Monitor
Independent Regulator
of NHS Foundation Trusts

Managing Operating Cash in NHS Foundation Trusts

Contents

Managing Operating Cash in NHS Foundation Trusts

Introduction

Following consultation, Monitor issues this advice on managing operating cash as best practice advice rather than mandatory guidance. Given that this advice reflects prudent practice, we recommend that NHS foundation trusts take account of it, in conjunction with independent professional advice where appropriate.

Under Section 17 of the Health and Social Care (Community Health and Standards) Act 2003 ("the Act"), NHS foundation trusts have wide discretion to invest money (other than money held by them as a trustee) for the purposes of, or in connection with, their functions. While this freedom offers greater opportunity to improve patient care, it should be managed carefully to avoid financial and/or reputational risks.

Treasury management generally refers to the set of policies, strategies and transactions that a company adopts and implements to manage its cash resources, to raise finance at acceptable cost and risk, and to reduce interest rate, foreign exchange and commodity price risks, as well as in the conduct of its relationships with its financial stakeholders (mainly banks).

This advice focuses on investment of surplus operating cash likely to be needed within 12 months to support ongoing operations. These investments need to be safe and liquid, so that the risk to invested capital is minimised and the investments can be realised quickly. This document describes guidelines that are intended to ensure adequate safety (i.e. manageable risk profile) and liquidity (i.e. accessibility of funds at short notice), of such investments, while generating a competitive return.

Monitor is aware that the investment of surplus operating cash in short-term deposits and liquid vehicles is a new endeavour for NHS foundation trusts. Experience has shown that when an industry initially acquires freedom to invest, industry players encounter common pitfalls. This advice, drawn from examples of treasury management policies for profit-making and non-profit entities in the UK and elsewhere, is aimed at NHS foundation trust boards to help them mitigate risks arising from cash management activities, while allowing them to seek competitive returns.

While this advice should lessen the possibility of imprudent or inappropriate cash management activities, compliance with it should not be construed as any kind of guarantee of the performance of investments or of the success of treasury management activities in general. **Monitor assumes no responsibility for investment risk**. NHS foundation trusts are encouraged to educate and inform themselves of the detailed processes and the risks and returns associated with managing their operating cash.

Objectives

NHS foundation trusts are public benefit corporations, with the principal role of providing healthcare services for the NHS in England. As such, boards of NHS foundation trusts need to ensure that surplus operating cash is invested in accordance with their duty to safeguard and properly account for the use of public money. The chief executive of an NHS foundation trust is the accounting officer, with direct accountability to Parliament.

This advice aims to promote fiscal responsibility and prudent investments that do not compromise effective, efficient, and economic delivery of services.

Another important goal of this advice is to minimise potential reputational risks associated with investments. As public benefit corporations and healthcare providers, NHS foundation trusts occupy a special position in the public mind and are expected to maintain probity. This advice aims to promote investments that are in keeping with NHS foundation trusts' reputation as beneficial and service-driven organisations.

Operating cash management

The overall objectives of an NHS foundation trust in relation to operating cash management should be to:

- ensure a competitive return on surplus cash, within an acceptable risk profile;
- manage the financial risk associated with operational activities, for instance, interest rate and foreign currency risks; and
- ensure availability of competitively priced funding for working capital with an acceptable risk profile.

This advice focuses primarily on the first objective.

Monitor strongly encourages NHS foundation trusts to:

- invest surplus operating cash in ‘safe harbour’ investments (see Section A below); and
- have a written operating cash management policy (see Section B below).

A. Safe harbour investments

This section describes Monitor’s perspective on a ‘safe harbour’ for investment of surplus operating cash. Safe harbour means that NHS foundation trust boards do not need to undertake an individual investment review for these investments nor will Monitor require a report on them as part of its risk assessment process, since they are deemed to have sufficiently low risk and high liquidity.

The emphasis of this advice is to ensure adequate safety (i.e. manageable risk profile) and liquidity (i.e. accessibility of funds at short notice). Securities that are considered sufficiently safe and liquid to be in the safe harbour meet all of the following criteria (see page 5 for further elaboration):

- meet permitted rating requirement issued by a recognised rating agency;
- are held at a permitted institution;
- have a defined maximum maturity date;
- are denominated in sterling, with any payments or repayments for the investment payable in sterling;
- pay interest at a fixed, floating, or discount rate; and
- are within the preferred concentration limit.

These investments include (but are not limited to) money market deposits, money market funds, Government and local authority bonds and debt obligations, certificates of deposit, and sterling commercial paper, provided that they meet the criteria on page 5.

The following definitions elaborate on the criteria outlined on page 4:

Term	Advice
Recognised rating agency	Only the following are recognised rating agencies[1]: ■ Standard & Poor's; ■ Moody's Investors Service Ltd; and ■ FitchRatings.
Permitted rating requirement	The short-term rating should be at least: ■ A-1 Standard & Poor's rating; or ■ P-1 Moody's rating; or ■ F1 FitchRatings. The long-term rating should be at least: ■ A1 (Moody's); or ■ A+ (Standard & Poor's/FitchRatings).
Permitted institutions	Permitted institutions include: ■ institutions that have been granted permission, or any European institution that has been granted a passport, by the Financial Services Authority to do business with UK institutions provided it has an investment grade[2] credit rating of A1/A+ issued by a recognised rating agency; and ■ the UK Government, or an executive agency of the UK Government, that is legally and constitutionally part of any department of the UK Government, including the UK Debt Management Agency Deposit Facility.
Maximum maturity date	■ The maximum maturity date for all investments should be 3 months. ■ The maturity date for any investment should be before or on the date when the invested funds will be needed.
Preferred concentration limit	■ Surpluses below £500K may be invested with one institution. ■ Surpluses above £500K should be invested across a number of permitted institutions to spread the investment risk. ■ Investment limits should be set for permitted institutions based on their credit rating and net worth. These limits should be reviewed annually and reset if there is a change in either the credit rating or the net worth of the financial institution. If an institution is either downgraded or put on credit watch by a recognised rating agency, the decision to invest with them should be reviewed. ■ Investments with permitted institutions should not exceed the set limit at any time.

1 Moody's, Standard and Poor's and FitchRatings are the three top agencies that deal with credit ratings for the investment world

2 Ratings lie on a spectrum ranging from highest credit quality at one end to default or "junk" at the other. Long-term credit ratings are denoted with a letter. "Aaa" or "AAA" is the highest credit quality and "C" or "D" (depending on the agency issuing the rating) is the lowest or junk quality. For Moody's ratings between "Aaa" and "Baa" are investment grade ratings and for Standard and Poor's and Fitch Ratings the equivalent range is "AAA" to "BBB". Ratings that fall below "Baa" (Moody's) and "BBB" (S&P and FitchRatings) are considered to be non-investment grade

Investments that do not fulfil the criteria for safe harbour are higher risk instruments and include bonds, equities, commodities and products based on them, derivative products such as futures, options and swaps and contracts for differences, investments linked to other trade instruments, index-linked investments, private equity or venture capital investments, leveraged investments, hedge funds and foreign currency-linked investments.

For the purpose of calculating the liquidity ratio used in deriving the financial risk rating of NHS foundation trusts, investment of surplus operating cash in safe harbour investments will be treated as cash.

NHS foundation trusts do not need to report investments in safe harbour to Monitor under the *Compliance Framework* (published in March 2005, and available on Monitor's website[3]).

B. Elements of an operating cash management policy

In keeping with best practice, NHS foundation trusts are strongly encouraged to have a written, integrated policy covering all aspects of risk arising from treasury activities. An anonymous example of a private sector treasury management policy is included in Appendix 1. While recognising that private companies will often face a broader range of issues than NHS foundation trusts (e.g. more complex funding and borrowing arrangements and foreign exchange risk), this example may be helpful as a reference for NHS foundation trusts in developing their operating cash management policies.

The operating cash management policy should include a set of governance measures designed to ensure prudence and oversight of such activities, as illustrated below. It should be noted that this is illustrative only and NHS foundation trusts are strongly encouraged to seek external professional advice when developing their own policies.

An NHS foundation trust's operating cash management policy should normally cover:

- objectives;
- attitude to risk;
- organisation and responsibilities;
- bank relationships and cash management;
- reporting;
- performance management; and
- controls.

(i) Objectives

The operating cash management policy should state the NHS foundation trust's objectives in each of the principal areas, for instance, cash forecasting, investment of surplus cash and bank relationships. For example, the objective in relation to investing surplus cash is typically to obtain a competitive return within defined risk limits. The objective on bank relationships could be to maintain a strong set of core relationships with banks who may meet current and future banking and funding needs.

3 Monitor's website address is www.monitor-nhsft.gov.uk

(ii) Attitude to risk
The operating cash management policy should also state the NHS foundation trust's attitude to risk in each of these categories. For example, for investment of surplus cash, the risk profile of investments and institutions might be defined by the safe harbour provisions on page 4.

(iii) Organisation and responsibilities
It is strongly recommended that an investment committee be set up. Typically the functions of the investment committee will be to approve investment and borrowing strategy and policies, approve performance benchmarks, review performance against the benchmarks, ensure proper safeguards are in place for security of the NHS foundation trust's funds, monitor compliance with treasury policies and procedures, approve proposals for acquisition and disposal of assets above a de minimus amount and approve external funding arrangements within their delegated authority.

The investment committee should comprise executive and non-executive directors, with a majority of non-executive directors. It should be chaired by a non-executive director with relevant investment decision-making experience. It may therefore be a committee of the board, or the board itself in the case of smaller NHS foundation trusts.

The NHS foundation trust's operating cash management policy should describe the treasury organisation and responsibilities. This should include the different responsibilities of the main board, investment committee, finance director and the accounts/treasury functions. For example, the board of directors is typically responsible for approving all external credit and borrowing above a specified limit and for approving the overall treasury management policy, with detailed policy and oversight delegated to the investment committee. The latter in turn can delegate responsibility for treasury operations to the finance director (see section 3 of Appendix 1 for an example).

The operating cash management policy should be clear on the processes for achieving the desired objectives and risk profile, e.g. when to engage outside experts.

(iv) Bank relationships and cash management
The NHS foundation trust's operating cash management policy should identify the key banks with which it has core relationships and specify the services provided by each bank (e.g. deposit taking, working capital facilities, bank accounts and cash management). The NHS foundation trust may choose to have core relationships with a small number of banks and negotiate specific additional services from a larger group. The NHS foundation trust should also ensure that it monitors compliance with any bank covenants, for instance, on gearing and interest cover.

(v) Reporting

The NHS foundation trust's operating cash management policy should set out the daily, weekly and monthly treasury reports that will be produced and their circulation. It should also include examples of authorisation letters to banks for treasury transactions.

For example, the daily movement report might detail the opening and closing net cash position, the facilities available and the amount drawn down.

The weekly treasury report might provide details of cash deposits, facilities available, a summary of all borrowings, and the net cash and borrowings position.

The monthly treasury report might include this and add broader analysis, e.g. market movements, analysis of investments (performance, liquidity and security) and bank relationships. Further details are given in section 5 of Appendix 1.

(vi) Performance management

The NHS foundation trusts' operating cash management policies should include a rational and objective performance measurement structure that can be used by its investment committee and its board to monitor effectiveness of its policies. A market-based metric should be defined for tracking performance and the return on investments should be measured against this benchmark at regular intervals. An example of such a benchmark is the three-month London Interbank Bid Rate or Libid.

(vii) Controls

The operating cash management policy should define controls to ensure that treasury activities are undertaken in a controlled and properly reported manner. Key components include:

- clearly defined roles and responsibilities;
- regular reporting of treasury activities;
- segregation of duties between those who deal, those who initiate payment and those who account for treasury activities;
- strict investment limits on permitted institutions, types of investments and the circumstances in which they may be used; and
- controls on bank accounts in terms of mandates, signatories and sign-off limits.

C. Investments outside of safe harbour

Monitor does not expect NHS foundation trusts to invest surplus operating cash outside of the safe harbour. To the extent that NHS foundation trusts do so, it should only be for the management of operational risk (e.g. foreign exchange risk, interest rate risk) and never for speculative reasons. NHS foundation trusts should always define the risk management processes in place for use of such instruments. These processes should include scrutiny proportional to risk and the use of external expert advisers as appropriate.

In contrast to safe harbour investments, investments outside of this category will not be treated as cash for the purpose of calculating the liquidity ratio used in deriving the financial risk rating of NHS foundation trusts.

Monitor considers investment of surplus operating cash outside of safe harbour as an exception which should be reported under the exception reporting process described in the *Compliance Framework*. Monitor will accordingly assess the impact of such investments on the NHS foundation trust's financial risk rating. If an NHS foundation trust receives foreign currency income which it uses as a hedge against future costs in that currency, Monitor will use its discretion in deciding whether to treat the investment as cash for calculation of the liquidity ratio.

Monitor will issue additional advice on managing long-term investments not covered by this document.

Appendix 1: Sample treasury management policy for a multinational company

1. Treasury objectives

1.1 Introduction

In order to reflect the climate on corporate governance issues, it is both appropriate and necessary to formally set out current treasury activities and establish a treasury risk management environment in which all objectives, policies and operating parameters are clearly defined.

1.2 Scope of a treasury function

The objectives of a treasury function are to support the group's development by:

- ensuring the most competitive return on surplus cash balances, within an agreed risk profile;
- ensuring the availability of flexible competitively priced funding at all times;
- identifying and managing the financial risks, including interest rate and foreign currency risks, arising from operational activities; and
- ensuring compliance with all banking covenants.

The group's treasury activities will be undertaken in a manner that achieves the following key objectives:

Surplus cash: To obtain the most competitive deposit rates using a group of relationship banks, in line with deposit guidelines ratified by the investment committee.

Funding: Ensure the availability of flexible and competitively priced funding from alternative sources to meet the group's current and future requirements.

Interest rate management: Maintain an interest rate structure which smoothes out the impact of rises or falls in interest rates on profits.

Foreign currency management: Reduce the group's exchange rate movement risk by covering known foreign exchange exposures.

Bank relationships: Develop and maintain strong, long-term relationships with a core group of quality banks that can meet current and future funding requirements.

1.3 Treasury controls
The wide range of complex financial instruments available to companies can significantly reduce financial risk when used wisely. Equally, they can lead to financial distress, when used unwisely.

The treasury controls proposed in this document are designed to ensure the group's treasury activities are undertaken in a controlled and properly reported manner.

The key components of the overall treasury operating environment include the following:

- clearly defined roles and responsibilities in treasury activities for the main board, the investment committee, the finance director, the group treasury, group accounts, and operating subsidiaries. These are set out in section 3;
- regular reporting of treasury activities;
- controls on who can operate bank accounts and authorisation limits;
- segregation of duties between those who deal, those who initiate payment and those who account for treasury activities[4]; and
- strict limits on the types of derivatives and the circumstances in which they may be used by group treasury.

1.4 Conclusion
Treasury management is the efficient management of liquidity and financial risks in a business and the actions to manage these risks will vary as their nature changes over time.

This policy provides a clearly defined risk management framework for those responsible for treasury operations. In order to fully realise the benefits it is essential that the policy is kept up to date to reflect any changes in the group's operations.

4 Normally, all dealing is carried out by the group treasury manager who cannot sign either confirmations or payment instructions. It is recognised that within a small department, others may deal when that person is not available, subject to the normal mandate signature on any confirmations of such deals

2. Attitude to risk in key treasury activities

2.1 Funding

The principal role of the treasury function is to maintain liquidity, to mitigate and manage risk and to ensure a competitive return within an acceptable risk profile. For instance, surplus cash will be invested with counterparties that meet the credit criteria and in instruments that have an acceptable risk profile. Under no circumstances will the treasury function be authorised to enter into trading positions or to undertake trading for purely speculative reasons.

The key funding objective is to ensure the availability of flexible and competitively priced funding from alternative sources to meet the group's current and future requirements. The group will maintain a risk-averse approach to funding, recognising the ongoing requirement to have committed funds in place to cover existing business cash flows and to provide reasonable headroom for seasonal cash flow fluctuations, capital expenditure programmes and acquisition financing.

The group's approach to funding is that whilst it is beneficial to retain reasonable headroom in committed facilities, the group should not pre-finance in anticipation of potential future acquisitions.

2.2 Investments

All cash balances should remain in a comparatively liquid form and all investments resulting from them should be realisable and have a maturity not exceeding three months.

Cash deposits should only be placed with relationship banks, in line with deposit limits agreed by the investment committee and based on Moody's ratings.

The limits are as follows **[note: these are only examples and NHS foundation trusts should decide on the appropriate limits for their NHS foundation trust if adopting this approach]**:

1. Clearing banks have a limit of £15 million.

2. Banks rated Aaa have a limit of £10 million.

3. Banks rated Aa1 have a limit of £5 million.

4. Banks rated Aa2 and Aa3 have a limit of £3 million.

5. Banks rated A1 have a limit of £2 million.

6. Banks rated A2 and A3 have a limit of £1 million.

7. Banks rated below this have a NIL limit.

2.3 Foreign exchange management

Group policy is to cover forward all known transaction exposures, except for de minimus amounts, as soon as they are identified.

The group's approach to managing translation exposures is reviewed on a regular basis, taking into account taxation and accounting issues.

The group's balance sheet is hedged against foreign exchange fluctuations in the major currencies by borrowings in those currencies to match a proportion of the foreign currency denominated net assets.

2.4 Interest rate management

Should the group enter into any long-term borrowings, group treasury will maintain an interest rate structure which reduces the impact of rapidly increasing interest rates on profits. The group's policy is to hedge interest rate exposure using interest rate swaps.

2.5 Bank relationships

The group's approach is to develop long-term relationships with a core group of quality banks. A transactional approach, without the development of relationships, may result in the group being unable to rely on the support of banks in the event of a major acquisition or deterioration in financial strength of the group, or in times of a crisis in the banking market.

The benefit of relationship banks is to establish a high degree of confidence and commitment between the parties so that banks are prepared to meet funding requirements at crucial times and at short notice.

2.6 Banking covenant compliance

In situations where funding arrangements have financial covenants attached to them, a regular review of the group's performance against these covenants should be included in the monthly treasury report, so that potential problems can be identified at an early stage.

3. Summary of key responsibilities

The key responsibilities are as follows:

Main board

- Approve external funding arrangements (other than loan renewals/refinancing and new loans up to £5m). **[Note: this is only an example and NHS foundation trust boards should determine their own threshold if adopting this approach.]**
- Approve overall treasury policy.
- The main board delegates responsibility for approval of the group's treasury procedures, controls and detailed policies to the investment committee.

Investment committee

- Approve the group's investment and borrowing strategy and policies in line with its appetite for risk.
- Approve the group's interest rate and foreign exchange risk management strategy and policies.
- Approve the relevant benchmarks for measuring performance.
- Review and monitor investment and borrowing policy and performance against the relevant benchmarks in respect of all group funds.
- Ensure proper safeguards are in place for security of the group's funds by:
  - agreeing a list of permitted institutions;
  - setting investment limits for each permitted institution;
  - agreeing permitted investment types; and
  - ensuring approved bank mandates are in place for all accounts and they are updated regularly for any changes in signatories and authority levels.
- Monitor compliance with treasury policies and procedures on investment/borrowing/interest rate/foreign exchange management in respect of limits, approved counterparties and types of investments/instruments.
- Approve external funding arrangements within delegated authority.
- Delegate responsibility for treasury operations to the group finance director. The group finance director will hold regular meetings with the treasury team to discuss issues and consider any points that should be brought to the attention of the investment committee.

Group finance director	■ Approve subsidiary cash budgets and cash management systems.
Group treasury	■ Define the group's treasury approach for approval by the investment committee. ■ Ensure treasury activities are reported on a timely and accurate basis. ■ Manage key banking relationships. ■ Manage treasury activities within the agreed policies and procedures. ■ Co-ordinate treasury operations between the parent company and its operating subsidiaries
Group accounts	■ Accurate and timely recording in the accounting records of all treasury transactions, undertake bank reconciliations and match bank/counterparty confirmations with internal deal documentation.

The group's treasury procedures will be subject to periodic review by the external auditors as part of their audit undertakings and any significant deviations from agreed policies and procedures will be reported where appropriate to the main board.

4. Bank relationships and cash management

The development and maintenance of strong banking relationships is an important factor in enhancing the availability of debt to fund the group's future expansion. The provision of efficient cash management systems throughout the group ensures that banking requirements are serviced at the optimal cost. This section details the group's objectives in these areas of treasury, including procedures for the incorporation of new businesses into the group's cash management structure.

4.1 Objectives

- To ensure the cost paid for banking services is competitive.
- To minimise the cost of borrowings and maximise the return on cash surpluses within acceptable risk parameters by maintaining efficient cash management systems throughout the group.
- To develop and maintain strong relationships with a number of key banks.
- To monitor and ensure compliance with banking covenants.

4.2 Overview

In order to achieve the above objectives, netting or "massing"[5] arrangements are in place with the group's UK clearers. Interest rate exposures will be covered by the use of interest rate swaps transacted by group treasury in accordance with approved limits.

4.3 Banking relationships

Group treasury will be responsible for managing all banking relationships, ensuring consistency in relationships across different banking services (e.g. funding, risk management and cash management) to achieve the optimum benefit to the group.

Group treasury will meet all relationship banks on a regular basis to discuss services provided and any new or improved products of potential interest to the group. Operating subsidiaries will be responsible for the efficient operation of bank accounts within their control and for managing day-to-day relationships.

a) Current operations

Apart from the relevant UK clearing banks, the group has established a core group of relationship banks which provide funding through a number of committed and uncommitted bilateral facilities. This group has a wide geographical spread.

b) Future acquisitions

As the group continues to expand, the banking structure will be reviewed on an on-going basis, with group treasury responsible for the integration of new businesses into the banking structure and with UK businesses being incorporated into the "massing" arrangements with the appropriate clearer.

5 Massing is the process of aggregating the individual accounts of a parent and its related subsidiaries for the purposes of managing the net overdraft/cash position

5. Treasury reporting

The regular reporting of treasury activities is crucial in allowing all relevant parties to be aware of transactions undertaken, appreciate the group's financial position and assess the on-going appropriateness of treasury objectives. The following reports are produced to meet these criteria.

5.1 Daily movement report

This report is sent daily by group treasury to group audit and details treasury payments to/receipts from the three clearing banks, together with opening group balances and forecast closing net position. Major transactions by subsidiaries are also shown in this daily report.

Group accounts use this information to record the transactions for accounting purposes and to compare treasury transaction details (deal slips) with bank confirmations received to ensure proper financial control.

Circulation: group treasurer, director of treasury, group treasury manager, group financial controller/head of group accounts, group accounts.

5.2 Weekly group treasury report

A concise report giving details of:

- facilities available in the UK and amounts drawn against those facilities;
- cash deposits held around the group;
- summary of borrowings outside UK massing arrangements (including finance leases);
- net cash/borrowings position; and
- record of previous five end of day positions.

Circulation: group finance director, group treasurer, director of treasury, group treasury manager, group financial controller/head of group accounts, group accounts.

5.3 Monthly group treasury report
Every month a detailed report is prepared for the group finance director containing the following information:

- market commentaries;
- analysis of cash/borrowings;
- details of facilities – committed and uncommitted;
- financial covenant compliance;
- liquidity and security of funding;
- interest rate exposure;
- bank relationships;
- counterparty risks;
- foreign exchange translation exposure;
- gearing and interest cover; and
- outstanding forward foreign exchange contracts and derivatives marked to market.

Circulation: group finance director, group treasurer, director of treasury, group treasury manager, group financial controller/head of group accounts.

5.4. Quarterly performance report
Performance management is an important part of the control environment from a corporate governance perspective. A performance management framework is a mechanism for the investment committee and the board to approve policy and to monitor the effectiveness of that policy. The metrics used to measure performance may be quantitative and qualitative. It is important that any quantitative measures are simple to compute and market related.

Treasury will prepare a quarterly performance report as follows:

- performance of the investment portfolio versus the benchmark of *3 month Libid*[6] at the start of each quarter; and
- performance of the borrowing portfolio versus the benchmark of *3 month Libor*[7] +1/8% at the start of each quarter.

The objective of the treasury function will be to achieve an overall return in line with or better than these benchmarks.

Significant over-or under-achievement against the benchmarks, for an extended period of time, should be closely scrutinised by the investment committee.

Circulation: board, investment committee, group finance director, group controller/head of group accounts, group treasurer, group treasury manager.

[Note: The benchmarks stated here are only examples and NHS foundation trusts should set their own benchmarks based on their circumstances.]

6 Libid is the London Interbank Bid Rate as defined in Appendix 2
7 Libor is the London Interbank Offered rate as defined in Appendix 2

6. Treasury controls

6.1 Summary

The overall objective of the procedures set out below is to ensure treasury activities are undertaken in a controlled manner, thereby ensuring the group is not exposed to undue operational risks. In particular:

- segregation of duties is specified between those who deal, those who initiate payments and those who account for transactions;
- confirmation of transactions will be requested from all counterparties and checked by group accounts, not group treasury;
- all transactions are recorded within the treasury management computer system and are supported by an instruction/confirmation;
- all payment instructions/confirmations will require two authorised signatories, in accordance with approved bank mandates; and
- mandates will be regularly reviewed and sent to all counterparties.

6.2 Operational procedures applicable to group treasury

6.2.1 Undertaking transactions/dealing

Those authorised to deal are: director of treasury, group treasurer and group treasury manager.

All transactions are recorded in the IT recording system which provides confirmations and contains a database of all transactions.

Treasury transactions are only carried out with authorised counterparties and within set counterparty exposure limits.

6.2.2 Confirmation/payment instructions

All confirmations/payment instructions are signed by two signatories and in accordance with the limits under the bank mandate as approved by the investment committee.

Payment to third parties from the group account will only be made by Barclays, Lloyds TSB or HSBC on receipt of instructions bearing original signatures in accordance with the mandate.

6.2.3 Verification of confirmations

All confirmations received from third parties are checked by group accounts, not group treasury. Banks are instructed to send confirmations directly to the group accounts department.

Group treasury will provide to group accounts the following:

- daily movements report;
- copies of all deal tickets, payments instructions/confirmations; and
- weekly cash/borrowings positions report.

6.2.4 Counterparty limits

When entering into treasury transactions, consideration will always be given to the group's total exposure by counterparty. As the group has a core of relationship banks, the policy is to give banking business to those banks within the core group. All of the banks with whom transactions are conducted are considered to be creditworthy counterparties and, based on Moody's ratings which are reviewed on a regular basis, approved by the investment committee.

Exposure under derivatives is calculated as 20% of the nominal amount of the transaction.

6.3 Operational procedures applicable to other group companies

The majority of treasury activity will be undertaken by group treasury. However, in some circumstances it will be appropriate for other group companies to undertake transactions directly. Transactions undertaken by other group companies will be controlled in that the counterparty and the transactions must be approved by group treasury.

6.4 Bank mandates

Copies of all bank mandates are maintained by the company secretarial department. The group mandate is approved by the investment committee as to signatories and appropriate limits and copies are sent to all counterparties together with specimen signatures. As approved by the main board, any instrument for an amount exceeding £2m must be signed by two 'A' signatories. **[Note: this is only an example and NHS foundation trusts should determine their own thresholds if adopting this approach.]**

Appendix 2: Glossary of terms

Bank covenants: These are financial covenants required of a borrower and frequently include maintenance of a ratio of earnings to interest payable, a ratio of borrowings to earnings and a ratio of current assets to current liabilities.

Bilateral facility: This is a borrowing facility agreed between a company and a single lender, usually a relationship bank.

Certificate of deposit: A negotiable money market instrument that can usually be readily realised in the secondary market.

Clearing bank: A bank which (of itself or through a subsidiary company) is a member of Cheque and Credit Clearing Company Limited, which oversees the bulk clearing of cheques and paper credits in the UK.

Covenants: Covenants impose obligations on a company to do, or not to do, something for the duration of the agreement. They are intended to ensure the continued soundness of a lender's asset and to give the lender certain inside information about the borrower.

Derivatives: Financial instruments that are off-balance sheet and may be used to manage risk or as speculative instruments. Examples include forwards, futures, swaps, options and credit derivatives.

Forward foreign exchange contract: This is a mutually binding contract between two parties to buy or sell a specific currency at a pre-specified price (the forward price) on a pre-determined date in the future.

Gearing: A financial covenant used by lenders and variously defined, including, the ratio of debt to equity or the ratio of debt to capital employed.

Interest cover: The ratio of profit before interest and tax to interest payable and often used as a financial covenant by lenders.

Interest rate swap: A swap is a contract that commits two parties to exchange, over an agreed period, two streams of interest payments each calculated using a different interest rate index, but applied to a common notional principal.

Investment grade rating: Ratings provided by recognised rating agencies lie on a spectrum ranging from highest credit quality at one end to default or "junk" at the other. The highest credit quality for long-term ratings is AAA (Standard & Poor's/FitchRatings)/Aaa (Moody's) and the lowest is D (S&P/FitchRatings) or C (Moody's). Within this spectrum there are different degrees of each rating, which are, depending on the agency, denoted by a plus or minus sign or a number. For Standard & Poor's/FitchRatings a "AAA" rating signifies the highest investment grade and means that there is very low credit risk; "AA" represents very high credit quality, "A" means high credit quality and "BBB" is good credit quality. These ratings are considered to be investment grade, which means that the security or entity being rated carries a level of quality that many institutions require. Ratings that fall below "BBB" are considered to be speculative or junk. For Moody's the lowest investment grade rating is Baa.

Libid: Libid stands for the London Interbank Bid Rate and is the rate of interest at which banks could lend funds to other banks, in marketable size, in the London interbank market.

Libor: LIBOR stands for the London Interbank Offered Rate and is the rate of interest at which banks could borrow funds from other banks, in marketable size, in the London interbank market. Administered by the British Bankers Association, the rate is fixed daily at 11.00am and is the most widely used benchmark or reference rate for short-term interest rates.

Marked to market: A procedure to adjust the carrying value of a security or derivative contract to its current market value or the valuation of open positions at prevailing settlement prices.

Money market fund: This is a specialised fund that invests in money market instruments on behalf of its clients. The fund has credit enhancement such that it is generally highly rated for credit purposes by rating agencies (often AAA or A1/P1), without compromise to the liquidity of investments.

Net worth:	Total assets minus total liabilities and can be used to determine creditworthiness because it gives a snapshot of a company's investment history. It is also called owner's equity, shareholders' equity, or net assets.
Operational risk:	Risks arising from the trading activities of a business.
Permitted institution:	Institutions that have been granted permission, or any European institution that has been granted a passport by the Financial Services Authority to do business with UK institutions, provided it has a long-term credit rating of A1 or A+ issued by a recognised rating agency. Also includes investments with the UK Government and its departments.
Preferred concentration limit:	The requirement for NHS foundation trusts to invest their surpluses above a de minimus of £500K, across a number of permitted institutions, based on set investment limits.
Permitted rating requirement:	The rating requirement for safe harbour investments which should be A1/P1/F1 for short-term ratings and A1/A+ for long-term ratings.
Recognised rating agency:	These are the three main international rating agencies, Moody's, Standard and Poor's and FitchRatings. Each of these agencies provides a rating system to help investors determine the risk associated with investing in a specific company, investing instrument or market.
Safe harbour investments:	These are investments that fulfil the following criteria: meet the permitted rating requirement issued by a recognised rating agency; are held at a permitted institution; have a defined maximum maturity date; are denominated in sterling, with any payments/repayments of interest/principal also in sterling; pay interest at a fixed, floating or discount rate; and are within the preferred concentration limit.

Sterling commercial paper:	Sterling commercial paper takes the form of negotiable short-term promissory notes, payable to bearer. They may be issued by UK-based or international companies or financial institutions, using the market as a flexible way of raising short-term funds.
Surplus operating cash:	Cash likely to be needed within 12 months to support ongoing operations.
Transaction exposure:	This is the risk that a company's cash flows and realised profits may be impacted by movements in foreign exchange markets. Generally foreign exchange transaction risk is short-term, is revenue in nature and arises where there is a firm commitment to pay or receive in a foreign currency.
Translation exposure:	Arises for companies with overseas subsidiaries as the domestic value of the assets and liabilities of these subsidiaries fluctuates with exchange rate movements. In addition, the domestic equivalent of the foreign currency earnings of these subsidiaries will also be affected by movements in exchange rates.

Monitor
Independent Regulator
of NHS Foundation Trusts

4 Matthew Parker Street
London SW1H 9NL

T: 020 7340 2400
W: www.monitor-nhsft.gov.uk

IRG 19/05 © Monitor (December 2005)