

**Statement of Position**
Legal Restrictions on Public Investing

Local government entities in Minnesota are allowed to invest in certain securities. Although all investments represent some risk of loss, State law permits investment in those securities that are generally considered to be among the safest available. State law permits investment in the following types of securities:

- Federal securities, which include treasury bills, notes and bonds, as well as bonds and notes issued by U.S. Government agencies such as the Small Business Administration or GNMA (Ginnie Mae), or by U.S. Government instrumentalities such as FNMA (Fannie Mae), the Federal Home Loan Bank, the Federal Farm Credit Bank, or FHLMC (Freddie Mac);
- State and local securities, which include bonds and other debt instruments issued by cities, counties, states, or other governmental units, subject to rating requirements;
- Commercial paper, which includes rated short-term debt issued by U.S. corporations or their Canadian subsidiaries;
- Guaranteed Investment Contracts;
- Transferable Certificates of Deposit issued by U.S. banks fully insured by the FDIC (Federal Deposit Insurance Corporation). Note: Certificates of Deposit or other time deposits issued by local banks or credit unions directly to governmental entities are authorized under State law as deposits;¹
- Bankers' Acceptances issued by U.S. banks;
- Money Market Mutual Funds, subject to rating requirements; and
- Government Investment Pools, including the 4M Fund, the Liquid Asset Fund, MAGIC Fund, and MN Trust.

There are additional statutory restrictions for each type of investment. To ensure legal compliance, government investors should read and make sure they understand the restrictions contained in sections 118A.04 and 118A.05 of Minnesota Statutes as they apply it to any investment under consideration. To fulfill the public entity's duty to taxpayers, the official document that provides information on the investment to potential investors must be reviewed for compliance with these restrictions. For example, debt obligations usually have "Offering Statements," which describe in detail the nature of the

¹ See Minn. Stat. §§ 118A.01, subd. 3; 118A.02, subd. 1; and 118A.03. See also the following document, attached to this Statement of Position: Op. Atty Gen'l 159a-13, May 25, 1960 (discussing, among other things, the difference between deposits and investments).

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This Statement of Position is not legal advice and is subject to revision.

obligation, the source of repayment and other information. A mutual fund's purpose and operation is described in a document called a "Prospectus," which sets forth the goals of the mutual fund, and the restrictions management has placed on the mutual fund's investments.

In addition to the statutory restrictions discussed above, the Office of the State Auditor (OSA) recommends that all public entities provide additional guidance to their public investor through the adoption of an investment policy. Such a policy can improve the investment process by:

- Identifying and prioritizing investment objectives and setting risk levels, including levels for credit risk, concentration risk, and custodial credit risk;
- Addressing ethics and conflict of interest issues not covered by the general conflict of interest statutes;
- Establishing internal controls for the investment function, as well as providing for interim and annual reporting;
- Establishing written investment procedures, directly or through the establishment of an investment committee, that address evaluation of economic outlook, diversification and maturity structure; and
- Establishing portfolio performance benchmarks and, where appropriate, establishing a process of outside review.

Minnesota law also mandates how public investments are to be handled. Before entering into an investment transaction with a broker, Minnesota law requires that public entities obtain the broker's signature on a "Broker Certification Form."² Once a relationship with a broker has been established, the public entity will need to obtain a signed Broker Certification Form from that broker every year.

If a public entity does not take possession of an investment, it may be held in safekeeping only with a "qualified safekeeper."³ A broker can be a safekeeper if the broker meets the statutory requirements. For a broker-dealer to be qualified as a safekeeper, the statute requires the broker to maintain sufficient SIPC (Securities Investor Protection Corporation) protection and excess SIPC coverage to protect investments being held. SIPC protects investors up to the value of \$500,000 for the loss of securities should the broker fail. Excess SIPC coverage can be purchased by brokers to protect their clients beyond the \$500,000 limit of basic SIPC coverage.

The public entity's ownership of investments must be evidenced by written acknowledgements identifying the securities by the names of the issuers, maturity dates, interest rates, CUSIP numbers, and other distinguishing marks.

If you have specific questions on the permissibility of particular investments, please feel free to contact the Legal Department at the Office of the State Auditor. Information is also available at the League of Minnesota Cities' website, at www.lmc.org. For information on securities generally appropriate for

² This form is available on the State Auditor's website at www.osa.state.mn.us. Download the Broker Certification Form, fill out the relevant portion and send it to the broker to sign.

³ See Minn. Stat. § 118A.06. See also the OSA's Statement of Position on Qualified Safekeepers.

public investments, see the Government Finance Officers Association's (GFOA) website, at www.gfoa.org.

EDUCATION: Deposit of school district money is regulated by M.S.A. 124.05, Subdivisions 1 & 2; investment of surplus in sinking fund is regulated by M.S. 475.66; investment of other surplus money of district is regulated by M.S.A. 124.05, Subd. 3 and M.S. 118.12 which are in pari materia. A certificate of deposit is not an authorized investment under 124.05, Subd. 3, 475.66, or 118.12-- it is a deposit of money within the meaning of "deposit" under M.S.A. 124.05, Subd. 2.

May 25, 1960

Honorable Peter S. Popovich
Peterson, Popovich & Marsden
Attorneys for Independent
School District No. 16
314 Minnesota Building
St. Paul 1, Minnesota

159a-13

Dear Sir:

This will acknowledge your letter addressed to Attorney General Walter F. Mandale wherein, as attorneys for Independent School District No. 16, Spring Lake Park, you state the following

FACTS:

Independent School District No. 16 has on hand surplus funds consisting of (1) sinking fund money, and (2) general maintenance and operational funds, building funds from the sale of bonds, and receipts from taxes levied under former statute M. S. Section 127.04.

You ask the following

QUESTION:

"May surplus funds of school district No. 16, Spring Lake Park, be invested in certificates of deposits of various banks in Minnesota, or are they limited in investment policy by the securities described in Chap. 71, 1959 Ed. Rec., Article V, Section 5, Subd. 1, tentatively coded as M.S. 124.05, Subd. 3?"

and you

COMMENT:

"In this connection, I call your attention to an opinion of the Attorney General rendered May 22, 1953 to Dougherty and Flynn, Attorneys for Fairmont

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Independent School District No. 1. In that opinion, apparently a School District may invest in certificates of deposit under M. S. 118.12 where such certificates of deposit are used for collateral security. I believe some confusion now exists in view of that previous opinion, and in view of the action taken by the 1959 Legislature in passing the Education Code. It would appear to me that M. S. 118.01 is permissible only as collateral security for deposits but the investment policies of school districts are now covered by the Depositary Law, tentatively coded as M. S. 124.05, and are thus limited by the subdivision therein to the securities therein expressly enumerated. I have personally come to the conclusion that school districts may not invest their surplus funds in certificates of deposits of banks and that this is the legislative intent, in view of the recent enactment."

OPINION

A distinction must be made between the "deposit" of school district funds and the "investment" of surplus school district funds. A further distinction must be made between the investment of a sinking fund surplus and any other surplus mentioned in your request.

M.S.A. 124.05, subdivisions 1 and 2 relate to the deposit of school district funds; Subd. 3 thereof provides for the investment of surplus funds, as does M.S.A. 118.12 which is in pari materia therewith (see M.S.A. 645.16 and cases annotated, M.45), and M.S. 1957, Section 475.66 which provides for the investment of a surplus in the sinking fund.

A certificate of deposit is not an investment or security within the provisions of either M.S.A. 124.05, Subd. 3, M.S.A. 118.12, or M.S. 1957, 475.66.

As stated in Durnell's Digest (3rd Ed., Section 1001: "In legal effect a certificate of deposit is a promissory note--negotiable paper." (Citing Barton v. Hyde (1868) 13 Minn. 90

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(611.03) and other cases) As such, it is subject to the provisions of M.S.A. 124.05, Subd. 2, which reads:

"In the event that the bank selected as a depository is a member of the Federal Deposit Insurance Corporation, the district may deposit an amount not to exceed \$10,000 in the depository without the execution of any bond. In the event that it is desired to deposit more than \$10,000 in any bank, prior to such deposit, the board shall require the bank to deposit a sufficient bond to the district, executed by a corporate surety company authorized to do business in the state in a sum at least equal to the estimated sum to be deposited in excess of \$10,000. The bond shall be approved by the board and filed in the office of the auditor of the county wherein the district may be situated. In lieu of such bond, the depository shall assign to the district treasurer collateral security for deposits, in accordance with Minnesota Statutes, Section 118.01."

Investment of surplus money of the district's sinking fund is regulated, as stated above, by M.S. 1957, Section 475.66; investment of surplus money in the other funds mentioned in the facts is determined by M.S.A. 124.05, Subd. 3 and M.S.A. 118.12.

The opinion to which you refer (May 23, 1958, File 159a-13), a copy of which is enclosed, cannot be construed as having authorized a district to make a time deposit of the money there in question as an "investment" within the meaning of the statutes. The apparent misinterpretation as to the holding of that opinion appears to be due to the use of the word "invested" in the footnote to the opinion, and the use of the word "invest" in the question. In that opinion the district wanted to know if it could make a time deposit of its surplus funds with government bonds pledged as collateral security for the money so deposited. It did not ask if it could purchase United States government bonds with its surplus funds. The former

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was a deposit; the latter would have been an investment.

It is therefore our opinion, in accordance with the opinion and statutes cited, that surplus school district funds held by a bank (for which the district has received from the bank a certificate of deposit whereby the bank acknowledges receipt of the money in the form of a promissory note) are on deposit with the bank and subject to the provisions of N.S.A. 124.05, Subd. 2. A certificate of deposit is not an investment within the meaning of N.S.A. 124.05, Subd. 3, N. S. 118.12, or N. S. 475.06, and the district's surplus funds may be "invested" only as the last three statutes provide.

Very truly yours

WALTER F. MONDALE
Attorney General

FRANK J. MURRAY
Special Assistant
Attorney General

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enc. (1)