NHS Foundation Trust Financial Reporting Manual 2008/09 *(FT FReM)*

23 April 2009

Contents

1. Annual Report and Accounts preparation and submission requirements

Statutory requirements for NHS foundation trusts' Annual Report and Accounts

1.1 There are three main statutory requirements for an NHS foundation trust in relation to its accounts:

- to keep accounts in such form as the regulator may with the approval of HM Treasury direct;
- to prepare in respect of each financial year annual accounts in such form as the regulator may with the approval of HM Treasury direct; and
- to comply with any directions given by the regulator with the approval of HM Treasury as to:
  - the methods and principles according to which the accounts are to be prepared,
  - the information to be given in the accounts.

1.2 These requirements are set out in paragraphs 24 and 25 of Schedule 7 to the National Health Service Act 2006 (the 2006 Act).

1.3 In determining the form and content of the annual accounts, Monitor, as the regulator, must aim to ensure that the accounts present a true and fair view (paragraph 25(3), Schedule 7). Monitor has to obtain HM Treasury's approval for the Accounts Direction. The agreed Accounts Directions in respect of the Annual Accounts and of the Annual Report are both shown at annex 1 to this chapter.

1.4 In order to present a true and fair view, the accounts of an NHS foundation trust must comply with UK Generally Accepted Accounting Practices (UK GAAP) unless directed otherwise. The main source of guidance, therefore, for NHS foundation trust finance staff will be published accounting standards and supplementary guidance. Extant UK accounting standards are available from the Accounting Standards Board's website at http://www.frc.org.uk/asb/technical/standards/accounting.cfm.

1.5 NHS foundation trusts also fall within the remit of the Financial Reporting Advisory Board (FRAB) which provides independent accounting advice in respect of public sector bodies to HM Treasury and the equivalent bodies in Scotland and Northern Ireland. The advice of FRAB is reflected in HM Treasury's *Financial Reporting Manual* (the *FReM*), which is written for Government departments, executive agencies, executive non-departmental public bodies and trading funds. This manual is consistent with the requirements of *FReM* and provides relevant guidance on departure from UK GAAP. Divergences from *FReM* for NHS foundation trusts have been agreed with FRAB and the current list of divergences is included as annex 1 to chapter 2 of this manual.

1.6 If NHS foundation trusts wish to refer to HM Treasury's *FReM* on a particular issue, a copy can be accessed on the resource accounting website at www.financial-reporting.gov.uk.

1.7 NHS foundation trusts should discuss the practical application of accounting standards with their auditors and agree the accounting approach which will be adopted. Guidance on accounting standards is included in this manual only where NHS foundation trusts are:

- required to depart from UK GAAP;
- required to make disclosures which are in addition to UK GAAP; or
- faced with particular circumstances which UK GAAP does not address.

1.8 It is expected that the preparers of an NHS foundation trust's Annual Report and Accounts will consult this manual in the first instance and then refer to accounting standards where necessary. Other relevant guidance is cross referenced in this manual where appropriate.

1.9 This manual has been finalised following the issue of a summary of proposed changes for consultation. A summary of responses to this consultation is available on the Monitor website: www.monitor-nhsft.gov.uk . It may be necessary for Monitor to issue amendments to this manual as issues arise during the year. Directors of finance will be notified by email of any amendments to the current manual and the amendments will also be published on Monitor's website. In addition, the manual will be updated annually and published on Monitor's website following consultation.

Annual Report and Accounts

1.10 The Annual Report and Accounts of an NHS foundation trust consist of:

- the annual report which includes the directors' report and remuneration report (see paragraph 4.6 and 4.22 for details);
- the accounting officer's statement of responsibilities (see paragraph 4.74 for details);
- the auditor's opinion and certificate (this should include a statement of the auditors' responsibilities in order to satisfy the requirements of paragraph F.1.1 of the Code of Governance);
- the statement on internal control (see paragraph 4.76 for details);
- the foreword to the accounts which should state that the accounts are prepared in accordance with paragraphs 24 and 25 of Schedule 7 to the 2006 Act;
- four primary financial statements (income & expenditure account, balance sheet, statement of total recognised gains & losses and cash flow statement); and
- the notes to the accounts.

1.11 NHS foundation trusts are able to present their Annual Report and Accounts in any way that they choose, providing that they are compliant with UK GAAP and the additional requirements laid down in this manual. Therefore, this manual does not include an accounts template although it does include some example statements and notes where it is considered useful.

Consolidated NHS foundation trust accounts

1.12 Monitor is required by statute (paragraph 11(3), Schedule 8 to the 2006 Act) to prepare a report in respect of each financial year which provides an overall summary of the accounts of NHS foundation trusts. This report must be prepared as soon as possible after Monitor has received the Annual Report and Accounts of all NHS foundation trusts for the relevant financial year and must be laid before Parliament and copied to the Secretary of State. The accounts of all NHS foundation trusts will also be consolidated into the *Whole of Government Accounts* prepared by HM Treasury. NHS foundation trusts will have to complete consolidation schedules to allow for the capture of accounting data for the summary of accounts and the *Whole of Government Accounts*.

Deadlines, approval and publication procedures

1.13 Monitor has issued the deadlines ***below*** for the production of NHS foundation trust Annual Reports and Accounts for the year ending 31 March 2009**.** Please note it is the responsibility of the trust's Accounting Officer (and not the auditors) to comply with these requirements:

Deadline	What is required?	Where should it be sent?
Thursday 23 April 2009	• **Draft** Annual Accounts; • **Draft** FT consolidated schedules (FTCs); • **MARS/emailed** to Monitor (**NOT** posted), and given to your auditors	**Your MARS portal folder** Ongoing\2008-09\accounts\unaudited **(or in case of technical difficulties) by email:** ft.accounts@monitor-nhsft.gov.uk
Monday 8 June 2009	• **Audited** Accounts and • **Audited** FTCs and • **Final** text of the Annual Report • **Posted** and **MARS/emailed** to Monitor. (posted first class before the last post on Monday 8 June 2009). It would assist us if subject lines of emails identified the trust and attached copies of certificates and accounts contained signatures as and where appropriate.	**Your MARS portal folder** Ongoing\2008-09\accounts\audited **(or in case of technical difficulties) by email:** ft.accounts@monitor-nhsft.gov.uk **Postal Address:** FT Accounts, Monitor 4 Matthew Parker St London SW1H 9NP
Tuesday 7 July 2009	**Laying reports before Parliament:** • **Full** annual report and **full** statutory accounts (bound as one document) • **5 hard copies** to be **posted** to the Parliamentary Clerk's office for laying before Parliament (posted first class before the last post on Tuesday 7 July 2009) **See Annex 2 to Chapter 1 for more details.**	**Postal Address:** Parliamentary Clerk's Office Department of Health Room 301 Richmond House 79 Whitehall London SW1A 2NS
Monday 20 July 2009	**Sending laid reports to Monitor:** • **Full** annual report and **full** statutory accounts • **Posted** and **MARS/emailed** to Monitor. One copy to be sent electronically for inclusion on the public register. Two hard copies to be sent by **post** (posted first class before the last post on Monday 20 July 2009). **See Annex 2 to chapter 1 for more details**	**Your MARS portal folder** Ongoing\2008-09\accounts\audited **(or in case of technical difficulties) by email:** ft.accounts@monitor-nhsft.gov.uk **Postal Address:** FT Accounts Monitor 4 Matthew Parker St London SW1H 9NP

1.14 The Annual Report and Accounts submitted on ***8 June 2009*** must be formally approved by the NHS foundation trust board of directors (the board). After adoption by the board, the chief executive, as the Accounting Officer, should sign and date the balance sheet and Annual Report as evidence of this. As Accounting Officer, the chief executive should also sign the foreword to the accounts, the statement on internal control and the remuneration report. The Annual Report and Accounts should disclose the name of the person who signed them.

1.15 Once the Annual Report and Accounts have been approved the auditor will sign the opinion on the accounts. However, auditors are required to read the information in the Annual Report and refer to this in their audit opinion. Therefore, the draft Annual Report must be submitted to the auditor to allow them sufficient time to do this prior to signing their opinion on the accounts.

1.16 Once the Annual Report and Accounts have been approved, the Accounting Officer or director of finance must sign a certificate which states that the FT consolidation schedules (FTCs) are consistent with the annual accounts. Annex 4 to this Chapter includes the proposed wording for such a certificate.

1.17 NHS foundation trusts are required to lay their Annual Report and Accounts, with any report of the auditor on them, before Parliament (paragraph 25(4)(a), Schedule 7 of the 2006 Act) before the summer recess begins in July 2009. Further guidance and a timetable for submission is provided in Annex 2 to chapter 1.

1.18 The requirement to lay the Annual Reports and Accounts before Parliament means that they are classified as an Act Paper and become the property of Parliament. There are strict rules about the format of the publication and these must be followed in every case. These rules and the timetable for submission are set out in Annex 2 to Chapter 1

1.19 The Annual Report and Accounts which are laid before Parliament **must include the full statutory accounts and not summary financial statements**. The Annual Report and Accounts that each NHS foundation trust submits to Parliament to be laid must be one document. It might be that this is formed from two electronic files but they must be presented (i.e. the hard copy must be bound) as one document. If an NHS foundation trust is getting an Annual Report and Summary Financial Statement document designed, a solution could be to bind a pdf of the annual report with a pdf of the full annual accounts and amend the title accordingly.

1.20 The Annual Report submitted on ***8 June*** must include all of the text which will be included in the final publication submitted to Parliament. This is because the auditors will need to see the form of the annual report prior to signing their opinions. The period between ***8 June*** and submission to Parliament is to allow NHS foundation trusts time to format the document to the standards required for publication.

1.21 Until the Annual Report and Accounts have been laid before Parliament nothing can be published by the NHS foundation trust for the wider public.

1.22 Once laid before Parliament the Annual Report and Accounts cannot be changed. Guidance on the form and content of the annual report is included in chapter 4 of this manual. However, NHS foundation trusts have the discretion to publish Annual Report and Summary Financial Statements locally, see paragraph 1.26 below for more details.

1.23 Copies of the audited annual accounts, any report of the auditor and the latest annual report must be made available for inspection by members of the public free of charge at all reasonable times (paragraph 22(1), Schedule 7 of the 2006 Act). Any person who requests a copy of or an extract from any of these documents must be provided with one, although a reasonable copying charge may be levied where the person requesting a copy or extract is not a member of the NHS foundation trust (paragraph 22(4), Schedule 7 of the 2006 Act).

Annual general meeting of the board of governors

1.24 The Annual Report and Accounts and auditor's report on the accounts must be presented to the board of governors at a meeting of the board of governors (paragraph 28, Schedule 7 of the 2006 Act). This meeting of the board of governors should be convened within a reasonable timescale after the end of the financial year but must not be before the Annual Report and Accounts have been laid before Parliament.

1.25 It is suggested that an advertisement be placed in the local media not less than 14 days prior to the date of the meeting, stating:

- the time, date and location of the meeting; and
- that copies of the Annual Report and Accounts (or Annual Report and Summary Financial Statements) of the NHS foundation trust are available, on request, prior to the meeting and how copies can be obtained.

Summary financial statements

1.26 Once the full Annual Report and Accounts have been laid before Parliament, NHS foundation trusts have discretion as to whether they wish to publish the full document locally or the Annual Report and Summary Financial Statements. If Summary Financial Statements (SFS) are published, they must be accompanied by a report from the auditor, which will be prepared in accordance with the APB Bulletin 2007/01 Example reports by auditors under company legislation in Great Britain. The title of the report should be amended to "Annual Report and Summary Financial Statements".

1.27 The Annual Report and Summary Financial Statements must be made available to the public free of charge, although a reasonable copying charge may be levied for copies of the full audited accounts where the decision has been made to publish SFS. SFS must contain the following:

- a prominent statement that the SFS are merely a summary of the information in the full accounts which are available on demand;
- the amount, if any, of the nominal fee charged for the full accounts must be stated together with the address/phone number of the person to be contacted to obtain a copy of the full annual accounts;
- summary financial data in line with section 428 of the Companies Act 2006 and Part 3 and Schedule 7 or 8 of the Companies (Summary Financial Statement) Regulations 2008 (SI 2008/374). This involves publishing either the primary statements in full or, as a minimum, disclosing the entries in the accounts under the main headings;
- the statement on internal control;
- the auditors' report on the SFS; and
- a statement that the SFS have been approved by the board. This should be evidenced by the signature of the chief executive as accounting officer.

1.28 The SFS must not be published before the full Annual Report and Accounts have been laid before Parliament.

NHS foundation trusts in their first period of operation

1.29 When an NHS trust is awarded NHS foundation trust status, an Annual Report and Accounts must still be published for the final period of the NHS trust's existence. This may cover a full financial year where the change in status occurs on 1 April or a shorter period where the change in status occurs during the financial year. NHS foundation trusts will be required to prepare the final accounts and summarisation schedules for the predecessor NHS trust and meet the deadlines set by the Department of Health. NHS foundation trusts should be aware that auditors may require the NHS trust accounts to be prepared in accordance with the NHS foundation trust deadline, where earlier, in order for the auditor to sign their opinion on the NHS foundation trust accounts.

1.30 A public meeting must be held by the 30 September following the end of the financial year in which the NHS foundation trust was authorised at which the predecessor NHS trust's final Annual Report and Accounts for the final period of NHS trust status must be presented.

1.31 The annual report, annual accounts and consolidation schedules for the final period of NHS trust status must be prepared in accordance with the guidance in the *NHS Trust Manual for Accounts* issued by the Department of Health for the period in question. It is recommended that the Annual Report and Accounts for the final period of the NHS trust is produced as a separate document to the Annual Report and Accounts for the first period of the NHS foundation trust status. This is because the corporate governance regimes and accounting procedures are different for each type of body.

1.32 Where an NHS foundation trust is awarded that status from 1 April, there is no requirement to include prior year comparatives for the income and expenditure account, statement of recognised gains and losses and cash flow statement. However, the opening balance sheet should be included in the accounts and FTCs and some balance sheet notes will have to include an opening balance. These should be drawn up in accordance with the provisions of this manual.

1.33 Where an NHS foundation trust is authorised part way through a financial year, two part-year sets of accounts are required. The first part-year accounts in respect of the predecessor NHS trust should be prepared in accordance with the *NHS Trusts Manual for Accounts*. The second part-year accounts in respect of the NHS foundation trust must be prepared in accordance with this manual. Opening balances for the balance sheet and related notes as at the date of the NHS foundation trust's establishment should be disclosed but no other comparatives are required. These should be drawn up in accordance with the provisions of this Manual.

1.34 An NHS foundation trust which started part way through a financial year will show only part year comparatives against its full year results in its second year of operation. The difference in accounting periods should be explained in a narrative note to the accounts.

1.35 The closing balances of the predecessor NHS trust will be transferred to the NHS foundation trust using NHS trust accounting policies. Therefore, in accordance with proper accounting practice, these opening balances must be re-stated in accordance with NHS foundation trust accounting practice where this is materially different. In 2008/09 this could include the following instances:

- impairments which under the NHS trust rules would automatically be charged to the revaluation reserve may have to be taken to the I&E reserve under NHS foundation trust accounting policies (see paragraph 3.108);

- NHS foundation trusts are required to account for government grants in accordance with SSAP 4 and therefore do not have a government grant reserve (see paragraph 3.121);

- NHS foundation trusts are required to account for Big Lottery Fund grants in accordance with SSAP 4 (see paragraph 3.121 to 3.122); and

- any locally agreed changes in accounting policy.

1.36 The NHS foundation trust Annual Report and Accounts and consolidation report must be prepared in accordance with this manual.

Annex 1 to chapter 1 – directions

NATIONAL HEALTH SERVICE ACT 2006

DIRECTION BY MONITOR, INDEPENDENT REGULATOR OF NHS FOUNDATION TRUSTS IN RESPECT OF THE KEEPING OF ACCOUNTS AND THE PREPARATION OF ANNUAL ACCOUNTS

Monitor, the Independent Regulator of NHS Foundation Trusts, in exercise of powers conferred on it by paragraphs 24 and 25 of Schedule 7 to the National Health Service Act 2006, hereby directs that the keeping of accounts and the annual report and accounts of each NHS foundation trust shall be in the form as laid down in the annual reporting guidance for NHS foundation trusts within the *NHS Foundation Trust Financial Reporting Manual,* known as the NHS foundation trust FReM, that is in force for the relevant financial year.

Signed by authority of Monitor, the Independent Regulator of NHS Foundation Trusts

Signed:

Name: Dr. William Moyes (Chairman)

Dated: 17 January 2008

NATIONAL HEALTH SERVICE ACT 2006

DIRECTIONS BY MONITOR IN RESPECT OF NATIONAL HEALTH SERVICE FOUNDATION TRUSTS' ANNUAL ACCOUNTS

Monitor, the Independent Regulator of NHS Foundation Trusts, with the approval of HM Treasury, in exercise of powers conferred on it by paragraph 25(1) of Schedule 7 of the National Health Service Act 2006, (the 2006 Act) hereby gives the following Directions:

1. Application and interpretation

(1) These Directions apply to NHS foundation trusts in England.

(2) In these Directions "The Accounts" means:

> for an NHS foundation trust in its first operating period since authorisation, the accounts of an NHS foundation trust for the period from authorisation until 31 March; or
>
> for an NHS foundation trust in its second or subsequent operating period following authorisation, the accounts of an NHS foundation trust for the period from 1 April until 31 March.
>
> "the NHS foundation trust" means the NHS foundation trust in question.

2. Form of accounts

(1) The accounts submitted under paragraph 25 of Schedule 7 to the 2006 Act shall show, and give a true and fair view of, the NHS foundation trust's gains and losses, cash flows and financial state at the end of the financial period.

(2) The accounts shall meet the accounting requirements of the *NHS Foundation Trust Financial Reporting Manual* (FT FReM) as agreed with HM Treasury, in force for the relevant financial year.

(3) The Balance Sheet shall be signed and dated by the chief executive of the NHS foundation trust.

(4) The Statement on Internal Control shall be signed and dated by the chief executive of the NHS foundation trust.

3. Statement of accounting officer's responsibilities

(1) The statement of accounting officer's responsibilities in respect of the accounts shall be signed and dated by the chief executive of the NHS foundation trust.

4. Approval on behalf of HM Treasury

(1) These directions have been approved on behalf of HM Treasury.

Signed by the authority of Monitor, the Independent Regulator of NHS Foundation Trusts

Signed:

Name: Dr. William Moyes (Chairman)

Dated: 17 January 2008

Annex 2 to Chapter 1 – laying annual report and accounts before Parliament

Statutory requirement

NHS foundation trusts are required to lay their annual report and accounts, with any report of the auditor on them, before Parliament. NHS foundation trusts do this via the Department of Health's Parliamentary Clerk's office.

The annual report and accounts which are laid before Parliament **must include the full statutory accounts and not summary financial statements**.

Once laid before Parliament the content of the annual report and accounts cannot be changed. Guidance on the form and content of the annual report is included in chapter 4 of this manual. However, NHS foundation trusts have the discretion, following laying the document before Parliament, to publish an annual report and *summary* financial statements locally; see paragraph 1.26 for more details.

Until the annual report and accounts have been laid before Parliament, nothing can be published by the NHS foundation trust.

The process of laying documents before Parliament

There are strict requirements as to the form and layout of documents laid before Parliament. These must be followed to ensure that a document is accepted for laying.

These requirements stipulate that the document laid before Parliament must have a title page. This must state the legislation under which the document is being laid:

> "Presented to Parliament pursuant to Schedule 7, paragraph 25(4) of the National Health Service Act 2006."

This information **must** appear on the title page. The title page is page 3, which is the first page **after** the inside front cover. Please note that if this information is not on the title page, your paper may not be accepted for laying. The "Presented to Parliament" sentence must be prominent and not overshadowed by other information or compressed into very small print in the corner of the page. The other information on the title page should be restricted to the name of your organisation and the title of the document (e.g. Annual Report and Accounts 2008-09). The title page must not be combined with the contents list or any other information, nor should it contain any images.

An example of a title page is at Annex 3 to Chapter 1 of this manual.

You must check your title page meets the requirements of Parliament **before** printing the final copies. Please send a copy of the title page with your full contact details (email address and direct telephone) to Tim.Elms@dh.gsi.gov.uk. You will receive a response to confirm if the title page is acceptable and you can then proceed with printing.

When your annual report and accounts are ready to be laid, with the correct information on the title page, the following requirements must be followed.

- The Annual Report and Accounts that each NHS foundation trust lays before Parliament must be one document and in A4 format. It might be that this is formed from two electronic files but they must be presented (i.e. the hard copy must be bound) as one document. If an NHS foundation trust is getting an Annual Report and Summary Financial Statement document designed, a solution could be to bind a pdf of the annual report with a pdf of the full annual accounts and amend the title accordingly.

- Five copies of the annual report and accounts must be sent to the Parliamentary Clerk at the Department of Health. The Parliamentary Clerk will then arrange for the documents to be laid. MPs and Peers are entitled to their own free copies of all Act papers and further copies will be requested for this purpose if necessary.

- The laying copies should preferably be the final printed version. Where this is not possible, proofs can be accepted provided the text is correct, complete and will not differ in any way from the final printed version. Pictures do not have to be included in proofs, but captions to them should be.

To find out when your annual report and accounts have been laid before Parliament, visit the UK Parliament website at www.publications.parliament.uk/pa/cm/cmvote/cmvote.htm. Select a date and go to Appendix 1 for a list of papers laid that day.

Please send your annual reports and accounts for laying to:

Parliamentary Clerk's office
Department of Health
Room 301
Richmond House
79 Whitehall
London SW1A 2NS

On the package label, please clearly state the name of your NHS foundation trust. Please also include a named contact, telephone number and email address, in case of queries.

Deadlines for laying documents before Parliament

All annual reports and accounts **must** be posted to the Parliamentary Clerk by **Tuesday 7 July 2009**, to ensure enough time for laying the documents before the summer recess in July (the exact date of this in 2009 has not yet been published). Reports and accounts will be accepted and laid by the Parliamentary Clerk before this date. However, **all** reports and accounts must be posted to the Parliamentary Clerk by **7 July 2009**. It is the trust's responsibility to ensure its accounts are laid.

Process for sending documents to Monitor

As soon as your annual report and accounts have been laid, you **must** send two hard copies and one electronic copy to Monitor. The two hard copies should be posted together in one envelope marked 'FT Accounts' to:

FT Accounts
Monitor
4 Matthew Parker St
London SW1H 9NP

An electronic copy must be provided through your MARS portal, (or in case of technical difficulty, emailed to ft.accounts@monitor-nhsft.gov.uk)

These electronic files will be added to the Public Register of NHS foundation trusts on the Monitor website. Maintaining the Public Register is a statutory requirement of Monitor under the 2006 Act, and it must be kept up-to-date at all times.

The emailed files must be in pdf format. It is acceptable to send in more than one electronic document (for example, a pdf of the annual report and a pdf of the full accounts). Each pdf must not be larger than 3.5MB in size. Files larger than this cannot be placed on the public register.

Deadline for documents to be sent to Monitor

All electronic copies should arrive at Monitor by 20 July 2009. All hard copies of the annual report and accounts must be posted first class before the last post on 20 July 2009.

Annex 3 to Chapter 1 – example title page for Parliamentary Act papers

Presented to Parliament pursuant to Schedule 7, paragraph 25(4) of the National Health Service Act 2006.

[Name of NHS foundation trust]
[Title of document]

Annex 4 to Chapter 1 – example Certificate on FT Consolidation Schedules

FTC Summarisation Schedules for […] NHS Foundation Trust

Summarisation schedules numbers FTC01 to FTCxx for 2008/09 are attached.

Finance Director Certificate

1. I certify that the attached FTC schedules have been compiled and are in accordance with:
   - The financial records maintained by the NHS foundation trust; and
   - Accounting standards and policies which comply with the *NHS Foundation Trust Financial Reporting Manual* 2008-09 issued by Monitor, the Independent Regulator of NHS Foundation Trusts
2. I certify that the FTC schedules are internally consistent and that there are no validation errors*.
3. I certify that the information in the FTC schedules is consistent with the financial statements of the NHS Foundation Trust [**except for *[insert text highlighting where the schedules differ from the accounts and explain the differences]*].

[signed]

[name], Finance Director

xx June 2009

Chief Executive Certificate

1 I acknowledge the attached FTC schedules, which have been prepared and certified by the Finance Director, as the FTC schedules which the Foundation Trust is required to submit to Monitor, the Independent Regulator of NHS Foundation Trusts.

2 I have reviewed the schedules and agree the statements made by the Finance Director above.

[signed]

[name], Chief Executive

xx June 2009

** If you are unable to eliminate validation errors after discussions with your auditors and contacting Monitor then amend this accordingly.*

*** Please insert the 'except for' clause only if applicable*

[for information this revised form of certificate has been provided by the National Audit Office who audit the Consolidated Accounts of NHS Foundation Trusts]

2. Financial reporting requirements

2.1 Monitor has agreed that it will apply the principles outlined in the *Financial Reporting Manual* (*FReM*) when producing accounting guidance for NHS foundation trusts (Paragraph 1.1.3 of the *FReM*). As the *FReM* is produced for a range of central Government departments and bodies there are parts of it which are not applicable to NHS foundation trusts. This chapter therefore highlights the parts of the guidance which are applicable to NHS foundation trusts and provides additional guidance where necessary.

2.2 This manual and *FReM* follow UK Generally Accepted Accounting Practice (UK GAAP) to the extent that it is relevant and appropriate in the public sector. Although UK GAAP has no formal definition it is usually taken to mean:

- the accounting and disclosure requirements of the Companies Act 2006 and its supporting regulations;
- pronouncements by the Accounting Standards Board (ASB) – principally statements of standard accounting practice (SSAPs), financial reporting statements (FRSs) and urgent issue task force (UITF) abstracts; and
- the body of accumulated knowledge built up over time and promulgated in text books, research papers and technical journals.

2.3 NHS foundation trust accounts should be prepared under the historic cost convention modified by the revaluation of tangible fixed assets and current asset investments.

International accounting standards

2.4 EU listed companies have been required to follow international accounting standards for accounting periods beginning on or after 1 January 2005. ***In the 2008 Budget it was announced that all public bodies following the HM Treasury FReM would follow international accounting standards from 2009/10.*** Chapter 5 of this FReM sets out the key differences between UK GAAP and IFRS as it will be adopted by NHS foundation trusts.

2.5 Those preparing Annual Report and Accounts for NHS foundation trusts should keep ***all*** proposed changes **to accounting standards** under review to ensure that they understand the impact any new accounting standards may have on long term plans. Discussions on future standards should be held regularly with auditors. However, NHS foundation trusts should not make individual decision to adopt new accounting standards early as the consolidation requirements mean that NHS foundation trust accounts must be prepared on the same basis. Individual early adoption of standards for the accounts would require additional consolidation adjustments and audit work which would not be economical.

Users of the Annual Report and Accounts

2.6 The information presented in the financial statements should be adequate for the needs of the key users of the financial statements. Users include, but are not limited to:

- parliament, including relevant select committees;

- HM Treasury;
- Monitor and other regulatory bodies;
- the NHS foundation trust's board of governors;
- the NHS foundation trust's board of directors and audit committee;
- commissioning PCTs;
- patients and their carers;
- members of the NHS foundation trust; and
- the taxpayer.

2.7 The ASB's *statement of principles for financial reporting interpretation for public benefit entities* ("the ASB's interpretation") concludes that the defining class of user of public benefit entities' financial statements will be funders and financial supporters. Funders and financial supporters provide a source of cash or other resources to the entity without the incentive of a direct return on their investment. They generally provide taxation, direct grants and donations to the entity. The discussion of the user of the accounts in paragraphs 1.11 to 1.16 of the ASB's interpretation should be considered when producing the financial statements of NHS foundation trusts.

2.8 The ASB's statement of principles for financial reporting sets out the principles that the ASB believe should underlie the preparation and presentation of general purpose financial statements. The preparers of NHS foundation trust Annual Report and Accounts should familiarise themselves with these principles.

Extant accounting standards

2.9 The table below provides references to the guidance provided in HM Treasury's *FReM* on extant accounting standards. However, where there is guidance relevant to NHS foundation trusts this is provided either in the table itself or elsewhere in this manual in which case a reference is provided. The final column of the table also provides guidance on whether the requirements of the standard or the application of the standard for NHS foundation trusts have changed since 2006/07. For NHS foundation trusts in their first year of operation a table in annex 3 to this chapter provides an indication of the differences between NHS foundation trust and NHS trust accounts.

Accounting standard	FReM reference	Applicability, additional guidance and reference to relevant guidance in this manual	Revisions since 2007/08
Statements of Standard Accounting Practice (SSAP)			
4: Accounting for Government grants	5.2.42 – 5.2.46	NHS foundation trusts are not required to follow the amendments to SSAP 4 set out in *FReM*. They are not therefore required to maintain a Government grant reserve but are required to show capital grants as deferred income. FReM (paragraph 5.2.13) states that Big Lottery grants should be treated as donated asset rather than government grants. From 2005/06 onwards, Monitor concluded that Big Lottery grants meet the SSAP 4 definition of government grants and therefore should be treated as such in the accounts. See paragraphs 3.121 to 3.123 of this manual	No change

Accounting standard	FReM reference	Applicability, additional guidance and reference to relevant guidance in this manual	Revisions since 2007/08
5: Accounting for VAT	4.4.6-4.4.8	Fully applicable	No change
9: Stocks and long term contracts	6.3.1-6.3.4	Fully applicable	No change
13: Accounting for research and development	5.3.6-5.3.8	Fully applicable but development costs should only be capitalised where there is a clearly defined project for which expenditure can be separately identified and which, when completed, will result in an asset of the NHS foundation trust being brought into use or a commercially viable project for which the NHS foundation trust retains the profits. Internal costs should not be capitalised when they relate to activities which can only be carried out in house. Contracts with companies to undertake clinical research and clinical trials should be accounted for in accordance with SSAP 9 and application note G to FRS 5	No change
19: Investment properties	5.2.24 – 5.2.25	Fully applicable	No change
21: Accounting for leases	5.2.30- 5.2.31	Fully applicable	No change
25: Segmental reporting	7.4.30 -7.4.32	Fully applicable	No change
Financial Reporting Standard (FRSs)			
1 (revised): Cash flow statements	*FReM* guidance is not applicable to NHS foundation trusts (see 7.4.24)	Fully applicable	No change
2: Accounting for subsidiary undertakings	The guidance in chapter 2 of *FReM* relates to departmental boundaries and is therefore not applicable to NHS foundation trusts (see 7.4.1).	Where NHS foundation trusts acquire subsidiary companies ***or entities which fall outside of the WGA boundary*** this standard is fully applicable	No change
3: Reporting financial performance	7.4.15 – 7.4.18	Fully applicable	No change
5: Reporting the substance of transactions	*FReM* guidance in chapter 2 is not applicable to	The principles of FRS 5 are applicable to NHS foundation trusts. Application note F of FRS 5 on PFI	No change

Accounting standard	FReM reference	Applicability, additional guidance and reference to relevant guidance in this manual	Revisions since 2007/08
	NHS foundation trust's circumstances. However, other guidance is: Application note G to FRS 5 4.2.16 – 4.2.17 Application note F to FRS 5 5.2.26 – 5.2.29	contracts is relevant to NHS foundation trusts but should be followed in conjunction with HM Treasury technical note 1 (revised) "How to account for PFI transactions". Application note G of FRS 5 on revenue recognition is relevant to NHS foundation trusts. Additional guidance on the relevance of this application note to income for partially completed spells is given in paragraph 3.42	
6: Acquisitions and mergers	5.4.2-5.4.5	The FReM includes guidance on business combinations and transfers of services involving NHS foundation trusts	No change
7: Fair values in acquisition accounting	5.4.6 – 5.4.8	The FReM includes guidance on business combinations and transfers of services involving NHS foundation trusts	No change
8: Related party disclosures	7.4.61 – 7.4.63	Fully applicable	No change
9: Associates and joint ventures	*FReM* guidance in chapter 2 is not applicable to NHS foundation trust's circumstances	Where NHS foundation trusts have entered into associations or joint ventures then FRS 9 is fully applicable. Traditionally, NHS bodies have entered into pooled budget arrangements which are joint arrangements which are not entities (JANEs) under FRS 9. There is no UK GAAP requirement for the memorandum account required by the Health Act to be included in the statutory accounts of any of the members of the JANE. NHS foundation trusts can therefore choose whether or not to produce this information. The approach adopted must be agreed with the NHS foundation trust's auditors	No change
10: Goodwill and intangible assets	5.3.3-5.3.5	Fully applicable	No change
11: Impairment of fixed assets and goodwill	5.2.32 – 5.2.41 Paragraphs 5.2.37 to 5.2.41 of the HM Treasury FReM discuss the funding of impairments which is not directly applicable to	Fully applicable to NHS foundation trusts, however, paragraph 5.2.35 of the FReM allows bodies to hold a negative revaluation reserve in certain circumstances. NHS foundation trusts are required to comply with FRS 11 in full and will therefore charge impairments to the I&E account where there is no balance on the revaluation reserve relating to the impaired asset unless the particular circumstances set out in FRS 15 are met (see paragraph	No change

Accounting standard	FReM reference	Applicability, additional guidance and reference to relevant guidance in this manual	Revisions since 2007/08
	NHS foundation trusts	3.107).	
12: Provisions, contingent assets and contingent liabilities	6.6.2 – 6.6.9	FRS 12 is fully applicable to NHS foundation trusts. The only additional requirement for NHS foundation trusts is that where the time value of money is material the provision must be discounted using the real discount rate set by HM Treasury. From 1 April 2005 this rate is 2.2%	No change
15: Tangible fixed assets	5.2.2 – 5.2.33	FRS 15 is fully applicable to NHS foundation trusts. Further guidance is to be found in chapter 3. NHS foundation trusts will not hold infrastructure assets. Therefore, these sections of *FREM* are not applicable to NHS foundation trusts. If NHS foundation trusts hold heritage assets then the relevant chapters of FReM applies. This manual departs from *FREM* in the following instances: 5.2.5a - Gains on assets financed by Government grant are credited to the revaluation reserve and transferred to the I&E reserve on disposal of the asset in the same way that they would be accounted for if they were purchased. *FReM* requires such gains to be credited to the Government grant reserve but NHS foundation trusts do not hold such reserves. 5.2.5b – losses on revaluation will be accounted for in accordance with the requirements of FRS 11. 5.2.6c – NHS foundation trusts should not subject land and building assets to indexation each and every year. 5.2.7a – NHS foundation trusts should follow the requirements of FRS 15 and cannot opt to have a quinquennial review with annual indexation for property assets as detailed in the Government FReM. 5.2.17 – NHS foundation trusts are not required to transfer assets to other public sector bodies for nil consideration. These transfers should be done as any other sale or purchase of fixed assets.	No change

Accounting standard	FReM reference	Applicability, additional guidance and reference to relevant guidance in this manual	Revisions since 2007/08
16: Current tax	4.4.2-4.4.3	Fully applicable if NHS foundation trusts are subject to the tax regime. Guidance in relation to Corporation Tax and NHS foundation trusts can be found on the HMR&C website http://www.hmrc.gov.uk/specialist/ct-nhs-guidance.pdf	No change
17: Retirement benefits	6.5.4 – 6.5.5 Chapter 8	Most NHS foundation trust staff will be members of the NHS pension scheme. This is a defined benefit scheme but the assets and liabilities of the scheme cannot be attributed to the member bodies of that scheme. NHS foundation trusts therefore account for transactions with the NHS pension scheme as if it were a defined contribution scheme. NHS foundation trusts therefore have to disclose the fact that the scheme is a defined benefit scheme which prepares its own scheme statements and any information about the existence of the surplus or deficit and the implications of that surplus or deficit on the employer. If any NHS foundation trust is a member body of any other pension scheme, for example, a local authority superannuation scheme then it must apply FRS 17 in full to transactions with that scheme	No change
18: Accounting policies	2.3.1 - 2.3.4	This standard is fully applicable to NHS foundation trusts. Where it is necessary to choose between accounting policies, the standard requires entities to select the most appropriate in order to provide a true and fair view. NHS foundation trusts should firstly consider whether this manual requires that all NHS foundation trusts adopt a particular policy. Where there is no guidance in the manual or *FReM* then the NHS foundation trust should follow the requirements of the standard. Additional guidance in relation to: • changes in accounting policy; and • going concern, can be found in chapters 3 and 4	No change
19: Deferred tax	4.4.4-4.4.5	Fully applicable if NHS foundation trusts are subject to the tax regime	No change
20 (IFRS2): Share based payment	4.3.1	Applicable in principle. Not directly relevant to NHS foundation trusts as they do not have equity share capital. It	No change

Accounting standard	FReM reference	Applicability, additional guidance and reference to relevant guidance in this manual	Revisions since 2007/08
		would apply, however, where a NHS foundation trust has a subsidiary company which has such transactions and group accounts are prepared	
21 (ISA 10): Events after the balance sheet date	7.4.21 – 7.4.23	Fully applicable For those NHS foundation trusts which become NHS foundation trusts mid-year, the part year I&E account of the NHS foundation trust should reflect only the dividend payable in the period that it was an NHS foundation trust	No change
22 (IAS 33): Earnings per share	4.3.1	The standard is only mandatory for entities which have shares that are, or are about to be, traded publicly. It is not directly relevant to NHS foundation trusts. It would apply to any listed subsidiaries that an NHS foundation trust may have, but the standard's requirements would be met by disclosures in that entity's own statutory accounts	No change
23 (IAS 21): The effects of changes in foreign exchange rates	4.3.10 to 4.3.13	Fully applicable in principle but in practice NHS foundation trusts are unlikely to undertake transactions in any currency other than sterling	No change
24 (IAS 29): Financial reporting in hyperinflationary economies	7.4.2	Applicable in principle but is unlikely to apply in practice	No change
25 (IAS 32): Financial instruments: Disclosure and presentation	9.1.3 to 9.1.5	<u>Presentation</u> Fully applicable PDC is not an equity instrument under FRS 25 and should be presented as a form of financing in the balance sheet. Dividends on PDC should be presented in the I&E account	No change
26 (IAS 39): Financial instruments: measurement	9.1.7 to 9.1.9	Fully applicable	No change
27: Life assurance		Not applicable	No change
28: Corresponding amounts	7.4.12 – 7.4.14	Fully applicable	No change
29 (IFRS 7): Financial instruments: disclosure	9.1.10 to 9.1.11	Fully applicable	No change
Reporting Statement			
Operating and	7.2.9 – 7.2.19	Fully applicable	No change

Accounting standard	FReM reference	Applicability, additional guidance and reference to relevant guidance in this manual	Revisions since 2007/08
financial review		In November 2005, this standard was re-designated a reporting statement. Its impact is discussed in chapter 4	
Urgent Issues Task Force (UITF) Abstracts			
4: Presentation of long term debtors in current assets	6.4.2-6.4.3	Fully applicable	No change
5: Transfers from current assets to fixed assets	6.4.4 – 6.4.6	Fully applicable	No change
9: Accounting for operations in hyper-inflationary economies		Applicable in principle, but only if an NHS foundation trust has a foreign operation in a hyper-inflationary economy	No change in substance
11: Capital instruments: issuer call options		Applicable in principle. Not relevant to an NHS foundation trust, but might be to a subsidiary company where group accounts are prepared	No change in substance
15: Disclosure of substantial acquisitions		Not applicable. The UITF clarifies a provision in FRS 6 that applies to listed entities only. NHS foundation trusts are covered by a separate provision in the FRS	No change in substance
19: Tax on gains and losses on foreign currency borrowings that hedge an investment in a foreign enterprise		Applicable in principle if an NHS foundation trust has an investment in a foreign operation	No change for most NHS foundation trusts who do not have operations outside of the UK
21: Proposed introduction of the euro	4.3.12 – 4.3.14	Fully applicable	No change
22: The acquisition of a Lloyd's business		Not applicable	No change
23: Application of the transitional rules in FRS 15		No longer applicable	No change
24: Accounting for start up costs	5.2.47-5.2.48	Fully applicable	No change
25: National Insurance contributions on share option gains		Not applicable to NHS foundation trusts. Could be applicable to a subsidiary company that provides share options	No change
26: Barter transactions for advertising	4.3.15 – 4.3.17	Fully applicable	No change
27: Revisions to	5.3.9-5.3.10	Fully applicable	No change

Accounting standard	FReM reference	Applicability, additional guidance and reference to relevant guidance in this manual	Revisions since 2007/08
estimates of the useful economic life of goodwill and intangible assets			
28: Operating lease incentives	5.2.49-5.2.50	Fully applicable	No change
29: Website development costs	5.2.51-5.2.53	Fully applicable. However, as NHS foundation trusts cannot deliver healthcare via the internet it is not expected that capitalisation of such costs will be allowable within the requirements of this abstract	No change
31: Exchanges of business or other non-monetary assets for an interest in a subsidiary, joint venture or associate	5.2.52- 5.2.56	Fully applicable	No change
32: Employee benefit trusts and other intermediate payment arrangements		Applicable in principle	No change
34: Pre-contract costs	4.3.18-4.3.19	Fully applicable	No change
35: Death in service and incapacity benefits	6.5.6-.6.5.7	Fully applicable	No change
36: Contracts for sales of capacity		Not applicable	No change
38: Accounting for ESOP trusts		Applicable in principle	No change
39: Members' shares in co-operative entities and similar instruments		Not applicable	No change
40: Revenue recognition and service contracts	4.2.18 – 4.2.21	Fully applicable Income receivable for partially completed patient spells should be accounted for as accrued income. See paragraphs 3.42 to 3.44	No change
41: Scope of FRS 20		Applicable in principle but see comments on FRS 20 above	No change
42: Reassessment of embedded derivatives		Applicable in principle	Applicable in principle as FRS 26 is now applicable
43: The interpretation of		Not relevant	No change

Accounting standard	FReM reference	Applicability, additional guidance and reference to relevant guidance in this manual	Revisions since 2007/08
equivalence for the purposes of section 228A of the Companies Act 1985			
44: Group and treasury share transactions		Not applicable to NHS foundation trusts. Could be applicable to a subsidiary company that provides share options	No change
45: Liabilities arising from Participating in a Specific Market Waste Electrical and Electronic Equipment		Not relevant	No change

Annex 1 to chapter 2

Departures from HM Treasury's *Financial Reporting Manual* (*FReM*)

HM Treasury accept that the following are fundamental differences between NHS foundation trusts and Government departments rendering some requirements in the *Financial Reporting Manual* (*FReM*) irrelevant to NHS foundation trusts.

Government departments	NHS foundation trusts
On-vote	Off-vote
Appropriations in Aid (AinA) apply	AinA do not apply.
Have revenue and capital resource limits	NHS foundation trusts do not have revenue or capital resource limits. Individual NHS foundation trusts are required to comply with the *Prudential Borrowing Code.*
Have cash limits	NHS foundation trusts are required to comply with the *Prudential Borrowing Code* but do not have cash limits.
Have an Operating Cost Statement	Have an income and expenditure account.
Have a General Fund	Have Public Dividend Capital and pay dividends.
Have a statement of recognised gains and losses	Have a statement of total recognised gains and losses.
Have statement of parliamentary supply and associated notes	Do not have statement of parliamentary supply nor associated notes
Ministers directly involved	Ministers not directly involved.
Departments do not present their reports and accounts at public meetings	The annual report and financial statements of individual NHS foundation trusts are laid before Parliament and presented at a public meeting.

Largely due to their different structure and role compared to Government departments, the following are approved accounting practices in NHS foundation trusts that differ from those in HM Treasury's *FReM*:

HM Treasury's FReM requirement	NHS foundation trust accounting
Income and expenditure are recorded as administration and programme (para 4.3.4)	NHS foundation trust income is analysed by source and expenditure analysed subjectively
Cost of capital is a notional cost (para 4.5.1)	NHS foundation trusts do not have notional costs
Losses on revaluation can be taken to the statement of recognised gains and losses where the recoverable amount is greater than the revalued amount in accordance with the manual (para 5.2.5 and 5.2.35b)	Losses on revaluation can only be taken to the statement of recognised gains and losses where the requirements of FRS 15 and 11 are met.
The Government Grant reserve is revalued in line with the assets which have been funded by grant (para 5.2.5, 5.2.44b)	Government grants are held as deferred income in accordance with SSAP 4.
Research and development expenditure should be disclosed in accordance with SSAP 13 (para 5.3.6)	Separate disclosure is required but in some instances cannot be separated from the costs of patient care and is therefore not separately disclosed.

HM Treasury’s FReM requirement	NHS foundation trust accounting
FReM (paragraph 5.2.13) states that Big Lottery grants should be treated as donated assets rather than government grants	NHS foundation trusts are required to account for Big Lottery grants (and grants from its predecessor body, the New Opportunities fund) as government grants where the grant has been received by the NHS foundation trust itself.

Annex 2 to chapter 2

Main differences between NHS trust and NHS foundation trust accounts

This table is intended to assist new NHS foundation trusts to identify the main differences between the accounts they prepared as NHS trusts and those they will be required to prepare going forward. The table highlights major differences between NHS foundation trusts and NHS trusts and major changes which have been made to the NHS foundation trust FReM since its initial production. Where notes to NHS trust accounts do not differ from NHS foundation trusts they are not listed in this table.

NHS foundation trusts should refer to the detailed guidance in Chapter 3 for further information.

Main statements	
Income and expenditure account	The NHS trust pro forma does not take into account subsidiary, joint ventures or associate arrangements or taxation which may have to be paid by NHS foundation trusts. This comment applies to all of the accounts and notes.
Balance sheet	NHS foundation trusts are required to update their fixed asset valuations in accordance with FRS 15 rather than by the use of indexation and five yearly valuations (see paragraphs 3.93 to 3.111) NHS foundation trusts will not have a government grant reserve but may have government grant deferred in creditors (see paragraph 3.121 onwards) NHS foundation trusts will include any Big Lottery grant payments as government grants rather than donated assets (see paragraph 3.121).
Statement of total recognised gains and losses	NHS foundation trusts should include the line 'reductions in the donated asset reserve due to the depreciation, impairment and disposal of donated assets' which is omitted from the NHS trust accounts.
Cash flow statement	Additional sections may need to be added to recognise the different financing arrangements for NHS foundation trusts.
Notes to the accounts	
Accounting policies	This note will have to be adapted to suit the policies adopted by the NHS foundation trust. An example checklist is appended to chapter 3 but this must be tailored by each body for their own circumstances. The accounting policies in relation to: • valuation of fixed assets; • charging of impairments; • mergers and acquisitions; and • accounting for Government grants and Big Lottery payments are different to the policies adopted by NHS trusts under direction from the Secretary of State.
Segmental reporting	NHS foundation trusts may wish to show their non-core healthcare services as segments. If the NHS foundation trust does not have any segments to report, in accordance with the requirements of SSAP 25, this note may be omitted from the accounts.
Income from activities	The analysis of income may be different as NHS foundation trusts may chose to analyse income by activity rather than source as this is the requirement for the quarterly returns to Monitor. (From 2007-08 an income analysis appropriate for Mental Health foundation trusts was introduced in FTC forms) NHS foundation trusts are also required to disclose their income from mandatory and non-mandatory services. NHS foundation trusts recognise income in relation to partially completed spells where it is appropriate in relation to the contract.
Other operating income	NHS foundation trusts also have to include a note to disclose private patient income and the cap on such income
Staff costs and numbers	This note should be compiled on an accruals basis and should be able to be reconciled to staff costs reflected in the operating expense note.

Main statements	
Better payment practice code	This note is not required for NHS foundation trusts although it can be included if the NHS foundation trust considers it best practice. It should be included in the Annual Report of the NHS foundation trust if it is not included in the accounts.
Interest payable and similar charges	NHS foundation trusts will also have to disclose their performance against the *Prudential Borrowing Code*.
Tangible fixed assets	The arrangements for the valuation tangible fixed assets will be different for NHS foundation trusts as assets are not indexed annually but revalued every 5 years with an interim valuation every 3 years. NHS foundation trusts should disclose all tangible fixed assets on a gross basis with accumulated depreciation. The opening accumulated depreciation balance will be the amount brought forward from the previous year other than in the year of a revaluation. NHS trusts are required to reset brought forward accumulated depreciation to nil on some occasions.
Leases	The disclosures in relation to leases remain the same for NHS foundation trusts as for NHS trusts. However, NHS foundation trusts should comply with SSAP 21 when calculating the interest rate implicit in a lease and should not use proxy rates (as allowed in the DH Capital Accounting Manual).
Debtors	Income in relation to partially completed spells is recognised by NHS foundation trusts in accordance with application note G to FRS 5. (i.e. within accrued income)
Creditors	NHS foundation trusts show government grants (including Big Lottery fund grants) as deferred income
Movements on reserves	As NHS foundation trusts are required to charge any impairments on bringing an asset into use to the I&E account it is not expected that an NHS foundation trust would have a negative revaluation reserve. NHS foundation trusts do not have a government grant reserve
Notes to the cash flow statement	Note 18.3 is not necessary in the NHS foundation trust accounts.
Movements in PDC	Not required for NHS foundation trusts.
Financial performance	The standard NHS Trust note is not required but it should be replaced by a statement of performance against the NHS foundation trust's own financial targets, for example, private patient income, the prudential borrowing limit.
Pooled budget arrangements	Not required by the *FReM* or by UK GAAP and therefore not necessary for NHS foundation trusts unless the pooled budget agreement specifies that the memorandum account will be included in the accounts.

3. Financial statements

Introduction

3.1. NHS foundation trusts have discretion over the form of financial statements that they consider to be most appropriate to meet their own reporting needs, as long as the requirements of UK GAAP, as supplemented or amended by this manual, are met. A well-presented set of accounts will include all of the information required by the reader of the accounts to understand the financial position of the NHS foundation trust for the period. It will include only information relevant to its situation and will be appropriately cross referenced.

3.2. NHS foundation trusts are, however, required to complete foundation trust consolidation reports (FTC forms), which need to be prepared on a consistent basis in order to support the preparation of consolidated accounts of NHS foundation trusts.

3.3. This chapter provides guidance on:

- the application of UK GAAP to NHS foundation trusts and additional disclosures, beyond the requirements of UK GAAP, that are mandatory for all NHS foundation trusts in their financial statements; and
- the completion of FTC forms.

3.4. This chapter does not provide guidance on UK GAAP where there are no specific application issues for NHS foundation trusts. It is therefore essential that NHS foundation trusts review relevant accounting requirements when preparing their financial statements.

3.5. NHS foundation trusts must, at a minimum, ensure that they include in their accounts an income and expenditure account, a balance sheet, a statement of total recognised gains and losses and a cash flow statement. These are the four primary statements. NHS foundation trusts must include the headings provided in the FTC forms for all the primary statements. However, there is no requirement to include in the accounts notes with nil entries or lines in notes which are not applicable to that individual NHS foundation trust.

3.6. NHS foundation trusts must also include notes to the accounts corresponding to those of notes 2 to 25.3 inclusive of the FTC forms (FTC05 to FTC19A inclusive). The content of these notes, however, need not follow the format of the FTC forms, as long as the NHS foundation trust complies with UK GAAP and the additional requirements of this manual. The FTC forms will have to be consistent with the accounts. This means that they should be prepared using the same accounting policies and the same amounts should be disclosed in both the accounts and FTCs. The only difference between the accounts and FTCs will be where an NHS foundation trust has an acquired or discontinued operation which has been transferred from or to another public sector body. In the accounts this will be disclosed as discontinued or acquired but in the FTC should be shown as continuing (see paragraph 3.39).

3.7. Appendices to this manual contain a set of example accounting policies that could be used for an NHS foundation trust's financial statements (annex 1a).

Materiality

3.8. The Accounting Standards Board's (ASB's) foreword to accounting standards states that standards need not be applied to immaterial items. The process of preparing accounts gives rise to two types of materiality judgements:

- whether an item needs to be disclosed; and/or
- what margin of error, if any, is acceptable in the amount attributed to an item.

3.9. The ASB's statement of principles for financial reporting (3.28-32) defines and explains materiality as a threshold quality which is demanded of all information given in the financial statements and provides further information on the concept of materiality if this should be required.

Group accounts

3.10. NHS foundation trusts with subsidiary companies should note that they will be required to produce separate sets of accounts for their subsidiaries, compliant with UK GAAP and the Companies Acts, and will also need to produce consolidated group accounts.

3.11. NHS foundation trusts should apply the definition of a parent undertaking and subsidiary undertaking as set out in paragraph 14 of FRS 2.

3.12. Whether or not a company is a subsidiary is determined by the answers to the following questions:

- who holds the majority of the voting rights in the undertaking?
- who has the right to appoint or remove directors holding a majority of the voting rights at meetings of the board?
- who has the right to exercise dominant influence over the undertaking?
- who is a member of the undertaking and controls the majority of the voting rights in the undertaking?
- who has the power to exercise or actually exercises dominant influence over the undertaking?
- is the undertaking managed on a unified basis with the undertaking?

Mergers and acquisitions

Transfer of the business or part of the business of another WGA entity to an NHS foundation trust

3.13. ***Where an NHS foundation trust combines with another entity within the Whole of Government Accounts boundary (including other NHS foundation trusts and NHS trusts) this represents a 'machinery of government change' regardless of the mechanism used to effect the combination e.g. statutory merger or purchase of the business.*** Such a transaction falls within the 'Group Reconstruction' provisions of FRS 6 – as interpreted by HM Treasury's FReM - and shall be accounted for using merger accounting. This applies to all such transactions, even where the substance may be closer to that of an acquisition of the NHS trust by the NHS foundation trust

3.14. In the NHS foundation trust's financial statements the results of the two entities will be aggregated as if they had always been combined. In summary this means:

- restating the prior year figures of the NHS foundation trust to include the transactions and balances of the NHS trust.
- aligning the accounting policies of the NHS trust with those of the NHS foundation trust with effect from the beginning of the prior year. Any net adjustment is made to the prior year opening reserves.

3.15. Where the purchase has been funded by cash-backed PDC issue to the NHS foundation trust by the Secretary of State, any difference between the consideration given and the PDC of the NHS trust should be treated as a merger reserve in the accounts of the NHS foundation trust:

- where the consideration given exceeds the PDC of the NHS trust, this will give rise to a negative merger reserve, which should remain on the balance sheet.
- where the consideration given is less than the NHS trust's PDC, a positive merger reserve will be generated. This positive reserve is similar in substance to a merger reserve under FRS 6, and can be released to the I&E reserve in a manner similar to a revaluation reserve (as per Paragraph 2.11 of ICAEW Tech 01/08 'Guidance on the determination of realised profits and losses in the context of distributions under the Companies Act 1985'). Where the

total of the merger reserve is equal to or greater than the revaluation reserve of the NHS trust at the date of merger, the amount to be released in this manner when a fixed asset is disposed of will be limited to an amount equal to the revaluation reserve balance attributable to that asset at the date of the merger. Where the merger reserve is less than the revaluation reserve of the NHS Trust at the date of merger, the amount to be released will be proportionately lower.

Disclosures

3.16. The following disclosures are required by the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 (SI 2008/410) where merger accounting is adopted:

- the name of the NHS trust(s) merging with the NHS foundation trust;
- the fact that merger accounting had been adopted for the transaction;
- the effective date of the merger;
- the composition and fair value of the consideration given by the NHS foundation trust;
- an explanation of any significant adjustments made to the assets and liabilities of the NHS trust for example, to eliminate intra-entity balances and to align accounting policies, and the net adjustment to opening consolidated reserves.

3.17. FRS 6 requires certain further disclosures where merger accounting is adopted, but which are not mandatory for group reconstructions. However, in the interests of accountability, Monitor has decided that these disclosures should nevertheless be made unless, in management's view, the cost of obtaining the information significantly outweighs the benefits of providing it. These disclosures are:

- the aggregate book value of the net assets of each party to the merger at the date of merger;
- an analysis of the principal components of the current year's income and expenditure account and Statement of Total Recognised Gains and Losses (STRGL) into:
  - o post-merger amounts for the combined NHS foundation trust;
  - o pre-merger amounts for each of the NHS foundation trust and NHS trust;

  NB where the merger occurs on 1 April this disclosure would not be necessary
- an analysis of the principal components of the previous year's income and expenditure account and STRGL between the FT and the NHS trust.

3.18. The above analyses should show as a minimum, for the Income and Expenditure Account:

- Operating Income;
- Operating Surplus or Deficit
- Exceptional Items
- Interest
- Taxation
- PDC dividends payable

For the Statement of Total Recognised Gains and Losses:

- Surplus or Deficit for the year
- Exchange gains and losses taken direct to reserves
- Revaluation surpluses or deficits
- Total recognised gains or losses

3.19. Where the substance of the transaction is effectively that the NHS foundation trust takes over the activities of an NHS trust, the disclosures required under acquisition accounting should also be made. In practice, those disclosures above meet most of these requirements with the exception of the disclosure of book values and fair values of the assets and liabilities of the acquired NHS trust. However, since merger accounting is being applied, a fair value exercise may not have been undertaken. Consequently, the fair value disclosures are not required but disclosure should be made of the existing book values of each class of assets and liabilities of the NHS trust at the date of the merger.

Transfer of part of the business of an NHS foundation trust to another body within the WGA boundary

3.20. ***These transactions also meet the definition of a 'machinery of government change' and therefore merger accounting should be used. The assets and liabilities and reserve balances (where applicable e.g. revaluation reserve) should be de-recognised by the NHS foundation trust and comparative disclosures restated to reflect the position as if the activities had never been part of the NHS foundation trust's operations.***

Purchase of the business of a private sector entity by an NHS foundation trust

3.21. Where an NHS foundation trust purchases a non-NHS entity then the purchase should be accounted for in accordance with FRS 6. Such a transaction is likely to be accounted for as an acquisition by the NHS foundation trust, in which case a fair value exercise will need to be undertaken in accordance with FRS 7 and any goodwill accounted for in accordance with FRS 10.

Selection of accounting policies

3.22. An NHS foundation trust must choose the accounting policies that it judges to be most appropriate to its particular circumstances for the purpose of giving a true and fair view. Annex 1 to this chapter includes model accounting policies but these must be reviewed by each NHS foundation trust to ensure that they are the most appropriate to its particular circumstances.

3.23. The ASB's FRS 18 is a particularly important document to consider in this context. It states that accounting policies are:

"Those principles, bases, conventions, rules and practices applied by an entity that specify how the effects of transactions and other events are to be reflected in its financial statements through

- recognising;
- selecting measurement bases for, and
- presenting

assets, liabilities, gains, losses and changes to shareholders' funds."

Prior period adjustments

3.24. Changes in accounting policy will require an adjustment to prior period financial statements under FRS 3.

3.25. FRS 3 requires that prior period adjustments should be accounted for by restating the corresponding primary statements and notes for the preceding period. The column headings should be identified "restated" in the accounts but not in the FTCs. Opening balance of reserves should be adjusted accordingly so that the opening position of the current year reflects the new accounting policy.

3.26. Any difference between the reported financial results and the adjusted financial results should be reported in a note to the accounts and the reason for the difference explained. That note should be replicated in the free text sheets of the FTCs.

3.27. In the Statement of Total Recognised Gains and Losses (STRGL) the cumulative effect of the adjustments should also be noted at the foot of the current year column.

3.28. Where an NHS foundation trust has a change in accounting policy the free text FTC form should set out:

- all of the affected pre-adjustment 2007/08 balances;
- all of the adjusted 2007/08 balances; and
- an explanation of the movement between them.

An example has been prepared as part of Annex 4 to this chapter which is a worked example of the change in accounting policy for Big Lottery grants.

3.29. Where an NHS foundation trust has to make a prior period adjustment (for any reason other than an adjustment required by the NHS foundation trust FReM), they were required to inform Monitor so that the appropriate information could be collected for consolidation. There is no longer any need to inform Monitor of this change as the FTCs have been amended to collect the required data.

Going concern

3.30. FRS 18 requires directors to assess, as part of the accounts preparation process, whether there are significant doubts in relation to the entity's ability to continue as a going concern. NHS foundation trusts should base their analysis on their annual plan and compliance framework submissions. The depth of the assessment will be based on the assessed financial standing of the entity – a more in depth assessment will be required in relation to an NHS foundation trust in financial difficulties.

3.31. Where there are significant doubts as to the entity's ability to continue as a going concern then these should be disclosed in the accounts. However, in accordance with paragraph 21 of FRS 18 the accounts should still be prepared on the going concern basis unless:

- the entity has been liquidated or has ceased trading; or
- where the directors either intend to liquidate the entity or to cease trading, or have no realistic alternative but to do so.

Income and expenditure account

3.32. Generally, income and expenditure should be recorded gross and not netted off. The exception to this is where a member of staff is employed jointly by the NHS foundation trust and another NHS body then only the element of the salary relating to the NHS foundation trust should be recorded as expenditure. However, staff seconded to another organisation but still employed by the NHS foundation trust should be accounted for on a gross basis so that their costs are included in staff costs and the re-charge to the other organisation is shown as income. This is because the seconded staff member is still an employee of the NHS foundation trust, whereas the jointly employed member of staff works on a part-time basis for the NHS foundation trust and the recharge arrangement is simply an administrative arrangement.

3.33. Where an NHS foundation trust works with another NHS body on an agency basis, for example, processing invoices or managing a lease car scheme, then the transactions it processes on behalf of the other body do not need to be reflected in the NHS foundation trust accounts. Where the NHS foundation trust is paid for providing the service then that payment should be reflected in its accounts.

Intra NHS agreement of balances

3.34. NHS foundation trusts are encouraged to participate in the NHS wide agreement of balances exercise but participation is not mandatory. However NHS foundation trusts are required to give sufficient audit evidence for the carrying value of all balances, through either third party confirmation or internal analysis.

3.35. The FTCs do not include a line for disagreements between NHS bodies as Monitor would prefer the amounts shown as balances with PCTs and income and expenditure relating to PCTs to be the amounts that the NHS foundation trust considers to be the true amount relating to that PCT.

3.36. Where the NHS foundation trust knows that this is a different amount to that agreed with the PCT or that which the PCT will be showing in its accounts, any difference must be supported by sufficient evidence which is acceptable to the NHS foundation trust's auditors. Part of the difference may be due to different accounting treatment in relation to recharges (see paragraph 3.32). Where the NHS foundation trust is aware that the other body has included a different amount from them in their summarisation schedules this fact should be stated in the free text FTC along with the reason for the difference. This may avoid NHS foundation trusts being asked additional questions during the consolidation process.

3.37. A similar logic is applicable to income and expenditure with other NHS bodies, NHS foundation trusts are encouraged to participate in the exercise but it is not mandatory, NHS foundation trusts will need to give sufficient audit evidence to justify the total level of income and expenditure.

Acquisitions and discontinued operations

3.38. NHS foundation trusts should review their activities against FRS 3 to assess whether they are required to make disclosures in relation to acquisitions and discontinued operations.

3.39. Such disclosures in the financial statements may have to be adjusted in the FTC forms. For the purposes of consolidation, acquisitions and discontinued operations that are acquired from or disposed of to other bodies within the scope of *Whole of Government Accounts* should be treated as though they were continuing operations within the FTC forms.

3.40. For the purposes of the FTC forms, acquisitions from and discontinued operations disposed of to bodies outside the scope of *Whole of Government Accounts*, or discontinued operations that cease entirely, should also be treated as continuing operations within the FTC forms, but should be disclosed on the free text sheet, providing the details required by FRS 3. This will allow Monitor to take account of these movements on consolidation.

Income recognition

3.41. NHS foundation trusts are required to follow Application Note G of FRS 5 in relation to revenue recognition of donations. However, where donations are received in order to finance the purchase of fixed assets the accounting treatment set out in paragraphs 3.129 to 3.139 should be followed.

Partially completed spells

3.42. NHS foundation trusts enter into contracts for services based on a model contract. The suggested contract is three years in length but actual contracts could be longer or shorter. The key elements of the model contract are that:

- the NHS foundation trust have to provide the services or services needed by each patient who is referred or presents to the provider for healthcare or treatment in accordance with the contract;
- the NHS foundation trust can only refuse to treat patients in limited circumstances based on clinical needs or patient behaviour;
- even when treatment is refused the NHS foundation trust will be paid for activity undertaken up to the point that the treatment is refused and the patient discharged unless and to the extent that such an activity requires rectification by another provider; and
- the commissioner will pay the NHS foundation trust for activity delivered based on prices set out in the contract.

3.43. Therefore, if the NHS foundation trust can demonstrate that it is certain to receive the income for a treatment or spell once the patient is admitted and treatment begins then the income for that treatment or spell can start to be recognised at the time of admission and treatment starting. Costs of treatment are then expensed as incurred. Income relating to those spells which are partially completed at the financial year end should be apportioned across the financial years on a pro rata basis. This basis may be the expected or actual length of stay or may be based on the costs incurred over the length of the treatment. It is for the NHS foundation trust to establish a suitable pro rata basis, and where material, disclose this in the accounting policy note.

3.44. NHS foundation trusts should examine the terms of the contracts that they have entered into to determine exactly how revenue should be recognised in accordance with FRS 5 and UITF 40.

Income from activities

3.45. Income should be classified as income from activities when it is earned under contracts with NHS bodies and others for the provision of healthcare services to the NHS foundation trust's patients. Income from non-patient-care services should be classified as "other operating income". Income arising from the activities of subsidiaries consolidated into the accounts of the NHS foundation trust should be classified on the same basis, regardless of how is it classified in the accounts of the subsidiary.

3.46. Where "other income" is material additional disclosure should be made in the accounts as to its source.

Operating expenses – staff and directors' costs

3.47. The operating cost note should include separate lines disclosing staff costs and directors' costs. Only the costs relating to executive and non-executive directors should be included in the directors' costs line. All other staff costs should be included in the staff costs line.

3.48. The amounts disclosed should be the total paid or payable in the year to directors (executive and non-executive) or staff in respect of their services to the NHS foundation trust. The figure excludes redundancy and injury benefit costs but includes:

- employer's National Insurance contributions (NIC);
- employer's pension costs; and
- early retirement costs, whether lump sum or otherwise.

3.49. Redundancy costs and injury benefit costs should be included in "other expenses". If material, then separate disclosure of the nature of these payments should be made.

3.50. The reconciliation of this disclosure with the staff costs note is one of the main areas of difficulty when consolidating all NHS foundation trust accounts. Both this note and the staff costs note should be prepared on an accruals basis. NHS foundation trusts should review their disclosures for consistency - the total of the staff costs line plus the directors cost line in the operating expenses note will equal the total of the staff costs note to the accounts plus the costs of ***non***-executive directors. This is because the separate staff costs note includes the costs of executive directors but does not include non-executive directors. Both disclosures include salary, social services costs and pension costs. Where recharges of salary are netted off (see paragraph 3.32) then both notes should include the net amount. However, when a staff member is seconded to another body then both notes should include the total salary cost (as this is a cost to the NHS foundation trust of employing a staff member) and any income from the seconding body should be shown as income. Recharges should not be the cause of a difference between these two notes.

3.51. Total directors costs in the expenses note may not reconcile to the total of salary and pension entitlements of senior managers ('the Greenbury Note'), since the latter is not restricted to directors and also excludes employers' NI and superannuation contributions. However, NHS foundation trusts should be satisfied that the two notes have been prepared on a consistent basis and any differences can be explained.

3.52. Other reasons for differences between the two notes may be:

- capitalised staff costs – where the costs are disclosed in the staff costs note but not in the operating expenses note; or
- research staff – where the staff costs are included in research and development in the operating expenses analysis rather than staff costs.

Audit fees

3.53. This is the total of fees paid or payable to the external auditor for the financial year in question and should be analysed between audit services, further assurance services and other services in accordance with the Companies (Disclosure of Auditor Remuneration and Liability Limitation Agreements) Regulations 2008 (SI 2008/489), which requires that in addition to the disclosure of the audit fee, non-audit fees are disclosed across the following headings:

- Audit fee for associated companies;
- Taxation services;
- IT services;
- Internal audit services;
- Valuation and actuarial services;
- Litigation services;
- Recruitment and remuneration services;
- Corporate finance transactions; and
- All other services.

3.54. Fees for work done by external auditors under Monitor's *Audit Code for NHS Foundation Trusts* should be disclosed as "Audit services – statutory audit". Work by external auditors mandated by the Healthcare Commission should be disclosed as "Audit services – audit-related regulatory reporting", although NHS foundation trusts may also wish to disclose that this is work mandated by the Healthcare Commission.

3.55. ***In accordance with the Companies (Disclosure of Auditor Remuneration and Liability Limitation Agreements) Regulations 2008, where an NHS foundation trust's contract with its auditors provides for a limitation of the auditor's liability, the principal terms of this limitation and the date of the agreement to the principal terms should be disclosed in a note to the accounts.***

PDC dividends payable

3.56. The disclosure of PDC dividends payable on the face of the income and expenditure account is the total of PDC dividends payable by the NHS foundation trust for the given year. ***The amount of PDC dividend payable in the year is set before the start of the financial year as part of the capital charge estimates process.***

3.57. Legislation requires that NHS foundation trusts should pay a PDC dividend on the same basis as NHS trusts. The Department of Health defines the repayment basis which is currently 3.5%. This charge of 3.5% is therefore made on average relevant net assets held in the year.

3.58. Average relevant net assets are calculated by adding the opening and closing balances of relevant net assets for the year (as calculated below) and dividing by 2. Opening relevant net assets are to be calculated from values carried forward from the previous year. Closing relevant net assets are calculated from values reported at the balance sheet date, after all the year's transactions and valuations have taken place.

3.59. The calculation of relevant net assets is as follows:

Total public dividend capital and reserves	X
Less donated asset reserve	(X)
Less cash balances in Paymaster accounts	(X)
	X

3.60. For 2008/09 there will be no change to the basis of the calculation of PDC dividend payable for NHS foundation trusts, the calculation basis therefore remains consistent with that of NHS trusts.

Notes to the income and expenditure account

Segmental reporting

3.61. The FTC forms assume that any segmental analysis will be analysed between healthcare and other activities. It is possible, however, that other segmental classifications may be appropriate under SSAP 25. For instance, healthcare may itself be divided into more than one segment. NHS foundation trusts should also consider whether mandatory and non-mandatory services represent distinct business segments in accordance with FRS 3 and report accordingly. The accounts should be prepared with the segmental analysis that best presents a true and fair view of the NHS foundation trust's activities. Those NHS foundation trusts who have service line reporting information may wish to consider whether to report each service line as a separate segment. However, service line reporting is not a requirement of SSAP 25.

3.62. A cost that is directly attributable to an individual segment should be allocated to that segment. Common costs are costs relating to more than one segment. In most cases it will be possible to apportion these reasonably between the segments, in which case the apportioned costs should be netted off within the first line of surplus/deficit figures. For instance the cost of support staff may be apportioned between the segments according to the amount of time spent on the different activities. Where common costs cannot be reasonably apportioned, they should be deducted from the total of the segment results.

3.63. Net assets (if any) are the average relevant net assets for the segment, calculated in the same way as net assets are calculated for the purpose of calculating the dividend on PDC. Assets and liabilities used jointly by the two segments should be allocated to the segments on a reasonable basis.

3.64. The segmental analysis of income and the surplus/deficit before interest should clearly distinguish between that of the group and that of its associates and joint ventures.

3.65. Even when an NHS foundation trust has no segments meeting the FRS 25 definition the FTC form must be completed – the healthcare column should be completed with the total income and expenditure of the NHS foundation trust. There is no requirement for segmental analysis to be included in the accounts in this case.

Income from activities arising from mandatory and non-mandatory services

3.66. NHS foundation trusts should disclose the level of income from activities arising from mandatory and non-mandatory services (as set out in the NHS foundation trust's Terms of Authorisation) in a separate note to the accounts. This note should equal the total income from activities set out on the face of the income and expenditure account.

Private patient income

Please note that paragraphs 3.67 to 3.73 are the subject of a consultation exercise, following Unison's challenge to Monitor on our interpretation of the private patient income cap, which restricts the amount of income an NHS foundation trust can generate from charges for private healthcare. More information is available in the minutes from Monitor's Board meeting which took place on 30 January 2008; these are available on the Monitor website: http://www.monitor-nhsft.gov.uk/publications.php?cat=1.

Pending the outcome of the private patient income consultation exercise, NHS foundation trusts preparing their accounts for 2008-09 should use the guidance set out below for accounting for private patient income.

3.67. Section 44 of the 2006 Act requires that the proportion of private patient income to the total patient related income of NHS foundation trusts should not exceed its proportion whilst the body was an NHS Trust in 2002/03 (the Private Patient Cap). If the predecessor NHS Trust was not in existence in 2002/03 the proportion in the first year of existence of the predecessor NHS Trust should be used. The NHS foundation trust's Private Patient Cap is set out in the NHS foundation trust's Terms of Authorisation. If the cap is amended by Monitor subsequent to authorisation then the revised cap should be disclosed with a narrative disclosure as to why the change has been made.

3.68. The following table should be included in the notes to the income and expenditure account:

	20XX/XX	2002/03 [or state base year]
Private patient income		
Total patient related income		
Proportion (as a percentage)	%	%

3.69. Private patient income is defined as patient related income arising from charges imposed by the NHS foundation trust in respect of goods and services provided by the NHS foundation trust directly to patients other than for the purposes of the National Health Service. For the avoidance of doubt, income receivable in relation to NHS patients but not receivable from NHS bodies (e.g. NHS Injury Scheme income) and income for EEA, other overseas patients treated under reciprocal healthcare agreements and treatment given in an accident and emergency department are not private patient income. Further guidance in this area is set out in the National Health Service (Charges to Overseas Visitors) Regulations 1989, as amended, located on the Department of Health's website.

3.70. Patient related income includes the following:

- income received from PCTs and specialist commissioners for contracted patient care services;
- income received from other NHS trusts for contracted patient care services;
- income received from the Department of Health for patient care services;

- non-NHS private patient income;
- other income for patient care services (including NHS Injury Scheme income, income from the Ministry of Defence, local authorities, the prison service, etc.); and
- any amounts received from SHAs for patient care services, including income for overseas patients treated under reciprocal agreements.

3.71. Where an NHS foundation trust prepares group accounts, patient related income and private patient income receivable by the NHS foundation trust, and the relevant proportion from its subsidiaries (as defined by FRS2), should be included in the calculation of private patient income and patient related income for the purposes of the Private Patient Cap. Income from joint arrangements that are not entities also falls within the scope of the definition of private patient income and patient related income. Income from associate relationships, joint ventures and investments (as defined by UK GAAP) falls outside the scope of the definition of private patient income and patient related income.

3.72. Any income receivable from NHS bodies that is not related to the provision of healthcare and falls outside the scope of contracts for patient care should not be included in the calculation of patient related income.

3.73. NHS foundation trusts should also include within this note narrative explaining that section 44 of the 2006 Act requires that the proportion of private patient income to the total patient related income of NHS foundation trusts should not exceed its proportion whilst the body was an NHS Trust in 2002/03 or the base year.

Staff costs

3.74. These are defined to include:

- all persons with a contract of employment with the NHS foundation trust (this will include executive directors but exclude non-executive directors);
- the costs of staff recharged by another organisation where no element of overhead is included i.e. where the staff costs are shared between the NHS foundation trust and other bodies;
- staff agency payments i.e. payments to an agency for the employment of staff where the staff remain employees of the agency;
- contract staff i.e. where the NHS foundation trust has control over numbers and qualifications of staff (in contrast to a service obtained under contract); and
- staff on secondment or on loan from other organisations.

3.75. This note should make the following disclosures in relation to staff costs:

- salaries and wages;
- social security costs;
- employer contribution to NHS Pensions; and
- other pension costs.

3.76. The note should also include an analysis of average staff numbers. These should be disclosed in the categories defined in DSCN 18/2001 (which can be found on the DH website http://www.connectingforhealth.nhs.uk/dscn/dscn2001/).

3.77. A footnote to this note should disclose the total employer pension contribution payable for the year (with a prior period comparison where possible).

3.78. The staff costs note should be reconcilable to the staff costs element of the operating expenses note (see paragraph 3.50).

Pension costs

3.79. FRS 17 requires the following disclosures in relation to defined benefit schemes which are accounted for as a defined contribution scheme, such as the NHS pension scheme:

- the fact that the scheme is a defined benefit scheme;
- the reason why sufficient information is not available to enable the employer to account for the scheme as a defined benefit scheme;
- any available information about the existence of the surplus or deficit in the scheme;
- the basis used to determine that surplus or deficit;
- the implications of that surplus or deficit for the employer; and
- the fact that the scheme is a defined benefit scheme which prepares its own scheme statements (this is a requirement of HM Treasury's FReM).

3.80. NHS foundation trusts should be aware of the following information in relation to the NHS pension scheme when they are drafting the disclosures required under the first bullet point:

- the NHS pension scheme is subject to a full valuation every four years by the Government Actuary. ***The latest published valuation relates to the period 1 April 1999 to 31 March 2004 which was published in December 2007 and is available on the Pensions Agency website*** ***http://www.nhspa.gov.uk/nhspa_site/foi/foi1/Scheme_Valuation_Report/NHSPS_Valuation_report.pdf***
  The notional deficit of the scheme was £3.3 billion as per the last scheme valuation by the Government Actuary for the period 1 April 1999 to 31 March 2004. The conclusion of the valuation was that the scheme continues to operate on a sound financial basis.
- ***employer contribution rates are reviewed every four years following the scheme valuation, on advice from the actuary. At the last valuation, it was recommended that employer contribution rates should continue at 14% of pensionable pay. From 1 April 2008, employees' contributions will be on a tiered scale from 5% to 8.5% of their pensionable pay.***

Early retirements due to ill-health

3.81. The number of, and average additional, pension liabilities for individuals who retired early on ill-health grounds during the year must be disclosed in a note to the income and expenditure account. The amount entered should be the figure supplied to the NHS foundation trust by NHS Pensions.

Profits and losses on disposal of fixed assets

3.82. These should be analysed in a note to the income and expenditure account between profits or losses arising from the disposal of protected and assets which are not protected.

Private finance transactions

3.83. PFI transactions should be accounted for and disclosed in accordance with Treasury Technical Note 1, "How to account for PFI transactions".

Off balance sheet disclosures

3.84. ***Under section 410A of the Companies Act 2006, where an NHS foundation trust is a party to an arrangement (including PFI) which is not reflected in its balance sheet and where, at the balance sheet date, the risks or benefits in relation to them are material, it must disclose in a note to the accounts:***

- ***The nature and business purpose of the arrangement; and***
- ***The financial impact of the arrangement on the NHS foundation trust.***

3.85. ***The information need only be given to the extent necessary for enabling the financial position of the NHS foundation trust to be assessed.***

Related party transactions

3.86. NHS foundation trusts should consider whether they have any relationship which would meet the definition of a related party in accordance with FRS 8. NHS foundation trusts ***should disclose the main NHS entities with which they have dealings. The amounts of the transactions need not be disclosed where they can be identified in other parts of the published accounts (not simply the FTCs).*** This is consistent with HM Treasury's FReM.

3.87. In particular, NHS foundation trusts should consider whether the relationship with any of their governors meets the FRS 8 definition of a related party relationship.

3.88. It is prudent to assume that transactions between NHS foundation trusts and the related funds held on trust also fall within the scope of FRS 8.

3.89. ***In accordance with the requirements of the Companies Act 2006, particulars should also be given of transactions the NHS foundation trust has entered into with related parties where the transactions are material and have not been concluded under normal market conditions. If this is the case, the following particulars must be disclosed:***

- ***The amount of the transaction;***
- ***The nature of the related party transaction; and***
- ***Other information necessary for an understanding of the financial position of the NHS foundation trust.***

3.90. ***Information about individual transactions may be aggregated according to their nature, except where separate information is necessary for an understanding of the effects of related party transactions on the financial position of the NHS foundation trust.***

Losses and special payments

3.91. A note disclosing information on losses and special payments should be included in the accounts. This note should disclose:

- the total number and value of losses and special payment cases;
- the number and value of clinical negligence, fraud, personal injury, compensation under legal obligation and fruitless payment cases where the net payment for the individual case exceeds £100,000;
- a statement that these payments are the cash payments made in the year and are not calculated on an accruals basis; and
- any other explanation considered necessary.

3.92. Guidance on the definitions of losses and special payments can be found in Annexes 4.10 to 4.13 of the HM Treasury manual Managing Public Money (MPM, available on the HM Treasury website http://documents.treasury.gov.uk/mpm/mpm_whole.pdf). The guidance in MPM will apply to NHS foundation trusts in full except where it is superseded by guidance in this document.

Balance sheet

Tangible fixed assets

Valuation and valuation basis

3.93. NHS foundation trusts must adopt a policy of revaluation within the scope of FRS 15.

3.94. Land and buildings have to be fully revalued every five years with an interim valuation every three years. The interim valuations should be undertaken by external professional valuers unless the NHS foundation trust can provide evidence that there is reliable information available to allow the valuation to be undertaken in house by a qualified valuer. The five yearly valuations must be carried out by an external professional valuer, who must meet the requirements of FRS 15.

3.95. FRS 15 allows that for tangible fixed assets other than properties, for example equipment and vehicles, directors may be able to establish the asset's value with reasonable reliability using other methods. Therefore, where there is an active second hand market then a valuation may be obtained using market values. Alternatively, appropriate indices may exist which will allow a reasonable valuation. The indices used must:

- be appropriate to the class of asset to which it is to be applied;
- take account of technological change; and

- have a proven record of regular publication which will continue for the foreseeable future.

3.96. Where there is no active second hand market or indices then a valuation should be performed by a qualified valuer every 5 years with a three year update.

3.97. NHS foundation trusts should discuss and agree their proposed method of valuing non-property assets with their auditors and should apply this method on a consistent basis.

Capitalisation threshold of fixed assets - de minimis limits

3.98. *FReM* leaves discretion for individual Government departments to set their own capitalisation thresholds, having regard to practicality, flexibility, consistency and asset grouping considerations. The Department of Health has adopted a £5,000 capitalisation threshold for individual assets, although assets of lesser value should be capitalised if they form part of a group, with a group value in excess of £5,000, as defined below. It is recommended that NHS foundation trusts continue to use this threshold. However, if NHS foundation trusts wish to adopt a lower de minimis threshold then that would be acceptable. Where a change in the de minimis is made then the NHS foundation trust must consider whether a prior period adjustment is required. The £5,000 figure includes VAT where this is not recoverable.

Grouped assets

3.99. "Grouped assets" are a collection of assets which individually may be valued at less than £5,000 but which together form a single collective asset because the items fulfil all the following criteria:

- the items are functionally interdependent;
- the items are acquired at about the same date and are planned for disposal at about the same date;
- the items are under single managerial control; and
- each individual asset thus grouped has a value of over £250.

3.100. Assets acquired in the course of the initial setting up of a new building or on refurbishment may also to be treated as "grouped" for capitalisation purposes.

Capitalisation of software and software licenses

3.101. Software code owned by a NHS foundation trust such that it could copy, licence or sell the application at its discretion should be carried as a tangible fixed asset, within the category "IT hardware“ and depreciated over the expected economic life of the software. However, a purchase of software is generally the purchase of a licence to use software code developed by, and which remains the property of, a third party.

3.102. The provisions of this manual on the capitalisation threshold and grouping of assets also apply to the capitalisation of expenditure on software as an intangible fixed asset under FRS 10. As with IT hardware, it is expected that software used on a network will meet the “interdependence” criterion for the grouping of fixed assets.

IT assets

3.103. It is expected that IT hardware will be considered interdependent if it is attached to a network, the fact that it may be capable of stand-alone use notwithstanding. The effect of this will be that all IT equipment purchases, where the final three criteria listed in paragraph 3.99 apply, will be capitalised.

Initial equipping and setting-up costs of new building

3.104. Assets which are capital in nature but which are individually valued at less than £5,000 but more than £250 may be capitalised (at the NHS foundation trust's discretion) as collective, or “grouped”, assets where they are acquired as part of the setting-up of a new building. The decision on whether or not to capitalise such costs is a choice of accounting policy and consequently the NHS foundation trust should ensure consistency in adhering to this accounting policy if it decides that it is the most appropriate way of valuing its fixed assets. In this context, the enhancement or refurbishment of a ward or unit should be treated in the same way as "new build", provided that the work would be considered as “subsequent expenditure” in FRS 15 terms. It is therefore appropriate to capitalise the purchase of new furniture in a new build or refurbishment exercise, provided that assets thus capitalised can be subsequently identified for audit purposes.

Impairment of fixed assets

3.105. Much of the detail of FRS 11 is concerned with the identification of "income-generating units" (as defined by FRS 11) and the measurement of value in use (the present value of cash flows from the use of an asset). For NHS foundation trusts, these sections of FRS 11 will apply where the NHS foundation trust can identify income generating units in accordance with FRS 11.

3.106. FRS 11 defines value in use as the present value of the future cash flows from the asset's continued use. However, it adds that, where a fixed asset is not held for the purpose of generating cash flows, an alternative measure of its service potential may be more relevant. HM Treasury have interpreted this for the public sector, stating that, where assets are not held for the purpose of generating cash flows, value in use will be assumed to be at least equal to the cost of replacing the service potential provided by the asset unless there has been a reduction in service potential.

3.107. As NHS foundation trusts are required to adopt a revaluation policy they are required to revalue new assets when they are first brought into use. Traditionally, in the NHS this results in a fall in value from the cost of constructing the asset. Where the NHS foundation trust can demonstrate that the value in use (determined using the method set out in FRS 11) exceeds both the previous carrying amount and the revalued amount then the asset is not impaired. In these circumstances it is acceptable for the NHS foundation trust to have a negative revaluation reserve as the lower revalued amount should be recognised in the accounts as the value of the asset.

3.108. Where NHS foundation trusts have negative opening revaluation reserve as a result of the policy adopted by the Department of Health these opening balances should be re-stated using the accounting policy stated in the paragraph above. Any downward valuation which should be treated as an impairment should be transferred from the opening revaluation reserve to the opening I&E reserve.

3.109. As land and buildings are reported separately in the notes to the balance sheet, impairments and revaluations need to be analysed between land and buildings, based on the valuer’s analysis of the overall valuation of the property, and upward revaluations or impairments need to be recognised separately on land and on buildings.

Depreciation and asset lives

3.110. Depreciation policies other than straight-line depreciation are not permissible. NHS foundation trusts should depreciate all assets other than land.

3.111. When assets are revalued then the carrying amount of the asset should be re-stated at its revalued amount. Any accumulated depreciated is eliminated. This is illustrated in the table below:

Details of the fixed asset before revaluation:

	£
Fixed asset at cost/valuation	1,000
Accumulated depreciation	(400)
Net book amount	600

The asset is re-valued to £1,500

Details of the fixed asset after revaluation

	£
Fixed asset at cost/valuation	1,000
Gain on revaluation	500
Fixed asset at revalued amount	1,500
Accumulated depreciation	400
Gain on revaluation	(400)
Depreciation after revaluation	Nil

EU Emission Allowance Trading Scheme

3.112. Where NHS foundation trusts are members of the EU Greenhouse Gas Emission Allowance Trading Directive the scheme gives rise to an intangible asset in relation to allowances held for use on a continuing basis, if not the they should be classified as current assets, within current asset investments.

3.113. The allowance held for use should be shown valued at fair value even when it is purchased for less than fair value. The intangible fixed asset is written down at the year end to the extent that the NHS foundation trust has made emissions and used up its allowances. If allowances are traded then the NHS foundation trust could generate a loss or profit on disposal.

3.114. See also government grants (3.123) and liabilities (3.127) for other accounting entries relating to this scheme.

Debtors

Prepayments: deferred assets in PFI schemes

3.115. Where land and buildings are "transferred" to the private sector partner in a PFI scheme for subsequent sale, this will usually be in exchange for a reduction in rental payments. Equipment, cash or other assets may similarly be injected in exchange for a reduction in payments where the land becomes available later in the contract period. Such contributions of assets typically create “deferred assets” (prepayments) in the accounts of the NHS foundation trust. These deferred assets should be accounted for in accordance with Treasury Task Force Technical Note 1 (revised).

3.116. NHS foundation trusts should also consider the guidance issued by the Department of Health in relation to the change in the discount rate and valuation of deferred assets as this is considered to be best practice. The guidance can be found on the DH’s finman website http://www.info.doh.gov.uk/doh/finman.nsf

Provision for irrecoverable debts

3.117. The Road Traffic Accident (RTA) scheme was replaced by the NHS Injury Scheme on 22 January 2007. On average the Compensation Recovery Unit advise that there is a 7.8% probability of not receiving the income. Therefore, if it is material, 7.8% of accrued ICR income should be included in the provision for irrecoverable debts under the ‘bad debts’ heading within operating expenses. NHS foundation trusts should review this in the light of local information.

3.118. Contracts for patient care entered into by NHS foundation trusts are legally binding and may be resolved by litigation. It is therefore possible for NHS foundation trusts to provide for irrecoverable debts where they have evidence that an invoice will not be paid in full.

Completion of FTC forms: tax and social security balances

3.119. All debtor and creditor balances relating to tax and social security should be included in the FTC forms under the relevant heading on FTC 20F (“NHS debtors and creditors reconciliation: other WGA bodies”).

Creditors

3.120. Overdrafts should be shown as part of creditors under the heading “committed facilities”.

Deferred income

3.121. Government grants received, including receipts from the Big Lottery Fund (or its predecessor bodies), directly by the NHS foundation trust, to finance fixed assets should be credited to the deferred income balance. Where these balances are material they should be separately disclosed as deferred government grants under deferred income. In prior years these balances would have been credited to the government grant reserve but from 2005/06 onwards, NHS foundation trusts are required to account for government grants in accordance with SSAP 4 and therefore they will no longer hold government grant reserves.

3.122. The deferred government grant should be credited to the I&E account over the useful economic life of the asset.

3.123. Where the NHS foundation trust is a member of the EU Greenhouse Gas Emission Allowance Trading scheme and it has been issued allowances at less than fair value then the difference between the amount paid and the fair value should be disclosed as a government grant. The grant should be written off to the I&E account as the allowances are used.

Provisions

Clinical negligence claims

3.124. For NHS foundation trusts within the NHS Litigation Authority (NHSLA) clinical negligence scheme, all clinical negligence claims are recognised in the accounts of the NHSLA. Consequently, the NHS foundation trust will have no provision for clinical negligence claims. The NHSLA will provide a schedule showing the claims recognised in the books of the NHSLA on behalf of the NHS foundation trust. This must be disclosed at the foot of the main provisions table.

Early retirement costs

3.125. NHS employers are responsible for meeting additional costs arising from early retirement. A provision should be established in relation to these costs as soon as the conditions set out in FRS 12 are met. Once a decision has been made then agreement must be reached with NHS Pensions as to how the liability will be discharged. Once this agreement has been reached the provision will either be written off if a lump sum payment is made or transferred to creditors if a 5 year payment schedule will have been agreed.

Injury benefits

3.126. NHS employers are responsible for meeting the cost of injury benefits awards in respect of claims made by NHS employees. The entitlement to injury benefits and the amount of the awards are decided by NHS Pensions. The agency will notify the claimants' employer of the award made. Shortly after payments are made, NHS Pensions will invoice the employer for the rechargeable amount. The details provided on the award notification and the subsequent invoice should be used for calculating injury benefit provisions as per FRS 12, including discounting if material.

EU greenhouse gas emissions allowance trading scheme

3.127. Where the NHS foundation trust is a member of the EU Greenhouse Gas Emission Allowance Trading scheme, it should recognise a liability as emissions are made and the NHS foundation trust is obliged to deliver allowances equal to the emissions made. The liability should be shown as a provision which should be valued at the best estimate of the expenditure required to settle the obligation. This will be market price at the balance sheet date. The provision will be settled by giving up allowances held and therefore writing down the associated intangible asset.

Public dividend capital

3.128. The closing balance of public dividend capital will be confirmed by the Department of Health.

Donated asset reserve

3.129. Donated assets are brought to account in the same way as purchased assets, at cost if newly purchased or constructed, then revalued to a current cost valuation. They are valued, depreciated and subject to impairment in the same way as other assets. The donated asset reserve is used to remove donated assets from the calculation of PDC dividend charges while a release from the reserve compensates for the revenue impact of the depreciation charge.

3.130. Donated assets or cash donations made specifically to buy a fixed asset will be recognised in fixed assets and the donated asset reserve. However, other donations, made to the NHS foundation trust rather than its charitable fund, would be taken to the income and expenditure account as any conditions attached to them are met. The treatment of donations remains under review as a result of the publication of the proposed Statement of Principals for Public Entity Bodies. Under its proposals all donations would be taken to revenue as soon as any conditions attached to the donations have been met. This would include any donations made to purchase fixed assets once the asset has been purchased. If implemented this will be a major change for all public entities and its implementation will therefore be subject to further consultation. The accounting treatment in relation to donations has not been changed in 2008/09. However, it will be reconsidered when determining the appropriate treatment for donations under IFRS.

3.131. For an asset to be treated as donated, there should be no consideration given in return (thus the donor, or individuals are organisations nominated by the donor, may not be offered preferential treatment or other advantages or benefits).

3.132. The following examples do not qualify as "donated":

- an asset transferred between public bodies as a result of a transfer of functions (unless the asset was legitimately a donated asset in the transferor's books);
- assets financed by Government grants, including the Big Lottery Fund (and its predecessor body);
- subsequent capitalised expenditure on a donated asset; and
- the provision by a developer of an access road or transport scheme that will benefit the developer's business. Any asset provided as part of a PFI scheme by the developer cannot be considered as donated.

3.133. Any restrictions imposed by the donor on the use of an asset must be disclosed in the accounts

3.134. The donated asset reserve is maintained to:

- represent the financing associated with the receipt of a donated asset (i.e. provides the credit side to the transaction debiting fixed assets); and
- to provide a mechanism for neutralising depreciation, impairments or profit/loss on disposal charged to the income and expenditure (I&E) account in respect of donated assets (a transfer from the donated asset reserve is made to the I&E account to match the I&E account charge).

3.135. The donated asset reserve is used to account for the following transactions involving donated assets:

- on revaluation of donated assets, the debit or credit is taken to the donated asset reserve, not the revaluation reserve;
- on impairment of a donated asset, any debit that would otherwise be charged to the revaluation reserve under FRS 11 is taken to the donated asset reserve;
- where an impairment is due to loss of economic benefit, the debit is taken to the I&E account, as it would be for a purchased asset. However, an equal sum is debited to the donated asset reserve and credited to the I&E account to neutralise this; and
- depreciation is charged to the I&E account in exactly the same way as would the depreciation on a purchased asset. A transfer is made from the donated asset reserve to the I&E account to match the depreciation charged. No release is made in respect of revalued amounts to the I&E reserve (as for purchased revalued assets) as the full credit is required in the current year I&E account to neutralise the charge.

3.136. The carrying amounts of donated assets continue at all times to equal the value of the donated asset reserve.

3.137. On disposal of a donated asset, the profit or loss on disposal is calculated in the normal way, as the difference between the carrying amount and net sale proceeds, and credited or charged to the I&E account. A transfer from the donated asset reserve to the I&E account is made to match the profit/loss. The net result of this transaction is to re-state the donated asset reserve such that it is equal to the value of the sale proceeds. Finally, a transfer clears any remaining donated asset reserve balance to the I&E reserve.

3.138. Transfers from the donated asset reserve to the I&E account should be accounted for within other operating income or other operating expenditure as appropriate, and should be disclosed separately in the notes analysing these lines of the income and expenditure account.

3.139. The donated asset reserve should be disclosed as part of taxpayers' equity. This is consistent with the FReM disclosure requirements. The rationale for this treatment is that net assets will have increased through the provision of the donated asset (as there is no related liability) and as such taxpayers' equity will also increase.

Notes to the balance sheet

Tangible fixed assets: protected and non-protected assets

3.140. The split of net book value for land, buildings and dwellings should also be analysed between protected and non-protected assets. Guidance on this classification is available on Monitor's website (www.monitor-nhsft.gov.uk) (*Protection of Assets: Guidance for NHS Foundation Trusts*, published October 2004).

PFI

3.141. NHS foundation trusts' involvement in PFI schemes should be accounted for in accordance with Treasury Task Force Technical Note 1 which provides definitive guidance for the application of FRS 5.

3.142. Renegotiation of off balance-sheet PFI contracts may involve a reduction in overall costs in recognition of lower finance costs available in the current economic conditions. In general, such cost savings should be allocated to the period over which the contract runs. This is consistent with the practice of allocating all the other contractors' costs to the life of the arrangement – there is little justification for treating a cost reduction as lump-sum in-year income. Early discussion with auditors is recommended in view of the material sums often involved.

Prudential Borrowing Limit

3.143. NHS foundation trusts are required to comply with the *Prudential Borrowing Code* (available on Monitor's website, www.monitor-nhsft.gov.uk). The prudential borrowing limit (PBL) set out in that code is made up of two elements:

- the maximum cumulative amount of long-term borrowing; and
- the amount of any approved working capital facility.

3.144. NHS foundation trusts should include a note to the accounts disclosing their performance against both elements of their prudential borrowing limit (PBL) at the balance sheet date. NHS foundation trusts should also disclose their actual performance during the year against the key ratios upon which the PBL is based and explain any significant variances that may be highlighted by this disclosure. The following is an example of these disclosures:

The trust has a prudential borrowing limit of £x in 2008/09 (£x in 2007/08). The trust actually borrowed / (repaid) a net £x in 2008/09 (£x in 2007/08) and at 31 March 2009 had £x of outstanding borrowing (£x at 31 March 2008).

Financial ratio	*Actual ratios 2008/09*	*Approved PBL ratios 2008/09*	*Actual ratios 2007/08*	*Approved PBL ratios 2007/08*
Maximum debt/capital ratio				
Minimum dividend cover				
Minimum interest cover				
Minimum debt service cover				
Minimum debt service to revenue				

The trust has an actual working capital facility of £x (£x in 2007/08) [within its approved limit of £x (£x in 2007/08) if actual and limit are different]. The trust had drawn down £x of its working capital facility at 31 March 2009 (£x at 31 March 2008).

3.145. The NHS foundation trust should add the following narrative explaining what this note refers to:

"The NHS foundation trust is required to comply and remain within a prudential borrowing limit. This is made up of two elements:

- the maximum cumulative amount of long-term borrowing. This is set by reference to the five ratio tests set out in Monitor's *Prudential Borrowing Code*. The financial risk rating set under Monitor's *Compliance Framework* determines one of the ratios and therefore can impact on the long term borrowing limit.
- the amount of any working capital facility approved by Monitor.

Further information on the *NHS Foundation Trust Prudential Borrowing Code* and *Compliance Framework* can be found on the website of Monitor, the Independent Regulator of Foundation Trusts."

Financial instruments

3.146. The three UK accounting standards which deal with financial instruments are FRSs 25, 26 and 29. These standards are based on equivalent international accounting standards and can be very complex in areas, in particular the very detailed definitions that can be found throughout the standards. The comments below represent only a general overview and cannot convey all of the nuances of these standards, NHS foundation trusts' finance staff should therefore ensure they are thoroughly familiar with the standards and take care to ensure that their transactions are properly classified, measured and disclosed.

Presentation (FRS 25)

3.147. The presentation aspects of FRS 25 have been applied by NHS foundation trusts from 2006/7 and do not change in 2008/09.

3.148. The presentation aspects of the standard require that all financial instruments should be identified and classified as financial assets, financial liabilities or equity instruments but should be accounted for on the appropriate line of the balance sheet. Financial assets and financial liabilities should be shown within 'net assets' in the balance sheet.

3.149. HM Treasury has concluded, with the agreement of FRAB, that PDC is not a financial instrument within the scope of FRS 25. It should continue to be presented within 'Taxpayers' Equity' in the balance sheet.

3.150. A financial instrument is defined in paragraph 11 of FRS 25 as a "contract that gives rise to a financial asset of one entity and a financial liability or equity instrument of another entity". Using the balance sheet in FTC02 as a starting point, NHS foundation trusts could have financial instruments under any of the following balance sheet categories:

- Investments;
- Interests in subsidiaries, associated and joint ventures – in some circumstances, depending on their classification;
- Finance lease receivables;
- Trade debtors (but not prepayments);
- Cash at bank and in hand;
- Trade creditors (but not deferred income);
- Loans;
- Finance lease obligations; and
- Provisions.

3.151. Some financial instruments are covered by other standards and therefore do not fall under the remit of FRSs 25, 26 and 29. These include:

- employers' rights and obligations under pension schemes; and

- interests in subsidiaries, associated and joint ventures.

Recognition and De-recognition (FRS 26)

3.152. In accordance with FRS 26, financial assets and liabilities should be recognised on the balance sheet when the NHS foundation trust becomes party to the contractual provisions of the financial instrument. In most cases, financial assets will be recognised when the purchaser becomes committed to the purchase. Trade debtors are the exception to this as they are recognised when the goods or services have been delivered. In the case of financial liabilities the NHS foundation trust becomes party to the transaction when the third party has performed under the contract, for example, has transferred the cash it is lending or has delivered the goods or services.

3.153. Financial instruments are de-recognised when the obligations under them are discharged, for example through payment, expire or otherwise lapse.

3.154. The rules for de-recognising financial assets are more complex and first require an assessment of whether partial de-recognition should occur. Where the rights to a financial asset have been transferred to another party, de-recognition may be possible depending on the terms of the transfer.

Measurement (FRS 26)

3.155. Certain types of financial instrument which have their own accounting standards should be measured in accordance with those standards rather than FRS 26. Examples include finance leases which are measured in accordance with SSAP 21 and Provisions which should be measured in accordance with FRS 12. Paragraph 2 of FRS 26 provides a full list. However, any embedded derivatives contained in these transactions will fall within the scope of FRS 26.

3.156. All other financial instruments should be measured in accordance with FRS 26.

Initial measurement at Fair Value

3.157. Once financial assets and liabilities have been identified and recognised they are initially measured at Fair Value. Fair Value is the amount at which an asset can be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction. In some instances, NHS foundation trusts may enter into brokerage or loan arrangements with other NHS bodies where the amount of interest repaid is less than market rate or is nil. In these instances, the NHS foundation trust should discuss with their auditor how these loans should be valued and disclosed in the accounts. Such arrangements should be disclosed in the freetext sheets of the FTCs.

Subsequent measurement

3.158. For subsequent measurement, financial instruments need to be classified in accordance with the standard. Financial assets will be classified into one of the following 4 measurement bases depending on their type:

- Fair value through income and expenditure – assets which meet the definition of 'held for trading' and all derivatives (other than any designated as hedging instruments) are valued at fair value and any changes in the carrying amount are taken through the income and expenditure account. Other financial assets can be designated voluntarily by the entity as 'fair value through income and expenditure' on initial recognition but only if the criteria specified in the standard are met;

- Amortised cost – loans and other receivables and investments which are held to maturity are valued at amortised cost and any changes in the carrying amount are taken through the income and expenditure account. It is likely that NHS foundation trusts will have financial assets which fall into this category;

- Fair value through reserves – financial assets which are designated as available for sale are valued at fair value but changes to the carrying amount are taken to a fair value reserve. When an asset is subsequently disposed of, any cumulative gain or loss in the reserve attributable to the asset is taken to the Income and Expenditure Account (not the I&E Reserve) in the year of disposal;

- Historical cost – investments in unquoted companies whose fair value cannot be determined are held at historic cost.

3.159. Financial liabilities which meet the definition of 'held for trading' or which are derivatives (other than any designated as hedging instruments) must be measured at 'fair value through income and expenditure'. Other financial liabilities can be designated voluntarily by the entity as 'fair value through income and expenditure' on initial recognition but only if the criteria specified in the standard are met.

Derivatives and embedded derivatives

3.160. Derivatives are financial assets or liabilities which require no initial investment, will be settled at a future date and whose value changes in relation to:

- a specified rate, index or other financial variable; or
- a non-financial variable which is not specific to either party to the contract.

3.161. An example of a derivative is a forward contract with a bank to purchase euros on a future date at a pre-determined exchange rate. This might be used when an NHS foundation trust agrees to purchase an asset from a European manufacturer and payment must be in euros on the day of delivery. The forward contract therefore protects the NHS foundation trust from the exchange rate risk. The arrangement to fix the exchange rate does not require any investment and changes with exchange rate fluctuations.

3.162. Derivatives need not necessarily be stand alone – they can be embedded in other contracts wherever there are contract terms which permit the cash flows under the contract to vary. Where the variable is closely related to the contract then the embedded derivative can be ignored and the contract accounted for in accordance with the relevant accounting standard. Where, however, the embedded derivative is not 'closely related' to the host contract, it has to be split from the main contract and accounted for separately at 'Fair Value through income and expenditure'. FRS 26 does not define the term 'closely-related' but a series of examples of embedded derivatives which are 'closely-related' and are not 'closely-related' is contained in the Application Guidance of the standard.

3.163. Embedded derivatives can often be found in loans, leases and PFI contracts, but can also be found in contracts for the supply of goods or services. NHS foundation trusts will have to review all contracts to identify whether they contain embedded derivatives. Where they are identified an assessment will need to be made as to whether or not they are closely related to the host contract and if they are not they will need to be accounted for separately from the host contract.

Disclosures (FRS 29)

3.164. These disclosures apply to all financial instruments within the scope of FRS 25, even where they are not measured in accordance with FRS 26. For example the FRS 29 disclosures apply to finance leases in addition to the disclosure requirements in SSAP 21

3.165. FRS 29 requires that all financial instruments should be disclosed in the accounts, either on the face of the balance sheet or in separate notes. This analysis should also distinguish between the different classifications of financial assets and liabilities (as defined in paragraph 3.155 and 3.159 above.

3.166. Where a financial asset has been reclassified then the amount reclassified and the reasons for the reclassification should be disclosed.

3.167. Where all or part of a category of financials asset is derecognised then the nature of the assets retained and the nature of the risks and rewards of ownership to which the entity is exposed should be disclosed. Where the NHS foundation trust continues to recognise some of the asset then the amounts held and the extent of its continuing involvement should also be disclosed.

3.168. The NHS foundation trust should disclose the following items of income, expense, gains or losses either on the face of the financial statements or in the notes to the accounts:

- net gains or losses on:

- o financial assets or financial liabilities at fair value through income and expenditure;
    - o available for sale financial assets, showing the gain or loss recognised in the STRGL and that recognised in the Income and Expenditure Account separately;
    - o loans and receivables;
    - o financial liabilities measured at amortised cost.
- total interest income and total interest expense for financial assets and liabilities not measured at fair value through profit and loss;
- the amount of any impairment loss for each class of financial asset.

3.169. The accounting policies note should disclose:

- the measurement basis used in preparing the financial statements;
- for assets and liabilities measured at fair value, how that fair value has been calculated;
- the basis for reporting realised and unrealised gains and losses, interest and other items of income and expenditure in the income and expenditure account;

3.170. FRS 29 also requires qualitative and quantitative disclosures relating to the risks associated with financial instruments. There are 3 types of risk:

- Market risk – this is the risk that the fair value or cash flows of a financial instrument will fluctuate because of changes in market prices. It is subdivided into three types of risk:
    - o interest rate risk;
    - o currency risk;
    - o other price risk which may relate specifically to the instrument or may relate to all similar financial instruments in the market;
- Credit risk – this is the risk that one party to a financial instrument will cause financial loss for another party by failing to discharge an obligation;
- Liquidity risk – this is the risk that the NHS foundation trust will encounter difficulties meeting obligations associated with financial liabilities.

3.171. For each of the classifications of financial asset and liability detailed disclosures in relation to the NHS foundation trust's exposure to risks and the objectives, policies and processes used to mitigate that risk.

3.172. Paragraphs 55 to 57 of Schedule 1 to the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 (SI 2008/410) require some disclosures in respect of financial instruments measured at fair value in addition to those in FRS 29.

Third party assets

3.173. *HM Treasury's FReM* requires that third party assets are separately disclosed but are not recognised in the accounts of the NHS foundation trust. These are assets held by the NHS foundation trust on behalf of a third party such as money held on behalf of patients or bank balances held on behalf of other organisations with which the NHS foundation trust operates agency arrangements.

Statement of total recognised gains and losses

Statement of total recognised gains and losses: completion of FTC forms

3.174. Impairment losses other than those chargeable to the income and expenditure account should be included in this note to the accounts.

Movements in taxpayers' equity

3.175. This note highlights the taxpayers' stake in the NHS foundation trust and identifies any changes in the year. A suggested format for the note would follow the analysis required in the FTC forms.

Cash flow statement

3.176. The financing section of the cash flow statement must include the headings required in the FTC forms as well as any relevant lines prescribed by FRS 1.

3.177. The notes to the cash flow statement “Reconciliation of net cash flow to movement in net funds/(debt)” and “analysis of changes in net funds/(debts)” should include all movements in loans, working capital financing facility as well as cash movements.

Annex 1a to chapter 3: Example accounting policies

This annex provides an example accounting policies note that NHS foundation trusts may wish to use as the basis for their own disclosure of accounting policies. As these are only examples they **must be adapted to fit the circumstances of each organisation** – i.e. an organisation should include any additional accounting policies adopted locally and exclude policies which are not relevant to that organisation. They have been revised to include the effect of FRS 26. No polices are required for FRS29.

Alternatively, Annex 1b to chapter 3 contains a checklist of areas that, if present, would require the NHS foundation trust to consult UK GAAP for appropriate accounting policies. That list is not exhaustive but is aimed at identifying common areas where disclosures of accounting policies may be required. As such it represents an alternative way for an NHS foundation trust to formulate its accounting policies rather that copy the policies below and adapt them as appropriate.

Model accounting policies note (applicable to the accounts of an individual NHS foundation trust)

Accounting policies and other information

Monitor has directed that the financial statements of NHS foundation trusts shall meet the accounting requirements of the *NHS Foundation Trust Financial Reporting Manual* which shall be agreed with HM Treasury. Consequently, the following financial statements have been prepared in accordance with the *20XX/XX NHS Foundation Trust Financial Reporting Manual* issued by Monitor. The accounting policies contained in that manual follow UK generally accepted accounting practice for companies (UK GAAP) and HM Treasury's *Financial Reporting Manual* to the extent that they are meaningful and appropriate to NHS foundation trusts. The accounting policies have been applied consistently in dealing with items considered material in relation to the accounts.

Accounting convention

These accounts have been prepared under the historical cost convention modified to account for the revaluation of tangible fixed assets at their value to the business by reference to their current costs. NHS foundation trusts, in compliance with HM Treasury's *Financial Reporting Manual*, are not required to comply with the FRS 3 requirements to report "earnings per share" or historical profits and losses.

Acquisitions and discontinued operations

Activities are considered to be 'discontinued' where they meet all of the following conditions:

a. the sale (this may be at nil consideration for activities transferred to another public sector body) or termination is completed either in the period or before the earlier of three months after the commencement of the subsequent period and the date on which the financial statements are approved;

b. if a termination, the former activities have ceased permanently;

c. the sale or termination has a material effect on the nature and focus of the reporting NHS foundation trust's operations and represents a material reduction in its operating facilities resulting either from its withdrawal from a particular activity or from a material reduction in income in the NHS foundation trust's continuing operations; and

d. the assets, liabilities, results of operations and activities are clearly distinguishable, physically, operationally and for financial reporting purposes.

Operations not satisfying all these conditions are classified as continuing.

Activities are considered to be 'acquired' whether or not they are acquired from outside the public sector.

Income recognition

Income is accounted for applying the accruals convention. The main source of income for the trust is under contracts from commissioners in respect of healthcare services. Income is recognised in the period in which services are provided. Where income is received for a specific activity which is to be delivered in the following financial year, that income is deferred.

The NHS foundation trust changed the form of its contracts with NHS commissioners to follow the Department of Health's Payment by Results methodology in 200x/xx. To manage the financial impact of this change on the NHS foundation trust and its commissioners, [set out details of timing and nature of transitional gain or clawback arrangements].

Expenditure

Expenditure is accounted for applying the accruals convention. [Add details of any other significant accounting policies or estimation techniques applied to expenditure and not disclosed elsewhere.]

Tangible fixed assets

Capitalisation

Tangible assets are capitalised if they are capable of being used for a period which exceeds one year and they:

- individually have a cost of at least £5,000; or
- form a group of assets which individually have a cost of more than £250, collectively have a cost of at least £5,000, where the assets are functionally interdependent, they had broadly simultaneous purchase dates, are anticipated to have simultaneous disposal dates and are under single managerial control; or
- form part of the initial setting-up cost of a new building or refurbishment of a ward or unit, irrespective of their individual or collective cost.

Valuation

Tangible fixed assets are stated at the lower of replacement cost and recoverable amount. On initial recognition they are measured at cost (for leased assets, fair value) including any costs, such as installation, directly attributable to bringing them into working condition. The carrying values of tangible fixed assets are reviewed for impairment in periods if events or changes in circumstances indicate the carrying value may not be recoverable. The costs arising from financing the construction of the fixed asset are not capitalised but are charged to the income and expenditure account in the year to which they relate.

All land and buildings are revalued using professional valuations in accordance with FRS 15 every five years. A three yearly interim valuation is also carried out.

Valuations are carried out by professionally qualified valuers in accordance with the Royal Institute of Chartered Surveyors (RICS) *Appraisal and Valuation Manual*. The last asset valuations were undertaken in 2004 as at the prospective valuation date of 1 April 2005. The revaluation undertaken at that date was accounted for on 31 March 2005.

The valuations are carried out primarily on the basis of depreciated replacement cost for specialised operational property and existing use value for non-specialised operational property. The value of land for existing use purposes is assessed at existing use value. For non-operational properties including surplus land, the valuations are carried out at open market value.

Additional alternative open market value figures have only been supplied for operational assets scheduled for imminent closure and subsequent disposal.

Assets in the course of construction are valued at cost and are valued by professional valuers as part of the five or three-yearly valuation or when they are brought into use.

Residual interests in off-balance sheet private finance initiative (PFI) properties are included in assets under construction within tangible fixed assets at the amount of unitary charge allocated for the acquisition of the residual with an adjustment. The adjustment is the net present value of the change in the fair value of the residual as estimated at the start of the contract and at the balance sheet date.

Operational equipment is valued at net current replacement cost. Equipment surplus to requirements is valued at net recoverable amount. [*Add in detail of valuation basis here*]

Depreciation, amortisation and impairments

Tangible fixed assets are depreciated at rates calculated to write them down to estimated residual value on a straight-line basis over their estimated useful lives. No depreciation is provided on freehold land, and assets surplus to requirements.

Assets in the course of construction and residual interests in off-balance sheet PFI contract assets are not depreciated until the asset is brought into use or reverts to the trust, respectively.

Buildings, installations and fittings are depreciated on their current value over the estimated remaining life of the asset as assessed by the NHS foundation trust's professional valuers. Leaseholds are depreciated over the primary lease term.

Equipment is depreciated on current cost evenly over the estimated life. [Details of useful economic lives should be provided, for instance the range within which useful economic lives fall for the main classes of asset.]

Fixed asset impairments resulting from losses of economic benefits are charged to the income and expenditure account. All other impairments are taken to the revaluation reserve and reported in the statement of total recognised gains and losses to the extent that there is a balance on the revaluation reserve in respect of the particular asset.

Intangible fixed assets

Intangible assets are capitalised when they are capable of being used in a trust's activities for more than one year; they can be valued; and they have a cost of at least £5,000.

Intangible fixed assets held for operational use are valued at historical cost and are amortised over the estimated life of the asset on a straight line basis. The carrying value of intangible assets is reviewed for impairment at the end of the first full year following acquisition and in other periods if events or changes in circumstances indicate the carrying value may not be recoverable.

Purchased computer software licences are capitalised as intangible fixed assets where expenditure of at least £5,000 is incurred and amortised over the shorter of the term of the licence and their useful economic lives.

Donated fixed assets

Donated fixed assets are capitalised at their current value on receipt and this value is credited to the donated asset reserve. Donated fixed assets are valued and depreciated as described above for purchased assets. Gains and losses on revaluations are also taken to the donated asset reserve and, each year, an amount equal to the depreciation charge on the asset is released from the donated asset reserve to the income and expenditure account. Similarly, any impairment on donated assets charged to the income and expenditure account is matched by a transfer from the donated asset reserve. On sale of donated assets, the net book value of the donated asset is transferred from the donated asset reserve to the Income and Expenditure Reserve.

Liquid Resources

Deposits and other investments that are readily convertible into known amounts of cash at or close to their carrying amounts are treated as liquid resources in the cashflow statement.

Government grants

Government grants are grants from Government bodies other than income from primary care trusts or NHS trusts for the provision of services. Grants from the Department of Health, including those for achieving three star status, are accounted for as Government grants as are grants from the Big Lottery Fund. Where the Government grant is used to fund revenue expenditure it is taken to the Income and Expenditure account to match that expenditure. Where the grant is used to fund capital expenditure the grant is held as deferred income and released to the income and expenditure account over the life of the asset on a basis consistent with the depreciation charge for that asset.

Private Finance Initiative (PFI) transactions

The NHS follows HM Treasury's Technical Note 1 (Revised) "How to Account for PFI transactions" which provides definitive guidance for the application of application note F to FRS 5.

Where the balance of the risks and rewards of ownership of the PFI property are borne by the PFI operator, the PFI payments are recorded as an operating expense. Where the trust has contributed land and buildings, a prepayment for their fair value is recognised and amortised over the life of the PFI contract by charge to the income and expenditure account. Where, at the end of the PFI contract, a property reverts to the trust, the difference between the expected fair value of the residual on reversion and any agreed payment on reversion is built up over the life of the contract by capitalising part of the unitary charge each year, as a tangible fixed asset.

Where the balance of risks and rewards of ownership of the PFI property are borne by the trust, it is recognised as a fixed asset along with the liability to pay for it which is accounted for as a finance lease. Contract payments are apportioned between an imputed finance lease charge and a service charge.

Stocks and work-in-progress

Stocks and work-in-progress are valued at the lower of cost and net realisable value. Work-in-progress comprises goods and services in intermediate stages of production.

Cash, bank and overdrafts

Cash, bank and overdraft balances are recorded at the current values of these balances in the NHS foundation trust's cash book. These balances exclude monies held in the NHS foundation trust's bank account belonging to patients (see "third party assets" below). Account balances are only set off where a formal agreement has been made with the bank to do so. In all other cases overdrafts are disclosed within creditors. Interest earned on bank accounts and interest charged on overdrafts is recorded as, respectively, "interest receivable" and "interest payable" in the periods to which they relate. Bank charges are recorded as operating expenditure in the periods to which they relate.

Research and development

Expenditure on research is not capitalised. Expenditure on development is capitalised if it meets the following criteria:

- there is a clearly defined project;
- the related expenditure is separately identifiable;
- the outcome of the project has been assessed with reasonable certainty as to its technical feasibility and its resulting in a product or services that will eventually be brought into use; and
- adequate resources exist, or are reasonably expected to be available, to enable the project to be completed and to provide any consequential increases in working capital.

Expenditure so deferred is limited to the value of future benefits expected and is amortised through the income and expenditure account on a systematic basis over the period expected to benefit from the project. It is revalued on the basis of current cost. Expenditure which does not meet the criteria for capitalisation is treated as an operating cost in the year in which it is incurred. Where possible, NHS foundation trusts disclose the total amount of research and development expenditure charged in the Income and Expenditure account separately. However, where research and development activity cannot be separated from patient care activity it cannot be identified and is therefore not separately disclosed.

Fixed assets acquired for use in research and development are amortised over the life of the associated project.

Provisions

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

Contingencies

Contingent assets (that is, assets arising from past events whose existence will only be confirmed by one or more future events not wholly within the entity's control) are not recognised as assets, but are disclosed in note XYZ where an inflow of economic benefits is probable.

Contingent liabilities are provided for where a transfer of economic benefits is probable. Otherwise, they are not recognised, but are disclosed in note XYZ unless the probability of a transfer of economic benefits is remote. Contingent liabilities are defined as:

Possible obligations arising from past events whose existence will be confirmed only by the occurrence of one or more uncertain future events not wholly within the entity's control; or

Present obligations arising from past events but for which it is not probable that a transfer of economic benefits will arise or for which the amount of the obligation cannot be measured with sufficient reliability.

Clinical negligence costs

The NHS Litigation Authority (NHSLA) operates a risk pooling scheme under which the NHS foundation trust pays an annual contribution to the NHSLA, which, in return, settles all clinical negligence claims. Although the NHSLA is administratively responsible for all clinical negligence cases, the legal liability remains with the NHS foundation trust. The total value of clinical negligence provisions carried by the NHSLA on behalf of the NHS foundation trust is disclosed at note XYZ.

Non-clinical risk pooling

The NHS foundation trust participates in the Property Expenses Scheme and the Liabilities to Third Parties Scheme. Both are risk pooling schemes under which the trust pays an annual contribution to the NHS Litigation Authority and in return receives assistance with the costs of claims arising. The annual membership contributions, and any 'excesses' payable in respect of particular claims are charged to operating expenses when the liability arises.

Pension costs

Past and present employees are covered by the provisions of the NHS Pensions Scheme. The scheme is an unfunded, defined benefit scheme that covers NHS employers, general practices and other bodies, allowed under the direction of Secretary of State, in England and Wales. As a consequence it is not possible for the NHS foundation trust to identify its share of the underlying scheme liabilities. Therefore, the scheme is accounted for as a defined contribution scheme under FRS 17.

Employers pension cost contributions are charged to operating expenses as and when they become due.

Additional pension liabilities arising from early retirements are not funded by the scheme except where the retirement is due to ill-health. The full amount of the liability for the additional costs is charged to the income and expenditure account at the time the trust commits itself to the retirement, regardless of the method of payment.

[Add similar details of any other pension scheme used.]

Value Added Tax

Most of the activities of the NHS foundation trust are outside the scope of VAT and, in general, output tax does not apply and input tax on purchases is not recoverable. Irrecoverable VAT is charged to the relevant expenditure category or included in the capitalised purchase cost of fixed assets. Where output tax is charged or input VAT is recoverable, the amounts are stated net of VAT.

Corporation Tax

[this note should disclose:
- the basis of the charge for taxation;
- the policy adopted for providing for deferred taxation;
- the policy adopted regarding discounting.

If the NHS foundation trust has determined that it is has no corporation tax liability then the basis for that decision should be disclosed.]

Foreign exchange

Transactions that are denominated in a foreign currency are translated into sterling at the exchange rate ruling on the dates of the transactions. Resulting exchange gains and losses are taken to the income and expenditure account.

Third party assets

Assets belonging to third parties (such as money held on behalf of patients) are not recognised in the accounts since the NHS foundation trust has no beneficial interest in them. However, they are disclosed in a separate note to the accounts in accordance with the requirements of the HM Treasury *Financial Reporting Manual*.

Leases

Where substantially all risks and rewards of ownership of a leased asset are borne by the NHS foundation trust, the asset is recorded as a tangible fixed asset and a debt is recorded to the lessor of the minimum lease payments discounted by the interest rate implicit in the lease.

The asset and liability are recognised at the inception of the lease, and are de-recognised when the liability is discharged, cancelled or expires.

The interest element of the finance lease payment is charged to the income and expenditure account over the period of the lease at a constant rate in relation to the balance outstanding. Other leases are regarded as operating leases and the rentals are charged to the income and expenditure account on a straight-line basis over the term of the lease.

Public dividend capital

Public dividend capital (PDC) is a type of public sector equity finance based on the excess of assets over liabilities at the time of establishment of the original NHS trust.

A charge, reflecting the forecast cost of capital utilised by the NHS foundation trust, is paid over as public dividend capital dividend. The charge is calculated at the real rate set by HM Treasury (currently 3.5%) on the average relevant net assets of the NHS foundation trust. Relevant net assets are calculated as the value of all assets less the value of all liabilities, except for donated assets and cash held with the Office of the Paymaster General. Average relevant net assets are calculated as a simple mean of opening and closing relevant net assets.

Financial instruments and financial liabilities

Recognition

Financial assets and financial liabilities which arise from contracts for the purchase or sale of non-financial items (such as goods or services), which are entered into in accordance with the Trust's normal purchase, sale or usage requirements, are recognised when, and to the extent which, performance occurs i.e. when receipt or delivery of the goods or services is made.

[Financial assets or financial liabilities in respect of assets acquired or disposed of through finance leases are recognised and measured in accordance with the accounting policy for leases described above/below.]

[Regular way purchases or sales are recognised and de-recognised, as applicable, using the Trade/Settlement - *delete as appropriate*- date].

[All other financial assets and financial liabilities are recognised when the Trust becomes a party to the contractual provisions of the instrument.]

De-recognition

All financial assets are de-recognised when the rights to receive cashflows from the assets have expired or the Trust has transferred substantially all of the risks and rewards of ownership.

Financial liabilities are de-recognised when the obligation is discharged, cancelled or expires.

Classification and Measurement

Financial assets are categorised as ['Fair Value through Income and Expenditure',] Loans and receivables [or 'Available-for-sale financial assets'].

[Financial liabilities are classified as 'Fair value through Income and Expenditure' or as 'Other Financial liabilities'.]

Financial assets and financial liabilities at 'Fair Value through Income and Expenditure'

Financial assets and financial liabilities at 'fair value through income and expenditure' are financial assets or financial liabilities held for trading. A financial asset or financial liability is classified in this category if acquired principally for the purpose of selling in the short-term. Derivatives are also categorised as held for trading unless they are designated as hedges. [Derivatives which are embedded in other contracts but which are not 'closely-related' to those contracts are separated-out from those contracts and measured in this category.] Assets and liabilities in this category are classified as current assets and current liabilities.

These financial assets and financial liabilities are recognised initially at fair value, with transaction costs expensed in the income and expenditure account. Subsequent movements in the fair value are recognised as gains or losses in the income and expenditure account.]

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments which are not quoted in an active market. They are included in current assets.

The Trust's loans and receivables comprise: [current investments, cash at bank and in hand, NHS debtors, accrued income and 'other debtors'].

Loans and receivables are recognised initially at fair value, net of transactions costs, and are measured subsequently at amortised cost, using the effective interest method. The effective interest rate is the rate that discounts exactly estimated future cash receipts through the expected life of the financial asset or, when appropriate, a shorter period, to the net carrying amount of the financial asset.

Interest on loans and receivables is calculated using the effective interest method and credited to the income and expenditure account.

Available-for-sale financial assets

Available-for-sale financial assets are non-derivative financial assets which are either designated in this category or not classified in any of the other categories. They are included in long-term assets unless the Trust intends to dispose of them within 12 months of the balance sheet date.]

Available-for-sale financial assets are recognised initially at fair value, including transaction costs, and measured subsequently at fair value, with gains or losses recognised in reserves. When items classified as 'available-for-sale' are sold or impaired, the accumulated fair value adjustments recognised in reserves are included in the income and expenditure account.]

Other financial liabilities

All [other] financial liabilities are recognised initially at fair value, net of transaction costs incurred, and measured subsequently at amortised cost using the effective interest method. The effective interest rate is the rate that discounts exactly estimated future cash payments through the expected life of the financial liability or, when appropriate, a shorter period, to the net carrying amount of the financial liability.

They are included in current liabilities except for amounts payable more than 12 months after the balance sheet date, which are classified as long-term liabilities.

Interest on financial liabilities carried at amortised cost is calculated using the effective interest method and charged to the income and expenditure account.

Determination of fair value

For financial assets and financial liabilities carried at fair value, the carrying amounts are determined from [quoted market prices/independent appraisals/discounted cash flow analysis/other (describe)].]

Impairment of financial assets

At the balance sheet date, the Trust assesses whether any financial assets, other than those held at 'fair value through income and expenditure' is impaired. Financial assets are impaired and impairment losses are recognised if, and only if, there is objective evidence of impairment as a result of one or more events which occurred after the initial recognition of the asset and which has an impact on the estimated future cashflows of the asset.

For financial assets carried at amortised cost, the amount of the impairment loss is measured as the difference between the asset's carrying amount and the present value of the revised future cash flows discounted at the asset's original effective interest rate. The loss is recognised in the income and expenditure account and the carrying amount of the asset is reduced - *delete as appropriate:* [directly] or [through the use of an allowance account/bad debt provision]

[Where an allowance account/bad debt provision is used, disclosure should be made of the criteria for determining when an asset's carrying value is written-down directly and when the allowance account is used, and the criteria for writing off amounts charged to the allowance account against the carrying amount of the financial asset].

Annex 1b to chapter 3: Accounting policy checklist

This annex provides a checklist for the accounting policies that NHS foundation trusts should consider including in note 1 to their accounts.

The objective of FRS 18 is to ensure that for all material items:

- an entity adopts the accounting policies most appropriate to its particular circumstances for the purpose of giving a true and fair view;
- the accounting policies adopted are reviewed regularly to ensure that they remain appropriate, and are changed when a new policy becomes more appropriate to the entity's particular circumstances; and
- sufficient information is disclosed in the financial statements to enable users to understand the accounting policies adopted and how they have been implemented.

In many instances, this FReM and UK GAAP mean that an NHS foundation trust is required to follow a particular accounting policy. Accounting standards require certain accounting policies to be disclosed. However, in some instances, the policy may not be applicable to an NHS foundation trust's transactions. This checklist is intended to assist the NHS foundation trust with its preparation of note 1 to its accounts.

FRS 18 requires that an entity's accounting policies are reviewed regularly to ensure that they remain the most appropriate to its particular circumstances for the purpose of giving a true and fair view. An NHS foundation trust's accounting policy should meet the requirements of this FReM as well as UK GAAP.

Subject matter	***UK GAAP requirements***	***UK GAAP reference***	***Reference in this FReM***
Accounting convention	Statement that the accounts have been prepared under the historical cost convention in accordance with the NHS foundation trust FReM and UK GAAP	The Large and Medium Sized Companies and Groups (Accounts and Reports) Regulations 2008	N/A
Changes in accounting policy	A description of each of the accounting policies that is material in the context of the entity's financial statements; A description of those estimation techniques adopted that are significant; Details of any changes to the accounting policies including: • a brief explanation of why each new accounting policy is thought more appropriate; • where practicable, the effect of a prior period adjustment on the results for the preceding period; and • where practicable, an indication of the effect of a change in accounting policy on the results for the current period. Where it is not practicable to make the disclosures described above, that fact, together with the reasons, should be stated. Where the effect of a change	FRS 18 paragraph 55 FRS 28 paragraph 9	Paragraphs 2.1 to 2.9.

Subject matter	*UK GAAP requirements*	*UK GAAP reference*	*Reference in this FReM*
	to an estimation technique is material, a description of the change and, where practicable, the effect on the results for the current period		
Consolidation	In the period where there is a business combination, the names of the entities involved should be disclosed, the date of the combination and whether the combination has been accounted for as an acquisition or merger. Disclosure of: • basis of consolidation; • inclusion of all subsidiaries; • basis of accounting for associates and joint ventures; • uniform accounting policies; • elimination of inter-group transactions; • elimination of investor's shares of profits or losses	FRS 6 para 21 FRS 2 para 23, 39, 40 FRS 9 para 20, 26, 31b	Paragraphs 3.10 to 3.24
Income recognition	Basis of income recognition and measurement for each principal income stream	FRS 5, Application Note G UITF 26	Paragraphs 3.41 to 3.96
Capitalisation of finance costs	Statement that interest is not capitalised	FRS 15 para 31	
Tangible fixed assets	Statement that assets are held at revalued amount Disclosure of: • Basis and frequency of revaluations; • Method of depreciation; • Useful economic lives/depreciation rate; • Reason for any change in depreciation method, useful lives or residual value; • Basis for determining impairment; • Use of discounting in determining value in use; • Treatment of impairment write down on revalued assets	FRS 18 para 55a, 55d, 56 FRS 15 para 42, 100 UITF 24, 29 FRS 11 para 14, 41, 45	
Intangible fixed assets and goodwill	Disclosure of • Method used to value intangible assets; • Methods and periods of amortisation; • Treatment of goodwill on disposal; • Reason for any change in	FRS 10 para 52, 55, 56, 57, 58, 59, 64, 71 FRS 18 para 55a FRS 11 para 14, 41, 45	

Subject matter	UK GAAP requirements	UK GAAP reference	Reference in this FReM
	amortisation method; • Basis for determining impairment; • Use of discounting in determining value in use; • Treatment of impairment write down on revalued assets		
Donated fixed assets	As tangible fixed assets above	N/A	
Investments	Basis of inclusion of investment property on balance sheet; Treatment of changes in value	SSAP 19 para 11, 13	
Government grants	Treatment of capital grants; Treatment of revenue based grants; Period over which grants are credited to I&E account	SSAP 4, para 17, 28a	
Accounting for financial assets	Basis of recognition and measurement; Recognition of impairments; For financial assets designated as at fair value through profit and loss: • Nature of the financial assets or liabilities; • Criteria for designation; • How paras 9, 11A or 12 of FRS 26 have been satisfied The criteria for designating financial assets as available for sale; Criteria used to determine method of accounting for impairments; Method and assumptions in determining fair values; How assets are classified	FRS 26 para 9, 14, 15, 21, 39, 43, 45-47, 58, appendix B5a-f	
Derivative financial instruments and hedging activities	Description of how derivatives are initially accounted for and subsequently revalued; Description of treatment of changes in valuation; Description of the hedging documentation in place	FRS 26, para 21, 23, 24, 86, 89, 85, 97, 98, 101, 102	
Fair value estimation	Description of the basis of fair valuation of interest rate swaps, currency swaps, short term deposits, loans and overdrafts	FRS 19 para 27 FRS 26 para 46, 47	
Private Finance Initiative (PFI) transactions	Basis on which the amounts charged as an expense are calculated; Basis on which amounts have been capitalised; Basis on which the on or off balance sheet accounting has been reached	HM Treasury Task Force Technical Note no.1	

Subject matter	***UK GAAP requirements***	***UK GAAP reference***	***Reference in this FReM***
Stocks and work-in-progress	Basis of amount stated in the balance sheet; Method of valuation; Basis for inclusion of overheads; Basis of provision for obsolete stock; Method of ascertaining turnover and attributable profit for long term contracts	SSAP 9 para 32	
Cash, bank and overdrafts		FRS 29 para 21	
Research and development	Classification of expenditure; Treatment of expenditure	SSAP 13, para 30	
Trade debtors		FRS 26 para 43, 46a, 59 FRS 29 app B para 5df	
Trade creditors		FRS 26 para 43, 47	
Borrowings	Measurement basis of financial liabilities; The fact that substance over form determines the classification on the balance sheet	FRS 26 para 43, 47 FRS 25 para 18a, 28, 33 FRS 29 para 27a	
Provisions including clinical negligence costs and non-clinical risk pooling	Basis of accounting for each class of provision; Extent of use of discounting	FRS 12 para 14	
Contingencies	Basis of accounting for contingencies	FRS 12 paragraph 27	
Pension costs	Type of scheme For defined benefit scheme – valuation frequency and method; Method of charging to I&E; Treatment of actuarial gains and losses for defined benefit schemes; Funding policy	FRS 17 UITF 35	
Value Added Tax	Basis of accounting for VAT	SSAP 5	
Corporation Tax	Basis of charge for taxation; Policy adopted for providing for deferred taxation; Policy adopted regarding discounting	FRS 16 FRS 19 UITF 19	
Foreign exchange	Basis of translating foreign currency assets and liabilities; Basis of translating results of foreign subsidiaries; Treatment of exchange differences	FRS 23 para 23, 44	
Third party assets	Basis of accounting for third party assets	N/A	
Leases – lessee	Basis of recognition of finance lease assets; Depreciation policy for assets held under finance leases; Treatment of the interest element of finance lease rentals;	SSAP 21 para 57	

Subject matter	***UK GAAP requirements***	***UK GAAP reference***	***Reference in this FReM***
	Treatment of operating lease payments; Treatment of operating lease incentives		
Leases – lessor	Policy for operating leases; Policy for finance leases; Policy for finance lease income; Treatment of costs of assets acquired for letting under a finance lease; Treatment of lease incentives	SSAP 21 para 60	
Public dividend capital	Statutory basis of PDC; Accounting treatment	HM Treasury FReM	

Situations requiring reference to UK GAAP

- Does the NHS foundation trust hold investments in subsidiaries?
- Has the NHS foundation trust acquired an interest in a subsidiary, joint venture or associate?
- Does the NHS foundation trust carry out two or more classes of business that are substantially different?
- Has the NHS foundation trust disposed of any material business segments in the period?
- Has the NHS foundation trust classified any operations as discontinued during the period?
- Is the NHS foundation trust a lessor of assets?
- Has the NHS foundation trust sold any assets and leased them back from the purchaser?
- Has the NHS foundation trust undertaken any foreign currency transactions?
- Does the NHS foundation trust employ members of a pension scheme other than the NHS Pension Scheme?
- Has the NHS foundation trust entered into any transactions involving consignment stock, sale and repurchase agreements, debt factoring, securitisation, loan transfers or quasi-subsidiaries?
- Does the NHS foundation trust have any long-term contracts?
- Does the NHS foundation trust have any corporation tax liabilities, or any deferred tax?
- Does the NHS foundation trust hold any investment properties?
- Has the NHS foundation trust revised the useful economic lives of any of its assets during the period?
- Have any exceptional items arisen during the accounting period?
- Have there been any changes in accounting policy since the prior year?
- Have any fundamental errors been detected in the accounts of an earlier period that require correction?
- Does the NHS foundation trust hold “other reserves”?
- Have there been any circumstances arising which would cause an asset to be impaired?

Annex 2 to chapter 3: Worked example – merger accounting

An NHS foundation trust acquires the entire business of an NHS Trust on 1 September 2007 in return for cash consideration of £25.0m paid by the NHS foundation trust to the NHS Trust.

Accounting entries for PDC issued and repaid:

Transactions in NHS foundation trust accounts (pre-merger)

1 NHS foundation trust's receipt of PDC funding from SoS:

Dr	Cash	£25m
Cr	PDC	£25m

2 NHS foundation trust purchases business from NHS Trust

Dr	Net Assets	£25m
Cr	Cash	£25m

Transactions in NHS Trust accounts

3 NHS Trust sells business to NHS foundation trust

Dr	Cash	£25m
Cr	Net Assets	£25m

4 NHS Trust repays PDC to Secretary of State

Dr	PDC	£25m
Cr	Cash	£25m

Following the merger, the accounts are combined as if they always existed. Thus transactions 2 and 3 are consolidated-out.

The resulting balance sheet at the date of merger is as follows:

	NHS Trust	Foundation Trust	Adjustments for Alignment of		Foundation Trust
	Balances 31/8/07	Balances 31/8/07	**Accounting Policies**		Balances 1/9/07
	£000	£000	£000		£000
FIXED ASSETS:					
Intangible Fixed Assets	15	20			35
Tangible Fixed Assets	30,000	60,000			90,000
CURRENT ASSETS:					
Stocks and WIP	400	500			900
Debtors	6,000	5,500			12,000
Cash at Bank and in hand	5	15			20
CREDITORS:					
Amounts falling due within one year	(7,500)	(3,000)			(10,500)
NET CURRENT ASSETS (LIABLITIES)	**(1,095)**	**3,015**			**1,920**
CREDITORS:					
Amounts falling due after more than one year	0	(2,000)	(400)	*	(2,400)
PROVISIONS FOR LIABILITIES AND CHARGES	(1,000)	(1,500)			(2,500)
TOTAL ASSETS EMPLOYED	27,920	59,535			87,055
PDC	25,000	48,000			73,000
Revaluation Reserve	5,000	6,000			11,000
Donated Asset Reserve	200	100			300
Government Grant Reserve	400	0	(400)	*	0
Other Reserves	0	0			0
Income and Expenditure Reserve	(2,680)	5,435			2,755
TOTAL CAPITAL AND RESERVES	27,920	59,535			87,055

Opening Balances established on basis of FT Accounting Policies

* Alignment of NHS Trust balance to accord with FT accounting policy on government grant funded assets, results in the reclassification of the government grant reserve to deferred income balance

NB In the above example the consideration payable by the FT is fixed against the existing PDC of the NHS Trust. If however, the amount payable (and funded by new PDC) is for a different amount, for example the carrying value of the NHS Trust's net assets, then a merger reserve will need to be created to reflect the difference between the 'capital' given and received.

e.g. The net assets and PDC of the acquired Trust are £40m and £35m respectively. The consideration payable is set at £40m,and PDC is issued to the NHS foundation trust by the SoS for this amount. Following the purchase, the £40m cash is repaid by the NHS Trust to the SoS. The PDC of nominal value £35m is therefore repaid to the SoS along with a premium of £5m. This premium is dealt with by creating a negative merger reserve of £5m.

Example Disclosures

- On 1 April 2007 the NHS foundation trust acquired the whole business of Northern Hospital NHS Trust. The transaction involved the purchase of the net assets of Northern Hospital NHS Trust, with a value of £27,920,000. The consideration given by the NHS foundation trust was £25,000,000 in cash, which was financed through additional Public Dividend Capital received from the Secretary of State.

- This transaction represents the transfer of services between public sector bodies and therefore is a 'machinery of government' change. Consequently, in accordance with the *NHS Foundation Trust Financial Reporting Manual* and the group reconstruction provisions of FRS 6, merger accounting has been applied to this transaction.

2007/08	**NHS Trust Pre-merger £000**	**NHS foundation trust Pre-merger £000**	**Combined Post-merger £000**	**Total £000**
Income and Expenditure Account				
Operating Income	12,100	15,900	31,300	59,300
Operating Surplus/(Deficit)	(1,300)	960	1,550	1,210
Profit on disposal of fixed assets	50			50
Costs of fundamental reorganisation			(60)	(60)
PDC Dividends payable	(100)	(240)	(350)	(690)
Total Recognised gains and losses:				
Surplus/(Deficit) for the period	(1,350)	720	1,140	510
Revaluation gains/(losses)	1,500	2,100	0	3,600
	150	2,820	1,140	4,110

2006/07	NHS Trust £000	Foundation Trust £000	Combined £000
Income and Expenditure Account			
Operating Income	22,700	29,200	51,900
Operating Surplus/(Deficit)	(1,100)	1,800	700
Profit on disposal of fixed assets	200	0	200
PDC Dividends payable	(210)	(450)	(660)
Total Recognised gains and losses:			
Surplus/(Deficit) for the period	(1,110)	1,350	240
Revaluation gains/(losses)	1,320	1,900	3,220
	210	3,250	3,460

The disclosure requirements in respect of the book values of the net assets, and the differences arising from alignment can be met through including the earlier table showing the aggregation of the balance sheets.

Annex 3 to chapter 3: Worked example of the prior period adjustment in relation to the change in accounting policy for donations

From 2005/06 onwards, NHS foundation trusts should treat grants from the Big Lottery fund and its predecessor bodies as government grants rather than as part of the donated asset reserve. The annex sets out a simple worked example of the prior period adjustment and the required disclosures. From 2007/08 onwards, there will be no need for a prior period adjustment in relation to Big Lottery funds as NHS foundation trusts should have made the adjustment during 2005/06 or as an adjustment to opening balances on achieving foundation trust status. The worked example is retained in the FReM as a general example of a prior period adjustment.

During 2004/05, the NHS foundation trust received a grant of £3m from the New Opportunities Fund to purchase a new piece of equipment.

The equipment is expected to have a useful economic life of 15 years and the NHS foundation trust has continued its policy of applying indexation to its equipment assets.

2004/05

Dr Cash
Cr Donated asset reserve

Dr Donated asset
Cr Cash

With £3m for the receipt and purchase of the equipment

Dr I&E account
Cr Donated asset depreciation

Dr Donated asset reserve
Cr I&E account

With £200,000 for the annual depreciation charge

2005/06

Dr Donated asset
Cr Donated asset reserve

With £62k indexation

Dr I&E account
Cr Donated asset depreciation

Dr Donated asset reserve
Cr I&E account

With £204k for the annual depreciation charge

2006/07

Dr Donated asset
Cr Donated asset reserve

With £82k indexation

Dr I&E account
Cr Donated asset depreciation

Dr Donated asset reserve
Cr I&E account

With £211k for the annual depreciation charge

Therefore, the balance sheet before the change in accounting policy is:

	2006/07 £'000	2005/06 £'000	2004/05 £'000
Tangible fixed assets			
• Donated assets	2,529	2,658	2,800
Donated asset reserve	2,529	2,658	2,800

However, applying the new accounting policy would result in the following transactions:

2004/05

Dr Cash
Cr Government grants deferred account

Dr Fixed asset
Cr Cash

With £3m for the receipt and purchase of the equipment

Dr I&E account
Cr Fixed asset depreciation

Dr Government grants deferred account
Cr I&E account

With £200,000 for the annual depreciation charge

2005/06

Dr Fixed asset
Cr Revaluation reserve

With £62k indexation

Dr Revaluation reserve
Cr I&E reserve

With £4k backlog depreciation

Dr I&E account
Cr Fixed asset depreciation

With £204k for the annual depreciation charge

Dr Government grants deferred account
Cr I&E account

With £204k with that year's share of the government grant

2006/07

Dr Donated asset
Cr Revaluation reserve

With £82k indexation

Dr Revaluation reserve
Cr I&E reserve

With £11k backlog depreciation

Dr I&E account
Cr Fixed asset depreciation

Dr Government grants deferred account
Cr I&E account

With £200k for the annual depreciation charge

So, the revised accounts look as follows:

Balance sheet

	2006/07 £'000	**2005/06 £'000**	**2004/05 £'000**
Tangible fixed assets	2,529	2,658	2,800
Government grant deferred	(2,400)	(2,600)	(2,800)
	129	58	0
Revaluation reserve	129	58	0
I&E reserve	0	0	0
	129	58	

The operating cost note should be adjusted to remove the transfer from the donated asset reserve and, instead to reflect the transfer from the government grant deferred account.

Therefore the 2006/07 balance sheet would show these amounts as the current and prior period comparatives. The STRGL reflects the cumulative effect of the prior period adjustment.

	Revaluation reserve	**Donated asset reserve**	**I&E reserve**	**Total**
Opening balance 1 April 2006	0	2,658	0	2.658
Prior period adjustment	58	(2,658)	0	2,600
Opening balance as restated	58	0	0	58
Transfer from I&E account			(11)	(11)
Indexation	82			82
Transfer between reserves	(11)		(11)	0
Closing balance 31 March 2007	129	0	0	129

The additional free text sheet to the FTCs should disclose the following:

	2005/06 £'000 Adjusted	2005/6 £'000 Unadjusted	Comments
Tangible fixed assets	2,658	2,658	No change as the value of the asset has not changed
Government grant deferred	(2,600)		The difference is due to the change in policy from donated asset reserve to government grant deferred
Total	**58**	**2,658**	
Revaluation reserve	58		The difference is due to indexation of £62 being taken to the revaluation reserve and then the backlog depreciation charge of £4 being transferred to the I&E reserve
I&E reserve	0		
Donated asset reserve	0	2,658	This is the removal of the donated asset reserve
Total	**58**	**2,658**	

In this instance the cumulative effect of the adjustments is the movement in reserves disclosed as a prior period adjustment in the reserves note - £2,600k. This cumulative effect should be disclosed at the foot of the current year column of the STRGL.

	2006/07 £'000	**2005/06 (as restated) £'000**
Surplus/(deficit) for the financial year before dividend payments		(4)[1]
Fixed asset impairment losses		
Unrealised surplus/(deficit) on fixed assets and current asset investments revaluations		
Increase in the donated asset reserve due to receipt of donated assets		
Reductions in the donated asset reserve due to depreciation, impairment, and/or disposal of donated assets		0[2]
Additions/(reduction) in "Other reserves"		
Other recognised gains and losses *		
TOTAL RECOGNISED GAINS AND LOSSES FOR THE FINANCIAL YEAR		
Prior period adjustments	(2,600)[3]	
TOTAL RECOGNISED GAINS AND LOSSES IN THE FINANCIAL YEAR		

[1] This is the removal of the donated asset reserve transfer of £204k which would have been in the 2004/05 under the old accounting policy and the insertion of the release of £200k from the deferred income - government grant account under the new policy

[2] This is the removal of the £204k donated asset reserve transfer which would have been in the 2005/06 accounts

[3] This is the cumulative movement on reserves taken from the movement on reserves note

4. Annual reporting guidance for NHS foundation trusts

Introduction

4.1 Paragraph 26 of Schedule 7 to the National Health Service Act 2006 (the 2006 Act) requires NHS foundation trusts to prepare an annual report. Paragraph 26(3) of Schedule 7 provides that it is for Monitor to decide the form of reports, when the reports are to be submitted in and the periods for which the reports are to relate.

4.2 This chapter sets out the requirements for the content and format of the annual report element of the Annual Report and Accounts of NHS foundation trusts.

4.3 NHS foundation trusts should ensure they have read and understood chapter 1 and Annexes 2 and 3 to chapter 1 about preparing and submitting their annual report and accounts.

Content of the annual report

4.4 This guidance draws on HM Treasury's FReM, which interprets commercial requirements in the context of the public sector. As the HM Treasury FReM applies to a wide number of bodies some of its requirements are not applicable to NHS foundation trusts – this chapter therefore includes the requirements of HM Treasury's FReM as relevant to NHS foundation trusts.

4.5 The annual report of NHS foundation trusts should include the following sections:

- a directors' report including a management commentary;
- a remuneration report;
- the disclosures set out in the NHS Foundation Trust Code of Governance;
- other disclosures in the public interest;
- a statement of Accounting Officer's Responsibilities; and
- a statement on Internal Control; and
- **details of the NHS foundation trust's quality objectives and performance against those objectives**

Directors' report

4.6 The directors' report should be prepared in accordance with:

- ***Sections 415 to 418 of the Companies Act 2006 (it should be noted that section 415 (4) and (5) and section 418(5) and (6) do not apply to NHS foundation trusts; and***

- ***Regulation 10 and Schedule 7 of the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 ("the Regulations"); and***

- ***Additional disclosures required by the FReM as described below.***

General Companies Act disclosures (s416)

4.7 **This section sets out the following further information, as interpreted, to be included in the Directors' Report:**

- ***The names of individuals who at any time during the financial year were directors of the NHS foundation trust;***

- ***The principal activities of the NHS foundation trust during the year (including that of any subsidiaries).***

Further Companies Act disclosures (s416 and Regulation 10 and Schedule 7 of the Regulations)

4.8 The Regulations, issued under s416, set out a series of disclosures to be included in the Directors' Report. A summary of the requirements is included in Annex 1 to this chapter, but practitioners should refer to the regulations themselves to ensure that they comply with all of the requirements. NHS foundation trusts should ensure that the information is only included where it is relevant to its operations.

Business review (s417) / Management Commentary / Operating and Financial Review

4.9 The FReM interprets the reporting requirements of the Business Review to be met through a Management Commentary, which should also reflect the recommendations set out in the Accounting Standards Board's Reporting Statement: Operating and Financial Review. The purpose of the business review is to inform users of the accounts and help them assess how the directors have performed their duties.

4.10 The business review must contain:

- a fair review of the NHS foundation trust's business;
- a description of the principal risks and uncertainties facing the NHS foundation trust;
- a balanced and comprehensive analysis of the development and performance of the NHS foundation trust's business during the financial year; and of
- the position of the NHS foundation trust's business at the end of that financial year;
- the business review must, to the extent necessary for an understanding of the development, performance and position of the NHS foundation trust's business include:
  - the main trends and factors likely to affect the future development, performance and position of the NHS foundation trust's business;
  - information about:
    - environmental matters (including the impact of the NHS foundation trust's business on the environment);
    - the NHS foundation trust's employees; and
    - social and community issues.

    including information about any policies of the NHS foundation trust in relation to those matters and the effectiveness of those policies.

- ***information about persons with whom the NHS foundation trust has contractual or other arrangements which are essential to the business of the NHS foundation trust (unless disclosure would, in the opinion of the directors, be seriously prejudicial to that person and contrary to the public interest);***
- ***An analysis using key financial performance indicators;***
- ***Where appropriate, an analysis using other key performance indictors, including information relating to environmental and employee matters;***

"Key performance indicators" means factors by reference to which the development, performance or position of the NHS foundation trust's business can be measured effectively.

- ***the review must, where appropriate, include references to, and additional explanations of, amounts included in the NHS foundation trust's financial statements.***
- ***In relation to a directors' report on consolidated accounts, these requirements apply to the activities and business of all entities included in the consolidation.***
- ***Disclosures of information about impending developments or matters in the course of negotiation are not required if the disclosure would, in the opinion of the directors, be seriously prejudicial to the interests of the NHS foundation trust.***

ASB Reporting Statement: Operating and Financial Review (OFR)

4.11 As noted above, the Business Review should reflect the recommendations of the ASB's Reporting Statement on the OFR, which seeks to ensure that a Business Review/Management Commentary/OFR is a balanced and comprehensive analysis of:

- the development and performance of the business of the entity during the financial year;
- the position of the entity at the end of the year;
- the main trends and factors underlying the development, performance and position of the business of the entity during the financial year; and
- the main trends and factors that are likely to affect the entity's future development, performance and position.

4.12 The key principles underlying the information reported are that the OFR should:

- set out an analysis of the business through the eyes of the board of directors;
- focus on matters that are relevant to the interests of users of the Annual Report and Accounts;
- have a forward-looking orientation, identifying those trends and factors relevant to an assessment of current and future performance of the NHS foundation trust and the progress towards the achievement of long-term business objectives;
- complement as well as supplement the financial statements, in order to enhance the overall corporate disclosure;
- be comprehensive and understandable;
- be balanced and neutral, dealing even-handedly with both good and bad aspects; and
- be comparable over time.

4.13 In addition to the Reporting Statement's recommended disclosures in respect of the strategies, performance, resources and financial position of the business, NHS foundation trusts may wish to consider including information in respect of patient care activities and stakeholder relations, for example:

Patient Care

- descriptions of how the NHS foundation trust is using its foundation trust status to develop its services and improve patient care;
- performance against key patient targets;
- arrangements for monitoring improvements in the quality of healthcare and progress towards meeting any national and local targets, incorporating Healthcare Commission assessments and reviews and the NHS foundation trust's response to any recommendations made;
- progress towards targets as agreed with local commissioners, together with details of other key quality improvements;
- any new or significantly revised services;
- service improvements following staff or patient surveys or comments and Healthcare Commission reports;
- improvements in patient/carer information;
- information on complaints handling;

Stakeholder relations

- descriptions of significant partnerships and alliances entered into by the NHS foundation trust to facilitate the delivery of improved healthcare. These should be described together with the benefits to patients and the methods used to fund these activities; and
- development of services involving other local services/agencies and involvement in local initiatives.

Statement as to disclosure to auditors (s418)

4.14 The directors' report must include a statement to the effect that, for each individual who is a director at the time that the report is approved:

- so far as the directors are aware, there is no relevant audit information of which the auditors are unaware, and
- the director has taken all of the steps that they ought to have taken as a director in order to make themselves aware of any relevant audit information and to establish that the auditors are aware of that information.

4.15 "Relevant audit information" means information needed by the NHS foundation trust's auditor in connection with preparing their report.

4.16 A director is regarded as having taken all the steps that they ought to have taken as a director in order to do the things mentioned above:

- made such enquiries of his fellow directors and of the NHS foundation trust's auditors for that purpose, and

- taken such other steps (if any) for that purpose, as are required by his duty as a director of the NHS foundation trust to exercise reasonable care, skill and diligence.

Additional disclosures required by the FReM

4.17 The FReM requires further disclosures, of which those relevant to NHS Foundation Trusts are:

- A note that the accounts have been prepared under a direction issued by Monitor;
- A brief history of the NHS foundation trust and its statutory background;
- An explanation of the adoption of the going concern basis (see below);
- A statement that accounting policies for pensions and other retirement benefits are set out in note XYZ to the accounts and that details of senior employees' remuneration can be found in page x of the remuneration report.
- Details of company directorships and other significant interests held by directors [or Governors] which may conflict with their management responsibilities. Where the NHS foundation trust maintains a Register of Interests that is open to the public, the disclosure may be limited to a comment on how access to the information in that Register may be obtained

Going concern

4.18 There is no presumption of going concern status for NHS foundation trusts. Directors must decide each year whether or not it is appropriate for the NHS foundation trust to prepare its accounts on the going concern basis, taking into account best estimates of future activity and cash flows.

4.19 The NHS foundation trust should include a statement on whether or not the financial statements have been prepared on a going concern basis and the reasons for this decision, with supporting assumptions or qualifications as necessary (*Code of Governance F.1.2*).

4.20 A typical disclosure, based on guidance from the Accounting Standards Board, would read:

"After making enquiries, the directors have a reasonable expectation that the NHS foundation trust has adequate resources to continue in operational existence for the foreseeable future. For this reason, they continue to adopt the going concern basis in preparing the accounts."

4.21 Where there is fundamental uncertainty over the going concern basis (for instance, continuing operational stability depends on finance or income that has not yet been approved), or where the going concern basis is not appropriate, the directors will need to disclose the relevant circumstances and should discuss the basis of accounting and the disclosures to be made with their auditors.

Remuneration report

4.22 The FReM requires NHS foundation trusts to prepare a remuneration report in their Annual Report and Accounts which complies with:

- ***Section 420 to 422 of the Companies Act 2006 (it should be noted that section 420(2) and (3), section 421(3) and (4) and section 422(2) and (3) do not apply to NHS foundation trusts);***
- ***Regulation 11 and Schedule 8 of the Large and Medium-sized Companies and Groups (accounts and reports) Regulations 2008 (SI 2008/410); and***

- ***Elements of the NHS Foundation Trust Code of Governance.***

4.23 Compliance with this manual in relation to the disclosure of senior employees' remuneration and pension entitlements will ensure that some of the requirements of the remuneration report are met. The relevant notes to the accounts should be referenced in the main body of the remuneration report. The disclosures on senior employees' remuneration and pension entitlements will therefore be subject to audit. Auditors will also read the other information in the remuneration report and consider whether it is consistent with the financial statements.

4.24 The remuneration report must be signed by the chief executive.

4.25 The remuneration report must disclose information on those persons in senior positions having authority or responsibility for directing or controlling the major activities of the NHS foundation trust. This means those who influence the decisions of the NHS foundation trust as a whole rather than the decisions of individual directorates or sections within the NHS foundation trust. Such persons will include advisory and non-executive board members. In the following paragraphs, such persons are described as "senior managers".

4.26 The remuneration report shall include information under the following headings to the extent that they are relevant.

Contents of the remuneration report – information not subject to audit

4.27 The following information is required by Part 2 of Schedule 8 to the Regulations, or where stated by the NHS Foundation Trust Code of Governance, and is not subject to audit:

- details of the membership of the remuneration committee, this means the names of the chair and members of the remuneration committee should be disclosed (Code of Governance A.1.2);
- the number of meetings and individual's attendance at each should also be disclosed (Code of Governance A.1.2);
- ***the name of any person (and in particular any director of the NHS foundation trust who was not a member of the committee) who provided advice or services to the committee that materially assisted the committee in their consideration of any matter. Where such a person is not a director of the Trust: a description of the nature of any other services that person has provided to the Trust during the financial year and whether that person was appointed by the committee (Paragraph 2(1)(c) of Schedule 8 to the Regulations);***
- a statement of the policy on the remuneration of senior managers for current and future financial years, for instance whether a particular source of guidance was used to determine senior managers' pay and conditions of employment;
- an explanation of methods used to assess whether performance conditions were met and why those methods were chosen. If relevant, why and how the methods involved comparison with outside organisations;
- an explanation of relative importance of the relevant proportions of remuneration which are, and which are not, subject to performance conditions;
- a summary and explanation of policy on duration of contracts, and notice periods and termination payments;
- details of the service contract for each senior manager who has served during the

year;

  - date of the contract, the unexpired term, and details of the notice period;
  - provision for compensation for early termination;
  - other details sufficient to determine the entity's liability in the event of early termination;

- explanation of any significant awards made to past senior managers;

Contents of the remuneration report – information subject to audit

4.28 The following information is required by Part 3 of Schedule 8 to the Regulations, or where stated, by the NHS Foundation Trust Code of Governance, and is subject to audit.

4.29 For each senior manager (see definition below) who served during the year show, in tabular form this information:

- salary and allowances (in bands of £5,000), see definition below;
- if a payment for compensation for loss of office paid or receivable has been made under the terms of an approved Compensation Scheme, the fact that such a payment has been made (but no details of the amounts paid);
- estimated value of non-cash benefits (benefits in kind) (to the nearest £100);
- the total of the above items for both this and the previous year;
- details of any element of the remuneration package which is not cash;
- Pension disclosures (see below):
  - the real increase during the reporting year in the pension and (if applicable) related lump sum at age 60 in bands of £2,500;
  - the value at the end of the reporting year of the accrued pension and (if applicable) related lump sum at age 60 in bands of £2,500;
  - the value of the cash equivalent transfer value at the beginning of the reporting year to the nearest £1,000;
  - the real increase in the cash equivalent transfer value during the reporting year, to the nearest £1,000;
  - the real increase in the cash equivalent transfer value at the end of the reporting year, to the nearest £1,000.
- details of amounts payable to third parties for services of a senior manager;
- details of compensation payable to former senior managers; and
- where an executive director serves as a non-executive director elsewhere a statement as to whether or not the director will retain earnings relating to that non-executive appointment *(Code of Governance E.1.3).*

Definition of "senior managers"

4.30 The definition of "senior managers" is 'those persons in senior positions having authority or responsibility for directing or controlling the major activities of the NHS foundation trust'. The chief executive should confirm whether this covers more than the chair, the executive and non-executive directors of the NHS foundation trust (who should be treated as senior managers as a matter of course).

4.31 This note covers all those individuals who hold or have held office as chairman, non-executive director, executive director or senior manager (as identified by the Chief Executive) of the NHS foundation trust during the reporting year. It is irrelevant that:

- an individual was not substantively appointed (holding office is sufficient, irrespective of defects in appointment); or
- an individual's title as director included a prefix such as "temporary" or "alternate"; or
- an individual was engaged via a corporate body, such as an agency, and payments were made to that corporate body rather than to the individual directly.

4.32 Following a case arising under the Freedom of Information Act, the Information Commissioner determined that consent is no longer needed for the disclosure of salary and pension details for named individuals. Entities are therefore entitled to publish senior managers' remuneration details without obtaining their prior consent. For new appointments it may be made a condition on appointment. Consent to disclose pension and salary details should always be sought from departing senior managers on their final day of service.

4.33 Non-disclosure is only acceptable where senior managers can demonstrate that disclosure would cause or be likely to cause substantial damage or substantial distress and that damage or distress would be unwarranted. Where non-disclosure is agreed, the fact that certain disclosures have been omitted should be disclosed.

4.34 For further information see the Information Commissioner's ruling reference FS50093734 on their website http://www.ico.gov.uk/ or FRAB paper 81(08) on their website http://www.hmtreasury.gov.uk./documents/public_spending_reporting/frab/psr_reporting_statistics_frabmeeting_210906.cfm.

Definition of "salary and allowances"

4.35 Salary is the gross salary paid/payable to the individual and this should be shown in £5,000 ranges. Where an individual held a contract of employment for the entire financial year but was only a senior manager for six months, it is the remuneration for six months which should be shown. Where there has been overlap in a post, for example where there have been two finance directors for a month, both must be shown.

4.36 Salary includes:

- all amounts paid or payable by the NHS foundation trust to the individual including recharges from any other health body;
- overtime;
- the gross cost of any arrangement whereby a senior manager receives a net amount and a NHS foundation trust pays income tax on their behalf;
- any financial loss allowances paid in place of remuneration;
- recruitment and retention allowances;
- geographical allowances such as London weighting; and
- other allowances to the extent that they are subject to UK taxation; and
- any ex-gratia payments.

4.37 Salaries should exclude:

- employers' National Insurance and superannuation contributions;
- recharges to any other health body;
- reimbursement of out-of-pocket expenses;
- reimbursement of "travelling and other allowances" (paid under determination

order) including home to work travel costs;

- compensation for loss of office; and
- any amount paid which the senior manager must subsequently repay. However, these amounts must be disclosed in the next accounts, and distinguished from other remuneration, where a senior manager is subsequently released from the liability or a loan to a senior manager remains unpaid for two years after the due date.

Compensation for loss of office

4.38 This is the amount of any compensation paid or payable to senior managers or past senior managers in respect of loss of office.

Benefits in kind

4.39 This covers the monetary value of benefits in kind, such as the provision of a car. This category also includes expense allowances (not paid under determination order) where subject to income tax. A narrative disclosure detailing the nature of benefits in kind should be given after the table. Please note that this disclosure should be made in £00 rather than £000.

Pension disclosures

4.40 This will apply to executives only as non-executive directors do not receive any pensionable remuneration.

4.41 The requirement is to disclose cash equivalent transfer values (CETVs) of pensions at the year end (in bands of £1000), the real increase in the CETVs in the year (in bands of £1000), the value of automatic lump sums at the year end (in bands of £2500), and the real increase in year in the value of automatic lump sums (in bands of £2500).

4.42 The CETV is the actuarially assessed capitalised value of the pension scheme benefits accumulated by a member at a particular point in time. The benefits valued are the member's accumulated benefits and any contingent spouse's pension payable from the scheme. CETVs are calculated within the guidelines and framework prescribed by the Institute and Faculty of Actuaries.

4.43 The accrued benefits derived from the member's purchase of added years of service and any 'transferred-in' service must be included in all the pension calculations.

4.44 From 2005-06 all the information required in the senior managers' pension table will be provided by NHS Business Services Authority, Pensions Division (NHSBSAPD). The request for information from NHSBSAPD must be made by the NHS foundation trust by the deadline set by NHSBSAPD for providing complete information at that time.

4.45 Detailed guidance regarding the end of year procedures for requesting information from the NHSBSAPD can be found on their website http://www.nhspa.gov.uk/site/index.cfm.

4.46 Where the NHS foundation trust has senior managers who are members of a different pension scheme the disclosure information should be requested in good time from the scheme.

NHS Foundation Trust Code of Governance

4.47 In September 2006, Monitor published the *NHS Foundation Trust Code of Governance.* The purpose of the Code of Governance is to assist NHS foundation trust boards in improving their governance practices by bringing together the best practice of public and private sector corporate governance. The Code is issued as best practice advice, but imposes some disclosure requirements. Since 2007/08, NHS foundation trusts have been expected to observe the Code's disclosure requirements in full. In doing this NHS foundation trusts are required to include the following disclosure in their annual report.

4.47.1 In the first part of the statement, the trust has to report on how it applies the main and supporting principles of the code. The form and content of this part of the statement are not prescribed, the intention being that trusts should have a free hand to explain their governance policies, including any special circumstances applying to them which have led to a particular approach.

4.47.2 In the second part of the statement the trust has either to confirm that it complies with the provisions of the code or, where it does not, to provide an explanation

4.48 Schedule A to the Code lists all of the annual report disclosure requirements but, for ease, the requirements have been included in this chapter alongside the other disclosure requirements.

Board of governors

4.49 The annual report should include a statement of how the board of directors and the board of governors operate, including a high-level statement of which types of decision are to be taken by each of the boards and which are to be delegated to management by the board of directors *(Code of Governance A.1.1).*

4.50 The annual report should describe the composition of the board of governors during the reporting period and the name of any persons occupying positions as governors. It should also describe how the governors were appointed or elected, and how long their appointments are for. This should include a brief description of the constituency or organisation that each governor represents and information about any elections held during the year *(Code of Governance B.1.3).*

4.51 The report should include a statement about the number of meetings of the board of governors and individual attendance by governors and directors *(Code of Governance B.1.3).*

4.52 The report should disclose details of company directorships or other material interests in companies held by governors where those companies or related parties are likely to do business, or are possibly seeking to do business, with the NHS foundation trust. As each NHS foundation trust must have a register of governors' interests which is available to the public, an alternative disclosure is for the annual report to simply state how members of the public can gain access to the register instead of listing all the interests in the Annual Report.

4.53 A statement should also be included which sets out the steps that the members of the board, in particular the non-executive directors, have taken to understand the views of governors and members *(Code of Governance G.1.5)*

Board of directors

4.54 The annual report is primarily a report of the board of directors and this section of the report should provide information on the composition of the board during the reporting year. Specifically, information should be provided on:

- the name(s) of the person(s) occupying the position of chair, deputy chair (where there is one) and the senior independent director during the year, the date of their appointment and how long the appointment is for *(Code of Governance A.1.2);*
- the name(s) of the person(s) occupying the position of chief executive and the composition of the board of directors during the year;
- the names of the non-executive directors which the board considers to be independent, with reasons where necessary *(Code of Governance A.3.1);*
- the number of meetings of the board of directors and those committees and individual attendance by directors *(Code of Governance A.1.2);*
- a brief description of the length of appointments of the non-executive directors, and how they may be terminated; and
- a brief description of the background of each of the board members, including the their areas of expertise and experience *(Code of Governance A.3.4).*

4.55 The report should include a statement about the balance, completeness and appropriateness of the membership of the board *(Code of Governance A.3.4).*

4.56 The report should include a summary of how performance evaluation of the board of directors, its committees and its directors has been conducted. *(Code of Governance D.2).*

4.57 The report should disclose details of company directorships or other material interests in companies held by directors which may conflict with their management responsibilities. As each NHS foundation trust must have a register of directors' interests that must be available to the public, an alternative disclosure is for the annual report to simply state how members of the public can gain access to the register instead of listing all the interests in the Annual Report.

4.58 In particular, the report should include a statement in relation to the other significant commitments of the chairman and any changes to them during the year *(Code of Governance C.1.6)*

Audit Committee

4.59 The names of the chair and members of the audit committee should be disclosed *(Code of Governance A.1.2).*

4.60 The number of meetings and individual's attendance at each should also be disclosed *(Code of Governance A.1.2).*

4.61 A description of the work of the audit committee in discharging its responsibilities *(Code of Governance F.3.3).*

4.62 Where the board of governors does not accept the audit committee's recommendation on the appointment, reappointment or removal of the external auditor, the audit committee should make a statement in the annual report explaining their recommendation and the reasons for the governors taking a different position *(Code of Governance F.3.5).*

4.63 Narrative disclosures of the NHS foundation trust's policy for ensuring that the external auditor's independence has not been compromised where work outside the audit code has been purchased from the NHS foundation trust's external auditors *(Code of Governance F.3.5).*

4.64 An explanation of how, if the auditor provides non-audit services, auditor objectivity and independence is safeguarded *(Code of Governance F.3.7).*

4.65 An explanation from the directors of their responsibility for preparing the accounts and a statement by the auditors about their reporting responsibilities *(Code of Governance F1.1). The auditor's statement should be contained in the audit report.*

Nomination Committee

4.66 The names of the chair and members of the nomination committee should be disclosed *(Code of Governance A.1.2).*

4.67 The number of meetings and individual attendance by directors at each should also be disclosed *(Code of Governance A.1.2).*

4.68 A description of the work of the nomination committee, including the process it has used in relation to board appointments. This should include an explanation if neither an external search consultancy nor open advertising has been used in the appointment of a chairman or non-executive director *(Code of Governance C.1.12)*

Membership

4.69 This section of the annual report should include:

- a brief description of the eligibility requirements for joining different membership constituencies, including the boundaries for public membership;
- information on the number of members and the number of members in each constituency; and
- a summary of the membership strategy and an assessment of the membership and a description of any steps taken during the year to ensure a representative membership, including progress towards any recruitment targets for members.

4.70 Contact procedures for members who wish to communicate with governors and/or directors *(Code of Governance G.1.4).*

Other disclosures in the public interest

4.71 NHS foundation trusts are public benefit corporations and it is considered to be best practice for the annual report to include public interest disclosures on the NHS foundation trust's activities and policies in the following areas:

- actions taken by the NHS foundation trust to maintain or develop the provision of information to, and consultation with, employees;
- the NHS foundation trust's policies in relation to disabled employees and equal opportunities;
- information on health and safety performance and occupational health;
- information on policies and procedures with respect to countering fraud and corruption;
- a statement describing the better payment practice code or any other policy

adopted on payment of suppliers, and performance achieved together with disclosure of any interest paid under the Late Payment of Commercial Debts (Interest) Act 1998;

- details of any consultations completed in the previous year, consultations in progress at the date of the report, or consultations planned for the coming year;
- consultation with local groups and organisations, including the overview and scrutiny committees of local authorities covering the membership areas; and
- any other public and patient involvement activities.

4.72 It is also considered best practice for NHS foundation trusts to disclose:

- performance against the better payment practice code requirement to pay all trade creditors within 30 days (this should be linked to the payment policy disclosures described in Annex 1); and
- management costs calculated in accordance with the Department of Health's definitions (http://www.dh.gov.uk/PolicyAndGuidance/OrganisationPolicy/FinanceAndPlanning/NHSManagementCosts/fs/en); and
- the number of, and average additional pension liabilities for, individuals who retired early on ill-health grounds during the year. The amount entered should be the figure supplied to the NHS foundation trust by NHS Pensions; and
- detailed disclosures in relation to "other income" where "other income" in the notes to the accounts is significant.

4.73 In addition, the HM Treasury FReM requires that NHS foundation trusts publish:

- ***sickness absence data. This is the data which is provided quarterly to the Cabinet Office and published on the NHS foundation trust's website; and***
- ***a statement that the NHS foundation trust has complied with the cost allocation and charging requirements set out in HM Treasury and Office of Public Sector Information guidance; and***
- ***details of Serious Untoward Incidents involving data loss or confidentiality breach (required as part of NHS Information Governance rules).***

Statement of accounting officer's responsibilities

4.74 The NHS foundation trust's chief executive should explain his/her responsibility for preparing the financial statements. This should be positioned after the Annual Report and before the statement on internal control. A model statement of accounting officer's responsibilities is provided in annex 2 to this document.

4.75 Paragraph 25 of Schedule 7 to the 2006 Act states that the NHS foundation trust is to prepare annual accounts, and that such functions of the trust are to be delegated to the Accounting Officer. The Accounting Officer memorandum further states that it is the chief executive's personal responsibility to prepare the financial statements. In addition, the Code of Governance (F.1.1) requires directors to include in the annual report an explanation of their responsibility for preparing the financial statements.

Statement on internal control

4.76 All entities covered by the requirements of this manual shall prepare a statement on internal control. A possible model statement on internal control is reproduced in annex 3 to this document, but should be adapted to reflect the particular circumstance of the NHS foundation trust.

4.77 The Annual Report should also include a statement report that the board has conducted a review of the effectiveness of the trust's system of internal controls (*Code of Governance F.2.1*).

Quality Reports

NHS foundation trusts should include a report on the quality of care they provide within their annual report.

The aim of including a quality report is to improve public accountability for the quality of care.

The quality report must contain:

- A quality narrative, including:
  - a statement signed by the Chief Executive outlining the current position on quality and the trust's commitment to improving quality;
  - 3-5 priorities for quality improvement and the rationale for the selection of those priorities. The report should identify the quality improvement priorities for 2009/10 with the expectation of reporting on these in future annual reports. Trusts should consider including their current performance in these areas and the metrics against which they will track improvement, and any details of actions planned to improve performance;

    Where trusts have established quality improvement priorities for 2008/09 they should include the performance against each priority in the year of the report, and where possible the performance in previous years, and actions taken to improve quality for each of these priorities;
  - a response to any reports from regulators in relation to the quality of care offered by the trust and to concerns raised by bodies representing the public;
- A quality overview, including:
  - an overview of the quality of care offered by the NHS foundation trust based on performance in 2008/09 against indicators selected by the NHS foundation trust itself. The indicator set selected must include:
    - at least 3 indicators for patient safety;
    - at least 3 indicators for clinical effectiveness;
    - at least 3 indicators for patient experience;
  - for those indicators selected by the NHS foundation trust the report should include:
    - a reference of the data source for the indicators, including whether the data is governed by standard national definitions;
    - data for previous years, wherever possible, to enable readers to understand progress over time;
  - an overview of performance in 2008/09 against the key national priorities from the Department of Health's Operating Framework and against the Department of Health's National Core Standards. This must include:
    - performance against the relevant indicators and performance thresholds set

out in Appendix B of the Compliance Framework; and

- the number of core standards the NHS foundation trust has declared to the Healthcare Commission/Care Quality Commission that it is compliant with (displayed against the total number of core standards).

Annex 1 to Chapter 4: Summary of the requirements of Schedule 7 to the Regulations

Disclosure requirement	*Statutory Reference*
Where any market values of fixed assets are known to be significantly different from the values at which those assets are held in the NHS foundation trust's financial statements, and the difference is, in the directors' opinion, of such significance that readers of the accounts should have their attention drawn to it, the difference in values should be stated with as much precision as is practical.	***2 Sch 7***
Any political or charitable donations should be disclosed. However, it is doubtful whether any such donations would be lawful for an NHS foundation trust.	***3 to 5 Sch 7***
Any important events since the balance sheet date affecting the NHS foundation trust.	***7(1)(a) Sch 7***
An indication of likely future developments at the NHS foundation trust.	***7(1)(b) Sch 7***
An indication of any significant activities in the field of research and development.	***7(1)(c) Sch 7***
An indication of the existence of branches outside the UK.	***7(1)(d) Sch 7***
Policies applied during the financial year for giving full and fair consideration to applications for employment made by disabled persons, having regard to their particular aptitudes and abilities.	***10(3)(a) Sch7***
Policies applied during the financial year for continuing the employment of, and for arranging appropriate training for, employees who have become disabled persons during the period.	***10(3)(b) Sch 7***
Policies applied during the financial year for the training, career development and promotion of disabled employees.	***10(3)(c) Sch 7***
Actions taken in the financial year to provide employees systematically with information on matters of concern to them as employees.	***11(3)(a) Sch 7***
Actions taken in the financial year for consult employees or their representatives on a regular basis so that the views of employees can be taken into account in making decisions which are likely to affect their interests.	***11(3)(b) Sch 7***
Actions taken in the financial year to encourage the involvement of employees in the NHS foundation trust's performance.	***11(3)(c) Sch 7***
Actions taken in the financial year to achieve a common awareness on the part of all employees of the financial and economic factors affecting the performance of the NHS foundation Trust.	***11(3)(d) Sch 7***
In relation to the use of financial instruments, an indication of the financial risk management objectives and policies of the NHS Foundation Trust and the exposure of the entity to price risk, credit risk, liquidity risk and cashflow risk, unless such information is not material for the assessment of the assets, liabilities, financial position and results of the entity.	***6 Sch 7***
Disclosures in respect of policy and payment of creditors.	***12 Sch 7***

Annex 2 to chapter 4: Model statement of accounting officer's responsibilities

Statement of the chief executive's responsibilities as the accounting officer of xyz NHS Foundation Trust

The National Health Service Act 2006 states that the chief executive is the accounting officer of the NHS foundation trust. The relevant responsibilities of accounting officer, including their responsibility for the propriety and regularity of public finances for which they are answerable, and for the keeping of proper accounts, are set out in the accounting officers' Memorandum issued by the Independent Regulator of NHS Foundation Trusts ("Monitor").

Under the National Health Service Act 2006, Monitor has directed the [name] NHS foundation trust to prepare for each financial year a statement of accounts in the form and on the basis set out in the Accounts Direction. The accounts are prepared on an accruals basis and must give a true and fair view of the state of affairs of [name] NHS foundation trust and of its income and expenditure, total recognised gains and losses and cash flows for the financial year.

In preparing the accounts, the Accounting Officer is required to comply with the requirements of the NHS foundation trust Financial Reporting Manual and in particular to:

- observe the Accounts Direction issued by Monitor, including the relevant accounting and disclosure requirements, and apply suitable accounting policies on a consistent basis;
- make judgements and estimates on a reasonable basis;
- state whether applicable accounting standards as set out in the NHS foundation trust Financial Reporting Manual have been followed, and disclose and explain any material departures in the financial statements; and
- prepare the financial statements on a going concern basis.

The accounting officer is responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the NHS foundation trust and to enable him/her to ensure that the accounts comply with requirements outlined in the above mentioned Act. The Accounting officer is also responsible for safeguarding the assets of the NHS foundation trust and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

To the best of my knowledge and belief, I have properly discharged the responsibilities set out in Monitor's *NHS Foundation Trust Accounting Officer Memorandum*.

Signed………………..

Chief Executive Date: xx June 20xx

Annex 3 to chapter 4: Model statement on internal control

[The wording which is not in *italic* script in this pro forma statement on internal control (SIC) should be replicated in every SIC, the words in *italic* script being amended as appropriate to the body in question. **Bold** script indicates a rubric which should be fulfilled in a way appropriate to the actual processes in place in the body to which the SIC relates.]

Scope of responsibility

As Accounting Officer, I have responsibility for maintaining a sound system of internal control that supports the achievement of the NHS foundation trust's policies, aims and objectives, whilst safeguarding the public funds and departmental assets for which I am personally responsible, in accordance with the responsibilities assigned to me. I am also responsible for ensuring that the NHS foundation trust is administered prudently and economically and that resources are applied efficiently and effectively. I also acknowledge my responsibilities as set out in the NHS Foundation Trust Accounting Officer Memorandum.

The purpose of the system of internal control

The system of internal control is designed to manage risk to a reasonable level rather than to eliminate all risk of failure to achieve policies, aims and objectives; it can therefore only provide reasonable and not absolute assurance of effectiveness. The system of internal control is based on an ongoing process designed to identify and prioritise the risks to the achievement of the policies, aims and objectives of XYZ NHS Foundation Trust, to evaluate the likelihood of those risks being realised and the impact should they be realised, and to manage them efficiently, effectively and economically. The system of internal control has been in place in XYZ NHS Foundation Trust for the year ended 31 March [200X] and up to the date of approval of the annual report and accounts.

As an employer with staff entitled to membership of the NHS Pension Scheme control measures are in place to ensure all employer obligations contained within the Scheme regulations are complied with.

Capacity to handle risk

[Describe the key ways in which:

- leadership is given to the risk management process; and
- staff are trained or equipped to manage risk in a way appropriate to their authority and duties. Include comment on guidance provided to them and ways in which you seek to learn from good practice.]

The risk and control framework

[Describe the key elements of the risk management strategy, including the way in which risk (or change in risk) is identified, evaluated, and controlled. Include mention of how risk appetites are determined.

[Describe key ways in which risk management is embedded in the activity of the organisation.]

[Describe the key elements of the way in which public stakeholders are involved in managing risks which impact on them.]

[Specific reference should be made to information on governance and, in particular, identifying and managing information risks.]

Review of economy, efficiency and effectiveness of the use of resources

[Describe the key process that has been applied to ensure that resources are used economically, efficiently and effectively, including some comment on the role of the board, internal audit and any other review or assurance mechanisms.]

Review of effectiveness

As Accounting Officer, I have responsibility for reviewing the effectiveness of the system of internal control. My review of the effectiveness of the system of internal control is informed by the work of the internal auditors and the executive managers within the NHS foundation trust who have responsibility for the development and maintenance of the internal control framework, and comments made by the external auditors in their management letter and other reports. I have been advised on the implications of the result of my review of the effectiveness of the system of internal control by the board, the audit committee [and risk committee, if appropriate] and a plan to address weaknesses and ensure continuous improvement of the system is in place.

[Describe the process that has been applied in maintaining and reviewing the effectiveness of the system of internal control, including some comment on the role of:

- the board;
- the audit committee;
- if relevant, the risk committee/risk managers/risk improvement manager;
- internal audit; and
- other explicit review/assurance mechanisms.

Include an outline of the actions taken, or proposed to deal with any significant internal control issues and gaps in control, if applicable.]

Conclusion

[state either that no significant internal control issues have been identified or make specific reference to those significant internal control issues which have been identified in the body of the SIC above]

Signed………………..
Chief Executive Date: xx June 20xx

5. Adoption of International Accounting Standards in 2009/10

Introduction

5.1. This chapter describes, in general terms, the impact that the transition to IFRS may have on the financial reporting of NHS foundation trusts. It is based on the experience of listed companies when they undertook the transition a few years ago, together with an evaluation of the accounting requirements in the near final draft of the Treasury IFRS-based FReM and existing NHS foundation trust accounting requirements and practices.

5.2. A key message from the private sector experience is that the 'devil is in the detail'. The comments in this chapter are therefore intended to give only an overall assessment of the potential impact for NHS foundation trusts in general. However, individual standards may impact different NHS foundation trusts in different ways due to the nature of local transactions.

5.3. The chapter is divided into the following sections:

- areas of greatest likely impact; and
- other areas of possible significant impact.

5.4. This can only be a general picture of those standards likely to have the most significant impact. Where a standard is not described below it is likely, nevertheless, to have some impact on financial reporting, and NHS foundation trusts should ensure that they consider the impact of all IFRS requirements on their transactions and that they comply with the requirements of IFRS, as interpreted by this manual, in all material respects.

Areas of greatest likely impact

5.5. This section describes the areas of IFRS which Monitor anticipates will have the greatest impact for most or all NHS foundation trusts:

- private finance initiative (PFI) contracts;
- leases; and
- segmented operations.

5.6. The UK GAAP standards which deal with financial instruments – FRS 25, 26 and 29 – are effectively identical to the international standards and have been adopted in this 2007/08 NHS foundation trust FReM. Thus, although implementation of these standards may be a issue for NHS foundation trusts – for example, in respect of embedded derivatives – it does not represent a change arising from the conversion to IFRS in 2009/10.

Private finance initiative (PFI) contracts

5.7. The ‘Control’ approach under IFRIC Interpretation 12 ‘Service Concession Arrangements’ is very different to the present ‘Risk and Reward’ approach under Application Note F to FRS 5 and the Treasury Taskforce Technical Note Number 1. The new requirements mean that it is likely that some PFI schemes held by NHS foundation trusts will need to be recognised ‘on-balance sheet’ under IFRS. Where a scheme is brought ‘on balance sheet’, the property assets will need to be recognised along with an equivalent financial liability. Where there are deferred assets and residual interest assets associated with off-balance sheet PFI schemes at present, these will need to be de-recognised. The annual Unitary Payment will need to be split between a services element (which would continue to be expensed) and a property element which in turn would need to be split into an element to reduce the financial liability and an annual finance charge.

Leases - IAS 17

5.8. The international standard for leases matches the UK equivalent insofar as it distinguishes between finance and operating leases. The ‘90% test’ found in SSAP 21 does not appear in IAS 17, but there are a number of qualitative indicators to distinguish between finance and operating leases, which are consistent with the principles of SSAP 21.

5.9. A significant difference between the two standards is in respect of leases of land and buildings. Under IAS 17, all such leases must be split between the land component and the building component, and each assessed separately. Furthermore, the international standard requires that all land leases are treated as operating leases (due to the emphasis that the standard places on residual value risk which always lies with the freeholder).

5.10. In practice this means that:

- finance leases that include land will have to be split and the land element reclassified as an operating lease;
- operating leases of land and buildings will need to be split and the building element considered separately. In some cases this might result in the building element being reclassified as a finance lease; and
- where land acquired on a long lease through an up-front lease premium is currently recorded as a fixed asset (with no finance lease liability recognised), the lease will need to be reclassified as an operating lease and appropriate accounting adjustments made e.g. reclassifying the lease premium as a prepayment within current assets.

5.11. A number of complications may arise when an NHS foundation trust analyses its lease arrangements, for example:

- lease documentation may be difficult to locate, incomplete or even missing; or
- determining the split of the lease between the land and building elements may require a significant degree of subjective judgement.

5.12. Another significant difference in implementing international standards relates to IFRIC 4 ‘Determining whether another arrangement contains a lease’. Under this interpretation, arrangements should be assessed to determine whether they contain leases that should be accounted for in accordance with IAS17.

5.13. There are many arrangements in the NHS whereby one NHS body uses facilities and services belonging to another. Often these arrangements are informal in nature and each party simply accounts for a revenue transaction without recognising any underlying lease. All such arrangements will need to be analysed and may result in more leases being recognised than currently.

Segmented operations - IFRS 8

5.14. NHS foundation trusts typically have not disclosed segmented operations under UK GAAP, instead often treating 'Healthcare' as one segment. Under IFRS, NHS foundation trusts will need to provide disclosures on significant segments of their operations.

5.15. IFRS 8 places emphasis on reporting disclosures that reflect the way that management runs the entity. This involves firstly identifying the Chief Operating Decision Maker (CODM), which is the person or persons who receive and monitor financial information analysed by internal segments and uses that information to allocate resources. The significant segments that are reported internally are then the ones that are required to be disclosed in the financial statements. A significant segment is one whose revenue is at least 10% of the entity's overall revenues. If an NHS foundation trust does not report revenues for segments in its internal reporting, then Monitor is proposing an interpretation that reportable segments should be identified instead by reference to regulatory reporting requirements.

5.16. The information disclosed in the accounts reflects exactly that reported internally i.e. if it includes internal revenues and recharges then these are reported in the financial statements and the items need not be on an IFRS basis. There is however a requirement to include a reconciliation of the amounts reported in these segments to the total amounts reported in the financial statements.

Other areas of possible significant impact

Presentation of financial statements - IAS 1 & 7

Statement of Comprehensive Income (IAS 1, Revised)

5.17. Under IAS 1 (Revised), entities are required to prepare a Statement of Comprehensive Income which will effectively combine the present Income and Expenditure Account and Statement of Total Recognised Gains and Losses.

5.18. The standard does not prescribe the format of the statement, but does require the following items to be recorded on the face of the statement:

- Revenues
- Finance costs
- Share of profit/loss of associates and joint ventures accounted for using the equity method
- Tax expense
- Post-tax profits and losses of discontinued operations
- Profit or Loss (where applicable split between that attributable to minority interests and that attributable to equity holders of the parent)
- Other items of recognised income and expense (e.g. revaluation gains/losses on property, plant and equipment)

5.19. An analysis of expenses must be given either on the face of the Statement of Comprehensive Income (the standard's preference) or in a note to the accounts. This analysis must be either by the nature of the expense (e.g. staff costs, depreciation) or by the function (e.g. cost of sales, administrative expenses).

Balance Sheet

5.20. IAS 1 includes the minimum requirements for disclosing information on the face of the balance sheet. These are similar to present UK GAAP requirements, although 'Assets held for disposal' are required to be disclosed separately.

5.21. There are two options for the structure of the balance sheet. The standard's preferred option is to disclose current and non-current assets and current and non-current liabilities as separate classifications. The second option is to structure the balance sheet in the order of liquidity where that provides information that is more relevant and reliable.

5.22. To promote consistency and comparability, HM Treasury has removed the liquidity option in its draft IFRS-based FReM, and this is likely to be replicated in the 2009/10 IFRS-based NHS foundation trust FReM.

Cashflow Statement - IAS 7

5.23. There are two significant differences under IFRS that will affect NHS foundation trusts, but these reflect changes to the structure of the statement rather than requiring more information to be disclosed. Firstly, transactions in the Cashflow Statement need to be reported under three sections: Operating, Investing and Financing, compared with the current requirement to report under nine standard headings.

5.24. Secondly, under IFRS, the Cashflow statement reports movements in cash and cash equivalents rather than simply cash as at present. The definition of cash equivalents is effectively the same as 'liquid resources' under FRS 1, and therefore in practice the cashflows currently reported under 'management of liquid resources' would simply move to the end of the statement.

Statement Changes in Equity (SoCiE)

5.25. IAS 1 (Revised) requires other movements in equity to be shown in a Statement of Changes in Equity (SoCiE). In practice this statement is equivalent to the combination of the present Movement in Reserves note and the Movement in Public Dividend Capital note.

Accounting policies - IAS 8

5.26. IAS 8 requires that entities adopt those accounting policies that provide the most relevant and reliable information. Changes of accounting policy should only occur where they will provide more relevant and reliable information.

5.27. When selecting accounting policies, the standard provides a hierarchy of guidance for entities to follow. Entities should refer initially to any international standards or interpretations and then to the IASB Framework. In the absence of a standard or interpretation, when deciding on a policy, entities may also refer to recent pronouncements of other standard-setting bodies that use a similar conceptual framework (such as UK GAAP), other accounting literature and accepted industry practices provide that none of these conflict with an international standard, interpretation or the IASB Framework. However, NHS foundation trusts should always consult the IFRS-based NHS foundation trust FReM in the first instance in any cases where they have transactions for which there is no IFRS requirement or guidance.

5.28. Where a new international accounting standard has been issued, but not yet implemented then entities are required to disclose in their financial statements the nature of the standard, and if possible, an estimate of its likely effect on future financial statements. In the private sector 'issued' has been interpreted widely, so that it includes standards issued by the IASB even if they haven't yet been adopted by the EU (and therefore couldn't yet be implemented).

5.29. When considering how to correct errors in the accounts, IAS 8 does not have the distinction between fundamental errors and other errors that exists in UK GAAP. Under IFRS, where an error is material, it must be corrected through a prior period adjustment. This contrasts with UK GAAP where a prior period adjustment to correct an error is only permitted where the effect is fundamental to one or more prior year accounts. Under IFRS therefore, one might expect to see more prior period adjustments to correct errors in accounts.

Tangible fixed assets - IAS 16, 23 & 36, IFRS 5 (part)

General requirements - IAS 16

5.30. IAS 16 is the main standard dealing with property, plant and equipment and is generally very similar to its UK GAAP equivalent (FRS 15). Both FRS 15 and IAS 16 permit fixed assets to be held at cost or at a valuation. The draft HM Treasury IFRS-based FReM continues the previous HM Treasury FReM practice of requiring assets to be held at valuation and this is likely to be replicated in the 2009/10 IFRS-based NHS foundation trust FReM.

5.31. There are significant differences between the requirements of the other three standards and the current FT FReM in respect of borrowing costs, impairments and assets held for disposal.

Borrowing costs - IAS 23

5.32. A revised version of the IAS 23 was issued in March 2007 and requires interest costs on specific borrowings to be capitalised as part of the fixed asset cost. This represents a departure from previous practice by UK government bodies but nevertheless, HM Treasury have adopted the revised standard in their draft IFRS-based FReM.

5.33. However, the requirements of the standard are not mandatory for assets held at fair value, and thus do not apply to NHS foundation trusts as Monitor has adopted the Valuation Approach under IAS 16. Under IAS 23 such entities do still have the option to capitalise borrowing costs for initial measurement of the assets prior to the first revaluation, but Monitor is likely to choose not to permit NHS foundation trusts to exercise this option to capitalise borrowing costs for initial measurement.

Impairment of fixed assets - IAS 36

5.34. Under UK GAAP, a distinction is drawn between impairments arising from a loss of economic benefit to the asset itself e.g. physical damage, and other impairments. Impairments of the former type are charged directly to the Income and Expenditure Account. Other impairments, however, are charged initially to the Revaluation Reserve to the extent that it contains a balance in respect of that asset, and only thereafter, to the Income and Expenditure Account.

5.35. Under IAS 36, there is no such distinction between an impairment arising from a loss of economic benefits and other impairments. All impairments are therefore charged initially to the Revaluation Reserve, to the extent that there is an available balance for that asset, and only thereafter to operating expenses if necessary. Consequently, under IFRS, it is likely that fewer impairments will be charged to operating expenses.

Assets held for sale - IFRS 5 (part)

5.36. The present requirements under UK GAAP and the FT FReM are that, where assets are measured at valuation, any assets that become surplus to requirements and earmarked for disposal should be held at Open Market Value. Under IFRS, where assets are marked for disposal and meet certain requirements e.g. capable of being sold immediately and being actively marketed, they fall within the scope of IFRS 5.

Under this standard, the assets are then held at the lower of their carrying value and 'fair value less costs to sell'.

5.37. This may have a significant impact for NHS foundation trusts, due to the fact that most healthcare properties are considered to be specialised and, as noted above, are generally held at DRC. This valuation is usually lower than the open market value (OMV) of the site, because the latter will reflect possible alternative uses such as residential use, and therefore such assets would not be re-valued to an amount more closely reflecting their OMV. There is thus a greater likelihood under IFRS of NHS foundation trusts recording profits on disposal in operating income when they sell fixed assets. However, there should not be any overall impact on the I&E reserves of NHS foundation trusts as presently under UK GAAP the gain in value is recognised initially in the revaluation reserve but then any balance attributable to the asset is transferred from the revaluation reserve to the Income and Expenditure Reserve when the disposal is recognised in the accounts.

Donated assets

5.38. Under IFRS there are no accounting requirements for recording the gain arising from the receipt of donated assets. Applying the hierarchy approach to selecting accounting policies, the most relevant guidance is in the UK ASB's Statement of Principles for Public Benefit Entities, which requires Application Note G to FRS 5 to be followed. In practice this means that when a donated asset is received, the entire credit is recognised as operating income in the year of receipt rather than in a donated asset reserve.

Intangible fixed assets - IAS 38

5.39. There are two significant differences between UK GAAP and IAS 38. The first is a requirement to recognise more intangible assets acquired through acquisition of another entity in a business combination. As discussed below, the use of acquisition accounting by NHS foundation trusts is likely to be rare and therefore this difference is likely to have a limited impact in practice.

5.40. The second difference is that, where certain criteria are met, development expenditure must be capitalised. This contrasts with SSAP 13 where entities have the choice as to whether to capitalise development costs. At present few NHS foundation trusts recognise internally generated intangible assets and thus it is difficult to gauge the types of activities being undertaken and whether they might require recognition as intangible assets under IFRS.

5.41. Under IAS 38, intangible assets are initially measured at cost, but thereafter entities have a choice between continuing to measure them at cost or at a valuation. The Treasury's draft IFRS-based FReM removes the cost option and requires bodies to measure them at valuation. Monitor is likely to follow this approach in its 2009/10 IFRS-based FT FReM and specify the use of the valuation approach.

5.42. An additional point is that, unlike UK GAAP, accounting for software costs is specifically addressed under IAS 38. Where purchased software is integral to the operation of an item of hardware, for example operating system software, then the cost should be capitalised as part of that item of property, plant and equipment. Where the software is not integral to operating the hardware for example, application software, this should be capitalised as an intangible fixed asset. Many NHS foundation trusts already capitalise application software as intangible fixed assets. Where operating system software is currently capitalised as an intangible fixed asset, this will require reclassification and included as part of the item of property, plant and equipment to which it relates.

Employee benefits - IAS 19

5.43. This standard deals with both current employee benefits such as salaries, and retirement benefits.

Current employee benefits

5.44. For current employee benefits, the requirements are generally straightforward. There is, however, one area where a significant impact may occur for NHS foundation trusts, in respect of holiday pay, due to the fact that UK entities – both public and private sector – have not generally recognised accruals for holiday pay earned by employees which they have not taken but to which they remain entitled, at the balance sheet date.

Retirement benefits

5.45. The requirements here are similar to those of FRS 17, such as the distinction between defined benefit schemes and defined contribution schemes. Where multi-employer defined benefit schemes exist and the assets and liabilities cannot be split between the relevant parties then, as with FRS 17, they can be accounted for as defined contribution schemes. However, a difference under IAS 19 is that it assumes that all employers are members of the same group and therefore requires that one of the group companies recognises the overall scheme assets and scheme liabilities in its accounts. This requirement doesn't translate easily to the UK public sector schemes such as the NHS Pension Scheme, but here the requirement appears to be satisfied by the fact that the NHS Pension Scheme prepares its own resource accounts, which are aggregated into the Whole of Government Accounts and which include the present value of future scheme liabilities.

5.46. Thus NHS foundation trusts should continue to account for the NHS Pension scheme as a defined contribution scheme. In this circumstance there are additional disclosure requirements under IFRS, but FRS 17 itself has been amended to reflect these requirements, and this amendment has been adopted in this 2007/08 NHS foundation trust FReM.

5.47. There may be some NHS foundation trusts with former local government employees who remain members of the Local Government Pension Scheme (LGPS). The LGPS is also a multi-employer defined benefit scheme, but the assets and liabilities are generally capable of being identified separately between the employers and thus NHS foundation trusts should currently be accounting for their share as a defined benefit scheme. This should continue under IFRS, where the accounting requirements are similar to FRS 17, except in respect of accounting for actuarial gains and losses.

5.48. Under IAS 19, entities can choose to recognise actuarial gains and losses in one of three ways:

- recognise all such gains and losses (few entities use this option); or
- recognise all such gains and losses in reserves (the equivalent to current FRS 17 practice); or
- use a 'corridor approach' whereby gains and losses up to a threshold can be recognised in reserves, with the remainder (if any) required to be recognised as revenue income or expense, but spread over the average remaining working lives of the employees (similar to the old SSAP 24 principle for pension fund surpluses or deficits).

5.49. The Treasury, in its draft IFRS-based FReM has prohibited the use of the corridor approach for the recognition of actuarial gains and losses on defined benefit pension schemes. Although of limited application to NHS foundation trusts, Monitor is likely to do the same in its 2009/10 IFRS-based NHS foundation trust FReM and require NHS foundation trusts to recognise all actuarial gains and losses directly in reserves.

Related party disclosures - IAS 24

5.50. The requirements of IAS 24 are similar to those of FRS 8, but most of the disclosure exemptions that the latter has do not appear in the international standard, for example, transactions with parents or subsidiaries.

5.51. IAS 24 requires various disclosures of key management compensation, which are not satisfied by the disclosure requirements for directors remuneration under the Companies Act 2006 (which remains relevant under IFRS) and thus additional disclosures may be needed to comply with the standard. For example, under IAS 24, the structure of the disclosures is different, with management compensation required to be analysed between: short term employee benefits; post-employment benefits; other long term benefits; termination benefits and share-based payments. Within this, the items to be included can be different to the Companies Act disclosures, for example short term benefits includes social security contributions, which in the UK would also encompass employers' national insurance contributions.

5.52. The IAS requires the disclosures to be included in the notes to the financial statements. Where, therefore, the Remuneration Report is included in the Annual Report rather than the financial statements, the IFRS disclosures will still have to be included in the notes to the financial statements.

5.53. There is no exemption from disclosure under IAS 24 in instances where disclosure would conflict with an entity's legal duty of confidentiality.

Consolidated accounts and business combinations - IAS 27, 28 & 31, IFRS 3 & 5 (part)

5.54. HM Treasury's draft IFRS-based FReM adopts IAS 27, 28 and 31 in full, but retains the override from the existing FReM that consolidation encompasses only those entities within the Departmental Boundary, regardless of whether they should be a subsidiary, associate, joint venture or joint arrangement under the standards. This override is not relevant to NHS foundation trusts as they lie entirely outside resource accounting boundaries. They thus must follow the requirements of the standards.

Subsidiary undertakings - IAS 27

5.55. The requirements for recognising entities as subsidiaries under IAS 27 are identical to those of UK GAAP following the latter's amendment a few years ago to bring it into line with IFRS, so that where entities have the power to control or exercise a dominant influence over another entity so as to obtain benefits, this is sufficient to require recognition as a subsidiary.

Associated undertakings - IAS 28

5.56. The concept of an associated undertaking under IAS 28 is similar to that of FRS 9, but there are two significant differences. Firstly, recognition of an entity as an associate under IFRS requires merely the power to exercise a significant influence over it to gain access to economic benefits, rather than FRS 9's recognition criteria of having the power to exercise a significant influence to gain access to economic benefits **and** actually exercising that influence. It is therefore likely that more entities would qualify for recognition as associated undertakings under IFRS.

5.57. The second area of difference is that FRS 9 only requires entities to equity account for associates where they are already preparing group accounts; otherwise they can simply record them as a fixed asset investment. Under IAS 28, equity accounting of associates is required even where group accounts are not already being prepared. The effect of these two differences is that the accounts of NHS foundation trusts may include equity-accounted associates more frequently than is currently the case under UK GAAP.

Joint venture and joint arrangements - IAS 31

5.58. There are no significant differences between FRS 9 and IAS 31 in respect of joint venture and joint arrangements.

Business combinations – IFRS 3

5.59. IFRS 3 'Business combinations' differs significantly from FRS 6 and 7 insofar as merger accounting is not permitted and all business combinations are deemed to have an acquirer and an acquiree. However, the standard excludes from its scope transactions which meet the definition of 'Group reconstructions'. The definition is similar to the existing provisions for business combinations involving 'Entities under common control' in FRS 6. The Treasury has continued its existing FReM interpretation that any transfer of responsibilities or services from one part of the public sector to another is a 'machinery of government change' and qualifies as a group reconstruction. Such transactions therefore fall entirely outside the scope of IFRS 3, and there are no specific accounting requirements for these under IFRS. The hierarchy of guidance for selecting accounting policies under IFRS means that relevant UK GAAP requirements can be applied. The Treasury has done this and has retained the concept of merger accounting for 'machinery of government changes' in the draft IFRS-based FReM.

5.60. Monitor is likely to apply the Treasury interpretation in its 2009/10 IFRS-based foundation trust FReM and as such all transfers of services between NHS foundation trusts and other public sector bodies should be treated as 'machinery of government changes' and accounted for using merger accounting principles.

5.61. Where an NHS foundation trust purchases a business from outside the public sector, then the provisions of IFRS 3 will apply in full.

Discontinued operations – IFRS 5 (part)

5.62. IFRS 5 contains requirements in respect of discontinued operations, in a manner similar to FRS 3 under UK GAAP, although with more restrictive criteria before entities can recognise operations as discontinuing. As with business combinations, any transfer of services to another part of the public sector would not count as a discontinued operation but as a machinery of government change requiring the application of merger accounting. Thus NHS foundation trusts should only recognise discontinued operations where the activities have actually ceased to be provided or have been sold or transferred to a non-public sector body.

Investment Property - IAS 40

5.63. Foundation trusts are unlikely to hold investments properties themselves although some may do. NHS Charitable Funds may, however, hold such properties. Where the charitable funds are consolidated into the accounts of the NHS foundation trusts, any investment properties would need to be accounted for in accordance with IAS 40 in the consolidated accounts.

5.64. The principles of IAS 40 are similar to UK GAAP but there are some important differences. Most significantly, IAS 40 permits entities to measure investment properties either at cost or at fair value. This contrasts with SSAP 19 where entities must measure properties at Open Market Value. Monitor is likely to follow the Treasury's lead and prohibit the use of the cost option in its IFRS-based NHS foundation trust FReM.

5.65. Where properties are held at fair value, IAS 40 requires any movements to be taken to revenue income or expense. SSAP 19, by contrast, requires movements in open market value to be taken to a revaluation reserve, with only permanent diminutions in value being recognised in income and expenditure. Where NHS foundation trusts or their charitable funds, hold investment properties this could lead to greater volatility in the annual surplus or deficit.

Taxation - IAS 12

5.66. Commercial-type activities of NHS foundation trusts are potentially subject to corporation tax. While the approach to current tax assets and liabilities under IFRS is similar to UK GAAP, the requirements for deferred tax assets and liabilities is conceptually different from UK GAAP. This means that for those activities which are subject to taxation, there may be a requirement to recognise more deferred tax assets and liabilities than at present, and the amounts involved are likely to be greater.

Monitor

Independent Regulator
of NHS Foundation Trusts