Legislative Analysis

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TREASURY – MANAGEMENT OF TRANSPORTATION FUNDS IN COMMON CASH POOL

House Bill 5239
Sponsor: Rep. Paul Opsommer
Committee: Transportation

Complete to 10-27-09

SUMMARY OF HOUSE BILL 5239 AS INTRODUCED

House Bill 5239 would amend 1941 PA 258, an act which governs accounting for state funds. The bill would amend Section 10 of the act to require that cash and other assets deposited by the State Treasurer into the common cash pool be credited with the same rate of investment interest, and would further direct the State Treasurer to treat various state funds as "trust funds" or "uncapped funds" if necessary for those funds to be credited with a common rate of interest. The bill would also direct the Auditor General to investigate the practice of crediting different interest rates to various state funds and report to the Legislature within 180 days of the bill's enactment.

The bill would also amend the title of the act to include "and for a common rate of interest to be credited […] and to provide for certain duties of the state auditor general."

BACKGROUND:

It is our understanding that this bill follows from a recommendation contained in the report of the Transportation Funding Task Force (TF2), a group established under the authority of Public Act 221 of 2007, an act which amended Public Act 51 of 1951 (Act 51). The TF2 was established to study the effectiveness of Act 51, specifically with regard to alternatives to the fuel tax, and recommend transportation revenue options. The recommendation related to the Treasurer's treatment of transportation funds in the common cash pool is found under Section 5 of the report **Recommended Efficiencies**:

Reclassify MTF Funds as "trust funds."
Although the MTF is constitutionally dedicated to transportation, the fund is not currently considered a trust fund by the Michigan Department of Treasury. Reclassifying the MTF as a trust fund will allow MTF balances to earn a slightly higher rate of interest, which will generate additional revenue for transportation investment.

The entire report is found at www.michigan.gov/tf2.

The recommendation is an outgrowth of a policy adopted by the State Treasurer in FY 2004-05 with regard to certain funds managed by the Treasurer in the common cash pool. The policy remains in effect currently.

The State Treasurer manages the cash assets of well over 100 separate state funds. Although accounted for separately by fund, the cash is managed in a common pool. During the course of the year, some funds will have a negative cash position while others have a cash surplus. Rather than borrow from external lenders to provide for the needs of cash-deficit funds, the Treasurer effectively provides cash for deficit funds from funds with available cash through inter-fund borrowing. The Treasurer's authority to transfer cash between funds provided under the authority of 1941 PA 258, 1967 PA 55, and a State Administrative Board Resolution adopted April 6, 2004.

Note that this transfer of cash between funds is simply a cash-management process; it does not affect the separate accounting for restricted funds or the integrity of statutory or constitutional restrictions.

Also note that one fund with a significant cash deficit through much of the year is the School Aid Fund. As described in a State Budget Office FY 2004-05 budget document, "… the School Aid Fund […] runs a large cash deficit during most of the year. The School Aid Fund's cash deficit is due to a misalignment between when School Aid Fund revenues are received and when School Aid Fund payments are made." Transportation funds, in particular the State Trunkline Fund (STF), may carry large cash balances due to a similar but opposite situation, a time lag between when revenue is received and when construction project payments are made. As a result, transportation funds effectively loan cash to the School Aid Fund for part of the year.

Funds with positive cash balances are credited with interest earned on those balances – including cash loaned to other funds. However in FY 2004-05 the Treasurer adopted a policy which capped the interest earnings on certain funds. The Treasurer adopted the policy because interest credited to funds with positive cash balances exceeded the amount of interest earned on cash investments. The difference between actual interest earned and interest distributed was made up from the state General Fund – the Treasurer identified the FY 2002-03 cost to the General Fund of this interfund borrowing to be $13.3 million.

Effective with the 2004-05 fiscal year, state *operating* funds would be credited for interest earned on cash balances up to 3%. Only interest paid to *operating funds* was capped at 3%. Retirement funds, trust and agency funds, bond funds, and permanent funds were not capped; they received full interest earning and, effectively, did not loan cash for interfund borrowing. Transportation funds, other than transportation bond funds, were considered operating funds; interest earnings on common cash was capped at 3% for those funds.

FISCAL IMPACT:

The Michigan Department of Treasury indicates that since short-term interest rates are currently well below 3%, the Treasurer's current cash management policy has no impact on transportation funds. We cannot readily estimate the impact if effective short-term interest rates exceed 3%. The impact would depend on actual interest rates and average cash balances.

Similar considerations obtain with regard to the fiscal impact of the bill. To the extent that short term rates exceeded 3%, the impact would depend on actual short term interest earnings, actual average cash balances, and the inter-fund borrowing needs of the School Aid Fund. Should short term interest rates again exceed 3%, the bill could result in over-distribution of interest to funds with cash balances; these distributions in excess of actual earning would be made from the state General Fund. This was the situation which obtained prior to the 2004 change in Treasury policy.

In FY 2007-08, the State Trunkline Fund (STF) was credited with $22.2 million in interest earnings. During that period the STF carried an average cash balance of $653.3 million, including $135.0 million in the Transportation Economic Development Fund, a subsidiary fund of the STF.

In FY 2007-08 the Michigan Transportation Fund (MTF) was credited $5.2 million in interest earnings. Since the MTF is primarily a distribution fund, it would tend to carry a smaller average cash balance than the STF. The reference to the MTF in the TF2 report appears to be misplaced. Following the TF2 report, Senate Bill 670 would amend Section 10 of Act 51 to classify the MTF as a "trust fund."

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