank's community programme. The Bank estimates the total value of non-cash community contribution, including time spent by staff on community involvement, travel costs for volunteers and the costs of hosting charitable events at the Bank, to be £460,000 in 2016/17 (2015/16: £405,000), of which £262,000 was for staff time involved either in volunteering and undertaking civic duties or volunteering leave.

During this year we welcomed 140 students from the local community for work experience. In recognition of our volunteering work the Bank was Highly Commended for Outstanding Volunteering in 2016 in The Brokerage Citylink's 20th Anniversary Awards. We also received an award for Outstanding Work Experience Provider Host from the Tower Hamlets Education Business Partnership.

Charitable giving

The Bank and its employees also support local and national communities through a range of schemes that support charitable giving. Through our matched funding scheme the Bank helps staff raise monies for the charities and causes they are committed to. We also have an aspiration that all staff events have a charitable aspect.

The Bank supports two charities each year, as chosen by staff. This year, Bank staff chose The Lily Foundation and the Myotubular Trust and raised over £250,000 through various fundraising activities including the proceeds from our charity banknote auction. Due to the auction, the proceeds of which were £194,500, the monies raised were higher than normal and will have a lasting impact on both charities. The Lily Foundation will use the majority of funds raised to support their recently extended research strategy which now looks at both diagnostics and finding treatment options for mitochondrial disease. The Myotubular Trust is also using the funds raised for a wider set of research projects into treatments for myotubular myopathy. A final share of the proceeds from the banknote auction was donated to Bliss who work to provide care and support for all premature and sick babies and their families. Bliss was chosen by staff in our Notes Directorate who undertook the work involved in launching the new polymer £5 note.

The Bank continued to be one of the few recipients of a Platinum Award from Pennies from Heaven. Nearly a half of our staff currently round down their monthly income and donate this money to charity via the Pennies from Heaven scheme.

During 2016/17, the Bank contributed a total of £1,055,000 in support of its community programme (2015/16: £935,000). Cash donations totalled £765,000 (2015/16: £530,000). More detail is provided in the annex.

No donation was made for any political purpose in 2016/17 (2015/16: nil). And no paid leave was granted to staff for political purposes (2015/16: nil).

Our charities of the year

Lily x

myotubular trust FINDING STRENGTH 10th ANNIVERSARY

We were highly commended for our volunteering...

THE BROKERAGE CITYLINK

...and won an award for outstanding work experience

Tower Hamlets Education Business Partnership

Wellbeing

The Bank provides a wide range of services, benefits, initiatives and policies to support staff in managing their mental, physical and social wellbeing.

These include: a regular series of 'Working Life Seminars' that offer practical advice on work and family issues including techniques such as mindfulness and personal resilience; an Employee Assistance Programme that offers counselling and additional support; access to accredited in-house counsellors who work closely with the Bank's medical team; and benefits including discounted gym memberships and flexible leave options.

Over the past year the Bank has put in place a number of initiatives in support of our wellbeing goals, and these have been reinforced by an array of local initiatives. We have launched a network of 'Wellbeing Champions' across the organisation who help to communicate the importance of our Wellbeing agenda to their local area and act to raise awareness of the range of support available to staff.

Training and support

The Bank has completed its participation in a pilot study commissioned by the Bank Workers Charity and Mind, and independently evaluated by the Chartered Institute of Personnel and Development, to deliver a mental health training programme for line managers. This work has helped us better understand the positive impact that mental health training can have for managers and their teams.

New managers now attend an interactive session on how to create a supportive, inclusive culture as part of their induction. Managers also have access to training on dyslexia and dyspraxia so that staff with these conditions can reach their full potential.

Our Viewpoint survey showed that our Wellbeing agenda is making a real difference to our staff with close to 90% feeling that they are treated with respect as an individual, and two thirds saying that there is a good balance between their work and personal life. Our efforts are also helping to build staff engagement: around 500 employees attended our Wellbeing Fair which was run as part of the Bank's Inclusion Fortnight.

Environment

Key to the Strategic Plan is a commitment that we will be accountable for our actions and their consequences. This extends to our responsibility to minimise the impact the Bank has on the environment. This means taking active steps to improve our energy efficiency, reduce our consumption of natural resources, and manage our waste production and disposal.

This year we brought together all our initiatives under a coherent environmental programme called 'Greener Bank'. This includes hiring new specialised resources, mapping our key environmental impacts and establishing our carbon footprint.

We have also launched an employee-led network of close to 50 'Green Champions' across the Bank who have been instrumental in driving through local initiatives such as improving our recycling facilities and switching to more environmentally-friendly paper.

90%

of staff feel that they are treated with respect as an individual

Our new environmental programme

Carbon emissions
In support of our commitment to reduce our carbon emissions the Bank has established its carbon footprint and has worked with the Carbon Trust to independently verify our starting position. During 2016/17 the Bank's total emissions of CO_{2e} was 24,846 tonnes (2015/16: 25,534 tonnes) or 5.8 tonnes (2015/16: 6.4 tonnes) per full-time equivalent staff. Looking forward, we have set ourselves a challenging target of a 20% reduction in our carbon emissions by 2020. This is our first carbon reduction target and it will be reviewed regularly to ensure it reflects any material changes to how we operate. Our main areas of focus to meet our target are to increase the energy efficiency of our building, reduce our use of resources, and work with colleagues to adopt more environmentally friendly business practices.

Energy management
The Bank continuously controls and monitors the status of building services including: lighting, heating, cooling, ventilation and environmental control. This year we have begun a programme of in-depth energy audits to help us identify ways in which we can further reduce our energy consumption. We have also identified over 10% in potential energy savings (equivalent to a reduction in carbon emissions of over 1,000 tonnes) through RE:FIT London which is an award-winning programme to help make London's public buildings and assets more energy efficient. We have now appointed a partner using the RE:FIT London framework to help us continue to improve our energy use.

Travel
During the year we have launched a number of initiatives to help us reduce the carbon impact of our travel. For instance some of our executive cars have been replaced with electrical vehicles, a greener alternative to diesel. And to support colleagues who want to reduce their carbon footprint we have a Cycle to Work scheme and a very active employee-led Bicycle User Group.

Waste and resources management
Our primary focus this year has been to reduce the volume of waste we produce and to increase the amount of recycling we do. For instance we are working to replace disposable catering items with reusable options. So far this has led to a 40% reduction in disposable cups being used across the organisation. We have now set ourselves the stretching target that by the end of 2017 all our current disposable catering items will be replaced with reusable or fully recyclable alternatives. To support that we have also put in place food waste collections and coffee grounds recycling in a number of areas of the Bank.

In recognition of our work on waste and resources management we were presented with a Platinum Award by the City of London as part of their Clean City Awards Scheme.

Banknotes
The Bank recycles banknotes that are returned unfit for use. More than 700 million paper banknotes (equivalent to over 1,000 tonnes) are turned into briquettes that are used to make compost for agriculture. Looking forward, the Bank has secured a UK-based recycling solution for returned polymer banknotes.

Overall, the Bank's decision to move to polymer notes will deliver lasting environmental benefits. These stem from the reduced environmental burdens associated with raw material production and processing of new banknotes to replace unfit ones with polymer banknotes lasting at least 2.5 times longer than paper notes. The Bank is working closely with the Carbon Trust to obtain independent certification of the expected carbon reduction benefits of polymer notes compared with paper notes.

Carbon emissions target

↓20%

by 2020

Clean City Awards

Health and safety

The Bank attaches the utmost importance to the health and safety of its staff. Through its safety management system the Bank delivers a safe working environment and promotes and maintains a positive health and safety culture.

Monitoring the performance of the system is an integral part of effective safety management and demonstrates the Bank's commitment to ensuring the health, safety and welfare of all persons who enter Bank premises. Consequently, the Bank monitors its performance on a regular basis, and reports annually to Court.

Following a recent review the Bank committed to utilise the Institution of Occupational Safety and Health's Reporting Performance Guide to set the Bank's performance indicators. This will lead to improvements in objective setting and management information in support of the Bank's commitment to health and safety.

Bank of England employees work in a relatively low-risk environment and are not exposed to significant occupational health and safety hazards. During 2016/17 there were a total of 20 recorded accidents involving employees and one reportable injury as defined by the UK Health and Safety Executive's reporting of Injuries, Diseases and Dangerous Occurrences. Overall, the Bank's Annual Injury Rate was 27 which compares favourably against the benchmark for similar institutions published by the Health and Safety Executive.

Ethics and conduct

Our ability to achieve our mission relies on public trust. To maintain that trust it is essential that the Bank holds itself and its staff to the very highest ethical standards.

Our Code

Our standards on ethics and conduct are embedded in Our Code. Our Code represents our commitment to how we work at the Bank of England and how we should conduct ourselves both within and outside the Bank. It applies to all staff including Governors, MPC, FPC and PRC members.

Our Code is based on five principles that are drawn from the Nolan principles of public life, the values we established in the Strategic Plan, and the principles we require of others under the Senior Managers Regime. They are: acting with integrity; creating an inclusive environment; demonstrating impartiality; being open and accountable; and feeling empowered.

Our staff are required to attest as new joiners and on an annual basis, confirming that they have read, understood, and complied (as appropriate) with the policies in Our Code. As part of Our Code we also expect our staff to escalate any concerns they have through the Bank's 'Speaking Up' policy. The Bank has set up a central compliance division to support Our Code and other policies. This function reports to the General Counsel and independently to the Audit and Risk Committee, and through them to Court.

Conflicts of interest

During the year Court approved new conflict of interest codes for the MPC, FPC and PRC. Following Charlotte Hogg's resignation in March, Court has also appointed a committee of Non-executive Directors to review and evaluate the Bank's approach to identifying and managing potential conflicts of interest and the supporting governance arrangements (see page 73).

Annex

Cash donations

During 2016/17 cash donations totalled £765,000 including:

- £82,000 to community organisations via the Staff Volunteering Award Scheme;
- £60,000 to charities supported by the Bank's regional Agencies;
- £50,000 to match record staff fundraising for the staff charities of the year;
- £32,000 matched funding under the Payroll Giving Scheme;
- £15,000 via the Bank of England Court Awards through which donations are made to community organisations in recognition of outstanding volunteering contributions by members of staff;
- £168,000 made to partner charitable organisations and membership subscriptions;
- £10,000 for the David Sharp School Governor Awards; and
- £115,000 in donations to support academic research.

Carbon footprint (Greenhouse gas emissions)[1]

		2016/17		2015/16	
Type of emissions	Activity	tCO_{2e}	% of total	tCO_{2e}	% of total
Direct (Scope 1)	Natural gas	3,158	12.7	3,320	13.0
	Oil — generators	49	0.2	5	0.0
	Vehicles fleet	151	0.6	97	0.4
	Subtotal	**3,358**	**13.5**	**3,421**	**13.4**
	Refrigerants	138	0.6	n.a.[2]	
	Subtotal	**3,497**	**14.0**	**3,421**	
Direct (Scope 2)	Electricity	15,079	60.6	16,195	63.4
	Subtotal	**15,079**		**16,195**	
Indirect (Scope 3)	Electricity — T&D[3]	1,364	5.5	1,337	5.2
	Air travel	4,710	18.9	4,334	17.0
	Rail travel	39	0.2	34	0.1
	Water	75	0.3	83	0.3
	Office paper	86	0.3	96	0.4
	Waste	39	0.2	34	0.1
	Subtotal	**6,312**		**5,918**	
Total gross emissions (tCO_{2e})		**24,888**		**25,534**	
Intensity metric					
Number of full-time equivalent staff		4,261		3,983	
Tonnes of CO_{2e} per full-time equivalent staff		5.84		6.41	

1 Figures may not sum to total due to rounding.

2 Emissions associated with the use of refrigerants were not accounted in 2016.

3 T&D — carbon emissions associated with the Transmission and Distribution of electricity from its production point to the end user.

Assessment parameters

Baseline year	2015/16
Reporting organisation	Bank of England
Person responsible	Energy and environmental manager
Reporting period covered	1 March 2015–29 February 2016/1 March 2016–28 February 2017
Organisational boundaries	Facilities over which the Bank of England has operational control
Methodology used	ISO 14064-1 and DEFRA Reporting guidelines (2013)
Emissions factors used	UK Government conversion factors for Company Reporting set
External verification 2016 baseline	Limited assurance to ISO 14064-3 provided by the Carbon Trust
Exclusions	Emissions associated with the use of refrigerants were not accounted in 2016

Report of the Remuneration Committee

The Remuneration Committee (RemCo) determines the remuneration of the Governors, and advises Court on the remuneration of other senior executives and of the external members of the MPC, the FPC and the PRC (formerly the PRA Board). The Committee also advises on major changes to remuneration structures within the Bank, including pension schemes. The Committee's aim is to ensure the remuneration policy and all remuneration decisions support the Bank in recruiting and retaining the people it needs, taking account of the market in which we operate in and our duty to work in the public interest. The Committee takes account of external comparisons from the public and private sector when reviewing policy and making remuneration decisions.

During 2016/17 the Bank continued to embed the 2015 One Bank remuneration framework, which aligned the framework for pay, pension and benefits for Bank and former Financial Services Authority (FSA) colleagues. This introduced a new set of salary scales, a fixed benefits allowance of 7% and a discretionary performance award budget of 10% for all colleagues up to and including Executive Directors. The One Bank transformation also introduced a single Career Average pension scheme (CARE), and the Bank's final salary scheme was closed to new accrual in April 2015 (it had been closed to new members since 2007). A key intention of the changes was to offer colleagues a degree of choice, including the ability to exchange pension accrual for additional income and *vice versa*, and to stop pension accrual entirely when tax limits were reached. This approach has been effective in creating consistency across the Bank and enabling internal movement of talent, and it has also moderated the growth of future pension liabilities.

The Governors

The remuneration structure for Governors remains straightforward. In addition to their annual salaries, the Governors are eligible to participate in the Career Average section of the Bank Pension Fund. When relevant tax limits are reached they may choose to reduce their accrual rates or to opt out altogether, receiving a salary supplement of 30% in lieu of pension. They may also choose to increase pension accrual subject to a reduction in salary calculated at rates consistent with the Bank's funding valuation. They do not receive a benefits allowance or any performance awards or other performance-related pay.

The Committee has permitted pay increases for Governors in line with public sector norms. In the latest year this has meant increasing the Deputy Governors' pay by 1%. As in previous years Mr Carney declined to accept the increase.

Governors' remuneration policy

The Governor is appointed by the Crown for a non-renewable term of eight years, and Deputy Governors are each appointed by the Crown for five-year terms, which may be renewed once. As office-holders, the Governors have no termination provisions, although RemCo has discretion to impose a period of restricted duties, for which they will be paid for up to six months, before individuals can accept roles outside the Bank.

Following the announcement of Andrew Bailey's appointment as CEO of the Financial Conduct Authority (FCA), Sam Woods was appointed Deputy Governor for Prudential Regulation and CEO of the Prudential Regulation Authority with effect from 1 July 2016. Mr Woods' new salary and pension arrangements match those of the other Deputy Governors.

Since there was no conflict between Mr Bailey's new role at the FCA and his position in the Bank, the Committee imposed no period of restricted service. They did however impose a three-month restriction on Dame Minouche Shafik, the Deputy Governor for Markets and Banking, who resigned to take up, later in the year, a role as Director of the London School of Economics; she left the Bank on 28 February.

Under the Bank of England Act 1998, Governors and Deputy Governors are required to provide remunerated services only to the Bank. With Court's approval other directorships relevant to the Bank's work may be accepted, but any fees must be waived or surrendered to the Bank. Directorships held during the past year have been the (statutory) appointment to the Financial Conduct Authority Board held by Mr Bailey as Deputy Governor for Prudential Regulation and subsequently by Mr Woods; and Mr Carney sits on the Board of the Bank for International Settlements, as did Sir Jon Cunliffe until 31 December 2016.

The Committee keeps under review other benefits available to the Governors. It is the Bank's policy to provide for relocation support as necessary to those appointed to senior positions. Mr Carney receives, as was announced on his appointment, an annual accommodation allowance of £250,000 per annum to reflect the additional cost of living in London rather than in Ottawa. Insurances and health checks were the principal other non-salary benefits received by Governors during the year.

Overview
Court, and the Bank's policy committees
Our organisation
Review of 2016/17
Financial Stability Strategy
Financial review 2016/17
Risk management and business practices
Corporate social responsibility
Report of the Remuneration Committee
Report on Oversight Functions
Report of the Audit and Risk Committee
Statement of the responsibilities of the Court of Directors in relation to the financial statements
Financial statements
Contacting the Bank of England

Governors' remuneration

	Mr M J Carney		Mr A J Bailey		Dr B Broadbent		Sir Jon Cunliffe	
£	2016/17	2015/16	2016/17	2015/16	2016/17	2015/16	2016/17	2015/16
Base salary	480,000	480,000	90,209	267,946	268,170	240,928	270,626	267,946
Taxable benefits	253,365	251,734	628	578	1,187	578	1,798	1,518
Pension benefits	12,510	145,584	–	–	63,401	104,586	–	–
Payment in lieu of pension	132,000	–	27,063	80,384	23,071	–	81,188	80,384
Total pension benefits	**144,510**	**145,584**	**27,063**	**80,384**	**86,472**	**104,586**	**81,188**	**80,384**
Other remuneration	2,167	2,167	764	1,402	974	1,402	1,413	1,438
Total remuneration	**880,042**	**879,485**	**118,664**	**350,310**	**356,803**	**347,494**	**355,025**	**351,286**

	Ms C Hogg		Dame Minouche Shafik		Mr S Woods	
£	2016/17	2015/16	2016/17	2015/16	2016/17	2015/16
Base salary	270,626	267,946	270,626	267,946	180,417	–
Taxable benefits	–	–	1,978	10,832	2,254	–
Pension benefits	85,311	81,765	70,670	82,009	60,305	–
Payment in lieu of pension	–	–	13,396	–	–	–
Total pension benefits	**85,311**	**81,765**	**84,066**	**82,009**	**60,305**	**–**
Other remuneration	1,465	1,444	974	1,444	607	–
Total remuneration	**357,402**	**351,155**	**357,644**	**362,231**	**243,583**	**–**

The following table shows accrued pension for those Governors who remained active members of the pension scheme

	Accrued pension as at 28 Feb 17 £p.a.	Accrued pension as at 29 Feb 16 £p.a.	Increase in accrued pension £p.a.	Pensionable age
Mr M J Carney	20,610	20,000	610	65
Dr B Broadbent	11,157	8,000	3,157	65
Ms C Hogg	12,145	7,900	4,245	65
Dame Minouche Shafik	10,040	6,500	3,540	65
Mr S Woods	5,087	2,071	3,016	65

Remuneration of Non-executive Directors

The Bank of England Act 1998 provides for the remuneration of the Non-executive Directors to be determined by the Bank with the approval of the Chancellor of the Exchequer. With effect from 1 June 2009, these rates were set at £15,000p.a. for Directors, £20,000p.a. for Committee Chairs, and £25,000p.a. for the Senior Independent Director and Deputy Chair. The Chair of Court is paid £48,000p.a. Non-executive Directors do not receive any post-retirement or medical benefits from the Bank, nor any additional fees for serving on Committees. The Bank meets appropriate travel and subsistence expenses.

External members of the FPC, the MPC and the PRC

The external members of the FPC, the MPC and the PRC are appointed on a part-time basis, and their remuneration reflects the different time commitments involved for each committee. In 2016/17, the external members of the FPC were each paid at a rate of £92,990p.a., independent PRA Board members were paid at a rate of £104,900 and the external MPC members were paid £149,682. For 2017/18, all fees were increased by 1%. MPC members, who work on average three days a week in the Bank, are also entitled to join the Bank's private medical insurance scheme.

Members of the policy committees (including the PRC) must not during their terms of office retain or accept other appointments or interests that would create a conflict with their responsibilities at the Bank. On leaving the Bank, members are paid their fee for a further period of three months, during which time the Bank has the right to veto any employment that would conflict with their former FPC, MPC or PRA responsibilities, and requires continued adherence to the relevant committee's code of conduct.

Executive Directors' salaries and benefits

The remuneration framework for Executive Directors is consistent with that offered to all colleagues across the Bank, comprising a salary commensurate to their role, a 7% flexible benefit allowance, discretionary performance award budget of 10% and a Career Average defined benefit pension.

The table opposite shows, for Executive Directors serving at the end of 2016/17, the first two elements of their remuneration as well as their individual pension accrual rates. In recommending salaries for Executive Directors the Committee takes into account the differences in their pension accrual so as to achieve a greater consistency in their total remuneration. In recommending individual performance awards the Committee takes account of both performance against objectives and values.

A key feature of the Bank's pension scheme is that it allows individuals to vary their rate of pension accrual annually, either by surrendering pension accrual for a cash supplement or by sacrificing salary to secure more pension. Each year the Committee reviews and approves the rates at which pension is exchanged for cash and *vice versa* to ensure they are consistent with the scheme funding valuation, and updated to reflect market movements and changes in actuarial assumptions. Currently these rates are elevated by the low levels of risk-free interest rates, and for 2016/17 ranged from 29% of salary (1/95th accrual) to 55% of salary (1/50th accrual). What these valuations do not take account of is the mitigation of longevity risks that result from an overall lower accrual rate, and the potential longer-term benefits to the Bank of that.

£ Year to 28 February 2017	Salary[1]	Benefits	Contractual pension accrual
Sonya Branch	207,050	16,313	1/95th
Alex Brazier	176,750	14,041	1/50th
Sarah Breeden	167,009	13,309	1/50th
Stephen Brown	162,523	12,976	1/50th
Rob Elsey	183,333	14,537	1/95th
John Footman	187,295	14,832	1/65th
Andrew Gracie	183,527	14,549	1/65th
Andy Haldane	183,909	14,578	1/50th
Andrew Hauser	176,750	14,041	1/50th
Lyndon Nelson	222,622	17,480	1/95th
Rommel Pereira	105,000	8,389	1/95th
Joanna Place	157,579	12,604	1/50th
James Proudman	175,000	13,910	1/50th
David Rule	224,794	17,643	1/95th
Chris Salmon	183,909	14,578	1/50th
Victoria Saporta	163,699	13,066	1/50th
Jenny Scott	151,411	12,142	1/65th

1 Pro-rated for those who joined the Bank, were promoted during the year or who work part-time.

The Bank's overall pension contribution is driven by both the current CARE scheme, as well as the now closed final salary scheme. Long-serving employees from the Bank will have built up a much greater accrued pension during their years of service and participation in the final salary scheme. While the final salary scheme is now closed, any increases in salary for those individuals will result in a consequent increase in their accrued pension which in turn will drive the Bank's contribution. The table below shows the accrued pension in the Bank's defined benefit schemes of those Executive Directors who were active members during the year. It also identifies those Executive Directors who have stopped further accrual and therefore receive cash in lieu at the rates listed above.

	Accrued pension £p.a. Feb 17	Accrued pension £p.a. Feb 16	Increase in pension £p.a.	Pensionable age
Sonya Branch	4,574	1,960	2,614	65
Alex Brazier**	47,288	46,656	632	60
Sarah Breeden**	60,686	59,953	733	60
Stephen Brown	30,081	27,766	2,315	60
Rob Elsey	2,102	600	1,502	65
John Footman*	–	–	–	65
Andrew Gracie	12,907	10,478	2,429	65
Andrew Haldane	86,258	83,816	2,442	60
Andrew Hauser	75,229	72,902	2,327	60
Lyndon Nelson*	–	–	–	65
Rommel Pereira	1,108	–	1,108	65
Joanna Place*	–	–	–	60
James Proudman*	–	–	–	60
David Rule**	2,782	2,546	236	65
Chris Salmon*	–	–	–	60
Victoria Saporta	59,584	47,247	12,337	60
Jenny Scott	8,252	5,161	3,091	65

*Denotes those who have opted out of further pension accrual and receive cash in lieu.

Mr Footman and Mr Nelson currently have no pension in the Bank scheme; Mr Salmon was granted a deferred pension of £73,253p.a. in 2014; Ms Place was granted a deferred pension of £87,808p.a. and Mr Proudman was granted a deferred pension of £65,490, both in 2015.

** Denotes those who have opted out during the year and their pension accrual shown is pro-rated.

Other Executives' salaries and benefits

The following table shows remuneration ranges for the year to February 2017 for all colleagues below Executive Director level with remuneration in excess of £80,000p.a. on a full-time equivalent basis, excluding employer pension contributions and performance awards. All participate in the career average defined benefit pension with flexible accrual rates, receive a flexible benefits allowance equal to 7% of base salary and are eligible for a discretionary performance award.

Remuneration range £	Number of colleagues
200,000–249,999	4
190,000–199,999	4
180,000–189,999	10
170,000–179,999	9
160,000–169,999	16
150,000–159,999	28
140,000–149,999	32
130,000–139,999	45
120,000–129,999	52
110,000–119,999	87
100,000–109,999	125
90,000–99,999	179
80,000–89,999	244
Total	**835**

Dido Harding
Chair of the Remuneration Committee

Report on Oversight Functions

Court — the Oversight Functions

Court is responsible for managing the affairs of the Bank. It also has statutory responsibilities for monitoring the Bank's performance against its statutory and other objectives, the Bank's financial management and controls, and the procedures of the policy committees, whose meetings non-executive members of Court are entitled to attend as observers.[1] Court is required to make an annual report on these 'Oversight Functions'. The Review of 2016/17 (pages 17–31), the Financial Review (pages 36–42), the Report on Risk Management and Business Practices (pages 44–48), the statement on Corporate Social Responsibility (pages 50–62), and the Reports of the Remuneration Committee (pages 63–69) and the Audit and Risk Committee (pages 75–78) should be seen, insofar as they relate to Court's oversight responsibilities, as part of this Report.

The policy committees

The objectives of the policy committees — the FPC, the MPC and the PRC[2] — are objectives of the Bank and while strategic and tactical decisions are taken by the Committees themselves, Court keeps their performance under review, with the non-executive members observing their meetings and receiving regular reports at Court. It also keeps under review their processes and, in the case of the MPC, is required to determine whether the Committee has collected the regional, sectoral and other information necessary for formulating monetary policy.

Court is responsible for formulating the Bank's Financial Stability Strategy. It is permitted to delegate that function, and has delegated it to the FPC: the strategy determined by the FPC is on pages 32–35 of this *Report*.

The FPC's agenda and workload has increased considerably over the past year, reflecting the external environment (for example, the United Kingdom's withdrawal from the EU), some internal governance changes (such as delegation to the FPC to review the Bank's Financial Stability Strategy), and the FPC's own reviews, often statutory, of its previous actions. Nevertheless, FPC members felt that the process around their meetings had improved from what was already a high level.

Feedback from FPC members suggested that the staff briefings are of high quality and that meetings are effective with an increasingly busy agenda. Regular pre-briefings had contributed to the effectiveness of meetings. The Committee would be reviewing its priorities and existing commitments during the coming year. The drafting process for FPC communications had improved. The stress-testing process, conducted jointly with the PRA, was seen as working well.

FPC members were positive about joint meetings with the PRC. Further work was needed to get the full potential benefit from joint MPC/FPC meetings. MPC members shared that view.

MPC members remain very positive about the support provided by staff for the policy meetings and the *Inflation Report*. Improvements to data briefings outside the policy rounds were suggested and are being implemented; and as with the FPC there was a demand for earlier circulation of analytical notes ahead of both policy and forecast meetings. Research work and 'special topics' meetings were seen as good, and external members rated highly the support provided by their own dedicated unit. The move to eight meetings a year was welcomed as giving more space for reflection, and the simultaneous publication of decisions and minutes was also thought to be working well.

In terms of processing regional and sectoral information, the work of the Bank's regional Agencies — which have between them nearly 5,000 business contacts — remains an important input to the MPC process. In terms

1 Court took over these functions from the pre-existing Oversight Committee following the adoption of the Bank of England and Financial Services Act 2016. There has been no diminution in oversight functions following the change.

2 During the year under review, the PRC assumed responsibility for the Bank's functions as Prudential Regulation Authority; the separate PRA subsidiary, governed by the PRA Board, will in due course be wound up.

of sectors, particular areas of focus for the MPC have been the property and housing market, the distribution of occupational pension deficits, and disaggregated labour market data. In August 2016 the Bank launched a 'Decision Maker Panel' which tracks 1,250 firms' expectations for various business outcomes and the probabilities attached to each. This has already helped to inform the MPC's deliberations.

Members of the PRC felt that the transition from the PRA Board on 1 March had gone well, and that the change should increase focus on thematic and strategic questions. The workload of the PRC remained high — there are two meetings each month and frequently decisions between meetings — but the current composition of the Committee allowed for effective discussions and the external members could still influence the agendas. The joint sessions with the FPC were seen to be working well — the overlap of interests was sufficient for the members of both Committees to get real benefits from the process.

Independent Evaluation Office

The Independent Evaluation Office reports directly to the chair of Court and supports the Court in discharging its Oversight Functions. The mainstay of the IEO's work is two planned, in-depth evaluations a year. Since the previous Report, the IEO has undertaken and published two studies — one into the Bank's approach to the supervision of financial market infrastructures (FMIs), the other into the PRA's approach to its insurance objective.

FMIs

The Bank's supervision of FMIs — including payments systems, securities settlement systems and central counterparties — has evolved since 2009 amid a fast-changing regulatory and technical landscape. Reflecting these changes, and in particular the push towards central clearing in the global OTC derivatives market, the Bank made significant investments in governance, staffing and supervisory capability at the time of the 2014 Strategic Plan. The IEO was asked by Court to consider whether the function was on course to deliver the step change that had been intended and also whether the Bank's approach was appropriately forward-looking and flexible. The report concluded that the investments made by the Bank in recent years had indeed had the desired effect, and noted that the Bank was an acknowledged world leader in the field; there were many examples of good practices and no material shortcomings. In the context of a fast-changing FMI landscape, there was scope to build on those gains, including by clarifying the objectives of FMI supervision, by leveraging resources available to the wider Bank as effectively as possible and by strengthening governance. The Bank in its response accepted these recommendations.[1]

Insurance objective

The PRA's general objective, which applies to insurers as well as banks, is to promote the safety and soundness of regulated firms. In relation to insurers there is a further objective, relating to the protection of policyholders, which has no parallel in bank regulation. Safety and soundness and policyholder protection work most of the time in the same direction — but not all the time, and Court commissioned a study by the IEO to establish more clearly how the PRA interpreted and articulated this dual remit.

The IEO evaluated the PRA's approach to its statutory responsibilities and found that there was a range of understanding about the insurance objective among PRA supervisors. A central theme was the need for the PRA to do more to articulate and communicate its approach. The IEO was clear, however, that there was no evidence of PRA supervisors falling short, or stepping beyond, their policyholder protection duties. The question was rather one of consistency, of ensuring that supervisory practices were aligned with the preferred

1 www.bankofengland.co.uk/about/Documents/ieo/fmidresponse0217.pdf.

approach of the Prudential Regulation Committee, of allocating resource efficiently and of mitigating any risk of overreach, for instance the risk of supervisors being drawn into issues more appropriately addressed by the Financial Conduct Authority (FCA).

The PRA has agreed to set out and agree with the PRC a clear interpretation of the insurance objective by the end of 2017, which would then be communicated externally and embedded in supervisory practice internally. The PRA will agree with the PRC by the end of 2017 the appropriate levels of protection between different types of policyholders, the extent to which supervision should take the compensation scheme into account, the approach to firm categorisation and the co-ordination arrangement with the FCA.

For both studies, Court will be following up progress on implementing the IEO proposals for change.

The IEO has also facilitated a series of teach-ins for Court Non-executive Directors, on subjects ranging from the new polymer £5 note, to innovative financial technology ('FinTech') and the Bank's progress on diversity and inclusion. And it has supported Court in following up progress on recommendations made in previous reports — specifically, on forecasting performance and the PRA's approach to its secondary competition objective.

For 2017/18, Court has commissioned two further studies, into the Bank's framework for bank resolution and the provision of liquidity to the banking system through the Sterling Monetary Framework.

Investigations

Throughout the year the Court has been kept informed of the progress of the Serious Fraud Office (SFO) investigation of the issues referred to it by the Bank in 2014, concerning the conduct of certain liquidity auctions during the 2007–08 financial crisis. In June 2017, the SFO closed its investigations and concluded that there was 'no evidence of criminality'.

Codes of Conduct

During the year the Court approved new conflict of interest codes for the Monetary Policy Committee, the Financial Policy Committee and the Prudential Regulation Committee. Separately, the Bank has for many years had policies for requiring staff to report personal relationships within and outside the Bank, financial transactions and gifts and entertainment received; these and other policies were brought together in 2015 under the general title 'Our Code': the Code applies to all members of staff, contractors, Governors and members of policy committees.

The Bank rightly takes seriously any failure to comply with Our Code and the underlying policies. Following Charlotte Hogg's resignation in March, Court appointed a Committee of Non-Executives chaired by Mr Fried to review and evaluate the Bank's approach to identifying and managing potential conflicts of interest and the supporting governance arrangements. The Director of the IEO is leading the support for the Review with advice and assistance, as appropriate, from the Bank's Internal Auditor.

Specifically, the Review is examining:

i. the policies and processes for identifying and managing conflicts of interest at the Bank, including the lessons arising from Ms Hogg's case;
ii. what the Bank should do to ensure full and timely compliance with those policies, especially among senior members of the Bank; and
iii. the supporting governance arrangements, including the extent to which the changes to reporting lines and internal structures announced by the Bank on 14 March 2017 are adequate.[1]

1 On 14 March 2017, the Bank announced the following measures to 'safeguard more effectively the governance of its Code of Conduct, compliance and disciplinary processes':

- Senior Management Responsibility for Bank-wide risk management moved to the Deputy Governor for Prudential Regulation in his capacity as Chair of the Executive Risk Committee and reporting to Court's Audit and Risk Committee (ARCo) on risk matters.
- A dual reporting line for the Head of Compliance to the General Counsel and to the Chair of ARCo.
- Senior Management Responsibility for the Code of Conduct moved to the General Counsel reporting to the Chair of ARCo in this regard.

Herbert Smith has been appointed by the NEDs to advise on the Review, and the National Audit Office has been commissioned to author a self-contained piece of work outlining the features of relevant best practice in the UK public sector.

The findings and recommendations of the Review will be made public in due course.

The National Audit Office

The NAO's engagement with the Bank increased in 2016 with the passage of amendments to the Bank of England Act. As well as auditing the functions of the Bank that are indemnified by the Treasury — mainly at present the Asset Purchase Facility — the NAO may conduct examinations into the economy, efficiency and effectiveness with which the Bank has used its resources in discharging its functions. As required by the legislation the NAO consulted the Court about the content of the first such study, which concerns the planning and outcomes of the Bank's 2014–17 One Bank Strategic Plan. Court welcomed the proposed study and has monitored its progress closely. It is hoped that the conclusions will help in implementing the new Vision 2020 Strategic Plan, which is focused on how we communicate and how we work (pages 30–31).

Members of Court attendance for Annual Report 2016–17

Attendance	Court (7)	Oversight (2)	Audit & Risk (6)	RemCo (4)	NomCo (2)
Mr Habgood	7	2	6	4	2
Mr Fried	7	2	6	–	2
Mr Frost	7	2	6	4	–
Mr Prentis	6 of 7	2	–	3 of 4	–
Baroness Harding	7	2	–	4	–
Mr Robert	6 of 7	2	6	–	–
Ms Thompson	6 of 7	2	6	–	2
Mr Carney	7	–	–	–	–
Mr Bailey	2 of 2	–	2 of 2	–	–
Sir Jon Cunliffe	7	–	–	–	–
Mr Broadbent	7	–	–	–	–
Ms Shafik	7	–	5 of 6	–	–
Mr Woods	5 of 5	–	3 of 4	–	–

Report of the Audit and Risk Committee

Introduction

This report provides an overview of the work of the Audit and Risk Committee (ARCo) and how it has discharged its duties over the year. The body of the report is split into two sections — '*audit*' and '*risk*' — reflecting the components of the Committee's remit.

Meetings and attendance

The Court of Directors monitors the integrity of the Bank's financial statements and its risks and controls mainly through ARCo. The Committee's remit is set out in 'Matters Reserved to Court'.[1]

ARCo comprises four Non-executive Directors of Court, with wide and recent experience of company board practice and risk control. The Chair of ARCo is appointed by Court.

ARCo met six times during the year. The Chair of Court, the Deputy Governor and Chief Executive Officer for the PRA, the Deputy Governor for Markets and Banking, the Chief Operating Officer, the Finance Director, the Executive Directors for Markets and for Banking, Payments and Financial Resilience, the Head of Internal Audit, the Head of Risk, and a Non-executive Director of the PRA attend ARCo meetings by invitation. The Bank's external auditors and the National Audit Office (NAO) which audited the PRA until its de-subsidiarisation on 1 March 2017 and audits the Bank of England Asset Purchase Facility Fund Limited (BEAPFF) from 1 March 2017, attend the audit part of ARCo meetings.

In addition to its scheduled meetings, Committee members meet separately and privately from time to time. Committee members also hold separate, private meetings with the Governor, the Deputy Governors, the Chief Operating Officer, the internal and external auditors, and the Heads of Risk and Compliance so that they can have an open discussion without the Bank Executives present.

The Chair of ARCo regularly meets the Chief Operating Officer, the Finance Director, the Heads of Risk and Internal Audit as well as with other Bank Executives outside the formal ARCo meetings.

The Chair of ARCo is chairing the Non-executive Directors' of Court's internal review of the Bank's approach to managing conflicts of interest.

Section 1 — audit-related items

Integrity of financial reporting

In terms of discharging its responsibilities in relation to monitoring the integrity of the Bank's Annual Financial Report, ARCo:

- Reviewed the accounting policies and practices adopted in the preparation of the Bank's annual financial statements.
- Reviewed the annual financial statements for the Bank and PRA before their submission to Court at its May 2017 meeting, including the adequacy of the disclosures made. Supporting these, ARCo considered Executive Management's Annual Risk Control attestations prior to submission of the results to Court.
- Reviewed and approved the Bank's proposed Letter of Representation to the auditors before final approval by and signature on behalf of Court.
- Reviewed reports from the Finance Director, including regular accounting updates, an update on the financial accounting considerations relating to the transfer of the PRA's functions, and assets and liabilities to the Bank on 1 March 2017, and an annual update on taxation.

1 See page 9.

External auditors

In relation to the external auditors, ARCo:

- Monitored the arrangements set up in relation to the NAO under the 2016 Bank of England and Financial Services Act, and considered the Letter of Understanding between the Bank and the NAO relating to the NAO's audit functions.

- Considered the NAO's memorandum of understanding regarding its approach to Value for Money (VFM) work, and discussed with the NAO the scope of its first VFM exercise covering the Bank's One Bank Strategic Plan.

- Received and discussed regular updates from KPMG, the Bank's external auditors, and from the NAO, the PRA's external auditors (until 1 March 2017) and the external auditors of the Bank of England's Asset Purchase Facility Fund Limited (BEAPFF) from 1 March 2017. These included the nature and scope of the external audit plans for the Bank, PRA and BEAPFF and a review of the findings of the audits.

- Reviewed the external auditors' Management Letters for the Bank and the PRA.

- Assessed the extent to which non-audit services were provided by KPMG to the Bank and the associated fees.

Internal Audit

The Internal Audit Department evaluates the design and effectiveness of the governance, internal controls and risk management processes that exist across the Bank to help Court and Executive Management protect the assets and reputation of the Bank. The Head of Internal Audit reports to the Chair of ARCo and has direct access to the Audit and Risk Committee and Executive Management.

In relation to Internal Audit, the Committee:

- Considered and approved the remit, Charter, resources and budget for the Internal Audit function and confirmed that it was satisfied that the Internal Audit function had appropriate resources.

- Reviewed and approved the Internal Audit plan and monitored its execution.

- Considered major findings arising from Internal Audit's work, and reviewed and monitored management's responsiveness to Internal Audit's recommendations and the progress made in implementing agreed actions.

Section 2 — risk-related items

Risk and control processes

ARCo is responsible for reviewing and reporting on the effectiveness of the Bank's risk management framework, risk management policies and systems of internal control. It reviews regular reports on the Bank's risk profile, and evaluates the actions being taken by management to bring these risks within tolerance. As part of these responsibilities, the Committee:

- Reviewed the revised Quarterly Risk Reports from the Bank-wide Risk Division and Financial Risk and Resilience Division covering the main strategic, operational and financial risks to the Bank (including the PRA), including a forward-looking consideration of risks. During 2016/17 the Committee discussed risks including those relating to the outcome of the EU referendum. ARCo also considered the actions being taken by management to bring risks within tolerance.

- Received and considered regular reports from the Executive Director of Markets and from the Executive Director, Banking, Payments and Financial Resilience on developments relating to the Bank's balance sheet, including reviews of the balance sheet remit and collateral management, and sought assurance that the financial risks to the Bank's balance sheet were being managed effectively.

- Received and discussed regular 'deep dive' individual Directorate Risk Drilldown Reports, including reports from the PRA Directorates, and provided feedback to the Directors.

- Received and discussed regular updates and reports from the Bank's Chief Operating Officer summarising major operational issues and control-related and risk issues including those relating to strategic and other key Bank initiatives. Areas of focus in 2016/17 included: actions taken forward to deliver Central Services' priorities for 2017 in relation to its functions to protect, strengthen and enable the Bank.

As part of its oversight of the effectiveness of the Bank's systems of internal control, the Committee:

- Received updates on improvements made to the management of the Bank's project portfolio, and regular reports on the management of current significant projects and related controls. In 2016/17 these included Structural Reform and the Information Security programme.

- Received regular updates from the Executive Director for Technology and from the Head of Information Security on initiatives and projects relating to information technology and data architecture, cyber risk and systems resilience and security.

- Assessed reports from the internal and external auditors to ensure that necessary standards of risk management were being applied and that appropriate action was being taken in relation to significant incidents.

- Reviewed and approved the new Compliance Division's Charter, and considered its annual strategy and plan and its report on the annual staff attestation against the Bank's Code of Conduct.

- Reviewed annual reports on controls in place against business practice risk, including Notes Division's report on the counterfeit threat to the Bank's issue of banknotes; a report on the Bank's insurance arrangements; a report on business continuity; a report on Freedom of Information requests received by the Bank; a Health and Safety annual update; a report on the Bank's adherence to the Senior Managers Regime; a report on the Bank's framework for managing the risk from money laundering; and a report on cyber threat assessment.

- The Committee reviewed the Bank's arrangements for detecting and deterring fraud and considered the annual report on the Bank's arrangements for its employees to raise concerns in confidence about possible fraud, malpractice or misconduct ('Speaking Up') from the Bank Secretary.

Audit and Risk Committee Terms of Reference

The Committee reviewed its Terms of Reference which had been revised to incorporate changes arising from the 2016 Bank of England and Financial Services Act and to make them consistent with the new NAO relationships and the intention to have separate audit and risk elements within a single ARCo.

Audit and Risk Committee effectiveness

The effectiveness of the Audit and Risk Committee was reviewed as part of the 2016/17 evaluation of Court and its sub-committees.

Other responsibilities

The Committee reviewed a summary of the annual expenses of the members of Court.

Audit and Risk Committee: regular attendees 2016–17[1]

ARCo members	ARCo meetings (6)
Bradley Fried (Chair)	6
Tim Frost	6
Don Robert	6
Dorothy Thompson	6
Anthony Habgood[2]	6
Executive	
Minouche Shafik	3 of 4
Sam Woods	5 of 6
Charlotte Hogg	5 of 5
Andrew Hauser	6
Rommel Pereira	5 of 5
Joanna Place	1 of 1
Chris Salmon	6
Internal Auditor	
Stephen Brown	6
External Auditor (KPMG)[3]	
Michelle Hinchliffe (KPMG)	6
Satish Iyer (KPMG)	6
NAO	
Nick Bateson	6
Alex Clark	3 of 6
Peter Gray	1 of 1
Mark Yallop (PRA)	6

1 Covering ARCo meetings held on 4 July 2016, 6 October 2016, 30 November 2016, 23 January 2017, 27 March 2017 and 15 May 2017.

2 Anthony Habgood is not a member of the Committee but attends the meetings by invitation.

3 KPMG and NAO attend the Audit part of the meeting and to present their reports.

Statement of the responsibilities of the Court of Directors in relation to the financial statements

The Court of Directors is responsible for ensuring that the financial statements of the Banking Department are properly prepared on the basis set out therein, as at 28 February 2017 and for the year to that date.

The statements of account of the Issue Department are prepared in accordance with provisions agreed between the Bank and HM Treasury to implement the requirements of the Currency and Bank Notes Acts 1928 and 1954, the National Loans Act 1968 and the Currency Act 1983. The Court of Directors is responsible for ensuring that the statements of account are prepared in accordance with these requirements as at 28 February 2017 and for the year to that date.

The Court of Directors is responsible for ensuring proper accounting records are kept, which disclose at any time the financial position of the Bank and enable Court to ensure that the financial statements comply with the requirements set out in note 2 of the Accounts. The Court of Directors is also responsible for safeguarding the assets of the Bank and its subsidiaries, and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The Court of Directors confirms that suitable accounting policies, consistently applied and supported by reasonable and prudent judgement and estimates, have been used in the preparation of the financial statements of the Banking Department. The accounting framework adopted is set out on pages 87 to 96.

The Directors who held office at the date of approval of this *Annual Report* confirm that, so far as they are aware, there is no relevant audit information of which the Bank's auditors are unaware; and each Director has taken all steps that they ought to have taken as a Director to make themselves aware of any relevant information and to establish that the Bank's auditors are aware of that information.

The Directors are responsible for the maintenance and integrity of the corporate and financial information included on the Bank's website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Report of the Independent Auditor

Independent Auditor's Report to the Governor and Company of the Bank of England and its Shareholder

We have audited the financial statements of the Banking Department ('financial statements') for the year ended 28 February 2017, set out on pages 82 to 135, and the statements of account of the Issue Department ('statements of account') for the year ended 28 February 2017, set out on pages 136 to 140. The financial reporting framework that has been applied in their preparation is applicable law and the accounting policies set out therein.

This report is made solely to the Governor and Company of the Bank of England and its Shareholder in accordance with Section 7 of the Bank of England Act 1998. Our audit work has been undertaken so that we might state to the Governor and Company of the Bank of England and its Shareholder those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Governor and Company of the Bank of England and its Shareholder for our audit work, for this report or for the opinions we have formed.

Respective responsibilities of Members of Court and auditor

As explained more fully in the Statement of the Responsibilities of the Court of Directors set out on page 79, the Members of Court are responsible for the preparation of the financial statements and statements of account in accordance with applicable law and the bases of preparation set out in note 1 on page 87 and note 2 on pages 87 to 95 respectively.

Our responsibility is to audit, and express an opinion on, the financial statements and statements of account in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practice's Board's Ethical Standards for Auditors.

Scope of the audit of the financial statements and statements of account

An audit involves obtaining evidence about the amounts and disclosures in the financial statements and statements of account sufficient to give reasonable assurance that the financial statements and statements of account are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Bank's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Members of Court; and the overall presentation of the financial statements and statements of account. In addition, we read all the financial and non-financial information in the *Annual Report* to identify material inconsistencies with the audited financial statements and statements of account and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

Opinion on financial statements and statements of account

In our opinion:

- the financial statements of the Banking Department on pages 82 to 135 for the year ended 28 February 2017 have been properly prepared, in all material respects, in accordance with the bases of preparation set out in note 2 on pages 87 to 95.

- the statements of account of the Issue Department on pages 136 to 140 for the year ended 28 February 2017 have been properly prepared, in all material respects, in accordance with the bases of preparation set out in note 1 on page 138.

Opinion on other matter as prescribed by the terms of our engagement letter

In our opinion the information given in the Remuneration report, the Financial Review, the Risk Management and Business Practices, and the Report of Oversight Functions for the financial year for which the financial statements and statements of account are prepared is consistent with the financial statements and statements of account.

Michelle Hinchliffe
for and on behalf of KPMG LLP,
Statutory Auditor

Chartered Accountants
15 Canada Square
Canary Wharf
London E14 5GL

26 June 2017

Banking Department statement of income
for the year to 28 February 2017

	Note	2017 £m	2016 £m
Net interest income		15	15
Fee income	4	169	182
Other income from financial instruments	4	210	214
Management fees	4	214	191
Other income	4	26	24
Net operating income		**634**	**626**
Staff costs	4	(357)	(354)
Infrastructure costs	4	(84)	(84)
Administration and general costs	4	(122)	(111)
Less: Costs recharged to the PRA		151	156
Operating expenses		**(412)**	**(393)**
Profit before tax		**222**	**233**
Taxation	7	(20)	(24)
Profit after tax		**202**	**209**

The notes on pages 87 to 135 are an integral part of these financial statements.

The income statement has been represented to show gross costs incurred by the Bank less costs recharged to the PRA.

Banking Department statement of comprehensive income
for the year to 28 February 2017

	2017 £m	2016 £m
Profit for the year attributable to shareholder	**202**	**209**
Other comprehensive income/(loss) that may be recycled to profit or loss:		
Available for sale reserve		
Net gains from changes in fair value	154	920
Current and Deferred tax	(9)	(162)
Property revaluation reserve		
Net (losses)/gains from changes in fair value	(9)	34
Deferred tax	3	(5)
Total other comprehensive income that may be recycled to profit or loss	**139**	**787**
Other comprehensive income/(loss) not recycled to profit or loss:		
Retirement benefit remeasurements	(100)	358
Deferred tax	24	(58)
Total other comprehensive income/(loss) not recycled to profit or loss	**(76)**	**300**
Total comprehensive income for the year	**265**	**1,296**

The notes on pages 87 to 135 are an integral part of these financial statements.

Banking Department statement of financial position
as at 28 February 2017

	Note	2017 £m	2016 £m
Assets			
Cash and balances with other central banks	9	1,641	637
Loans and advances to banks and other financial institutions	10	9,843	12,706
Other loans and advances	11	485,154	375,198
Securities held at fair value through profit or loss	12	9,157	7,190
Derivative financial instruments	13	308	488
Available for sale securities	14	8,402	7,944
Investments in subsidiaries	15	–	–
Inventories	16	4	2
Property, plant and equipment	17	400	392
Intangible assets	18	21	18
Current tax assets		34	–
Retirement benefit assets	19	917	932
Other assets	20	1,798	251
Total assets		**517,679**	**405,758**
Liabilities			
Deposits from central banks	21	15,094	15,355
Deposits from banks and other financial institutions	22	415,488	324,546
Other deposits	23	73,313	55,583
Foreign currency bonds in issue	24	6,450	4,333
Derivative financial instruments	13	108	476
Current tax liabilities		–	34
Deferred tax liabilities	25	377	341
Retirement benefit liabilities	19	229	194
Other liabilities	26	1,866	306
Total liabilities		**512,925**	**401,168**
Equity			
Capital	27	15	15
Retained earnings		3,036	3,011
Other reserves		1,703	1,564
Total equity attributable to shareholder		**4,754**	**4,590**
Total liabilities and equity attributable to shareholder		**517,679**	**405,758**

On behalf of the Governor and Company of the Bank of England:
Mr M Carney Governor
Mr B Broadbent Deputy Governor
Mr A Habgood Chair of Court
Mr R Pereira Finance Director

Banking Department statement of changes in equity
for the year to 28 February 2017

		Attributable to equity shareholder				
	Note	Share capital £m	Available for sale reserve £m	Property revaluation reserve £m	Retained earnings £m	Total £m
Balance at 28 February 2015		**15**	**577**	**200**	**2,607**	**3,399**
Post-tax comprehensive income/(loss) for the period		–	758	29	209	996
Retirement benefits remeasurements		–	–	–	300	300
Payable to HM Treasury in lieu of dividend	8	–	–	–	(105)	(105)
Balance at 29 February 2016		**15**	**1,335**	**229**	**3,011**	**4,590**
Post-tax comprehensive income/(loss) for the period		–	145	(6)	202	341
Retirement benefits remeasurements		–	–	–	(76)	(76)
Payable to HM Treasury in lieu of dividend	8	–	–	–	(101)	(101)
Balance at 28 February 2017		**15**	**1,480**	**223**	**3,036**	**4,754**

The notes on pages 87 to 135 are an integral part of these financial statements.

Banking Department statement of cash flows
for the year to 28 February 2017

	Note	2017 £m	2016 £m
Cash flows from operating activities			
Profit before taxation		**222**	**233**
Adjustments for:			
Amortisation of intangibles	18	5	3
Depreciation of property, plant and equipment	17	22	19
Dividends received	4	(11)	(10)
Net movement in accrued interest and provisions, including pensions		100	182
Changes in operating assets and liabilities:			
Increase in loan advanced to the Bank of England Asset Purchase Facility Fund Ltd	11	(109,956)	–
Net (increase)/decrease in other advances		3,662	556
Net increase/(decrease) in securities held at fair value through profit and loss		228	(2,046)
Net increase in deposits		108,123	836
Net increase/(decrease) in foreign currency bonds in issue		518	465
Net (increase)/decrease in financial derivatives	13	(188)	1,193
Net decrease in other accounts		23	14
Net increase in inventories		(2)	(2)
Corporation tax (paid)/received		(34)	(11)
Net cash inflow from operating activities		**2,712**	**1,432**
Cash flows from investing activities			
Purchase of available for sale securities	14	(870)	(532)
Proceeds from redemption of available for sale securities	14	483	427
Dividends received	4	11	10
Purchase of intangible assets	18	(11)	(6)
Purchase of property, plant and equipment	17	(46)	(30)
Net cash outflow from investing activities		**(433)**	**(131)**
Cash flows from financing activities			
Net increase/(decrease) in Cash Ratio Deposits		288	38
Payment to HM Treasury under Section 1 (4) of the Bank of England Act 1946		(105)	(93)
Net cash outflow from financing activities		**183**	**(55)**
Net increase in cash and cash equivalents		**2,462**	**1,246**
Cash and cash equivalents at 1 March	28	6,674	5,428
Cash and cash equivalents at 28 February	**28**	**9,136**	**6,674**

Notes to the Banking Department financial statements

1 General information

The Bank of England is the central bank of the United Kingdom and is incorporated under a Royal Charter of 1694 and is located at Threadneedle Street, London, EC2R 8AH. Legislation covering its operations includes the Bank Charter Acts of 1694 and 1844, the Bank of England Acts 1946 and 1998, the Banking Act 2009 and the Financial Services Act 2012.

The Bank Charter Act 1844 requires that the Bank's note issue function be separated from its other activities. Accordingly, for accounting purposes, the Bank is divided into Issue Department and Banking Department, which are accounting designations and reporting entities. Neither is an organisational unit of the Bank. The Issue Department is solely concerned with the note issue and the assets backing the issue. The statements of account of the Issue Department are given on pages 136 to 140, and show the note issue, the assets backing the issue, the income generated by those assets and the costs incurred in the production, issue, custody and payment of notes. The net income of the Issue Department is paid over to the National Loans Fund. Securities held by the Issue Department are revalued quarterly at their clean market price. If a revaluation of securities shows a net gain this is included in income. A deficit is not taken against income but is settled by a transfer from the National Loans Fund. The Banking Department comprises all other activities of the Bank. The post-tax profits of the Banking Department are effectively shared equally with HM Treasury unless the Bank and HM Treasury agree otherwise (see note 8).

2 Bases of preparation

The principal accounting policies applied in the preparation of the financial statements of the Banking Department are set out below. These policies have been applied consistently to all of the years presented, unless otherwise stated.

a Form of presentation of the financial statements

The financial statements of the Banking Department comprise the statement of income, the statement of comprehensive income, the statement of financial position, the statement of changes in equity, the statement of cash flows and related notes.

Under the Bank of England Act 1998, the Bank, in preparing the financial statements of the Banking Department, is subject to requirements corresponding to the Companies Act requirements relating to a banking company. The Bank may, however, disregard a requirement to the extent that it considers it appropriate to do so having regard to its financial stability objective.

The financial statements of the Banking Department have been prepared in accordance with the measurement and recognition requirements of the International Financial Reporting Standards (IFRS) and International Financial Reporting Interpretations Committee (IFRICs) as adopted by the EU (together, 'adopted IFRS').

The financial statements have been prepared on the historical cost basis of accounting, modified to include the revaluation of land and buildings, financial assets that are available for sale and all financial assets, financial liabilities (including derivatives) that are held at fair value through profit or loss and retirement benefit assets and liabilities.

Adopted IFRS and the Companies Act have been used as a model for the presentation and disclosure framework to provide additional information and analysis of key items in the financial statements except insofar as the Bank considers disclosures inappropriate to its financial stability objective.

In exceptional circumstances, as part of its central banking functions, the Bank may act as 'lender of last resort' to financial institutions in difficulty in order to prevent a loss of confidence spreading through the financial system as a whole. In some cases, confidence can best be sustained if the Bank's support is disclosed only when conditions giving rise to potentially systemic disturbance have improved. Accordingly, although the financial effects of such operations will be included in the Banking Department's financial statements in the year in which they occur, these financial statements may not explicitly identify the existence of such support. However, the existence of such support will be reported in the *Annual Report* when the need for secrecy or confidentiality has ceased.

Notes to the Banking Department financial statements continued

2 Bases of preparation continued

As a result, the financial statements of the Banking Department disclose less detail of certain elements than would be required under either adopted IFRS or the Companies Act. Disclosure limitations include:

- Presentation of the Statement of Income disclosures.
- Operating segments.
- Contingent liabilities and guarantees.
- Information on credit and liquidity risk.
- Fair value of collateral pledged and held.
- Related party disclosure.
- Off balance sheet arrangements.

b New and amended accounting standards

i Future accounting developments

The IASB has published IFRS 9 'Financial Instruments', IFRS 15 'Revenue from Contracts with Customers' and IFRS 16 'Leases'. IFRS 9 and IFRS 15 have been endorsed for use in the EU and IFRS 16 has not yet been endorsed.

ii IFRS 9 'Financial Instruments'

In July 2014, the IASB issued IFRS 9 'Financial Instruments', which is the comprehensive standard to replace IAS 39 'Financial Instruments: Recognition and Measurement', and includes requirements for classification and measurement of financial assets and liabilities, impairment of financial assets and hedge accounting.

Classification and measurement

The classification and measurement of financial assets will depend on how these are managed (the entity's business model) and their contractual cash-flow characteristics. These factors determine whether the financial assets are measured at amortised cost, fair value through other comprehensive income ('FVOCI') or fair value through profit or loss ('FVPL'). The combined effect of the application of the business model and the contractual cash-flow characteristics tests may result in some differences in the population of financial assets measured at amortised cost or fair value compared with IAS 39. Based on an assessment of financial assets performed to date the Bank expects to reclassify the debt securities held as available for sale to amortised cost, with a corresponding reduction to the available for sale reserve.

For financial liabilities designated to be measured at fair value, gains or losses relating to changes in the entity's own credit risk are to be included in other comprehensive income.

Impairment

The impairment requirements apply to financial assets measured at amortised cost and FVOCI, and lease receivables and certain loan commitments and financial guarantee contracts. At initial recognition, an impairment allowance (or provision in the case of commitments and guarantees) is required for expected credit losses ('ECL') resulting from default events that are possible within the next twelve months ('twelve-month ECL'). In the event of a significant increase in credit risk, an allowance (or provision) is required for ECL resulting from all possible default events over the expected life of the financial instrument ('lifetime ECL'). Financial assets where ECL is recognised are in 'stage 1'; financial assets that are considered to have experienced a significant increase in credit risk are in 'stage 2'; and financial assets for which there is objective evidence of impairment, so are considered to be in default or otherwise credit impaired, are in 'stage 3'.

The assessment of credit risk and the estimation of ECL are required to be unbiased and probability-weighted, and should incorporate all available information relevant to the assessment, including information about past events, current conditions and reasonable and supportable forecasts of economic conditions at the reporting date. In addition, the estimation of ECL should take into account the time value of money. As a result, the recognition and measurement of impairment is intended to be more forward looking than under IAS 39, and the resulting impairment charge will tend to be more volatile. IFRS 9 will also tend to result in an increase in the total level of impairment allowances, since all financial assets will be assessed for at least twelve-month ECL and the population of financial assets to which lifetime ECL applies is likely to be larger than the population for which there is objective evidence of impairment in accordance with IAS 39.

The Bank manages credit exposures by taking collateral on lending positions and applying haircuts based on prevailing economic and counterparty specific conditions. The current assessment is that the ECL allowance is expected to be minimal however the Bank will perform regular assessments to confirm this remains the case.

Hedge accounting

The general hedge accounting requirements aim to simplify hedge accounting, creating a stronger link with risk management strategy and permitting hedge accounting to be applied to a greater variety of hedging instruments and risks. However they do not explicitly address macro hedge accounting strategies, which are particularly important for banks. As a result, IFRS 9 includes an accounting policy choice to remain with IAS 39 hedge accounting.

The Bank does not apply hedge accounting, as such there is no anticipated impact from these amendments.

Transition

The classification and measurement and impairment requirements are applied retrospectively by adjusting the opening balance sheet at the date of initial application, with no requirement to restate comparative periods. The Bank does not intend to restate comparatives.

The mandatory application for the standard as a whole will be first applicable for the Bank in the financial year ending 28 February 2019, the Bank does not anticipate early adoption of any of the standard.

The Bank's IFRS 9 implementation plan continues to progress with system developments, accounting policy documentation and development of an updated impairment assessment methodology expected to be completed in 2017.

The Bank expects to commence parallel running of internal reporting by late 2017 to inform those charged with governance of the likely impact of the switch to IFRS 9, and provide reliable estimates of those. Until reliable estimates of the impact are available further information on the expected impact on the financial position cannot be provided.

iii IFRS 15 'Revenue from Contracts with Customers'

In May 2014, the IASB issued IFRS 15 'Revenue from Contracts with Customers'. The original effective date of IFRS 15 has been delayed by one year and the standard is now effective for annual periods beginning on or after 1 January 2018 with early application permitted. IFRS 15 provides a principles-based approach for revenue recognition, and introduces the concept of recognising revenue for performance obligations as they are satisfied. The standard should be applied retrospectively, with certain practical expedients available. The Bank has assessed the impact of IFRS 15 and expects that the standard will have no significant effect, when applied, on the financial statements.

iv IFRS 16 'Leases'

In January 2016, the IASB issued IFRS 16 'Leases' with an effective date for annual periods beginning on or after 1 January 2019. IFRS 16 results in lessees accounting for most leases within the scope of the standard in a manner similar to the way in which finance leases are currently accounted for under IAS 17 'Leases'. Lessees will recognise a 'right of use' asset and a corresponding financial liability on the balance sheet. The asset will be amortised over the length of the lease and the financial liability measured at amortised cost. Lessor accounting remains substantially the same as under IAS 17. The Bank is currently assessing the impact of IFRS 16, and it is not practicable to quantify the effect at the date of the publication of these financial statements. Existing operating lease commitments are set out in note 31.

c Consolidation

The financial statements of the Bank's subsidiaries, including the Bank of England Asset Purchase Facility Fund Ltd and the Prudential Regulation Authority, have not been consolidated. Under the Bank of England Act 1998 the financial statements are prepared on a non-consolidated basis. Investments in subsidiaries are stated in the balance sheet at cost, less any provision for impairment in value. Dividends from subsidiaries are recognised in the income statement when declared.

d Foreign currency translation

i Functional and presentation currency

The financial statements of the Banking Department are presented in sterling, which is also the Bank's functional currency.

Notes to the Banking Department financial statements continued

2 Bases of preparation continued

ii Transactions and balances

Foreign currency transactions are translated into sterling using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the income statement. Where a gain or loss on a non-monetary item is recognised directly in other comprehensive income, such as equity investments classified as financial assets that are available for sale, the related exchange gain or loss is also recognised in other comprehensive income.

e Financial instruments: assets

i Classification of financial assets

The Bank classifies its financial assets in the following categories: loans and advances; financial assets at fair value through profit or loss; and financial assets that are available for sale. The Bank determines the classification at initial recognition.

Loans and advances measured at amortised cost

Loans and advances are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They arise when the Bank provides money or services directly to a counterparty with no intention of trading the receivable. Assets in this category exclude those reverse repurchase agreements which are designated at fair value through profit or loss.

Financial assets at fair value through profit or loss

A financial asset is classified in this category if it is acquired principally for the purpose of selling in the short term or if so designated by management.

Derivatives must be held at fair value through profit or loss. The Bank does not currently hold any financial assets for trading but designates the following at fair value through profit or loss at inception:

- Securities and reverse repurchase agreements matching the Bank's issued foreign currency securities; and
- Securities and reverse repurchase agreements matching the fixed-term deposits placed at the Bank by other central banks.

This designation is to eliminate, or significantly reduce, inconsistencies that would otherwise arise from measuring assets and liabilities on different bases. The relevant assets and liabilities (including derivatives) are managed together and internal reporting is evaluated on a fair value basis.

The Bank defines fair value as the price, as at the measurement date, that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants.

Available for sale

Available for sale investments are those intended to be held for an indefinite period of time, which may be sold as part of the Bank's official operations or otherwise. They include sterling debt securities and unlisted equity investments.

ii Initial recognition of financial assets

Loans and advances and reverse repurchase agreements designated at fair value through profit or loss are recognised on a settlement date basis. Purchases of all other categories of financial assets are recognised on a trade date basis. All financial assets are initially recognised at fair value.

iii Subsequent valuation of financial assets

Gains and losses arising from changes in the fair value of assets classified as fair value through profit or loss are included in the income statement in the period in which they arise.

Gains and losses arising from changes in the fair value of financial assets that are available for sale are recognised as other comprehensive income until the financial asset is derecognised or impaired (see (iv) below), at which time the cumulative gain or loss previously recognised as other comprehensive income is recognised in the income statement. Any premium or discount paid on the purchase of available for sale debt instruments is amortised through the income statement using the effective interest rate method.

The fair values of quoted investments in active markets are based on current bid prices. In other cases, the Bank establishes fair value by using appropriate valuation techniques. The policy for establishing fair values of securities in non-active markets is described in note 3 'Significant accounting estimates and judgements in applying accounting policies' on page 96.

Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or where the Bank has either transferred substantially all of the risks and rewards of ownership or the Bank deems that it no longer retains control of the risks and rewards of ownership.

iv Impairment of financial assets

Loans and advances

At each balance sheet date the Bank assesses whether there is objective evidence that a financial asset or group of assets is impaired. If there is objective evidence that an impairment loss on loans and advances has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of the estimated future cash flows relating to that loan discounted at the asset's original effective interest rate. The carrying amount of the asset is reduced and the amount of the loss is recognised in the income statement. A loan is normally written off, either partially or in full, when there is no realistic prospect of recovery of the principal amount and, for a collateralised loan, after taking into account any value of the security which has been realised.

Available for sale financial assets

At each balance sheet date the Bank assesses whether there is objective evidence that a financial asset or group of assets is impaired. If such evidence exists for financial assets that are available for sale, the cumulative loss measured as the difference between acquisition cost and the current fair value, less any impairment loss previously recognised, is removed from equity and recognised in the income statement.

If, in a subsequent period, the fair value of a debt instrument designated as available for sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognised, the impairment loss is reversed through the income statement.

If, in a subsequent period, the fair value of an equity investment designated as available for sale increases the impairment loss is not reversed through the income statement except on realisation.

No impairments to financial assets have been recognised in the year.

v Interest income

Interest income is recognised in the income statement using the effective interest method for all interest-bearing financial instruments except for assets measured at fair value through profit and loss.

The effective interest method is a method of calculating the amortised cost of a financial asset or liability and of allocating the interest income or interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument to the net carrying amount of the financial asset or liability on initial recognition. When calculating the effective interest rate, the Bank estimates cash flows considering all contractual terms of the financial instrument, and any revisions to these estimates are recognised in the income statement. The calculation includes amounts paid or received that are an integral part of the effective interest rate of a financial instrument, including transaction costs and all other premiums or discounts.

vi Dividends

Dividends on equity investments that are available for sale are recognised in the income statement when declared.

f Derivative financial instruments

Derivatives are initially recognised at fair value on the date on which a derivative contract is entered into and are subsequently remeasured at their fair value. Fair values are obtained from quoted market prices in active markets, including recent market transactions, or valuation techniques such as discounted cash-flow models. Generally the best evidence of the fair value of a derivative at initial recognition is the transaction price (ie the fair value of the consideration given or received). All derivatives are carried as assets when the fair value is positive and as liabilities when the fair value is negative.

Notes to the Banking Department financial statements continued

2 Bases of preparation continued

Derivatives are used for matching exposures on assets and liabilities, both individually and of portfolios. The Bank does not apply the hedge accounting rules of IAS 39.

g Offsetting financial instruments

Financial assets and liabilities are offset and the net amount reported in the balance sheet when there is a current and legally enforceable right to offset the amounts recognised and there is an intention to settle on a net basis, or to realise the asset and settle the liability simultaneously.

h Property, plant and equipment

i Initial recognition

Expenditure on property, plant and equipment is capitalised if the asset is expected to have a useful economic life of three years or more. The amount capitalised at initial recognition is the purchase price of the asset along with any further costs incurred in bringing the asset to its present condition and location.

ii Subsequent valuation

Subsequent costs are added to an asset's carrying amount or are recognised as a separate asset as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Bank and the cost of the item can be reliably measured. All other repairs and maintenance are charged to the income statement during the financial period in which they are incurred.

Professional valuations of the Bank's properties are carried out each year with subsequent additions included at cost, and provisions made for depreciation as explained below.

Any surplus arising on revaluation is recognised directly in a revaluation reserve within equity, except to the extent that the surplus reverses a previous revaluation deficit on the same asset recognised in the income statement, in which case the credit is to the income statement.

iii Depreciation

Land is not depreciated. Depreciation on other property, plant and equipment is charged on a straight-line basis:

Freehold buildings	over the estimated future lives which range from ten to seventy-five years
Leasehold improvements	over the estimated remaining life of the lease
Plant within buildings	over periods ranging from five to twenty years
IT equipment	over periods ranging from three to seven years
Other equipment	over periods ranging from three to twenty years

The depreciable amount of a revalued asset is based on its revalued amount less any residual value. The revaluation surplus is not transferred to retained earnings until the asset's ultimate disposal.

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date. Assets that are subject to depreciation are reviewed at each reporting date to assess whether there is any indication that an asset may be impaired. An asset's carrying amount is written down immediately to its recoverable amount if the carrying amount is greater than its estimated recoverable amount. The recoverable amount is the higher of the asset's fair value (less costs to sell) and value in use.

iv Gain or losses on the disposal of property, plant and equipment

Gains and losses on disposals are determined by comparing proceeds with carrying amount. These are included in the income statement.

i Leases

i As lessee

The leases entered into by the Bank are primarily operating leases. The total payments made under operating leases are charged to the income statement on a straight-line basis over the period of the lease. When an operating lease is terminated before the lease period has expired, any payment required to be made to the lessor by way of penalty is recognised as an expense in the period in which termination takes place.

Where property, plant and equipment have been financed by lease agreements under which substantially all the risks and rewards of ownership are transferred to the Bank, they are treated as if they have been purchased outright and classified as finance leases. Finance leases are capitalised at the commencement of the lease at the lower of the present value of the minimum lease payments or the fair value of the leased asset. Finance charges payable are recognised over the period of the lease based on the interest rate implicit in the lease to give a consistent periodic rate of return.

ii As lessor

Long leases granted on property owned by the Bank are treated as finance leases. Finance lease receivables are stated in the balance sheet at the amount of the net investment in the lease being the minimum lease payments and any unguaranteed residual value discounted at the interest rate implicit in the lease. Finance lease income is allocated across accounting periods giving a constant periodic rate of return before tax on the net investment. Unguaranteed residual values are subject to regular review to identify potential impairment. If there has been a reduction in the estimated unguaranteed residual value, the income allocation is revised and any reduction in respect of amounts accrued is recognised immediately.

j Intangible assets

Intangible assets primarily consist of computer software and the costs associated with the development of software for internal use. Costs associated with externally purchased software and costs directly associated with the internal production of unique and separately identifiable software products, which are controlled by the Bank and which will generate economic benefits exceeding those costs are recognised as intangible assets. These costs are amortised over the expected useful lives of the software, which range from three to five years. Costs associated with maintaining software programs are recognised as an expense when incurred. Intangible assets are tested for impairment annually. Intangible assets are also subject to an impairment review if there are events or changes in circumstances that indicate that the carrying amount may not be recoverable.

k Financial instruments: liabilities

i Classification of financial liabilities

The Bank classifies its financial liabilities in the following categories: liabilities measured at amortised cost and financial liabilities at fair value through profit and loss.

Liabilities measured at amortised cost

Short-term customer deposits held are carried at cost with interest expense accruing on an effective interest rate basis. Cash Ratio Deposits are taken to fund certain activities of the Bank in accordance with the Bank of England Act 1998. These deposits are held at cost and are interest free. Money market instruments are carried at cost and are issued at a discount which is amortised through the income statement on an effective interest rate basis.

Financial liabilities at fair value through profit or loss

The Bank designates the following financial liabilities at fair value through profit or loss:

- Four three-year bonds denominated in US dollars, which were issued as part of the Bank's annual medium-term issuance programme; and
- Fixed-term deposits placed by other central banks.

This designation is to eliminate, or significantly reduce, inconsistencies that would otherwise arise from measuring assets and liabilities on different bases. The relevant assets and liabilities (including derivatives) are managed together and internal reporting is evaluated on a fair value basis.

ii Initial recognition of financial liabilities

Fixed-term deposits taken from central banks are recognised on a settlement date basis. Money market instruments issued, short-term deposits and bonds issued by the Bank are recognised on a trade date basis.

iii Subsequent valuation of financial liabilities

Gains and losses arising from changes in the fair value of liabilities classified at fair value through profit or loss are included in the income statement in the period in which they arise.

Notes to the Banking Department financial statements continued

2 Bases of preparation continued

The fair values of these liabilities are based on current offer prices, as this is considered to be the price that would be paid to transfer a liability in an orderly transaction between market participants.

Financial liabilities are derecognised when the obligation to pay cash flows relating to the financial liabilities has expired. If the Bank buys any of its own securities as part of its operations, these are removed from the balance sheet.

l Current and deferred tax

Corporation tax payable on profits, based on the UK tax laws, is recognised as an expense in the period in which profits arise. The Bank is entitled to tax relief on the amount due to HM Treasury as a payment in lieu of a dividend in accordance with Section 1 (4) Bank of England Act 1946. Tax relief on amount due to HM Treasury is credited directly to the income statement in accordance with paragraph 52B of IAS 12.

Deferred tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. Deferred tax is determined using tax rates and laws that have been enacted or substantially enacted and which are expected to apply when the related deferred tax asset or liability is realised.

The principal temporary differences arise from depreciation of property, plant and equipment, revaluation of certain financial assets, property revaluations, and provisions for pensions and other post-retirement benefits.

Deferred tax assets are recognised where it is probable that future taxable profit will be available against which the temporary differences and losses can be utilised.

Deferred tax related to fair value remeasurement of available for sale securities and actuarial gains and losses on retirement benefit obligations is credited or charged directly to other comprehensive income and is subsequently recognised in the income statement together with the current or deferred gain or loss if and when realised.

m Retirement benefits

The Bank operates a non-contributory defined-benefit pension scheme providing defined benefits based on career average pensionable pay. The final salary element of the scheme is closed to future accrual for service but a link to final salary remains for current active members. The assets of the scheme are held by the Bank in an independent trustee-administered fund. The asset recognised in the balance sheet in respect of the defined-benefit pension scheme is the fair value of the scheme's assets less the present value of the defined-benefit obligation at the balance sheet date. The defined-benefit obligation is calculated annually by an independent actuary using the projected unit method. The present value of the defined-benefit obligation is determined by discounting the estimated cash outflows using interest rates of high-quality sterling corporate bonds that have terms to maturity approximating to the terms of the related pension liability. Remeasurements on retirement benefits comprise experience adjustments (the effects of differences between the previous actuarial assumptions and what actually occurred), as well as the effects of changes in actuarial assumptions. Remeasurements on retirement benefits are recognised immediately in equity and reflected in other comprehensive income. Current and past service costs are recognised immediately in the income statement. Any net defined-benefit surplus is limited to the benefit that is available to the Bank.

The Bank also provides other post-retirement benefits, principally related to redundancy provisions and healthcare for certain pensioners, which are accounted for on a similar basis to the accounting for pension obligations.

n Equity capital

The entire equity capital comprising £14,553,000 of Bank Stock is held by the Treasury Solicitor on behalf of HM Treasury.

Under Section 1 (4) of the Bank of England Act 1946, as amended by the Bank of England Act 1998, subsequent to the end of each year HM Treasury receives payments of half the post-tax profits unless the Bank and HM Treasury agree otherwise. The payments are deductible for corporation tax and charged to equity in the year to which they relate on the basis agreed at the end of the relevant year.

o Cash and cash equivalents

For the purposes of the statement of cash flows, cash and cash equivalents comprise balances with less than three months' maturity from the date of acquisition, consisting of cash and balances with other central banks, loans and advances to banks and other financial institutions, amounts due from banks and short-term government securities.

p Fees and commission income

Fees and commissions are recognised as the service is provided. Where the level of fee is contingent on a particular outcome, the Bank only recognises the fee that is known to be recoverable.

q Provisions

Provisions are recognised in respect of restructuring, onerous leases and legal claims arising from past events, where a present legal or constructive obligation exists, where it is probable that an outflow of resources will be required to settle the obligation and the amount can be reliably estimated.

r Indemnified operations

The Bank may enter into arrangements where it is fully indemnified, without charge, from loss by HM Treasury. Surpluses from such indemnified operations, after the deduction of fees, operating costs and tax, are treated as a capital contribution and taken directly to equity as distributable reserves.

s Collateral pledged under sale and repurchase agreements

Securities sold subject to repurchase agreements are assets provided as collateral where the transferee has the right by contract or custom to sell the collateral. These securities remain on the balance sheet and the liability is included in deposits from banks and other financial institutions. Securities purchased under agreements to resell ('reverse repurchase agreements') are not recognised on the balance sheet; the asset is included in loans and advances to banks and other financial institutions. The difference between sale and repurchase price is treated as interest and accrued over the life of the agreements.

Securities loaned to counterparties also remain on the balance sheet. Securities borrowed are not recognised on the balance sheet, unless they are sold to third parties, in which case the obligation to return the securities is recorded at fair value as a liability.

The Bank may accept its own securities as collateral for reverse repurchase agreements. Such reverse repurchase transactions are treated as collateralised and are treated in the same way as other reverse repurchase transactions.

t Commitments on behalf of HM Treasury

Commitments on behalf of HM Treasury in foreign currencies and gold arising in the course of operating the Exchange Equalisation Account are not included in these financial statements as the Bank is concerned in such transactions only as agent.

u Inventories

Inventories comprise the raw materials utilised in the production of polymer banknotes.

Inventories are valued at the lower of cost and net realisable value.

Notes to the Banking Department financial statements continued

3 Significant accounting estimates and judgements in applying accounting policies

The Bank makes estimates and assumptions that affect the reported amounts of assets and liabilities. Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

a Post-retirement benefits

Post-retirement benefits are long-term liabilities whose value can only be estimated using assumptions about developments over a long period. The Bank has employed actuarial advice in arriving at the figures in the financial statements (see note 19, which includes relevant sensitivity analysis). Members of Court consider the assumptions used by the actuary in their calculations to be appropriate for this purpose.

b Fair value of equity investments that are available for sale

The Bank's accounting policy for the valuation of financial instruments is described in note 2 (e) and (k). The best evidence of fair value is a quoted price in an actively traded market. In the event that the market for a financial instrument is not active, a valuation technique is used. The majority of valuation techniques employ only observable market data, and so the reliability of the fair value measurement is high. Details of valuation techniques for the different classifications are given in note 29. Fair values of equity investments classified for accounting purposes as available for sale rely to a greater extent on unobservable inputs and therefore require a greater level of management judgement to calculate a fair value than those based on wholly observable inputs. These equity investments, disclosed in note 14, are held by the Bank for the long term as part of its central banking activities and may not be readily saleable. The values have generally been established using an adjusted net asset value basis (see note 14b, which includes relevant sensitivity analysis).

c Intangible assets

Management has made certain judgements when capitalising intangible assets. Various costs incurred in the production of an internal project are capitalised if a number of criteria are met. Management has made judgements and assumptions when assessing whether a project meets these criteria and when measuring the costs and economic life attributable to such projects.

d Onerous lease provision

The Bank recognises an onerous lease provision, originally recognised in 2013, in respect to certain leased property occupied by the FSA which was vacated on the commencement of the new regulatory regime.

In determining the provision Management made certain judgements in respect of decommissioning costs. The provision is included within note 26.

4a Net operating income

	Note	2017 £m	2016 £m
Fee income			
Funding for Lending Scheme fees	30	146	160
Payment services fee income		13	12
Banking operations		10	10
Net fee income		**169**	**182**
Other income from financial instruments			
Net income from financial instruments designated at fair value		34	23
Income from available for sale securities	14	176	191
Net other income from financial instruments		**210**	**214**
Management fees			
Fee for services to BEAPFF	32	4	2
Charges to HM Government bodies	32	112	92
PRA corporate services fee	32	98	97
Total management fees		**214**	**191**
Other income			
Dividend income		11	10
Premises income		11	10
Sundry income		4	4
Total other income		**26**	**24**
Net operating income (excluding net interest income)		**619**	**611**

Notes to the Banking Department financial statements continued

4b Operating expenses

	Note	2017 £m	2016 £m
Infrastructure costs			
Property and equipment		51	54
Depreciation of property, plant and equipment	17	22	19
Operating lease rentals		6	7
Amortisation of intangible assets	18	5	3
Impairment of property, equipment and intangible assets		–	1
Less: PRA infrastructure recharge		–	(3)
Total infrastructure costs		**84**	**81**
Administration and general costs			
Consultancy, legal and professional fees		29	38
Subscriptions, publications, stationery and communications		6	5
Travel and accommodation		6	6
Other administration and general expenses		81	62
Less: PRA administration and general costs		(13)	(18)
Total administration and general costs		**109**	**93**
Staff costs	**5**	**357**	**354**
Less: PRA staff costs		(138)	(135)
Total staff costs		**219**	**219**
Operating expenses		**412**	**393**

5 Staff costs

	2017 £m	2016 £m
Wages and salaries	290	271
Social security costs	34	28
Pension and other post-retirement costs	30	54
Costs of restructuring	3	1
	357	**354**

Of which the following was recharged to the PRA:

	2017 £m	2016 £m
Wages and salaries	105	102
Social security costs	13	11
Pension and other post-retirement costs	20	22
	138	**135**

Average number of employees

The average number of persons employed by the Bank during the year was made up as follows:

	2017	2016
Governors and other members of Executive Team	22	22
Managers and analysts	2,802	2,555
Other staff	1,437	1,406
	4,261	**3,983**

Of which deemed to work exclusively for the PRA:

	2017	2016
Governors and other members of Executive Team	6	5
Managers and analysts	1,124	1,028
Other staff	197	209
	1,327	**1,242**

The number of persons employed by the Bank at the end of February 2017 was 4,380 of which 3,883 were full-time and 497 part-time (2016: 4,108; with 3,650 full-time and 458 part-time). These include 1,367 persons deemed to work exclusively for the PRA of which 1,199 were full-time and 168 part-time (2016: 1,285; with 1,137 full-time and 148 part-time).

Mr Bailey and Mr Woods are deemed to work exclusively for the PRA in the table above. They are remunerated by the Bank but the total remuneration is recharged to the PRA.

Notes to the Banking Department financial statements continued

6 Auditor's remuneration

	2017 £000	2016 £000
For the period to 28 February 2017		
Fees relating to audit services performed for the current year	262	260
Fees relating to prior year	–	27
Fees payable to the Auditor for services provided to the Bank		
Non-audit assurance services	43	43
Taxation advisory services	4	7
All other services	18	–
	327	**337**

Audit-related services comprise £25,000 for providing assurance to HM Treasury on the allocation of costs (2016: £25,000), and £18,000 for the submission for Whole Government Accounts (2016: £18,000). Other non-audit fees principally relate to advisory services to the Bank.

Fees of £30,000 for prior year audit services in relation to Bank of England Asset Purchase Facility Fund Ltd were paid by the Bank and recovered via a management fee in 2016 (these are not included in the table above). Following changes introduced by the Bank of England and Financial Services Act 2016, the Bank of England Asset Purchase Facility Fund Ltd is now audited by the National Audit Office.

7 Taxation

The tax charged within the income statement is made up as follows:

	2017 £m	2016 £m
Current year corporation tax	12	14
Prior year corporation tax	–	(1)
Deferred tax – current year	8	10
Deferred tax – prior year	–	1
Tax charge on profit	**20**	**24**

The tax charged within the income statement differs from the amount calculated at the basic rate of tax on the profit for the year and is explained below:

	2017 £m	2016 £m
Profit before tax	**222**	**233**
Tax calculated at rate of 20.00% (2016: 20.08%)	44	47
Tax relief on payment to HM Treasury	(20)	(21)
Matured AFS recycled to income statement	(1)	–
Dividend not subject to corporation tax	(2)	(2)
Change in tax rate to 17% (2016: 18%)	(1)	–
Total tax charge for the period	**20**	**24**

Notes to the Banking Department financial statements continued

7 Taxation continued

Tax (credited)/charged to other comprehensive income comprises:

	2017 £m	2016 £m
Tax (credited)/charged to equity through the statement of comprehensive income		
Current year corporation tax	(46)	23
Deferred tax	28	202
Tax (credited)/charged to other comprehensive income	**(18)**	**225**

Tax (credited)/charged to other comprehensive income comprises:

	2017 £m	2016 £m
Tax (credited)/charged to equity through the statement of comprehensive income		
Revaluation of available for sale securities	65	185
Use of tax losses carried back	(33)	–
Revaluation of property	(2)	7
Remeasurements of retirement benefits	(20)	72
Change in tax rate to 17% (2016: 18%)	(28)	(39)
Tax (credited)/charged to other comprehensive income	**(18)**	**225**

The main UK corporation tax rate was 20% for the year beginning 1 April 2016 (1 April 2015: 20%). The effective rate for the year ended 28 February 2017 is 9.01% (2016: 10.24%).

8 Payable to HM Treasury under Section 1 (4) of the Bank of England Act 1946

	2017 £m	2016 £m
Payable April 2017 (2016: 5 April)	51	51
Payable October 2017 (2016: 5 October)	50	54
	101	**105**

The Bank of England Act 1946, as amended by the Bank of England Act 1998, requires the Bank to pay HM Treasury, in lieu of dividend on the Bank's capital, on 5 April and 5 October, a sum equal to 25%, on each of those dates, of the Banking Department's post-tax profit for the previous financial year or such other sum as the Bank and HM Treasury may agree. When the due date falls on a non-business day, the payment is made on the last business day before the due date. These payments have been accrued and charged to equity at 28 February 2017. The payments are deductible for corporation tax in the year to which the payments relate. The overall effect is that the Bank and HM Treasury will normally share Banking Department's post-tax profits equally.

9 Cash and balances with other central banks

	2017 £m	2016 £m
Balances with other central banks	1,641	637
	1,641	**637**

Balances with other central banks are correspondent accounts with other central banks used for Bank and customer business.

10 Loans and advances to banks and other financial institutions

	2017 £m	2016 £m
Secured lending agreements held at amortised cost	2,400	2,177
Reverse repurchase agreements held at fair value through profit and loss	7,440	10,525
Other loans and advances	3	4
	9,843	**12,706**

These balances include advances, secured lending and reverse repurchase agreements arising as part of the Bank's open market operations, as well as advances matching the deposits taken (notes 21 to 23). The level and composition of the Bank's open market operations, including the split between Banking and Issue Departments, depends on movements in the Bank's balance sheet as described in the published Bank of England's *Sterling Monetary Framework*.

At 28 February 2017 loans and advances to banks and other financial institutions included cash and cash equivalents of £6,448m (2016: £5,648m) which are disclosed in note 28i.

Notes to the Banking Department financial statements continued

11 Other loans and advances

	2017 £m	2016 £m
Loan to the Bank of England Asset Purchase Facility Fund Ltd	485,149	375,193
Term loans	5	5
	485,154	**375,198**

Loan to Bank of England Asset Purchase Facility Fund Ltd

In January 2009, the Chancellor of the Exchequer authorised the Bank to set up an Asset Purchase Facility (APF) to buy high-quality assets financed by the issue of Treasury bills and the Debt Management Office's (DMO) cash management operations. The aim of the APF was to improve liquidity in credit markets. The Chancellor also announced that the APF provided an additional tool that the Monetary Policy Committee (MPC) could use for monetary policy purposes. When the APF is used for monetary policy purposes, purchases of assets are financed by the creation of central bank reserves.

The APF transactions are undertaken by a subsidiary company of the Bank of England — the Bank of England Asset Purchase Facility Fund Limited (BEAPFF). The transactions are funded by a loan from the Bank, with interest charged at Bank Rate.

In line with the MPC's August 2016 decision in relation to the asset purchase programme; the APF will increase its purchases of assets by the creation of central bank reserves since the inception of the scheme in 2009 to a total of £545.0bn. At 28 February 2017, the total amount of gilts purchased, less redemptions, valued at initial purchase price was £431.9bn (operations to increase this to £435bn concluded on 13 March 2017). The total amount of loans made through the TFS since the drawdown window opened, until 28 February 2017, less repayments, was £42.3bn. The sum of corporate bonds purchased, less redemptions, valued at initial purchase price, was £7.7bn (operations to increase this to £10bn concluded on 27 April 2017). Additionally, the APF continues to offer its corporate facilities, with purchases financed by the issue of Treasury bills and the DMO's cash management operations but these were unused at year end. The loan in relation to the corporate facilities is £0.2bn. The total loan from the Bank to BEAPFF is £485.1bn (2016: £375.2bn). Accrued interest of £89m on the loan is recognised in note 20.

12 Securities held at fair value through profit or loss

	2017 £m	2016 £m
Money market instruments	2,944	2,381
Listed foreign government securities	6,213	4,809
	9,157	**7,190**

The holdings of foreign government securities are funded by the Bank's issuance of medium-term securities (note 24) and fixed-term deposits placed by other central banks. At the year end bond purchases settling on 6 March 2017 led to the recognition of items in course of collection within Other liabilities (note 26).

At 28 February 2017 money market instruments included cash and cash equivalents of £1,047m (2016: £389m) which are disclosed in note 28i.

13 Derivative financial instruments

The Bank uses the derivative instruments described below. The main purpose of these is to manage the currency and interest rate exposures on the Bank's portfolio of financial assets and financial liabilities. They may also be used as an instrument in monetary policy transactions.

Cross-currency interest rate swaps, interest rate swaps and forward exchange contracts are commitments to exchange one set of cash flows for another. Swaps result in an economic exchange of currencies or coupons (eg fixed rate for floating rate) or a combination of these. An exchange of principal occurs for cross-currency interest rate swaps and forward exchange contracts. The Bank's credit risk represents the potential cost to replace the swap contracts if counterparties fail to perform their obligations. The risk is monitored on an ongoing basis with reference to the current fair value. To control the level of credit risk taken, the Bank assesses counterparties using the same techniques as for its lending activities and will take collateral, either securities or cash, if the net replacement cost of all transactions with the counterparty exceeds relevant thresholds.

The notional amounts of derivative financial instruments provide a basis for comparison with other instruments recognised in the balance sheet but do not necessarily indicate the amounts of future cash flows involved or the current fair value of the instruments and therefore do not indicate the Bank's exposure to credit or price risks. The derivative instruments move into profit (in which case they are treated as assets) or loss (in which case they are treated as liabilities) as a result of fluctuations in market prices relative to their terms. The aggregate contractual or notional amount of derivative financial instruments outstanding, the extent to which instruments have moved into profit or not, and thus the aggregate fair values of derivative financial instruments, can fluctuate significantly over time. The fair values of derivative instruments are set out below.

a As at 28 February 2017

	Contract notional amount £m	Fair Values	
		Assets £m	Liabilities £m
Cross-currency interest rate swaps	4,335	246	(20)
Interest rate swaps	8,505	7	(15)
Forward exchange contracts	11,308	55	(73)
Total recognised derivative assets/(liabilities)		**308**	**(108)**

b As at 29 February 2016

	Contract notional amount £m	Fair Values	
		Assets £m	Liabilities £m
Cross-currency interest rate swaps	3,196	367	(48)
Interest rate swaps	6,282	17	(19)
Forward exchange contracts	14,184	104	(409)
Total recognised derivative assets/(liabilities)		**488**	**(476)**

Notes to the Banking Department financial statements continued

14 Available for sale securities

	2017 £m	2016[1] £m
Debt securities at fair value		
British Government securities listed on a recognised UK exchange	7,032	6,703
Other sterling securities listed on a recognised exchange	124	130
	7,156	**6,833**
Unlisted equity investments at fair value	1,246	1,111
	8,402	**7,944**

1 Certain prior year comparatives have been changed to be consistent with current year presentation.

The movement in available for sale securities comprises:

	2017 £m	2016 £m
Available for sale debt securities		
At 1 March	6,833	6,703
Purchases	870	532
Redemptions	(483)	(427)
Mark-to-market movements through equity	19	100
Amortisation of premium/discount and movement in accrued interest	(83)	(75)
At 28 February	**7,156**	**6,833**
Available for sale unlisted equity investments		
At 1 March	1,111	291
Revaluation of securities	34	793
Foreign currency gains	101	27
At 28 February	**1,246**	**1,111**
	8,402	**7,944**

There were no items in the course of settlement for available for sale securities at the year ended 28 February 2017 (2016: £nil). The significant decrease in the revaluation of unlisted equity investments was due to a change in valuation methodology from a dividend growth model to adjusted net asset value that occurred in the prior year. There has been no change in valuation methodology this year.

There were no gains or losses on the sale of available for sale securities transferred to the income statement during the year (2016: £nil).

Net income recognised in the year ended 28 February 2017 for the Bank's available for sale investments was £176m (2016: £191m), in the current and prior year this comprises interest income and purchase premium amortisation.

a Debt securities

British Government securities and other sterling securities are held as investments and are one of the principal sources of income for the Bank. The Bank holds these securities for the long term, generally to maturity. However, as the Bank can envisage circumstances in which they might be sold before maturity they have been classified as assets that are available for sale.

All debt securities have fixed coupons.

b Unlisted equity investments

The unlisted equity investments held by the Bank are held as part of its functions as a central bank and are thus of a long-standing nature. The Bank's holdings in any particular institution may change from time to time as part of realignments of holdings among the shareholders and participants. Fair values of unlisted equity investments reflect the price that a knowledgeable willing party would pay in an arm's length transaction.

The Bank's investment in the Bank for International Settlements (BIS) (incorporated in Switzerland) consists of shares of 5,000 Special Drawing Rights, which are 25% paid. At 28 February 2017 the holding represents 8.5% (2016: 8.5%) of the issued share capital.

The fair value of the BIS shares is estimated to be 70% of the Bank's interest in the net asset value of the BIS at the reporting date. The most unobservable input for the BIS valuation is the 30% discount to net asset value, which is based on the discount rate used by the BIS for all share repurchases since the 1970s and was further endorsed by a decision by the International Court at the Hague relating to a share repurchase by the BIS in 2001 (the last share repurchase conducted by the BIS). The Bank's financial statements incorporate the most recently available data from the BIS. The Bank expects the value of the BIS shares to fluctuate over time in conjunction with the strength of the BIS balance sheet and exchange rates. If the value of the net assets of the BIS changed by 1%, the value of the investments would change by £12m (2016: £11m).

Since 1930 there has also been a contingent liability in respect of uncalled capital on the Bank's investment in the BIS, now denominated in Special Drawing Rights (SDR). The sterling equivalent of this liability based on the SDR price at the balance sheet date was £195m (2016: £178m). The balance of £195m is callable at three months' notice by a decision of the BIS Board of Directors.

The Bank's holding in the European Central Bank (ECB) represents 0.7% (2016: 0.7%) of the ECB's paid-up share capital. In accordance with the Treaty on the Functioning of the European Union, and in line with other non euro area national central banks, the Bank is only required to pay up 'a minimal percentage' by way of contribution to the operational costs of the ECB; in the Bank's case this is currently 3.75% amounting to €56m (2016: 3.75% amounting to €56m) of its total allocation of the ECB's subscribed capital of €1.5bn (2016: €1.5bn).

Contributions to the ECB by EU Member States under Article 28 of the Statute of the ECB, are non-refundable and as a non euro area member the Bank is not entitled to any dividends. The fair value of the holding has therefore been assessed as £nil (2016: £nil), the status of the Bank's capital contribution will need to be reassessed in the context of the negotiations under Article 50 of the Treaty on European Union.

15 Investments in subsidiaries

The Bank has a number of subsidiaries, which are wholly owned and incorporated in the United Kingdom, that are stated in the Bank's balance sheet at an aggregate cost under £1m. These are:

The Securities Management Trust Ltd 1,000 ordinary shares of £1, principal activity is that of a nominee company.
Bank of England Asset Purchase Facility Fund Ltd 100 ordinary shares of £1, principal activity is to fulfil the remit given to the Bank by the Chancellor of the Exchequer and for monetary policy.
BE Pension Fund Trustees Ltd 2 ordinary shares of £1, principal activity is that of provision of trustee services to the Bank of England Pension Fund.
Prudential Regulation Authority Ltd 1 ordinary share of £1, principal activity was that of the United Kingdom's prudential regulator.
Bank of England Nominees Ltd, a wholly owned subsidiary, has been in members voluntary liquidation since 13 October 2016. During the year no distributions were received from the liquidators. The company was liquidated on 31 March 2017.
Houblon Nominees Ltd, a wholly owned subsidiary, was liquidated during the year.

Notes to the Banking Department financial statements continued

16 Inventories

	2017 £m	2016 £m
Raw materials (at cost)	4	2
	4	2

During 2017, £24m (2016: £14m) was recognised as an expense for inventories carried at the lower of cost or net realisable value. This is recognised in other general and administration expenses.

17 Property, plant and equipment

For the period to 28 February 2017	Freehold land and buildings £m	Leasehold improvements £m	Equipment[1] £m	Total £m
Cost or valuation				
At 1 March 2016	317	12	106	435
Additions	8	1	30	39
Disposals/write-offs	–	–	(8)	(8)
Revaluation of properties	(13)	–	–	(13)
At 28 February 2017	**312**	**13**	**128**	**453**
Accumulated depreciation				
At 1 March 2016	–	3	40	43
Charge for the period	4	1	17	22
Disposals/write-offs	–	–	(8)	(8)
Revaluation of properties	(4)	–	–	(4)
At 28 February 2017	–	**4**	**49**	**53**
Net book value at 1 March 2016	317	9	66	392
Net book value at 28 February 2017	**312**	**9**	**79**	**400**

1 Net book value of equipment at 28 February 2017 included £1m held under finance leases.

The figures for freehold land and buildings reflect independent professional valuations performed in accordance with the Royal Institution of Chartered Surveyors (RICS) on a market value basis as at 28 February 2017 by Deloitte LLP, members of RICS.

Included within additions is £3m (2016: £10m) of assets purchased but not paid for at the balance sheet date.

For the period to 29 February 2016	Freehold land and buildings £m	Leasehold improvements £m	Equipment[1] £m	Total £m
Cost or valuation				
At 1 March 2015	278	11	86	375
Additions	9	1	27	37
Disposals/write-offs	–	–	(7)	(7)
Revaluation of properties	30	–	–	30
At 29 February 2016	**317**	**12**	**106**	**435**
Accumulated depreciation				
At 1 March 2015	-	2	32	34
Charge for the period	4	1	14	19
Disposals/write-offs	-	-	(6)	(6)
Revaluation of properties	(4)	-	-	(4)
At 29 February 2016	**-**	**3**	**40**	**43**
Net book value at 1 March 2015	278	9	54	341
Net book value at 29 February 2016	**317**	**9**	**66**	**392**

1 Net book value of equipment at 29 February 2016 included £2m held under finance leases.

Notes to the Banking Department financial statements continued

18 Intangible assets

	2017 £m	2016 £m
Cost		
At 1 March	26	38
Additions	8	10
Disposals/write-offs	(1)	(22)
At 28 February	**33**	**26**
Accumulated amortisation		
At 1 March	8	26
Charge for the year	5	3
Disposals/write-offs	(1)	(21)
At 28 February	**12**	**8**
Net book value at 1 March	18	12
Net book value at 28 February	**21**	**18**

Intangible assets primarily comprise computer software and related costs.

Included within additions is less than £1m (2016: £4m) of intangible assets purchased but not paid for at the balance sheet date.

19 Retirement benefits

a Defined contribution

Staff transferred to the Bank from the Financial Services Authority (FSA) in April 2013 retained the employment terms and conditions of the FSA. These staff members continued to be active members within the FSA Pension Plan, which operated on a defined contribution basis, until 31 March 2015. The Bank made fixed contributions for employees into this scheme which are accounted for as contributions in the period they relate to. During the year total contributions made by the Bank were £nil (2016: £0.7m) of which £nil was recharged to the PRA (2016: £0.5m). No contributions were outstanding at the year end.

From 1 April 2015 staff on the FSA legacy contracts became members of the Bank's career average pension scheme.

b Defined benefit and career average

The Bank operates a non-contributory defined-benefit pension scheme providing benefits based on career average pensionable pay. The final salary element of the scheme is closed to future accrual for service but a link to final salary remains for active members. The assets of the scheme are held by the Bank in an independent trustee-administered fund. The Bank also provides other post-retirement benefits, principally healthcare, for certain pensioners.

The pension scheme is an HMRC registered pension scheme and is subject to standard UK pensions and tax law. This means that the payment of contributions and benefits are subject to the appropriate tax treatments and restrictions and the scheme is subject to the scheme funding requirements outlined in section 224 of the Pensions Act 2004.

In accordance with UK trust and pensions law, the pension scheme has appointed trustees who are independent of the Bank. Although the Bank bears the financial cost of the scheme, the responsibility for the management and governance of the scheme lies with the trustees, who have a duty to act in the best interest of members at all times.

The pension scheme's assets are mostly invested in fixed interest and index-linked gilts which are intended to match the nature of the future benefit payments due from the scheme. This helps to reduce volatility in the funding level on the scheme funding basis and, to a lesser extent, in the statement of financial position in the Bank's accounts. The effect of the liability-matching investment policy is not fully reflected in the accounting figures as the assumptions dictated for the purposes of the valuation under IAS 19 are different from those used for the funding valuation.

Valuation for funding purposes

The main pension scheme, the Bank of England Pension Fund, is valued for funding purposes at intervals of not more than three years by an independent qualified actuary, with interim reviews in the intervening years. The latest valuation for funding purposes was as at 28 February 2014 (the valuation as at 28 February 2017 will be finalised later in 2017); it used the Defined Accrued Benefit Method. Under this method, active members are assumed to leave the Fund on the date of the valuation and hence the past service liability does not include an allowance for any salary increases or in-service CARE revaluation after that date. Instead members' benefits are assumed to increase in line with the deferred pension revaluation assumptions.

The valuation as at 28 February 2014	£m
Value of Fund assets	3,075
Actuarial value of scheme liabilities in respect of:	
– In-service members	(613)
– Deferred pensioners	(663)
– Current pensioners and dependants	(1,825)
– Members' additional voluntary contributions	(5)
Total	(3,106)
Scheme (deficit)/surplus	**(31)**
Funding level	99%
Service contribution rate for March	32%

For the 2014 valuation, the liabilities were valued by the actuary on an index-linked gilts yield discount rate, and no credit was taken in advance for the possibility that returns on investments held by the Fund would exceed the long-term interest rate. Allowance was made for past and prospective mortality improvements. The rate of RPI inflation used in the valuation and the pension increase assumption was 3.3%.

The Bank and the Pension Fund Trustees had agreed a deficit reduction plan and a new schedule of contributions following the valuation. The Bank paid an additional lump sum contribution of £4.4m to the Fund in July 2014 which when taken together with the contribution of £26.7m paid in March 2014 under the previous recovery plan, is sufficient to eliminate the deficit as at 28 February 2014. The scheme is expected to be fully funded on an ongoing basis.

Excluded from the contribution rate is the cost of administration and other services which is met by the Bank.

Summary of amounts recognised in the financial statements under IAS 19

In the statutory financial statements the Bank accounts for pension costs, other post-retirement benefits and related redundancy provisions in accordance with IAS 19 (Employee Benefits). Under the standard, the difference between the market values of scheme assets and the present value of scheme liabilities is reported as a surplus or deficit in the balance sheet. The accounting value is different from the result obtained using the funding basis.

Notes to the Banking Department financial statements continued

19 Retirement benefits continued

The accounts show the main scheme in surplus, while the Bank cleared the deficit revealed by the previous funding valuations in 2014. The main reason for this is the different assumptions used to value the liabilities in the accounting and funding valuations for the main scheme. The aim of the liability matching policy is that by investing in a range of assets (mostly government bonds) that broadly match the expected future benefit payments from the scheme, no surplus or deficit will arise.

The funding valuation, therefore, discounts expected future benefit payments at the appropriate yield available on government bonds to produce the value of the funding liabilities. The accounting standard requires that expected future benefit payments are discounted at the appropriate yield available on high-quality corporate bonds, which is higher than the corresponding yield available on government bonds. The value placed on the liabilities for accounting purposes is, therefore, lower than the funding valuation.

In the preparation of their valuations under IAS 19 referred to in this note, the actuary has used the assumptions indicated below, which members of Court have accepted for the purposes of accounting and disclosure under the standard.

Amounts recognised as assets/(liabilities) in the balance sheet

	Note	2017 £m	2016 £m
Funded pension schemes	(i)	917	932
Unfunded post-retirement benefits:			
Redundancy provisions	(ii)	(79)	(73)
Other pension schemes	(iii)	(9)	(8)
Medical scheme	(iv)	(141)	(113)
		688	**738**

Pension expense recognised in the income statement[1]

	Note	2017 £m	2016 £m
Funded pension schemes	(i)	21	44
Unfunded post-retirement benefits:			
Redundancy provisions	(ii)	3	3
Other pension schemes	(iii)	–	–
Medical scheme	(iv)	5	5
		29	**52**

1 Of the total defined-benefit pension expense of £29m, £20m relates to staff working for the PRA and has been included in the PRA accounts.

Remeasurements recognised in the statement of comprehensive income

	Note	2017 £m	2016 £m
Funded pension schemes	(i)	(62)	346
Unfunded post-retirement benefits:			
Redundancy provisions	(ii)	(8)	7
Other pension schemes	(iii)	(1)	1
Medical scheme	(iv)	(29)	4
		(100)	**358**

(i) Funded pension scheme

As described above, the Bank has a final salary section within the pension scheme that provides pensions based on members' pensionable service and final salary at retirement. The pension is payable for life and increases in payment in line with inflation. This section of the scheme ceased to accrue benefits on a final salary basis from 1 April 2015. Former members of this section can continue to accrue benefits in the career average revalued earnings (CARE) section.

For new employees the Bank offers a CARE section of the pension scheme that provides pensions based on members' earnings each year revalued in line with inflation up to retirement. The pension is payable for life and increases in payment in line with inflation.

(ii) Redundancy provisions

As part of redundancy arrangements with staff in place until 5 April 2010, the Bank could give enhanced pension entitlement in the form of added years service or early pension rights. The costs of such benefits cannot be charged to the Pension Fund. The costs are therefore borne in the Bank's accounts, and represent the future cost of decisions that have already been taken. Provision was made for the costs of these benefits at the time the redundancy offer was announced based on actuarial advice. No further similar entitlements will be given by the Bank.

The valuation of these provisions has been performed using the relevant assumptions applied for the IAS 19 valuation of pension schemes and updated annually.

(iii) Other pension schemes

Previously for Governors subject to the pensions earnings cap introduced in the Finance Act 1989, the Bank offered additional unfunded pensions so that their total pensions broadly match what would have been provided by the former Court Pension Scheme in the absence of a cap. Provision is made for these in the Bank's accounts. In addition certain former Governors and Directors and the widows of some former Governors and Directors were granted *ex-gratia* pensions. Provision for these was made in the Bank's accounts when the grants were made.

The valuation of this scheme has been performed by using the relevant assumptions applied for the IAS 19 valuation of pension schemes and updated annually.

Notes to the Banking Department financial statements continued

19 Retirement benefits continued

(iv) Medical scheme

Some current and former staff are entitled to receive healthcare benefits in retirement. Separate provision is made for these in the Bank's accounts as these cannot be paid out of the pension scheme. The defined-benefit liability is the expected cost to the Bank of the claims expected to be incurred by the eligible members once in retirement.

Risks

The main risks to which the Bank is exposed in relation to the funded pension scheme are:

- Mortality risk — the assumptions adopted by the Bank make allowance for future improvements in life expectancy. However, if life expectancy improves at a faster rate than assumed, this would result in greater payments from the Fund and consequently increases in the scheme's liabilities. The Bank and the scheme's trustees review the mortality assumption on a regular basis to minimise the risk of using an inappropriate assumption.

- Investment risk — the Fund invests the vast majority of its assets in a portfolio of UK Government bonds as the changes in the value of the bonds most closely match the movements in the Fund's liabilities. There are risks with the selected portfolio such that it does not match the liabilities closely enough or that as it matures there is a risk of not being able to reinvest the assets at the assumed rates. The scheme's trustees review the structure of the portfolio on a regular basis to minimise these risks.

- Yield risk — a fall in government bond yields will increase both the scheme's assets and liabilities. As the scheme's liabilities, on the funding basis used to calculate the Bank's contributions to the scheme, are greater than its assets, the liabilities would be expected to grow by more in monetary terms, increasing the deficit in the scheme.

- Inflation risk — the majority of the scheme's liabilities increase in line with inflation and so if inflation is greater than expected, the liabilities will increase. The scheme's investment strategy is to hold government bonds that are also linked to inflation so this risk is mostly mitigated.

The redundancy provision and other pension schemes are primarily exposed to the mortality and inflation risks above. As they are not backed by any assets, these risks cannot be so easily managed. However, these arrangements (and therefore the risks associated with them) are small in comparison to the funded pension scheme.

The two main risks to which the Bank is exposed in relation to the medical scheme are mortality risk, as described above, and increases in the costs incurred being greater than assumed, either due to inflation of future medical costs or the frequency of members' claims.

Components of pension expense in the Income Statement

	2017			2016		
	Main pension scheme £m	Other pensions £m	Medical scheme £m	Main pension scheme £m	Other pensions £m	Medical scheme £m
Current service cost	56	–	1	63	–	1
Past service cost	–	–	–	–	–	–
Net interest on the net defined liability/asset	(35)	3	4	(19)	3	4
Total pension expense	**21**	**3**	**5**	**44**	**3**	**5**

Remeasurements recognised in other comprehensive income

	2017			2016		
	Main pension scheme £m	Other pensions £m	Medical scheme £m	Main pension scheme £m	Other pensions £m	Medical scheme £m
Remeasurements recognised at the beginning of the period	389	(26)	9	43	(34)	5
Actuarial gains/(losses) arising from changes in demographic assumptions	112	2	(2)	96	3	–
Actuarial losses arising from changes in financial assumptions	(807)	(14)	(27)	139	3	5
Actuarial losses/(gains) arising from experience on the scheme's liabilities	43	3	–	50	2	(1)
Return on scheme's assets excluding interest income	590	–	–	61	–	–
Remeasurements recognised at the end of the period	**327**	**(35)**	**(20)**	**389**	**(26)**	**9**

Reconciliation of present value of defined-benefit obligation

	2017			2016		
	Main pension scheme £m	Other pensions £m	Medical scheme £m	Main pension scheme £m	Other pensions £m	Medical scheme £m
Present value of defined-benefit obligation at the beginning of the period	2,825	81	113	3,052	92	116
Current service cost	56	–	1	63	–	1
Interest expense	104	3	4	104	3	4
Actuarial (gains)/losses arising from changes in demographic assumptions	(112)	(2)	2	(96)	(3)	–
Actuarial losses arising from changes in financial assumptions	807	14	27	(139)	(3)	(5)
Actuarial losses/(gains) arising from experience on the scheme's liabilities	(43)	(3)	–	(50)	(2)	1
Benefits paid out	(120)	(5)	(6)	(109)	(6)	(4)
Present value of defined-benefit obligation at the end of the period	**3,517**	**88**	**141**	**2,825**	**81**	**113**

During the reporting period there have been no plan amendments, curtailments or settlements.

Notes to the Banking Department financial statements continued

19 Retirement benefits continued

Reconciliation of the fair value of assets

	2017			2016		
	Main pension scheme £m	Other pensions £m	Medical scheme £m	Main pension scheme £m	Other pensions £m	Medical scheme £m
Fair value of scheme's assets at the beginning of the period	3,757	–	–	3,592	–	–
Interest income	139	–	–	123	–	–
Return on scheme's assets excluding interest income	590	–	–	61	–	–
Bank contributions	68	5	6	90	6	4
Benefits paid out	(120)	(5)	(6)	(109)	(6)	(4)
Fair value of scheme's assets at the end of the period	**4,434**	–	–	**3,757**	–	–

Summary of assumptions

Under IAS 19 measurement of scheme liabilities must be calculated under the projected unit method, which requires certain demographic and financial assumptions, including an assumption about future salary growth. The assumptions used are applied for the purposes of IAS 19 only.

The significant financial and other assumptions used by the independent actuary to calculate scheme liabilities over the life of the scheme on an IAS 19 basis were:

	2017 %	2016 %
Discount rate	2.4	3.7
Rate of increase in salaries	3.5	3.5
Rate of increase of pensions in payment[1]	3.0	3.3
Rate of increase for deferred pensioners[1]	3.2	3.3

1 This represents a weighted average of RPI and CPI, which are the indices used in the scheme.

The discount rate assumption reflects the investment return on a high-quality corporate bond at the balance sheet date, as required by the standard.

The assumption on salary growth is for the long term over the life of the scheme.

An age-related promotion scale has been added to the increase in salaries assumption.

The assumption for life expectancy for the scheme is that a male member reaching 60 in 2017 will live for 27.8 years (29 February 2016: 28.2 years) and a female member 29.4 years (29 February 2016: 30 years), and a male member reaching 60 in 2037 will live for 29.7 years (29 February 2016: 30.6 years) and a female member 31.4 years (29 February 2016: 32.5 years).

The Bank has adopted the latest available mortality projections model, which reduces the Fund's liability as a result of recent improvements in mortality being slightly lower than previously assumed.

The assets in the scheme were:

	2017 Value £m	2017 Percentage of total value %	2016 Value £m	2016 Percentage of total value %
UK Government fixed-interest bonds	404	9	356	9
UK Government index-linked bonds	2,699	61	2,280	61
Corporate index-linked bonds	1,310	30	1,081	29
Cash and other assets	21	–	40	1
Total market value of investments	**4,434**	**100**	**3,757**	**100**

For the purposes of IAS 19, the asset values stated are at the balance sheet date. Market values of the scheme's assets, which are not intended to be realised in the short term, may be subject to significant change before they are realised.

Of the corporate index-linked bonds £868m were quoted and £442m were unquoted (2016: £686m quoted and £395m unquoted). Of the corporate index-linked bonds £1,273m (2016: £1,039m) were guaranteed by the UK Government.

Main scheme

	2017 £m	2016 £m
Present value of defined-benefit obligations	(3,517)	(2,825)
Assets at fair value	4,434	3,757
Defined-benefit asset (liability)	**917**	**932**

The Bank has recognised the net surplus in full on the balance sheet as it can realise any surplus on the winding up of the scheme after all other benefits have been paid in full in accordance with the Fund's rules. The Trustee does not have any unilateral powers which would prevent this and the rules can only be amended with agreement between the Bank and the Trustees.

The duration of the pension scheme liabilities is in the region of 20 years. A +/- 0.1% change to the discount rate would change the surplus on the pension scheme by +/- £71m (29 February 2016: +/- £51m).

A +/- 0.1% change to the assumed difference between CPI and RPI inflation (ie a +/- 0.1% change to RPI inflation) would change the present value of defined-benefit obligations for the pension scheme by +/- £55m (29 February 2016: +/- £42m).

A +/- 0.5% change to the assumed rate of increases in salaries would change the surplus on the pension scheme by +/- £29m (29 February 2016: +/- £22m).

If mortality rates were adjusted such that individuals were assumed to live for an additional year, the scheme's liabilities at the year end would increase by approximately £115m (29 February 2016: £87m).

The Bank expects to pay contributions of £97m in the forthcoming year (2016: £68m).

Notes to the Banking Department financial statements continued

19 Retirement benefits continued

Redundancy provisions

	2017 £m	2016 £m
Unfunded defined-benefit liability	**(79)**	**(73)**

The Bank expects to make payments of £6m in the forthcoming year (2016: £6m).

Other pension schemes

	2017 £m	2016 £m
Unfunded defined-benefit liability	**(9)**	**(8)**

The Bank expects to make payments of less than £1m in the forthcoming year (2016: less than £1m).

During the year to 28 February 2017 the Bank incurred services costs of less than £1m (2016: less than £1m).

Medical scheme

Some staff are entitled to receive healthcare benefits in retirement. Separate provision is made for these in the Bank's accounts as these cannot be paid out of the Pension Fund.

Summary of assumptions

The discount rates used for the purposes of measuring post-retirement medical benefit liabilities is the same as used in the IAS 19 valuation of pension scheme liabilities (see Summary of assumptions on page 116). Additionally, for accounting purposes the following assumptions have been made in respect of medical expense inflation:

	2017 %	2016 %
Initial medical trend	5.0	5.0
Ultimate medical trend	5.0	5.0
Years to ultimate	–	–

Post-retirement benefits — medical

	2017 £m	2016 £m
Unfunded defined-benefit liability	**(141)**	**(113)**

Sensitivity analysis provided by the actuary indicates that 0.1% decrease in the discount rate would change the deficit on the other post-retirement benefits by £2m (29 February 2016: £2m) and a 1% increase in the rate of medical claims by £25m (29 February 2016: £19m). If the mortality rates were adjusted such that individuals were assumed to live for an additional year, the other post-retirement liabilities at the year end would increase by approximately £6m (29 February 2016: £4m).

The Bank expects to pay premiums of £5m in the forthcoming year (2016: £4m).

20 Other assets

	2017 £m	2016 £m
Finance lease receivables	6	6
Short term debtors and other assets	149	190
Amounts due from the PRA	37	55
Items in course of settlement	1,606	–
	1,798	**251**

The amount owed by the PRA includes nil due in more than one year (2016: £15m). Finance lease receivables also include £6m due in more than one year (2016: £6m).

21 Deposits from central banks

	2017 £m	2016 £m
Deposits repayable on demand	3,713	1,497
Term deposits held at fair value through profit and loss	11,381	13,858
	15,094	**15,355**

22 Deposits from banks and other financial institutions

	2017 £m	2016 £m
Deposits repayable on demand	411,064	320,410
Cash Ratio Deposits	4,424	4,136
	415,488	**324,546**

The majority of deposits repayable on demand comprise of reserves accounts held at the Bank. Reserves accounts are sterling current accounts for banks and building societies. They are the most liquid asset a bank or building society can hold and are the ultimate means of settlement between banks and building societies.

The rate paid by the Bank on reserves account balances is also the means by which the Bank keeps market interest rates in line with Bank Rate. All reserves balances are remunerated at Bank Rate.

Under the Cash Ratio Deposit (CRD) scheme, institutions place non-interest bearing deposits at the Bank of England. The Bank invests these deposits (mainly in gilts) and the income earned is used to fund the costs of its monetary policy and financial stability operations, which benefit sterling deposit-takers.

Under the Bank of England Act 1998, the percentage and threshold used in calculating the CRDs is set by HM Treasury, having regard to the financial needs of the Bank and subject to approval of both Houses of Parliament. This is reviewed, at the latest, every five years and was last reviewed in May 2013.

Notes to the Banking Department financial statements continued

23 Other deposits

	2017 £m	2016 £m
Deposit by Issue Department	63,049	50,870
Public deposits repayable on demand	3,745	2,781
Other deposits repayable on demand	6,519	1,932
	73,313	**55,583**

Public deposits are the balances on HM Government accounts, including Exchequer, National Loans Fund, Debt Management Office, National Debt Commissioners and dividend accounts.

24 Foreign currency bonds in issue

	2017		2016	
	£m Fair value	US$m Nominal	£m Fair value	US$m Nominal
Total amounts issued to third parties	**6,450**	**8,000**	**4,333**	**6,000**

All changes in fair values since 1 March 2016 are considered attributable to changes in prevailing interest rates and movements in relative foreign currency exchange rates, as well as issuance and maturity of bonds.

At 28 February 2017, as part of the Bank's annual medium-term security issuance programme the Bank had four US$2,000m three-year dollar bonds in issue (2016: three US$2,000m three-year dollar bonds); the first maturing on 17 March 2017, the second on 16 March 2018, the third on 14 March 2019 and the fourth on 6 March 2020.

The most recent bond (the eleventh in the overall programme) was issued on 27 February 2017 with settlement on 6 March 2017. This bond matures on 6 March 2020. Refer to www.bankofengland.co.uk/markets/Pages/reserves/default.aspx for further details of the issuance. As this bond settled on 6 March 2017 the proceeds due have been recognised as an item in course of settlement in Other assets (note 20).

Of the above liabilities to third parties, £1,614m (2016: £1,435m) fall due within one year.

25 Deferred tax liabilities

The deferred tax liability at 28 February has been calculated on all temporary differences under the liability method using an effective rate of 17% (2016: 18%) substantively enacted as at balance sheet date.

A reduction in the UK corporation tax rate to 17% (effective from 1 April 2020) was announced in September 2016 and had been substantially enacted as at 28 February 2017.

The movement on the deferred tax account is as follows:

	Note	2017 £m	2016 £m
Deferred tax			
Net liability at 1 March		341	128
Income statement charge	7	8	11
Tax credited/(charged) directly to other comprehensive income		28	202
Net liability at 28 February		**377**	**341**

	2017 £m	2016 £m
Deferred tax liability relates to:		
Available for sale equity investments through comprehensive income	206	193
Revaluation of available for sale debt securities	100	–
Transitional adjustment on available for sale debt securities	(58)	–
Pensions and other post-retirement benefits	117	133
Other provisions	12	15
	377	**341**

26 Other liabilities

i Analysis of other liabilities

	2017 £m	2016 £m
Items in course of collection	1,610	1
Payable to HM Treasury	100	102
Short term creditors and other liabilities	147	196
Provisions	9	7
	1,866	**306**

Payable to HM Treasury includes payment in lieu of dividend (note 8) and any over/under recoveries of management fees for the management of the notes issue and the Exchange Equalisation Account.

Notes to the Banking Department financial statements continued

26 Other liabilities continued

ii Analysis of provisions

	Restructuring provision £m	Onerous lease provision £m	Other provisions £m	Total £m
Balance at 1 March 2016	–	5	2	7
Provisions utilised during the year	–	(1)	–	(1)
Provisions made during the year	4	–	–	4
Provisions reversed during the year	–	–	(1)	(1)
Balance at 28 February 2017	4	**4**	**1**	**9**

Onerous lease provision

The Bank has undertaken to bear the costs arising from certain leased property previously occupied by the Financial Services Authority and which was vacated upon the commencement of the new regulatory regime. The amount provided for represents the net present value of the future lease payments and the costs of dilapidations required as part of the lease less any expected lease income from sub-letting the floor space.

The lease expires in November 2018. Of the above provision £2m (2016: £2m) falls due within one year. The cash flows are discounted at a risk free rate at 28 February 2017. The impact of the discount unwind is negligible.

27 Capital

	2017 £m	2016 £m
Capital	**15**	**15**

The entire capital comprising £14,553,000 of Bank Stock is held by the Treasury Solicitor on behalf of HM Treasury. The Bank regards its shareholder's funds as the capital it uses to support its normal operations. For special operations it may also obtain indemnities from HM Treasury.

28 Cash and cash equivalents

i Analysis of cash balances

	Note	At 1 March 2016 £m	Cash flows £m	At 28 February 2017 £m
Cash and balances with other central banks	9	637	1,004	1,641
Loans and advances to banks and other financial institutions	10	5,648	800	6,448
Securities held at fair value through profit and loss	12	389	658	1,047
		6,674	**2,462**	**9,136**

ii Stock of liquidity

For the purposes of the cash flow statement, cash and cash equivalents comprise cash in hand and amounts due from banks within three months from the date of acquisition. This definition, which is required by IAS 7 (Cash Flow Statements), covers the Bank's stock of liquidity for operational purposes, but is not well suited to the Bank which as the central bank is the ultimate source of sterling liquidity. These include advances to the money market and banks, and reverse repurchase agreements which are regarded as a pool of assets for these purposes. The allocation of this liquidity between the components depends upon prevailing market conditions.

29 Financial risk management

The Bank is required to manage the financial risks that arise on its balance sheet and as a consequence of its operations to deliver its policy objectives. These include credit risk, market risk and liquidity risk.

The Bank's management seek to ensure that effective risk management processes exist for assessing, managing and monitoring risk, within clear risk policies. There are governance arrangements set out in a Balance Sheet Remit and financial risk standards approved by the Governor, and documented delegated authorities for implementation of financial risk management and oversight of the Bank's operations.

The Bank applies fundamentally the same risk management policies for off balance sheet risks as it does for its on balance sheet risks. In the case of commitments to lend, customers and counterparties will be subject to the same credit management policies as for loans and advances.

Specialist teams and committees support senior management in ensuring that agreed standards and policies are followed.

The Financial Risk Management Division (FRMD) within the Bank's Markets Directorate is responsible for analysing the financial risks faced by the Bank in its operations in financial markets.

The Financial Risk and Resilience Division (FRRD) is responsible for providing forward-looking assessment and challenge of financial risks to the Bank's balance sheet across all its financial operations.

Middle Office is responsible for the pricing, valuation and financial control of exposures and collateral positions arising from the Bank's market operations, including counterparty and instrument management.

This section reflects practice in the 2016/17 financial year. A new financial risk management framework is being developed, consistent with the financial risk component of the Risk Tolerance Statement described in the Risk management and business practices section (pages 44–48).

The Bank makes extensive use of stress tests to assess financial risk across its balance sheet. These stress tests are designed by FRRD to test the Bank's ability to withstand extreme but plausible scenarios, and cover credit, market and liquidity risks.

Key risk features captured by the stress tests include (but may not be limited to):

- Potential expansion of the Bank's balance sheet in a stress eg through additional liquidity provision.
- Rating migration and potential default of counterparties.
- Shocks on asset prices, both where the Bank has positions on its balance sheet, and where these assets are held as collateral.

The stress tests are calibrated such that they are suitably severe — at least as severe as the banking system stress test, given the Bank's role as lender of last resort. For credit risk, the Bank uses a Stressed Exposure at Default (EAD) metric to measure the potential financial loss that could be incurred in the event of counterparty default, net of collateral held, where that collateral is also stressed. For market risk, the Bank uses a Stressed Loss metric to measure the potential mark-to-market losses from shocks to asset prices.

The stress tests used by the Bank are adjusted periodically and reviewed by internal committees, to continue to capture key risk drivers of the balance sheet and current market conditions, as well as potential future risks that could arise due to changing economic outlooks.

Notes to the Banking Department financial statements continued

29 Financial risk management continued

a Credit risk

Credit risk is the risk of loss arising from the failure of a borrower, issuer, counterparty or customer to meet its financial obligations to the Bank. The Bank is exposed to credit risk both through direct exposures and contingent exposures, such as via collateral or insurance contracts. The primary source of credit risk arises as a result of the Bank providing liquidity to financial institutions via the Funding for Lending Scheme and Sterling Monetary Framework; intraday in the Bank's provision of liquidity to facilitate the operation of the sterling high-value payment system (CHAPS) and the securities settlement system, CREST; and elsewhere in the Bank's management of its balance sheet, for example in the investment of the Bank's own funds and in the course of the banking services it provides to its customers. In addition, the Bank incurs credit risk in connection with any support operations it may undertake.

The Bank's balance sheet remit and risk standard define high-level risk parameters under which credit risk is monitored and controlled. Unsecured credit exposures are controlled by a system of limits based on internal credit ratings. This system applies to all unsecured credit exposures, including intraday exposures, foreign exchange settlement exposures and exposures arising from settling securities trades for customers. Separately, limits exist to control the maximum outright (uncollateralised) exposures to a single entity. Credit assessments are performed on all market counterparties, issuers and customers to which the Bank may be exposed. These are performed both regularly, following a timetable that reflects the risk of the actual or potential exposure, and dynamically, in response to market or specific entity conditions.

Internal committees, chaired by the Head of FRMD, review the creditworthiness of issuers, counterparties and customers to whom the Bank may have credit exposures. These committees are supported by a credit risk analysis team. Counterparty ratings are signed off by the Head of FRRD.

The Bank provides wholesale banking services to the UK Government, other central banks, and, where there are financial stability reasons to do so, certain other financial sector firms. The Bank may incur credit exposures to its customers in the course of providing such services. The reinvestment of customer deposits via secured on-placements may also give rise to credit exposures.

Credit risk on the securities held outright by the Bank is managed by holding only securities internally rated as equivalent to investment-grade in routine circumstances, which are issued chiefly by governments, government agencies and supranational organisations; and by a schedule of credit limits that vary based on internal rating.

Collateral management

In providing short-term liquidity via the Bank's Sterling Monetary Framework operations and, intra-day, via the Bank's operation of wholesale payment systems, credit risk is managed by ensuring that exposures are fully collateralised (with appropriate haircuts) by securities, which are issued chiefly by governments, government agencies and supranational organisations, which meet the Bank's minimum standards of liquidity and credit risk. A summary of eligible collateral can be found on the Bank's website.

In the Bank's Indexed Long-Term Repo Operations, Discount Window Facility, Contingent Term Repo Facility and Funding for Lending Scheme, the Bank accepts a wide range of private sector collateral. The collateral can include mortgage-backed securities, covered bonds backed by mortgages or public sector securities, other asset-backed securities (such as those backed by credit card receivables, student loans or auto loans), or portfolios of loans in unsecuritised form. The collateral must meet published eligibility criteria.

The Bank manages the risk in this wider collateral portfolio by applying haircuts to take account of market risk, liquidity risk, credit risk, and all other material risks to the realisable value of the collateral. Where appropriate the Bank undertakes stress testing of securities in order to ensure that haircuts are sufficient to protect against idiosyncratic risk in the underlying collateral pool and counterparty risk. The Bank may vary haircuts at its discretion, including on individual securities.

The Bank values securities daily and calls for additional collateral where the haircut-adjusted value is less than the value of its exposure. Where possible the Bank uses a market price to value securities; where a market price is not available the Bank uses a model to approximate a market value. The pricing methodologies and the use of spreads in models are under regular review, including via a Valuation Review Committee chaired by the Head of Middle Office.

A Collateral Risk Committee chaired by the Head of FRMD, reviews issues relating to the full range of collateral and considers policy issues relating to stress testing, valuation and eligibility of collateral including in response to market or entity-specific conditions. It also reviews eligibility of a counterparty to pledge portfolios of loans as collateral, based on an assessment of the firm's risk management policies, and also reviews eligibility of individual portfolios.

Models used for calculating haircuts are designed by FRMD, then independently reviewed and validated by FRRD.

In non-routine circumstances, the Bank may seek other methods of mitigating credit risk, which may include indemnities from HM Treasury.

Geographical concentration of assets and liabilities

The Bank undertakes its operations in the United Kingdom. It does, however, accept deposits from overseas central banks. An analysis of the Bank's assets and liabilities by geographical area is given below:

	2017 £m	2016 £m
Assets		
United Kingdom	498,928	392,591
Rest of Europe	12,114	10,463
Rest of the world	6,637	2,704
	517,679	**405,758**
Liabilities and equity		
United Kingdom	496,582	382,663
Rest of Europe	6,212	7,952
Rest of the world	14,885	15,143
	517,679	**405,758**

b Market risk

Market risk is defined as the risk of losses arising from movements in market prices. The risks which give rise to market risk include but are not limited to: interest rate risk and foreign exchange risk. The Bank is exposed to market risk as a consequence of its operations to deliver its policy objectives and, in the course of managing the Bank's balance sheet, principally through changes in the relative interest rates received on its assets and paid on its liabilities. Limited exposure may also be incurred due to changes in exchange rates (see below) and to changes in the liquidity of asset markets.

The Bank has a low risk tolerance to market risk. The Bank's balance sheet remit and risk standard sets out risk management parameters, governance and control frameworks as well as reporting arrangements for key risk indicators.

Interest rate risk

The Bank is exposed to interest rate risk through the investment of the Bank's capital and Cash Ratio Deposits in high-quality securities in the sterling bond portfolio. These are bought and, in normal circumstances held to maturity, with the intention of maintaining the value of the Bank's capital and generating income to pay for the Bank's policy functions. A 1% change in market prices would change the value of the sterling bond portfolio at 28 February 2017 by approximately £72m (2016: £67m).

Notes to the Banking Department financial statements continued

29 Financial risk management continued

Value at Risk measurement

The Bank measures the Value at Risk (VaR) of all its positions. VaR estimates the potential loss that might arise if existing positions were unchanged for ten working days under normal market conditions, given the historical volatility of the returns on different assets, and the historical correlation between those returns.

VaR on the Bank's balance sheet is calculated against the risk factors to which the Bank is exposed. During the year VaR arose mostly from market risk on the Bank's sterling bond portfolio.

Value at Risk

	2017 £m	2016 £m
At 28 February	148.3	126.7
Average	137.5	115.2

Although VaR is an important tool for measuring market risk, the assumptions on which the model is based do give rise to some limitations, including the following:

- A 99% confidence level does not reflect losses that may occur beyond this level. Even within the model used there is a 1% probability that losses could exceed the VaR.
- A ten-day holding period assumes that it is possible to hedge or dispose of positions within that period. This may not be realistic in a situation where there is severe market illiquidity.
- VaR data are calculated on data from the end of the previous day and do not reflect exposures that may arise on positions during the day.
- The model uses two years of historical data as a basis for determining the possible ranges of outcomes and may not always cover all possible scenarios, especially those of an exceptional nature.
- An assumption of log-normality, which may underestimate the size of extreme movement in market data.

The Bank back-tests its VaR by comparing actual profit or loss to the VaR estimation. The results of the back-testing process are one of the methods by which the Bank monitors the ongoing suitability of its VaR model.

To mitigate the fourth limitation above, the Bank has developed two additional variations of VaR: an exponentially weighted measure that gives greater weight to the most recent data and also a 'Stressed' VaR measure. The latter is calibrated not specifically on recent data, but on data drawn from the two-year period of maximum volatility since January 2000. Stressed VaR helps to mitigate the understatement problem as changes generally arise from a change in the underlying portfolio, rather than a short-run change in market volatility. The Bank introduced the Stressed VaR in June 2013; at 28 February 2017, Stressed VaR was £210m (2016: £183m).

c Liquidity risk

Liquidity risk is the risk of encountering difficulty in meeting obligations associated with financial liabilities that are settled by delivering cash or another financial asset.

In sterling, liquidity risk does not arise as the Bank is able to create sterling liquidity through its market operations.

For foreign currency, in addition to holding appropriate cash balances, the Bank manages liquidity through cash-flow matching and the use of forward exchange contracts and currency swaps; the Bank also holds a portfolio of liquid foreign exchange reserves.

The Bank's Balance Sheet Remit and Liquidity Risk standard and supporting policies set out risk tolerances and detailed parameters and controls to minimise the foreign currency liquidity risk that arises. These include limits over cash flow and maturity mismatches, and for bond holdings, minimum issue size and concentrations limits are set as well as reporting requirements for key risk indicators.

The following tables analyse the Bank's foreign currency financial assets and liabilities at the balance sheet dates into relevant maturity groupings based on the remaining period to the contractual maturity date. These cash flows have not been discounted.

Foreign currency liquidity risk

As at 28 February 2017	Up to 1 month £m	1–3 months £m	3–12 months £m	1–5 years £m	Over 5 years £m	Total £m
Assets						
Cash and balances with other central banks	1,641	–	–	–	–	1,641
Loans and advances to banks and other financial institutions	3,779	2,853	807	–	–	7,439
Securities held at fair value through profit and loss	1,254	1,926	1,921	4,048	–	9,149
Derivative financial instruments:						
Cash inflow	3,745	3,202	905	2,200	–	10,052
Cash outflow	(3,533)	(3,194)	(867)	(2,086)	–	(9,680)
Other assets	1,766	–	–	–	–	1,766
Total assets	**8,652**	**4,787**	**2,766**	**4,162**	–	**20,367**
Liabilities						
Deposits from central banks	5,239	4,035	1,390	–	–	10,664
Deposits from banks and other financial institutions	–	–	–	–	–	–
Other deposits	305	–	–	–	–	305
Foreign currency bonds in issue	1,635	–	34	4,934	–	6,603
Derivative financial instruments:						
Cash inflow	(3,526)	(736)	(557)	(1,125)	–	(5,944)
Cash outflow	3,480	1,226	1,146	1,124	–	6,976
Other liabilities	1,763	–	–	–	–	1,763
Total liabilities	**8,896**	**4,525**	**2,013**	**4,933**	–	**20,367**
Net liquidity gap	**(244)**	**262**	**753**	**(771)**	–	–
Cumulative gap	**(244)**	**18**	**771**	–	–	–

Notes to the Banking Department financial statements continued

29 Financial risk management continued

As at 29 February 2016	Up to 1 month £m	1–3 months £m	3–12 months £m	1–5 years £m	Over 5 years £m	Total £m
Assets						
Cash and balances with other central banks	637	–	–	–	–	637
Loans and advances to banks and other financial institutions	4,913	2,688	2,921	–	–	10,522
Securities held at fair value through profit and loss	1,298	1,037	2,422	2,429	–	7,186
Derivative financial instruments:						
Cash inflow	4,475	2,242	1,110	1,340	–	9,167
Cash outflow	(4,158)	(2,209)	(1,086)	(1,175)	–	(8,628)
Other assets	–	–	–	–	–	–
Total assets	**7,165**	**3,758**	**5,367**	**2,594**	–	**18,884**
Liabilities						
Deposits from central banks	4,113	2,384	1,231	–	–	7,728
Deposits from banks and other financial institutions	69	–	–	–	–	69
Other deposits	529	–	–	–	–	529
Foreign currency bonds in issue	1,454	–	15	2,904	–	4,373
Derivative financial instruments:						
Cash inflow	(1,310)	(144)	(5)	(551)	–	(2,010)
Cash outflow	2,580	1,230	3,843	535	–	8,188
Other liabilities	–	–	–	–	–	–
Total liabilities	**7,435**	**3,470**	**5,084**	**2,888**	–	**18,877**
Net liquidity gap	**(270)**	**288**	**283**	**(294)**	–	**7**
Cumulative gap	**(270)**	**18**	**301**	**7**	**7**	–

d Fair value of financial assets and liabilities

The table below shows the financial instruments carried at fair value by valuation method:

As at 28 February 2017	Note	Level 1 £m	Level 2 £m	Level 3[1] £m	Total £m
Assets					
Loans and advances to banks and other financial institutions	10	–	7,440	–	7,440
Securities held at fair value through profit or loss	12	9,157	–	–	9,157
Derivative financial instruments	13	–	308	–	308
Available for sale securities	14	7,156	–	1,246	8,402
		16,313	**7,748**	**1,246**	**25,307**
Liabilities					
Deposits from central banks	21	–	11,381	–	11,381
Foreign currency bonds in issue	24	6,450	–	–	6,450
Derivative financial instruments	13	–	108	–	108
		6,550	**11,489**	**–**	**17,939**

As at 29 February 2016	Note	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Assets					
Loans and advances to banks and other financial institutions	10	–	10,525	–	10,525
Securities held at fair value through profit or loss	12	7,190	–	–	7,190
Derivative financial instruments	13	–	488	–	488
Available for sale securities	14	6,833	–	1,111	7,944
		14,023	**11,013**	**1,111**	**26,147**
Liabilities					
Deposits from central banks	21	–	13,858	–	13,858
Foreign currency bonds in issue	24	4,333	–	–	4,333
Derivative financial instruments	13	–	476	–	476
		4,333	**14,334**	**–**	**18,667**

1 Level 3 assets comprise entirely of unlisted equity investments, movements are disclosed in note 14.

Notes to the Banking Department financial statements continued

29 Financial risk management continued

There have been no transfers between levels in the year.

Level 1 Valued using unadjusted quoted prices in active markets for identical financial instruments.
Level 2 Valued using techniques that rely upon relevant observable market data curves. This category of instruments comprised derivatives, repurchase transactions, commercial paper and deposits.
Level 3 Valued using techniques where at least one input that could have a significant impact on the valuation is not based on observable market data. During the year this category consisted primarily of the Bank's investment in the Bank for International Settlements (note 14b).

The fair values of financial assets and liabilities classified as loans and receivables and deposits at amortised cost approximate to their carrying values due to their short-term nature, all these financial assets and liabilities would be classified as Level 2.

30 Off balance sheet arrangements — Funding for Lending Scheme

The Funding for Lending Scheme (FLS) is designed to incentivise banks and building societies to boost their lending to the UK real economy.

It does this by providing funding for an extended period, with both the price and quantity of funding provided linked to their lending performance.

				2017		2016	
	Up to 1 year £m	1 to 3 years £m	3 to 5 years £m	Nominal £m	Fair value £m	Nominal £m	Fair value £m
Securities lent to banks and other financial institutions	14,652	31,639	5,879	52,170	52,110	57,645	57,540
Securities borrowed from the DMO	(14,652)	(31,639)	(5,879)	(52,170)	(52,110)	(57,645)	(57,540)
Total obligations	–	–	–	–	–	–	–

As of the end of February 2017 there were 41 banking groups signed up to the latest part of the FLS extension, and a further 15 groups had signed up to earlier parts of the scheme but were not participating in the extension. 43 groups had outstanding drawings as at the end of February 2017 (2016: 41 groups). Treasury bills with a market value of £52.1bn had been lent to the participants at year-end (2016: £57.5bn). The Bank has borrowed these Treasury bills from the DMO to whom they are owed back. In the year to 28 February 2017, the Bank recognised income of £146m from FLS (2016: £160m).

31 Contingent liabilities and commitments

a Contingent liabilities

Contingent liabilities and commitments, some of which are offset by corresponding obligations of third parties, arise in the normal course of business, including contingent liabilities in respect of guarantees and indemnities in connection with liquidity support operations. As part of its normal business, the Bank acts as custodian of its customers' assets and fulfils an agency role. No significant irrecoverable liability arises from these transactions.

The Bank has been required to subscribe to the share capital of the European Central Bank (ECB) since its establishment in 1998. Subscriptions depend on shares which are fixed in accordance with Article 29.3 of the European System of Central Banks (ESCB) Statute and which must be adjusted every five years and on the accession of new states to the European Union. The next quinquennial adjustment is due in 2019.

As a result of the Bank's shareholding and in accordance with the Treaty on the Functioning of the European Union, the Bank is required to pay a 'minimal percentage' of its subscribed share capital, currently 3.75% amounting to €56m (2016: 3.75% amounting to €56m) by way of contribution to the operational costs of the ECB. The value of this contribution will be adjusted in line with amendments to our subscription to the ECB as detailed above. In addition, the 'minimal percentage' can be varied by the General Council of the ECB, as detailed above. The Bank has not been notified of any intentions to change the 'minimal percentage'.

Overview
Court, and the Bank's policy committees
Our organisation
Review of 2016/17
Financial Stability Strategy
Financial review 2016/17
Risk management and business practices
Corporate social responsibility
Report of the Remuneration Committee
Report on Oversight Functions
Report of the Audit and Risk Committee
Statement of the responsibilities of the Court of Directors in relation to the financial statements
Financial statements
Contacting the Bank of England

b Capital commitments

Capital commitments outstanding at 28 February 2017 amounted to £11m (2016: £30m), relating primarily to machinery purchases.

In addition the Bank did not have any contingent capital commitments outstanding at 28 February 2017 (2016: nil).

c Operating lease commitments — minimum lease payments

	2017		2016	
	Land and buildings £000	Computer and other equipment £000	Land and buildings £000	Computer and other equipment £000
At the year end, minimum lease payments under non-cancellable operating leases were:				
Expiring within one year	7,794	153	7,768	141
Between one and five years	23,440	151	26,275	206
Expiring in five years or more	29,166	–	34,169	–
	60,400	**304**	**68,212**	**347**

The Bank leases the premises occupied by its Agencies and the PRA.

32 Related parties

Transactions with those commercial banks which are related parties but not wholly-owned by HM Treasury have not been disclosed as the Bank does not believe such disclosures to be appropriate having regard to its financial stability objective.

a HM Government

The Bank provides a range of activities to its shareholder, HM Treasury, and to other Government departments and bodies:

- Provision of banking services, including holding the principal accounts of Government.
- Management of the Exchange Equalisation Account (EEA).
- Management of the note issue.

The Bank also engaged in transactions with the Financial Services Compensation Scheme and other related parties.

The aggregate balances on HM Treasury and other public sector accounts are disclosed in note 23 as public deposits. The total charges made to the Government are disclosed in note 4a. A management fee of £112m (2016: £92m) was payable by HM Government in the year ended 28 February 2017 to the Bank in respect of services provided to the EEA of £5m (2016: £8m), Issue Department of £105m (2016: £83m), and for banking services to HM Government of £2m (2016: £1m).

Notes to the Banking Department financial statements continued

32 Related parties continued

Debt Management Office and Debt Management Account

The Bank has entered into agreements with the UK Debt Management Office (DMO) through the Debt Management Account (DMA) whereby the DMA lends UK government securities to the Bank with the simultaneous agreement that the Bank would deliver equivalent securities to the DMA on termination of those agreements.

At 28 February 2017 the Bank had a loan from the DMA of £193m (2016: £193m) in relation to the provision of funding to the Bank of England Asset Purchase Facility Fund Ltd.

At 28 February 2017 the Bank had borrowed Treasury bills with a nominal value of £52.2bn (2016: £57.6bn) under the Bank's Funding for Lending Scheme. The Bank has paid the DMA a loan fee for the Treasury bills borrowed.

In addition, the DMA placed interest-bearing deposits with the Bank during the year, which is included within note 23 as public deposits.

The interest paid in respect of DMO deposits was £5m in 2017 (2016: £5m).

HM Treasury

HM Treasury continued to indemnify the activities of the Bank of England Asset Purchase Facility Fund Ltd during the year.

The Bank, in discussion with HM Treasury, expects to recover the sum of £2.9m in respect of expenses incurred by the Bank in connection with the resolution of Dunfermline Building Society in accordance with the Financial Services and Markets Act 2000 (Contribution to Costs of Special Resolution Regime) Regulations 2010.

Financial Services Compensation Scheme

The Financial Services Compensation Scheme (FSCS) is the United Kingdom's statutory fund of last resort for customers of authorised financial services firms set up under the Financial Services and Markets Act 2000 (FSMA). The FSCS is independent from the Prudential Regulation Authority and Financial Conduct Authority, although accountable to them and ultimately to HM Treasury.

The FSCS placed interest-bearing deposits with the Bank during the year, which are included within note 23 as public deposits.

b Subsidiaries

Full details of the subsidiaries of the Bank are disclosed in note 15.

Bank of England Asset Purchase Facility Fund Ltd (BEAPFF)

BEAPFF is a wholly-owned subsidiary of the Bank. It was established on 30 January 2009 in order to fulfil the remit of the Chancellor of the Exchequer given to the Bank on 19 January 2009. This remit was subsequently expanded to enable the asset purchase facility operated by the company to be used as a monetary policy tool at the request of the Monetary Policy Committee.

BEAPFF's operations are fully indemnified for loss by HM Treasury and any surplus for these operations is due to HM Treasury.

Purchases of assets and lending through the Term Funding Scheme by BEAPFF are financed via a loan from the Bank. From 6 March 2009 to 4 February 2010 and from 7 October 2011 advances on this loan were financed by the issuance of central bank reserves. Prior to 6 March 2009 and from 4 February 2010 to 6 October 2011 advances on this loan were financed by a loan from the DMO.

At 28 February 2017 the loan from the Bank to BEAPFF was £485.2bn (2016: £375.2bn). Interest on this loan is receivable at Bank Rate and amounted to £1.4bn for the year ending 28 February 2017 (2016: £1.9bn).

At the year end BEAPFF held a deposit at the Bank of £6.2bn (2016: £1.3bn), which is included in other deposits (note 23). Interest on this deposit is payable at Bank Rate and totalled £14m for the year ending 28 February 2017 (2016: £18m).

A management fee of £4m was payable by BEAPFF to the Bank in respect of the year ended 28 February 2017 (2016: £2m).

Prudential Regulation Authority (PRA)

The PRA is a wholly-owned subsidiary of the Bank. The company was established on 21 November 2011 and began to operate when the new regulatory framework for the United Kingdom's financial sector came into effect on 1 April 2013. Following enactment of the Bank of England and Financial Services Act 2016 on 1 March 2017 the regulatory activity, along with the assets and liabilities, of the PRA transferred to the Bank.

The Bank initially pays all of the expenses of the PRA. The Bank then recharges relevant expenditure either via the corporate services fee or a direct recharge. In the year the Bank charged the PRA a corporate services fee of £98m (2016: £97m) and recharged direct costs of £151m (2016: £156m).

As at 28 February 2017 the Bank was owed £22m (2016: £26m) by the PRA in respect of recharged expenditure and corporate services fee, this amount is included in note 20.

The PRA Board had previously agreed that the costs of the transition will be recovered from the fee-payers over a period of five years. As a result the PRA has a liability to the Bank and the Bank has a receivable from the PRA as at the year end of £15m (2016: £29.5m), which is disclosed as a receivable within note 20.

c Key management personnel

Members of Court are covered by an indemnity from the Bank, granted in 2000 (see page 9). Members of the FPC, MPC and PRC are also covered by an indemnity granted by the Bank (see pages 12–15).

The following information is presented only in respect of those employees of the Bank who would be considered as key management personnel, as defined under IAS 24 (Related Party Disclosures). This comprised the Governors, members of the Executive Team and Non-executive Directors. At 28 February 2017, the number of key management personnel was 29 (2016: 29).

The following particulars relate to loans and deposits between the Bank and key management personnel and persons connected with them:

	2017 £000	2016 £000
Loans		
Balance brought forward	26	55
Loans made during year	32	2
Loans repaid during year	(19)	(31)
	39	**26**
Interest income earned	1	1
Number of key management personnel with loans at 28 February	3	3

No provisions have been recognised in respect of loans given to related parties (2016: £nil).

There were no other transactions that would be required to be shown under the provisions of the Companies Act 2006. None of the key management personnel had a material interest, directly or indirectly, at any time during the year in any other significant transaction or arrangement with the Bank or any of its subsidiaries.

All employees, excluding external MPC members, are entitled to season ticket loans (repayable monthly over five to twelve months) and may choose to take personal loans (for periods of up to five years and at a variable interest rate equal to HMRC's Official Rate of Interest currently 3%) as part of their remuneration package.

Notes to the Banking Department financial statements continued

32 Related parties continued

Staff, including Governors and Executive Directors, holding current and interest-bearing deposit accounts at the Bank of England receive interest at commercial rates.

	2017 £000	2016 £000
Deposits		
Governors and Executive Directors		
Balance brought forward	193	271
Deposits taken during year	326	426
Deposits repaid during year	(519)	(504)
	–	**193**
Interest expense on above deposits	–	1
Number of key management personnel with deposits at 28 February	–	4

Key management remuneration

	2017 £000	2016 £000
Salaries and short-term benefits	6,119	6,017
Post-employment benefits	1,856	2,031
	7,975	**8,048**

Post-employment benefits have been estimated using an expected cost of pension on a funding valuation basis.

Full information on the remuneration (including pension arrangements) of the Members of Court is given in the Report of the Remuneration Committee on pages 63 to 69.

d The Bank's pension scheme

The Bank provides the secretariat, accounting services and some banking and custodial services to the Bank's funded pension scheme. In the year to 28 February 2017 no charge was made for these services (2016: £nil). These activities are undertaken on behalf of, and under the supervision of, the Trustee of the Pension Fund. The contribution paid to the scheme during the year was £68m (2016: £90m). There were no other material transactions between the Bank and the pension scheme during the year to 28 February 2017. At 28 February 2017 the balances on accounts held with the Bank were £12m (2016: £31m).

e Other entities with links to the Bank

In the normal course of its activities as a central bank, the Bank has relationships, involving some representation at management level and participation in funding, with international and domestic institutions. The Bank does not consider these institutions to be related parties.

33 Post balance sheet events

On 1 March 2017 the Bank of England and Financial Services Act 2016 (Commencement No. 4 and Saving Provision) Regulations 2016 came into force, at which point the prudential regulatory activities of the Prudential Regulation Authority, along with its assets and liabilities, transferred to the Bank.

The assets transferring comprised cash, trade and other receivables and intangible assets totalling £73.5m. Liabilities comprised amounts due to fee payers, fine penalties payable to HM Treasury and amounts due to the Bank totalling £73.5m.

The assets and liabilities transferred at the carrying value at the point of transfer for a net consideration of nil. This is deemed appropriate as the regulatory activity of the PRA continues within the Bank, and as such the Bank inherits the assets and liabilities to perform these functions in the future.

The amounts due to the Bank from the PRA were settled on transfer, with the remaining items recognised on the Bank's balance sheet from 1 March 2017.

34 Date of approval

The Members of Court approved the financial statements on pages 82 to 135 on 26 June 2017.

Issue Department account
for the period ended 28 February 2017

	2017 £m	2016 £m
Income and profits		
Securities of, or guaranteed by, the British Government	281	243
Other securities and assets	257	299
	538	**542**
Expenses		
Cost of production of banknotes	(66)	(43)
Cost of issue, custody and payment of banknotes	(29)	(27)
Other expenses	(11)	(10)
	(106)	**(80)**
Net income paid to National Loans Fund	**432**	**462**

Issue Department statement of balances
for the period ended 28 February 2017

	Note	2017 £m	2016 £m
Assets			
Securities of, or guaranteed by, the British Government	3	3,194	3,604
Other securities and assets including those acquired under reverse repurchase agreements	4	70,004	64,214
Total assets		**73,198**	**67,818**
Liabilities			
Notes issued:			
In circulation	5	73,198	67,818
Total liabilities		**73,198**	**67,818**

On behalf of the Governor and Company of the Bank of England:

Mr M Carney	Governor
Mr B Broadbent	Deputy Governor
Mr A Habgood	Chair of Court
Mr R Pereira	Finance Director

The notes on pages 138 to 140 are an integral part of these statements of accounts.

Notes to the Issue Department statements of account

1 Bases of preparation

The statements of account are prepared in accordance with the requirements of the Currency and Bank Notes Acts 1928 and 1954, the National Loans Act 1968 and the Currency Act 1983. All profits of the Issue Department are payable to the National Loans Fund.

- The statements of account are prepared on the basis of amounts received and paid as modified by the effects of a revaluation of securities.
- All securities are revalued quarterly at their clean mid-market price and are stated, with purchased accrued interest, in the balance sheet at this valuation. The last valuation was made as at 27 February 2017.
- If a revaluation of securities shows a net gain this is included in income. A deficit is not taken against income but is settled by a transfer from the National Loans Fund. Total gains taken to income in the year to 28 February 2017 amounted to £137m (2016: £47m) and total deficits paid by the National Loans Fund amounted to £171m (2016: £104m).
- Notes in circulation exclude those old series notes which have been written off. The value of the note is still given by the Bank on presentation. The Bank is reimbursed by HM Treasury in these instances.

2 Expenses

The expenses of £106m (2016: £80m) represent charges from the Banking Department for costs incurred in relation to the note issue of £105m (2016: £83m) plus amounts under-collected in prior years.

3 Securities of, or guaranteed by, the British Government

	2017 £m	2016 £m
British Government Stocks	2,824	3,234
Ways and Means advance to the National Loans Fund	370	370
	3,194	**3,604**

The Ways and Means advance earns interest at Bank Rate.

4 Other securities and assets including those acquired under reverse repurchase agreements

	2017 £m	2016 £m
Deposit with Banking Department	63,049	50,870
Reverse repurchase agreements	6,955	13,344
	70,004	**64,214**

The deposit with Banking Department earns interest at Bank Rate.

5 Notes in circulation

	2017 £m	2016 £m
£5	1,912	1,645
£10	8,006	7,767
£20	43,357	41,037
£50	15,601	13,157
Other notes[1]	4,322	4,212
	73,198	**67,818**

1 Includes higher-value notes used as backing for the note issues of banks in Scotland and Northern Ireland.

6 Assets and liabilities

a Interest rate exposure

As the liabilities of the Issue Department are interest free, the income of the Issue Department is directly exposed to movements in interest rates. As at the year end 28 February 2017, the assets of the Issue Department had the following repricing period profile.

	2017 £m	2016 £m
Repricing up to one month	70,374	64,584
Repricing in greater than one month but less than three months	–	–
Repricing in greater than three months but less than six months	201	–
Repricing in greater than six months but less than twelve months	–	383
Repricing in greater than twelve months	2,623	2,851
	73,198	**67,818**

b Currency exposure

All the assets and liabilities of the Issue Department are denominated in sterling. The collateral provided under reverse repurchase agreements may be in currencies other than sterling but this does not give rise to any direct currency exposure.

c Credit risk

Credit risk is the risk of loss arising from the failure of a borrower, issuer, counterparty or customer to meet its financial obligations to the Bank. The Bank is exposed to credit risk both through direct exposures and through contingent exposures, such as custody arrangements and holdings of collateral. Credit risk arises in the course of the operations of the Note Circulation Scheme, Agency Notes Store and Notes Printing Contract; and as a result of the Bank providing liquidity to financial institutions via open market operations.

In providing liquidity via routine open market operations credit risk is managed by ensuring that exposures are fully collateralised (with appropriate margin) by internally rated as equivalent to investment-grade securities.

Credit risk on the securities held by the Bank is managed by holding only internally rated as equivalent to investment-grade securities in routine circumstances, issued chiefly by governments and central banks.

Notes to the Issue Department statements of account continued

7 Accrued interest

At 28 February 2017 the unrecognised accrued interest on the assets held on the Issue Department statement of balances was £42m (2016: £63m).

8 Date of approval

The Members of Court approved the statements of account on pages 136 to 140 on 26 June 2017.

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BANK OF ENGLAND

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