

EXECUTIVE DIGEST

STATEWIDE CASH FLOW AND SHORT-TERM BORROWING

INTRODUCTION

This report, issued in February 2000, contains the results of our performance audit* of Statewide Cash Flow and Short-Term Borrowing.

AUDIT PURPOSE

This performance audit was conducted as part of the constitutional responsibility of the Office of the Auditor General. Performance audits are conducted on a priority basis related to the potential for improving effectiveness* and efficiency*.

BACKGROUND

Pursuant to Article V, Section 3 of the State Constitution, the State Treasurer is responsible for collecting, investing, and disbursing State money. The State Treasurer manages the State's cash flow through the Common Cash Pool, which pools the combined cash balances of State money. This pooling of cash allows the State Treasurer to invest money not needed to pay immediate obligations so that investment earnings on available cash are maximized. Each quarter, the State Treasurer allocates earnings to the various funds comprising the Common Cash Pool based

on each fund's average daily balance and the Common Cash investment earnings rate.

In order for the State to meet its obligations incurred pursuant to the appropriations for any fiscal year, Act 55, P.A. 1967, authorizes the State Treasurer to transfer cash on hand and on deposit among the various funds in the Common Cash Pool in such a manner as to best manage the available cash on hand. Those funds within the Common Cash Pool that have a net negative cash balance in any quarter of the fiscal year (internal borrowing*) are required to pay interest on such balances at a rate equal to the Common Cash investment earnings rate.

Further, Article IX, Section 14 of the State Constitution authorizes the State to issue short-term general obligation notes (external borrowing*). The State shall pledge undedicated revenues to be received within the same fiscal year for the repayment of the notes. Such indebtedness in any fiscal year shall not exceed 15% of undedicated revenues received by the State during the preceding fiscal year and shall be repaid at the time the pledged revenues are received, but not later than the end of the same fiscal year. For fiscal year 1998-99, the State's external borrowing limitation was \$1,336,561,650. Short-term borrowing is often necessary because of differences in the timing of revenue collections and the payment of obligations within a fiscal year.

As of the fiscal year ended September 30, 1999, the total equity in Common Cash was approximately \$3,987,806,000.

AUDIT OBJECTIVE,
CONCLUSION, AND
NOTEWORTHY
ACCOMPLISHMENTS

Audit Objective: To assess the effectiveness and efficiency of the State's management of its cash flow.

Conclusion: We concluded that the State was generally effective and efficient in the management of its cash flow. However, despite the State's restructuring of payments as described in the following paragraph, it continues to have an imbalance in receipts and disbursements that will likely result in future cash flow deficits. The State could address these deficits within the constitutional short-term borrowing limitation. Our audit disclosed a reportable condition* relating to internal borrowing (Finding 1).

Noteworthy Accomplishments: The State recognized the need to make structural changes to its cash flow to help correct the imbalances between receipts and disbursements and to reduce the amount of short-term borrowing. Beginning in late fiscal year 1997-98, the State restructured school aid and colleges' and universities' payments. The payment restructuring had a favorable impact on the cash flow and the extent of short-term borrowing.

On September 27, 2000, subsequent to our audit fieldwork, Standard & Poor's upgraded the State's rating on the issuance of general obligation bonds to AAA (its highest quality rating). Also, Moody's upgraded the State's rating to Aaa (its highest quality rating) on October 5, 2000. Both rating services attributed the upgraded ratings, in part, to a significantly strengthened cash flow position, as a result of the restructuring of school

aid payments and the accumulation of significant County-Cyclical Budget and Economic Stabilization Fund and General Fund cash reserves.

**AUDIT SCOPE AND
METHODOLOGY**

Our audit scope was to examine the program and other records of the State's cash flow process. Our audit was conducted in accordance with *Government Auditing Standards* issued by the Comptroller General of the United States and, accordingly, included such tests of the records and such other auditing procedures as we considered necessary in the circumstances.

Our audit procedures included the testing of records covering the period October 1, 1988 through September 30, 1999.

To accomplish our audit objective, we gained an understanding of and evaluated the State's procedures and methods to manage its cash flow, including its need to borrow on a short-term basis. We accumulated extensive data from the Department of Treasury relating to the Common Cash Pool. The data accumulated included, but was not limited to, fund balances, receipts, disbursements, cash flow projections, and short-term borrowing amounts and costs. We summarized and analyzed the data obtained to identify historic trends and relationships.

AGENCY RESPONSES

Our audit report includes 1 finding and 2 corresponding recommendations. The agency preliminary response indicated that the State Treasurer acknowledges the 2 recommendations.