

*United Kingdom*  
**Debt  
Management  
Office**

Cheapside House  
138 Cheapside  
London  
EC2V 6BB

# **EXCHEQUER CASH MANAGEMENT OPERATIONAL NOTICE**

**Issued: 29 July 1999**



# **OPERATIONAL NOTICE FOR THE UNITED KINGDOM DEBT MANAGEMENT OFFICE'S ("DMO") EXCHEQUER CASH MANAGEMENT OPERATIONS**

This notice (the "Operational Notice") sets out the arrangements for the DMO's Exchequer cash management operations ("cash management")<sup>1</sup>. It outlines the typical cash management operations the DMO will undertake although these may vary over time. This Operational Notice will be revised from time to time.

Any questions on this notice should be addressed to Jo Whelan or Mike Ness at the United Kingdom Debt Management Office, Cheapside House, 138 Cheapside, London EC2V 6BB.

<u>List of contents</u>	<u>Page number</u>
Introduction	2
Treasury bills	3
Structured tenders	3
Ad hoc tenders	6
Bilateral dealing	9
Dealing relationship with counterparties	10
<u>Appendices</u>	
Treasury bill settlement convention	13
Telephone dealing arrangements	14
Dealing Room Voice Systems	16

---

<sup>1</sup> Further information on the DMO's proposed cash management arrangements are set out in "UK Government Cash Management: The New Framework" issued in December 1998. The DMO's gilts operations are set out in the Operational Notice "Operations in the Gilt-Edged Market". Both documents are available on request from the DMO and also appear on the DMO's website ([www.dmo.gov.uk](http://www.dmo.gov.uk)).

## **INTRODUCTION**

The Chancellor of the Exchequer's letter to the Governor of the Bank of England of 6 May 1997 set out details of the new monetary policy framework and the transfer of sterling government debt and cash management responsibilities from the Bank to HM Treasury. The DMO, an Executive Agency of HM Treasury, took over responsibility for debt management on 1 April 1998. The Chancellor's decision to transfer cash management responsibilities to the DMO was predominantly intended to clarify the roles of the Bank and HM Treasury to avoid any perception of conflicts of interest in market operations conducted by these institutions.

The transfer of responsibility for cash management to the DMO from the Bank will take place in stages including the enactment of the relevant secondary legislation. An indicative timetable has been published by the DMO and will be confirmed nearer the time of commencement.

The DMO will aim to smooth, in a cost-effective way, the forecast net daily cash flows across the central government accounts at the Bank of England. This will be managed firstly through the structured (ie weekly) Treasury bill programme and then through daily market operations. The DMO would therefore plan to run down the Treasury bill stock in months of positive cash flows and then increase it in months of higher net expenditure.

The DMO and the Bank will work to avoid clashes in the delivery of their respective objectives. The DMO will not therefore take speculative positions on interest rate decisions by the Bank nor hold certain operations which could be perceived to clash with the Bank's Open Market Operations ("OMOs").

Notwithstanding this, and although the DMO intends to conduct its cash management operations in accordance with the provisions contained in this Operational Notice, it will act at all times in accordance with its published objectives and will operate as required in order to achieve these objectives.

## **TREASURY BILLS**

1. Treasury bills issued after the transfer of cash management will be issued from, and be liabilities of, the Debt Management Account (“DMA”). This will not, however, change the fundamental nature of the instrument and they will continue to be negotiable, bearer, zero-coupon obligations of Her Majesty’s Government, with recourse to the National Loans Fund (“NLF”) and the Consolidated Fund. They will have a maximum time to maturity at issue of 364 days and will continue to be paid on maturity on presentation to the Bank of England. The bidding, settlement and administrative arrangements for weekly Treasury bill tenders (“structured tenders”) will however be slightly modified; the key features of the new arrangements are set out below.

## **STRUCTURED TENDERS**

### Timetable

2. Structured tenders will be held on the last business day of each week (ie usually on Fridays). Following the final structured tender at the end of each calendar quarter, the DMO intends to issue a notice broadly outlining the maturities of Treasury bills available in each week of the next quarter. The quantities of Treasury bills on offer and the maturity of bills on offer in each week would be announced one week prior to the relevant tender.

### Maturities

3. The DMO intends to issue bills with maturities of 1 month (approximately 28 days), 3 months (approximately 91 days), 6 months (approximately 180 days) and to a lesser extent 12 months (364 days) with up to two sets of bills with different maturity dates being made available at each structured tender. Bills issued via structured tenders will mature on the first business day of the week, four weeks, thirteen weeks, twenty six weeks or fifty one weeks respectively following the issue date, which will be the first business day of the week following the tender. If Treasury bills are due to be issued or to settle in weeks containing Bank Holidays, the exact maturity of the

bills at issue may be adjusted to ensure repayment on the first business day of the relevant week. Bills with less than 28 days to maturity will be made available at ad hoc tenders (see below). It is envisaged that the DMO will ensure there is a sizeable minimum total stock of bills in issue at any one time; at present this stock is intended to be £5 billion. To help increase liquidity, the DMO may reopen some Treasury bill issues as they approach standard maturity periods (ie 1 month and 3 months).

### Bidding

4. Structured Treasury bill tenders will be held on a competitive bidding basis. All bids must specify the maturity of bills being bid for, the bid, which must be made on a percentage money market yield basis<sup>2</sup> to two decimal places, and the nominal amount bid for at each yield. For DMO counterparties, and for those tenderers who have made arrangements with the DMO to bid by telephone (see paragraph 5), bids at structured tenders must be for a minimum of £1 million nominal of bills. Paper bids from other tenderers may be made by completing a tender form and delivering it to the DMO according to the timetable and settlement arrangements set out below. Paper bids must be for a minimum of £50,000 nominal. Above this minimum, bids may be made in multiples of £5,000. There is no plan to limit the number of telephone or paper bids which may be submitted by each tenderer.
5. DMO counterparties and other regular wholesale markets tenderers may bid at structured tenders by telephone providing that this arrangement has been pre-agreed with the DMO (see Appendix 2). Applications to become telephone bidders should be made to the DMO at least ten business days prior to the first structured tender at which the tenderer wishes to bid.
6. All bids must be received by 12.30pm on the day of the tender. Bids for each maturity will be ranked by yield and bills will then be allotted to those bids which are at, or below, the highest yield deemed by the DMO to be

---

<sup>2</sup> See Appendix 1 for the settlement convention the DMO intends to use for these purposes.

the highest accepted yield. Bids at the highest accepted yield may only receive a proportion of the nominal amount of bills bid for. The DMO reserves the right to reject and scale bids. The DMO will aim to publish the tender results on the wire services pages, which will be the DMO's key means of disseminating information for tenders and bilateral dealing, within 40 minutes of the close of the tender. The results will set out the amounts applied for and allotted respectively at each maturity, the lowest, average and highest accepted yields together with the approximate percentage allotment at this latter level. The DMO will announce, at the same time, the amounts on offer at each maturity at the next structured tender together with an outline of any ad hoc tenders to be held in the following week.

7. It has been agreed by HM Treasury that the DMO may from time to time issue additional Treasury bills to the market to assist the Bank in its management of sterling money market conditions where it has requested the deposit of funds. The Bank would request that the DMO adds an additional amount of bills to the size(s) of the next structured bill tender(s). The size of the amount of each tender which was being additionally offered for the Bank's money market operations would be published by the DMO when announcing the size(s) of the following week's tender(s). On settlement of the tender, the additional proceeds would be deposited at the Bank by the DMO to be repaid on the day the relevant bills mature. The deposit would then be remunerated by the Bank at the average yield of the relevant tender(s). On the day of settlement of the bills and the repayment of the deposit, the Bank would publish any impact on the money market shortage as part of its daily forecast. Treasury bills issued at the request of the Bank will be identical in all respects with the rest of the stock of Treasury bills outstanding.

#### Settlement

8. Those tenderers who have been allotted bills will be contacted by the DMO following the tender. The DMO will confirm the nominal amount of Treasury bills allotted, the required purchase consideration given the

accepted bids and the purchasers' settlement instructions. The DMO will also ask the purchaser for their preferred bill denominations. An exchange of written or electronic confirmations will follow. All Treasury bill allocations resulting from structured tenders must be settled on the first business day of the following week; this will also be the issue date of the Treasury bills purchased. A CHAPS payment for the full consideration must be received by the Bank of England from a European Economic Area regulated credit institution, for credit of the DMO's account, by 1.30pm on the settlement date, unless in any particular case the DMO agrees a different method of settlement. The purchased Treasury bills will only be released to the purchaser's account at the CMO or its equivalent or be made available for withdrawal from the CMO or its equivalent once this payment has been received

#### Splitting of Treasury bills

9. Treasury bills may be split into smaller denominations (subject to a minimum denomination of £5,000) or reconstituted into larger denominations on request to the Bank of England, Customer Settlements Services, Treasury bills section (0171-601 3302).

#### **AD HOC TENDERS**

10. The DMO may also issue shorter maturity Treasury bills (up to 28 days) at ad hoc Treasury bill tenders as part of the new Exchequer cash management operations. The objective of ad hoc tenders will be to provide additional flexibility for the DMO in smoothing the Exchequer's cash flows which the structured tender programme may not provide. Treasury bills issued as a result of ad hoc tenders will be identical in every respect with those issued by way of structured tenders. There will, however, be some important distinctions in the associated bidding, settlement and administrative arrangements; these are set out below.
11. In addition, the DMO may hold ad hoc repo and reverse repo tenders in which the collateral would be gilts or Treasury bills (see below) and ad hoc

tenders for buying in gilts (including strips). The DMO plans to limit the latter operations to buying in gilts (or strips) with a residual maturity of less than 6 months. Broadly, the same structure in terms of announcement, bidding and settlement would be used as for ad hoc Treasury bill tenders.

### Timetable

12. The DMO will usually announce the intention to hold ad hoc tenders in the wire services announcement of the structured tender results each week. This announcement will provide details of the day(s) in the following week on which the tender(s) will be held and of the type of tender together with a guide to the expected maturity and size. The precise details of the maturity and nominal amount on offer will be announced on the morning of the tender. Up to two ad hoc tenders could be held per day although it is not envisaged that this would be a regular occurrence. Tenders for the same maturity date might be made on successive business days if necessary. Initially the DMO envisages that the following timetables would be used for ad hoc tenders:

	<u>Slot 1</u>	<u>Slot 2</u>
Announcement & open offer	8.30am	10.00am
Close of offer	8.45am	10.15am
Aim to announce results shortly after	9.00am	10.30am
CHAPS payments in by	1.30pm	1.30pm
CGO/CMO movements by	close	close

The DMO does not intend to conduct ad hoc tenders in the second slot on gilt auction days or Monetary Policy Committee decision days.

### Bidding

13. Bidding at ad hoc tenders would be open to DMO counterparties bidding by telephone in accordance with the arrangements for telephone bidding which are set out in Appendix 2. DMO counterparties at ad hoc tenders would need to specify for which maturity tender they were bidding, the quantity of each bid (for bills and gilts this would be the nominal amount



and for repo and reverse repo this would be the cash amount) and the bid at each quantity (which must be a money market yield to two decimal places). Bidding would be on a competitive basis. Bids would need to be for a minimum of £5 million at each yield and in £1 million multiples thereafter; counterparties should submit no more than five bids per maturity on offer in each tender. The DMO reserves the right to reject and scale bids. As for bilateral transactions (see below), margining arrangements would be applied to ad hoc repo and reverse repo tenders. The tender results, which the DMO aims to issue on the wire services around 15 minutes after the close of offer, will, for each tender, contain details of the amount allocated, the average accepted yield and the yield and scaling factor at the cut off point.

### Settlement

14. For those counterparties which are successful at the tender, the DMO will, in addition to exchanging written or electronic confirmations, confirm by telephone the settlement and custody details with counterparties shortly after the tender. However, in the case of bill tenders, to aid the shortened settlement process (see below) the DMO will use its discretion to select a range of suitable bill denominations for counterparties. Settlement of allocations from ad hoc tenders will be for value on the same day in sterling. CHAPS payments<sup>3</sup> in settlement must therefore be with the Bank of England, for credit of the DMO, by 1.30pm on the day of the tender. Treasury bills and Treasury bill repo will be credited to counterparties' nominated account at the CMO or its equivalent on the day of the tender providing that settlement has been effected. Gilt repo and reverse repo will be settled through CGO or its equivalent.

### Splitting of Treasury bills resulting from ad hoc tenders

15. The same arrangements as for structured tenders will apply to ad hoc tenders for the splitting of Treasury bills subsequent to the tender at which they were allocated.

---

<sup>3</sup> Which must be made from a European Economic Area regulated credit institution unless in any particular case the DMO agrees a different method of settlement.

## **BILATERAL DEALING**

16. The DMO intends to trade in a range of instruments on a bilateral basis with its counterparties and will score, against its internal credit usage and counterparty limits, its exposures to any issuer<sup>4</sup> or counterparty.

### **Range of instruments**

17. The range and type of instruments in which the DMO initially intends to deal for cash management purposes are set out below. The DMO intends regularly to publish a similar indicative list on its website and reserves the right to revise the list from time to time.

18. As the list below indicates, the DMO is prepared to accept certain high quality foreign currency securities as collateral against sterling consideration providing that these are capable of being settled in CGO or its equivalent, Euroclear or Cedelbank according to the DMO's settlement requirements and timetable.

### **Purchases from the market for future resale (“reverse repo”)**

<b><u>Instruments</u></b>	<b><u>Basis of dealing</u></b>
Gilts (deliveries by value “DBV” <sup>5</sup> and General Collateral “GC” including strips)	Tenders & bilateral
HMT bills	Tenders & bilateral
Non-Sterling HMT paper	Bilateral
Selected eligible bank bills	Bilateral
Highest-rated Supranational £ and euro paper	Bilateral
Highest-rated European Government debt (in euro)	Bilateral

---

<sup>4</sup> Including the accepting bank.

<sup>5</sup> The DMO intends to use and will only accept stripped and unstripped British Government Stock for DBV transactions.

## **Sale to the market for future repurchase (“repo”)**

<u>Instruments</u>	<u>Basis of dealing</u>
Gilts (DBV” and GC including strips)	Tenders & bilateral
HMT bills	Tenders & bilateral
Gilts (Specific named stocks)	Bilateral
Non-Sterling HMT paper	Bilateral
Selected eligible bank bills	Bilateral
Highest-rated Supranational £ and euro paper	Bilateral
Highest-rated European Government debt (in euro)	Bilateral

<b>Outright purchases and sales</b>	<b>Basis of dealing</b>
Gilt purchases <sup>6</sup> (< 6 months to maturity)	Tenders & bilateral
Gilt strip purchases (< 6 months to maturity)	Tenders & bilateral
HMT bills	Tenders & bilateral
Selected eligible bank bills (< 3 months to maturity)	Bilateral

<b>Other</b>	<b>Basis of dealing</b>
Unsecured cash borrowing and lending	Bilateral

## **DEALING RELATIONSHIP WITH COUNTERPARTIES**

### General

19. Before a trading relationship can begin, the DMO and the respective counterparty need to have performed the following action:

- (i) Completion of any relevant legal and other documentation<sup>7</sup>.
- (ii) Confirmation of the counterparty’s regulatory status and details of its legal entity.
- (iii) Agreement of margining arrangements.

---

<sup>6</sup> This will succeed the existing arrangement where the Bank purchases “near maturity” gilts.

<sup>7</sup> The DMO’s repo agreement (providing that the counterparty intends to enter into repo or reverse repo transactions with the DMO) and also a letter confirming the counterparties’ agreement to adhere to this and subsequent versions of the Operational Notice.

- (iv) Provision of Standard Settlement Instructions and lists of authorised signatories and contacts.
- (v) Set up of a direct, dedicated telephone link to the DMO's dealing desk (see Appendix 3 for the specification).

20. The DMO does not intend, at least initially, to conduct business through brokers.

#### Repo and reverse repo

21. In trading repo and reverse repo with counterparties, the DMO intends broadly to use the following approach.

- The maximum maturity for repo and reverse repo transactions will be six months.
- The DMO will refer to the amount of a repo/reverse transaction in cash as opposed to stock terms (ie a £10 million start leg of a repo will signify £10 million of cash not nominal of stock).
- The DMO does not intend to be pro-active in the “specials”<sup>8</sup> repo market. As the DMO's main objective will be to smooth Exchequer cash flows, it does not envisage deliberately seeking and holding as collateral stock which is trading “special”. The DMO may, however, need to deal in stock specific repo. For example, it may need to trade out of a gilt held that has become “special” in the repo market.
- A right of substitution will not normally be expected or given by the DMO. If substitution rights are given or taken, this will be confirmed at the point of trade.
- For GC<sup>9</sup> reverse repo transactions, the DMO will require counterparties to identify the collateral being pledged to it within five minutes of the point of trade.
- The DMO will mark to market exposures to its repo counterparties and will call margin, if required, on a daily basis.

---

8 Defined in the Gilt Repo Code of Best Practice produced by the Stock Lending & Repo Committee as “Securities which, for any reason, are sought after in the repo market, thereby enabling holders to earn incremental income (in excess of General Collateral) through lending them via a repo transaction.”

9 Defined in the Gilt Repo Code of Best Practice produced by the Stock Lending & Repo Committee as “Securities, which are not “special”, used as collateral against cash borrowing.”

- Where initial margin (“a haircut”) is to be calculated on a repo or a reverse repo transaction, the DMO will follow the calculation methodology set out in the Gilt Repo Code of Best Practice produced by the Stock Lending & Repo Committee.

#### Selected eligible bills

22. The DMO may deal in eligible bills with three months or less to maturity on the following basis:

- As with other transactions, purchases will be subject to the DMO’s internal credit limits. In the case of eligible bank bills the DMO will have regard to the accepting bank name in its internal credit limits. Before the deal is committed, therefore, the DMO would expect to confirm that the accepting bank name(s) did not breach internal limits.
- If the DMO sells eligible bills, it shall not be deemed to have endorsed the bills.

#### Unsecured borrowing and lending

23. The DMO may borrow and lend on an unsecured basis with counterparties although it envisages undertaking such transactions initially only as a fine-tuning measure. Unsecured borrowing and lending shall be conducted on such terms as the DMO may agree from time to time. Contracts may be entered into either orally (including by telephone) or in writing. The “general terms and conditions for telephone dealing” set out in Appendix 2 shall apply in the case of contracts entered into by telephone.

#### Settlement

24. Unless specified otherwise, all bilateral transactions with the DMO will be settled on the trade date and in sterling.

**25. Expressions of interest in becoming a counterparty should be made in the first instance to the DMO (0171-862 6500 asking for Mike Ness or Jim Juffs).**

## APPENDIX 1

### Treasury bill settlement convention

Treasury bills will be issued on a yield basis, with the quotation of yield being to two decimal places. They will be settled according to the following price/yield formula:

$$P = \frac{N}{\left(1 + \frac{y \times n}{36500}\right)}$$

where:  $P$  = Settlement proceeds in pounds  
 $N$  = Nominal value in pounds  
 $y$  = Yield, quoted as a percentage to two decimal places  
 $n$  = Number of calendar days from the settlement date to the maturity date

The settlement proceeds  $P$  will be rounded to the nearest penny for each transaction (0.5 pence is rounded up).

Structured bill tenders will settle on the next business day; ad hoc tenders will be for same day settlement.

### Example

A Treasury bill for a nominal value of £100,000 and maturing on 18 October 1999 is issued for settlement on 19 August 1999 at a yield of 5.74%. The settlement proceeds are given by :

$$P = \frac{N}{\left(1 + \frac{y \times n}{36500}\right)}$$

where:  $P$  = Settlement proceeds in pounds  
 $N$  = 100,000  
 $y$  = 5.74  
 $n$  = 60

$$P = \frac{100000}{\left(1 + \frac{5.74 \times 60}{36500}\right)} = \text{£}99,065.26 \text{ if rounded to nearest 1p}$$

## APPENDIX 2

### Telephone dealing arrangements

As indicated above, all counterparties will need to install a direct, dedicated telephone line to the DMO's dealing desk. In addition, non-counterparties who are active in the wholesale markets and who will be regular participants at structured tenders may also arrange with the DMO to bid by telephone at structured tenders<sup>10</sup>. The terms and conditions under which the DMO would be prepared to deal by telephone are set out below.

### General terms and conditions for telephone dealing

- Telephone deals with the DMO will be irrevocable.
- Telephone calls to the DMO's dealing desk will be taped.
- The DMO's record of a deal will prevail in the event of any dispute or misunderstanding.

### Structured tender terms and conditions for telephone dealing

- The terms and conditions of issue, as set out in the weekly cash management announcement, will apply to telephone applications and to any issue of Treasury bills allotted to the tenderer (as principal or agent) as a result of such applications.
- Telephone applications must be for a minimum of £1 million nominal.
- Bids must be received by 12.30pm at the latest on the day of the tender.
- Each bid must specify; the name of the tenderer; the yield at each bid; the quantity at each bid; and the maturity of the bills being bid for. Separate bids must be made for each maturity.
- The DMO reserves the right to scale and reject bids.
- Shortly after the announcement of the results of the tender, which will be made on the DMO's wire services pages, the DMO will contact each tenderer who has been allotted bills at the tender to confirm the settlement

---

<sup>10</sup> In order to complete the necessary administrative arrangements, tenderers should make applications to the DMO at least ten business days prior to the prospective date on which they would first like to deal by telephone. In particular, they will need to send the DMO a letter confirming their agreement to adhere to this and subsequent versions of the Operational Notice.

and custody arrangements. The DMO will also request the tenderers' preferences for bill denominations.

- Settlement of allotments must be effected on the first business day following the tender day.
- Proceeds in respect of tenders must be received at the Bank of England before bills will be made available.

Ad hoc tenders' terms and conditions for telephone dealing (for DMO counterparties only)

- The terms and conditions of issue as set out in the weekly cash management announcement will apply to telephone applications and to any allotments as a result of such applications.
- Telephone applications must be for a minimum of £5 million and must be made in multiples of £1 million thereafter.
- A maximum of five bids per maturity on offer at each tender may be submitted by any one counterparty.
- Bids must be received by the latest time specified as such in the DMO's cash management announcement.
- Each bid must specify: the name of the counterparty; the yield at each bid; the quantity at each bid; and the maturity being bid for. Separate bids must be made for each maturity.
- The DMO reserves the right to scale and reject bids.
- Shortly after the announcement of the results of the tender, which will be made on the DMO's wire services pages, the DMO will contact each counterparty who has been successful at the tender to confirm the settlement and custody arrangements.
- Settlement of allotments will be effected on the same day as the tender.
- Proceeds (if appropriate to the type of tender) must be received by the Bank of England before bills will be made available.



## APPENDIX 3

### Dealing Room Voice Systems

The DMO's dealing room voice system is an IPC DK2000 digital voice switch. This system as currently configured supports Fig.1 (Ring In / Loop Out) and Fig. 2 (Ring In / Ring Out) line interfaces. Other standard line interfaces can be accommodated by arrangement if required.

Counterparties will need to order a private voice circuit between their own and the DMO's respective dealing rooms, with themselves as the "A" end and the DMO as the "B" end. Counterparties are free to select the carrier of their choice subject to suitable presentation at the DMO's site. The DMO currently has telecommunications presentation from COLT Telecommunications, Cable & Wireless and BT.

The technical contact at the DMO for any enquiries relating to voice communications is Andrew Wasielewski (Tel. 0171-862 6529, e-mail [andrew.wasielewski@dmo.gov.uk](mailto:andrew.wasielewski@dmo.gov.uk)).