
Policy

Elexon Treasury Policy

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Classification **Public**

Policy owner **Elexon Finance**

Document version **4.0**

1. Objective

The objectives of this policy are:

- To protect our business from future banking failures
- To ensure staff know their roles and responsibilities
- To be clear and transparent to our customers

2. Scope

To set out appropriate parameters as deemed fit by the Board for Elexons banking arrangements, in order to minimise counterparty risk, while delivering a reasonable rate of return on the Elexon Group cash balances and being able to meet the organisation's financial obligations. There are three core objectives this policy covers; security, liquidity and yield.

The primary objective is to ensure the preservation of principal when investing. Liquidity should also be maintained such that the Group should seek to avoid having cash investments whilst it has any short-term requirements for funds. Yield should only determine an investment decision when deciding between two or more instruments which satisfy the first two objectives.

3. Background

Modification P249 proposed to revise the BSC banking arrangements in order to enable the BSC Clearer to invest a proportion of the monies lodged in the Reserve Account in financial institutions other than the BSC Banker, and to provide capability for these monies to be invested on term deposit. This arrangement is intended to enhance the rate of return for Trading Parties on the cash balances lodged in the Reserve Account.

4. Responsibility

Elexon Board and Finance Team

5. Policy

Introduction

- 5.1. Due to the nature of Elexon's cost recovery model, where by BSC costs are invoiced one month in advance, Elexon Ltd always maintains a cash surplus. In addition to this, Elexon Clear holds some of the credit cover for imbalance charges in cash.
- 5.2. In order to minimise counterparty risk, Elexon will spread funds across a range of financial institutions. However as the funds in question ultimately belong to Trading Parties, Elexon will adopt a low risk approach, and the policy therefore reflects this by establishing stringent criteria for the selection of financial institutions.
- 5.3. Improved returns are achievable through the selection of investments with longer maturity; however Elexon must be mindful of liquidity requirements. This is dealt with by ensuring accurate cashflow forecasting, and establishing parameters within this policy for the permitted term of any deposits.

5.4. There shall be no cross subsidising of funds between Elexon Limited and Elexon Clear Limited

Instruments & Currencies

5.5. Surplus funds will only be invested in UK bank/ building society deposits or corporate savings accounts, denominated in pounds sterling.

Selection Criteria

5.6. Elexon Group funds will only be invested with Financial Service Authority (FSA) regulated UK financial institutions, i.e. banks or building societies incorporated in the UK, with a registered office in the UK and authorised and regulated by FSA. In addition, only banks or building societies obtaining a satisfactory rating – at least an A grade (high quality/upper medium grade/strong) – with Standard and Poors, Fitch and Moody's will be selected. Finance will monitor the ratings, and should an institution fall below the required level they will be deselected at the next possible time (i.e. when funds are due for re-investing). The minimum required ratings are shaded in the table below:

| International Long Term Credit Ratings | Fitch Ratings | Moody's | S&P |
|--|---------------|---------|-----|
| Investment Grade | | | |
| Highest quality/ Best quality/ Extremely strong | AAA | Aaa | AAA |
| Very high quality/ High quality/ Very strong | AA | Aa | AA |
| High quality/ Upper medium grade/ Strong | A | A | A |
| Good quality/ Medium grade/ Adequate | BBB | Baa | BBB |
| Non-investment grade | | | |
| Speculative/ Lower medium grade/ Speculative- less vulnerable | BB | Ba | BB |
| Highly speculative/ Low grade/ More vulnerable | B | B | B |
| Poor quality/ currently vulnerable | CCC | Caa | CCC |
| High default risk/ Highly speculative/ Currently highly vulnerable | CC | Ca | CC |
| High default risk/ Extremely poor/ Imminent default | C | C | C |
| In default | D | C | D |

Note: Fitch Ratings and Standard and Poor's may append their ratings with '+' or '-' to denote relative status within major rating categories. Moody's may append their ratings with '1', '2' or '3' to denote relative status.

5.6. A counterparty will have to have equivalent A ratings with 2 out of the 3 rating agencies. If an entity is on credit watch negative, then the limit to be applied should be taken as the limit for one rating notch lower.

5.7. In the event that a limit is exceeded because of a downgrade after the original investment was made, the Finance and Commercial Director will review the risks and possible flexibility to come back within limit. Any investments remaining in excess of limit will be reported to the Board as part of the monthly report.

Spreading Proportions and Main Account Liquidity

5.8. For the purpose of security and risk diversification, the following limits will be placed on the institutions depending on their credit ratings. The exception to this rule is Barclays Bank Plc who remains the Group's main banker (Main Account) through whom all regular daily transactions are processed.

- 5.9. Elexon Ltd and Elexon Clear will each use no more than five financial institutions at any one time in order to reduce multiple counterparty exposures.
- 5.10. Sufficient liquidity should be maintained in the Main Account to enable access to cash cover monies within current timescales.
- 5.11. For Elexon Clear, the minimum amount we endeavour to retain in the Main Account will be equivalent to the single largest deposit of cash cover plus a further 10% of the overall balance held.
- 5.12. For Elexon Limited, when deciding the amount of funds to be maintained in the Main Account consideration will be given to liquidity by the Finance Team by referring to the cash flow forecast.
- 5.13. Investment limits will be applied to each legal entity individually, rather than as a group.

| Investment Grade | Investment Limit £(m) |
|------------------|-----------------------|
| AAA/Aaa | 25 |
| AA/Aa | 20 |
| A | 15 |

Term of Investment

- 5.14. The main purpose of spreading funds is to minimise risk as opposed to aggressively pursuing maximum yields. The longer the time to maturity of any investment, the better the return, however consideration must be given to minimising risk and ensuring sufficient funds to meet Elexon's obligations; therefore security and liquidity are of greater importance than yield.
- 5.15. Subject to satisfactorily assessing liquidity requirements through cashflow forecasting, funds may be placed with a financial institution for longer than overnight, subject to a maximum period of 3 months.
- 5.16. The 3 month limit doesn't apply to corporate savings accounts in which we have instant access to money invested.

Treatment of Gains and Losses

- 5.17. The principle for treating gains and losses will differ slightly between Elexon Ltd and Elexon Clear.
- 5.18. Any interest earned or any losses suffered in relation to Elexon Ltd funds lodged will be offset against, or added to, BSC Co costs and will therefore be spread across the industry on the basis of Funding Shares, in the same manner as all regular costs.
- 5.19. Interest earned on Elexon Clear funds will be paid to Trading Parties who have physical funds on deposit in proportion to their share of the overall total of all cash lodged with the FAA, on a quarterly basis, as is the current practice. Similarly, any losses suffered will be borne by Trading Parties in proportion to their share of overall deposits lodged.

Responsibilities & Reporting

- 5.20. Investment selection will be approved by the Finance and Commercial Director, within the constraints of this policy. This document will be reviewed by the Board from time to time as they see fit or when there are significant changes proposed. Any change will come into effect 15 working days after publication.
- 5.21. When requested, investment decisions will be reported to the Board as part of the monthly Finance report. This will cover investment decisions taken in the month, investment performance, as well as any breaches of limits.

6. Document History

| Version | Date | Author | Reviewer | Reason for review |
|---------|------------|--------|----------|---------------------|
| 1.0 | | DAD | NPS | Initial Draft |
| 2.0 | | DAD | NPS | Periodic Review |
| 3.0 | 12/09/2018 | DAD | YAM | Housekeeping update |
| 4.0 | 17/09/2021 | DAD | YAM | Housekeeping update |
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7. Related Documents

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| EAC 29/03 – Elexons Banking Arrangements |
| EAC 30/06 - Elexon's Banking Arrangements |
| EAC 31/06 - Elexon's Banking Arrangements |
| EB103/06 - Draft Treasury Policy |
| EB118/03 – Revised Treasury Policy |
| Finance Team – Banking LWI |