

MANAGEMENT DIRECTIVE

Commonwealth of Pennsylvania Governor's Office

Subject:

Cash Management

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By Direction of:

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Contact Agency:

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Accelerated cash-gathering and timely cash-disbursing are cost effective means of maximizing the amount of cash available for investment. This amendment defines cash management and updates policy and procedures to reflect new processes resulting from the Finance Transformation Project. References have been updated as a result of the reorganization of the Office of Comptroller Operations. Marginal dots are excluded due to major changes.

1. **PURPOSE.** To establish policy and responsibilities and provide guidelines, alternatives, and considerations for developing and improving cash management systems and processes that will strengthen the commonwealth's financial position.
2. **SCOPE.** This directive applies to all administrative departments and independent boards and commissions, hereinafter referred to as agencies, under the Governor's jurisdiction. It is recommended that other agencies adopt similar policies and responsibilities.
3. **OBJECTIVES.**
 - a. To maximize interest earned on short-term investment of commonwealth funds by the Treasury Department.
 - b. To minimize bank service charges and fund balances not earning interest.
 - c. To reduce borrowing and interest costs through the institution of cost effective revenue collection and depositing systems.
 - d. To render the payment of the commonwealth's obligations in a responsible manner.

4. DEFINITION.

- a. **Cash Management.** Financial management practices used to accelerate the collection of receivables, control payments to trade creditors, and maximize the amount of cash available for investment.

5. POLICY.

- a. Commonwealth funds shall be safeguarded from loss or theft.
- b. Federal funds shall be drawn down in a timely manner, consistent with federal regulations and grant requirements.
- c. Items of expenditure chargeable to federal appropriations shall be paid directly from such accounts whenever possible or transferred thereto in a timely manner.
- d. Every effort shall be made to improve procedures for billing the public and private sectors for goods and services provided.
- e. All monies due the commonwealth shall be collected by the most expeditious means and deposited as timely as possible. Locations with minimal revenue must deposit weekly or when the amount to be deposited reaches \$500.
- f. With respect to terminated employees only, overpayments for annual, sick, or personal leave will be addressed as follows:
 - (1) One dunning letter will be sent.
 - (2) Amounts of \$50 or less will thereafter be written off.
 - (3) Write-off is not permitted for taxes, levies, or required payroll deductions.
- g. Revenue collection and disbursement systems shall be reviewed to ensure that current applications continue to be advisable in the light of fluctuations in interest rates and escalation of bank service charges.
- h. Agencies and the Office of Comptroller Operations shall seek to establish improved business relationships with suppliers of goods and services by paying incurred obligations within or as close as possible to 30 days after receipt of invoices or of the goods and services, whichever occurs later; to avail themselves of offered discounts, if cost effective; and to avoid penalties for late payments.

6. RESPONSIBILITIES.

- a. **The Secretary of the Budget** shall be responsible for the coordination of the commonwealth's cash mobilization activities. In consultation with the Secretary of Revenue and the State Treasurer, the Secretary of the Budget shall review and approve agency proposals and recommendations to initiate procedures to deposit collections directly in state approved repositories. In consultation with the State Treasurer, the Secretary of the Budget shall review and approve proposals and recommendations to enhance agency disbursement procedures.

b. Agencies shall be responsible for:

- (1) Ensuring that commonwealth funds in possession of the agency are safeguarded from loss or theft, in accordance with Procedure 1.
- (2) Adhering to cash-gathering and cash-disbursement practices that maximize the amount of cash available for investment, in accordance with Procedures 2 and 3.
- (3) Initiating reviews of existing billing, collecting, and depositing systems; evaluating alternate methods; and instituting improvements determined to be cost effective. Changes that depart from the standard procedure of depositing revenues through the Department of Revenue shall be submitted through the Office of Comptroller Operations for coordination with the Secretary of Revenue, other interagency coordination, and approval of the Secretary of the Budget.
- (4) Consulting periodically with the Office of Comptroller Operations to identify and address revenue streams with potential for improved cash-gathering procedures.
- (5) Consulting periodically with the Office of Comptroller Operations to review cash disbursement practices and procedures, and to consider possible improvements.

c. The Office of Comptroller Operations shall be responsible for:

- (1) Ensuring that commonwealth funds in possession of the Office of Comptroller Operations are safeguarded from loss or theft, in accordance with Procedure 1.
- (2) Providing consultative services, through the Bureau of Quality Assurance, to agency heads in the analysis and development of agency cash management systems and coordinating and assisting in the implementation of revisions thereto with agencies and appropriate officials in the Department of Revenue and the Treasury Department.
- (3) Adhering to cash-gathering and cash-disbursement practices that maximize the amount of cash available for investment, in accordance with Procedures 2 and 3.

7. PROCEDURES.

a. Procedure 1: Safeguarding commonwealth funds from loss or theft. Agencies and the Office of Comptroller Operations shall use the following procedures to safeguard commonwealth funds in their possession:

- (1) Obtain a safe or other mechanism to secure funds during non-business hours at locations receiving checks, money orders or cash.
- (2) Assign, or delegate responsibility to assign, a reasonable number of individuals to have access to, and be responsible for, the safe and its contents.

- (3) Maintain a current list of individuals who have access to open the safe.
 - (4) Ensure that at least two individuals are present each time the safe is accessed.
 - (5) Develop a tracking mechanism to record signatures of individuals who are present each time the safe is accessed.
 - (6) Establish specific times during each business day in which at least one individual with access to the safe is available to make deposits and withdrawals.
 - (7) Perform at least one review at the close of each business day to ensure that all checks, money orders, or cash in mailrooms, employee work areas, or other unsecured locations are deposited in the safe.
- b. **Procedure 2: Depositing commonwealth funds using efficient cash-gathering methods.** The following manuals have been created to provide instruction for depositing commonwealth funds and are incorporated by reference:
- (1) Revenue Processing Desk Procedure Manual
 - (2) Refund of Expenditure Desk Procedure Manual
 - (3) Accounts Receivable – Process Receipts Manually Desk Procedure Manual
- c. **Procedure 3: Processing payments using efficient cash-disbursement methods.** The following manuals have been created to provide instruction for issuing payments and are incorporated by reference:
- (1) PO Invoice Processing Desk Procedure Manual
 - (2) Non PO Invoice Processing Desk Procedure Manual
 - (3) Agency Non PO Invoice Processing Desk Procedure Manual

Enclosure 1 – Guidelines for the Development of Cash Management Systems

This directive replaces, in its entirety, *Management Directive 305.5*, dated November 16, 1992.

GUIDELINES FOR THE DEVELOPMENT OF CASH MANAGEMENT SYSTEMS

These guidelines do not purport to be all inclusive nor do they prescribe rigid rules for effective cash management within state agencies. Rather, they are intended to encourage agency administrators to focus on cash management and to offer alternatives for consideration in their analysis of existing systems and procedures.

I. GOAL. Agencies should address the goal of a cash management system, which is to bring revenue into the State Treasury as quickly as possible and to keep it there as long as possible to maximize the amount of cash available for short-term investment on a continuing basis. The benefits are twofold:

- A.** the realization of the highest interest earning potential; and,
- B.** a reduction in the need to borrow.

NOTE: The latter is a form of cost avoidance, resulting in a reduction in interest costs. Effective cash management can be accomplished only by addressing both cash-gathering and cash-disbursing.

II. CASH-GATHERING. Cash-gathering is the process of collecting and depositing revenues from all sources as quickly as possible. Effectiveness, or lack of it, in the cash-gathering process is readily measurable in terms of gain or loss. At a 10 percent interest rate, collection and deposit of \$100 million one day earlier will yield approximately \$27,400 in additional interest income. A review of the cash-gathering process, therefore, should take the following into consideration:

- A. Frequency of billing for federal reimbursable costs.** Federal regulations permitting, billings to federal agencies should be prepared and submitted, at a minimum, on a weekly basis. Electronic funds transfer of reimbursement amounts to a State Treasury account is preferable and should be requested of federal agencies. If reimbursement is made by check, agencies should request that the disbursing office of the federal agency sends the check by the most efficient and secure means available.
- B. Frequency of drawdown on federal letters of credit.** Federal regulations permitting, drawdowns on letters of credit should coincide with State Treasury disbursements, i.e., issuance of checks or transfer by electronic means, to preserve state funds for state purposes. Items of expenditure chargeable to federal appropriations should be paid directly from such accounts whenever possible or transferred thereto in a timely manner.
- C. Frequency of collecting from other government jurisdictions and private parties.** Agencies should review and endeavor to accelerate collections from local government officials who serve as collectors of state revenues. The timeliness of their remittances to the state agency involved is a prime consideration in improving the cash management effort. Billings to and collection of charges from private parties, as lessors of state properties or recipients of state services, should likewise be subject to review.

- D. Reduction in float time.** Float is defined as funds in the process of collection and deposit. Agencies should take appropriate action to reduce float time applicable to:
- 1. Mail float.** The time lapse between the mailing of a check by a remitter and the receipt of the check by the state agency.
 - 2. Processing float.** The time lapse between the receipt of a check by the state agency and the actual deposit of the check at the State Treasury depository bank.
- E. Security.** Agencies should develop effective procedures for safeguarding remittances received, particularly cash, from loss or theft. This is especially important when circumstances preclude same-day deposit. It entails the maintenance and use of appropriate receipts and remittance documents, as well as providing for the security of the remittance in a safe or vault.
- F. Eliminating peaks and valleys.** Agencies should review applications and renewal dates for licenses, fees, and similar sources of revenue and reduce backlogs by revising due dates where indicated and permissible.

III. ANALYSIS OF EXISTING CASH-GATHERING PROCESSES.

- A.** The objectives of the cash-gathering analysis should be to reduce mail and processing floats and processing costs. The findings and recommendations of this analysis must be cost effective and demonstrate conclusively that the potential additional income to be earned is greater than the expenses entailed to effect and maintain systems and procedural changes.
- B.** Since the costs of processing transactions are generally fixed, i.e., the cost of a single transaction is the same regardless of its dollar value, factors that should be considered in determining total costs and cost effectiveness should include:
- 1.** the number of transactions;
 - 2.** the frequency of remittances;
 - 3.** the number and types of supporting documents; and,
 - 4.** the total dollar value.
- C.** While the overall aim should be to effect tangible economies of size, intangible nonfinancial benefits, such as improved client relationships, can also be important considerations.

D. Analysis of cash-gathering processes should ensure the consideration of the following techniques:

1. Giving processing preference to items with substantial dollar value. Where the dollar range of individual items is broad, multirange processing priorities may be warranted. The use of separate post office boxes or color coded envelopes is particularly adaptable for segregation purposes.
2. Separating receipts, i.e., checks and other forms of remittances, from accompanying transmittal forms, applications, and reports, for two-stream processing. This permits processing of checks for the earliest possible deposit.
3. Standardizing of forms for optimum use with electronic data processing (EDP), optical character readers (OCR), and magnetic ink character readers (MICR).
4. Scheduling the delivery of deposits by messenger and courier to arrive at depositories to ensure that same-day credit to state accounts is achieved.
5. Staffing for peak demand periods. The frequency and volume of remittances should be reviewed and temporary staffing arranged to meet the workloads inherent in meeting application dates for licenses and fees.

IV. ALTERNATIVES TO CENTRALIZED AGENCY CASH-GATHERING AND DEPOSITING PROCESSES.

A. Lockbox systems. A lockbox system is an extension of a state agency's central collecting and depositing system. It entails having remitters of monies due the commonwealth mail their remittances and accompanying forms to a bank-designated post office box. The bank serves as the immediate collector, check processor, and depositor of the collections to a State Treasury-designated account.

1. Lockboxes, in cities which serve as postal distribution centers, afford significant advantages because rerouting of the mail to other points is eliminated. Furthermore, unique zip codes assigned lockboxes and continuous daily pickups by bank personnel further speed mail handling, affording around-the-clock processing of receipts.
2. Processing float is reduced because the mail is immediately opened and the check is processed at the bank. Same-day deposit of remittances received is virtually assured through the use of the latest processing equipment and techniques.
3. Manpower scheduling by commonwealth offices to meet peak period requirements is eliminated,
4. There is a reduced need for capital investment for additional or updated EDP facilities and equipment.

- B. Depository transfer checks.** Under the depository transfer check system, a State Treasury-designated concentration bank is authorized to draw nonnegotiable checks on the local banks for immediate deposit to a state account. A three-day reduction in mail and processing floats can be reasonably expected through the use of depository transfer checks.
- C. Central agency transfer checks.** This system is a variation of the depository transfer check system. The field location advises the agency central office daily of the account balance in the local bank. The central office then draws a check on the local bank and deposits it with the State Treasury depository bank through established procedures.
- D. Field location transfer checks.** This system permits field locations to control the transfer of funds to the central agency. Generally, collections at field locations, i.e., parks, hospitals, and schools, are deposited in a local bank and, subsequently, field location checks are drawn and forwarded to the central office at the state agency for deposit to the State Treasury.
- E. Electronic fund transfers (EFT).** This includes wire transfers, automatic or preauthorized debits, and direct deposits through the Automated Clearing House (ACH) system. Remitters of large sums to the commonwealth, particularly federal agencies that conduct programs on a reimbursable cost basis, should be solicited to make remittances by EFT. This method is useful also in transferring revenue collected at remote locations directly into a Treasury-designated bank.

V. CASH DISBURSEMENTS.

- A.** Control of cash disbursements is an integral part of the cash management process. It involves three (3) interrelated functions:
 - 1. determination of the validity of the debt;
 - 2. payment of bills when due; and,
 - 3. investment of the disbursement float.

NOTE: The latter is a function of the State Treasury and relates to the time lapse between the issuance of a check and its debit to the state account.

- B.** Control of cash does not mean delaying payment of bills past their due date to permit investment of funds for a longer period. Such a practice is self-defeating in that it creates ill will and could lead to suppliers refusals to bid, as well as less competitive bids on state purchases. By this practice, short-term gains become long-term losses. Suppliers have a right to expect payment within 30 days of an invoice receipt or delivery date of the services and supplies.
- C.** The objectives of cash disbursement control should be:
 - 1. to take advantage of discounts offered by suppliers;
 - 2. to avoid penalties for late payment of bills; and,

3. to pay non-discount bills close to the due date.
- D.** To these ends, existing cash disbursement systems and practices should be analyzed to evaluate the cost effectiveness of the following techniques:
1. Segregation of bills at the beginning of the processing stream according to the following categories:
 - a) discount items;
 - b) late payment penalty items; and,
 - c) non-discount items.

NOTE: Depending on the volume and dollar range, prioritization by dollar amount levels might also be considered. To achieve maximum cost effectiveness, high value discount invoices should be given the highest processing priority.

NOTE: Cost effectiveness can be quantified by determining if the discount earned would be greater than the amount of interest accruing if payment were withheld until the gross amount due date. This can be established by applying the following formula:

$$r > i ((n-d)/365) a$$

Let r = discount to be earned (\$)
 i = prevailing annual interest rate
 n = number of days to gross payment
 d = number of days to discount
 a = gross amount of invoice

Assumptions:

(1) \$1,000 invoice, terms 2%/10 days ($r = \$20.00$)

(2) 10% annual interest rate ($i = .10$)

$$\$20.00 > .10 (30-10/365) \$1,000$$

$$\$20.00 > .10 \times .05479 \times 1,000$$

$$\$20.00 > \$5.48$$

NOTE: In addition to the discount and interest factors, cost effectiveness should take into consideration any added expenses inherent in priority processing of discount items. Such expenses need to be reduced to a per transaction cost based on the volume of discount invoices handled during a given period. A discount of less than two percent on a \$50.00 purchase may not warrant discounting on a cost effective basis, except for purchases paid from advancement accounts.

2. Scheduling high dollar recurring obligations for payments on a certain date. This procedure involves preparation of payment schedules by the agency and the Office of Comptroller Operations for coordination with the Office of the Budget and Treasury Department. It permits disbursement at the latest possible time.
3. Active solicitation of discounts on purchase of nonscheduled items for payment from advancement accounts.
4. **Direct deposit.** This system is to be encouraged in connection with salary and wage payments to employees and annuities to retirees. Savings from this system are inherent on a state basis through reduced need to produce and handle individual checks and matching checks to earnings statements.
5. **Payments to local governments and nonprofit organizations.** Agencies are increasingly required to provide program working capital, in the form of advance payments, to local governments and other nonprofit organizations. Such advances, collectively, represent a substantial interest earnings potential, meriting agency review of advance payment policy and procedures.

a) State agencies should ensure that:

- (1) cash advances are only in amounts necessary to meet current expenditures of the recipient organization; and
- (2) cash advance replenishments consider cash balances remaining with the recipient.

6. **Advancement accounts.** These accounts should be examined periodically to review frequency of use and to determine optimum balances required for effective use.

VI. SUMMARY. Effective cash management requires a continuing analysis of existing cash-gathering and cash-disbursing systems. Changes to volume and frequency of receipts, and over emphasis on the need for special detailed reporting can contribute to processing bottlenecks. Management must also be alert to changing conditions affecting cash flow and must periodically assess the time interval between receipt and final processing of transactions to identify causes of excessive delays, in order to improve overall cash management.