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Learning and Implications from Peterborough & Stamford Hospitals NHS Foundation Trust

Monitor – Independent Regulator of NHS Foundation Trusts

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INTERNAL AUDIT, RISK AND COMPLIANCE SERVICES

Contents

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1. Introduction and scope

Background

Monitor commissioned KPMG to conduct a 'lessons learnt' exercise based on the events relating to Peterborough & Stamford Hospitals NHS Foundation Trust (Peterborough) during the period 1 January 2007 to 31 December 2011. The purpose of the exercise was to identify where existing processes across the Monitoring & Compliance function could be improved by analysing the events during that period with the benefit of hindsight, understanding why decisions were made and actions taken, and identifying learning and recommendations to improve processes. This analysis has included a consideration of Monitor's powers and how these may have affected or impacted on decisions.

Scope of services

This exercise was designed to address a series of questions relating to developments at Peterborough. These were:

1. When were the Board of Peterborough aware of the potential scale of the problem and why did they not act sooner?
2. Why was Monitor not aware earlier of the size of the impending problem at Peterborough until quarter 4 2010-11?
3. Is there additional information and reporting that Monitor could require Foundation Trusts to provide that would have helped identify this problem sooner?
4. Are there disproportionate constraints on the powers of Monitor to intervene in cases like this?
5. What changes if any has Monitor made to its approach as a result of Peterborough?

Within question 4 there are further sub-questions to be considered. These are:

4.1 When could Monitor have acted? And what could it have done?

4.2 What would the impact have been had Monitor acted earlier?

Approach

At a high level, the key steps in this review included:

- A kick off meeting to finalise the approach to the review on 3 January 2012;
- A review of key documentation to identify issues to explore and additional questions that might need to be addressed;
- Reviewing the timeline already established by Monitor that shows the chronology of events over the specified time period including any management decisions within Monitor and external communications;
- Early meetings with Compliance & Monitoring staff involved with Peterborough during the period being considered plus key senior individuals at Monitor to check out the high level chronology and lessons already identified so that the review does not focus on known lessons learnt but builds on existing knowledge;
- Identification of any additional information required and issues to explore in specific interviews;
- Drawing on a range of KPMG specialists through an advisory panel, with knowledge of the sector, to help challenge and analyse the issues identified, confirm areas to explore further in interviews. We have also used an advisory panel to help identify recommendations for change at an early stage;
- Undertaking interviews with key individuals to investigate specific issues and identify areas to explore further and develop recommendations;
- Presenting preliminary findings to the Monitor Board in January 2012;
- Scheduling of additional interviews and/or calls to gain further information to supplement lessons learnt and recommendations;
- Further analysis and finalisation of recommendations in a report including high level recommendations.

A glossary of terms used is attached on page 23 as Appendix A.
An exchange of letters is attached on pages 25 to 29 as Appendix B.
A list of people interviewed and documents examined is attached on page 30 as Appendix C

2. Executive Summary

Peterborough and Stamford Hospitals NHS Foundation Trust developed a business case for a new hospital under a PFI scheme in 2006. On 12 January 2007 Monitor wrote to Peterborough stating that it believed the long term affordability of the proposal to be in significant doubt. The letter was copied to the DH and HMT whose approval was required in order to obtain the Deed of Safeguard. However, Peterborough committed to the scheme in June 2007. Monitor's power to prevent Peterborough's Board from committing to a potentially unaffordable PFI in 2007 was very limited.

In 2007 Monitor wrote to the Peterborough Board and set EBITDA and CIPs targets for the next three years. Peterborough maintained an acceptable financial position from then until late 2010 when the new hospital was opened. In Q4 2010/11 an additional £10m of transitional funding was provided to Peterborough to cover that quarter's deficit. However, it was not until June 2011 that it became clear that the underlying annual deficit for Peterborough in the new hospital was in excess of £40m per annum on revenues of £200m.

While a turnaround plan has been developed at Peterborough, the details are still being developed and shaped. A turnaround plan was developed and presented to Monitor on 4 July 2011, followed by a detailed financial plan. The standard annual plan submission was delayed until the end of June 2011 in agreement with Monitor. Until such time as it has been finalised and signed up to by the Board and the new CEO, the figures will continue to change.

However, for the purposes of providing an indication of the core reasons for the forecast deficit in 2011/12, the analysis summarised below can be regarded as representative:

	£'M
• Structural/PFI related costs	22
• Backlog of CIPs/Financial control	12
• Income/Commissioning	10
• **Underlying deficit**	**44**
• One off costs in 2011/12	2
• **Forecast deficit for 2011/12**	**46**

Five questions have been asked of Monitor by the DH with a view to establishing what lessons can be learned from these events.

Q1: When were the Board of Peterborough & Stamford aware of the potential scale of the problem and why did they not act sooner?

1.1: The Peterborough Board was not aware of the loss for Q4 2010/11 before January 2011. They were not aware of the full extent of the underlying annual deficit until June 2011; six months after the new hospital opened. The nature and extent of the potential deficit was further clarified during the subsequent months.

1.2: The Board was not aware of the scale of the deficit until those dates because their budgets for Q4 2010/11 were inaccurate. Management had failed to track assumptions in the PFI business case and include realistic figures in their financial projections. Accordingly, their budgets did not reflect a realistic expectation of actual events and costs after moving into the new hospital at the end of 2010.

Q2: Why was Monitor not aware earlier of the size of the impending problem at Peterborough & Stamford until quarter 4 2010-11?

2.1: Monitor requires financial projections to be provided each year by FTs for the next three years. For the purpose of both annual planning and assessment, Monitor publishes future assumptions each year. Monitor does not plan or expect to audit APR returns from FTs.

2.2: Monitor set EBITDA and CIP targets for three years from April 2007 and reviewed Peterborough's financial projections each year as a part of the APR. While the EBITDA targets were met, CIPs targets were only achieved through one-off measures.

2.3: However, these targets had placed reliance on the financial information and APR projections received from Peterborough during this period. The projections in the APR returns made use of the assumptions provided by Monitor. However, they did not reflect realistic values for the period after the opening of the new hospital because other values and assumptions in the PFI business case had not been tracked and updated. Accordingly, Monitor was only aware of the deficit as it started to crystallise in 2010/11.

2. Executive Summary

Q3: Is there additional information and reporting that Monitor could require Foundation Trusts to provide that would have helped identify this problem sooner?

3.1: Monitor could have required Peterborough to submit recalibrated numbers for the PFI business case based on actual values each year. This would have enabled Peterborough management and Monitor to challenge the numbers and identify a growing gap between revenue and costs between 2007 and the end of 2010. This would have enabled an earlier warning of the impending deficit; certainly in 2010 and possibly in 2009.
3.2: While the time gained would have helped to reduce the level of failed CIPs (£10m), it would not have impacted the underlying structural deficit of £20m pa and would have had only an uncertain impact on the £10m pa commissioning aspects of the deficit.

Q4: Are there disproportionate constraints on the powers of Monitor to intervene In cases like this?

4.1 When could Monitor have acted? And what could it have done?
4.2 What would the impact have been had Monitor acted earlier?

4.1: Monitor had very limited powers to prevent the Peterborough Board from committing to an unaffordable PFI in 2007.
4.2: Monitor did establish EBITDA and CIPs targets for the next three years.
4.3: Monitor could have engaged more actively with the FT's management to ensure that the original business case was updated each year for actual values and Monitor's view of future assumptions eg on revenue tariffs, pay and non pay cost inflation. This should have highlighted the emerging position at least a year, and possibly two, before the PFI went live.
4.4: The impact would have been to enable additional CIPs improvements in the intervening period. It would not have reduced the £20m pa structural deficit and is unlikely to have impacted the commissioning element of £10m pa.
4.5: When IFRS was adopted as at 1 April 2009 PFI schemes came onto the balance sheets of FTs. Changes were made to the PBC that required Monitor to set Tier 2 borrowing limits. The impact of these limits is to effectively block unaffordable PFI schemes based on an FT's financial state. However, schemes that had already been approved were grandfathered into the system.
4.6: The explicit power to set borrowing limits under the PBC powers will move to whichever NHS body operates the NHS bank under the Health and Social Care Act 2012. However, under that Act, Monitor is set to have a different power to licence and regulate FTs. Monitor is in the process of determining the licence conditions that may be appropriate under this new power and the extent to which regulatory action might be taken in the event of the risk of prospective failure. These proposals will be subject to consultation during 2012. Had such powers been in place in 2007 then, subject to whatever interpretations and licence conditions might be developed during 2012 in the light of the Act, Monitor might potentially have been able to take regulatory action. Whether or not this is practicable will only be established during the next year as the detail of the new regulatory regime is developed and implemented.

Q5: What changes, if any, has Monitor made to its approach as a result of Peterborough?

5.1: FTs with major investments and PFIs are now subject to a more rigorous challenge during the APR and after.
5.2: Monitor is more assertive about ensuring that business cases for major investments are updated for actual values and ensuring the financial projections from FTs accurately reflect these numbers.
5.3: Monitor is more active in ensuring that independent evaluations are performed on any area where there is an uncertainty or a lack of transparency.
5.4: Further changes being planned including the greater use of:

a) diagnostic exercises on escalation;
b) the use of Chief Restructuring Officers; and
c) a new Licensing Framework, which is being developed in response to the Health and Social Care Act 2012.

3. Findings: Background

Background

Before addressing the five primary questions posed we think it is helpful for a reader to understand the flow of events during the period under review. In that context there are also some important matters to understand in relation to Monitor's Compliance regime and the extent and nature of its regulatory powers.

Timeline

Following its authorisation as an FT in 2004 the management at Peterborough developed its plans for a PFI to build a new hospital. By late 2006 these had come close to completion. Monitor had been kept informed of these plans and concluded in early 2007, based on its analysis of the Trust's own model, that they were not affordable.

Monitor's power to intervene as the regulator was very limited in scope. This is because the financial breach that might arise as a result of Peterborough entering the PFI was prospective. At the time the contract was signed Peterborough was not in financial failure and its financial risk rating under Monitor's Compliance Framework was satisfactory. Under the guiding legislation, the National Health Service Act 2006, Monitor can use its intervention powers only where there is a current and significant failure by an FT to comply with the terms of its Authorisation or there was a previous such failure and a likelihood that the FT would repeat that failure. That was not the case at the time the contract was signed by Peterborough. Responsibility for committing to the PFI rested with Peterborough's Board of Directors in accordance with the PFI process that was defined by Private Finance Unit of HMT/DH.

Accordingly on 12 January 2007 Monitor wrote to the Peterborough Board setting out its views and concerns and recommending that the FT's Board should not approve the scheme. The letter was copied to the DH and HM Treasury because, in order to proceed, a Deed of Safeguard would be needed from the Government. Peterborough responded on 16 March and Monitor wrote again on 4 April 2007 (see Appendix B). Notwithstanding Monitor's views, the PFI was approved by the Board and subsequently approved in their respective roles by the SHA and the DH, The HMT deed of Safeguard was provided and the Board duly signed the contract.

Monitor set quarterly EBITDA and CIPs targets for three years from 2007/8 to 2009/10 based on Peterborough's financial submissions. The EBITDA targets were being met by Peterborough, but not the CIPs targets.

In June 2008 a new Chairman was appointed. In November 2010 the Finance Director left . His post was found to be difficult to fill and an interim was in place until June 2011 when a permanent replacement was found.

In November 2009 Peterborough was escalated by Monitor for breaching the 18 week target. Management commissioned a review (and report) from EY of the self-certification process. EY reported in February 2010 when management also reported that the trajectory set by Monitor had been met. The EY report cited a number of key findings including:

- Multiple concerns regarding the recording, validation, monitoring and reporting of performance data many of which management had been aware of;
- A lack of validation of performance data, when it is known that data is not error free at the point of capture;
- Executive management were stretched and spending a lot of time fire fighting rather than managing to best effect; and
- The lack of a robust assurance framework combined with an Audit Committee and Internal Audit service that were not sufficiently robust to address the Trust's major risks.

Based on this report and Monitor's own evaluations Peterborough was escalated and formally considered for intervention; an escalation letter was sent on 1 March 2010 indicating that concern. A meeting was held between Monitor and the Peterborough Chairman on 15 March 2010 during which management agreed to take a range of actions designed to address the underlying concerns. The primary mechanism to achieve this was to engage EY for a range of tasks. The brief was controlled by Peterborough management .

3. Findings: Background (continued)

During May 2010 Peterborough breached its cancer target for the third consecutive quarter and was escalated. A decision was made by Monitor not to Intervene so as to allow the Chairman time to oversee the remedial action already in process with the assistance of EY.

The 2010 APR was submitted by Peterborough during this period and showed an FRR of 3 for all quarters of 2010/11 and 2011/12.

The EY report responding to the scope referred to above was issued in June 2010 and includes a range of criticisms and recommendations that indicate a significant level of concern as to the ability of the existing management to manage and oversee the Trust's plans for 2010/11, including the implementation of the PFI, and beyond.

Peterborough management appointed EY to a further exercise in June 2010 to support them in making improvements in preparation for the move to the new hospital. The scope of work included:

- "Programme management support;
- Assistance with turnaround and Cost Reduction Work;
- Medical Productivity and Core Service Review (CSR) Work;
- Assistance in transforming the operating model; in preparation for your move to the new Peterborough hospital in November 2010"

Monitor met with the Chairman on 12 July 2010 and an escalation letter was sent on 29 July 2010. Further escalation meetings were held by Monitor with the Chairman in October and November 2010.

The new hospital was opened at the start of December 2010. A further EY engagement was entered into in December 2010. This was scoped to cover support in managing an organisational change programme within the Trust.

Monitor called a formal meeting with Peterborough management in January 2011 to discuss its circumstances. The results for Q3 showed a deficit some £3.8m worse than had been expected in the projected results. Management appointed a Turnaround Director in March 2011 to support the Finance Director.

In March 2011 Peterborough informed Monitor of a rapidly deteriorating financial position for Q4 2010/11 following the opening of the new hospital and the need for an additional £10m of transitional funding approved by the SHA to manage its finances up to 31 March 2011 on top of the £10m already received. The CEO left on long term sick leave in May 2011.

In April 2011 Peterborough wrote to Monitor to confirm that they had agreed with Monitor that the final Annual Plan submission for 2011/12 would be provided at the end of June 2011.

In May 2011 Peterborough indicated that it was at risk of not achieving an FRR of 3 for the next 12 months. At the end of May 2011 an initial APR submission indicated an FRR of 1 in 2011/12 and 2 in 2012/13 and a projected loss approaching £40m. A senior independent Board Advisor was appointed in June 2011.

On 4 July 2011 a formal meeting was held with Peterborough management At this meeting, the outline turnaround plan was shared and there was the determination to appoint additional management support, which was subsequently Deloitte (who were appointed in August). This support was in addition to the senior independent Board Advisor who had been appointed in June 2011, and the Turnaround Director who had already been appointed on 31 March 2011.

The final APR was submitted on 30 June 2011 with an FRR of 1. The projected loss for 2011/12 was then in the region of £40m.

On 6 September 2011 an escalation meeting was held with Peterborough management.

3. Findings: Background (continued)

On 3 October 2011, following completion of the Deloitte work, a meeting was held with the Acting CEO and the Board Adviser which indicated that the actual financial position was worse than originally anticipated. The Trust was found to be in significant breach on 10 October 2011.

A detailed financial plan was completed on 21 November 2011 that showed the actual deficit could be as much as £56m for the year after redundancy costs of £10m. The underlying deficit was believed to be £46m.

While a turnaround plan has been developed at Peterborough the financial details are still emerging. However, for the purposes of providing an indication of the core reasons for the current deficit in 2011/12, and within that the extent of the underlying deficit prior to management action, the analysis summarised below can be regarded as representative:

	£' M
• Structural/PFI related costs	22
• Backlog of CIPs/Financial control	12
• Income/Commissioning	10
• **Underlying deficit:**	**44**
• One off costs in 2011/12	2
• **Forecast deficit for 2011/12**	**46**

Within this analysis of the numbers the following definitions have been used.

Structural/PFI related costs

Structural elements of the deficit represent the difference between the actual charges for the unitary payment, interest and depreciation and those that are regarded as affordable based on the HMT guidance on PFI schemes. The current Peterborough management has calculated this value as being approximately £22m pa.

This amount is expected to rise each year as the unitary payment increases with the RPI while revenues are subject to a tariff deflator (the business case had assumed that the tariff would increase by at least the RPI each Year).

Backlog of CIPs/Financial control

During the period from 2007 to 2010 Peterborough managed to meet its EBITDA targets. Although it appeared to meet its CIPs targets, savings were achieved largely as a result of in-year activity and not in embedded change in the operations and services being delivered. The failure to embed these changes is now being seen largely in the form of higher pay costs. Accordingly there is a backlog of CIPs. The impact in 2010/11 was masked by the additional transitional funding.

Income/Commissioning

Current levels of income are broadly in line with the original business case. However, other factors are involved including: activity levels being insufficient to utilise the hospital's capacity; penalties exercised by PCTs through their contracts; and, we understand, further reductions in payments negotiated by the core contracting PCTs and non payment for actual activity (not all activity under the PbR has been paid for). In addition, income from the sale of the PDH site has not materialised and will not be to the level considered in the original business case due to the economic down turn and resultant drop in land values.

One off costs:

In addition to the elements described above, during 2011/12 a range of other costs have been incurred in the light of the transition to the new hospital and in developing the turnaround plan for the trust. These costs would not be expected to recur at the same level in future years.

4. Findings: Q1 When were the Board of Peterborough & Stamford aware of the potential scale of the problem and why did they not act sooner?

The Board papers at Peterborough and returns to Monitor provide a picture of the broad timing of their awareness of the extent of the deficit arising from the PFI. The APR submitted in April 2010 showed an FRR of 3 for 2010/11 and 2011/12 indicating no awareness of an impending deficit.

A deficit was incurred in Q3 (up to 31 December 2010); a result that was worse than expected. However, this was the month when the new hospital was opened. The additional costs were attributed to the transition and possibly the failure of some CIPs.

In February 2011 the interim FD, drafted a paper showing the outturn for the year and the draft APR numbers for 2011/12. This was showing a much larger deficit for 2011/12 than was expected or had been projected by management previously.

In March 2011 a conference call was held at Monitor's request to discuss the funding position for 2010/11 and in particular the need identified by Peterborough management for an additional £10m of transitional funding on top of the £10m included in the budget. The additional £10m was to be drawn forward from the 2011/12 transitional funding to cover what appeared to Peterborough management to be transitional costs.

A Turnaround Director was appointed by Peterborough on 31 March 2011. The actual outturn for 2010/11, a surplus of £260k, was established in April 2011 and communicated to Monitor.

The numbers in the APR for 2011/12 were still changing at this time as further investigations were performed regarding the figures. The final APR was submitted on 30 June 2011, with the additional month for the final submission being agreed by Monitor and showing a projected deficit of some £40m for 2011/12.

In June 2011 a paper had been submitted to the Peterborough Board regarding the affordability of the PFI. The paper provided high level explanations of the majority of the factors in terms of changes to the underlying assumptions in the original 2007 PFI business case.

As a result, the Peterborough Board was only aware of the deficit for 2010/11, excluding the additional £10m of transitional funding, by around February 2011. However, the Board appears not to have been fully aware of the real nature of the underlying deficit post the PFI and the actual extent of the funding that might be required to rectify the position year-on-year until June 2011, when a paper was presented to the Board. In practice the final numbers in the financial plan were submitted in November 2011.

Why was the Board not aware sooner?

Financial projections at Peterborough focused mainly on the next year; reflecting the NHS's annual contracting cycle. While the Board had been aware of the risks associated with the original PFI proposal based on the assumptions made, no focus appears to have been placed on monitoring how these assumptions might be changing and crystallising with a view to measuring the impact on the ultimate affordability of the new hospital.

The business cases for PFI schemes include a wide range of assumptions that impact their affordability. These include estimates for activity levels, tariff changes, inflation in staff and non staff costs, revenues for the sale/rental from the old site and others. It is not credible that all of the assumptions made in 2007 were crystallising exactly as predicted in the business case. In fact the expectation should have been that the outcome would move regularly as assumptions proved to be incorrect and other events impacted the calculation.

4. Findings: Q1 When were the Board of Peterborough & Stamford aware of the potential scale of the problem and why did they not act sooner? (continued)

The first time that Peterborough management appears to have attempted to recast the numbers in the original PFI business case was in June 2011, after the PFI had gone live and by which point a major deficit had already been incurred.

Underpinning the facts of the timing are some broader questions. Given the concerns expressed by Monitor and the wide range of assumptions made in the PFI business case: Why did the Board at Peterborough not take steps to reassess the assumptions at least each year? Had they done that, then they would have been alerted to the impact of variations from the assumptions at a much earlier date.

Had that earlier warning then been available, it would have been possible to take earlier action on the need for CIPs. However, even in this situation, the earlier warning would:

- Not have changed the underlying structural deficit. The PFI would still have been unaffordable; the risk raised by Monitor in 2007;
- Have allowed more time to debate local commissioning decisions with the various stakeholders involved. It would not necessarily have changed the outcome of them.

On this basis it would have been possible to alert the DH and HMT at least a year earlier, and potentially two years earlier, as to the likelihood of a deficit and its extent.

Summary

The Peterborough management involved through the period from 2007 to early 2011 failed to look ahead and manage the single biggest financial and service risk facing them; a PFI contract starting and the move into a new hospital.

The executive management did not submit accurate papers projecting the Trust's financial position to the Board or to Monitor.

The non executive management has failed to challenge the executive management sufficiently through this period to be sure that the FT was managing its financial position leading up to and through a major change.

4. Findings: Q2. Why was Monitor not aware earlier of the size of the impending problem at Peterborough & Stamford until quarter 4 2010-11?

Monitor was aware in 2007 based on its own analysis of Peterborough's PFI model that the scheme was potentially not affordable. Having raised its concerns in a letter to the FT, Monitor put in place targets for EBITDA and CIPs for Peterborough that it thought would help them to manage their finances in each of the next three years (2007/8 to 2009/10) with a view to the PFI going live at the end of 2010/11. These EBITDA targets were met for each of the three years. However, CIP improvements appear to have been achieved through in year cost reductions rather than embedded (and so lasting) changes to services.

No EBITDA target was set for 2010/11 based on the experience of the last three years and the fact that Peterborough's management had, at Monitor's suggestion, engaged with EY to help them to achieve savings and to improve systems, projections and the operating model in the run up to the new facility when the PFI would go live.

Management appeared to be taking appropriate action. Accordingly, under their own Compliance regime, Monitor relied on the management to work towards achieving the financial targets and out-turns that had been set. No additional challenge was placed on the numbers over and above what would have been expected of other FTs.

There is an expectation that the annual APR returns submitted by FTs covering the next three years are soundly based. This includes using the assumptions provided by Monitor around tariffs, pay and non pay inflation. There is no formal requirement in Monitor's Compliance regime to require FTs engaging in major investments, such as a PFI scheme, to demonstrate that they have recalculated the business case numbers each year to ensure that the post opening impact has been correctly included. Rather, there is an expectation that the FT management will be doing this in order to ensure that accurate financial projections are made and with a view to managing the finances of the FT prior to and after the PFI goes live. It is simply good financial management.

During this period, and in particular during late 2009 and through 2010, there were a number of events or results that constituted a service breach or might have given sufficient cause for concern to warrant them being regarded as a significant breach. These included:

- **November 2009:** breach of 18 week patient target. Escalated and a management trajectory agreed;
- **February 2010:** Multiple concerns re A&E, PFI affordability. Decision by Monitor not to intervene based on Management's response;
- **May 2010**: Third consecutive breach of cancer target. Decision by Monitor not to intervene to enable the existing series of meetings with Peterborough's management team to continue;
- **June 2010**: EY report cites significant weaknesses in planning, CIPs delivery, leadership and Finance. Peterborough was still meeting an FRR of 3;
- **October 2010**: Escalation meeting held to discuss cancer target, wider governance concerns and financial risk associated with the hospital move; and
- **January 2011**: Formal meeting with Monitor to discuss a series concerns raised by Monitor in respect of: executive capacity, quality of financial plans and delivery of targets.

Through this period Monitor actively considered each of these events, which were not financial, through the Compliance and Monitoring system. Regular meetings were held between the Peterborough Chairman and Monitor's Executive Chairman and COO. In each case Monitor concluded that an intervention would not necessarily improve or change the outcome positively. They had confidence in the Chairman during most of this period and were satisfied that the combination of management action being described and the use of external advisors to assist with both cost savings and the transition to the new premises was appropriate. An intervention was not considered by Monitor's management to be likely to change any of the actions being taken by management during this period.

4. Findings: Q2. Why was Monitor not aware earlier of the size of the impending problem at Peterborough & Stamford until quarter 4 2010-11? (continued)

Accordingly, during this period Monitor was not aware of the full extent of the impending problem because:

- Monitor was relying on the Peterborough's APR returns regarding the post hospital opening period. It is now clear that these were inaccurate in that they failed to recognise the actual impending impact of the PFI (eg as could have been calculated in 2010) rather than the estimated impact as calculated in 2007;
- The actions being proposed and taken by Peterborough management had all the appearances of being appropriate;
- Monitor had not found a substantive reason to challenge the projected financial numbers in any greater depth.

At the start of 2011 calendar year when the Q3 results were submitted, these indicated a deficit. However, Peterborough had just opened its new hospital and cost over runs were not necessarily a surprise. Management had kept them informed.

Monitor was kept informed by Peterborough of the impending deficit for the year and the fact that additional transitional funding was being advanced to enable it to manage its finances up to 31 March 2011. It was not clear at this stage to Peterborough or Monitor that the additional transitional funding for Q4 was covering an underlying deficit of £10m per quarter.

Monitor formally became aware of a significant impending deficit in 2011/12 when the APR was submitted in May 2011. The actual quantum of the deficit and the extent to which it was structural became clearer during the summer when the updated APR was submitted on 1August 2011 and later in the year when the turnaround plan was finalised. An escalation meeting followed the 1August submission on 6 September 2011. A formal indication of the extent of the problem was received from the Interim Chief Executive and Board Advisor on 3 October 2011. This indicated the extent of the structural deficit and Peterborough was found to be in significant breach on 10 October 2011.

Summary

In essence Monitor was only aware of the extent of the problem and the deficit in this timeline because it was relying on financial projections and returns from Peterborough's Board. On the basis that the governance was acceptable while under the control of the Chairman, CEO and Finance director, there appeared to be no need for further challenge to the underlying numbers.

Monitor's assumptions for the APR projections had been used by Peterborough in its calculations. However, because no attempt had been made by Peterborough management to recalculate the impact of the PFI on opening the hospital, the projections post December 2010 failed to take account of the structural deficit. It is not clear why the figures for the post PFI period had always been based on the original business case and had not been updated to reflect the latest view of the likely outcome.

In the next section we deal with whether there is other information that Monitor might have used to identify this problem sooner.

4. Findings: Q3. Is there additional information and reporting that Monitor could require Foundation Trusts to provide that would have helped identify this problem sooner?

Monitor identified the primary cause of the current problems at Peterborough in January 2007 when it wrote to the Trust. However its powers of intervention were too limited to prevent the PFI contract from being signed, with other approvals having being gained as required from the SHA and DH and HMT's Deed of Safeguard.

The majority of the financial returns required during the year are retrospective. However, at the start of each financial year an APR is required from each FT projecting results for the next three years. The first year is regarded as the most significant because subsequent changes to commissioning and contracting can impact the second and third years. The APR in April 2010 showed an FRR of 3 for the remainder of 2010/11and also for the whole of 2011/12 ie after the PFI implementation. The numbers for 2010/11 recognised additional (transitional funding) in the last quarter. The numbers for Q3 and Q4 2010/11 appear not to have included realistic figures associated with the transition. Optimistic assumptions also appear to have been made about the extent of CIPs that would be achieved during those years.

In the case of the 2010 APR numbers projected for 2011/12, the figures differ so far from the actual values subsequently reported that it is clear no effective attempt had been made to recalibrate the PFI assumptions (extra costs of £4m per annum as opposed to £25m) to enable realistic projections to be made in preparing forecasts for the APR. The projections also appear to be based on unrealistic assumptions regarding the operating costs after opening. NB These are operational assumptions and not the assumptions provided by Monitor to FTs for using in projecting cost and revenue changes in future years.

The Peterborough Board received a paper produced in June 2011 by the new Finance Director that shows how the assumptions in the original business case changed and the broad impact of those changes.

There is one simple way in which different information might have enabled Monitor to identify the extent of the financial problem sooner which relates back to the PFI business case.

PFI Schemes and major investments

The three year projections required by Monitor in the annual APR returns are designed to be based on a set of assumptions provided by Monitor to assist in the evaluation of the prospective financial performance of each FT. This is a sound basis. However, in making their forecasts FTs inevitably need to make use of a range of operational assumptions in completing their calculations. These might typically be associated with service changes and specific CIP plans. In the case of major investments such as a complete hospital rebuild or a PFI scheme the level of risk and uncertainty involved in these assumptions is much greater. Accordingly the risk of an error in the projections is much greater. Monitor has practical experience of PFIs that demonstrate this to be so.

Monitor could take a more assertive approach with FTs that have a PFI (or major investment) in prospect to ensure that the FT management can demonstrate how they have assembled the APR projections covering the post opening period. This might involve ensuring that they have reworked their business case each year to reflect actual values rather than assumptions. A well managed FT should be doing this anyway. This reworking would provide the FT management and Monitor with a better estimate of the prospective out-turn when the PFI goes live and the extent of the CIP gap that needs to be closed before the go live date. Consideration might also be given to potentially optimistic assumptions regarding transitional and operating costs after opening based on Monitor's experience across the sector. The availability of updated information would also enable EBITDA and CIP targets to be recalibrated leading up to the PFI go-live date. Failure by the FT to manage that gap would give Monitor:

- an early warning of impending financial failure, eg unachievable CIPs;
- the ability to react and intervene; subject to whatever powers it may have;
- the ability to alert the SHA, DH and HMT to any impending structural deficits at least a year ahead of the crystallisation;
- the ability to raise the need for a local commissioning review or even a financial restructuring ahead of a PFI going live; in the event that there is a gap created by changes in commissioning strategy.

4. Findings: Q3. Is there additional information and reporting that Monitor could require Foundation Trusts to provide that would have helped identify this problem sooner? (continued)

Where Monitor might have concerns as to the quality of finance management or the accuracy of any such calculations it could require an independent review to be performed with a brief to allow direct reporting to Monitor. This might be done either as a part of the existing APR process through a stage 2 review or as a separate exercise at any suitable time through the year.

It needs to be noted that even with these additional checks in place, once a PFI contract has been signed, any actions taken will only mitigate the impact; they will not turn an unaffordable PFI into one that is affordable. However, these checks would provide the benefit of an early warning and additional time to address CIPs and discuss commissioning patterns with other stakeholders.

Summary

In making recommendations for change later in this report we have generalised from these specific issues to ensure that similar risks would also be addressed by changes to Monitor's processes. This might mean any significant investment, merger, acquisition or contract.

We recognise that Monitor is revising the APR process this year and have made some suggestions as to further changes that might be considered to help address risks such as those at Peterborough.

In order to achieve these changes it is important to be clear as to Monitor's powers. These have changed since it was established under the Health & Social Care (Community Health and Standards) Act 2003 and are due to change again under the Health and Social Care Act 2012. They are dealt with in the next section.

4. Findings: Q4 Are there disproportionate constraints on the powers of Monitor to intervene in cases like this?

In addition to the primary question noted above there are further sub-questions to be considered:

4.1 When could Monitor have acted? And what could it have done?

4.2 What would the impact have been had Monitor acted earlier?

Monitor's relevant powers are currently enabled through section 52 of the 2006 Act. In 2007 when the PFI was signed these were the only intervention powers available to Monitor. Monitor's power to intervene as the regulator was very limited in scope. This is because the financial breach that might arise as a result of Peterborough entering the PFI was prospective. At the time the contract was signed Peterborough was not in financial failure and its financial risk rating under Monitor's Compliance Framework was satisfactory. Under the guiding legislation, the National Health Service Act 2006, Monitor may use its intervention powers only where there is a current and significant failure by an FT to comply with the terms of its Authorisation or there was a previous such failure and a likelihood that the FT would repeat that failure. That was not the case at the time the contract was signed by Peterborough. Responsibility for committing to the PFI rested with Peterborough's Board.

As at 1 April 2009 the NHS adopted IFRS in place of UK GAAP for its accounting basis. One of the consequences of this change was to bring PFI balances onto the balance sheet of individual FTs. Changes were made to the PBC at this time that required Monitor to set Tier 2 borrowing limits for FTs seeking to make major investments. The effect of this limit was, in essence, to allow Monitor to limit the size of a PFI investment that it believed might be beyond an FT's reasonable borrowing powers.

Within the PBC, PFI schemes that had been entered into but not yet been implemented, were grandfathered. As a result Monitor had no power to intervene with PFIs that had already been signed but not implemented. More realistically this was two years after the PFI had been signed and it would have been impractical to consider any action of that nature.

Turning to the sub-questions:

When could Monitor have acted? And what could it have done?

What would the impact have been had Monitor acted earlier?

Monitor regarded the Peterborough PFI as a high level risk from 2007. The financial values projected in the 2010 APR for the post PFI period showed a surplus based on optimistic assumptions regarding CIP improvements. These and related concerns identified were considered in the light of the extensive engagement with advisors leading up to the opening of the hospital. Had Monitor challenged the Peterborough management to demonstrate the affordability of the PFI in subsequent years (after 2007) by updating the business case to show the impact of actual values rather than the assumptions, then such analysis would have shown a growing affordability gap. The APR projections submitted to Monitor should have shown this gap as a large deficit immediately after opening the new hospital. However, they did not because they failed to take account of the reality post opening. Trust was placed on Peterborough's management to have done this.

We have not attempted to calculate the path of this growth for Peterborough. However, even taking a broad view the size and growth of the gap would have been visible to all concerned at least a year before the PFI went live and possibly well before that, eg the 2009 APR.

4. Findings: Q4 Are there disproportionate constraints on the powers of Monitor to intervene in cases like this?

Based on its current powers, Monitor would still not have been able to intervene in 2009; the PFI contract would of course still be a real commitment. However, Monitor would have been aware of the rising gap (and affordability) at an earlier date and might have been able to:

- encourage Peterborough management to take more action on costs and revenues;
- liaise with the SHA and PCT to prompt a further discussion about commissioning intentions;
- liaise with the same to start a service reconfiguration in the locality;
- advise the DH and HMT as to the growing gap and the need for funding to cover a structural shortfall well ahead of the current date.

The impact in this case might have been to reduce the extent of the cost overruns and failed CIPs, by perhaps £5 to £15m over a period of up to two years. However, it would:

- have had no impact on the structural deficit that causes the hospital to be unaffordable. Peterborough remains unaffordable even with CIPs because it is too big/expensive for the volume of activity that it serves;
- only have had a limited impact on the commissioning intentions of the PCT had it been raised early enough.

It is not known whether this information would have had an impact on other Decisions in this part of the country.

Summary

Alternative courses of action, including a stronger focus during the APR process in horizon scanning for future risks, and a recalibration of the business case might have flushed out the extent of the impending deficit at Peterborough at an earlier date, which is most likely to have been during 2010, but which might have been during 2009.

Based on this earlier identification, additional CIPs might have been achieved. However, none of this would have changed the inherent (un)affordability of the PFI itself or the changes in commissioning profile which together appear to comprise some 75% of the underlying annual deficit.

Had Monitor's powers enabled it to intervene when the likelihood of a significant breach was high, then it could have taken earlier action more easily. Therefore, before concluding this section further comment is warranted on Monitor's powers in the context of the Health and Social Care Act 2012.

Monitor's powers as described in the Health and Social Care Act 2012

At the time of drafting this report the Health and Social Care Act 2012 has just received Royal assent. The changes made during its passage through Parliament have included revisions to Monitor's powers under the new structure of the NHS. It is not yet clear exactly how these powers might be used to deal with a prospective risk to the viability of an FT.

During the coming months Monitor will need to establish and consult on its draft licence conditions drawing on the various clauses within the Act with a view to determining how best to establish a licence regime that makes best use of the powers now available to it. Accordingly, it may be some time before the substance of these powers is clarified.

At this stage the most relevant clauses that might impact the circumstances in which Monitor found itself in relation to Peterborough appear to be:

Section 94: This allows Monitor to set standard conditions and to determine different standard conditions for different types of licence holders. It would be possible for Monitor to define FTs as a class, consequently set different conditions on FTs relating to governance. If any of the conditions are not complied with then Monitor can use licence enforcement powers;

4. Findings: Q4 Are there disproportionate constraints on the powers of Monitor to intervene in cases like this? (continued)

•**Section 95**: This allows Monitor to place special licence conditions, in addition to the standard conditions, on individual FTs or defined groups. This requires their consent;

•**Section 97**: This describes the types of standard or special conditions which may be contained in a licence, including those to ensure the continuity of service to patients.

•**Section 111**: This section provides for Monitor's imposition of additional licence conditions on individual FTs. Where Monitor is satisfied that the governance of an FT is such that it will fail to comply with conditions of its licence, Monitor may impose additional licence conditions on individual FTs. If they fail to comply with an additional condition, Monitor can makes changes to the Board of Directors and/ or Council of Governors.

The intention of the licences is to enable Monitor to help ensure that FTs meet their obligations. For example, in the Act's explanatory notes regarding section 98:
"Monitor may set such other licence conditions for the purposes of ensuring a provider continues to be able to provide NHS services under the terms of its licence, as Monitor considers appropriate, subject to sections 94-96. This may include, for example, requirements relating to liquidity and, where appropriate, long-term financial viability.

Monitor could take a number of measures under licence conditions set under section 97 (1) (i) (i) to protect the continuity of NHS services in the case of a provider in financial difficulties (in "distress"). For example, Monitor could direct a provider in distress to appoint a "turnaround team", or require a provider to provide information and access to their records and premises to a continuity of service planning team appointed by Monitor. The aim of such measures would be, wherever possible, to return the provider to normal operation as soon as possible and ensure the continuity of services which required protection.

Section 98(3) requires Monitor to carry out an on-going assessment of the risks to the continued provision of services to which a licence condition under section 96(1)(i), (j) or (k) applies. This enables Monitor to intervene early to assist providers to reduce any unacceptable risk."

The purpose of these powers would appear to be to enable Monitor to act on risks to an FT's long term viability; on the basis that they put at risk the FT's ability to maintain continuity of care to patients.

In relation to section 111 the guidance notes add:
"Subsection (1) and (2) provide transitional powers for Monitor to impose requirements on a foundation trust (in the form of additional licence conditions), as Monitor considered appropriate, to address a governance failing. Monitor would be able to impose such requirements where it is satisfied that this is necessary to prevent or remedy a breach of a foundation trust's licence, and that risk is due to the actions or inaction of the board of directors and/or council of governors. [This] allows Monitor to impose licence conditions relating to governance on a foundation trust where it is satisfied that the governance of the trust will cause it to fail to comply with its licence conditions to provide NHS services. Subsection (2) specifies that the circumstances in which these powers may be used include those where the trust's directors, governors, or both, are failing to comply with conditions in the trust's licence, or are failing to reduce the risk of a breach of licence conditions. Monitor's transitional powers are intended to provide an additional safeguard to protect patients' interests by ensuring that foundation trusts are well-governed and clinically and financially sustainable, in the early years of the new regulatory regime, when some foundation trust governors may be inexperienced and when some foundation trusts may be newly authorised. "

And later:
"Subsection (7) provides that Monitor's exercise of its transitional powers in subsection (5) would be without prejudice to its ability to exercise enduring powers to set and enforce requirements on foundation trusts, including requirements relating to governance, or requirements to ensure a foundation trust's continued ability to provide services for the purpose of the NHS. This

4. Findings: Q4 Are there disproportionate constraints on the powers of Monitor to intervene in cases like this? (continued)

clarifies that the transitional powers are in addition to Monitor's enduring powers to intervene where a licence holder is in breach of licence conditions, for example, requirements to maintain continuity of NHS services or to operate effectively, efficiently and economically."

These explanations appear to reinforce Monitor's powers to intervene when the trust's board and/or governors are failing to manage a risk that places continuity of service at risk.

The Health and Social care Act 2012 also contains express provision requiring Monitor to act so that there is no actual or perceived conflict between its exercise of FT specific functions and any of its other functions. In addition, in setting standard or special licence conditions Monitor must not act in such a way that it considers would result in a particular licence holder or holders of licences of a particular description being put at an unfair advantage or disadvantage in competing with others in providing NHS health care services as a result of being in the public or private sector or some other aspects of its or their status.

While the full implications of these and other clauses and provisions have not been confirmed through legal advice, it would appear to be the case where an FT was about to sign a major contract that was potentially unaffordable, Monitor could take action. This would involve Monitor placing licence conditions to reduce the risk, ie re the FT's ability to maintain continuity of service due to unmanaged risks to its long term viability. How this might work in practice is of course unclear and will only be determined once the relevant structures and processes have been developed, consulted on, revised and then implemented during 2013.

4. Findings: Q5 What changes if any has Monitor made to its approach as a result of Peterborough?

Changes since 2007

In January 2007 Monitor's systems and procedures had been operating for some 3 years but were still being refined and improved to reflect the new and emerging issues that FTs were encountering and to which Monitor needed to respond.

A range of practices existed regarding escalation and intervention. These were relatively ad hoc in 2007 due to the limited number of FTs and small number of interventions at that time. Towards the end of 2009 Monitor had started to refine and document more formally its escalation procedures. These were published internally in June 2010 as a pilot manual. A year later further refinements were incorporated in the manual when it was finalised

Changes have been made to the APR process in Compliance each year from 2007 to 2010. In 2010 a two stage evaluation process was adopted so that FTs identified as being of higher risk would be subject to a second stage review. The latest change made in 2011 was to include a cross check between FT's revenue projections and DH's analysis of commissioning intentions from PCTs.

From the middle of 2011 a different approach has been taken to FTs with PFI schemes in prospect. This has involved taking a more assertive approach from Monitor and required:

- FTs to submit more information to Monitor as a part of the APR relating to the schemes;
- Business cases to be reworked for actual values in place of assumptions;
- Independent evaluations to be obtained where Monitor required greater transparency of the prospective outcome.

Such changes have not been formally incorporated in the Compliance manual. This approach was not applied in 2010 for Peterborough because the scheme was about to go live and assurances had been received from management as to the basis of the projections for 2010/11 and 2011/12.

Current proposals

Since the start of this engagement Monitor has incorporate a number of changes to its Compliance framework. In relation to financial risk ratings, transitional funding is now excluded from the calculation of the FRR with a view to enabling the underlying position to be used as the basis of any escalation and intervention trigger.

Further changes are being planned for the APR in 2012. Some of these will be designed to capture risks that have been identified from a review of the Peterborough case.

The C&M system is always subject to challenge and review. There is a proposal under discussion currently to make further changes to the way Monitor acts on intervention. This would potentially involve:

1 A diagnostic phase at the start of an intervention to make sure that Monitor is clear as to the nature of the underlying problem. This can be particularly important in situations when the information from the FT may not be regarded as being reliable;
2 Introducing the use of Chief Restructuring Officers (CROs) to help manage the change and ensure a communication line to Monitor. These would be individuals paid for by the FT Board and sitting on the Board to advise on the changes required. They would have a role and responsibility to report to Monitor as and when required.

Other proposals

Based on the findings of this report we believe that there are further matters that Monitor may wish to consider evaluating with a view to building into its Compliance & Monitoring and Intervention procedures and practices. Of these there are three related matters that we believe impact directly the Peterborough case. They are presented first. The other recommendations have been identified during the course of our work but, while we believe they warrant attention, we do not regard them as primary recommendations in relation to the five questions.

5. Recommendations: Primary

Findings	Recommendations
1.1: While Monitor identified the risk associated with the Peterborough PFI in 2007, its follow through was not complete. While Monitor set EBITDA and CIPs targets each year, these were based on financial returns from the FT. Therefore they were not based on a recalculated business case which would have highlighted the growing affordability problem leading up to 2010/11.	When FTs make significant investments, and in particular when those investments are long term such as a PFI contract, Monitor should place additional focus on the associated risks including the uncertainties inherent in the business case and the FT's financial projections as submitted in the APR forecasts. Monitor should require FT management to submit updated calculations showing the impact on the business case of changes to assumptions over time. They might further require management to demonstrate how these changes have impacted projections in the APR where this is not clear. Any EBITDA and CIP targets set by Monitor will then be based on a more realistic projection of the actual outcome for the three years ahead of the go live date.
1.2: The APR process in Monitor involves an evaluation of financial performance and analysis of projections. However, it does not require the FT management to demonstrate how changes to long term investments are impacting their forecasts and long term viability & sustainability.	Within the APR process Monitor should require any FT with an impending investment to demonstrate how the forecast numbers incorporate the contract with a view to providing transparency on the affordability of the investment and the implicit need for the FT to find more CIPs (see above). A specific Focus should also be placed on the years after the implementation of the investment. NB Monitor needs to continue using its experience of the practical difficulty that FTs encounter in both projecting and then managing costs in the immediate post PFI period needs to advise FTs.
1.3: Within the APR process there is a second stage review for selected FTs to enable concerns to be investigated in more depth.	Where Monitor has continuing concerns as to the accuracy or robustness of the financial projections, it should require independent challenge to any projections that give cause for concern with a view to ensuring transparency on their potential accuracy. This can be achieved through a well focused the stage 2 review or at any other time during the year through the Compliance dialogue.

Secondary recommendations

In order that the benefit of the analysis and thinking should not be lost, we have recorded for Monitor a number of other recommendations where we believe changes could be made to its processes with a view to improving the quality of its decisions and the information on which those decisions are made. These matters are set out on the following pages.

In making these recommendations, it is recognised that Monitor has adopted a more assertive approach to its C&M activities over the last year with a view to ensuring transparency on key issues so as to provide its own management with greater visibility of the actual issues faced by FTs.

5. Recommendations: Secondary

Findings	Recommendations
2.1: We are aware that changes are being planned for the APR process for 2012. In making those changes we recommend that a consideration should be given to the follow matters which were identified in the course of this engagement as being of potential benefit.	1. In conducting its high level analysis of risk in the APR, a holistic view needs to be taken on the nature of the risks at an FT. Consideration should be given to using a balanced scorecard and defining a wider range of red flag and escalation triggers e.g. for recognised patterns of poor governance. Analyses should draw on a wider range of factors including such matters as the loss of key individuals such as the FD, the use of interims, major deficits in the PCT and other relevant factors. These factors could be developed by drawing on the combined knowledge and experience of the CMs and SCMs. Key combinations should also be defined. Consideration should to be given to defining patterns that might indicate poor governance with a view to requiring diagnostic reviews, such as FTs where there is a history or pattern of financial and service problems. Through this type of broader analysis a greater focus might be placed on re-evaluating risk indicators associated with the quality of governance and management. NB The same definitions could be used in the APR as in the (broader) escalation and Intervention manual to trigger suitable proportionate actions. 2. Increased use of information from stakeholders in the system might be considered with a view to establishing different lenses through which to evaluate the FT's performance; 3. A greater focus should be placed on the long term sustainability of the FT. This would need to include a consideration of the contracting environment in the area of the country, the extent of local competition for services and other related factors. Monitor may wish to consider providing specific guidance in relation to its expectations for long term projections eg on PFIs. 4. As part of the APR process, evaluations are subject to challenge to ensure consistency and to identify FTs that are regarded as being of higher risk. While CMs and SCMs contribute to the initial analysis, they do not take part as a matter of course in the final challenge processes. While the challenge is conducted by PDs and senior management, there may be important information or views held by CMs and SCMs that would add colour to the final debate. Consideration should be given to how to best involve them in the discussion; there should at least be structured feedback on the final decisions for risk ratings. 5. The APR process has evolved over recent years. While parts of the process are documented in a form for training/briefing, there is no single document that describes its purpose and how that is delivered from end to end. In order to enable the process to be maintained and developed it would be beneficial if the process were to be documented as a part of this year's revision.

5. Recommendations: Secondary

Findings	Recommendations
(Continued) 2.1: We are aware that changes are being planned for the APR process for 2012. In making those changes we recommend that a consideration should be given to the follow matters which were identified in the course of this engagement as being of potential benefit.	(2.1 continued) 6 A Stage 2 APR review is performed on FTs where there is an identified risk. In 2011 the reviews were all of a similar size and provided confirmation or analysis of the relevant issues where they were conducted. We believe that, if the terms of reference for these engagements were to be varied more in future years, this would improve Monitor's depth of understanding of the issues. For example, consideration should also be given to increasing the scope for selected FTs where a deeper analysis might be required to fully understand the underlying nature of the issues at the FT. This might result in a smaller number of exercises but with a stronger focus on the root causes and greater depth of analysis of the particular issues. 7 Monitor should reconsider the focus of its APR review. Currently the greatest focus is placed on the next financial year for practical reasons. However, where an FT has a major investment in process, the risks and uncertainties to financial performance can be much greater and longer term. By clarifying its expectations in relation to financial projections when there are long term investments in process Monitor could take greater account of these risks and place a greater emphasis on their analysis. Accordingly alternative courses of action can be developed to ensure that, through the dialogue with the relevant FTs and suitable use of diagnostic exercises, Monitor is able to establish complete transparency as to the level of uncertainty in such projections. It should also be possible to assist FTs through this challenge process by ensuring that they are sufficiently focused themselves on the extent of the risks involved. 8 In a similar vein Monitor might place a greater emphasis on the FTs' existing plans when completing the APR. For example, rather than asking FTs to compile plans in a particular form to support the APR, the process could be simplified by: a) obtaining copies of existing strategic and operational/development plans from FTs with a view to: - evaluating them to help inform Monitor's view of the state of the FTs' strategic thinking and governance; - understanding how well they might correlate with commissioning intentions in the geographic area; and - explaining the financial results in the financial returns. b) Seeking additional information just on those matters of particular concern/risk such as CIPs, major investments and PFIs. In both cases the information would form a part of the balanced scorecard referred to in the first bullet.

5. Recommendations: Secondary (continued)

Findings	Recommendations
2.2: Active management of external advisors	When an FT has been identified as being in significant breach, Monitor requires a degree of control over the brief provided to external consultants. In other cases where an FT has been identified as having a high risk and external consultants are being engaged in response to that risk, Monitor should consider requiring a degree of controls over the brief to ensure that it addresses Monitor's need as well as the FT's. When such briefs are set, the terms of reference need to be explicit making it clear that an open line of communication will be provided between the professional firm and Monitor, as the entity's regulator, to enable discussion about any matters arising from the engagement.
2.3: Escalation and intervention triggers	In addition to the use of the FRR and breach of a service target, Monitor should define other bases that can be regarded as either triggers requiring action or as constituting a significant breach, based on its experience. These might include combinations of financial and service problems, over an extended period, that are indicative of poor or failing governance. It would be helpful if such definitions were to be aligned with the holistic evaluations being performed during the APR. This would ensure that the APR includes a formal reconsideration of the state of risk and control at each FT. Consideration should be given to drawing on the range of tools available to bodies such as the FSA with a view to building relevant or similar steps into the escalation process. These additional tools would largely comprise diagnostic type exercises designed to provide Monitor (and management) with better information in relation to the relevant risks.
2.4: Diagnostic exercises in FTs	Consideration should be given to establishing a mechanism that allows Monitor to evaluate issues where is has concerns as to their status within an FT (c/f diagnostic exercises above). A simple way of achieving this would be to define the need for a diagnostic exercise to be performed within the FT based on a brief defined by Monitor. The FT would be responsible for engagement but, as with the use of external advisors, there would be an open line of communication to Monitor to enable discussion about any matters arising from the engagement
2.5: Monitor's escalation processes	The escalation process in Monitor requires papers to be presented at the CEC by the Portfolio Director. The CM and SCM responsible for the FT do not take part in these meetings; they prepare a paper for the PoD to take to the committees. Where the decision to escalate is not clear, it may be helpful to included the CM or SCM in the discussion should further detail and colour relating to the background of the FT be required. The CM and SCM would also be better informed as to the reason for and basis of any decision to escalate/or not as the case may be.

5. Recommendations: Secondary (continued)

Findings	Recommendations
2.6: External auditors	Through the various interviews conducted it has become clear that the interaction between Monitor and the external auditors of FTs is limited. The Audit Code and technical meetings (TIF) provide a basic structure at the highest level. The external auditors are required to communicate potential audit qualifications to Monitor. However, there is no other defined mechanism for any liaison or exchange of information. We believe that consideration should be given to exploring this area with a view to identifying areas where there would be a benefit for both the auditors and Monitor from sharing information; particularly in relation to higher risk FTs.
2.7: Periodic re-assessments of the state of Governance in FTs	The assessment process at Monitor places a considerable focus on the quality of governance and top management. It is a known phenomenon that after assessment and authorisation there is a risk that the quality and focus of governance fades and declines over time due to the lack of any impending re-assessment. It is not known whether or not this was a factor impacting Peterborough's decision in 2007 and the subsequent failure to recast the business case to reflect actual values. However, given the broader concern that arises regarding the extent to which Monitor needs to place reliance on an FT Board, we believe that further consideration should be given to the concept of periodic re-assessment of an FT's Board and governance. Such a mechanism would provide Monitor with an additional tool to encourage FT management to maintain the quality of its performance. There are many ways of doing this. FTs that have been identified from the holistic view as a part of the APR, or at any other time during the year, could be subject to a re-evaluation of governance. Whatever the mechanism adopted it is important that any FT could be selected for re-review in any year. Within this range of options consideration should also be given to methods such as observation of Board meetings by suitably experienced advisors. We understand that the use of periodic reviews is being considered as a part of the new licensing regime in the light of the Health and Social care Act 2012.
2.8: Knowledge management	The original letter written by Monitor to Peterborough in January 2007 was not captured in the C&M knowledge systems until 2011. While there is no indication that this impacted any decisions, it would be helpful to check the knowledge system for any FTs for which there are long term contracts in process to ensure that any historic comments and views from Monitor have been captured. While doing this Monitor should consider whether there are additional analyses that should be requested from FTs with long term investments in process in line with the core recommendations. The same principle would apply to information and views established during Assessment on transfer into Compliance & Monitoring system.

Appendix A. Glossary of terms

Acronym	Definition
APR	Annual Planning Review: Performed may to July each year; financial projections for 3 years are evaluated together with governance and non financial matters to evaluate the level of risk at an FT
C & M	Compliance & Monitoring
C & M and I	Compliance & Monitoring and Intervention
CM/SCM	Compliance manager/Senior Compliance Manager
CIPs	Cost Improvement programmes / plans
CQC	Care Quality Commission: primarily accountable for the inspection of healthcare bodies for clinical quality performance from 1 April 2009
CEC	Compliance Executive Committee
DH	Department of Health
FRR	Financial Risk Rating
FT	Foundation Trust
HMT	HM Treasury
PbR	Payment by Results
PBC	Prudential Borrowing Code
PCT	Primary Care Trust
PDs	Portfolio Directors
SHA	Strategic Health Authority
Trust	Foundation Trust (as in 'the Trust')

Appendix B: Monitor's letter dated 12 January 2007

Monitor

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12 January 2007

Dr Clive Morton
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Edith Cavell Hospital
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By email

Dear Clive

Peterborough and Stamford Hospitals NHS Foundation Trust – Proposed PFI Scheme

I refer to the Trust's proposed PFI Scheme ('the Proposal') and to the financial models submitted by Christopher Hall for Monitor's consideration.

It is not Monitor's role to approve a PFI deal or offer a recommendation to the Trust's Board or the Department of Health. The Trust's Board should satisfy itself, prior to financial close, that the deal is affordable, in the best interests of both the Trust and the community it serves and that it has considered carefully all aspects of the Proposal and has clear plans to mitigate the risks identified. In addition, the Trust's Board should continue to consider alternative options.

It is Monitor's role to review a Trust's proposals for major investments, including PFI projects, and to ensure that the financial viability of an NHS foundation trust will not be undermined if a transaction proceeds. We would expect the Trust's Board therefore to take into consideration the findings of our review and the likely impact on the published financial risk ratings were the transaction to proceed.

I am therefore writing in the first instance to obtain some additional clarification and, second, based on our review of the Trust's model and our limited further analysis, to highlight some specific concerns to the Trust's Board that Monitor has as to the affordability of the Proposal.

1. **Financial close and Unitary Payment ('UP')**

   I understand that financial close did not occur before the expiry of the UP price guarantee on 31 December 2006. However, your team has confirmed that the price guarantee has been extended to 31 March 2007 on the previous basis and to 1 June 2007 at a slightly increased value. I further understand that ABN Amro has withdrawn and been replaced by Macquarie Bank as a funder of the Proposal.

   Our analysis assumes the above with regard to the UP price guarantee. Please confirm that the terms under which the SPV is contracting with the Trust have remained unchanged and that the price guarantee has been extended as described above.

2. **Financial model, assumptions and sensitivity analysis**

   My team has reviewed the financial model submitted by the Trust and has taken the opportunity to test a number of the assumptions and sensitivities regarding the longer term affordability of the Proposal. It is worth emphasising that we have used the Trust's model as the basis for our review and testing.

   When running various sensitivities, it is clear that the affordability of the Proposal is crucially dependent on the ability of the Trust to deliver ongoing and consistent cost improvements over the period leading up to and post completion of construction. Principally as a result of these anticipated cost savings and in 2007/08 the expiry of the claw-back relating to PBR, in the first three years of the model the Trust's financial position is shown to improve from a planned I&E surplus for 2006/07 of £0.2m to an £8.2m surplus for 2009/10 (the last year before the proposed completion of the new building). This is equivalent to an EBITDA margin of 9.2% (compared with 7.0% currently being achieved for the six months to 30 September 2006). The average EDITDA margin across all FTs is currently 6.5%, with only 6 out of 48 achieving in excess of 9.2%.

   This improvement in operating performance and the creation of a significant surplus prior to completion of construction is central, along with further cost improvements following construction, to support the affordability of the Proposal. The Trust's model assumes ongoing cost reductions of 2% per annum on costs (excluding UP) following completion of construction up to 2016. The overall implication is that the Trust will be required and able to deliver in aggregate a £30.7m reduction in costs over 9 years (equivalent to over 18% of the total cost base of the Trust) in order to maintain financial stability.

   For a period of about two years, and following a review of all operating costs by the Trust and assisted by Alvarez and Marsal, the Trust has successfully progressed a recovery plan, in a significant part focused on improvements in efficiency and productivity. Given this background and the progress made to date in the area of reducing costs and improving returns, we are concerned as to the extent the Trust can be confident that it can continue to deliver reductions in its cost base in line with those assumed in the Trust's model both ahead of and following construction.

Appendix B: Monitor's letter dated 12 January 2007

Without these continued cost improvements over a long period, combined with the realisation of the other outcomes set out below including tariff and activity growth assumptions, the Proposal will not be affordable and the Trust risks the delivery of increasing deficits and cash outflows, ultimately exceeding its available funding.

Other important but potentially less influential variables in the Trust's model relate to assumed activity growth, site income derived from redundant property, tariff increases and other inflation related assumptions. Whilst assumptions over a long period around these aspects are understandably difficult to demonstrate with certainty, we highlight the following:

- the Trust appears to have assumed limited net activity growth over the period of the model;
- the Trust model assumes net revenues generated from the redundant site of about £4m per annum (at current prices). We understand that these revenues have since been reviewed and that the Trust (and Department of Health) has received independent confirmation that revenues of this order are reasonable. Monitor has not seen these reports, but a material shortfall of these revenues will significantly impact the affordability of the Proposal; and
- since the Trust sent us its financial model, the Department of Health has issued 2007/08 road test assumptions for tariff inflation of 2.5%; and pay and non-pay inflation of 5%. These compare with inflationary assumptions in the Trust's model for 2007/08 of 3% and 4.7% per annum respectively. Were the differential in tariff inflation and other costs to continue at this level, then the Proposal would almost certainly be unaffordable on any reasonable basis.

Finally, we are concerned that even if the Trust delivers the improvements in financial performance required by the model, the cash position of the Trust is shown to worsen over the post construction period. This will limit the Trust's ability to invest in or develop new services. At the same time the Financial Risk Rating ('FRR') of the Trust is shown to decline from the highest rating of 5 at 2009/10, to an FRR of 3 following construction

Monitor has stress tested the Trust's model to reflect some of the above concerns and to assess the potential risks of the Proposal and, if the cost improvements and site revenues fail to be delivered in line with assumptions, the longer term impact on the Trust's Financial Risk Rating.

By partially applying some of the sensitivities outlined above, and in the absence of other mitigating actions, the Proposal can quickly appear unaffordable in the medium term. Monitor has rerun the model using reasonable assumptions which shows the Trust's FRR declining to a 2, as the construction completes. Further, the FT would exceed its cash resources within a very short period post completion. We attach as Appendix 1 a summary of a potential scenario which incorporates our revised assumptions and two further adjustments.

On basis of the review we have undertaken, the details of which we will be happy to share with your team, and the possible downward trend in the Trust's FRR, we believe that the long-term affordability of the Proposal to be in significant doubt. Notwithstanding the amount of time and effort invested in the project to date, we believe that your Board should consider again the Proposal prior to taking a final decision to enter into a legally binding commitment. In particular, it will wish to review a final business case and supporting sensitivity analysis, which sets out the assumptions employed and the detailed support for the scale and ongoing nature of the cost improvement plans. It will also wish to consider again whether alternative options exist for funding the improvement of the services available to the Trust's users either within its existing funding facilities or potential borrowing which may be available to it based on anticipated future surpluses, without the need to proceed with the Proposal.

I look forward to receiving your response to this letter and an update on the overall status of the Proposal. Please contact me if further clarification is required on any of the matters covered above.

Yours sincerely

William Moyes
Chairman

Cc: Peter Coates - Department of Health
John Hall - HM Treasury

Appendix B: Peterborough's response letter dated 16 March 2007

16 March 2007

Dr William Moyes
Chairman
Monitor
4 Matthew Parker Street
London
SW1H 9NL

Dear Bill

Peterborough and Stamford Hospitals NHS Foundation Trust – Proposed PFI Scheme

Thank you for your letter dated 12 January 2007 which the Trust Board has considered very carefully at two successive full Board meetings. May I start by providing the clarification that you requested and then go on to address the specific concerns that you raised on the affordability of the scheme.

1. **Financial Close and Unitary Payment (UP)**

I can confirm that the terms on which the SPV is contracting with the Trusts has not changed as a result of Macquarie replacing ABN Amro as an equity sponsor of the SPV. I have attached at Enclosure 1 a copy of the letter signed by all parties prior to Macquarie taking over, which sets out the terms of the replacement. Paragraph 5A of that letter sets out the price guarantee, which can be summarised as a total UP for the scheme of £38.542m until 31 March and capped at £38.588m until 4 June. The approvals by the 3 Trust Boards and the DoH review in July 2006 are based on a total UP of £38.588M.

2. **Financial Model, assumptions and sensitivity analysis**

It is correct that the Trust's financial model shows an improved I & E surplus of £0.2m in 2006/07 and an £8.2m surplus for 2009/10. The Board is confident that these predictions are robust based on a combination of the current financial position (an in year surplus of £1.1m at the end of December 2006) and the detailed "Fit for the Future" financial improvement plan that has been the subject of much discussion between the Trust and Monitor over many months. Further, as you know, we have a long and effective track record of transforming patient pathways, cutting out redundant processes and improving cost effectiveness. The Service Improvement Team, which in December 2006 won the competition for the best transformation team in the whole of the public sector, believes there is still much to go for leading to confidence in further potential cost reductions.

Your challenges concerning the addition of cost savings over multiple years could be levelled at all Trusts and applies whether the scheme is pursued or not.

An additional, and helpful, factor is that the Trust's current financial predictions take no account of the East of England Strategic Health Authority's Acute services Review. Whilst this review will take some time to complete, it is clear that there is a high probability that there will be a net increase in activity in Peterborough (see letter from the SHA Chief Executive at Enclosure 2). It is not possible to predict with any certainty how much or what type of activity this will be, but there is no doubt that the Trust will be much better placed to respond to future increases in demand with a new hospital than with the current sub-standard facilities. The Trust Board's strategy is to expand both the range and quantity of activity in Peterborough, whilst still increasing the percentage of activity transferred from the hospital into the community. Neither aspect of this strategy will be possible in the foreseeable future if the PFI scheme does not go ahead. You will recall that this is a whole health scheme giving facilities to the PCT to aid the process of transferring activity into the community.

A clear endorsement of the need to update our current facilities was given by the Minister of State for Delivery and Reform, Mr Andy Burnham MP in his recent report "Days out in the NHS; listening to NHS Staff". Mr Burnham visited the Trust in July 2006 and his report states:

"What came over very clearly throughout this day was the importance of a high-quality working environment for both staff and patients. This trust was like many English hospitals; a piecemeal collection of buildings all reaching the limits of their usefulness. It was a busy day and not easy to be a patient or a member of staff. Even after an unprecedented building programme, too many parts of our NHS still do not provide staff with a decent working environment."

In response to the specific points on page three of your letter:

- The average net activity growth over the period of the model is 0.9% per annum. The Board believes this to be a prudent approach and is based on conservative (ONS) population growth assumptions. The balance of probability is that demand will increase faster than assumed, even without the effects of the SHA's Acute Services review. The key PCTs support this assumption. Population growth in Cambridgeshire is designed to grow by 22.5% in the next five years and Peterborough is on track to expand by 30% in the next decade. We have not factored in these assumptions. The SHA has confirmed (see letter at Enclosure 3) that the activity models that underpin the project are robust and that the modelling takes into consideration, where appropriate, anticipated local strategic changes to service delivery.

- The assumed net revenues from the redevelopment of the District Hospital site have been subject to independent reviews by both the DoH Estates and Facilities Department and the District Valuer (commissioned by HMT). The Trust is not privy to the DoH report, but the District Valuer's report is attached at Enclosure 4. Paragraphs 3.5 and 4 of that report suggest that "the assumption of receipts of £5m pa for 7.5 years from 2012/13 are reasonable". It should be noted that, whilst the Trust's Base Case I & E model assumes revenues of £5m from the redevelopment, a sensitivity analysis based on this revenue being halved still shows an I & E surplus (albeit reduced) in each year to 2015/16. One of the attractions of the Joint Venture model described in the King Sturge report is the flexibility it offers the Trust in terms of when, and in what form, the Trust takes the benefits of the District Hospital redevelopment. If necessary, the Trust could take some or all of the benefit earlier than planned in order to support a worse than predicted income and expenditure position. Similarly, the Trust could choose to take some or all of the benefit in cash rather than annuity revenue to support a worse than predicted cash position. This gives the Trust significant financial flexibility in the future that it would not have if the PFI does not go ahead. We believe this to be a prudent view and do not share your down side approach regarding this potential input.

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Appendix B: Peterborough's response letter dated 16 March 2007

- It is accepted that the DoH 'road test' assumptions for 2007/2008 of a net savings requirement of 2.5% (now confirmed within the published national tariff for 2007/2008), as opposed to the 1.7% assumed in the Trust's earlier financial model, are challenging. It is accepted that were the differential in tariff inflation and other costs to continue at this level then the PFI would become increasingly difficult to afford. However, the Board considers that, in these circumstances the Trust's (and indeed all other Trusts') financial projections would inevitably come under pressure as a result of the increasing cumulative cash-releasing savings requirement.. Hence these assumptions apply whether or not the Trust moves ahead with the project, and would affect all other Trusts in similar fashion.

- We have, of course, revised the financial models to reflect the latest net savings requirement of 2.5%, and the Board has considered these later projections at length. In revising the financial model, we have taken into account other relatively small changes. This approach, which we believe to be prudent and reasonable, shows the Trust still securing a financial risk rating of '3' in the years immediately after the PFI development.

The Board debated the paper attached at Enclosure 5 in detail on 6 March 2007. This paper sets out details of the base case assumptions, key risks and issues and in particular the stress-testing undertaken in connection with our financial projections and the foreward view. It also sets out areas of risk and uncertainty, and how these might be mitigated. This paper also refers to the in-depth consideration of these matters by the Board of Directors over a number of different meetings over time.The balance that the Board has to weigh is the financial and delivery risks of entering into a legally binding contract with Progress Health on the one hand against the long term effects on this Trust, our partners in the project and the Peterborough health economy of pursuing some other strategy on the other.

The primary consideration for the Board in drawing this balance is the additional cost of entering into the PFI contract over other possible alternatives, including funding improvement of services to the Trust's patients within our existing funding facilities and/or potential borrowings. The paper also sets out our consideration of alternative options for funding improvements in services. In this area, the Board examined all the options open to the Trust and concluded that the current capital regime contains no facility or potential to enable the replacement of the current three hospital sites in the city with a single new hospital, other than through the Private Finance Initiative. The Board also examined the feasibility of further reducing the scope of the PFI scheme in order to reduce liabilities (you will recall that following earlier Board challenge in 2005 the prospective Unitary payment was substantially reduced) but concluded that the current scheme was at the optimum level required to release capacity and improve efficiency for our commissioners and patients..

The paper shows that the additional costs of the PFI scheme over the "status quo" is £3m to £4m per annum. The financial predictions, taking on board your comments, still show surpluses albeit small, in the life of the project and the securing of a financial risk rating of '3' These calculations take no account of any additional revenue that might be generated by having the new facilities, nor any reduced costs from improved retention/reduced recruitment.

The calculations also take no account of the inevitable additional estates costs in the medium to long term if the PFI project does not go ahead. These factors have not been included in the calculations because it is not possible to quantify them with any certainty. However, it should be recognised that there is a major long term maintenance back log in the current estate since, other than for immediate needs, work has been shelved due to the anticipated short life of premises to be replaced under GPHIP. In terms of alternative options to PFI for funding improvement of the services it should be noted that the difference in quantum is very large. It is believed that the maximum that the Foundation Trust Finance Facility has granted to any one trust is of the order of £20M compared to the capital cost needed for major estates replacement in our case of in excess of £130M, depending on the option chosen.

In view of the importance of this issue, and being very aware of our corporate governance responsibilities, having been through the prolonged process described above the Board voted formally on whether it should continue to support the PFI and give the necessary approvals to enter into contact with Progress Health. The result of the vote was unanimous support for the scheme.

In conclusion, I think the following points are important:

- The Board appreciates and understands the challenges presented by Monitor; this has helped the Board to test fully a range of issues and develop its forward thinking;
- The Board has been able to consider, test and validate the whole spectrum of key assumptions which underpin its strategy, and the Board considers these to be sound and reasonable;
- We have worked hard to stress-test our key assumptions through a number of different scenarios, and believe that our strategy remains robust and credible;
- The Board has considered, at some length, other options for funding improvements to services for our patients, and concluded that that the current capital regime contains no facility or potential to enable the replacement of the current three hospital sites in the city with a single new hospital, other than through the Private Finance Initiative.

In light of the analysis above and in the attached papers, and cognisant of the robust process that the Board has been through, with effective challenge to every assumption, I would be grateful for your support in confirmation of the Board's position.

Yours sincerely

CLIVE MORTON OBE
Chairman

Copy: Mr K Pearson Chairman EoE SHA
Mr P Coates DoH

Appendix B: Monitor's response dated 4 April 2007

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Independent Regulator of NHS Foundation Trusts

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04 April 2007

Dr Clive Morton
Chairman
Peterborough and Stamford Hospitals NHS Foundation Trust
Edith Cavell Hospital
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Peterborough
Cambridgeshire
PE3 9GZ

Dear Clive

Peterborough and Stamford Hospitals NHS Foundation Trust – proposed PFI scheme ('the scheme')

Thank you for your letter dated 16 March 2007 and the revised financial models sent by Christopher Hall. You requested Monitor's support in confirmation of your board's position. Before I address that issue, I believe it would be useful to recap Monitor's role in the PFI process.

It is not Monitor's regulatory role to approve the scheme or offer a recommendation to the Department of Health. Rather it is for the Trust's board to satisfy itself, prior to financial close, that the scheme is affordable and in the best interests of both the Trust and the community it serves.

That said, the future financial viability of your Trust is critically dependent upon the proper assessment of risk and the successful delivery of any significant investment plans, such as the scheme.

Financial Model assumptions and sensitivity analysis
I note the steps taken by the Trust's board to ensure that debate and review has been thorough, that the risks and alternative options have been fully considered and concerns as to affordability raised by Monitor in our earlier correspondence addressed. In particular, I note that your SHA has confirmed activity planning assumptions. I do not propose to ask my team to run further sensitivities on the financial model provided.

Financial Risk Ratings (FRR)
In my earlier correspondence dated 12 January 2007, I raised concerns regarding the potential decline in the Trust's FRR in the period following the implementation of the scheme. You have confirmed that under the scenarios considered by your board, the Trust should secure a FRR of 3 in the years immediately after the PFI implementation.

As you will be aware, any under-achievement against planned FRRs could trigger a significant breach of the Trust's terms of Authorisation under section 52 of the National Health Service Act 2006 (the "2006 Act").

Failure to achieve a FRR of 3, as planned in the Trust's financial model and agreed by the Trust's board, may also signal serious governance failings. In particular, Monitor would be obliged to assess whether the Trust was complying with its general duty under section 63 of the 2006 Act to exercise its function effectively, efficiently and economically, as replicated in condition 2 of the Authorisation.

Cost Improvement Plans (CIPs)
My letter dated 12 January 2007 demonstrated that the affordability of the scheme is crucially dependent on the ongoing and consistent delivery of cost improvements leading up to and after completion of construction. Principally as a result of these anticipated cost savings, the Trust is forecasting to move from an I&E surplus in 2006/07 of £0.2m, to a surplus of £8.2m in 2009/10, the final year before the proposed completion of the scheme.

If material under-performance were to arise, including the failure to deliver these cost improvements, and there were a consequent worsening of the planned FRR, your Board should expect Monitor to act rapidly. To ensure performance levels are agreed and understood by both parties, Monitor will require the Trust, at the date of the Annual Plan submission each year, to agree a quarterly CIP and FRR profile for the following three financial years. This is to ensure the FRR of 3 can be secured once the full unitary payment is in the cost base. Failure by the Trust to deliver the projected CIPs and a related improvement in FRR could put the Trust's future financial viability at risk and may also signal serious governance failings.

Monitor will compare as part of the quarterly monitoring process (or monthly monitoring should this be required) actual performance versus the target improvement in costs, and if necessary, require the Trust to provide additional commentary on adverse variances and action plans for rectifying these. Monitor will assess the factual circumstances of and reasons for any under-achievement and deploy its statutory powers of intervention as appropriate. This additional data requirement will commence from the Annual Plan submission for 2007/08.

As previously stated, it is not Monitor's role to approve the scheme. Our significant concerns as to the scheme's affordability remain and we have already written to you and your board documenting these. It is now for your Board to decide whether to proceed with the scheme as planned or whether to take steps to ensure that the full unitary payment is affordable within an FRR of 3 or better. In reaching its final decision, your board should fully understand the potential implications of the Trust failing to deliver the significant and sustained improvement in performance required to enable it to continue to comply with its Authorisation.

Yours sincerely

William Moyes
Executive Chairman

CC Nik Patten – Chief Executive

Appendix C: Monitor and Peterborough staff interviewed and documents examined

Staff Interviewed

Name	Title
	Monitor
David Bennett	Chairman and acting Chief Executive
Adrian Masters	Director of Strategy
Stephen Hay	Chief Operating Officer
Kate Moore	Director of Legal Services
Merav Dover	Compliance & Monitoring Director
Richard Guest	M&A and Restructuring Director
Adam Cayley	Portfolio Operations Director
Robert Davidson	Portfolio Operations Director
Alex Coull	Compliance Manager
Kath Cawley	Compliance Manager
	Peterborough Management
Nigel Hards	Chairman
Louise Barnett	Acting Chief Executive
Chris Preston	Finance Director
Jane Pigg	Company Secretary
Pelham Allen	Board Adviser
Ross Tudor	**External Auditor of Peterborough (KPMG)**

Documents Examined

Monitor letter to Peterborough management 12 January 2007 and associated responses
Monitor APR papers 2009, 2010 and 2011
Peterborough Compliance files from 2007 to 2011
Monitor Compliance Executive Committee agendas, papers and minutes over the period under review relating to Peterborough
Monitor Compliance Board Committee papers and minutes over the period under review relating to Peterborough
Monitor communications sent and received regarding Peterborough over the period under review with Peterborough management
Sundry Peterborough Board papers mainly from December 2010 to November 2011
Final Financial plan for Peterborough dated 21 November 2011
Timeline of events relating to Peterborough developed by the Monitor C&M team
Compliance Framework over the period and Monitor Compliance Escalation Procedures for Issue Trusts

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