

TREASURY MANAGEMENT BASICS

Know Your Position

The ins and outs of cash positioning

BY TONY VU

How much is in your bank account right now? Cash position is the quantity of cash that a company is holding at a given point in time, so by extension, cash positioning is the calculation of the net inflows and outflows of cash that add to or use the existing cash sources that a government holds. This is a fundamental responsibility of a treasury team or cash manager.

Cash positioning is necessary because the daily flow of funds into an organization rarely matches the outflows and requires coordinating actions—cash management—to ensure that financial obligations are met in a timely manner. Basic cash management comprises two parts: bank polling and cash positioning.

POLLING

Bank polling requires connecting to your bank's financial systems and receiving a feed of your account information. This can be an automated, manual, or hybrid feed using a variety of communication standards and formats. Manual polling usually involves accessing a bank's portal and downloading the cash management information multiple times to calculate the current day cash position. Automated polling is usually done through a secure file transmission protocol (SFTP) that delivers bank reports to a specific data location via secure connections on a set schedule. The primary format for

automated file transfers is known as BAI2, a standardized file format maintained by the banking industry—although there may be small variations between financial institutions.

POSITIONING

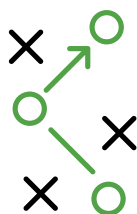
Once connected, a government can determine its cash position. Cash positioning should be done on a daily basis, or more accurately, a banking day basis. A more recent development or focus has been on liquidity positioning and enterprise liquidity management. Liquidity management is managing your cash positions beyond the current day—over a week, month, or year—and it supports planning purposes including the cash flow projection and cash/debt budgeting. Projecting your liquidity position is also a fundamental task for treasury teams.

Perfect, or 100 percent, cash visibility would allow a treasurer to know their cash and liquidity positions at all times. But most organizations operate with less than perfect cash visibility, which

means they'll need to estimate or forecast some or all of their cash and liquidity positions. Building any position or cash forecast depends on three building blocks: accounts, balances, and transactions.

ACCOUNTS

Funds flow into and out of an organization through the cash management system composed of the bank accounts that an organization opens, closes, and maintains. From an operational perspective, the accounts are fixed and determine the flow of funds. Typically, organizations use a concentration structure where funds are collected in accounts opened either for specific revenue types (sales tax, utility fees), departments (parking, public safety), or payment rails (credit cards, checks). The funds are typically concentrated into a master account that then funds various disbursement accounts, which are also opened for specific purposes (payroll, vendor payments), departments (procurement, facilities), or payment rails (checks, wire transfer, ACH).



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Whether concentration structures are in place or not, it's critical to understand, first, how many accounts you have and what services you use. This drives your ability to track the cash flows into and out of the organization. This is key to improving fraud prevention and forecasts. For example, ACH service on an account can create exposure to fraud from unauthorized transactions if the account is not protected by ACH blocks and filters. For accounts where no ACH activity should occur, it's a good idea to implement ACH blocks to prevent any ACH transactions from posting to the account. If an account needs ACH services, specific filters for what entities can be paid or can withdraw (for example, for payroll taxes) can be placed on the account to control outflows and minimize fraud exposure.

For forecasting, having an effective bank account structure can help segregate predictable, reportable, and/or large transactions from smaller and/or ad hoc transactions. This will allow a cash manager to develop more accurate projections based on the cash flow behaviors that vary by purpose, department, or payment rail. Behaviors might be driven by factors such as a set schedule (payroll), seasonality (property tax, tuition), projects (capital expenditures), or contracts (debt service, leases, subscriptions). A robust forecast supported by a bank account structure that's tailored around the organization's primary cash inflows and outflows provides better visibility into the cash needs of the organization for planning purposes.

BALANCES

Balances provide the starting point for the cash position process, more specifically, the opening available balance. The available balance is the portion of a commercial account ledger balance versus what the bank normally limits the account holder to draw, and it's the cash management "version of the truth" in cash positioning. This is different from the opening ledger balance, which is a commercial

MEASURING SUCCESS

KPI: Banking Day Coverage

Number of Cash Positions Calculated/Total Number of Banking Days in a Period
Measures the effectiveness of a cash management policy

KPI: Cash Visibility

Reported Cash/Total Cash
Measures the effectiveness of a cash management system

KPI: Liquidity Availability

Amount/Percentage of Cash Accessible in 0, 1 to 5, 5 to 20, 20+ business days
Measures the efficiency of liquidity sources

account balance that is the result of the total debit and credit activity as of a specific date and time. There is no indication of funds availability or usability. Ledger balance is also known as the book, gross, or statement balance, and it's the accounting version of the truth and the basis for account reconciliations and financial reporting.

The relationship between the two is: ledger balance less net of the 1-6-day available funds buckets = available balance. Available balance is also known as good funds or investable balance—which are important terms in relation to the ending or closing cash position.

Once an opening available balance is set, usually early in the day/cash positioning process, the cash manager can start their process to connect the actual and forecasted transactions happening that day that will increase or reduce the available balance.

TRANSACTIONS

If balances provide the starting point of a financial journey, then transactions are the twists and turns that happen along the way. For treasury purposes, transactions are categorized as liquidity sources or uses.

Sources are the inflows into an account or cash management system. They can be any type of cash inflow (revenues) such as taxes and fees, bond proceeds, credit card sales, or intergovernmental transfers/grants. Sources also include the cash on hand, credit facilities, draw programs, investments, and bond proceeds that can be transferred into an operating funds system.

Uses are the cash flows out of the cash management system. These include payroll, vendor payments, debt service, and capital expenditures. Uses can also include the repayment of credit facilities and investment of excess funds.

DAILY CUTOFF

Once all the balance and transaction information is collected, cash managers need to make a decision by their daily cutoff time. The daily cutoff time for cash positioning is just the deadline for making decisions about how to manage the cash position for that day. Daily cutoff times are based on factors including investment and borrowing notification requirements. Decisions include whether to invest/divest and borrow/repay based on the cash position at the daily cutoff time. Another driver for a daily cutoff time is the necessary time to complete any actions needed to either fund a cash deficit or invest a cash surplus based on the cash position.

CONCLUSION

Cash management is necessary because of the mismatch in timing between cash inflows and outflows. It consists of two main functions, bank polling—gathering data on accounts, balances, and transactions—and cash positioning—structuring the data into information to help a cash manager make a decision about whether to fund a shortfall or invest a surplus on a daily basis. ■

Tony Vu is an experienced public finance professional with three decades of financial management experience who lends his expertise in treasury management to governments and gov/fintech providers.