State Cashflow Management

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In response to repeated general fund cashflow problems in the early 1980s, the state developed a number of cashflow management procedures that continue in use. This paper provides an overview of these procedures, including the statutory provisions that govern cashflow management. In addition, information is presented on recent state cashflow experience and cashflow management alternatives.

State Cashflow Management Procedures

Under current law, there are three tools that are available to the Secretary of the Department of Administration (DOA) in managing the state's cashflow. These tools are: (a) borrowing cash from other state funds on a temporary basis; (b) borrowing cash from investors through the issuance of short-term operating notes; and (c) delaying payments from a fund until enough cash is available to meet its obligations.

Temporary Borrowing from Other State Funds

The state uses the state investment fund as an investment pool for portions of retirement trust assets and cash balances of the state's various funds. In addition, local governments can elect to invest their cash balances in the fund. The state investment fund, which is managed by the State of Wisconsin Investment Board, had approximately $7.7 billion in assets during October, 2012.

Under the provisions of 2011 Act 32, during the 2011-13 biennium, the Secretary of DOA is authorized to temporarily reallocate to the general fund an amount equal to 9% of total general purpose revenue (GPR) appropriations in order to support the fund's cashflow (approximately $1,328 million in 2012-13). This 9% amount will revert to 5% on July 1, 2013. The Secretary may permit an additional 3% to be used for temporary reallocations to the general fund for a period not to exceed 30 days (approximately $443 million in 2012-13). Reallocations of the additional 3% may not be made for consecutive periods. In total, 12% of GPR appropriations ($1,771 million in 2012-13) may be allocated to the general fund on a temporary basis. No limit applies to temporary reallocations from the budget stabilization fund to the general fund.

For funds other than the general fund, up to $400 million can be reallocated between the general fund, certain segregated funds, and the local government investment pool.

In order to be eligible for temporary reallocations, a fund must have accounts receivable balances or monies anticipated to be received from lottery proceeds, tax revenues, gifts, grants, fees, sales of service, or interest earnings. The Secretary of Administration determines the allowability of accounts receivable balances and anticipated monies to be received for this purpose.

In no case can borrowing be made from retirement trust assets or from several specific segregated funds. In addition, the fund from which money is borrowed receives interest at the current state investment fund earnings rate. Further, the Secretary cannot temporarily reallocate balances if such borrowing would cause cashflow problems for the fund or account from which it is made. The Department of Administration estimated that the state investment fund had an estimated $1.9 billion of monies available for tempo-

rary reallocations in October, 2012.

Short-Term Borrowing from Investors--Operating Notes

Operating notes can be issued to fund a cash-flow deficit in the general fund. Operating notes were first issued by the state in 1983-84. If a general fund cashflow problem is anticipated, the Secretary of DOA, with the Governor's approval, can request the issuance of operating notes. This request is subject to approval by the Joint Committee on Finance under a 14-day passive review process. If the request is approved, the Building Commission issues the notes.

The amount of operating notes that can be outstanding during a fiscal year is limited to 10% of total GPR and program revenue appropriations for that year. In 2012-13, this 10% limit is approximately $1.9 billion. In addition, operating notes must be repaid before the end of the fiscal year of issuance. Table 1 shows the amount of operating notes that have been issued annually since 1998-99.

In deciding on the amount of operating notes to issue, three factors are considered. First, federal arbitrage regulations require that the actual cash deficit equal at least 90% of the issuance amount, or the state must rebate interest earnings above the rate paid on the note.

Second, the operating notes should provide sufficient cash to largely avoid temporary reallocations of available state investment fund balances during the fiscal year.

The third factor involves a comparison of the interest cost of the notes and the investment earnings the state would accrue on the note proceeds. In the absence of interest rates favoring operating notes over interfund borrowing, the minimum amount needed to ensure that no payment delays will occur should be issued. If interest rates favor operating notes over interfund borrowing, then a larger amount of notes could be issued, to reduce the state's use of interfund borrowing, but still within the limits of the federal arbitrage regulations. In a case where interest rates favored operating notes over interfund borrowing, the state's general fund could achieve interest savings by issuing notes in excess of the minimum amount needed to avoid payment delays, compared to not issuing notes or issuing the minimum needed.

As shown in Table 1, there were no notes issued during 1999-00, 2000-01, or 2002-03 because it was anticipated that there was sufficient cash available in each of those years to avoid a deficit. For the 2003-04 fiscal year, the administration received authority to issue up to $800 million in operating notes. However, following an assessment of interest rates and cash flow projections, only $400 million in operating notes was issued in 2003-04. In 2004-05, the administration was authorized to issue up to $800 million in operating notes, but decided not to issue notes, based on interest rates and cash flow projections at the time. DOA did not request authority to issue operating notes in 2005-06 or in 2006-07. Notes were issued in each fiscal year from

Table 1: Operating Notes Issuance Since 1998-99 (In Millions)

Fiscal Year	Amount
1998-99	$350
1999-00	0
2000-01	0
2001-02	800
2002-03	0
2003-04	400
2004-05	0
2005-06	0
2006-07	0
2007-08	600
2008-09	800
2009-10	800
2010-11	800
2011-12	800
2012-13	0

2007-08 through 2011-12. At the time of writing, DOA has indicated that the issuance of operating notes for 2012-13 will not be needed.

Payment Delays

The Secretary of DOA can prorate or delay payments from any fund that is having cashflow problems. This authority can only be used after all other possible procedures, including temporary reallocations of available state investment fund balances, have been used and found to be insufficient. In addition, the Secretary has to notify the Joint Committee on Finance and cannot act without a meeting of the Committee if such a meeting is scheduled within two working days after notification by the Secretary.

The statutes establish a priority schedule for payment in case of cashflow problems. The first priority is debt service payments on state general obligation debt and the second priority is debt service payments on state operating notes. Neither of these debt service payments may be prorated or reduced. State employee payrolls have third priority. The Secretary determines the priority of payments for all other items.

If payments to local units of government are delayed, the Secretary must establish a procedure under which the delay can be appealed for a unit that would be adversely affected. In addition, interest is paid on delayed payments to local units of government at the state investment fund earnings rate for the period of the payment delay.

State Cashflow Experience

The general fund receives revenues and makes expenditures for programs funded with general purpose revenue, federal revenue, and program revenue. Due to the timing of revenue collections and payments of large aid amounts, the state has experienced repeated cashflow problems.

Historically, the general fund experiences negative cash balances in the first half of the fiscal year in the absence of operating notes. Table 2 shows the lowest daily cash balance for each month in 2011-12, after deducting operating note proceeds. The negative cash balances reflect a number of larger local aid payments that occur each July, including shared revenue, the school property tax credit and first dollar credit, as well as school aid payments in September and December and shared revenue again in November. However, the state was able to cover the negative cash balances in the general fund by the issuance of $800 million in operating notes and temporarily borrowing from other state funds under the authority described above.

Table 2: Worst-Day Cash Balance in Each Month in 2011-12 After Deducting Operating Note Proceeds (In Millions)

Month	Balance
July	-$863.5
August	-998.3
September	-644.7
October	-110.7
November	278.0
December	-703.8
January	11.0
February	809.6
March	68.0
April	68.0
May	1,037.2
June	720.3

Generally, the state's cashflow pattern is attributable to the uneven distribution of both revenues and expenditures. On the revenue side, 51.8% of all general fund revenues were received during the last half of fiscal year 2011-12. The state's individual income tax and federal receipts were revenue sources that contributed to this imbalance, with 56.7% of individual income tax receipts and 51.8% of federal receipts collected in the second half of the fiscal year. It would be dif-

ficult for the state to modify the timing of these revenues, because income tax filing deadlines coincide with federal deadlines, and payments under other federal programs are not subject to direct state control.

For expenditures, the current payment schedule for county and municipal aids, and for property tax relief through the school levy and first dollar tax credits, contributes to the general fund cashflow difficulties. Payments under these state aid and credit programs are made in July and November. In 2011-12, these appropriations total approximately $1.77 billion, which were all paid out in the first five months of the fiscal year.

Over the full course of fiscal year 2011-12, general fund receipts of $29.81 billion, including general purpose revenue, program revenue, and federal receipts, were more than disbursements of $29.14 billion by $670 million. The fiscal year, which had started with a $300 million cash balance, ended with a cash balance of $970 million.

While 2011-12 ended with a cash balance of $970 million, the undesignated balance in the general fund at the year's end was $342 million. The undesignated balance is calculated by comparing general fund assets and liabilities as of June 30, of the fiscal year, and deducting required reserve and designated amounts. Since it is an accounting balance relating to general purpose revenue, it differs from the cash balance of the general fund, which includes program revenue and federal receipts and varies on a daily basis. The state's cashflow problems have occurred even when the general fund ended with positive undesignated balances.

Cashflow Management Alternatives

Historically, the state has managed its need for additional cash at certain times of the year by issuing operating notes. Under current law, the state is able to borrow money at tax-exempt interest rates to support the general fund's cashflow, rather than at the rate paid on the taxable securities held in the state investment fund. Under this authority, the state issued operating notes each fiscal year from 1983-84 to 1998-99. Each of these note issues was repaid by the end of the fiscal year of issue and supplied sufficient cash for the state to make payments in a timely manner, without having to make significant temporary reallocations from available balances of the state investment fund after the note issue.

Depending on market interest rates, the interest paid on operating notes may be less than the earnings rate paid in the state investment fund. In this case, the state may reduce its borrowing costs by issuing operating notes. As an example, in fiscal year 1998-99, it was estimated that the state saved approximately $3.8 million through the issuance of operating notes, compared to utilizing temporary reallocations from the state investment fund.

While issuing operating notes can be less costly than temporary borrowing through the investment fund, this is not always the case. In 2001-02, the interest rate paid to investors for the operating notes exceeded the rate earned in the state investment fund for some months. Therefore, the interest paid on the notes was higher than the interest that would have been paid for temporarily using other state funds in those months. However, in the absence of the operating notes, there would have been a greater risk of negative cash balances exceeding the amounts available under the temporary borrowing authority.

With short-term market interest rates being held at very low levels in recent years, since 2009-10, the average rate of return for balances held in the state investment fund has been less than 0.25%, and has been as low as 0.14%. While the net interest costs on operating notes have also

been quite low (0.22% for the issue in 2011-12), the state has continued to issue operating notes primarily in order to ensure that the general fund has sufficient cash balances to make payments in a timely manner through each fiscal year, rather than to reduce its borrowing costs.

One alternative to relying on operating notes would be to increase the statutory balance requirements under current law. Wisconsin statutes provide that no bill may be enacted by the Legislature if it would cause the estimated general fund balance on June 30 of any fiscal year to fall below a specified amount or a specified percentage of budgeted gross general fund appropriations plus GPR compensation reserves for the fiscal year. The most recent reserve requirements, provided under 2011 Act 32, established a $65 million reserve for fiscal years 2011-12 through 2014-15, and a reserve of 2.0% of total GPR appropriations plus compensation reserves for 2015-16 and thereafter. The $65.0 million reserve requirement represents approximately 0.44% of total GPR appropriations plus compensation reserves budgeted for 2012-13. Based on 2012-13 budgeted expenditures, a reserve of $296 million would be required to provide a reserve equal to 2.0% of total GPR appropriations plus compensation reserves. Similarly, a reserve of $889 million would represent 6.0% of total GPR appropriations plus compensation reserves budgeted for 2012-13.

A second alternative to issuing operating notes would be to add to the current budget stabilization fund. Under the provisions of 2001 Act 16, the Secretary of DOA is required to transfer into the budget stabilization fund 50% of the amount by which actual tax collections exceed those that had been forecast for the fiscal year (up to a maximum of 5% of estimated GPR expenditures for that fiscal year). In the absence of an excess of actual revenues over those forecast, no amounts are transferred to the budget stabilization fund under this mechanism. Also, under 2003 Act 33, the State Building Commission and DOA are required to deposit certain property sales proceeds to the budget stabilization fund.

In 2010-11, actual general fund tax revenues exceeded the amounts projected for 2010-11 in the 2009-11 budget bill. Under the Act 16 provisions, $14.6 million was transferred from the general fund to the budget stabilization fund in the fall of 2011. Similarly, for fiscal year 2011-12, an additional $108.7 million was transferred in the fall of 2012. As a result of this additional transfer, the June 30, 2012, balance in the budget stabilization fund was $125.4 million

In order to guarantee future increases in the budget stabilization fund, the Legislature could require that sums be transferred to the fund whether or not actual revenues exceed tax collections that had been projected for the fiscal year.

An additional alternative to issuing operating notes would be to shift a portion of the shared revenue and school levy credit payments to later in the fiscal year. The lowest cash balance after deducting the operating notes occurred in the first half of the state's fiscal year. Under current law, all of the county and municipal aid under the various shared revenue appropriations and the school levy and first dollar credit are paid in the first half of the fiscal year (approximately $1.7 billion in 2011-12). If $300 to $400 million of these payments were shifted to May or June in the state's same fiscal year, the state's cashflow in the fiscal year would be improved.

A major disadvantage of this alternative is the effect this type of shift would have on municipal budgets. Since municipalities budget on a calendar year basis, the shift of $300 to $400 million in shared revenue or school levy credit payments to the following May or June would result in a significant one-time loss of revenues for municipalities. Alternatively, the state could advance $300 to $400 million of payments from July and

November to the preceding May or June to establish the proposed payment schedule. However, this approach would represent a one-time cost of the same amount to the state's general fund.

A final alternative would be to channel any future increases in these state aid programs to payment dates in the later part of the state's fiscal year. This would more slowly balance the state's cashflow pattern. This alternative does not relate to the policy decision of which state aid programs should receive additional funding, but rather to the timing of the payment of any increased funding for each of these state aid programs. If additional payment amounts for these programs could be scheduled late in the state's fiscal year, the general fund's cashflow situation would be improved.